BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the	)	
	)	Docket No. UT-003013
Continued Costing and Pricing of	)	*PART B*
Unbundled Network Elements, Transport,	)	
Termination, and Resale.	)	
	)	

BRIEF OF COMMISSION STAFF

CHRISTINE O. GREGOIRE
Attorney General
MARY M. TENNYSON
Senior Assistant Attorney General
GREGORY J. TRAUTMAN
Assistant Attorney General
1400 S Evergreen Park Drive SW
P.O. Box 40128
Olympia, WA 98504-0128

May 29, 2001

TABLE OF CONTENTS

I. INTRODUCTION

In November 1996, the Washington Utilities and Transportation Commission (Commission) issued an Order Instituting Investigation, creating the Generic Costing and Pricing Proceeding under Docket Nos. UT-960369, UT-960370, and UT-960371. The proceeding was instituted to fulfill the Commission's obligations under the Telecommunications Act of 1996 (1996 Act) and under Title 80 RCW to establish rates and charges for telecommunications services.

This is the second part of the Commission's proceedings in Docket No. UT-003013 to develop the costs and prices that Qwest Corporation (Qwest), f/k/a U S WEST Communications, Inc., and Verizon Northwest, Inc. (Verizon), f/k/a GTE Northwest Incorporated, Incumbent Local Exchange Carriers (ILECs), charge for various unbundled network elements, continuing the process started by the Commission in Docket No. UT-960369, et al. The prices established through that proceeding, and this proceeding, are intended to replace interim prices set in arbitration proceedings and in ILEC tariffs and/or Qwest SGAT for interconnection rates and charges. The issues to be addressed in this phase (designated as Part B) of the proceedings, and the procedural schedules, were originally set out in the Commission's First Supplemental Order—Prehearing Conference Order, issued on March 16, 2000. As revised by later orders in this docket,[1] the issues addressed in this Phase B include UNE-P (Unbundled Network Element Platform), subloop unbundling, recurring UNE rates, high capacity loops, loop conditioning, inside wiring, dark fiber, shared transport, enhanced extended loops, reciprocal compensation,

[1]Each of the following orders in this case made modifications to the issues to be addressed and the scheduling of the proceedings, in response to input from the parties: Third Supplemental Order, Docket No. UT-003013; Notice Extending Part B Schedule, served July 17, 2000; Fourth Supplemental Order, Supplemental Prehearing Conference Order, issued July 25,

line sharing on fiber loops/DLC systems, rates for converting existing retail services into UNEs, nonrecurring rates related to any UNE, OSS issues, and UNE-P/line splitting.

II. LEGAL AND POLICY ISSUES

A. LEGAL

The objective of the 1996 Act was to "provide for a pro-competitive, de-regulatory national policy framework designed to accelerate rapidly private sector deployment of advanced telecommunications and information technologies and services to all Americans by opening all telecommunications markets to competition. . . ." H.R. Conf. Rep. No. 104-458, 104th Cong., 2d Sess. 13 (1996). A fundamental requirement of the 1996 Act imposes on the ILECs the obligation to provide their competitors with access to unbundled network elements. (Thirteenth Supplemental Order, Docket No. UT-003013, ¶ 86.) This phase of the proceedings arises out of the FCC's UNE Remand Order, Third Report and Order, *In the Matter of Implementation of the Local Competition Provisions of the Telecommunications Act of 1996,* CC Docket No. 96-98. FCC 99-238 (1999). As noted by the FCC in its press release announcing the release of that order:

> This FCC decision removes a major uncertainty surrounding the unbundling obligations of the Telecommunications Act of 1996 and is expected to accelerate the development of competitive choices in local services for consumers. Unbundling allows competitors to lease portions of the incumbent's network to provide telecommunications services.
>
> Today's order adopts a standard for determining whether incumbents must unbundle a network element. Applying the revised standard, the Commission reaffirmed that incumbents must provide unbundled access to six of the original seven network elements that it required to be unbundled in the original order in 1996:

2000; Fifth Supplemental Order, issued August 3, 2000; Seventh Supplemental Order, issued September 12, 2000.

(1) loops, including loops used to provide high-capacity and advanced telecommunications services;
(2) network interface devices;
(3) local circuit switching (except for larger customers in major urban markets);
(4) dedicated and shared transport;
(5) signaling and call-related databases; and,
(6) operations support systems.

FCC Report No. CC 99-41, September 15, 1999. This Commission initiated this proceeding to establish rates for those UNEs that were not yet priced, to fulfill its obligations under the 1996 Act and its authority under Title 80 RCW and Title 480 WAC. In the earlier Generic Proceeding, Docket No. UT-960369, et al., the Commission adopted the TELRIC costing methodology for setting UNE prices. The Commission noted that the FCC's Interconnection Order and rules (*In the Matter of the Implementation of the Local Competition Rules of the Telecommunications Act of 1996,* CC Docket 96-98, First Report and Order (1996), Appendix B – Final Rules) (Interconnection Order) provide guidance, but that its recommendations are "largely unbinding." Eighth Supplemental Order, Docket No. UT-960369, et al., ¶ 9. The Commission also noted that all of the parties in the case advocated the use of the TELRIC methodology as the appropriate costing analysis, and thus adopted use of TELRIC for these proceedings. *Id*. The Commission stated that the TELRIC methodology: (1) assumes the use of best available technology within the limits of existing network facilities; (2) makes realistic assumptions about capacity utilization rates, spare capacity, field conditions, and fill factors; (3) employs a forward-looking, risk-adjusted cost of capital; (4) uses economic depreciation rates for capital recovery; and (5) properly attributes indirect expenses to network elements on a cost-causative basis. *Id.* at ¶ 10.

B. POLICY

1. Setting Prices For OSS

As this Commission stated in its Thirteenth Supplemental Order in Docket No. UT-003013:

> In the 1996 Act, Congress left it to the FCC to enact the rules that would specify which network elements would be available to CLECs. In defining the network elements that ILECs must offer, the FCC specifically included '[o]perations support systems functions consist[ing] of pre-ordering, ordering, provisioning, maintenance and repair, and billing functions supported by an incumbent LEC's databases and information.' (Citing to 47 C.F.R. § 51.319(f)(1).) Operations Support Systems are used by telephone companies – both CLECs and ILECs – to provision plant, to process service orders, to manage service connections, disconnections, moves and changes, and to track network maintenance. OSS consists of computer hardware, and software, such as databases.

Thirteenth Supplemental Order, at ¶ 87. In the Seventeenth Supplemental Order in Docket No. UT-960369, et al., this Commission required the CLECs to bear the costs of OSS modifications.

2. Non-Recurring Costs Play A Significant Role In Determining Whether An Entrant Can Afford To Enter The Local Market

Nonrecurring charges are the one-time charges that are associated with items such as provisioning and installation. (TR 1822: 6-12). The Commission's determinations on the appropriate cost levels will play an important role in determining the prices a new entrant will have to pay up front to enter the local market in direct competition with an ILEC. Therefore, the Commission must balance the interests of all the parties in this proceeding to insure that the appropriate expenses incurred by ILECs are recovered through reasonable, cost-based rates and that new entrants will pay their fair share to enter the market. The Commission-established prices for various UNEs should not be barriers to entry. Therefore, Staff recommends that Qwest's and Verizon's cost studies and prices for non-recurring costs be modified as set forth (in sections III. A. 1 and III. B. 1) below.

III. UNE COSTS/PRICES

A. QWEST

1. Non-Recurring Costs/Study Methodology

In her response testimony filed on October 23, 2000, Staff witness Jing Y. Roth testified as follows:

> Qwest's proposed non-recurring costs are expense-based. The direct costs are a function of the time required to perform tasks multiplied by appropriate labor rates. Qwest also applies the Commission-approved percentages for attributed and common costs to arrive at the non-recurring charges. Staff has concerns about the estimated time for order entry and 'probability of occurrence' proposed by Qwest to complete each task necessary for processing an order.

Ex. T-1360, page 14.

The cost studies that Qwest filed in this case are based on Qwest's actual experience or company practice (TR 1821; Ex. T-1001, page 5; *See also* Ex. 101, pages 7-8), although they purport to yield forward-looking replacement costs. The time estimates for various activities are based on the estimates of subject-matter experts (SMEs). However, as brought out in the cross-examination of Ms. Million by Ms. Steele (*See* TR 1834-1836), the information provided to the SME's to produce those estimates, and the detail of the activities performed, are not in the record. The Commission requested that, in briefs, the parties address the issue of how it can validate the reasonableness of the opinions of the SMEs (Commission Issue No. 1). It is Staff's view that, without time and motion studies or the opportunity to observe the activities that are performed, it is difficult, if not impossible, to obtain such validation.

Staff recommends that the Commission apply the Customer Transfer Charge (CTC) adopted in Phase II of Docket No. UT-960369, et al., (Seventeenth Supplemental Order, at

¶ 465) to the proposed UNE-combination (UNE-C)[2] costs, because there should be minimal difference between processing an order for UNE-P (existing POTS) and for a customer transferring from one carrier to another. In this phase of the proceeding, through some of its time estimates and probability analysis, Qwest inflated the underlying costs for processing an order for UNE-C. Staff recommends that the Commission adopt the costs for CTC for processing UNE-C orders. A comparison of the proposed costs by Qwest with Staff's recommended costs for UNE-C is shown in Ex. C-1363. Staff recommended the Commission make those specific changes to time estimates and probability.

After reviewing Ms. Roth's October 23, 2000, testimony, Qwest filed revised cost studies with the responsive testimony of Theresa Million. In its revised cost study, admitted as Ex. C-1010, Qwest used the six minutes for processing orders at the interconnection service center that the Commission ordered[3] Qwest to use for order processing time at the ISC. TR 1826: 16-24. Qwest adopted Staff's recommended times and probability adjustments for these elements (UNE-P New and existing). On cross-examination by Ms. Anderl at the hearing, the recommendations adopted by Qwest, and the specific nature of Staff's recommendations, were clarified. TR 3900-3904: 16. Staff recommends that Qwest reduce the order processing time at the interconnection center, and the probability of mechanized and non-mechanized order handling to the amounts contained on page 15, lines 19-20, to page 16, lines 1-2, of Ex. CT-1360.

These modifications apply to the following ordering activities:

1. UNE-C new POTS first line (mechanized) for connect and disconnection.

---

[2]Qwest uses the term UNE-C for the same service that is generally referred to in this proceeding as UNE-P, or UNE-Platform.

[3]See ¶ 474 of the Eighth Supplemental Order in Docket No. UT-960369, et.al.

2. UNE-C new POTS EA additional line - mechanized (probability change only).

3. UNE-C new POTS First line and manual (time estimate adjustment only)

For other ordering and processing activities, Staff recommends that the Commission require Qwest to apply the times and probabilities listed in Ex. C-1363 to reduce the times for typing and screening an order at the interconnection service center, to process a disconnect order, for "input order processor" and internal phone calls, to modify the percentage of flow-through at interconnection service center for mechanized orders, and change the probability for "non-electronic interface."

Because the non-recurring cost studies presented by Qwest have incorporated various unbundled network elements, specific time estimates and probability adjustments should be implemented throughout the studies wherever applicable. In particular, Staff makes the following recommendations, with the specific recommended adjustments shown in Ex. C-1363:

1. Reduce the time for typing and screening an order at the interconnection service center.

2. Modify the percentage of flow-through at the interconnection service center for mechanized orders.

3. Decrease the time to process a disconnect order.

4. Reduce the time for "input order processor."

5. Modify the time for internal phone calls.

6. Change the probability for "non-electronic interface."

Staff has not calculated the total effect of these recommended modifications specifically for each category of UNE as they are proposed by Qwest. However, Staff provided in its testimony and exhibits the detailed adjustments that need to be made throughout the entire cost

studies and pricing proposals wherever applicable. It is important to note that all of the modifications proposed by Staff, if adopted, will reduce the proposed non-recurring and recurring rates.

2. Recurring Costs

a. Recurring cost issues

1) Total Investment Factor (TIF)

In its supplemental response testimony, Staff indicated concerns with the calculation of the TIF because the response to a Staff data request showed that Qwest was using hours to calculating the TIF factor rather than expense. Ex. T-1352, pages 5-6. In rebuttal testimony, Qwest witness Ms. Million stated that the response to the Staff data request using hours was actually a labeling error, and she provided an update to the data request correcting the response. Ex. T-1009, pages 10-11; Ex. C-1015.

As a general matter, however, the level of the TIFs appears inflated. As discussed by Mr. Spinks on cross-examination, Staff has continuing concerns with the loading factors in the range of 1.7 to 2.1, because historically, such loadings have been in the range of 1.3 to 1.5. TR 3886.

In addition, Staff has two other concerns with the TIFs. First, the expense and investment amounts used to develop the TIFs is based on experience from 1997. Ex. C-1027. Forward-looking costs should be based on reasonably current data, and Staff believes the 1997 data is borderline, at best, as representing forward-looking costs. Second, as discussed in Ex. 1028, the 1997 expense data are stated to be based on 1997 General Ledger entries. Qwest provided no documentation or workpapers showing how the General Ledger amounts were used to arrive at state specific expenses for calculating the TIFs. Hence, Staff is not able to affirm the accuracy or validity of the proposed TIFs.

Staff notes that intervenor witness Mr. Weiss also recognizes that Qwest's proposed TIFs do not comport well with his experience and has recommended TIF levels ranging from 1.2 to 1.4, for instance, in recalculating the DS-1 cost of optical/digital hard wired and plug-in plant investments. Ex. T/CT-1330, pages 9-11, 17. Staff believes that given the age of the data and lack of documentation, the intervenor-proposed TIFs are more reasonable than Qwest's and should be adopted by the Commission.

2) Deaveraged DS-1 rates

Since the underlying loop facility used to provide DS-1 service is deaveraged, Staff recommended that rates for DS-1 service also be deaveraged. Qwest has now agreed to deaverage these rates. Ex. T-1009, page 11.[4]

d. High capacity loops

Qwest estimated DS-1 costs by weighting costs for eight different possible architectures using SONET Fiber Mux, which are assumed to have varying fill levels. Intervenors have objected to the studies, citing for instance the low fill factor for common equipment of 37 percent. Ex. T-1009, page 26. Staff believes one point that parties may be overlooking is that TELRIC requires the use of both forward-looking technology as well as the most cost efficient technology. Hence, while SONET may be the most forward-looking technology for DS-1 provisioning, it may not be the most cost efficient technology to deploy at this time. The Commission needs to compare the cost of provisioning DS-1 circuits using 4-wire copper distribution loops with the cost of provisioning DS-1 using SONET technology. Copper loops are also a forward-looking technology and copper loops may well be the most cost efficient way of provisioning DS-1 circuits given rivaling opinions as to the appropriate fill and TIF factors

[4]Verizon has also proposed deaveraged rates for DS-1 service.

used in the cost studies. Staff is troubled by Qwest's approach to estimating DS-1 costs and believes the intervenors have produced credible alternative cost studies that should be considered by the Commission.

e. Subloops

Staff has concerns with the proposed subloop estimates. The estimates of feeder-distribution cost show little or no variation between density zones; Qwest estimates that approximately 30 percent of investment is in feeder facilities and 70 percent is in distribution facilities for all five density zones. On a conceptual level, one would expect that the ratio of feeder and distribution would be closer together in dense urban areas, and that the amount of distribution investment would increase relative to feeder investment in less dense rural areas. Ex. T-1350, pages 8-9. Mr. Spinks elaborated:

> The dense packed urban wire centers because of their smaller geographic area and much higher population density cause you to have more, bigger, expensive feeder cables and shorter distribution loops than you do in the rural areas where there are hundreds of square miles in size and relatively fewer, smaller feeder cables and longer, [m]ore expensive distribution loops.

TR 3880.

Table 1 of Mr. Spinks' testimony comports with this analysis. Staff's estimates, developed using the HM3.1 cost model and following the Commission's prior decisions regarding inputs and other adjustments, show that the ratio of feeder to distribution is approximately 40-60 percent in dense urban areas (zone 1), with the percentage of distribution steadily increasing to a 28-72 percent split in the least dense area (zone 5). *Id.* at 10. Accordingly, Staff recommends that the Commission adopt the feeder/distribution ratio estimates set forth in Table 1 for Qwest.

h. Unbundled dark fiber

Staff noted that Qwest originally proposed using a 14-state average sheath mile weighting for direct buried and underground investment to calculate the cost of interoffice dark fiber. Ex. C-1004 ("July 99 Sheath Miles-Tax 7A report", page 1 of 1). On page 85, paragraph 258 of the Thirteenth Supplemental Order in Part A of this Docket, the Commission expressed a preference for using Washington-specific data.

Staff recommended that Qwest use Washington-specific data for calculating Washington-specific costs in this Docket. TR 3885; Ex. T-1350, page 4. Since Washington has a lower proportion of the higher-cost direct buried dark fiber than the region-wide average, the use of non-Washington data would result in higher cost estimates than the costs Qwest actually incurs in Washington. *Id.* at 4-5. On cross-examination, Ms. Million indicated that Qwest would use Washington-specific data for dark fiber, satisfying Staff's concerns in this area. TR 1961-62. *See* Ex. C-1040 (Qwest's Response to Staff Data Request No. 6).

B. VERIZON

1. Non-Recurring Costs/Rates

On August 4, 2000, Verizon filed recurring and non-recurring cost studies in support of its proposed recurring rates and non-recurring charges for the UNEs that result from the Federal Communication Commission's (FCCs) UNE Remand Order.[5] Specifically, Verizon sponsors the GTE Integrated Cost Model Version 4.1b (ICM) to estimate costs in support of Verizon's proposed recurring rates.

[5] *In the Matter of the Implementation of the Local Competition Provisions of the Telecommunications Act of 1996,* Third Report and Order, 15 FCC Rcd 3696 (Nov. 5, 1999).

a. Study methodology

As a general principal for UNE's, cost studies should be forward-looking analyses of efficient technology and processes, and must adhere to cost causation principles. Verizon's formula to determine the non-recurring costs is as follows:

Activity Time ***x*** *Probability* ***x*** *Labor Rate = Cost*

1) Service ordering and
2) Provisioning costs

After reviewing Verizon's voluminous cost studies, Staff determined that the proposed non-recurring costs are unreasonably high. Staff concentrated its analysis on the "activity time" proposed by Verizon. Verizon presented in its cost study an "order entry time study" of the time it took its personnel to perform various activities. However, it does not use those times directly in performing the non-recurring cost calculations. A clear exposition of how Verizon has inflated its NRCs is contained in Ex. C-1317, sponsored by John Klick. Staff concurs in this analysis. Verizon's times used in the NRC calculations are inflated and illogical. It is important to note that, in making the adjustments recommended in Ex. C-1362, Staff used Verizon's own time estimates in its non-recurring cost study.

Staff recommends that the Commission modify Verizon's non-recurring cost studies and pricing proposal as follows:

--Reduce processing times for "Production Order Entry" (Connection and Disconnection).

--Decrease time estimates for "Error Correction" and "Jeopardies" to zero.

--Modify the time estimate for "Meet Point."

--Downward adjustments be made to the time estimates for processing orders.

Staff's proposed specific adjustments are listed in Ex. C-1362.

3) Fixed/Shared – NOMC

In the Thirteenth Supplemental Order in Docket No. UT-003013, at ¶ 180, the Commission approved Verizon's proposed charge of $4.92 per LSR for recovery of the National Open Market Center (NOMC) shared costs, without any analysis. Verizon's ICM cost model presented in this part of the proceeding has created a need for this Commission to re-evaluate the NOMC shared costs and common cost factor previously adopted. Verizon applies the $4.92 charge to each order as part of its proposed non-recurring charges. The $4.92 charge was derived by dividing the total NOMC shared/fixed costs by the forecasted annual average wholesale orders. Based on a close examination of the costs as characterized by Verizon as fixed costs, Staff found that:

1. There is no valid basis for the total amount of the costs.

2. The costs are not Washington-specific.

3. The total annual charge factor utilized in the analysis is a composite of capital factor, income tax factor, and property tax factor. Verizon provides no documentation to support the validity of these factors.

4. The so-called "shared/fixed expenses" have been recovered through the shared cost allocation or the common cost allocator established by Verizon in its ICM.

No matter how Verizon characterizes these NOMC costs, these cost categories reflect support and administrative costs such as rent expense, furniture, human resources, and PC expenses. Because these costs are not product-specific, the Company normally proposes to recover these general costs through its calculation of shared and common costs generated on a total Company basis, then allocates these costs through a factor to different products and services. Verizon has done so in its ICM. Verizon has centralized the total shared and common costs incurred on a total Company basis. Appendixes and tables as presented in Verizon's ICM Expense Module documentation, include land and building, human resources, and other

administrative expenses. Verizon has not made a convincing argument that the NOMC "Share/Fixed" costs are separate expenses from those general expenses incurred and incorporated in its ICM, which are recovered through shared cost allocation on a total Company basis.

Because these costs have already been incorporated in Verizon's ICM, Staff recommends that the Commission eliminate the amount of $4.92 for NOMC fixed cost recovery which was approved in the Thirteenth Supplemental Order.

b, c, d, e. Verizon's non-recurring costs for dark fiber, sub-loop unbundling, EELs, and UNE-P are unreasonably high and should be reduced

The adjustments recommended by Staff in its testimony and exhibitis[6] should be made throughout Verizon's non-recurring cost studies whenever applicable. The overall effect of these adjustments would be a reduction to Verizon's non-recurring costs for various activities, which will in turn reduce non-recurring charges.

Staff bases its adjustments contained in Ex. C-1362 on Verizon's own time estimates. In her response testimony, Ex. C-1360, page 5, lines 15-21, and page 6, lines 1-3, Staff witness Jing Y. Roth provides an illustration to explain how Staff's adjustments were developed. These adjustments should be made throughout Verizon's non-recurring cost studies wherever applicable.

An Enhanced Extended Loop (EEL) is a combination of an unbundled loop, interoffice dedicated transport, and multiplexing, if required. A basic UNE-P would be comprised of a two wire UNE-Loop and a basic analog line side port. Under Verizon's proposal, a CLEC would pay a non-recurring charge for ordering an initial basic UNE-P, and an additional charge for each

additional unit; in addition, a CLEC would also pay monthly recurring charges. The amount of Verizon's proposed charge is shown in Ex. C-1360, page 4, line 21. A simple comparison of Verizon's non-recurring charges for UNE-P with the current Verizon tariffed rate for residential and business customers to order basic exchange phone lines is illuminating. The tariff shows $48.50 for ordering an initial business line and $26.25 for a residential line. It is important to note that this type of UNE order is highly mechanized while retail service orders require interface with untrained customers; therefore, the more mechanized order should cost less to process.

At the minimum, as an alternative, Staff recommends that six minutes for order entry be incorporated in Verizon's cost studies. This time estimate of six minutes for processing an LSR has been adopted by the Commission for GTE in the 17th Supplemental Order in Docket Nos. UT-960369, et al.

Furthermore, Staff recommends other adjustments to time estimates proposed by Verizon for various activities such as "Error Correction," "Jeopardies," and "Meetpoint." (Ex. C-1160.) Staff's comparison of the total non-recurring cost of processing a basic EEL order, as adjusted by Staff, and Verizon's proposal, is summarized in Ex. CT-1360, page 6, lines 10-12.

1) Verizon cost study for EELs, migration as is (migration from special access to UNE-P) is flawed

Verizon filed another category of ordering cost for EELs called "Migration As Is." According to Verizon witness Mr. Richter, this type of order is used when an Interexchange Carrier has an existing Special Access Arrangement and wants the billing be handled on a UNE basis. Ex. T-1163, page 17. The proposed costs and prices for processing this type of order are higher than the ones proposed for EELs in the earlier filing. In this new filing on January 8,

[6] *See* Ex. C-1360, pages 3-6; C-1362.

2001, the ordering cost for a basic "Migration As Is" exceeds the price in its August 4, 2000, cost studies for ordering a basic new EEL by $17.35, and exceeds the price for a change order by over $30.00. To understand why the "Migration As Is" ordering cost is higher, Staff reviewed the previously filed costs and examined the new costs. Staff found that Verizon has added two more categories of costs to this type of order: Mass Order Generator (MOG) Template and Termination Liability Calculation. This new ordering cost is calculated by adding these two categories of costs to the ordering costs proposed in the previously submitted cost study that included the costs for EELs ordering.

Staff believes that there are two flaws in this calculation of the ordering costs. First is the use of the previously filed ordering cost. Staff has pointed out that the previous ordering cost is inflated, and Staff, therefore, recommended certain modifications and downward adjustments to the underlying costs. Second, Verizon has chosen to use the ordering cost for a new basic order, instead of the lower change order cost. The same problem exists for "Advanced DS0" and "DS1 or Higher" ordering. A "Migration As Is" order should be no different from a change order. The other problem with this new ordering cost is that Verizon has included the category of cost for "MOG" twice. There is no explanation given by Verizon witness Mr. Richter as to why MOG is included twice in this calculation. Staff recommends the Commission require Verizon to incorporate the modifications recommended by Staff in Ms. Roth's testimony previously filed on October 23, 2000, and to treat this type of order as a change order and include the MOG entry cost only once. Verizon, on the record, has committed to file a revised costs study on this issue (Ex. 1167, page 10, lines 4-7); however, no filing date for this new study has been established.

f. Verizon's proposed charges for loop conditioning are unreasonably high

After its initial testimony on this topic,[7] Verizon revised its proposed costs of loop conditioning submitted by Verizon witness Larry Richter. Ex.1162 and C-1162. As noted in Ex. CT 1360, pages 6-7, Staff's major concern lies with Verizon's time estimates for construction and engineering required for loop conditioning. Compared to the rates the Commission set for Qwest in the Eighth Supplemental Order in Docket No. UT-960369, et al., Verizon's proposed charges are unreasonably high. In this new submission, Verizon has made no change to reflect Staff's concerns. Verizon's revisions did change the proposed costs and charges compared to its original filings. However, as the table in Ms. Roth's confidential rebuttal testimony[8] shows, both the original and the new costs and charges are still much higher than the Commission-approved Qwest rates. It should be noted that Qwest's charge for Load Coil Removal is the charge for unloading 25 pairs, and Qwest charges only the cable unloading charge, when cable unloading and bridge tap removal are ordered at the same time.

Verizon's mathematical equation for calculating the underlying costs for loop conditioning is as follows:

Time for Construction and Engineering ***x*** *Probability of Occurrence* ***x*** *Loaded Labor Rates*

Verizon's time estimates are several times greater than the time estimates used by Qwest for the same activities. The comparison between the costs proposed by Verizon and those the

[7]Verizon witness Larry Richter adopted the testimony and cost study performed by Linda Casey, a witness for Verizon, in Phase A of this proceeding. Ex. T-1161. However, Mr. Richter also presented a revised cost study for the non-recurring costs associated with loop conditioning and bridge tap removal (Ex. 1162, C-1162).

[8]Ex. CT-1366, page 2.

Commission has ordered Qwest to use for these same services[9] is significant because, as noted in Ms. Roth's testimony (Ex. CT-1160, page 8, lines 17-20) the times for a Verizon employee to perform these tasks should not differ significantly from the times required for a Qwest employee to perform those same tasks. Even if the times for a Verizon employee are longer (3 and 4 times) than the time for a Qwest employee to perform the same task, when the prices are being set for competitors to purchase the service, with a goal of increasing competition, the most efficient time estimate should be used.

Staff recommends that the Commission disallow Verizon's time estimate for Loop Conditioning relating to Engineering activities and Field Work as excessive, and require Verizon to recalculate its costs and charges based on the Commission-approved time estimates for Qwest. (*See* ¶¶ 150, 151, 153, of the Eighth Supplemental Order.) There is no solid basis for Verizon's high estimates of this type of costs. Verizon's support for the time estimates is that they "were obtained from interviews and discussions with construction and support personnel." (Ex. C-1160, page A4-WA 24.) Verizon's study goes through multiple layers in generating the time estimates because of the difficulties in performing such studies, and in reducing the multi-layered time estimates that Verizon presented, Staff recommends that the Commission require Verizon to recalculate its costs based on the minutes ordered by the Commission for Qwest.

The Commission required Qwest to reduce its time for field work to 120 minutes and its time for engineering activities for loop conditioning to 60 minutes. There is no reason to believe that a Verizon engineer or technician is less productive or less efficient than a Qwest engineer or technician. Even if there is a reason for this gross difference in efficiency and productivity, under the theories used to set rates based on TELRIC, the most efficient and productive time

[9] *See,* Eighth Supplemental Order Interim Order Establishing Costs for Determining

estimates should be used. Staff recommends that the Commission require Verizon to recalculate its costs and charges based on the time estimates for loop conditioning as ordered by the Commission for Qwest. It would be inappropriate to treat Verizon differently from Qwest on this issue.

Commission Issue No. 1—Validation Of Opinions Of Subject Matter Experts. The Commission has asked the parties to address the issue of how it can validate the reasonableness of opinions of SME's. This was also an issue that the Commission asked the parties in Docket No. UT-960369, et al., to address.[10] In the earlier phases of this proceeding, the Commission had the SMEs before it, and subjected them to cross-examination. *Id.* at ¶ 456. In this case, however, the SMEs were not witnesses in the case and their estimates, and even their method of providing them, were not subject to cross-examination. Staff's view is that these cannot be validated, except through comprehensive and logical time and motion studies.

2. Recurring Costs/Rates

a. ICM cost methodology

1) The Commission should not accept UNE cost estimates obtained by using the Verizon ICM 4.1(b) cost model

Verizon's UNE cost estimates for this proceeding are based on its in-house Integrated Cost Model Version 4.1(b) cost model (ICM). Staff has serious and fundamental concerns with the estimates developed by this model. Simply put, the ICM model programming is not open to inspection. This Commission has long held that it will accept only cost models that provide a "transparent, rational, stable, consistent, and understandable approach." Docket No. UT-950200,

---

Prices in Phase II, Docket No. UT-960360, et al. (April 16, 1998).

[10] Eighth Supplemental Order, at ¶ 451.

WUTC v. US West, Ninth Supplemental Order (October 19, 1995), at 2. The ICM model does not meet these requirements, particularly that of transparency.

Staff has been unable to examine the model itself for programming errors because all of the data, including numerous complex mathematical formulas, is compiled. As Mr. Collins, speaking for Verizon, admitted, "If you were to look at the compiled code, it would be nonsensical to most of the human population. It's generally not much more than ones and zeros." TR 2731-32. The ICM has produced three to four feet of documentation filling nine binders, plus a CD-ROM. Exs. 1171 and C-1171; Ex. T-1350, page 5. However, the only way that one can determine whether any programming errors were made--*i.e.*, whether the program version of the model is consistent with what the documentation says is in the model--is to do a sensitivity analysis; an extremely time-consuming process that cannot be accomplished in the timeframes set in this proceeding. TR 3868-3869. Absent such an analysis, Staff cannot conclude that the model engineers plant and determines cost in an acceptable manner. Staff, therefore, recommends that the Commission not accept UNE cost estimates obtained by using the Verizon ICM 4.1(b) cost model.

In addition to the issue of model transparency, Staff's overall conclusion that the ICM costs estimates should not be used for determining UNE cost is also supported by a number of additional specific deficiencies, as set forth below.

2) ICM loop length estimates

Staff continues to have concerns with the inaccuracies produced by the ICM's loop length estimates. Staff pointed out these discrepancies in its testimony. Ex. T-1352, page 2. Verizon responded by claiming that it has updated data from 1998 which represents "the most accurate actual loop length data available to Verizon at this time." Ex. T-1174, page 35. But,

obviously aware that even with this new data, the difference is between the actual and the ICM modeled loop lengths is in many cases quite large, Verizon is quick to discount the fact. In its Response to Record Requisition 105, Verizon goes so far as to claim that any loop length comparisons are "virtually meaningless."

The Commission obviously did not find these comparisons meaningless; in Docket No. UT-960369, et al., Ninth Supplemental Order, at ¶ 49, the Commission stated that "where the difference in lengths is substantial, the sponsor of the cost study should identify the magnitude of the difference, indicate how it affects cost, and explain the basis for the difference." Using the updated 1998 data, one can see that nearly one-third of the wire centers have loop lengths that are more than 25 percent different than the actual lengths. *See* Confidential Attachment 105A to Response to Record Requisition 105. In many instances the differences are far more substantial, with ratios varying from 0.19 to 2.16. *See* Response to Record Requisition 105.

As Staff further noted, the ICM does not have a mechanism to reconcile wire center distance sensitive investments. And because the ICM does not accurately replicate Verizon's Washington network, this results in incorrect estimates of feeder and distribution investment in Verizon's five deaveraged zones. Staff disagrees with Verizon's assertion that loop length comparisons are meaningless and "not appropriate." They are meaningful, and provide all the more reason for the Commission to reject UNE prices based on the ICM cost model.

3) Pole cost support

Verizon's ICM cost model uses pole costs that are unreasonably high and based on loading factors unsupported by documentation. In Docket No. UT-960369, et al., Eighth Supplemental Order, at ¶ 104, the Commission rejected GTE's proposed cost of $737 for poles, which the Commission described as an "undocumented value" that "appears inconsistent with

some of the evidence in the record." In this proceeding, Verizon proposes an even higher pole cost.

Ex. C-1175 shows that the "base cost" of the pole—what Verizon actually paid for the pole—is increased enormously by loading factors (*e.g.*, shipping, handling, minor materials) to arrive at the "ICM material cost"—the pole cost used in the model. This does not include the cost of installing the pole, which is an additional, separate cost. Verizon adds all of these multiple factors despite the fact that it obtains its poles and other materials from its own supply affiliate, and not from any other source. TR 2738-2740.

Verizon provided no supporting documentation to show how the loading factors were determined. Mr. Collins simply said these are "traditional factors" that the Company has always used, and that the Company does not generally look beyond its ARMIS data. TR 2741-42. Verizon further takes the position that supply factor data from 1995-1997 represents the Company's forward-looking costs. TR 2743.

In Staff's view, Verizon has not supported the pole costs it proposes to use in the ICM model.

4) NID costs

Verizon's ICM Material Cost file shows the cost for a 12-pair NID to be 90 times larger than the cost for a 6-pair NID and about twice the cost of a 25-pair NID. This cost clearly does not comport with the use of cost-efficient methods in long run incremental cost models. In response to Staff's concerns over this extremely high cost, Mr. Collins stated that "the ICM does not use a 12-pair NID." When asked why the 12-pair NID is included in the model if the model does not use it, Mr. Collins surmised that it might be a "placeholder" for future use. Ex. T-1174, page 34; TR 2743.

If true, this means that the ICM must use a 25-pair NID, rather than a 12-pair NID, to serve 7-12 line customers and calls into question the soundness of the model. In this situation, a 12-pair NID with a reasonable cost should be used by the model. This is an instance in which the ICM either produces unreasonably high costs using a 12-pair NID or incorrectly provisions plant by using a 25-pair NID for 7-12 line customers.

5) Structure sharing

Staff noted that Verizon's cost studies do not reflect the Commission's prior determinations on structure sharing that were decided in Docket No. UT 960369,et al. (*See*, *e.g.*, Binder 9 of 9, Tab 22, Dark Fiber Investment Worksheet, page 1.) On rebuttal, Mr. Collins states that the model used "actual structure sharing experience." Ex. T-1174, page 30. Staff has two concerns with this response. First, no party has been able to verify whether Verizon correctly reflected its actual structure sharing experience in this case. Second, the ICM model does not allow structure sharing to be reflected on a density zone basis. Hence, if Verizon's structure sharing is greater in higher density areas, which was the assumption made in running the cost models in the generic docket (UT-960369, et al.), the ICM model will not reflect that difference. This problem with structure sharing is yet another reason why the Commission should reject the ICM model.

6) Depreciation rates

Staff originally noted that Verizon's capital recovery rates shown in its ICM cost documentation did not use Commission-authorized depreciation rates. Ex. T-1350, page 6-7. Mr. Collins' rebuttal testimony addressed this deficiency, however, and Staff no longer has a concern with this issue. *See* Ex. T-1174, pages 28-30.

c. Common costs

Verizon used the cost factor for markup on its recurring costs approved by the Commission in the Seventeenth Supplemental Order in Docket No. UT-960369, et.al., at ¶ 203. It does appear, however, from Verizon's Response to Bench Request No. 43, that Verizon has the ability to calculate a Verizon-specific factor for markup that is reasonable. In the Seventeenth Supplemental Order, the Commission rejected Verizon's common cost study and directed Verizon to use the Qwest common cost markup factor, as adjusted, because at ¶ 202 the Commission found that Verizon's proposed factor was "flawed, contrary to federal law," and relied on "historical, embedded numbers, not on forward-looking costs and because GTE seeks to use its common cost methodology as a means to recover its actual costs."

In this proceeding, Verizon bases its monthly recurring charges for UNEs on the recurring costs produced by Verizon's Integrated Cost Model **plus** a 24.75 percent fixed allocator, which is generally referred to as common cost markup. For non-recurring charges, Verizon uses the non-recurring costs developed in its non-recurring cost studies with no additional markup for recovery of common cost. However, Verizon does mark up its non-recurring costs with additional cost elements. These cost elements are pre-ordering, record order, shared and fixed recovery, and OSS recovery. Staff proposes to make downward adjustments to the fixed allocator.

In its Seventeenth Supplemental Order in Docket No. UT-960369, et al., at paragraph 202, the Commission clearly stated why it had to use Qwest's common cost allocator as a proxy for GTE.

> Accordingly, the Commission finds that GTE's common cost study is flawed, contrary to federal law, and should be rejected because GTE's analysis relies on

> historical, embedded numbers, and not on forward-looking costs and because GTE seeks to use its common cost methodology as a means to recover its actual costs.
>
> In paragraph 203 of the same order, the Commission further stated that:
>
> [T]he Commission denies GTE proposed common cost markup factor of 55 percent. While GTE has the burden of proving the magnitude of its common costs, it would not be appropriate to simply state that GTE failed to meet its burden and prohibit recovery of any common costs. For the appropriate common cost markup, the data provided by U S WEST are reasonable proxies. Since this is the best data available, the Commission will apply U S WEST's 19.62 percent attributed cost factor and its 4.05 percent common cost factor to GTE.

The reasons for requiring Verizon to utilize Qwest's common markup factor, as adjusted, no longer apply. Staff believes that Verizon should be required to calculate and use a common cost allocator based on Verizon's own data, reflecting the actual expense incurred by the Company. In its Response to Bench Request No. 43, Verizon showed that it can calculate a common cost factor specific to the Company, but argues against the Commission using that factor because some of the direct costs derived from the ICM are different than the costs the Commission has previously found and ordered as direct costs for several UNE items. Verizon indicates that, because the direct costs ordered by the Commission in some cases (which it does not list) are lower than those generated by the ICM, the direct costs derived from the ICM should be adjusted to represent the Commission-ordered direct costs. Verizon obviously has many resources available to it; after all, it developed the ICM model. Its own intransigence in developing and employing a company-specific cost allocator should not allow it to reap the benefits of a higher allocator, set in earlier proceedings because of inadequacy of reliable information presented by Verizon in that proceeding. Verizon has not made an effective showing of why it should not be directed to implement a company-specific common cost markup factor, based on the calculations used in its Response to Bench Request No. 43.

If the Commission nevertheless decides to allow Verizon to use the 24.75 percent common cost markup factor, Staff believes that the figure needs to be adjusted downward to 24.47 percent. In paragraph 204 of its Seventeenth Supplemental Order in Docket No. UT-960369, et al., the Commission took Qwest's 24.47 common cost markup factor[11] and adjusted it to 24.75 percent to account for some of the accounts that Qwest treated as direct or administrative expenses, but Verizon included in its common cost markup factor of 55 percent, which the Commission rejected in paragraph 203 of the Seventeenth Supplemental Order.[12] Based on Verizon's ICM model, specifically in the Expense Module, these specific accounts are taken into consideration as inputs to the ICM to produce the unit cost. Therefore, at a minimum, markup for recovery of common costs should be reduced to 24.47 percent given that Verizon applies the markup to its recurring costs produced by the ICM.

d. Recurring rates

7. Sub-loop elements

Staff's first concern is with the drop lengths used in the ICM model. Staff's first concern regarding sub-loop elements is with Verizon's proposal to establish a separate rate for drop wire. Ex. 1191, page 1, of Verizon witness Mr. Trimble shows proposed sub-loop elements and rates for feeder, distribution, and drop wire. The sum of the feeder and distribution rates equals the deaveraged zone rate for each zone. However, since drop costs are already included in the deaveraged zone rates, Verizon's inclusion of a separate, additional drop wire rate is

[11]The Commission applied Qwest's 19.62 percent attributed cost factor and its 4.05 percent common cost factor to Verizon, for a markup factor of 24.47 percent.

[12]Paragraph 204 of the Seventeenth Supplemental Order lists the specific cost accounts that Qwest treated as direct or administrative expenses and Verizon included in its common cost factor, and which the Commission considered in raising the 24.47 percent markup factor to 24.75 percent.

inappropriate, and would result in higher than the Commission-approved deaveraged loop rates for the UNE loop.

Staff does not object to establishing a separate rate for the drop as part of the sub-loop unbundling exercise, but if such a charge is established, the Commission should reduce the cost of the unbundled loop previously established in Phase 1 of the Generic Proceeding by the amount of the drop rate.[13] For the subloop pricing, the drop rate should be subtracted from the distribution loop rate. Ex. T-1350, page 6. Moreover, in light of Staff's overall objections to Verizon's ICM cost model, Staff recommends that the Commission not adopt Verizon's estimates of drop costs.[14] Instead, the Commission should adopt the more reasonable Qwest estimates and apply those to Verizon.

Staff's second concern in the area of sub-loop unbundling involves Verizon's estimates of feeder-distribution ratio. As with Qwest, these estimates show little or no variation between density zones; Verizon estimates that approximately 30 percent of investment is in feeder facilities and 70 percent is in distribution facilities for all five density zones. As discussed previously, on a conceptual level, one would expect that the ratio of feeder and distribution would be closer to a 50-50 split in dense urban areas, and that the amount of distribution investment would increase relative to feeder investment in less dense rural areas. Ex. T-1350, pages 8-9. In fact, Table 1 of Mr. Spinks' testimony reveals this to be the case. Staff's estimates developed using the HM3.1 cost model, and following the Commission's prior decisions

[13]In Phase 1 of the Generic Proceeding, the Commission established the cost of the loop. *See* Docket No. UT-960369, et al., Eighth Supplemental Order, page 55, ¶ 70 (April 16, 1998). The Commission did not establish a separate drop rate, as subloop unbundling had not yet occurred at that stage.

[14]Staff also notes that Verizon has not conducted a study of drop lengths for Washington. Ex. T-1250, page 3. In paragraph 133 of the Eighth Supplemental Order in Docket No. UT-

regarding inputs and other adjustments, show that the ratio of feeder to distribution is approximately 48-52 percent in dense urban areas (zone 1), with the percentage of distribution increasing in less dense zones.[15] *Id.* at 10. Staff, accordingly, recommends that the Commission adopt the feeder/distribution ratio estimates set forth in Table 1 for Verizon.

IV. RECIPROCAL COMPENSATION

A-B. LEGAL AND POLICY ISSUES/JURISDICTION

1. Overview

As set forth in detail in the testimony of Dr. Blackmon, Staff recommends that the Commission not make fundamental changes to the reciprocal compensation arrangements it has previously approved in numerous negotiated and arbitrated interconnection agreements, as these arrangements are based upon sound economic principles. Staff agrees, however, that reciprocal compensation may over-compensate or under-compensate the terminating company in situations characterized by long or short call durations, or high or low load factors. For this reason, Staff recommends that the Commission order a more cost-based rate structure, including separate call setup and per-minute rate elements. This rate structure should apply to <u>all</u> local traffic, not just Internet-bound calls. Staff also recommends that the Commission reiterate its policy regarding bill-and-keep compensation – namely, that this compensation structure is appropriate only when traffic between two local exchange carriers is roughly in balance. Ex. T-1230, page 3.

Staff recognizes that the Commission must take into account the FCC's recently-issued reciprocal compensation order in addressing this issue. *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Intercarrier*

960369, et al., the Commission "strongly encouraged" the parties to use the results of such a study.

[15]Zone 5 is the one anomaly in this regard, in that it has a higher proportion of feeder.

Compensation for ISP-Bound Traffic, CC Docket Nos. 96-98 & 99-98, Order on Remand and Report and Order (FCC Order), released April 27, 2001. However, while the FCC Order does limit the Commission's freedom of action on the issue, it does not entirely preempt the Commission.

First of all, the FCC Order addresses only ISP-bound traffic and not section 251(b)(5) traffic which is clearly within the intrastate jurisdiction. Second, even as to ISP-bound traffic, the FCC has placed *caps* on this traffic, and suggests that states may freely act within the parameters set. Third, it is not at all clear that the FCC Order will ultimately withstand judicial review, if (as is virtually certain) the order is appealed to the federal Court of Appeals. Indeed, Commissioner Furchtgott-Roth filed a blistering dissent directly inviting an appellate court to overturn the FCC Order, should it choose to do so.[16]

But whether or not the FCC Order ultimately stands, it is incumbent upon this Commission to take action now to implement reciprocal compensation and not indefinitely defer this matter to a later time. Staff urges the Commission to follow the recommendations of Dr. Blackmon to the extent possible.

---

[16]In noting the FCC's significant departure from, and even reversal of, its previous decisions and orders, and (in the dissent's view) the FCC Order's inconsistency with the Act itself, dissenting Commissioner Furchtgott-Roth offered these comments:

> Today's order is the product of a flawed decisionmaking process that occurs all too frequently in this agency. It goes like this. First, the Commission settles on a desired outcome, based on what it thinks is good "policy" and without giving a thought to whether that outcome is legally supportable. It then slaps together a statutory analysis. The result is an order like this one, inconsistent with the Commission's precedent and fraught with legal difficulties.

2. The FCC's April 27, 2001, Order on Reciprocal Compensation for ISP-Bound Traffic

a. Jurisdictional analysis

The FCC's April 27, 2001, Order was issued in direct response to the District of Columbia Circuit Court of Appeals' ruling vacating its previous reciprocal compensation order in *Bell Atlantic Telephone Cos. v. FCC,* 206 F.3d. 1 (D.C. Cir. 2000) (vacating *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Intercarrier Compensation for ISP-Bound Traffic*, Declaratory Ruling in CC Docket No. 96098 and Notice of Proposed Rulemaking in CC Docket No. 99-68, 14 FCC Rcd 3689 (1999)). The FCC had previously ruled that ISP-bound traffic was jurisdictionally not local but, rather, "interstate" and, therefore, not subject to the reciprocal compensation provisions of section 251(b)(5) of the 1996 Act. The FCC had previously used an "end-to-end" analysis of ISP-bound calls in reaching this conclusion. The Court of Appeals vacated the prior FCC Order for "want of reasoned decisionmaking," and remanded the matter to the FCC. *Bell Atlantic*, 206 F. 3d at 3. Among other things, the court directed the FCC to demonstrate why this traffic was not, in fact, local traffic or "telephone exchange service" subject to reciprocal compensation.

In response to the court's ruling, the FCC issued its April 27, 2001, Order. The FCC revamped its jurisdictional analysis, ruling "[u]pon further review" that ISP-bound traffic is outside the scope section 251(b)(5)'s reciprocal compensation provisions because it falls under one or more of the categories of traffic that are "carve[d] out" of that section by virtue of section 251(g)—namely, "exchange access, information access, and exchange services for such access." FCC Order at ¶ 30 and n. 56; ¶¶ 31-36, 42. Instead, the FCC found that it has jurisdiction over

ISP-bound traffic pursuant to its general common carrier authority under section 201, "as preserved by section 251(i)."[17] *Id.* at ¶¶ 48-49, 52, 65. The FCC held:

> We conclude that subpart (i) provides additional support for our finding that Congress has granted us the authority on a going-forward basis to establish a compensation regime for ISP-bound traffic. When read as a whole, the most natural reading of section 251 is as follows: subsection (b) sets forth reciprocal compensation requirements for the transport and termination of "telecommunications"; subsection (g) excludes certain access services (including ISP-bound traffic) from that requirement; and subsection (i) ensures that, on a going-forward basis, the Commission has the authority to establish pricing for, and otherwise to regulate, interstate access services.

Id. at ¶ 49.

The FCC's April 27, 2001, Order thus arrives at the same *jurisdictional* conclusion as its previous order, namely, that dial-up ISP-bound traffic is jurisdictionally interstate—though it does so by a wholly new analysis. However, whereas the FCC in its previous Order expressly permitted the states to apply reciprocal compensation to ISP-bound traffic, the new FCC Order places limits on such compensation over at least a three-year period, as set forth below.

b. FCC-mandated limits on ISP-bound reciprocal compensation

Beginning on the effective date of its April 27, 2001, Order,[18] and continuing for at least three years, the FCC has capped intercarrier compensation for ISP-bound traffic. For the first 6 months following this date, the rate is capped at $.0015/minute of use (MOU). From the 7th-24th months, the rate is capped at $.0010/MOU. From the 26th-36th months, the rate is capped at

[17]Section 251(i) of the Act provides that "Nothing in this section shall be construed to limit or otherwise affect the Commission's [FCC's] authority under section 201."

[18]The "effective date" is 30 days after publication in the Federal Register. FCC Order at ¶ 112. The order was published in the Federal Register on May 15, 2001.

$.0007/MOU. The latter rate cap remains in effect until the FCC takes any further action, which it may do in a newly-initiated global rulemaking.[19] FCC Order at ¶¶ 8, 78.

In addition to the caps on rates per MOU, the FCC has also capped the total of ISP-bound minutes for which a LEC may receive intercarrier compensation. In 2001, a LEC may receive compensation for the amount of minutes to which it was entitled for the first quarter of this year under its interconnection agreements, annualized, plus a 10 percent growth factor. In 2002 and 2003, a LEC may receive the 2001 amount plus another 10 percent growth factor. *Id.* The FCC acknowledges that carriers may incur costs that exceed the rate and minute caps it adopted, but permits a LEC to recover these additional costs only from its own end users. FCC Order at ¶ 80.[20]

The FCC has determined that ISP-bound traffic should be identified by means of a "rebuttable presumption":

> In order to limit disputes and costly measures to identify ISP-bound traffic, we adopt a rebuttable presumption that traffic exchanged between LECs that exceeds a 3:1 ratio of terminating to originating traffic is ISP-bound traffic subject to the compensation mechanism set forth in this Order. . . . Carriers that seek to rebut this presumption, by showing that traffic above the ratio is not ISP-bound traffic, or conversely, that traffic below the ratio is ISP-bound traffic, may seek appropriate relief from their state commissions pursuant to section 252 of the Act.

FCC Order at ¶¶ 8, 79.

---

[19]On April 27, 2001, in addition to releasing its ISP reciprocal compensation order, the FCC also issued a notice of proposed rulemaking to "begin a fundamental reexamination of all currently regulated forms of intercarrier compensation." Among the options the FCC will consider is bill-and-keep. *In the Matter of Developing a Unified Intercarrier Compensation Regime,* CC Docket No. 01-92 at ¶ 1 (April 27, 2001).

[20]Staff finds it curious that the FCC apparently is permitting CLECs to recover additional costs they incur in terminating purportedly *interstate* traffic from their end users (ISPs) by raising the *intrastate* charges that ISPs pay—since ISPs are permitted to take service under local tariffs and pay local business rates for their connections to LEC central offices and the public switched network. *See* FCC Order at ¶¶ 11, 80.

While the above limits on reciprocal compensation are favorable to the ILECs, the FCC did place one potentially significant restraint on their application. An ILEC may take advantage of the capped rates only if it agrees to exchange all of its traffic subject to section 251(b)(5) (that is, traffic that the FCC formerly identified as "local" traffic and traffic not excluded by virtue of section 251(g)) at the same capped rates.[21] Otherwise, the ILEC must exchange ISP-bound traffic "at the state-approved or state-negotiated rates reflected in their contracts." FCC Order at ¶¶ 8, 89.

c. To what extent does the FCC Order restrict state commission action regarding ISP-bound traffic?

The answer to this question requires a review of the entire order. If one looked only to paragraph 82 of the FCC Order, one might conclude that state commission action on a going-forward basis is entirely preempted. That paragraph provides, in part:

> The interim compensation regime we establish here applies as carriers renegotiate expired or expiring interconnection agreements. It does not alter existing contractual obligations, except to the extent that parties are entitled to invoke contractual change-of-law provisions. This Order does not preempt any state commission decision regarding compensation for ISP-bound traffic for the period prior to the effective date of the interim regime we adopt here. *Because we now exercise our authority under section 201 to determine the appropriate intercarrier compensation for ISP-bound traffic, however, state commissions will no longer have authority to address this issue.*

(Emphasis added).

[21]Footnote 179 to the FCC Order says that "ILECs may make this election on a state-by-state basis." Yet it is not at all clear to Staff how this ILEC "option" is to be exercised if the state Commission determines that section 251(b)(5) traffic, or certain segments of that traffic, for cost-based reasons, should be priced at rates higher than the capped rates the FCC has mandated for ISP-bound traffic. The FCC has treated section 251(b)(5) traffic as jurisdictionally intrastate. To permit ILECs to "offer" a rate lower than that which a state Commission has set for intrastate, non-ISP traffic would essentially make the ILECs the ratesetting body for local traffic, an odd "solution," to say the least.

The matter is more complicated, however, for a number of reasons. First, the FCC has "exercised its authority under section 201" by placing *caps* on the amount of reciprocal compensation payable between carriers for the exchange of ISP-bound traffic. The FCC did not say that rates must be *at* particular rates over the next three years; it said that the rates are capped at those rates, thus implying a ceiling that one may go below. In addition, paragraph 80 of the FCC Order provides in part:

> We also clarify that, because the rates set forth above are *caps* on intercarrier compensation, they have no effect to the extent that states have ordered LECs to exchange ISP-bound traffic either at rates below the caps we adopt here or on a bill and keep basis (or otherwise have not required payment of compensation for this traffic).

(Emphasis in original). Though this paragraph is written in the past tense (*i.e.*, in terms of what states have ordered), it would not appear inconsistent for states in the future to adopt rates for ISP-bound traffic below the caps, if the evidence before the state Commission indicated that this was justified. Indeed, the FCC has expressed a desire in several places in the Order to move toward a bill-and-keep system, so state-imposed rates below the caps would appear consistent with the Order.[22]

Additionally, the FCC has ruled that the capped rates are available only to ILECs that offer to exchange all of their 251(b)(5) traffic at those rates, and that otherwise, the ILECs must exchange ISP-bound traffic "at the state-approved or state-arbitrated reciprocal compensation rates reflected in their contracts." Though this does not expressly refer to rates arrived at in a generic state proceeding, Staff believes that "state-approved" rates could be adopted in such a

[22]Furthermore, for carriers that are not exchanging traffic prior to the adoption of the FCC Order (*e.g.*, new carriers or an existing carrier serving a new market), the FCC has ordered bill-and-keep—which is, by definition, below the "capped" rates. *Id.* at ¶ 81.

proceeding, since these rates will ultimately be reflected in contracts that are consistent with the Commission's generic order.

The second point on which the FCC Order is unclear concerns the method of determining ISP-bound reciprocal compensation. Namely, may state commissions adopt rate structures that include both per-call and per-minute charges for ISP-bound traffic? Though the Order sets forth the caps in terms of minutes of use only (ranging from $.0015/MOU in months 1-6 to $.0007/MOU in months 25-36 and until further FCC action), Staff believes the Commission is not precluded from implementing a bifurcated rate structure, provided that the overall rate thereby applied does not exceed the MOU rate caps in the Order.

Staff reaches this conclusion in light of the FCC's extensive discussion of ISP-bound traffic versus voice traffic. The FCC rejected the ILECs' claims that delivering a data call to an ISP is inherently less costly than delivering a voice call to a local end-user, and it refused to take any action that would result in the establishment of separate intercarrier compensation rates, terms, and conditions for local voice and ISP-bound traffic. FCC Order at ¶¶ 90-91. Moreover, it expressly rejected the arguments of William Taylor[23] that ISP-bound calls should have a different rate because they are generally longer in duration than voice calls. The FCC's response directly invited states to set bifurcated rates to address this problem, both for ISP-bound and voice traffic.

> Mr. Taylor similarly argues that ISP-bound calls generally are longer in duration than voice calls, and that a per-minute rate structure will spread the fixed costs of these calls over more minutes, resulting in lower per-minute costs, and possible over recovery of the fixed costs incurred. Any possibility of over recovery associated with calls (*to ISPs or otherwise*) of longer than average duration can be eliminated through the adoption of rate structures that provide for

[23] Dr. Taylor submitted comments on behalf of Verizon in the FCC docket; he is a witness for Qwest in the present case.

> recovery of per-call costs on a per-call basis, and minute-of-use costs on a minute-of-use basis.

Id. at ¶ 91. (Emphasis added) (footnotes omitted). Since the states clearly may adopt bifurcated rates for traffic that is subject to section 251(b)(5), and since the FCC has said that it supports an ISP rate structure that mirrors the structure for other traffic, it follows that this Commission may adopt bifurcated rates, as recommended by Dr. Blackmon.

In summary, the Commission should establish economically efficient, cost-based prices for transport and termination of interconnection traffic. These rates should then be applied to whatever types of traffic are subject to state jurisdiction, now and after the courts review the FCC Order, including any circumstances where the cost-based rate for "presumptively ISP-bound" traffic falls below the FCC caps. Staff recognizes that the FCC caps may well result in carriers being forced to terminate traffic at rates below their costs, but that outcome is outside the Commission's control and should not excuse the Commission from setting appropriate rates for service that is within its control.

C. RATE STRUCTURE

At the outset, Staff notes that the FCC's Order is somewhat puzzling because it contains two contradictory lines of reasoning. On the one hand, the FCC treats ISP-bound traffic as though it presents unique problems requiring unique solutions. The FCC says that existing intercarrier reciprocal compensation for ISP-bound traffic "has created opportunities for regulatory arbitrage and distorted the economic incentives related to competitive entry into the local exchange and exchange access markets." FCC Order at ¶ 2. Though the FCC opines that these "market distortions" may relate to "any intercarrier compensation regime that allows a service provider to recover some of its costs from other carriers rather than from its end-users,"

the FCC believes that ISPs present particular problems because they typically generate large volumes of traffic that is virtually all delivered one-way, to the ISP. *Id.*

Staff does not concur with this view. As Dr. Blackmon succinctly points out, any possibility of arbitrage in connection with ISP-bound traffic depends upon the assumption that the compensation available to the CLEC exceeds its actual cost of delivering the traffic. In other words, this result stems from getting the price wrong, and not to having a price in the first place. Ex. T-1230, page 16.

But Staff strongly agrees with the FCC's corollary (though seemingly contradictory) observation that there is no basis for treating compensation for ISP-bound traffic any differently from voice traffic or other local traffic. The FCC rejected Dr. Taylor's recommendation (testifying for Verizon) for a lower "Internet" rate on the grounds that such calls are inherently less costly than delivering voice calls. FCC Order at ¶¶ 90-91. Staff opposes Verizon's proposal to do the same thing in Washington. While the duration of a call may affect its cost, Internet calls, just like voice calls, may be of long and short duration. The rate structure should be based on the actual cost-causation factor, not some imperfect indicator such as whether the call is ISP-bound. Ex. T-1230, pages 8-9.

As Staff indicated in its Response to Bench Request No. 42, Staff's first and foremost point regarding the rates for reciprocal compensation is that the Commission should order a more cost-based rate structure for all local traffic. The costs should be calculated based on the costs that the originating carrier would incur had the call terminated on its own network. Staff further recommends the Commission adopt a rate methodology and structure that includes: (1) call setup and call duration costs; (2) consideration of load factor; and (3) tandem switching versus

end-office switching (see part D below). As Dr. Blackmon articulated on the first of these factors:

> The [p]roposal—to establish separate charges for setup and duration—is a reasonable proposal. It would result in reciprocal compensation charges that more accurately reflect the costs of terminating calls of varying lengths. If a company's customers are originating many short calls, that company is imposing significant setup costs on the terminating carrier—setup costs that are not fully compensated by a fixed per-minute termination rate. On the other hand, if a company's customers are originating many long calls, the fixed per-minute termination rate is more than compensatory because the terminating carrier incurs setup costs less frequently than average.

Ex. T-1230, page 8. This holds true for both ISP and non-ISP traffic.

In addition, rate structure should take into account load factor, meaning the average calling volume relative to the peak calling volume. Much of the cost of switching is determined by peak volume, because the switch must have sufficient capacity to handle that peak load. As the load factor increases, the cost per minute decreases since the fixed costs of the switch can be spread over many more minutes of traffic than if the average traffic volumes are very low relative to the peak. Thus, the Commission should establish a rate structure in which the rates vary inversely with the load factor of the traffic being terminated. This factor also affects not only ISP-bound traffic, but all types of traffic subject to reciprocal compensation. *Id.* at 11; Staff Response to Bench Request No. 42.

Staff recommends that the Commission rule on the policy and rate design, then require the parties to put forward cost evidence of what they believe the appropriate rate or rates should be. This would be the default the either party could insist upon in an interconnection agreement.[24] If billing constraints or other reasons led companies to mutual agreement to use another structure, that should be permitted. The Commission should encourage the parties to

reach a mutually acceptable agreement. Staff believes the experience of other states, such as Texas and California, suggests that parties can reach agreement on the details of the rates once the Commission makes the fundamental rate design decision.[25]

Commission Issue No. 5. The Commission has requested comment on Verizon witness Mr. Jones' testimony that interoffice trunk reports indicate peg counts and MOU on an hourly basis, and asked about the implications of this on a rate structure having a call set-up and per minute charge. Staff believes that this information may well provide the basis for both setup/duration charges and load factor differentials. The Commission need not, however, resolve the issue at this time. Staff recommends that the Commission make the policy determination on rate structure and then direct the parties to address the details and find the technical solution.

D. TANDEM SWITCHING

Staff recommends that the end-office rate rather than the tandem switching rate should apply. This is consistent with the principle that the originating carrier should pay the terminating carrier an amount equal to the cost that the originating carrier would have paid had the call stayed on its own network. *See* Ex. T-1230, page 6. As Dr. Blackmon further explained:

> The policy of paying competitors the tandem rate for calls terminating on their switch is based on the general circumstance in which the competitor has customers spread over a broad geographic area on its fiber ring. Were Qwest to serve such a dispersed customer base itself, it would route much of that traffic through a tandem network, and thus it is appropriate to pay the competitor at the tandem rate. However, where there are large volumes of traffic terminating at a

---

[24]Any Commission mandated default, at least regarding ISP-bound traffic, would be subject to the caps mandated in the FCC Order.

[25]Staff directs the Commission's attention in particular to the table at page 1 of Staff's May 2, 2001, Reply to Joint Intervenors Re: Bench Request No. 42. That indicates that in both Texas and California parties were able to reach agreement on bifurcated rate structures including both call set-up and call duration charges and, in some instances, a "blended rate" taking account of both of these factors. The AT&T/SWBT Texas blended rate, moreover, is virtually identical to the rate cap set by the FCC for ISP-bound traffic for the first six-month period following the effective date of the FCC Order.

> single end office, Qwest would use direct end office trunking to deliver that traffic. The traffic would not go through the tandem. The competitor therefore is entitled to compensation at the end office rate and not the tandem rate.

Id. at 20-21.

V. DSL ISSUES

A. LINE SPLITTING—GENERAL

Line splitting is the situation when a CLEC is the underlying voice carrier, and a data CLEC is providing service over the high frequency portion of the loop. Line sharing is described as the situation in which the ILEC is providing the underlying voice service and a data CLEC purchases the high frequency portion of the loop. TR 2156: 24, through 2157: 3-7.

1. Line splitting—architecture

The original positions taken by Verizon and Qwest in this case were that they are not required to provide line splitting. This position would undermine the goal of the 1996 Act which is to provide a pro-competitive policy framework designed to accelerate deployment of advanced telecommunications services to all Americans by opening all telecommunications markets to competition. Line splitting increases consumer choices by making it possible for carriers to compete effectively with the combined voice and data services that are already available from incumbent LECs and through line sharing arrangements. In the FCC's recent rulings on line sharing and line splitting in its Line Sharing Order, the FCC designated the high frequency loop spectrum of an ILEC voice loop as an unbundled network element. *Id.* at ¶ 4. The FCC also permitted states to add their own line sharing requirements, recognizing that local markets may develop differently and more quickly than the national market. *Id*. at ¶¶ 223-225.

In its recent order on reconsideration,[26] the FCC further stated that "an incumbent LEC must permit competing carriers providing voice service using the UNE-platform to either self-provision necessary equipment or partner with a competitive data carrier to provide xDSL service on the same line." (Reconsideration Order, at ¶ 16). The FCC also found that incumbent LECs have an obligation to provide competing carriers with the ability to engage in line splitting arrangements. *Id*. at ¶ 18. During the course of the hearing, both Verizon and Qwest have changed their original positions, and will allow line splitting.

Staff recommends that the Commission require Verizon and Qwest to provide CLECs access to line splitting over UNE-P loops.

1-a. Ownership of the splitter

In their later testimony, both Qwest[27] and Verizon[28] modified their positions to state that they are willing to provide line splitting to competitors, but only where the CLEC purchases the entire loop and provides its own splitter. Ex. T-1192, page 5. Staff recommends that Qwest and Verizon (Incumbent LECs) should not be required to provide the line splitter in a line splitting arrangement because the FCC, in its Line Sharing Order, did not mandate the provision of the splitter.

The parties disagree significantly regarding the ownership and provider of the splitter. Both the AT&T and WorldCom witnesses maintain that the incumbent LECs must be required to provide the splitter in the event that a competitive carrier requests it. Both Verizon and Qwest

[26] *In the Matter of Deployment of Wireline Services Offering Advanced Telecommunications Capability and Implementation of the Local Competition Provisions of the Telecommunications Act of 1996,* Third Report and Order On Reconsideration in CC Docket No. 98-147, Fourth Report and Order on Reconsideration in CC Docket No. 96-98, Third Further Notice of Proposed Rulemaking in CC Docket No. 98-147, Sixth Further Notice Of Proposed Rulemaking in CC Docket No. 96-98, FCC 01-26 (January 19, 2001) ("Reconsideration Order").

[27] Ex. 1092, supplemental direct testimony of Barbara Brohl, at 11.

have stated that they should not be required to provide the splitter in the line splitting arrangement. Staff notes that this issue has been addressed by other state commissions and by the FCC. In its recent Order on Reconsideration, the FCC has deferred the ownership issue among others issues relating to line splitting to an upcoming rulemaking proceeding. (Reconsideration Order at ¶ 25).

At the present time, Verizon and Qwest should not be required to provide and furnish the line splitter if they do not own or provide the splitter in a line sharing arrangement. It is Staff's understanding that in a line sharing environment, the splitter is located in either the data LEC's collocation cage or a common collocation space. In some instances, the data LEC is the provider and owner of the splitter. A competing voice LEC that has purchased UNE-P or an unbundled loop from an incumbent LEC could negotiate with the data LEC to obtain the capability of line splitting. Staff does not exclude the scenario where the incumbent LEC is the owner of the splitter in a line sharing environment; in that instance, the incumbent LEC should continue to provide the splitter for line splitting if it is technically feasible. Staff views this as an efficient way of using an existing splitter if a competing voice LEC could negotiate with the incumbent LEC to continue to maintain the same splitter it provides on the same loop. Staff believes that incumbent LECs should not be required to purchase and install a splitter just for the use by competitive LECs to provide voice and data services, if they do not do this for themselves or their subsidiaries, as is the case with Verizon.

2. Line Splitting—Costs

In the testimony sponsored by Staff witness Jing Y. Roth, Staff reviewed and analyzed line splitting proposals and OSS cost recovery related to line splitting filed by Verizon and

[28]Ex. T-1133, 2nd Supplemental Direct Testimony of R. Kirk Lee, at page 2.

Qwest on January 7, 2001, in Part B of this Docket. Because of the incompleteness of Verizon's proposed OSS costs, Staff recommends that Verizon be required to use the OSS charges adopted by the Commission in its Thirteenth Supplemental Order in Part A of this proceeding on an interim basis until a complete OSS cost can be developed.

Staff recommends that the Commission require Verizon and Qwest to provide competing LECs access to the full functionality of the UNE-P loop. Access to the high frequency of the UNE-P loop will facilitate effective and meaningful competition. Lack of access to line splitting would limit the competitors' ability to compete and provide both voice and data services on the same loop to Washington consumers.

3. The Commission Should Establish A Time Schedule Within Which Qwest and Verizon Must Define The Line Splitting Product

Staff believes that further delay in defining the line splitting product and addressing the operational issues relating to OSS will unreasonably stall the development of competition in the UNE-P environment. It is evident from Qwest's testimony that, as of November 8, 2000, Qwest has provided the CLECs with a copy of the draft line splitting product description and scenarios. Ex. T-1092, page 6. In addition, as Ms. Brohl testified on cross-examination by Mr. Harlow, in January 2001, that Qwest held a meeting to introduce a preliminary concept called the "DA Hotel," and preliminary prices. TR 2212-2219; Exs. 1097, 1098.

Although progress may have been made through what Qwest witness Ms. Brohl called the "line sharing sub-team" (Ex. 1092, page 6) to address the issues of line splitting, Staff has concerns about the effectiveness of such discussions in the absence of a Commission-mandated schedule. Therefore, Staff recommends that the Commission establish a time schedule for the parties to complete these tasks. In establishing a time schedule, the Commission may take into consideration the time schedule set for Verizon by the New York Public Service Commission in

its recent order[29] and the 180 days requirement set by the FCC for line sharing in the Line Sharing Order. *Id.* at ¶ 13.

If the Commission finds insufficient evidence in the record to require a date certain deployment for line splitting, Staff, as an alternative, recommends that the Commission require parties to start a collaborative discussion and provide the Commission with operational results and a deployment schedule within a reasonable time frame.

B. LINE SHARING OVER DLC LOOPS; COMMISSION ISSUE NO. 6

WorldCom and AT&T have asked the Commission to prohibit Qwest from terminating DSL service that is currently provided to a Qwest customer if the CLEC purchases the loop for provision of local exchange service. At the hearing, Chairwoman Showalter asked Staff witness Jing Y. Roth what her recommendation is on this issue. Ms. Roth noted some potential legal/jurisdictional concerns with such a mandate.

The first concern that Ms. Roth noted was that DSL service is not tariffed at the state level, but is tariffed as an interstate service. This is because in FCC 98-292, Memorandum Opinion and Order, on GTE Tel. Operating Cos. GTOC Transmittal No. 1148, CC Docket No. 98-79, released Oct. 30, 1998, the FCC concluded that GTE's offering of DSL service is an interstate service and is properly tariffed at the interstate level. (GTE DSL Order at ¶ 1). The FCC found that the jurisdictional nature of communications is determined by the end points of the communication and not points of intermediate switching or exchanges between carriers. The FCC determined that GTE's ADSL service offering is properly tariffed at the federal level on the ground that it is similar to existing special access services that are subject to federal regulation under the mixed-use facilities rule. (GTE DSL Order at ¶ 23). As Ms. Roth also testified, in

[29]New York PSC Case No. 00-C-0127, Opinion No. 00-12, Opinion and Order

response to questions from the Chairwoman, the Commission's disconnection rules would not prevent Qwest from terminating this type of service to a customer. In addition, when asked to comment from a policy perspective, Ms. Roth expressed the view that it would not be good public policy to continue to require the ILEC to provide xDSL service to a customer if the Commission requires the ILEC to provide line splitting on a UNE-P, as it would, in a sense, hold the ILEC hostage. TR 3911-12.

VI. OSS COSTS

A-B. OSS COSTS ASSOCIATED WITH LINE-SPLITTING

Staff did not find any difference in the engineering and physical processes of splitting a line between a UNE-P loop and over an incumbent-owned voice loop. The only difference (that has been identified; cross-examination of Albersheim, page 2157; Brohl, pages 2184-2197) between line sharing and line splitting concerns the identity of the underlying voice provider. In the line sharing arrangement, the incumbent LEC is the local service (voice) provider, and another data LEC uses the unbundled high frequency portion of the loop to provide xDSL services. Line splitting, on the other hand, involves one or two competing carriers where either one carrier provides both voice and data service over a UNE-P loop, or one competing LEC provides the underlying voice service while another data LEC provides the high speed service. *See, e.g.,* Ex. T-1093, page 4; Ex. T-1365, page 5.

While the evidence in this case shows that there is likely no difference in the cost to provision line splitting as opposed to line sharing, there may be a difference in the operation of OSS, depending on the underlying voice provider. The OSS may need to be modified to accommodate the business relationships among competing providers. Staff believes that

---

Concerning Verizon's Wholesale Provision of DSL Capabilities, page 27 (October 31, 2000).

incumbent LECs should be required to make necessary network modifications to facilitate line splitting, including providing nondiscriminatory and timely access to OSS at reasonable rates and charges. In the Thirteenth Supplemental Order in this Docket,[30] this Commission determined that a charge of $3.27 per LSR for OSS transition shall apply to line sharing. *Id.* at ¶ 174, n. 173.

1) QWEST OSS COSTS RELATED TO LINE-SPLITTING

Qwest witness Ms. Albersheim asserted that because line splitting as a product has not been fully defined, it is impossible for Qwest to estimate the costs associated with OSS changes. Ex. 1071, page 3. Qwest did indicate, however, its willingness to work with interested competitive LECs to discuss the operational and provisioning requirements for line splitting. Given there is no new and specific incremental cost for line splitting, Staff does not object to Qwest's proposal to rely on already proposed or existing rates, as indicated by Qwest witness Ms. Brohl. See Ex. T-1092, page 3, lines 7-9; TR 2272-2273. Qwest did not propose a specific time frame for implementation of the line splitting product, or filing rates with the Commission; Staff does recommend that the Commission set a specific schedule or time frame for such a filing.

2) VERIZON OSS COSTS RELATED TO LINE SPLITTING

Verizon filed its estimated costs for line splitting even though Verizon repeatedly stresses that the process of identifying all necessary steps in facilitating line splitting has not been completed. Verizon has identified four types of costs associated with line splitting: ordering, provisioning, central office activity, and OSS costs. These costs are based on existing costs for

[30] *In the Matter of the Continued Costing and Pricing of Unbundled Network Elements, Transport, and Termination*, Docket No. UT-003013, Thirteenth Supplemental Order; Part A

line sharing and UNE-P costs. As with other cost studies filed by Verizon, the activity time and task probabilities are collected through the discussions with the SMEs. The nonrecurring costs for line splitting is calculated using the following formula:

Activity Time ***x*** *Probability* ***x*** *Labor Rate = Cost*

Staff has concerns about the level of the proposed costs and the timeline for Verizon to develop complete cost studies specific to the line splitting product.

The amounts that a competitive LEC would pay for ordering the initial unit and for provisioning in Verizon's proposal are shown on page 8 of Ex. CT-1365. In addition, Verizon has reserved space in its cost studies for unidentified cost amounts to be added to line splitting orders for categories such as arrangement, coordinated conversion, and OSS. There is no way of knowing the exact amount a competitor would have to pay to Verizon for a complete line splitting arrangement, and Verizon did not indicate when it will file a complete cost study for line splitting. Furthermore, in Verizon's incomplete and proposed interim costs, the underlying costs for specific activities are inflated. Staff identified certain flaws in the Verizon cost studies in the testimony filed on October 23, 2000. Ex. CT-1360. In that testimony, Staff recommended that the Commission modify Verizon's nonrecurring cost studies by:

- reducing processing times for "Production Order Entry,"
- decreasing time estimates for "Error correction" and "Jeopardies," and
- modifying the time estimate for "Meet Point."

Nonrecurring costs for UNE-P are part of the nonrecurring cost studies for which Staff has recommended these modifications. The same flaws exist because the line splitting costs are generated based on Verizon's proposed UNE-P and line sharing costs. Staff understands that the

(Jan. 31, 2001).

costs associated with line sharing have been determined by the Commission in Part A of this proceeding. Since all other nonrecurring costs for UNEs are being considered by the Commission as part of this phase of the proceeding, Staff recommends that the proposed interim line splitting costs be modified accordingly. Because of the incompleteness of the line splitting cost study, Staff also recommends that the Commission require Verizon to file a complete product description and cost study in a timely manner.

VII. CONCLUSION

For the reasons set forth above, Staff requests that the Commission adopt and implement its recommendations on the issues presented in this docket.

Respectfully submitted this 29th day of May, 2001.

CHRISTINE O. GREGOIRE
Attorney General

_____
MARY M. TENNYSON
Senior Assistant Attorney General

_____
GREGORY J. TRAUTMAN
Assistant Attorney General
Attorneys for Washington Utilities and Transportation Commission