BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of Review of Unbundled Loop and Switching Rates and Review of the Deaveraged Zone Rate Structure.	DOCKET NO. UT-023003 STAFF'S RESPONSE TO VERIZON'S MOTION FOR CLARIFICATION AND PETITION FOR RECONSIDERATION, AND TO XO AND PAC-WEST'S PETITION FOR RECONSIDERATION

1 On February 23, 2005, the Commission issued a Notice of Opportunity to Respond to Verizon's February 22, 2005, Motion for Clarification and Petition for Reconsideration of the Commission's Twenty-Fourth Supplemental Order ("Order") in this docket, and to XO and PAC-WEST's Petition for Reconsideration of the Order. Staff responds as set forth below.

Staff's Response to Verizon's Petition for Reconsideration

2 Verizon's Petition for Reconsideration asks the Commission for reconsideration in the following six areas: (1) the use of the HM 5.3 model; (2) cost

of capital; (3) depreciation; (4) using a forward-looking calibration (FLC) in HM 5.3; (5) inputs used in the models; and (6) switching costs.

3 According to Verizon's petition, the Commission erred in not rejecting HM 5.3 outright because HM 5.3 does not comply with cost modeling requirements, is not consistent with TELRIC principles, fails reasonable validation tests, is incapable of modeling inputs correctly, and suffers from other significant modeling defects. (Verizon Petition, at 6-23.) Verizon argues, likewise, that the Commission also erred in not adopting the cost of capital and depreciation rates advocated by Verizon. In describing the reasons why Verizon believes the Commission grievously erred in its decisions, Verizon brings no new facts or evidence to light. Nor is any showing made that the Commission acted in an arbitrary or capricious manner. In fact, the arguments made by Verizon are very much like the arguments made by AT&T and Staff in testimony urging the Commission to reject the VzCost model. The Commission, however, refused to reject either model, and noted that both models failed to comply fully with various cost model criteria set forth by the Commission. (*See* Order, at ¶¶220, 226.) Verizon's petition for reconsideration of the decisions regarding cost of capital, depreciation rates, and to reject HM 5.3 should be denied.

4 Verizon also alleges that the Commission erred in not applying the forward-looking calibration (FLC) adjustment to HM 5.3. Staff does not believe the Commission erred in its decision, and the Commission is correct to recognize that the current cost to book cost (CC/BC) ratio used in HM 5.3 is appropriate when it concluded that "each party's approach to determining annual expenses is generally acceptable." (Order, at ¶112.) The Commission also noted that "because of the idiosyncratic relationship between models and inputs, the selection of model and inputs cannot necessarily be made as independent decisions." (Order, at ¶202.) Staff agrees with the Commission that it would be unwise to attempt to mix and match input adjustment methods between models. The Commission should deny Verizon's request to use the Verizon's FLC adjustment in the HM 5.3 model. If the Commission, however, did intend to apply the FLC to HM 5.3, Staff recommends that the CC/BC adjustment first be removed.

5 Verizon also asks the Commission to reconsider various input decisions made in the Order, including plant mix, structure sharing, placement costs, material costs, cable size, and feeder fill.

6 With respect to plant mix, the Commission rejected both HM 5.3 and VzCost's plant mix assumptions. The Commission has decided to use the plant mix values used in the USF proceeding (Docket UT-980311(a)) for use in the HM 5.3

model and to adjust VzCost to better reflect its actual placement of underground facilities. (Order, at ¶¶285, 286) Verizon seeks reconsideration of both decisions. With respect to the adjustment to the VzCost model, Verizon argues that the Commission failed to address the engineering testimony regarding applicable engineering constraints.

7 Staff sees no need for the Commission to further address the issue. Since VzCost builds too much expensive underground plant, the Commission corrected that deficiency by adjusting the artificial constraints imposed by the model for deciding when to place underground facilities. Verizon's petition fails to address why the applicable engineering constraints result in a forward looking network with excessive underground plant when the existing network, which is presumably subject to the same constraints, has much less underground plant. With respect to the decision to use the plant mix from the USF order, Verizon argues that it did object to the use of Staff's plant mix input and that there was no evidence that Staff's prior density zone inputs were consistent with the more current plant mix data. Verizon concludes that "HM 5.3's recognized flaw cannot be saved by reference to these data." (Verizon Petition, at 38.) Verizon's objection appears to be that the Commission did not reject HM 5.3, which was addressed by Staff earlier. The Commission should deny the petition.

8 Verizon's request for reconsideration of the structure sharing and remaining inputs consist of little more than a rehash of the arguments it previously made and lost. Staff has reviewed the decisions made in the Order and found no errors of fact. The decisions were not made in an arbitrary or capricious manner. Verizon's request should be denied.

9 Verizon also contends that the Commission is in error when it concluded that it was too difficult to reduce line counts in the VzCost model by five percent to account for a fully competitive market. As a result, the Commission directed the Verizon loop rates to be increased by 3.1 percent, the same amount of increase obtained from the HM 5.3 model in response to the 5 percent demand reduction. Verizon now claims that the adjustment "can be easily accomplished by performing new BC runs using the adjusted demand," and asks the Commission for permission to do so in the context of making compliance runs. (Verizon Petition, at 45.) Whether or not this statement is accurate, however, it does raise a concern for Staff. As the Commission is aware, Staff did not have great success working with the VzCost model and, indeed, the Commission itself noted a number of issues and concerns with the time and manner in which the model must be run to produce results. (Order, Appendix A, VzCost Commentary.) It is not likely that Staff will be able to verify the results from the VzCost model independently within a reasonable

time frame in order to validate the accuracy of compliance filing made by Verizon. Staff also has particular concerns relating to other UNEs elements other than two-wire loop because the Commission's Order did not provide these specific results. To that end, the Commission may consider using its consultant to assure the Commission that Verizon has properly followed the Commission's directives, regarding cost results from the VzCost model used for the compliance filing.

10 The last area for which Verizon seeks reconsideration is switching costs. According to Verizon, the Commission erred in rejecting the SCIS model, using new switch discounts, and excluding vertical feature costs, and erred in its choice of a fill factor.

11 Staff believes the Commission did the best it could given the evidence presented in the record. Verizon's failure to provide the source code until it was too late for AT&T to analyze it in time for hearings was neither AT&T's nor the Commission's fault. Verizon points to a FCC brief and Notice of Proposed Rulemaking (NPRM) to support its proposition that new switch discounts do not comport with TELRIC. Verizon did not point out any court or FCC orders, however, that would directly support its assertions. Staff does not even understand Verizon's argument regarding vertical feature costs, as the HM 5.3 switching costs include the cost of vertical features. Finally, Verizon asks the Commission to

substitute its SCIS utilization factor into the HM 5.3 switch model. As discussed previously, Staff agrees with the Commission that it would be unwise to attempt to mix and match input adjustment methods between models. The Commission should deny Verizon's petition for reconsideration of the switching decision.

<u>Staff's Response to XO and PAC-WEST's Petition for Reconsideration</u>

12 XO and PAC-WEST petition the Commission for reconsideration of its decision to accept Verizon's calculation of the reciprocal compensation rate, contending that the Commission erred in stating that the XO and PAC-WEST position was not properly supported on the record, that arguments were not raised timely, and that the Telecommunications Act of 1996 allows the price of call termination to be lower that the cost of ordinary switching. XO and PAC-WEST take issue with the Commission's statement in paragraph 528 of the Order, stating that it directly conflicts with the FCC's Local Competition Order.

13 XO and PAC-WEST cite language from ¶1057 of the Local Competition Order, where the FCC states that the additional cost of terminating a call primarily consists of the traffic sensitive component of local switching, as the basis for their claim that the Local Competition Order expressly contradicts the Commission's decision. Staff notes that the last sentence of ¶1057 states: "For purposes of setting rates under section 252(d)(2), only that portion of the forward-looking, economic

cost of end-office switching that is recovered on a usage sensitive basis constitutes an 'additional cost' to be recovered from termination charges." What XO and PAC-WEST appear to be arguing is that the "portion of the forward-looking, economic cost of end-office switching" referred to in the Local Competition Order is the per-minute of use local switching rate, rather than some subset of the local switching costs. Staff believes it would be helpful to the parties if the Commission could provide additional explanation as to what it sees as being required by the FCC's statements regarding additional cost.

DATED this 7th day of March, 2005.

ROB MCKENNA
Attorney General

____

GREGORY J. TRAUTMAN
Assistant Attorney General
Counsel for Commission Staff