

**STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION**

MIDCONTINENT COMMUNICATIONS,)
A SOUTH DAKOTA PARTNERSHIP,)
COMPLAINANT)
VS.) Case No. PU-05-451
NORTH DAKOTA TELEPHONE COMPANY,)
RESPONDENT)
)

DIRECT TESTIMONY OF

WARREN R. FISCHER

On Behalf Of

MIDCONTINENT COMMUNICATIONS

December 21, 2005

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I. INTRODUCTION

Q. MR. FISCHER, PLEASE STATE YOUR FULL NAME AND BUSINESS ADDRESS FOR THE RECORD.

A. My name is Warren R. Fischer. My business address is 2500 Cherry Creek Drive South, Suite 319, Denver, Colorado 80209.

Q. BY WHOM ARE YOU EMPLOYED AND WHAT IS YOUR POSITION?

A. I currently serve as Director of Business Services and Research for QSI Consulting, Inc.

Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND.

A. I have a Bachelor of Science degree in Business Administration with a concentration in Accounting from the University of Colorado in Boulder, Colorado. I am licensed as a Certified Public Accountant in the States of Colorado and California.

Q. WHAT IS YOUR EMPLOYMENT BACKGROUND?

A. After graduating from the University of Colorado, I worked for several years as an accountant with Deloitte & Touche conducting financial audits. Thereafter, I worked for two major corporations as a financial analyst. I joined AT&T Wireless Services in 1995 as a financial analyst, and I managed the preparation of annual revenue forecasts for the company's cellular division. In 1996, I transferred to AT&T Corp. where I became a financial manager and a subject matter expert on pricing and

23 costing issues involving local exchange and exchange access services. In 2000, I
24 joined QSI as a Senior Consultant.

25

26 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THIS OR OTHER**
27 **PUBLIC UTILITY COMMISSIONS?**

28 A. Yes. I testified before the North Dakota Public Service Commission
29 ("Commission") on universal service cost issues in Docket No. PU-314-97-465 in
30 1998 on behalf of AT&T Communications of the Midwest, Inc. I have also testified
31 at the FCC and before 13 other state commissions on access reform and appropriate
32 cost-based rates under the FCC's Total Element Long-Run Incremental Cost
33 ("TELRIC") methodology. A more detailed description of the cases I have testified
34 in is included in my curriculum vitae as Exhibit WRF-1.

35

36 **Q. ON WHOSE BEHALF ARE YOU FILING THIS TESTIMONY?**

37 A. This testimony was prepared on behalf of the Midcontinent Communications
38 ("Midcontinent").

39

40 **II. PURPOSE OF TESTIMONY**

41 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

42 A. The purpose of my testimony is to support Midcontinent's bona fide request under 47
43 U.S.C. § 251(c) for wholesale resold service for the Devils Lake, North Dakota
44 exchange within North Dakota Telephone Company's ("NDTC's") serving territory.

45 This testimony, combined with that of my partner, Mr. Timothy Gates, will address
46 reasons why NDTc's exemption under 47 U.S.C. § 251(f) should be terminated.
47 The Commission's July 28, 2005 Notice of Hearing notes that the following must be
48 considered in evaluation a request for terminating the exemption under 47 U.S.C.
49 § 251(f):

- 50 1. Whether the request of Midcontinent is unduly economically burdensome.
- 51 2. Whether the request of Midcontinent is technically feasible.
- 52 3. Whether the request of Midcontinent is consistent with 47 U.S.C. § 254
53 (other than subsections (b)(7) and (c)(1)(D) thereof).
- 54 4. The implementation schedule for compliance with the request should the
55 exemption be terminated.

56 My testimony focuses on demonstrating that Midcontinent's provisioning of resold
57 services in Devils Lake will not be unduly economically burdensome to NDTc.

58

59 **III. RESALE REQUIREMENTS**

60 **Q. WHAT IS RESALE?**

61 A. Resale is one of three forms of competitive entry into the local exchange market
62 contemplated by the Telecommunications Act of 1996 ("the Act"). The other two
63 are construction of new networks and the use of unbundled network elements of the
64 incumbent's network. 47 U.S.C. § 251(c)(4)(A) requires incumbent LECs to offer
65 for resale at wholesale rates any telecommunications service that the carrier provides
66 at retail to subscribers who are not telecommunications carriers. The incumbent LEC

67 sells its finished services to a CLEC at wholesale rates based upon an interim
68 wholesale discount rate between 17 and 25% or based upon the discount produced by
69 an avoided retail cost study for that LEC that complies with FCC pricing rules.¹ The
70 discount reflects the retail related costs that are considered avoided or avoidable by
71 the incumbent LEC.

72

73 **Q. HOW DOES THE RESALE FORM OF COMPETITIVE ENTRY COMPARE**
74 **TO THE OTHER TWO FORMS IN TERMS OF POTENTIAL FINANCIAL**
75 **IMPACT ON AN INCUMBENT LEC?**

76 A. Of the three forms of competitive entry, resale will have the smallest financial impact
77 on the incumbent LEC while also requiring far less capital investment on the part of
78 the CLEC. In a resale environment, the incumbent LEC will retain the physical
79 connection with its former retail customer since the CLEC will resell an existing
80 service. No costs are incurred to disconnect and reconnect customers, nor are
81 network reconfigurations required. The incumbent LEC will continue to receive
82 revenue for each customer now served by the CLEC, albeit at a lower rate than
83 before. However, its revenue losses will be mitigated by avoiding costs required to
84 serve customers on a retail basis.

85

86 Potential financial losses for the incumbent LEC are greater with facilities-based
87 competition as are the risks for the new entrant. When a competitor enters the

¹ See 47 C.F.R. § 51.611.

88 market with its own network or by leasing the incumbents unbundled network
89 elements on a wholesale basis, the incumbent LEC loses its retail customer entirely.
90 In exchange for investing a significant amount of capital with no guaranteed
91 financial return, a facilities-based carrier has the opportunity to serve the incumbent
92 LEC's retail customers more cost effectively if it builds a more advanced and
93 efficient network and can offer innovative service packages. This translates into a
94 real loss of market share and profitability for the incumbent LEC if the CLEC can
95 retain the customer.

96

97 **Q. HOW ARE AVOIDED COSTS IDENTIFIED?**

98 A. In ¶ 911 of its *Local Competition First Report and Order*, the FCC concluded that,
99 “the avoided costs are those that an incumbent LEC would no longer incur if it were
100 to cease retail operations and instead provide all of its services through resellers.”²
101 Subsequently, the FCC adopted rules governing the resale of telecommunications
102 services in 47 C.F.R. §§ 51.601 – 51.617. Section 51.609(a) requires that avoided
103 retail costs be determined by a cost study that complies with the requirements of
104 §51.609 which identifies direct and indirect cost accounts within the 47 C.F.R. Part
105 32 account system used by telecommunications carriers that contain avoided or
106 reasonably avoidable costs. Reasonably avoidable costs include direct retail costs
107 such as marketing, sales, and billing and collection, as well as a portion of indirect or
108 shared costs such as general overhead.

109
110 **Q. HOW IS THE AVOIDED COST DISCOUNT DETERMINED?**

111 A. Total avoided or avoidable retail costs are divided by total revenue subject to resale
112 for the incumbent LEC. This requires identifying services that are subject to resale
113 under the FCC's rules. As noted previously, 47 U.S.C. § 251(c)(4)(A) requires an
114 incumbent LEC to offer any carrier any telecommunications service that it offers on
115 a retail basis to subscribers that are not telecommunications carriers for resale at
116 wholesale rates. This requirement excludes services such as switched and special
117 access, billing and collection and other miscellaneous service that are not sold to
118 retail customers. The resulting percentage is applied to retail rates charged by the
119 incumbent LEC to determine the wholesale price to be paid by the CLEC for resold
120 services. I discuss how the resale of services using an avoided cost discount might
121 impact NDT in Section IV of my testimony.

122
123 **IV. THE ESTIMATED FINANCIAL IMPACT OF RESALE ON NDT**

124 **Q. WERE YOU ABLE TO ESTIMATE THE FINANCIAL IMPACT OF
125 MIDCONTINENT'S ENTRY INTO NDT'S MARKET IN THE DEVILS
126 LAKE EXCHANGES THROUGH RESALE?**

127 A. Yes. I estimated this impact by using NDT's revenue data for these exchanges, as
128 well as company-wide accounting data provided in response to discovery. My

² See Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, CC Docket No. 96-98, First Report and Order, 11 FCC Rcd 15499, 15509 ("Local Competition First Report and Order.")

129 analysis included several scenarios based on different levels of an assumed resale
130 discount rate offered by NDTC, as well as different assumptions about
131 Midcontinent's market penetration. These financial analyses are contained in
132 Exhibits WRF-2, WRF-3 and WRF-4.

133

134 **Q. WHAT ARE THE MAIN CONCLUSIONS FROM YOUR ANALYSES?**

135 A. I reached two conclusions. First, the financial impact of such entry would be
136 minimal even under optimistic (from the standpoint of my client) assumptions about
137 Midcontinent's penetration into NDTC's Devils Lake market. This conclusion is
138 driven by several factors:

139

- 140 • Only the Devils Lake area would be affected;
- 141 • A significant portion of NDTC's revenue in these exchanges, such as from
142 switched and special access and billing & collection services, would not be
143 subject to resale;
- 144 • NDTC would continue to receive revenue on resold services; and
- 145 • NDTC should be able to realize cost savings on resold services because the
146 retail costs associated with resale-based customers would be borne by
147 Midcontinent.

148 Second, it is possible that NDTC would experience a net gain, rather than a net loss,
149 from Midcontinent's entry. A net gain would happen if the resale discount
150 governing the resale arrangement between NDTC and Midcontinent is lower than the

151 actual cost saving that NDTC would experience due to the reduction of its retail
152 operations costs associated with resold services. I discuss the loss of revenue NDTC
153 can expect to experience as well as the offsetting cost reductions that should occur in
154 a resale environment below.

155

156 **Q. HOW DID YOU DETERMINE WHAT PORTION OF NDTC'S REVENUE
157 WOULD BE SUBJECT TO RESALE?**

158 A. I estimated NDTC's revenue that would be subject to resale by subtracting wholesale
159 revenue from NDTC's total operating revenue in the Devils Lake exchanges. NDTC
160 provided Devils Lake-specific revenue information in its November 23, 2005
161 Response to Request for Disclosure of Information. Midcontinent made its bona fide
162 request under 47 U.S.C. § 251(c), which specifies that the incumbent LECs have a
163 duty "to offer for resale at wholesale rates any telecommunications service that the
164 carrier provides at retail to subscribers who are not telecommunications carriers[.]"³
165 Federal rules also specify that exchange access services "shall not be considered to
166 be telecommunications services that incumbent LECs must make available for resale
167 at wholesale rates to requesting telecommunications carriers."⁴ In other words,
168 Midcontinent's request concerns only NDTC's services offered to retail customers
169 and only retail revenue constitute revenue that would potentially be subject to resale.

170

³ See 47 U.S.C. § 251(c), subsection 4 (A).

⁴ See 47 CFR § 51.605. In addition, section §51.617 explains that the incumbent LEC should assess end user common line charges on the requesting telecommunications carriers.

171 Using federal rules on the 47 C.F.R. Part 32 accounts for telecommunications
172 companies, I identified NDTC's revenue groups that are likely to contain non-retail
173 revenue. As I discussed above, one obvious class of non-retail revenue are those
174 classified as Network Access Revenue.⁵ Other revenue accounts that likely contain
175 non-retail revenue are Directory and Rent, Carrier Billing and Collection, and a
176 portion of Other Miscellaneous Revenue⁶ that relates to intercarrier compensation
177 and services to non-retail customers. All three are collectively grouped under the
178 Miscellaneous Services category on NDTC's financial statements.

179

180 **Q. DID YOU MAKE ANY ASSUMPTIONS WHEN CALCULATING NDTC'S
181 REVENUES SUBJECT TO RESALE?**

182 A. Yes. In regard to Miscellaneous Services, NDTC's financial data for the Devils Lake
183 exchanges lacked the necessary account-level detail (were not split between
184 Directory, Rent and Other Miscellaneous Revenue⁷) required to identify revenue
185 from specific services that would be subject to resale. Because I assumed that a
186 portion of Other Miscellaneous Revenue might constitute retail revenue, I needed to
187 separate Rent and Directory revenue from Other Miscellaneous Revenue. I
188 apportioned Devils Lake Miscellaneous Service revenue between the three accounts
189 using proportions observed in the company-wide financial data. In addition, I made

⁵ Accounts of 508X series.

⁶ Account 5260.

⁷ Accounts 5230, 5240 and 5260 correspondingly.

190 an assumption about the portion of Other Miscellaneous Revenue that represents
191 wholesale services.⁸

192
193 The following Table 1 compares NDTc's per line total revenue in the Devils Lake
194 exchanges to per line revenue that would be subject to resale. As the table shows,
195 revenue subject to resale constitutes approximately one third of NDTc's total per
196 line revenue in this exchange, and the difference between the two numbers is driven
197 largely by network access revenue.

198 **TABLE 1**

NDTC's Revenue in the Devils Lake Exchanges Subject to Resale (Per Line Per Year)			
Revenue Account	2004 Revenue Per Line	2004 Revenue Per Line Subject to Resale	
Local Network Access	\$ 308.71	\$ 308.71	
Network Access Services	\$ 529.09	\$ -	
Long Distance Network Services	\$ 0.75	\$ 0.75	
Billing and Collection Revenue	\$ 18.55	\$ -	
Miscellaneous Revenue	\$ 32.14	\$ 9.86	
TOTAL DEVILS LAKE PER LINE PER YEAR	\$ 889.24	\$ 319.32	
<i>% of Total Revenues in Devils Lake</i>			36%

200
201 **Q. HOW DID YOU ESTIMATE THE POTENTIAL REVENUE LOSS FROM
202 RESALE?**

203 A. In essence, NDTc would lose revenue in the amount equal to the resale discount on
204 each customer acquired by Midcontinent through resale from NDTc. Therefore, the

⁸ This is a user-adjustable assumption that in the absence of any specific information I set at 50%.

205 potential revenue loss would depend on two factors –the resale discount governing
206 the resale arrangement between NDTC and Midcontinent and Midcontinent’s market
207 penetration rate.

208
209 According to FCC rules, the resale discount should be based on the retail cost that is
210 avoided or is reasonably avoidable through the resale process.⁹ The rules state that
211 state commissions may establish (absent of an avoided cost study) an interim
212 wholesale discount in the range between 17 and 25%.¹⁰ Another illustration of the
213 typical level of resale discount is the discount currently offered by Qwest in North
214 Dakota, which is 16.15%.¹¹ It is reasonable to assume that NDTC’s resale discount
215 would be somewhere close to the industry standards. As an illustration, I assumed
216 that NDTC would adopt the Qwest’s discount, and calculated the total annual
217 revenue loss per resale-based customer. The following Table 2 depicts the results of
218 this exercise:

⁹ See 47 CFR § 51.607.

¹⁰ See 47 CFR § 51.611.

¹¹ Exhibit A to *Qwest’s Statements of Generally Available Terms and Conditions for Interconnection, Unbundled Network Elements, Ancillary Services and Resale of Telecommunications Services in North Dakota*, Section 6.

220

TABLE 2

NDTC's Annual Per Line Revenue Loss On Resale-Based Customers at 16.15% Resale Discount

Revenue Account	2004 Revenue Per Line	2004 Revenue Per Line Subject to Resale	Potential Revenue Loss via Resale
Local Network Access	\$ 308.71	\$ 308.71	\$ 49.86
Network Access Services	\$ 529.09	\$ -	\$ -
Long Distance Network Services	\$ 0.75	\$ 0.75	\$ 0.12
Billing and Collection Revenue	\$ 18.55	\$ -	\$ -
Miscellaneous Revenue	\$ 32.14	\$ 9.86	\$ 1.59
TOTAL DEVILS LAKE PER LINE PER YEAR	\$ 889.24	\$ 319.32	\$ 51.57
<i>% of Total Revenues in Devils Lake</i>			36% 5.8%

221

222

223 As Table 2 demonstrates, if NDTC offers the same resale discount as Qwest's
224 discount in North Dakota, NDTC would lose only 5.8% of its revenue per line on
225 each customer that switches service to Midcontinent.

226

227 **Q. DOES TABLE 2 ABOVE ACCOUNT FOR THE POTENTIAL MARKET
228 PENETRATION OF MIDCONTINENT?**

229 A. No, it does not. Table 2 depicts the revenue loss on an average customer who
230 switches to Midcontinent. In other words, NDTC's actual loss of revenue in the
231 Devils Lake exchanges would be significantly less than 5.9% (the last row in Table
232 2) because only a portion of total customers would switch to Midcontinent. Industry
233 experience shows that the market penetration for resale-based CLECs is modest. For
234 example, according to data reported by Qwest on its Form 477 filed with the FCC,¹²
235 the portion of resale lines provided by Qwest in North Dakota constitutes only 1.6%

¹² Form 477 Local Competition and Broadband Reporting.

236 of its total end-user and wholesale lines.¹³ On a nationwide basis for all reporting
237 LECs this percentage is even smaller – 0.9%.¹⁴

238
239 Recognizing that Midcontinent may be able to achieve higher resale-based
240 penetration than the industry average through its ability to offer bundled services,¹⁵ I
241 estimated the total revenue loss from resale for a number of scenarios where assumed
242 penetration rates range from 2 to 30%.¹⁶ Table 3 summarizes this analysis.

243
244 TABLE 3

245 Devils Lake Gross Revenue Loss Under Different Penetration Scenarios and 16.15% Resale Discount

Devils Lake Total Annual Operating Revenue (2004)	\$ 5,040,579			
NDTC Total Annual Operating Revenue (2004)	\$ 16,977,056			
PENETRATION RATE SCENARIOS	2%	10%	20%	30%
Lines Lost to Resale	113	567	1,134	1,701
Estimated Annual Gross Revenue Loss	\$ 5,846	\$ 29,232	\$ 58,465	\$ 87,697
Gross Revenue Loss as % of Devils Lake Total Revenue	0.116%	0.580%	1.160%	1.740%
Gross Revenue Loss as % of NDTC Total Revenue	0.034%	0.172%	0.344%	0.517%

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247 As the last row of Table 3 demonstrates, NDTC's revenue loss from Midcontinent's
248 entry through resale is negligible compared to NDTC's total revenue. It is less than
249 1% even if we assume an optimistic 30% penetration rate for Midcontinent.

250

251 **Q. HOW DOES THE LEVEL OF RESALE DISCOUNT AFFECT THE NDTC'S
252 GROSS REVENUE LOSSES FROM RESALE?**

253 A. As the level of the resale discount decreases, so does the NDTC's gross revenue loss
254 from resale. This fact is illustrated in Table 4 below, from Exhibit WRF-3 that
255 compares the scenario depicted in Table 3 above (16.15% resale discount) with
256 another scenario where the resale discount is 10%:

257

TABLE 4

Devils Lake Gross Revenue Loss Under Different Penetration Scenarios and 16.15% Resale Discount

Devils Lake Total Annual Operating Revenue (2004)	\$ 5,040,579			
NDTC Total Annual Operating Revenue (2004)	\$ 16,977,056			
PENETRATION RATE SCENARIOS				
Lines Lost to Resale	113	567	1,134	1,701
Estimated Annual Gross Revenue Loss:				
At a 10% Resale Discount	\$ 3,620	\$ 18,101	\$ 36,201	\$ 54,302
At a 16.15 % Resale Discount	\$ 5,846	\$ 29,232	\$ 58,465	\$ 87,697
Gross Revenue Loss as % of NDTC Total Revenue:				
At a 10% Resale Discount	0.021%	0.107%	0.213%	0.320%
At a 16.15 % Resale Discount	0.034%	0.172%	0.344%	0.517%

258

259

260 As evident from this table, the gross revenue loss is smaller for the scenario where
261 the resale discount is smaller.

262

263 **Q. YOU MENTIONED ABOVE THAT ACCORDING TO 47 CFR § 51.607, THE
264 RESALE DISCOUNT SHOULD BE BASED ON THE AVOIDED COSTS.**

WHAT ARE THE AVOIDED COSTS?

A. The avoided costs are costs that “reasonably can be avoided when an incumbent LEC provides a telecommunications service for resale at wholesale rates to a requesting carrier.”¹⁷ Some costs would be avoided because the retail costs associated with the resold service are borne not by the incumbent, but by a carrier that purchases the services from the incumbent through wholesale. Federal rules¹⁸ list the expense accounts¹⁹ that would likely contain avoided costs. These accounts include product management and sales,²⁰ product advertising,²¹ services (call completion, number services and customer operations),²² a portion of general support expenses,²³ corporate operations,²⁴ as well as uncollectible revenue.²⁵ In addition, the rules specify that plant specific expenses other than general support expenses, as well as plant non-specific expenses,²⁶ may also be included in the avoided cost calculation to the extent a party proves to the state commission that these costs can reasonably be avoided.

¹⁷ See 47 CFR § 51.609(b).

¹⁸ See 47 CFR § 51.609.

¹⁹ For companies that record information in summary accounts (Class B companies) the rules suggest that the entire summary accounts, rather than specific accounts may be used in the determination of avoided cost (47 CFR § 51.609(e)).

20 Account 6611.

21 Account 6613.

22 Account 6620

23 Accounts 6121-6124

24 Account 6720

25 Account 5300

26 Accounts 6112

280 As I discussed above, the federal pricing standard for the provision of
281 telecommunications service for resale at wholesale rates is to set the resale rates
282 equal to retail rates minus the avoided retail costs.²⁷ In other words, the resale
283 discount on prices reflects the avoided retail costs.

284

285 **Q. HOW DOES THE FEDERAL REQUIREMENT THAT THE RESALE
286 DISCOUNT BE BASED ON AVOIDED COST AFFECT YOUR ANALYSIS?**

287 A. The pricing standard ensures that the incumbent's loss of revenue is offset by the
288 retail cost savings when providing a service for resale at wholesale rates. In terms of
289 the aforementioned financial analysis, it means that NDTC's expense savings need to
290 also be considered. In other words, we need to calculate the *net* impact of
291 Midcontinent's resale entry as the difference between NDTC's lost revenue and cost
292 savings.

293

294 **Q. WOULD THE AVOIDED COSTS PERFECTLY OFFSET REVENUE LOST
295 FROM RESALE?**

296 A. It is unlikely that the offset would be perfect (resulting in a zero net impact) because
297 the calculated resale discount captures the average potential cost savings, rather than
298 savings associated with the specific customers who actually migrated to the resale-
299 based competitor. Certain services, such as calling features, typically contain a
300 larger mark up over costs than the average service. Application of the (average)

²⁷ See 47 CFR § 51.607.

301 avoided cost discount to these services would result in a greater loss of revenue than
302 the corresponding savings of retail expenses.

To recognize this fact, I separated from NDTC's total revenue in Devils Lake a portion of revenue that corresponds to features²⁸ and assumed that no cost savings would be realized on this revenue in case of resale. I calculated cost savings on a dollar-for-dollar basis for the remaining services subject to resale by applying the avoided cost discount to the 2004 revenue in each account. Finally, I calculated the net per line impact ("net income") of Midcontinent's resale entry by subtracting NDTC's cost savings from lost revenue. Table 5 below summarizes this analysis from Exhibit WRF-2.

TABLE 5

NDTC's Annual Per Line Net Income Loss On Resale-Based Customers at 16.15% Resale Discount						
Revenue Account	2004 Revenue Per Line	2004 Revenue Per Line Subject to Resale	Potential Revenue Loss via Resale	Potential Avoided Cost	Net Loss via Resale	
Local Network Access	\$ 308.71	\$ 308.71	\$ 49.86	\$ 45.72	\$ 4.13	
Network Access Services	\$ 529.09	\$ -	\$ -	\$ -	\$ -	
Long Distance Network Services	\$ 0.75	\$ 0.75	\$ 0.12	\$ 0.12	\$ -	
Billing and Collection Revenue	\$ 18.55	\$ -	\$ -	\$ -	\$ -	
Miscellaneous Revenue	\$ 32.14	\$ 9.86	\$ 1.59	\$ 1.59	\$ -	
TOTAL DEVILS LAKE PER LINE PER YEAR	\$ 889.24	\$ 319.32	\$ 51.57	\$ 47.44	\$ 4.13	

\$4.13 on each customer who migrates to Midcontinent. Table 6 from Exhibit WRF-2

²⁸ Features revenue is available at the company-wide level only. This data was provided in Exhibit 8A to NDTC's May 31, 2005 Tariff Filing. I used the company-wide percentage of feature revenue in total local access revenue to estimate NDTC's features revenue in the Devils Lake exchanges.

318 below expands this analysis to estimate the NDTC's total net income loss under
319 different market penetration rates:

320
321 **TABLE 6**

322 Devils Lake Net Income Loss Under Different Penetration Scenarios and 16.15% Resale Discount

NDTC Net Operating Income (2004)	\$ 2,736,472			
PENETRATION RATE SCENARIOS	2%	10%	20%	30%
Lines Lost to Resale	113	567	1,134	1,701
Estimated Annual Net Income Loss	\$ 469	\$ 2,344	\$ 4,688	\$ 7,031
Net Income Loss as % of NDTC Net Operating Income	0.017%	0.086%	0.171%	0.257%

323
324 Table 6 shows that the total annual net income loss is minimal in both absolute and
325 percentage terms compared to NDTC's overall net income under all penetration
326 scenarios. In fact, the relative loss of net income in the last column in Table 6
327 (0.257% of total NDTC net income) is lower than the relative loss of gross revenue
328 in the last column of Table 3 (0.517% of total NDTC operating revenue).²⁹

329
330 **Q. IS IT POSSIBLE THAT THE NET IMPACT OF MIDCONTINENT'S
331 RESALE-BASED ENTRY INTO NDTC'S DEVILS LAKE MARKET WOULD
332 RESULT IN A NET GAIN (RATHER THAN NET LOSS) TO NDTC?**

333 A. Yes. NDTC may experience a net gain, rather than a net loss in income if the resale
334 discount is set at a level that is lower than the avoided retail costs. Because of the
335 asymmetric nature of information necessary to determine the avoided cost

²⁹ This table does not report the net income loss relative to Devils Lake net income because the latter information is not available.

336 (information that concerns NDTc's own operations and is available to NDTc but not
 337 Midco), it is possible that a resale discount rate negotiated between parties in a
 338 settlement agreement or the discount approved by a commission based upon an
 339 interim cost estimate or another carrier's avoided cost discount could be lower than
 340 the retail costs actually avoided by NDTc. As an illustration I estimated a scenario
 341 where the resale discount is set at 14%, which is only marginally lower than the
 342 actual avoided costs (the 16.15% as assumed in the above analysis) experienced by
 343 the incumbent LEC. It turns out that even such a small discrepancy between the
 344 resale discount and avoided cost may create a net gain for NDTc:

345 **TABLE 7³⁰**

346 **NDTC's Annual Per Line Net Income Loss (Gain) On Resale-Based Customers:
 Resale Discount (at 14%) is Lower than Avoided Costs (at 16.15%)**

Revenue	2004 Revenue Per Line	2004 Revenue Per Line Subject to Resale	Potential Revenue Loss via Resale	Potential Avoided Cost	Net Loss (Gain) via Resale
Local Network Access	\$ 308.71	\$ 308.71	\$ 43.22	\$ 45.72	\$ (2.50)
Network Access Services	\$ 529.09	\$ -	\$ -	\$ -	\$ -
Long Distance Network Services	\$ 0.75	\$ 0.75	\$ 0.10	\$ 0.12	\$ (0.02)
Billing and Collection Revenue	\$ 18.55	\$ -	\$ -	\$ -	\$ -
Miscellaneous Revenue	\$ 32.14	\$ 9.86	\$ 1.38	\$ 1.59	\$ (0.21)
TOTAL DEVIL'S LAKE PER LINE PER YEAR	\$ 889.24	\$ 319.32	\$ 44.71	\$ 47.44	\$ (2.73)

347
 348 In this table the net loss is negative, indicating a net gain on each customer who
 349 migrates from NDTc to Midcontinent's resale-based service. Even if a NDTc-
 350 specific discount is used, the differential could also occur if the proportion of
 351 avoided costs to revenue subject to resale changes in future years while the effective
 352 discount rate remains static.

³⁰ Based on Exhibit WRF-4.

353

354 **Q. BASED UPON THE VARIOUS ANALYSES YOU HAVE PERFORMED,**

355 **WHAT IS YOUR CONCLUSION REGARDING THE FINANCIAL IMPACT**

356 **OF RESALE ON NDTC?**

357 A. The financial impact of resale on NDTC's Devils Lake operation will be *de minimus*
358 and in no way will be unduly economically burdensome. I therefore recommend that
359 the Commission approve Midcontinent's request to terminate NDTC's exemption
360 under 47 U.S.C. § 251(f).

361

362 **Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

363 A. Yes, it does.