Before the

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

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

RESPONSE TESTIMONY OF RICHARD CABE ON BEHALF OF RHYTHMS LINKS INC. AND COVAD COMMUNICATIONS COMPANY

July 21, 2000

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

RESPONSE TESTIMONY OF RICHARD CABE ON BEHALF OF RHYTHMS LINKS INC. AND COVAD COMMUNICATIONS COMPANY

I. INTRODUCTION

Q. Please state your name and business address.

A. My name is Richard Cabe. My business address is 219 I Street, Salida, Colorado.

Q. Are you the same Richard Cabe who submitted Direct Testimony in this proceeding on May 19, 2000?

A. Yes, I am.

Q. What is the purpose of your response testimony?

A. My testimony responds to Qwest's proposal for a charge on line shared access to the high bandwidth portion of the loop and to Qwest's proposal for a recovery mechanism for costs of OSS improvements associated with line sharing.

II. ALLOCATION OF LOOP COST TO LINE SHARED ACCESS

Q. Qwest proposes to charge CLECs for line shared access to its local loops. Does Verison seek to impose a similar charge?

A. No. Verison recognizes that the FCC pricing rules for the line sharing UNE preclude allocation of more loop cost to the line sharing UNE than was allocated to

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

the carrier's retail ADSL tariff, which is zero dollars in every instance that I'm familiar with. Like all other carriers filing retail ADSL tariffs before the FCC, Verison did not believe that loop costs are direct costs of providing ADSL over a shared line, and made no such allocation in it's cost support. My direct testimony provides references positions of BellSouth and Bell Atlantic which recognize an obligation to provide line shared access to CLECs at prices which allocate no more loop cost to line sharing than to their own ADSL service over a line that is shared with POTS, and since they allocated no loop cost to their ADSL service they do not attempt to impose a line sharing charge on CLECs' access to line sharing.

Q. **Did Qwest allocate any loop cost to its ADSL service in its Federal tariff filing?**

A. No. In response to Covad request 1-22, which is attached as Exhibit RC-6, Qwest stated as follows: "The cost of the local loop is attributed to the basic service. There is no direct separate allocation of the cost of the MegaBit service on the local loop since both voice and MegaBit services are provided over a single loop. Therefore there is no incremental cost of the local loop attributed to MegaBit."

Q. Does Qwest take the position that line sharing with CLECs creates loop related costs that are not similarly created when Qwest shares use of a line between pots and its own XDSL service?

A. Apparently not. Covad request 1-21 asks Qwest to identify any differences in this respect between MegaBit service use of a loop and a CLEC's use of the line sharing UNE, and no differences were identified. Qwest's response to this request is attached as Exhibit RC-7.

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

Q. Please describe the consequences that would follow from charging CLECs a price greater than zero for access to line sharing.

A. The immediate consequence would be that CLECs would pay the amount of the line sharing charge to Qwest and would have to recover that amount from their customers. As explained in my direct testimony, this would amount to double recovery for Qwest. Moreover, while U S West enjoys its double recovery, it is the Washington consumers that will be harmed the most by U S West's proposal because those consumers will pay twice for the single loop that serves their home or business. In addition to collecting this charge from CLECs, Qwest's proposal would insulate it from vigorous price competition from CLECs, and Qwest could expect to maintain a margin on retail xDSL services at least equal to the line sharing charge. The imputation test that Qwest discusses, if it were effective, would merely enforce an artificial price floor and protect Qwest's margin on its MegaBit service. The net effect of a positive line sharing charge would be Washington consumers facing a higher retail price for line shared xDSL services and higher profits for Qwest than would be the case with a cost based price of zero for access to line sharing.

Q. Qwest witnesses discuss allocating cost to its retail rates for ADSL service and the outcome of imputation tests that could be imposed, then argue that their line sharing charge is consistent with the FCC's line sharing order. Do you agree?

A. No. The FCC's requirement is quite clear. The ILEC can charge no more for shared line access than it allocated for the loop in interstate retail rates for ADSL

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

services prior to the date of the line sharing order[1]. The clear implication is that if no loop cost is allocated to the ILEC's ADSL offering, then the rate for line sharing must be zero. It is a simple matter of arithmetic that whatever margin is built into the retail rates is an amount that could also be used in an imputation test that the rates would pass. However, this is simply irrelevant to the question of compliance with the FCC's order or the question of compliance with the Act's requirement of nondiscriminatory pricing. The FCC order did not require that charges for the line sharing UNE could not exceed the margin in existing retail rates, but referred very clearly to allocations of loop cost in cost support for those rates.

Q. Aside from the issue of compliance with the FCC's line sharing order, what relevance do you attach to Qwest's reliance on imputation rather than allocation.

A. Qwest seeks to blur a clear FCC determination based on cost allocation in a specific filing to the point of including amounts "perhaps *imputed*"[2] in a "secondary computation".[3] This shifting of attention from *cost allocation* to imputation tests in *retail price determinations* is clearly contrary to the FCC's Third Report and Order, but it also profers an empty promise which is worthy of note. In response to Covad request 1-46 , attached as Exhibit RC-8, which solicited Qwest's position on application of imputation tests to pricing of MegaBit service and advanced services

[1] Third Report and Order in CC Docket No. 98-147 and Fourth Report and Order in CC Docket No. 96-98, FCC 99-355, adopted November 18, 1999, released December 9, 1999 (hereinafter referred to as "Third Report and Order").

[2] Thompson Supplemental Direct Testimony of Jerold L. Thompson, JLT-T5, at page 3-4, footnote omitted, emphasis in original

[3] Thompson Supplemental Direct Testimony of Jerold L. Thompson, JLT-T5, at Page 5, lines 11 & 12

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

generally, Qwest refuses to respond, arguing that these matters are not relevant to the questions at issue in this proceeding. Thus, Qwest's testimony seems to (but clearly does not) offer an imputation test in lieu of the cost determination on which the FCC relied.

Q. If Qwest were willing to submit its price determinations for advanced services to an imputation test, would this be an adequate substitute for the FCC's approach to pricing line shared access by reference to the amount of loop cost included in cost support for federal tariff filings for ADSL service?

A. Not at all. An imputation test would simply codify an artificial price floor which insulates Qwest from price competition; no CLEC could compete below the floor because of Qwest's charge for access to line sharing. The effect of the FCC's requirement was to accomplish something much more fundamental than avoiding a price squeeze; the FCC's criterion enforces the 1996 Act's requirement of non-discriminatory pricing - an objective that cannot be accomplished by an imputation rule.[4] While a price squeeze cannot be accomplished with non-discriminatory pricing, the converse is not true. That is, the elimination of price squeezes does not necessarily eliminate discriminatory pricing. If Qwest were willing to submit to an imputation test for advanced service pricing (which apparently it is not), and if the

[4] *See* Third Report and Order. The FCC's approach was to rely on cost support for retail ADSL services filed before line sharing was required and thus to "take the ILECs at their word" as to any loop costs that are incremental to the use of an active POTS loop for xDSL services. The fact that the ILECs were unanimous in not charging loop cost to their retail ADSL services shows that the FCC's approach was a good one. If such filings were now amended with a view to manipulating the rate for wholesale line sharing the approach would no longer be reasonable.

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

imputation mechanism was successful in eliminating price squeezes,[5] there would still be no guarantee that the Act's requirement of non-discrimination was being enforced. While Qwest's line charge proposal may satisfy an imputation test it violates the Act's requirement of non-discriminatory pricing - it charges CLECs $9.08 per line per month for something that Qwest has the use of at a cost of zero.

Q. Qwest witness Fitzsimmons refers to "cable-based and wireless" providers of advanced services. How should the commission consider alternative technologies in establishing prices in the present case?

A. The right policy is for the Commission to set prices correctly and let the market choose among alternative technologies. The Commission should take care that prices established in this case do not distort the outcome of competition between alternative technologies. The Commission's determinations in this proceeding may influence the ability of the market to choose correctly among alternative technologies for the delivery of advanced telecommunications services. In order for price competition to send the correct cost signals to consumers, the price of xDSL services must not be burdened by a non-cost-based line sharing charge. Beyond its deleterious impact on competition among xDSL providers, a non-zero price would also distort competition between xDSL technologies and competing wireless or coaxial cable based technologies which do not rely on copper loops. In order for that

[5] The very best of imputation rules may fall short of complete success in eliminating price squeezes. Such rules establish an administrative process to limit an ILEC's ability to act on its incentives regarding price squeezes. Even when such an administrative process is functioning as well as it possibly can, it will only be a substitute for the incentives of a competitive market. In the case at hand there has been no credible contention that access to local loops is a competitive market.

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

competition between technologies to reach an efficient result, providers of services that rely on the high-bandwidth capabilities of copper loops must be able to reduce prices without being hampered by an arbitrary allocation of costs to the high-bandwidth portion of the loop. The high-bandwidth portion of the loop is a crucial input to production under some technologies (xDSL) but not others (wireless, cable); competition among these technologies can reach an efficient result only if the high-bandwidth line sharing UNE has a price equal to its cost: zero. Allowing the market to correctly choose among competing providers and technologies requires a price of zero for the high-bandwidth portion of the loop. The need to prevent windfall profits, encourage economically efficient outcomes, and promote the public policy imperative to promote the deployment of advanced services, such as DSL-based services, support Rhythms' and Covad's proposal to adopt no recurring line-sharing charge for access to the high-bandwidth portion of the local loop.

Q. Does Dr. Fitzsimmons' discussion of chickens and wings provide any useful guidance to the commission in this proceeding?

A. No. There are several shortcomings to any attempt to apply this entertaining textbook discussion of joint products to the case at hand. First, use of the analog voice portion of the loop, whether as a UNE or for POTS services, is not a joint product with line shared access to the same loop - at least not in the conventional sense of the conventional model of pricing joint products. This is so because line shared access is not available unless the analog voice portion of the loop has already been sold. One can buy the analog voice portion of the loop without line shared access to the same loop having been sold, but not the other way around. One cannot

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

buy line shared access to the high bandwidth portion of the loop unless the analog voice portion of the loop has already been sold. This asymmetry, or sequential character of the two products violates the most fundamental assumptions underlying the conventional model of joint product pricing. Imposition of this requirement on Dr. Fitzsimmons' example would mean that one can only buy chicken wings if the breast had already been sold, and until the breast is sold the wings are simply not available for purchase. If the breast is never sold, the wings cannot be offered for sale. If there were a law imposing this sequential character on chicken wings and breasts, the analysis would be very different than is now presented in ECON 101 texts. Line shared access to a local loop is the first product I have ever seen that partakes of this peculiarity, and I don't know if the textbooks will ultimately refer to the cost of the loop in this situation as a joint cost, a shared cost, a sequential products shared cost, or something else, but it is clear that current textbooks do not deal with this type of product. There are other glaring inconsistencies between the two examples: first, the market for loops isn't competitive. One obvious implication of this observation is that competition will constrain a chicken producer's relationship to the price of its products in a way that doesn't apply to Qwest's relationship to the price of loops - whether for POTS services or for access to the high bandwidth portion of the loop. For a competitive producer of joint products, the sum of the prices of the joint products must be equal to the average cost of production. Since Qwest's proposal in this proceeding is to set the sum of the prices of line sharing and services provided through the analog voice spectrum of the loop at 150% of average cost, it should be clear that applicability of the chicken wings story to Qwest loops

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

must be limited[6]. If Dr. Fitzsimmons intention was to use the example to illustrate the outcome in a competitive market, this is the first rule: competition will not allow the supernormal profit implied by the Qwest proposal, whether there are joint products or sequential products or anything else. Beyond the observations that analog voice channels and line shared access partake of a sequential character that does not apply to ordinary joint products, and that competition implies no more than a *normal* profit, use of this analysis of pricing of joint products to predict how a competitive market would price POTS and line shared access to the loop would require major conceptual extensions of the model and detailed demand estimates that are never available in regulatory proceedings. Two obvious further conceptual shortcomings of the model include its lack of analysis of demand relationships among the various products that are, or might soon be, provided over the two portions of the loop, and dynamic considerations in this group of products which are obviously in a state of considerable flux. Finally, the source that Dr. Fitzsimmons cites for the analogy between pricing chickens and pricing loops concludes that "under FCC assumptions, the DSL portion of loop should be zero."[7]

Q. Given your discussion of the sequential character of the two portions of the loop, do you agree with Qwest witnesses' contention that neither portion has any incremental cost?

---

[6] Note that the Qwest proposal to allocate 50% of loop cost to the line sharing arrangement is not accompanied by a proposal to reduce the allocation to services on the voice channel from 100% down to 50%.

[7] Presentation by George S. Ford, provided by Qwest in response to Rhythms discovery request 3-1. As indicated in my testimony, I'm not recommending that the Commission rely on any analysis similar to that contained in Mr. Ford's presentation.

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

A. No. As I indicated above, , there is a sequential peculiarity associated with the two portions of the loop, and the standard analysis of an underlying facility used to provide two or more services or UNEs does not apply. Interestingly, the FCC's Local Competition Order, at ¶691, clarifies the matter in describing cost causation: "Costs are causally-related to the network element being provided if the costs are incurred as a direct result of providing the network elements, or can be avoided, in the long run, when the company ceases to provide them." There are two tests, either of which will establish cost causation. Application of both tests to the two portions of the loop leads to the unqualified conclusion that the analog voice portion of the loop causes loop costs and line shared access to the high bandwidth portion of the loop does not cause any loop costs. The full complement of loop costs must be incurred in order to provide the analog voice portion of the loop, but no additional loop costs are incurred in order to provide line shared access. Likewise, discontinuing line shared access to a loop does not allow a company to avoid any loop costs, whereas discontinuing provision of the analog voice portion of a loop allows the company to avoid, in the long run, costs associated with that loop. Thus, cost causation allows no attribution of cost other than the result reached by the FCC: 100% of loop costs are attributed to the analog voice portion of the loop and none to line sharing. If it were possible to purchase the high bandwidth portion of a loop that is not already in use for analog voice services this analysis would be different. Thus, so long as the asymmetry or sequential character of the two portions of the loop continues, cost causation admits no attribution of costs other than the one reached by the FCC.

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

Q. What considerations other than cost causation favor the determination reached by the FCC?

A. My direct testimony discussed these considerations. In the context of discussing the Qwest proposal it is worth observing that public policy evaluation of regulated prices always requires consideration of (at least) the following two roles of prices: prices have the role of recovering costs, and they influence behavior in ways that affect economic efficiency. In the present case, the role of prices in recovering loop cost can be dismissed immediately, because the full costs of the loop are already being recovered through other prices. **Cost recovery doesn't require allocation of any loop cost to line sharing arrangements.** Indeed, any allocation of loop cost to line sharing would amount to **over allocation**, and would require adjusting other prices to avoid double recovery.[8]

The issue of prices influencing behavior in ways that affect economic efficiency is more complex. First, the principle of cost causation is based on economic efficiency, and, as discussed above, so long as it isn't possible to buy line shared access on an unused loop, the principle of cost causation requires a price of zero for line shared access. next, if any amount of loop cost is allocated to line sharing the resulting price will be discriminatory because it charges CLECs a positive amount for something available to the ILEC at a cost of zero. This discrimination violates Section 251 of the Act and affects economic efficiency in several ways. This

[8] Qwest is presently recovering 100% of loop cost from services provided over the analog voice channel on a POTS loop and now proposes to recover an additional 50% on loops used in line sharing arrangements. Since this proposal was not accompanied by a proposal to reduce prices on services provided over the voice channel, Qwest is proposing a recovery of 150% of loop costs on loops in line sharing arrangements.

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

discrimination will distort competition between the ILEC and CLECs, interfering with the development of a competitive market. The obvious immediate consequence of this distortion is that CLECs would not be in a position to engage in price competition on an even footing with the Qwest. By imposing a cost on the CLECS for a line sharing arrangement that is available to the ILEC without cost, the ILEC insulates its line shared xDSL operations from price competition. The lowest price that a CLEC engaged in price competition could otherwise sustain becomes inflated precisely in the amount of the discriminatory line sharing charge. This affords the ILEC an opportunity to earn higher than normal profit from its offerings in the xDSL market insulated from price competition, as well as from double recovery of loop costs in line sharing charges, and denies consumers the benefit of price competition. Further, establishing a discriminatory line sharing charge positions the ILEC to engage in a price squeeze if it so chooses. A non-zero line sharing charge would leave CLECs unable to compete with alternative technologies (cable, wireless technologies) at prices that reflect the true costs of line sharing. If a positive price for line sharing is established initially and an imputation mechanism is in place to prevent a price squeeze, the administrative process of the imputation mechanism could become an impediment to the ILEC reducing its retail price to compete with providers using other technologies. In addition to distorting competition, establishing a positive line sharing charge would keep the retail price of xDSL service higher than would otherwise be the case and consequently would discourage usage of this advanced telecommunications service, contrary to the mandate of the Act.[9]

[9] Beyond the mandate of the Act to promote advanced telecommunications services, broad adoption of xDSL services may promote efficiency by actually reducing costs. ILECs have often claimed that internet data traffic between subscribers and their internet service providers imposes congestion and additional costs on

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

Q. Qwest witnesses Thompson and Fitzsimmons argue that the TELRIC method of pricing is inadequate to the task of pricing line-shared access to the local loop. Do you agree?

A. No. First note that the discussion of cost causation above shows that no discussion of shared cost is really necessary. Nevertheless, the pricing methodology based on TELRIC cost calculations described in the FCC's First Local Competition Order in CC Docket 96-98 provides explicitly for recovery of shared costs.[10] In defining unbundled network elements the FCC has tried to establish definitions that correspond closely to physical facilities in the network so as to avoid the problems that arise whenever shared costs must be allocated between two or more unbundled network elements. The 'extension' of the TELRIC methodology that remained to the FCC in the line sharing order was merely to adopt a specific method of determining how the full cost of the loop should be recovered.

> In this Order, we establish guidelines to assist the states in applying our unbundled network element pricing rules to line sharing when they arbitrate modifications to interconnection agreements or otherwise adopt permanent prices for this unbundled network element. These guidelines either follow directly from the Total Element Long Run Incremental Cost (TELRIC) methodology that the Commission set forth in the *Local Competition First Report and Order* to govern interconnection and unbundled

---

the local switching and transport portions of the network. Insofar as this congestion is important, it applies only to dial-up internet connections - when an internet user switches from a dial-up connection to an xDSL arrangement, that user's internet traffic no longer goes through the ILEC's switch or local transport network. Thus, promoting the adoption of xDSL services may actually reduce costs of the local network.

[10] See, for example, the discussion of "shared costs" and the "costs of shared facilities and operations" at ¶ 682. *First Report and Order in CC Docket No. 96-98*, FCC 96-325, adopted August 1, 1996, released August 8, 1996 (hereinafter referred to as "*Local Competition Order*"). While the loop is a facility that is shared in a line sharing arrangement, the sequential character of the two portions of the loop avoids difficulties associated with shared costs.

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

> network element pricing, or, if not a direct outgrowth of those principles, are consistent with them in the context of this particular unbundled network element.[11]

Q. Mr. Thompson states that the FCC did not adopt a method of dividing the shared loop cost. Do you agree?

A. No. In the paragraph immediately following the paragraph on which Mr. Thompson relies for the need for an extension of the TELRIC methodology, the FCC defined the manner in which to allocate the shared cost of the loop between the POTS portion of the loop and the high bandwidth portion of the same loop: loop cost is to be allocated so as to assign no more loop cost to the line sharing UNE than the ILEC allocated to its interstate ADSL service at the time of filing cost support for that service. The FCC goes on in that paragraph to refer to the effect of its determination as "establishing the TELRIC of the shared line."

> 139. We conclude that, in arbitrations and in setting interim prices, states may require that incumbent LECs charge no more to competitive LECs for access to shared local loops than the amount of loop costs the incumbent LEC allocated to ADSL services when it established its interstate retail rates for those services. This is a straightforward and practical approach for establishing rates consistent with the general pro-competitive purpose underlying the TELRIC principles**. We find that establishing the TELRIC of the shared line in this manner** does not violate the prohibition in section 51.505(d)(1) of our rules against considering embedded cost in the calculation of the forward looking economic cost of an unbundled network element. We also note that this approach was recently approved by the Minnesota PUC. (footnotes omitted, emphasis supplied)

Contrary to Mr. Thompson's contention that some extension of the TELRIC methodology remains to be accomplished and Dr. Fitzsimmons' contention that the shared line UNE has no TELRIC, establishing the TELRIC of the shared line only required a determination as to how to allocate loop cost, and the FCC clearly and definitively made

[11] Third Report and Order at ¶ 132, footnote omitted

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

that determination. If any ambiguity remained from the FCC's use of the word "may" or if uncertainty remained regarding the amount of loop cost allocated to retail ADSL services, such questions were resolved in the FCC's recent Access Charge order. In that May 31, 2000 Order, the FCC interpreted its own rules adopted in the line sharing order to dictate no allocation of shared loop cost to line sharing:

> We also reject the argument that elimination of the PICC is inconsistent with the Line Sharing Order. The Line Sharing Order concluded that states should not permit incumbent LECs to charge more to competitive LECs for access to shared local loops than the amount of loop costs the incumbent LEC allocated to ADSL services when it established its interstate retail rates for those services. To date, we are not aware of any incumbent LECs that have allocated any loop costs to ADSL services.[12]

Q. As a matter of policy, do you agree with the FCC's determination to allocate all loop cost to the loop UNE and none to line sharing?

A. Yes. For the reasons set out in my direct testimony and above, this allocation was the obvious correct choice; any allocation of loop cost to line sharing would result in double recovery, would limit the development of a competitive market in residential xDSL services, and would discourage adoption of advanced telecommunications services which the Federal Telecommunications Act of 1996 sought to encourage. The obvious and immediate consequence of an allocation of loop cost to line sharing is to allow the ILEC to exercise market power to earn extraordinary profit and dominate a potentially competitive emerging market.

[12] FCC 00-193, Sixth Report and Order in CC Docket Nos. 96-262 and 94-1, Report and Order in CC Docket No. 99-249, Eleventh Report and Order in CC Docket No. 96-45 (rel. May 31, 2000), at ¶ 98.

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

III. RECOVERY OF OSS TRANSITION COSTS RELATED TO LINE SHARING

Q. Please describe Qwest's proposal for recovery of the costs of OSS upgrades to accommodate line sharing.

A. Qwest proposes a charge of $3.55 per line per month for a period of 5 years on every line used by a CLEC to provide xDSL service while that same line is also in use for POTS service. The charge is not applied to lines over which Qwest provides both xDSL service and POTS service.

Q. Please summarize your response to this proposal.

A. First, I will show that Qwest and its retail xDSL customers benefit from the OSS improvements at issue, and any recovery of these expenditures should be from all customers receiving xDSL services over a line that is also used for POTS. Contrary to Qwest's assertion, this issue was not addressed by the Commission in its 17th Supplemental Order and different considerations arise than were addressed in the record on which the 17th Supplemental Order was based. Next, skepticism regarding the amount of cost to be recovered, as expressed in the FCC's line sharing order and in this Commission's 17th Supplemental Order, is well founded. This skepticism is not assuaged by examination of the evidence presented by Qwest in this proceeding. The amounts claimed are neither forward looking economic costs nor are they known and measurable expenditures. I recommend that the Commission find at this time that it is appropriate to recover any line sharing-specific OSS transition costs from all xDSL customers who receive xDSL service over the same line used for their POTS service and

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

I recommend that the Commission defer the question of the amount of cost to be recovered until such time as convincing evidence is presented regarding the magnitude of the cost to be recovered.

Q. Qwest cites the commission's 17th supplemental order as authority for imposing a line sharing OSS charge exclusively on CLECs without assessing a similar charge against its own customers who subscribe to both pots and XDSL services using the same line. Do you believe this question was decided in that order?

A. No, I don't. The 17th Supplemental Order and the record on which it was based did not encompass line sharing, and cannot be regarded as resolving questions related to line sharing which raise different considerations than those which were pertinent to the issues addressed in the 17th Supplemental Order. In particular, the provision of xDSL service over a line also used for POTS is a new arrangement to which customers have only recently begun to subscribe. Recovery of the cost of OSS development for this new arrangement raises different issues than recovery of the cost of OSS development for the broad range of UNEs necessary to provide traditional telecommunications services.

Q. What considerations are different for recovery of OSS transition costs related to line sharing than for similar OSS costs related to other UNEs?

A. In the case of basic local exchange services, the incumbent local exchange carrier serves a broad base of captive customers, some of whom, arguably, will not receive the benefit of competition for some time into the future, and according to this reasoning shouldn't be compelled to pay for improved OSS developed to enable competition. This

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

is simply not the case for the line sharing UNE, which enables competition for a very recently introduced service which the ILECs still do not offer ubiquitously. Compelling the ILECs to offer non-discriminatory access to line sharing enables competition which immediately affords benefits to all customers using the technology - both ILEC customers and CLEC customers. Before "open" line sharing is available to CLECs, prices for ILEC xDSL offerings on shared lines are typically set to maximize profit in an environment devoid of very close competition. Availability of CLEC offerings over line sharing arrangements changes that environment and ILEC prices will promptly adjust.[13] Because all users of shared lines - both ILEC customers and CLEC customers - are buyers in the same market, they all derive immediate benefit from competition on price and on quality, all of which is enabled by improved OSS.

Beyond the difference, which arises from the nature of the ILECs' existing customer base, Qwest claims that OSS transition costs related to line sharing are caused by the existence of *separate firms* sharing the line with Qwest provided POTS, and claims that there are no such costs when Qwest uses identical technology to share a line between POTS and xDSL services when both services are provided by Qwest. I discuss this claim below, but mention it here to note that it is entirely foreign to the record on which the Commission's 17th Supplemental Order was based.

[13] *See* RC-10 "Bell Atlantic Drops Price 20% on Most Popular Infospeed DSL Plan for Consumers", News Release at http://newscenter.verizon.com/proactive/newsroom/release.vtml?id=39908. If Qwest can insulate itself from competition by imposing a line sharing charge or discriminatory OSS transition cost charge, no such price reductions will be necessary.

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

Q. You said that you would recommend that any approved OSS development costs for line sharing should be recovered from all customers who receive xDSL service and pots on the same line - not exclusively from customers of CLECs. Why do you make this recommendation?

A. As discussed above, all customers who receive POTS and xDSL service over a shared line benefit from competition enabled by the existence of improved OSS - thus, there is nothing "unfair" about recovering any approved cost of OSS development from all beneficiaries of line sharing technology. The basis for my recommendation, however, is not that it is required by fairness. Rather, I recommend that any approved cost of OSS development for line sharing be recovered from all customers served by a shared line - both ILEC and CLEC customers - because this is the recovery mechanism that is least discriminatory and serves the public interest by promoting the development of efficient competition.

Q. Please describe how it would be discriminatory and an impediment to the development of competition to recover these costs exclusively from CLECs?

A. Any policy that imposes different costs on similarly situated competitors is discriminatory and will distort the development of competition. If a charge is imposed exclusively on CLECs for OSS transition costs, that charge becomes a cost to the CLEC that is incremental to whatever increment of service the charge is assessed on - the charge may be assessed on a per line per month basis, on the basis of OSS transactions, or on some other measurable increment of service. Thus, the CLEC will invoke an additional unit of the charge whenever the pertinent increment of service occurs. The CLEC cannot

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

ignore this fact in setting prices, and is at a disadvantage for price competition precisely in the amount of the charge. For the ILEC, on the other hand, any costs associated with OSS improvement for line sharing are clearly not incremental to present activities in its retail xDSL offerings - thus, any such costs are irrelevant to the ILEC's xDSL pricing decisions. The ILEC may set its price equal to competing CLECs' costs - including the OSS transition charge - and take advantage of the insulation from price competition afforded by the charge. In the alternative, the ILEC could price below CLECs' cost - but above its own - and engage in a price squeeze. In this scenario, CLECs remain in business only at the pleasure of the ILEC; unless the ILEC is very inefficient, a significant charge will put the ILEC in a position to dominate the market.

If a charge is imposed on both the ILEC and on CLECs, the situation improves dramatically because the magnitude of the charge is calculated on projected volumes of both the ILEC and CLECs. The smaller the charge is, the smaller will be its adverse consequences. However, the charge remains discriminatory. When a CLEC pays this charge it is a real cost incremental to the CLEC's retail operations. When the ILEC pays such a charge *to itself*, it is merely rearranging funds between two pockets in the same corporate trousers - the charge doesn't represent a real cost to the ILEC's retail xDSL operations. Thus, calculating the charge on the basis of total volume - both ILEC and CLEC - is an improvement over imposing the entire cost on CLECs, but it is still discriminatory. This scenario is similar to the imposition of a line sharing charge which allows the ILEC to maintain margin that would otherwise be subject to competition, and also recover the line charge from competitors. The scenario is not as bad as imposing the

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

entire cost on CLECs because it affords the ILEC a smaller amount of insulation from price competition or it affords the opportunity to engage in a smaller price squeeze.

Q. Why do you recommend that the charge be imposed only until the commission established amount has been recovered?

A. To do otherwise would very likely lead to a windfall for Qwest - recovering more than the amount approved by the Commission. Verizon's proposal for OSS transition cost recovery in this proceeding calculates the charge that would be necessary to recover a specified amount within a certain period of time, but recognizes that the volume assumptions necessary for such a calculation are subject to great uncertainty. Verizon therefore proposes to discontinue the charge when the specified amount has been recovered. Qwest prefers to gamble that its volume assumption is lower than the volumes that will actually be realized, so imposing the proposed charge on realized volume will generate more revenue than the Commission approved amount. By comparison to publicly available projections, Qwest's volume assumptions appear calculated to make the gamble favorable to Qwest.

Q. You said that there is still reason for skepticism regarding the amount of any OSS development costs. Please explain.

A. Both this Commission and the FCC have expressed skepticism as to the magnitude of any increase in costs associated with improved OSS.[14] This skepticism is not diminished by evidence presented by Qwest in this proceeding.

[14] *Compare* 17th Supplemental Order, ¶107, *et seq.*, *with* FCC Third Report and Order, ¶94 and ¶96.

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

Q. Please discuss the evidence presented by Qwest.

A. The basis for the bulk of the amount that Qwest seeks to recover is a formal proposal for a contract issued by Telcordia. This document cannot serve as evidence of the forward looking economic cost of improved OSS or even as basis for a "known and measurable" expenditure for any purpose.

First, it should be said that the document was not available to Qwest at the time of filing direct testimony in this proceeding (19 May, 2000)[15]. At that time Qwest relied on telephone conversations which relayed the quote of 14 Million Dollars. Qwest also relied on telephone conversations with Telcordia for the determination that 85% of the 14 Million Dollars "could be attributed solely to line sharing."[16] At the time of filing testimony in this proceeding, when Qwest was relying on these telephone conversations, Telcordia's offer **USW proprietary (confidential subject to protective order).** Telcordia's offer contained a clause which provided that **USW proprietary (Confidential, subject to protective order).** Thus, Qwest's basis for the bulk of its claimed OSS transition charge for line sharing was an offer which apparently was never accepted[17] and **USW proprietary (confidential subject to protective order)**

Qwest claims no knowledge as to how the quote was prepared,[18] and still

[15] U S West response to Rhythms data request 3-8, part d, attached as Exhibit RC-11

[16] Exhibit RC-11

[17] If Qwest had accepted the offer ** Qwest proprietary (confidential-subject to protective order)** Qwest would surely have had an executed copy by the date of filing testimony on 5/19/00.

[18] Exhibit ***3-8, part c

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

apparently has nothing in writing to explain or substantiate the claim that 85% of the 14 Million Dollar total "could be attributed solely to line sharing."[19]

Q. Does Qwest provide other evidence for its claim that the great majority of its described OSS modifications are solely for the benefit of CLECs who hope to use line sharing arrangements and not for the benefit of Qwest's other operations?

A. No. The supplemental direct testimony of Barbara J. Brohl addresses this issue at a very high level of generality, particularly in the question and answer beginning on page 26, but Qwest declines to elaborate in response to Rhythms Data Request 3-8.b, which is attached as Exhibit RC-11. That request asks: "for each project or activity, please provide an explanation as to why the functionality described was not required in order to provide retail xDSL service over a shared line with its own retail basic exchange service." In response to this request Qwest merely reproduces the answer beginning at page 26 of the Supplemental Direct Testimony of Barbara J. Brohl. That answer concludes that "the complexity does not arise out of placing two different products on one line - voice and data. The complexity arises out of placing two different local service providers on one line- Qwest and the CLEC." If this assertion is accepted on its face, without the somewhat more detailed explanation requested in Rhythms Data Request 3-8.b, it only leads to additional skepticism.

Q. What additional concern is raised by Qwest's claim that OSS improvement costs for line sharing arise from the line being shared by separate companies rather than by separate services?

---

[19] *See* Exhibit RC-11

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

A. This explanation of the nature of the costs being claimed for recovery makes a strong argument for recovery of any approved costs from all customers of both POTS and xDSL services provided over a single line - without excluding Qwest data customers from the recovery mechanism. Qwest could choose to offer data services through one subsidiary and establish a separate subsidiary for local exchange carrier operations.[20] In this case Qwest's data subsidiary would be a separate company - and require the OSS improvements at issue. At this time, Qwest does not know whether it will or will not use a subsidiary separate from its local exchange carrier subsidiary to provide xDSL services over lines shared with POTS.[21] Thus, by the 'separate company' criterion, Qwest cannot know whether it will need the OSS improvements at issue to provide line shared xDSL services through a separate company.[22] In its present state of flux it clearly benefits from the option afforded by the OSS improvements to use a separate data affiliate if it so chooses. In any case, the Commission should recognize that a cost determination that hangs on the legal fiction of separate subsidiaries cannot reflect the real causation of cost. Under the mechanism proposed by Qwest the line sharing charge would differ greatly depending on whether Qwest chooses a separate subsidiary for its line shared data operations or not. The Commission should recognize that Qwest's organizational structure is not a reasonable consideration on which to base a cost recovery mechanism.

IV. SUMMARY AND CONCLUSION

[20] Bell Atlantic and SBC both use separate subsidiaries to provide data services.

[21] Response to Rhythms Data Request 4-19, attached as Exhibit RC-12

[22] It could be claimed that the affiliated separate company is different and that the OSS improvements aren't needed for such an affiliate, but this would clearly be discriminatory.

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711

Q. Please summarize your recommendations to the Commission.

A. I recommend that the Commission reject Qwest's proposal for a line sharing charge. I also recommend that the Commission should adopt the principle that any OSS transition charge for line sharing should be calculated on the basis of volumes of line shared xDSL subscribers including both the customers of Qwest and the CLECs. I recommend that any mechanism for the recovery of Commission approved OSS transition costs for Qwest should be delayed until Qwest has presented convincing evidence as to the proper amount of cost to be recovered.

Q. Does that conclude your testimony at this time?

A. Yes, it does.

ATER WYNNE LLP
LAWYERS
601 UNION STREET, SUITE 5450
SEATTLE, WASHINGTON 98101-2327
(206) 623-4711