BEFORE THE ILLINOIS COMMERCE COMMISSION

Docket No. 06-0027

Rebuttal Testimony Supporting Joint Proposal of W. Karl Wardin On Behalf of AT&T Illinois

AT&T Illinois Exhibit 1.5

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REBUTTAL TESTIMONY SUPPORTING JOINT PROPOSAL OF W. KARL WARDIN ON BEHALF OF AT&T ILLINOIS

I. INTRODUCTION AND PURPOSE OF TESTIMONY

Q. Please state your name and business address.

A. My name is W. Karl Wardin. My address is 225 West Randolph Street, Floor 27C, Chicago, Illinois 60606.

Q. Are you the same W. Karl Wardin who previously submitted testimony in this proceeding?

A. Yes, I am.

Q. What is the purpose of your Rebuttal Testimony supporting Joint Proposal?

A. In this testimony, I will respond to the Testimony Regarding Joint Proposal of Staff witness Dr. James Zolnierek, the Supplemental Rebuttal Testimony of Data Net Systems witness Joseph Gillan and the Supplemental Testimony of Illinois Attorney General witness Dr. Lee L. Selwyn.

II. RESPONSE TO STAFF

Q. Please summarize Staff's assessment of the Joint Proposal.

A. Staff's assessment of the Joint Proposal is positive and that it is "worthy of consideration." (Staff Ex. 9.0, lines 564-566). Dr. Zolnierek concludes that the Joint

Proposal advances many of the same objectives as Staff's own proposal in this proceeding – and will likely do so more quickly and efficiently from a market perspective and in a manner that provides more certainty that the outcome will reflect competitive market rates. Specifically, Staff finds that:

- Competitive reclassification of AT&T Illinois' residence services in MSA-1 will likely promote competition and benefit customers more over the long run than a continuation of current regulatory policies. (Staff Ex. 9.0, lines 112-141, 557-587).

- Both service packages and stand-alone measured service rate plans can be reclassified. (Staff Ex. 9.0, lines 58-105).

- The rate caps and safe harbor provisions in the Joint Proposal will likely benefit a significant number of customers. (Staff Ex. 9.0, lines 162-267).

- The Joint Proposal should be considered a worthy alternative to Staff's own proposal, because it accomplishes the same objectives, but sooner and with more certainty. (Staff Ex. 9.0, lines 557-587).

Q. Does AT&T Illinois agree with Staff's assessment?

A. Yes. If anything, Staff has understated the advantages of the Joint Proposal over its own plan.

Q. Will the Joint Proposal promote competition?

A. Definitely. All of the economists testifying in this proceeding – with the sole exception of Dr. Selwyn – agree that AT&T Illinois' stand-alone measured service rates are low and that stand-alone customers who make few calls and are not interested in central office features are not particularly attractive to competitors. As Mr. Panfil previously pointed out, competitors have made clear that, at existing rate levels, they have little interest in providing measured service rate plans. If the rates for these services are brought to a competitive market level, the residence marketplace will be more attractive to competitors overall and lower use customers will likely have more alternatives. In contrast, if stand-alone services remain under AT&T Illinois' Alternative Regulation Plan – which requires year-over-year rate decreases as long as inflation levels remain low – this situation will worsen, not improve.

Q. Dr. Zolnierek suggests that stand-alone measured service can be reclassified as competitive even if competitors do not, today, offer similar rate plans. (Staff Ex. 9.0, lines 58-105). Do you agree?

A. Yes. Since the outset of this proceeding, AT&T Illinois has taken the position that the kind of rate-plan-by-rate-plan approach taken by some of the parties is not required by Section 13-502 and is not consistent with economic theory. As Dr. Zolnierek concludes, the fact that competitors might not be offering prices comparable to AT&T Illinois' measured service offerings does not mean that competitors are not providing local exchange services at competitive rates. The evidence is clear that they are. Dr. Zolnierek's view that rates need only be comparable at "competitive market levels" is entirely appropriate, especially when coupled with the pro-competitive impact of the Joint Proposal. Otherwise, Section 13-502 is circular: competitors do not offer stand-alone rate plans today because AT&T Illinois' rates are too low, which, Dr. Selwyn contends, requires their reclassification as noncompetitive services. However, as noncompetitive services, these rates may not be restructured and cannot be made more competition-friendly without significant changes to the Alternative Regulation Plan – changes which Dr. Selwyn would undoubtedly oppose.

Q. Does AT&T Illinois support Dr. Zolnierek's assessment of the potential benefits of the Joint Proposal?

A. Yes. The safe harbor components of the Joint Proposal were intended to provide alternatives for those customers who find modest increases in their basic service rates problematical. Dr. Zolnierek primarily (and properly) evaluates the value of these rate commitments from a forward-looking perspective, assuming that AT&T Illinois implements the rate changes allowed under the Joint Proposal. As Dr. Zolnierek acknowledges, the mere fact of rate increases is not contrary to the public interest, given the fact that they are pro-competitive. Notably, network access line and local usage rates have not increased since *1990* (and, in fact, local usage rates have declined substantially under the Alternative Regulation Plan). Therefore, a maximum annual $1.00 NAL rate increase and an annual $.005 increase in the per-call local usage rate starting in 2007 over three years is hardly an unreasonable rate adjustment plan.

Q. Dr. Zolnierek suggests that the Joint Proposal may produce competitive market prices more efficiently than Staff's rate-rebalancing proposal. (Staff Ex. 9.0, lines 557-587). Do you agree?

A. Yes. In fact, in this instance, Staff is understating the benefits of the Joint Proposal. Under Staff's proposal, the Commission would reopen the Alternative Regulation Plan and adopt a multi-year transition plan that would increase stand-alone network access line rates and decrease local usage and feature rates on a revenue-neutral basis. Staff is correct that it would likely take at least a year for the Commission to develop such a plan (and several years to implement). (Staff Ex. 9.0, lines 581-584). However, Dr. Zolnierek does not focus on the rate neutrality aspect of Staff's proposal. As Mr. Panfil previously demonstrated, because all rate increases are offset by rate decreases, there is fundamentally no greater revenue opportunity for CLECs in this marketplace after the transition than there is today. Thus, this aspect of Staff's plan significantly reduces the likelihood that competition would increase during the transition period as compared to the Joint Proposal.

Q. Dr. Zolnierek reiterates Staff's position on imputation requirements, but concludes that the Joint Proposal will likely resolve the existing imputation problem more quickly than Staff's approach. (Staff Ex. 9.0, lines 497-531). Is this a significant issue?

A. Not in AT&T Illinois' view. Dr. Zolnierek seems to agree that the Joint Proposal accomplishes the policy objective of imputation when he states that it ". . . offers a reasonable alternative that likely favors speed over precision when resolving imputation concerns." (Staff Ex. 9.0, lines 527-531). Moreover, as Mr. Panfil and CUB previously explained, Staff's approach to imputation in this proceeding is not required by either the statute or the Commission's prior decision in Docket No. 04-0461. AT&T Illinois will discuss the legal issues at greater length in its brief. The Company believes that the Commission can and should resolve the imputation issues consistent with the recommendations of AT&T Illinois and CUB, which would eliminate any obstacles to approval of the Joint Proposal that might otherwise be presented by Section 13-505.1.

Q. Please summarize Staff's assessment of the portions of the Stipulation and Joint Proposal for which no Commission approval is being sought (*i.e.*, paragraphs 11-16).

A. Dr. Zolnierek only addresses two aspects of the Stipulation, paragraph 13 dealing with consumer education and paragraph 12 dealing with broadband deployment.

Q. Does AT&T Illinois support Dr. Zolnierek's opinion on consumer education (Staff Ex. 9.0, lines 457-486)?

A. Yes. Dr. Zolnierek correctly concludes that this portion of the Stipulation is not within the scope of the criteria that the Commission is required to consider under Section 13-502 and should not take this matter into consideration when making its competitive classification determination. He notes, however, that the Commission's Consumer Services Division will continue its own consumer education initiatives. With respect to the Stipulation's consumer education funding, Dr. Zolnierek also concludes that, although difficult to quantify, the benefits of an effective consumer education program outweigh its costs.

Q. What is Dr. Zolnierek's position regarding the broadband provisions in the Stipulation (Staff Ex. 9.0, lines 535-553)?

A. Dr. Zolnierek's understanding of the broadband commitment is accurate. If the Joint Proposal is approved, AT&T Illinois will install high speed digital subscriber line (DSL) Internet service to 99% of the wire centers in AT&T Illinois' Chicago LATA service area and upgrade its loop plant to make DSL available to 90% of customer living units in that area. Dr. Zolnierek correctly concludes that this additional commitment to increase broadband investment is in the public interest.

III. RESPONSE TO GILLAN

Q. Mr. Gillan asserts that "local competition for residential customers in the Chicago LATA is in broad retreat." (Data Net Ex. 5.0, lines 67-71). Do you agree?

A. No. In my Rebuttal Testimony, I presented an analysis of residential access lines served by CLECs in the Chicago LATA as of December 31, 2005. That analysis was shown in Schedules WKW-R1 and WKW-R2.

Q. In support of his assertion that "local competition for residential services in the Chicago LATA is in broad retreat," Mr. Gillan cites certain cross exhibits which he attached to his supplemental rebuttal testimony. Do those exhibits support Mr. Gillan's assertion?

A. No. Mr. Gillan has presumably attached the cross-exhibits because they show that the number of CLEC-served residential access lines in the Chicago LATA decreased from December 31, 2004 to December 31, 2005.

Moreover, the change in the number of CLEC lines during the year 2005 does not indicate that overall "local competition for residential customers in the Chicago LATA" is in "retreat." To the contrary, the data in Mr. Gillan's exhibits shows that, during 2005, the number of residential customers served by *all* wireline providers, including AT&T Illinois and the pre-merger AT&T CLEC, as well as other CLECs, declined. These line losses are a reflection of increased competition for local services from wireless and VoIP providers.

IV. RESPONSE TO DR. SELWYN

A. OVERALL ASSESSMENT OF THE JOINT PROPOSAL

Q. Dr. Selwyn contends that the Joint Proposal is not in the public interest. (AG Ex. 1.2, pp. 4-9). Do you agree?

A. No. Dr. Selwyn fundamentally misperceives the purpose of this settlement. Dr. Selwyn primarily criticizes it on the following grounds:

- The mere existence of the Joint Proposal demonstrates that reclassification is not appropriate.
- Customers currently subscribing to the "safe harbor" services will be the principal beneficiaries of the rate commitments and they represent a small percentage of AT&T Illinois' customer base.

Q. Does the mere fact of the Joint Proposal demonstrate that these services are not competitive?

A. No. AT&T Illinois has consistently stated that all of the its residence services in MSA-1 are competitive and that no transition mechanisms are required. However, *other parties* expressed concerns about the competitive alternatives available to stand-alone measured service customers who make little or no use of the network. AT&T Illinois entered into this Joint Proposal with CUB in an effort to reduce the contested issues in the proceeding. Thus, the Joint Proposal *in no way* constitutes a change in AT&T Illinois' position that all of its residence services in MSA-1 satisfy the criteria in Section 13-502(b) and (c)(1)-(4) without regard to rate commitments or service "safe harbors." These simply represent additional benefits to consumers that the Commission may consider as "other factors" that affect competition and the public interest pursuant to Section 13-502(c)(5). .

Q. Are the benefits as limited as Dr. Selwyn suggests?

A. No. Dr. Selwyn erroneously focuses on the rate reductions that accompany the "safe harbor" services. The purpose of the safe harbor commitments is to provide customers who want to take advantage of price protection with alternatives in the event that stand-alone network access line rates increase. The Joint Proposal is fundamentally *not* a rate reduction plan. At the time of AT&T Illinois' tariff filing in November 2005, most of AT&T Illinois' basic residence services were subject to the Alternative Regulation Plan and no rate reductions are required to make them "just and reasonable." AT&T Illinois agreed to reductions in the safe harbor services' rates as part of a comprehensive settlement with CUB and for no other reason. Dr. Zolnierek and Ms. McKibbin provide more realistic and appropriate analyses of the benefits of the Joint Proposal.

B. COMPETITION FOR RESIDENTIAL SERVICES

Q. Dr. Selwyn criticizes the Joint Proposal on the grounds that it does not "offer price protection" to customers who purchase packages of services other than the three "safe harbor" packages. (AG Ex. 1.2, p. 21). Is Dr. Selwyn's criticism justified?

A. No. In support of his criticism, Dr. Selwyn asserts that there would be no "regulatory or market constraint on IBT's prices for the package services" if the Joint Proposal is approved. This assertion is without merit. The evidence that has been presented by AT&T Illinois and the Commission Staff demonstrates that residential service packages that have been reclassified as competitive are reasonably available from numerous alternative providers throughout the Chicago LATA, including CLECs, wireless carriers and VoIP providers. The availability of services from these alternative providers does, in fact, constrain AT&T Illinois' ability to increase the prices of its residential local exchange services, including packages.

Q. Do you have additional evidence that refutes Dr. Selwyn's claim that there are no "price constraining competitive alternatives" to AT&T Illinois for the provision of residential local exchange service in the Chicago LATA? (AG Ex. 1.2, p. 25).

A. Yes. The evidence that I have presented above in response to Mr. Gillan directly refutes Dr. Selwyn's claim. Moreover, my Direct Testimony included several tables, which I have updated, which further demonstrate that consumers are continuing to choose competitive alternatives to AT&T Illinois for residential local exchange service. Table 1, below, details changes to AT&T Illinois' residential access lines since 2000. It shows that over the past five years AT&T Illinois has lost about 1.4 million residential access lines. This represents a 32% reduction since 2001 and is equivalent to about 46% of AT&T Illinois' residential access lines as of December 2005.

Table 1

AT&T Illinois Residential Access Line Changes (2000 – 2005)					
End of Year	Total Residential Access Lines	Annual Change	Cumulative Change	Annual % Change	Cumulative % Change
2000	4,288,582				
2001	3,871,354	-417,228	-417,228	-9.7%	-9.7%
2002	3,376,547	-494,807	-912,035	-12.8%	-21.3%
2003	3,104,394	-272,153	-1,184,188	-8.1%	-27.6%
2004	2,960,631	-143,763	-1,327,951	-4.6%	-31.0%
2005	2,927,988	-32,643	-1,360,594	-1.1%	-31.7%

Source: 2001 to 2005, ARMIS Report 43-08, TABLE III - ACCESS LINES IN SERVICE BY CUSTOMER.

Table 2, below, details the wireless growth since year end 1999. The 118% growth in wireless service is in stark contrast to the 32% decline in AT&T Illinois residential lines. To put the number of wireless phones in perspective, there are more wireless subscribers than wireline subscribers. For example, at the end of June 2005, there were 8,530,462 wireless subscribers in Illinois as compared to 7,815,880 wireline subscribers in Illinois.

Table 2

Illinois Wireless Telephone Subscribers (1999 – 2005)					
Year End	Illinois Wireless Users	Annual Change	Cumulative Change	Annual % Change	Cumulative % Change
1999	3,922,482				
2000	5,143,767	1,221,285	1,221,285	31.1%	31.1%
2001	5,631,172	487,405	1,708,690	9.5%	43.6%
2002	6,476,683	845,511	2,554,201	15.0%	65.1%
2003	7,183,989	707,306	3,261,507	10.9%	83.1%
2004	8,075,938	891,949	4,153,456	12.4%	105.9%
June ‘05	8,530,462	454,524	4,607,980	11.3%	117.5%

Source: FCC, Local Telephone Competition: Status as of June 30, 2005, released April 2006. The June 2005 line represents ½ year and therefore the annual change percent figure is doubled.

Tables 3 and 3A depict wireless revenues and their growth as compared to AT&T Illinois’ local service revenues and their decline. Since 2000, AT&T Illinois’ basic local service revenues[1] have declined by 47% and nationally wireless service revenues have increased by over 150%. These Tables also show that since 2000 AT&T Illinois’ local service revenues have declined by about $1.3 billion, while at the same time wireless carriers in Illinois have increased their revenue by $2.9 billion.[2] [3]

[1] ARMIS defines basic local revenues as the sum of Accounts 5001, 5040, and 5060, and are defined under the FCC's C.F.R. Part 32 and the ICC's Part 710 (see §32.5001, § 32.5040, §32.5060).

[2] The Illinois wireless number was derived by taking Illinois wireless growth (4,607,980) and dividing it by wireless growth from Dec ‘99 to Jun ’05 (108,432,361) and multiplying that result by the change in revenue since 2000 (68,242,671).

[3] For the year 2005 CTIA’s survey reports $113.5 billion in wireless service revenues. The combined RBOCs reported $96.6 billion in regulated and nonregulated landline revenues. See ARMIS Report 43-01 Table I.

Table 3

AT&T Illinois BASIC Local Service Revenues (2000 - 2005)					
Year End	Amount	Annual Change	Cumulative Change	Annual % Change	Cumulative % Change
2000	2,735,937				
2001	2,428,897	-307,040	-307,040	-11.2%	-11.2%
2002	1,973,738	-455,159	-762,199	-18.7%	-27.9%
2003	1,736,401	-237,337	-999,536	-12.0%	-36.5%
2004	1,516,213	-220,188	-1,219,724	-12.7%	-44.6%
2005	1,446,837	-69,376	-1,289,100	-4.6%	-47.1%

Source: Illinois Bell Annual Alternative Regulation Monitoring Report Filed with the ICC.

Table 3A

Wireless Industry Total Service revenues (6/1999 - 12/2005)					
July 1 to June 30	Industry Wireless Revenues	Annual Change	Cumulative Change	Annual % Change	Cumulative % Change
2000	45,295,550				
2001	58,726,376	13,430,826	13,430,826	29.7%	29.7%
2002	71,117,599	12,391,223	25,822,049	21.1%	57.0%
2003	81,185,272	10,067,673	35,889,722	14.2%	79.2%
2004	95,515,593	14,330,321	50,220,043	17.7%	110.9%
2005	108,534,727	13,019,134	63,239,177	13.6%	139.6%
Dec '05	113,538221	5,003,494	68,242,671	9.2%	150.7%

Source: CTIA Semi-Annual Wireless Industry Survey, Annualized Wireless Industry Survey Results – June 1985 to June 2005. The June 2005 line represents ½ year and therefore the annual change percent figure is doubled.

Q. You mentioned the decline in AT&T Illinois' residential access lines from 2000 through 2005. Do you have evidence that this trend is continuing in the Chicago LATA?

A. Yes. Tables 4 and 4A below show that AT&T Illinois has not only lost residential access lines in the Chicago LATA, it is continuing to lose residential primary access lines at an increasing pace. Since 2000, AT&T Illinois has, through the first quarter of 2006, lost over one million residential access lines in the Chicago LATA, or approximately 30% of all such lines. During the same time period, AT&T Illinois has lost almost 700,000 primary residential access lines in the Chicago LATA or approximately 26% of such lines.

Table 4

AT&T Illinois Chicago LATA Residential Access Line Changes (Dec 2000 - 1st Quarter 2006)					
Year End	Total Chicago LATA Residential Access Lines	Annual Change	Cumulative Change	Annual % Change	Cumulative % Change
2000	3,372,979				
2001	3,048,504	-324,475	-324,475	-9.6%	-9.6%
2002	2,721,082	-327,422	-651,897	-10.7%	-19.3%
2003	2,535,531	-185,551	-837,448	-6.8%	-24.8%
2004	2,422,559	-112,972	-950,420	-4.5%	-28.2%
2005	2,383,477	-39,082	-989,502	-1.6%	-29.3%
1Qtr '06	2,365,318	-18,159	-1,007,661	-3.0%	-29.9%

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Table 4A

AT&T Illinois Chicago LATA Residential Primary Access Line Changes (Dec 2000 - 1st Quarter 2006)					
Year End	Total Chicago LATA Residential Access Lines	Annual Change	Cumulative Change	Annual % Change	Cumulative % Change
2000					
2001					
2002					
2003					
2004					
2005					
1Qtr '06					

*****END CONFIDENTIAL AND PROPRIETARY*****

Q. In support of his assertion regarding the lack of competitive alternatives, Dr. Selwyn asserts that, in her March 6, 2006 testimony, CUB witness McKibbin "presented evidence that, for many areas – even in portions of the Chicago exchange – the most often-cited competitors, the cable companies, do not provide local service." (AG Ex. 1.2, p. 22). Do you have any comments in response to this assertion?

A. Yes. The testimony of Ms. McKibbin cited by Dr. Selwyn addresses only three of the over 70 CLECs which provide residential local exchange service throughout the Chicago LATA. The fact that not every one of these CLECs provides service in every single exchange does not mean that reasonably available alternatives do not exist throughout the Chicago LATA. In fact, they do, as I demonstrated in my direct and rebuttal testimony. In the Chicago exchange itself, 71 CLECs, including Comcast and RCN, the two cable companies referenced by Dr. Selwyn, served *****BEGIN CONFIDENTIAL AND**

PROPRIETARY*************END CONFIDENTIAL AND PROPRIETARY*** residential access lines as of March 31, 2006, as shown in Schedule WKW- JPR1.

Q. Dr. Selwyn asserts the number of Digital Phone lines in the City of Chicago, as reported by Comcast in response to the Commission's information request in Docket No. 06-0028, "confirms that Comcast's Digital Phone service is not widespread." (AG Ex. 1.2, p. 28). Do you have a response to Dr. Selwyn's assertion?

A. Yes. Comcast responded to Staff that it has ***BEGIN CONFIDENTIAL AND PROPRIETARY**************END CONFIDENTIAL AND PROPRIETARY*** Digital Phone customers in the Chicago LATA. This is a substantial number of customers. Moreover, as Dr. Selwyn acknowledges, Comcast is transitioning from its Digital Phone, circuit switched service to its Digital Voice, VoIP-based service.

Q. Is Comcast's Digital Voice Service currently available to customers in the Chicago Exchange?

A. Yes, it is. Comcast's website allows one to check for the availability of its services by address and zip code. In May 2006, I inputted zip codes that correspond to all five of the Chicago Cable Zones. A map of the Cable Zones is contained in AT&T Illinois Exhibit 11.0, a copy of which is attached. The website showed that Digital Voice Service is currently available in four of the five cable zones (all but Chicago Cable Zone 2). To verify the accuracy of the information on the website, I also called Comcast service representatives four times to inquire about the availability of Digital Voice Service in zip codes 60618, 60630, 60646, and 60643, four of the Chicago zip codes for which the website indicated availability. The Comcast service representatives confirmed that Digital Voice Service is currently available to customers residing in each of those zip codes.

Q. Dr. Selwyn asserts that Comcast does not represent a price constraining alternative to AT&T Illinois' local service packages. (AG Ex. 1.2, pp. 28-29). Is Dr. Selwyn correct?

A. Absolutely not. Comcast is competing heavily and effectively with AT&T Illinois for the provision of local and long distance service packages. Currently, Comcast is engaged in an intense direct mail advertising campaign to convince customers of AT&T Illinois to switch to Comcast for home phone service, Comcast Digital Voice. Examples of Comcast's direct mail pieces, which have been received by employees of AT&T Illinois at their homes in recent weeks, are contained in Schedule WKW-JPR3. These mailings have been received in locations throughout the Chicago LATA, including Chicago, Lombard, Grayslake, Algonquin, Crystal Lake, Dundee, Woodridge, Cary, Deerfield, Bolingbrook, Woodstock, Elmhurst, Brookfield, Bensenville, Elgin, Oak Park, Roselle, Berwyn, Lake Zurich, Schaumburg, Rolling Meadows, Wheaton, and Wilmette. Comcast's advertising is not limited to direct mail. Comcast also uses other media, such as the full page ad they ran in the Chicago Sun-Times on Friday, May 26, 2006, for Digital Voice, Internet and cable TV. A copy of that ad is included in Schedule WKW-JPR3-Part 6.

Comcast's marketing has been very effective. Based on data obtained from the E9-1-1 database, as of March 31, 2006, Comcast had ***BEGIN CONFIDENTIAL AND PROPRIETARY*************END CONFIDENTIAL AND PROPRIETARY *** access lines, as shown in Schedule WKW- JPR1, an increase of ***BEGIN CONFIDENTIAL AND PROPRIETARY ********* ***END CONFIDENTIAL AND PROPRIETARY *** since December 31, 2005. In each month from December 2005 through March 2006, AT&T Illinois has lost more lines to Comcast than to any other competitor. Competition from Comcast was a significant factor driving AT&T Illinois' net loss of 18,159 access lines during the first quarter of 2006.

Q. Dr. Selwyn asserts that "at prices starting at $54.95, Comcast Digital Voice will not discourage IBT from raising the prices of its local packages." (AG Ex. 1.2, p. 29). Is Dr. Selwyn's assertion accurate?

A. No. First, Dr. Selwyn has failed to fully explain Comcast's prices. Comcast offers a Digital Voice package that includes unlimited local and long distance calling, 12 calling features plus Voice Mail, and one-line voice mail access and account detail. For customers who subscribe to both Comcast's cable and high speed Internet services, the price for the Digital Voice (CDV) package is $39.95.[4] For customers who subscribe to Comcast's cable or high speed Internet service, but not both, the price of the CDV package is $44.95. The $54.95 price mentioned by Dr. Selwyn is the price of the CDV package for customers who do not subscribe to either Comcast's cable or high speed

[4] The Comcast Service representative at 866-594-1234 indicated that there is a special price for the Triple Play (basic cable, High Speed Internet, and CDV) of $99 per month for the first 6 months.

Internet service. On May 30, 2006, I spoke to a Comcast service representative who indicated that Comcast would be willing to offer me a $33 rate for six months for stand-alone CDV. Since many customers in the Chicago LATA subscribe to Comcast's cable service, high speed Internet service or both, it is the lower prices available to such customers, not the $54.95 price cited by Dr. Selwyn, which is relevant to the question of whether Comcast's Digital Voice offer constrains AT&T Illinois' ability to increase the prices of its offerings.

Second, it is not credible to assert that Comcast does not represent a price constraining alternative to AT&T Illinois' local service packages or is actively marketing its CDV at $54.95. Comcast emphasizes in its direct mail advertising that the price of its Digital Voice package is $39.95, if purchased with cable and cable modem service, and claims that this price "could save more than 16% over the phone company." This Comcast claim is based on a comparison to AT&T Illinois' $48.95 All Distance plan[5], which includes an access line, Caller ID with name, Line-Backer, Voice Mail, two selectable calling features and unlimited long distance. Comcast's advertising further notes that while AT&T Illinois also charges a $4.50 End User Common Line Charge, such a charge is not assessed for Digital Voice. Given Comcast's success in competing with AT&T Illinois, it is absurd to suggest that Comcast's offerings impose no constraints on AT&T Illinois' ability to raise its prices for packages.

[5] The price for AT&T Illinois' All Distance Plan is $49.95, not $48.95, as described by Comcast.

Q. You have discussed Comcast's advertising. Are other CLECs and VoIP providers actively marketing their services to residential local exchange customers in the Chicago LATA?

A. Yes, they are. In her Direct Testimony, AT&T Illinois witness Sandy Moore presented numerous examples of such advertising. More recent examples of direct mail advertising, all from this year (2006), are attached in Schedule WKW- JPR4 for Sage, RCN, Sun Rocket, WOW![6], Vonage and Earthlink.

Q. Dr. Selwyn asserts that the "prices quoted by McLeod on its website are only available to customers in certain locations where switching can be provided by a McLeod switch in conjunction with an IBT UNE-loop." (AG Ex. 1.2, p. 24). Do you have any comments in response to this assertion?

A. Yes. According to its tariff, McLeod currently provides residential basic local exchange service using its own switch in 51 Chicago LATA exchanges, including the Chicago Exchange. These 51 exchanges encompass 83% of AT&T Illinois' residential network access lines in the Chicago LATA. Accordingly, based on Dr. Selwyn's representation of the information he obtained from McLeod, its service is available to the vast majority of residential customers in the Chicago LATA at prices that do not include the alleged "additional $15-20 fee element added to the base rate for local service."[7]

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[6] WOW! Provides bundled voice service in Chicago Cable Area 5 to zip codes such as 60643.

[7] McLeodUSA's Illinois tariff, (Illinois C.C. Tariff No. 4 revised sheet No. 82 and Sheets No. 132 to 145), make it clear that the Local Line Price Adjustment surcharge of $0 for Access Area A, $15 for Access Area B and $13 for Access Area C applies only to lines established prior to January 19, 2006 and it does not apply to lines provisioned after that date. This was confirmed by talking to a McLeodUSA service representative on May 31, 2006. However, as stated above, most of the residential lines in the Chicago LATA can be served by a

Q. Dr. Selwyn asserts that MCI has "run for the exits" and is no longer competing for residential local exchange customers in Illinois. (AG Ex. 1.2, p. 30). Is Dr. Selwyn correct?

A. No. As I explained in my Rebuttal Testimony, there is no evidence that MCI has "exited" the residential market in Illinois. *****BEGIN CONFIDENTIAL AND PROPRIETARY*** *****END CONFIDENTIAL AND PROPRIETARY *****

C. EFFECT OF JOINT PROPOSAL ON PRICES

Q. Dr. Selwyn contends that one of the ". . . fundamental goals of a competitive telecommunications policy is to bring telecom prices *down*, not up." (AG Ex. 1.2, p. 29). Is he correct?

A. No. I am not an economist, but I understood the purpose of a competitive telecommunications policy is to bring telecom prices to *competitive market levels*. Those prices may be higher or lower than what regulators have prescribed. As Dr. Taylor explained, where the regulatory process has kept prices low, then it is entirely predictable that a competitive marketplace could result in higher prices. Conversely, where

McLeodUSA switch. For example, to a consumer who lives in the Chicago Exchange, with a 60643 zip-code, McLeodUSA (one of four facility-based wireline providers in that area) offers five packages with unlimited local service starting at $20.95. Its Preferred Advantage Unlimited package is $39.95 and includes unlimited local and long distance calling, up to 13 features including voice-mail. The $39.95 price of the package includes the EUCL and LNP surcharges.

regulators have kept prices high to provide support to other services, those prices may decline. The end result cannot be known until the marketplace has had a chance to function on a competitive basis.

Q. Dr. Selwyn asserts that if the Joint Proposal is approved, it is likely to result in rate increases producing "cumulative additional revenues over the period through 2010, of approximately $296.5 million." (AG Ex. 1.2, p. 27). Is there any basis for the AG's assertion?

A. No. Dr. Selwyn's assertion is based on a number of erroneous and unsupported assumptions.

First, Dr. Selwyn asserts that if AT&T Illinois were to increase its stand-alone network access line and usage rate to the full extent allowed by the Joint Proposal, those rate increase would affect all of the existing 830,000 local measured service lines in the Chicago LATA, providing cumulative additional revenues through 2010 of approximately $116 million. This assertion assumes that not one of the existing 830,000 local measured service customers will take advantage of the "safe harbor" packages which were designed with the express purpose of providing local measured customers who make few calls or use two or fewer features with a means of avoiding the impact of potential increases in stand-alone network access line and usage rates. This assumption is baseless. As I discussed in my Direct Testimony Supporting Joint Proposal, AT&T Illinois estimates that even at the current network access line and usage rates, 64% (528,654 or 830,236) of residential local measured rate customers can potentially benefit from switching to one of the "safe harbor" packages. As indicated by AT&T Illinois' response to Staff Data Request GS 3.02, if AT&T Illinois were to increase the network access line and usage rates by the minimum amount allowed under the Joint Proposal, the number of stand-alone customers who could potentially benefit form switching to one of the "safe harbor" packages would increase to 817,613 by the year 2008.

Second, Dr. Selwyn assumes that AT&T Illinois will increase rates to customers who purchase packages other than the "safe harbor" packages, producing "as much as $32.94 million in additional revenue each year through 2009." (AG Ex. 1.2, p. 27). This overstates cumulative additional revenues through 2010 by approximately $164 million, or 55% of Mr. Selwyn's $296.5 million estimate. This flawed assumption, however, is based on the erroneous assertion that there is no price constraining competition for packages. As I have previously discussed, there is no basis for this assertion.

Third, Dr. Selwyn includes in his calculation of the cumulative potential revenue resulting from the Joint Proposal an assumption that the pre-merger AT&T CLEC will increase rates to all of its customers. (AG Ex. 1.2, p. 26). The services provided by that entity are, however, already competitive. The Joint Proposal has no bearing whatsoever on the prices charges by the pre-merger AT&T CLEC. This overstates the cumulative additional revenues by another $16.2 million.

Removing these two overstatements decreases the $296.5 million figure, as calculated by Dr. Selwyn, to about $116 million. Additionally, this $116 million figure is overstated since it erroneously assumes that not a single residential customer purchasing stand-alone services would move to a "safe harbor" package. This $116 million cumulative figure would be equivalent to an increase in annual revenues of about $38.7 million.

Q. How does the $38.7 million increase compare with the reduction in AT&T Illinois' annual local service revenues since 2000?

A. The $38.7 million annual increase is equivalent to about 3% of the $1.3 billion reduction in AT&T Illinois' annual basic local service revenues (see Table 3 above) since 2000.

Q. Dr. Selwyn asserts that AT&T Illinois' ability to impose an additional $1.00 charge on the prices for packages of local services will be "protected" by increases in the base LWC monthly rates of $1.00 per year for 2006 and 2007, and by the annual increase in the urban Consumer Price Index thereafter. (AG Ex. 1.2, p. 27). Do you agree with this assertion?

A. No. Assuming that the Joint Proposal is approved, the prices that AT&T Illinois will be able to charge for packages of local services will be established by the market for retail residential service and will not be a function of wholesale rates paid by LWC carriers. AT&T Illinois' ability to increase its prices for all services, including packages, will be constrained by the retail prices charged by competing service providers, which include not only LWC carriers but also facilities-based CLECs such as Comcast, UNE-L carriers such as McLeod, independent VoIP providers and wireless providers. In this regard, I would note that, as of March 31, 2006, the number of Chicago LATA residential access lines served by facilities-based CLECs (including UNE-L providers) is 315,670, more than twice times the number of residential access lines served by LWC-based CLECs (151,479), as shown on Schedule WKW- JPR1.

D. CONSUMER EDUCATION FUNDING

Q. Dr. Selwyn disparages the $2.5 million for consumer education that AT&T Illinois will provide to CUB as being no match for AT&T Illinois' marketing budget. (AG Ex. 1.2, pp. 10-11). Is he correct?

A. No. Dr. Selwyn compares the $2.5 million to the $182 million which AT&T Illinois spent on "marketing-related activities" in 2005. (*Id.*, p. 11). This is the wrong comparison. The $182 million includes product management, *i.e.*, the development of new service offerings and the monitoring of AT&T Illinois' existing offerings in the marketplace, both "backroom" functions that customers do not see. The $182 million also includes "sales," which encompasses the Company's business offices which process service orders and handle a myriad of interactions with customers, including bill inquiries and bill disputes.

The appropriate comparison would be to AT&T Illinois' product advertising – *i.e.*, the amounts spent on print, radio, television and direct mail used to promote AT&T Illinois' products (Account 6613). AT&T Illinois spent $6.8 million in 2005 to promote all of its retail products, both residence and business and on a state-wide basis. The amount spent on promoting residence packages in 2005 was only *****BEGIN CONFIDENTIAL AND PROPRIETARY**********END CONFIDENTIAL AND PROPRIETARY***** million. Again, this is a state-wide number. The $2.5 million in funding that AT&T

Illinois is providing to CUB is significant relative to its product advertising budget for residence services.

Q. Dr. Selwyn implies that AT&T Illinois will engage in counter-marketing when CUB advises customers of their options under the Joint Proposal. (AG Ex. 1.2, p. 11). Is this correct?

A. No. AT&T Illinois has no intention of engaging in counter-marketing.

Q. Dr. Selwyn contends that AT&T Illinois' website is difficult to use and that information about the three "safe harbor" services is not easily accessed. (AG Ex. 1.2, pp. 11-12). Do you agree?

A. No. AT&T Illinois' website is easily accessible. AT&T Illinois is committed to providing as "consumer-friendly" an Internet experience as possible. Internet purchases are becoming a way of life today for many customers. Moreover, AT&T Illinois' costs of processing a service order placed online are much lower than taking the order through the business office, which requires the involvement of service representatives. Therefore, it is very much in AT&T Illinois' interest to offer a website that is easy to navigate and attractive to customers. However, the Company offers a wide range of services and rate plans today. This fact necessarily results in a much more complex website than would otherwise be the case. AT&T Illinois continually reviews its website to determine whether improvements can be made.

With respect to the three safe harbor services in particular, they have not been of much interest to customers to date – as Dr. Selwyn himself recognizes. (AG Ex. 1.2, pp. 6-7). Therefore, they have been a low priority from the standpoint of web design. However, as part of implementing the Joint Proposal, AT&T Illinois will review its business office practices and its webpage relative to these products, given their increased importance to customers. Likewise, Paragraph 11 of the Joint Proposal requires AT&T Illinois to take the necessary steps to reflect the new names of these three safe harbor services in appropriate internal methods and procedures, service representative material, Internet webpage listings and billing information.

Q. Ms. Zolot states that the AT&T Illinois website was "not working" twice when she attempted to use it. (AG Ex. 3.0, lines 57 and 85-89). Is this a common problem?

A. No. Whatever "not working" means, AT&T Illinois' website and online ordering tools are rarely down. For example, since January 2006, the web ordering tool was up 99.34% of the time and the web "shopping cart" was up 99.94% of the time. Ms. Zolot's experience seems to be highly atypical.

Q. Dr. Selwyn cites to an investigation of Pacific Bell by the California PUC which led to a 2001 marketing practices order. (AG Ex. 1.2, pp. 12-14). Is this decision relevant to this proceeding?

A. No. This proceeding is examining whether AT&T Illinois' residence services are competitive under Section 13-502 of the Act – not marketing practices.

Q. Have any of the other AT&T states had a similar order entered by their PUC?

A. Not to my knowledge. The California order appears to be unique to California.

Q. Do consumers in Illinois appear to have concerns about the marketing practices of the telecommunications carriers in this state?

A. Not to my knowledge. The best source available to assess this issue is the Annual Report issued by the Consumer Services Division of the Commission. The most recent report is for calendar year 2004 (the 2005 Annual Report should be released shortly). In that Report, the Consumer Services Division identifies the complaints they receive each year against regulated companies by industry, by number and by category of complaint. The top ten categories of complaints lodged with the Commission against telecommunications carriers were as follows:

REASON FOR CONTACT (detail problem codes)	NUMBER
Questions Responsibility for Account	760
Other- Wholesale Rates	749
Dispute Rate Class or Plan	742
Usage- Consumption	464
Schedule for Repair	439
Accuracy of Bill	436
Installation of New Service	399
Reconnection or Disconnection	394
Termination- Seeking Reconnection	341
Protest Rates	340

Based on conversations with the Consumer Services Division, AT&T Illinois understands that the "Dispute Rate Class or Plan" category primarily involves contentions that the customer was placed on a different plan than the customer thought he/she had selected. The "Protest Rates" category typically involves generalized customer complaints that rates are "too high." Neither of these two categories involve the kind of marketing issues raised by Dr. Selwyn. None of the other categories appear to have any relevance to marketing practices at all. Since AT&T Illinois is the largest provider of local exchange services in Illinois, it accounts for the largest number of complaints. Therefore, these data are likely to be representative for it individually, as well as for the industry as a whole.

Q. Dr. Selwyn suggests that customers currently subscribing to unlimited usage packages do not have sufficient information to decide whether they are on the right plan, because their monthly bills may not provide "any calling details, such as the total number of calls, total number of minutes or any itemization of individual calls." (AG Ex. 1.2, pp. 30-31). Is that true?

A. No. As demonstrated by the bills submitted by Ms. Zolot, AT&T Illinois' bills display the total number of local calls made each month by the customer and itemize every long distance call by time of day and total number of minutes. This is sufficient information to compare package prices to per-call rate plans. AT&T Illinois bills all local calls on a per-call basis, so that the local call total shown on the bill would simply be multiplied by $.03 per call to gauge the likely total local usage charges under a measured service plan (although there are also volume discounts that would be more difficult for customers to estimate, the simple $.03 times the number of local calls calculation provides a good proxy for local calling charges under measured service). Many long distance carriers (including AT&T Long Distance) have a per-minute plan. To determine total charges under this kind of rate plan, the per-minute rate for the long distance calls would be multiplied by the total number of minutes on the bill to determine the total long distance charges under a per-minute rate structure. These are not particularly complex calculations.

I appreciate that comparing rate plans can be confusing for some customers – Ms. Zolot apparently is one of them. AT&T Illinois regrets the fact that she felt that its service representatives were not as helpful as they could have been. However, this was simply one customer's experience. In any event, it is my understanding that CUB's consumer information campaign will be directed at customers like Ms. Zolot who have difficulty making rate plan comparisons for themselves.

Q. Dr. Selwyn suggests that the Commission would lose regulatory authority over AT&T Illinois' marketing practices if these services were declared competitive. (AG Ex. 1.2, pp. 36-37). Is this true?

A. No. A competitive classification does not constitute deregulation. The Commission retains jurisdiction over the reasonableness of AT&T Illinois' rate levels and business practices. However, any inquiry into these issues would properly be directed at AT&T Illinois and its competitors collectively to ensure even-handed treatment of all competitive providers in the marketplace.

E. FINANCIAL DATA

Q. Dr. Selwyn discusses certain financial results as reported in ARMIS and asserts that "these results, standing alone, provide compelling evidence of IBT's monopoly power." (AG Ex. 1.2, p. 39). Is Dr. Selwyn's assertion justified?

A. No. A complete financial picture demonstrates significant revenue loss consistent with a competitive marketplace. Dr. Selwyn, however, cherry-picked selected financial results, as reported in ARMIS, which he erroneously claims supports his assertion. Dr. Selwyn's discussion of those results is highly misleading. Moreover, Dr. Selwyn completely ignored, and omitted from his Table 2, financial results which demonstrate the enormous impact that competition in the market for local exchange service is having on AT&T Illinois. To present a complete picture, I have revised Dr. Selwyn's Table 2 to include such results, as shown in Table 5, below. The financial results which Dr. Selwyn excluded from his Table 2 are shaded.

Table 5
Illinois Bell Telephone Company
Financial Results as Reported in FCC ARMIS (Note 1)
December 31, 2001 through December 31, 2005 (000's)

	2001	2002	2003	2004	2005	TOTALS	CHANGE	2001 - 2005 Percentage
Total Stockholders' Equity	2,523,200	2,580,161	2,008,332	1,840,220	1,586,596		(936,604)	-37.1%
Total Switched Access Lines	6,230,181	5,969,763	5,479,186	5,217,259	5,150,602		(1,079,579)	-17.3%
Residential Access Lilnes	3,871,354	3,376,547	3,104,394	2,960,631	2,927,988		(943,366)	-24.4%
Local Services Revenues	2,428,897	1,973,739	1,736,401	1,516,212	1,446,837		(982,060)	-40.4%
Total Operating Revenues	4,147,646	3,764,102	3,739,032	3,728,323	3,730,451		(417,195)	-10.1%
Total Operating Expenses	2,593,330	2,910,029	3,020,268	3,048,556	2,957,084		363,754	14.0%
Net Income	653,176	279,726	199,586	260,769	333,884	1,073,965	(319,292)	-48.9%
Dividends Declared	642,834	532,088	771,416	428,881	587,508	2,319,893	(55,326)	-8.6%
Total Plant (Note 2)	12,441,237	12,941,163	13,088,293	13,250,278	13,479,390		1,038,153	8.3%
Telecom Plant in Service, Begin Bal.	11,346,357	12,267,508	12,731,792	12,982,810	13,169,786		1,823,429	16.1%
Plant Additions	1,085,425	800,433	499,692	456,530	451,758	3,293,838		Note 3
Plant Retirements	160,669	272,217	225,439	247,399	218,059	1,123,783		35.7%
Transfers Adjustments	(3,605)	23,558	(23,235)	(22,155)	(8,255)	(33,692)		129.0%
Telecom Plant in Service, End Bal.	12,267,508	12,819,282	12,982,810	13,169,786	13,395,230		1,127,722	9.2%
Accumulated Depreciation	6,681,547	7,239,940	7,880,293	8,509,832	9,199,572		2,518,025	37.7%
Net Plant	5,585,961	5,579,342	5,102,517	4,659,954	4,195,658		(1,390,303)	-24.9%
Return on Stockholders' Equity	25.90%	10.84%	9.94%	14.17%	21.04%			-18.8%
Intrastate Rate of Return (Note 4)	18.96%	10.27%	9.96%	8.66%	8.98%		-52.70%	-52.6%
Total Depreciation and Amortization	6,736,681	7,330,060	7,883,093	8,510,510	9,200,480		2,463,799	36.6%
Net Plant	5,704,556	5,611,103	5,205,200	4,739,768	4,278,910		(1,425,646)	-25.0%
Illinois Bell Employment	15,768	13,888	12,979	12,287	11,187		(4,581)	-29.1%
Employment Total in Illinois including the Service Company and Affiliates (Note 5)	23,696	22,160	21,047	20,098	19,271		(4,425)	-18.7%

Note 1: Source is ARMIS unless otherwise noted.
Note 2: Inappropriate as a measure of investment providing service. Measure includes Nonoperating Plant and Goodwill.
Note 3: Year-over-year percentage change is inappropriate. Total plant additions over the period were $3.3B, an amount comparable to the preceding 5 year period. Illinois Bell exceeded the $3B infrastructure spending commitment under alternative regulation by 10%.
Total Plant Additions over the period 2000-2004 were $3.8B. Illinois Bell exceeded the $3B SBC/Ameritech Merger Condition 7 amount by 26%.
Note 4: Source is Illinois Bell's Annual Monitoring Report, Exhibit B, Intrastate Amount, Column (e).
Note 5: Internal source.

Q. Please provide an example of how Dr. Selwyn's discussion of the ARMIS data is misleading.

A. Dr. Selwyn asserts that AT&T Illinois' net earnings increased from 2004 to 2005, resulting in a 21.04% return on shareholder's equity for 2005, up from 14.7% in 2004. Dr. Selwyn asserts that these earnings are at "supracompetitive levels." Dr. Selwyn, however, presents no analysis of comparable "competitive" earnings to support that assertion. Moreover, the return on equity figure which Dr. Selwyn cites is not indicative of the profitability of AT&T Illinois' local exchange services. To the contrary, the net earnings and return on equity figures relied on by Dr. Selwyn represent earnings for *all* of

AT&T Illinois' operations, both interstate and intrastate, and both regulated (including competitive and non-competitive) and non-regulated. In this regard, as shown in my Table 5, in 2005, local service revenues (which includes all business and residential local exchange services) were approximately $1.4 billion, equal to only 39% of the total operating revenue of approximately $3.7 billion.

Moreover, Dr. Selwyn's testimony is extremely misleading even as it relates to AT&T Illinois' overall net earnings. Dr. Selwyn asserts that AT&T Illinois has experienced a "persistent increase in earnings" (AG Ex. 1.2, p. 37), which Dr. Selwyn suggests is indicated by the net earnings figures for 2002 through 2005, as shown on his Table 2. Dr. Selwyn, however, neglected to include in his Table 2 the net earnings and return on equity figures for 2001, even though other financial results for 2001 are shown in the Table. As shown by my Table 5, when the full results for 2001 are included, it is clear that, far from a "persistent increase in earnings," AT&T Illinois experienced a 48.9% *decrease* in net earnings, from $653.18 million in 2001 to $333.88 million in 2005. The 2005 return on equity is also less than the return on equity for 2001.

Q. Does Dr. Selwyn ignore more pertinent evidence regarding AT&T Illinois' earnings?

A. Yes. As shown in my Table 5, AT&T Illinois' overall earned return on intrastate plant investment was 8.98%, a very small increase over the 8.66% return in plant investment in 2004 and a 53% *decrease* from the 18.96% return on intrastate plant investment for 2001. The rate of return on intrastate plant investment is a far better indication of the profitability of AT&T Illinois intrastate operations than the return on equity percentages cited by Dr. Selwyn.

Q. Are there other financial results which refute Dr. Selwyn's claim that AT&T Illinois has "undiminished monopoly power?"

A. Yes. As indicated in my Table 5, Dr. Selwyn's assertion completely ignores the facts that, over the period from 2001 through 2005 (the time period "analyzed" by Dr. Selwyn):

- the number of AT&T Illinois' switched access lines (including business and residential) *decreased* by 1,079,579 (of which 943,366 were residential), or 17%; and
- AT&T Illinois' annual local service revenues *decreased* by $982 million, or 40%.
- Moreover, as previously discussed, since 2000 the number of AT&T Illinois' residential access lines decreased by approximately 1.4 million, or 32%.

Dr. Selwyn ignores these relevant local results and misses the point completely. These trends are evidence of an extremely competitive market for local services, not "monopoly power."

Q. Dr. Selwyn asserts that the data shown in his Table 2 shows that "SBC (now AT&T, Inc.) has been steadily *disinvesting* in its Illinois operations for at least the past four years." (AG Ex. 1.2, p. 38). Is Dr. Selwyn's assertion valid?

A. No. First, Dr. Selwyn's assertion regarding "disinvestment," like most of the assertions on his supplemental testimony, has nothing whatsoever to do with the question being addressed in this proceeding (whether the residential services at issue were properly classified as “competitive”), much less the issues addressed by the Joint Proposal.

Furthermore, Dr. Selwyn’s allegations regarding “disinvestment” are based on an extremely misleading discussion of the ARMIS data. In particular, Dr. Selwyn asserts that AT&T Illinois’ “gross plant-in-service increased by only $1.04 billion.” (AG Ex. 1.2, p. 38). That number, however, reflects only the difference in the 2001 and 2005 end-of-year balances of Total Plant, including non-operating plant and goodwill. As shown on Table 5, the increase in the year end balance of Telecom plant-in-service (which represents investment in plant actually used to provide service) from 2001 to 2005 was approximately $1.13 billion.

More importantly, both the $1.04 and $1.13 billion figures are net of retirements and do not, therefore, reflect the full amount of AT&T Illinois’ investment in plant additions. For the five year period from 2001 through 2005, AT&T Illinois’ investment in plant additions was $3.3 billion, three times the amount suggested by Dr. Selwyn. This investment is about the same as the investment in plant additions for the preceding five year period (1996-2000) ($3.7 billion). I would also note that investment in total plant additions during the period from 2000 through 2004 was $3.8 billion, which exceeded by 26% AT&T Illinois’ obligation under merger condition 7 of the Commission’s SBC/Ameritech merger approval order, which required AT&T Illinois to spend $3 billion on infrastructure improvements during the time period.

Q. Dr. Selwyn also asserts that "the number of IBT full-time equivalent employees dropped by 4,581, from 15,768 at the end of 2001 to only 11,187 as of December 31, 2005, a 27% decrease." (AG Ex. 1.2, p. 38). Do you have any comments in response to this assertion?

A. Yes. Once again, Dr. Selwyn's assertion is not relevant to any issue in this case and is based on a misleading use of statistics. The numbers used by Dr. Selwyn represent the number of employees on AT&T Illinois' payroll. There are, however, numerous employees who support AT&T Illinois' operations who are formally employees of AT&T Illinois' service company affiliate and other affiliates. As shown in Table 5, while the total number of Illinois employees (including those employed by affiliates of AT&T Illinois) decreased between 2001 through 2005, the percentage reduction was approximately 19%, not 29%.

Q. Dr. Selwyn asserts that the drop in employment is "not consistent with a company that is being seriously challenged by competition." (AG Ex. 1.2, p. 39). Do you agree?

A. No. To the contrary, the drop in the number of employees is a direct result of the loss of business to competition and the competitive pressures to control expenses.

Q. Have the employment levels and the investment in plant additions over the past five years been sufficient to enable AT&T Illinois to provide quality service?

A. Yes. Since 2001 AT&T Illinois has not missed a single annual Part 730 or annual Alternative Regulation service quality measure. In my opinion, these outstanding service results are driven by a number of factors, each of which refute Selwyn's incorrect assumptions. First, the highly competitive marketplace in Illinois generally, and the Chicago LATA in particular, creates a strong incentive to ensure AT&T Illinois maintains a high level of service quality in Illinois. In addition, AT&T Illinois has invested over $3.3 billion to upgrade its local network to maintain and improve network reliability. Moreover, AT&T Illinois maintained employment levels to ensure excellent customer service and believes it has the best-trained and best-equipped workforce in the State, the vast majority of whom are union members. All of these factors are completely consistent with a rational business response to very real and ever increasing competition.

Q. Does Dr. Selwyn's reference to the increase in the depreciation reserve support his claim of "disinvestment?"

A. No. The $3.3 billion investment in plant additions is the relevant measure of AT&T Illinois investment in plant improvements over the period 2001 through 2005. In this regard, all capital-intensive companies incur substantial depreciation expense. Their investments in capital assets are recovered over long periods of time. Depreciation expense does not necessarily mean that plant is being physically replaced. Moreover, even where assets are actually retired, they are not necessarily worn out. Depreciation reflects not only the wear and tear associated with use and age, but, more importantly, technological obsolescence. Thus, to the extent that AT&T Illinois is replacing older technologies with state-of-the-art equipment, this is precisely what can be expected of a company operating in a highly competitive market.

Dr. Selwyn raised similar arguments in Dockets No. 92-0448/93-0239. In that docket, he claimed that Ameritech Illinois was "disinvesting" in its network, because projected depreciation expense over the five years of the Plan would exceed the $3 billion commitment. Dr. Selwyn made a similar argument in Docket Nos. 98-0252/98-0335/00-0764. The Commission ignored Dr. Selwyn's arguments in both of those proceedings and those arguments should be ignored again.

F. DSL COMMITMENTS

Q. Dr. Selwyn asserts that the provisions of the Stipulation and Joint Proposal related to expansion of DSL do not represent "very much of a commitment" at all "on the part of AT&T." (AG Ex. 1.2, p. 41). Do you agree with Dr. Selwyn's assertion?

A. No, AT&T's DSL commitments are significant. If the Joint Proposal is approved, AT&T Illinois has committed to expanding the number of wire centers with DSL from 91% of the wire centers operated by AT&T Illinois in the Chicago LATA to 99% of such wire centers within one year after the Effective Date. In addition, AT&T Illinois has committed to investing in and upgrading to loop plant in order to expand the availability of DSL from 86% of the total living units in the Company's service territory within the Chicago LATA to 90% of such living units, again, within one year after the Effective Date.[8]

[8] The Effective Date is defined in the Joint Proposal as 35 Days after the date of a final Commission order approving AT&T Illinois' competitive classification pending in this docket and the Joint Proposal or, in the event that an application(s) for rehearing is (are) filed with respect to such an order, ten days after the Commission's denial of such application for rehearing. Since a final order must be entered in this case by August 30, 2006, the one year period for AT&T Illinois to fulfill its DSL commitments will begin in the fourth quarter of 2006.

Q. Dr. Selwyn asserts that the cost of meeting the DSL commitments is "minimal." (AG Ex. 1.2, p. 42). Do you have any comments in response to this assertion?

A. Yes. Dr. Selwyn's assertion misses the point. What is relevant is not the cost to the Company of meeting its commitment. Rather, what is important is the benefit to consumers associated with the expansion of the availability of DSL. In any event, Dr. Selwyn's assertion is wrong. In support of his assertion, Dr. Selwyn cites a response to a data request in which AT&T Illinois stated that, if the Joint Proposal is approved "investment for DSL in Illinois will increase, ***BEGIN CONFIDENTIAL AND PROPRIETARY**END CONFIDENTIAL AND PROPRIETARY***." As stated, this figure is the *minimum* investment. It represents the cost of adding DSLAMs in additional wire centers. It does not include the cost of increasing the percentage of living units in the Chicago LATA with access to DSL from the current 86% to 90%. Contrary to Dr. Selwyn's assertion, such an increase is not "marginal." In fact, there was virtually no increase in that percentage during the year 2005. To meet the 90% commitment, AT&T Illinois must deploy fiber-fed remote terminals to reach customers that live beyond 18,000-route feet from the central office. The estimated investment in plant additions and upgrades in the Chicago LATA needed to meet the 90% commitment is approximately ***BEGIN CONFIDENTIAL AND PROPRIETARY******************END CONFIDENTIAL AND PROPRIETARY***. Thus, the total cost necessary to meet both the 99% wire center and the 90% living unit commitments in the Chicago LATA is estimated to be at a minimum, approximately ***BEGIN CONFIDENTIAL AND

PROPRIETARY***************END CONFIDENTIAL AND PROPRIETARY*****.

Q. Dr. Selwyn suggests that AT&T Illinois has plans to expand the number of wire centers with DSL to 99% and to increase the percentage of living units to which DSL is available to 90% even if the Joint Proposal is not approved. Is Dr. Selwyn correct?

A. No. Dr. Selwyn's suggestion is based purely on speculation. In fact, AT&T Illinois currently does not have plans to make the investment that would be necessary to meet the stipulated DSL thresholds if the Joint Proposal is not approved. In support of his speculation, Dr. Selwyn assumes that AT&T Illinois has a "strong economic incentive to expand the availability of DSL and, as such, is not really 'committing' to do anything that it would not do otherwise." Dr. Selwyn's assumption is wrong. As previously discussed, the estimated cost of meeting the stipulated thresholds for wire centers and living units is substantial. AT&T Illinois has a greater incentive to focus on growing its broadband business in areas where DSL is already deployed than it does to incur the substantial cost of expanding into new areas. Dr. Selwyn's assumption that AT&T Illinois is "not really 'committing' to do something that it would not be doing anyway" is also not supported by recent experience. The current percentages of wire centers with DSL (91%) and total living units with DSL availability (86%) have not changed since December 2004. The network investment made by AT&T Illinois to expand the availability of DSL in the years 2004 and 2005 combined was *****BEGIN CONFIDENTIAL AND PROPRIETARY*****************END CONFIDENTIAL AND**

PROPRIETARY***, 25% less than the estimated cost of expanding availability from the current 86% of total living units to 90%.

Q. Dr. Selwyn questions the benefit of the DSL commitments, asserting that AT&T's merger requirement to offer DSL on a stand-alone basis expires two years after that commitment takes effect. (AG Ex. 1.2, p. 43). Do you have any comments in response to Dr. Selwyn's testimony in this regard?

A. Yes. The merger condition speaks for itself and states:

> Within twelve months of the Merger Closing Date, SBC/AT&T will deploy and offer within its in-region territory ADSL service to ADSL-capable customers without requiring such customers to also purchase circuit switched voice grade telephone service. SBC/AT&T will continue to offer this service in each state for two years after the "implementation date" in that state. For purposes of this condition, the "implementation date" for a state shall be the date on which SBC/AT&T can offer this service to eighty percent of the ADSL-capable premises in SBC's in-region territory in that state. Within twenty days after meeting the implementation date in a state, SBC/AT&T will file a letter with the Commission certifying to that effect. In any event, this commitment will terminate no later than three years from the Merger Closing Date.

As is clear from its text, the condition remains in effect two years after the date on which AT&T can offer naked DSL service to 80% of the ADSL-capable premises in its in-region territory in a state. After AT&T has incurred the expense of adjusting its systems and procedures to meet the 80% test, it will be able to determine more accurately the demand for this service and the profitability of continuing to offer it. Dr. Selwyn's speculation regarding the benefits of this commitment made to and accepted by the FCC will be answered in the competitive marketplace, and there is no reason for anyone to speculate that this merger condition will not have either the short term benefit of bringing a new service to the marketplace or positive long-term effects in a marketplace in which there are alternatives to circuit-switched voice. In any event, this provision of the Stipulation and Joint Proposal does not require this Commission's approval, nor is it necessary for this Commission to second-guess the FCC's approval of this merger condition, as Dr. Selwyn appears to suggest.

G. OTHER ISSUES

Q. Dr. Selwyn asserts that "most customers" who purchase multiple customer calling features "may make little or no use of features" other than Call Waiting and Caller ID." (AG Ex. 1.2, p. 31). Does Dr. Selwyn provide any support for that assertion?

A. No. Dr. Selwyn simply assumes that most customers purchase plans with features that do not want, but does not provide any evidence to support that assumption. Dr. Selwyn further asserts that only ***BEGIN CONFIDENTIAL AND PROPRIETARY*** ************************END CONFIDENTIAL AND PROPRIETARY*** of local measured customers purchase features other than Call Waiting and Caller ID. (AG Ex. 1.2, pp. 31, 35). The alleged source for this assertion is the response to a data request in which AT&T Illinois was asked to identify the number of local measured service customers who purchase one feature and that one feature is something other than Call Waiting or Caller ID. This figure does not include features purchased by stand-alone customers who purchase two or more features. As discussed in Mr. Panfil's Rebuttal Testimony, 20% of AT&T Illinois' stand-alone customers subscribe to two features and 18% subscribe to three or more features. Even if one were to erroneously assume that every customer who subscribes to only two features subscribes to both Call Waiting and

Caller ID, there are at least approximately 150,000 (830,236 x 18%) stand-alone customers in the Chicago LATA who purchase features in addition to Call Waiting and Caller ID.

Q. Dr. Selwyn asserts that AT&T Illinois "does not offer a stand-alone unlimited long distance calling service." (AG Ex. 1.2, p. 31). Is Dr. Selwyn correct?

A. No. In support of his assertion, Dr. Selwyn refers to a response to a data request in which AT&T Illinois discussed the $15 National Connections Select price for long distance services offered by its affiliate, AT&T LD, which is available to customers who subscribe online and purchase local access line, Caller ID and two other features. However, AT&T offers an unlimited long distance calling plan for $30 per month which is available to any customer.

Q. Dr. Selwyn is critical of Ms. McKibbin's testimony regarding the potential savings to customers who may choose to switch from certain packages to one of the "safe harbor" packages. (AG Ex. 1.2, p. 33). Specifically, Dr. Selwyn asserts that the "*correct* regulatory solution would be for IBT to simply rerate its Economy Local Solution, Economy Solution and U-Select-3 customers to the appropriate 'safe harbor' service now, and provide those customers with the result that would arise under competitive market conditions." (*Id.*). Does Dr. Selwyn's assertion make sense?

A. No. Contrary to Dr. Selwyn's suggestion, AT&T Illinois has not "conceded" that all customers in the referenced packages would save money by switching to one of the "safe harbor" packages. Moreover, the packages referred to by Dr. Selwyn are not identical to any of the "safe harbor" packages. Again, the "safe harbor" packages are primarily intended to provide a "safe harbor" from potential increases in stand-alone network access and usage rates to stand-alone customers who make few calls or desire two or fewer features. The U-Select-3 package, for example, provides for three features. The customers to whom these packages are attractive have numerous competitive alternatives to choose from and these alternatives constrain AT&T Illinois' ability to increase rates for those packages. Although certain customers on those packages may conclude that it is beneficial to switch to one of the safe harbor packages, there is no basis for automatically changing the price and terms of the services currently being provided to those customers.

V. CONCLUSION

Q. Does this conclude your testimony?

A. Yes.