BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

| Parties | | Docket |
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| WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION,<br>Complainant,<br>v.<br>U S WEST COMMUNICATIONS, INC.,<br>Respondent.<br>. . . . . . . . . . . . . . . . . . . . . . . | ) | DOCKET NO. UT-941464 |
| TCG SEATTLE and DIGITAL DIRECT OF SEATTLE, INC.,<br>Complainant,<br>v.<br>U S WEST COMMUNICATIONS, INC.,<br>Respondent.<br>. . . . . . . . . . . . . . . . . . . . . . . | ) | DOCKET NO. UT-941465 |
| TCG SEATTLE,<br>Complainant,<br>v.<br>GTE NORTHWEST INCORPORATED,<br>Respondent.<br>. . . . . . . . . . . . . . . . . . . . . . .<br>GTE NORTHWEST INCORPORATED,<br>Third Party Complainant,<br>v.<br>U S WEST COMMUNICATIONS, INC.<br>Third Party Respondent.<br>. . . . . . . . . . . . . . . . . . . . . . . | ) | DOCKET NO. UT-950146 |
| ELECTRIC LIGHTWAVE, INC.,<br>Complainant,<br>v.<br>GTE NORTHWEST INCORPORATED,<br>Respondent.<br>. . . . . . . . . . . . . . . . . . . . . . | ) | DOCKET NO. UT-950265 |

FOURTH SUPPLEMENTAL ORDER REJECTING
TARIFF FILINGS AND ORDERING REFILING;
GRANTING COMPLAINTS, IN PART

## SUMMARY

**PROCEEDINGS:** On November 14, 1994, in Docket No. UT-941464, U S WEST Communications, Inc. ("USWC"), filed certain tariff revisions described as integrated carrier access and interconnection designed to accommodate alternative local exchange companies, as well as those carriers that limit their service only to interexchange service. The revisions include a complete reissue and restructure of the access services tariff; the introduction of local interconnection service; the restructure of local transport service for switched access transport service, directory assistance transport service, and switched access common channel signaling access capability transport service; the introduction of expanded interconnection - collocation service in the private line transport services tariff, for all carriers; the introduction of switched access expanded interconnection service for all carriers; and the removal of intraLATA Feature Group A foreign exchange service from the Access Service tariff. The tariff revisions involve a complete restructure and replacement of the existing Access Service Tariff, WN U-25 (to be entirely replaced by a new tariff, WN U-30), and revisions to the Private Line Transport Services Tariff, WN U-22. The filing letter indicated that the total effect of the tariff revisions is revenue neutral. The stated effective date of the tariff revisions is January 1, 1995. On December 15, 1994, the Commission entered a complaint and order suspending the tariff revisions and instituting investigation.

On November 15, 1994, in Docket No. UT-941465, TCG Seattle ("TCG") and Digital Direct of Seattle, Inc. (since acquired by TCG Seattle), filed a complaint against USWC alleging undue prejudice, discrimination, and unjust rates and practices in the provision of interconnection and mutual compensation. USWC answered and counterclaimed. On February 13, 1995, the Commission consolidated Docket Nos. UT-941464 and UT-941465 for discovery and hearing.

On February 7, 1995, in Docket No. UT-950146, TCG filed a complaint against GTE Northwest Incorporated ("GTE") alleging undue prejudice, discrimination, and unjust rates and practices in the provision of interconnection and mutual compensation. GTE answered, counterclaimed against TCG, and filed a third party complaint against USWC.

On March 1, 1995, in Docket No. UT-950265, Electric Lightwave, Inc. ("ELI"), filed a complaint against GTE for undue prejudice, discrimination, and unjust rates and practices in the provision of interconnection and mutual compensation.

On March 8, 1995, the Commission consolidated Docket Nos. UT-950146 and UT-950265 with Docket Nos. UT-941464 and UT-941465.

**HEARINGS:** The Commission held hearings before Chairman Sharon L. Nelson, Commissioner Richard Hemstad, Commissioner William R. Gillis, and Administrative Law Judge Lisa A. Anderl of the Office of Administrative Hearings.

**APPEARANCES:** Respondent U S WEST Communications, Inc. ("USWC"), is represented by Edward T. Shaw, Molly K. Hastings, William O'Jile, and Douglas N. Owens, attorneys, Seattle. The Staff of the Washington Utilities and Transportation Commission ("Commission Staff") is represented by Steven W. Smith and Gregory Trautman, assistant attorneys general, Olympia. The public is represented by Donald T. Trotter, assistant attorney general, Public Counsel Section, Seattle ("Public Counsel"). Complainant/intervenor TCG Seattle ("TCG") is represented by Daniel Waggoner and Gregory J. Kopta, attorneys, Seattle. Complainant/intervenor Electric Lightwave, Inc. ("ELI"), is represented by Arthur A. Butler, attorney, Seattle, and by Ellen Deutsch, attorney, Vancouver. The following intervenors appeared: Washington Independent Telephone Association ("WITA"), represented by Richard A. Finnegan, attorney, Tacoma; AT&T, represented by Susan D. Proctor and Rick D. Bailey, attorneys, Denver, Colorado; Interexchange Access Coalition ("IAC"), represented by Brad Mutschelknaus and Edward A. Yorkgitis, Jr., attorneys, Washington, D.C.; GTE Northwest, Inc. ("GTE"), represented by Richard Potter, attorney, Everett; MCI, represented by Sue E. Weiske, attorney, Denver, and MCI/MCI Metro by Clyde H. MacIver, attorney, Seattle; Sprint, represented by Lesla Lehtonen, attorney, San Mateo, California; Tenino Telephone Company and Kalama Telephone Company, represented by Richard Snyder, attorney, Seattle; United Telephone, represented by Seth Lubin, attorney, Hood River, Oregon; MFS Intelenet of Washington, Inc., ("MFS") represented by Andrew D. Lipman, Richard M. Rindler, and Charles H.N. Kallenbach, attorneys, Washington, D.C.; TRACER, represented by Stephen J. Kennedy, attorney, Seattle; and the Department of Defense/Federal Executive Agencies ("DOD/FEA"), represented by Robert A. Ganton, attorney, Arlington, Virginia.

**COMMISSION:** USWC did not establish its proposed tariff revisions to be fair, just, reasonable, and sufficient. The Commission rejects the cost studies and tariff revisions submitted by USWC in support of its reissue and restructure of the Access Service Tariff, WN-25, and its revisions to the Private Line Transport Services Tariff, WN U-22. The Commission orders USWC to refile tariff revisions. The Commission's decisions on the tariff filing appear to resolve all issues raised in TCG's complaint. The Commission grants the complaints of TCG and ELI against GTE, in part. The local interconnection terms that GTE has offered the complainants, based on a minutes of use structure, are not fair, just, and reasonable, are anticompetitive, subject the complainants to unreasonable prejudice or disadvantage, and are discriminatory. The Commission orders GTE to interconnect with TCG and ELI on the same terms and conditions as it interconnects with USWC and other incumbent LECs, including, on a transitional basis, terminating the local traffic (including EAS) of TCG and ELI on a bill and keep basis. The Commission orders GTE to file a local interconnection tariff pursuant to the terms of this order. The Commission dismisses the counterclaims of USWC and GTE, and dismisses the third party complaint of GTE.

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# MEMORANDUM

## I. SCOPE OF PROCEEDINGS

The Commission faces many difficult issues as it attempts to facilitate the transition of the telecommunications industry from a monopoly market structure to a competitive market structure. One set of issues, before us in this proceeding, relates to the terms and conditions under which competitors for local exchange service will interconnect their networks so that they can exchange traffic between their customers.

Before discussing the issues in this proceeding, we will review some of the basic terminology involved in telecommunications, and provide a brief background on the development of local service competition.

### A. TERMINOLOGY

Exchange. The local telephone exchange is the basic unit in the structure of telephone service in Washington. The Commission defines an exchange as "a unit established by a utility for communication service in a specific geographic area, which unit usually embraces a city, town or community and its environs. It usually consists of one or more central offices together with the associated plant used in furnishing communication service to the general public within that area." WAC 480-120-021. The exchange originated in the early development of telephone service, when it constituted the area served by a single telephone company central office, where the manual switchboard, attended by an operator, was housed.

Local Exchange Company ("LEC"). Each exchange historically has been served by a single local exchange company (LEC). USWC and GTE are the largest LECs in Washington. A LEC provides local calling service (calls that originate and terminate within a local service area) and a range of other telecommunications services.

Flat-rated Local Service. The rates for basic local exchange service in this state are set on a flat-rate pricing system; extended area service rate additives may include both a flat-rate and a measured rate component option. The Washington Legislature has declared that "[t]he implementation of mandatory local measured telecommunications service is a major policy change in available telecommunications service." RCW 80.04.130 The Commission is prohibited from accepting or approving a tariff filing which imposes mandatory local measured service on any customer or class of customers prior to June 1, 1998, except for EAS or foreign exchange service.

Interexchange Carriers ("IXCs"); Access Charges. Service between exchanges ("interexchange service") is provided by LECs (to a limited extent)[1], and by companies that

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[1] When the American Telephone and Telegraph Company (AT&T) was broken up in the

exclusively provide interexchange service, such as AT&T, MCI, and Sprint.[2] Any company providing interexchange service is an "interexchange carrier" or "IXC", although that term generally has been used to refer only to long distance companies that have been exclusively interexchange service providers. An interexchange call generally is a "toll" call, for which the customer originating the call may be charged a distance and/or time sensitive rate.

When a call between two exchanges (an "interexchange call") involves more than one telecommunications company, the IXC that carries the call generally compensates the LEC for providing the local link(s) to the end user(s). LECs provide a tariffed "access service" for the local link. For example, if AT&T is carrying a call that originates in a GTE-NW exchange and terminates in a USWC exchange, AT&T will be assessed access charges for both the originating and the terminating local links. Access charges historically have been a very large portion of an IXC's total cost of doing business.

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early 1980s, the provision of cross-country long distance service was separated from the provision of local service. By the terms of the court order, the "Baby Bells" that were assigned local service were restricted to providing intraexchange service and interexchange service within a Local Access and Transport Area (LATA), which is a geographic area consisting of many exchanges. This Commission authorized USWC to provide interexchange, intraLATA service statewide, and more recently authorized GTE to provide such service in most of western Washington. Exclusively interexchange companies ("IXCs"), such as AT&T, MCI, and Sprint, provide service between LATAs, and also are allowed to compete in providing intraLATA, interexchange service.

[2] Even this distinction is now blurring as AT&T has undertaken provision of local service as a cellular provider; MCI has formed "MCI Metro," which has been authorized to provide basic local exchange service in this state; and Sprint has entered into partnership arrangements to pursue local telephony with cable television providers.

Extended Area Service ("EAS"). Some interexchange calls are not toll calls for the originating customer. The Commission, pursuant to procedures set out in RCW 80.36.855 and WAC 480-120-400, has designated certain clusters of adjoining exchanges for which there is a high volume of interexchange traffic as extended area service (EAS) territories for which interexchange calling is toll-free to the caller. EAS thus is an enlarged local calling area. For most customers with EAS, an "EAS additive" is rolled into their monthly rate for basic local service, to compensate the LEC for the toll revenue it lost when the Commission ordered EAS for the territory.

Some EAS territories involve more than one LEC. For most EAS areas, incumbent LECs have agreed not to charge one another access charges for completing EAS traffic. Instead, they have exchanged EAS traffic on a bill and keep basis. Each LEC bills its own customers the EAS additive and keeps the revenue rather than sharing it with the other companies involved. Commission rules now require that intercompany EAS be on a bill and keep basis.

Central Office; End Office; Customer Loop; Tandem Switch. See "Exchange," above. Telephone company switching offices continue to be referred to as "central offices" (or as "wire centers"). A single exchange may have numerous central offices, depending on the number of customers served. A central office also is referred to by other terms that reflect its various functions. A central office that is the first switching point in the network from the end user's perspective commonly is referred to as an "end office." Usually, each customer is connected to the end office switch by means of a twisted pair of copper wires, called the "customer loop".

End offices are connected to one another by trunk lines and/or via a tandem switch. A tandem switch is the largest aggregation point in the network, a switching facility that interconnects trunk lines from the LEC's end offices and lines from other telecommunications companies. A tandem thus is an intermediate switch between the originating call location and the final location. Utilizing a tandem eliminates the need to directly connect all end offices to one another.

Point of Presence; Meet Points. IXCs and incumbent LECs that share EAS territories have interconnected with one another for years. IXCs generally interconnect with the LEC's network at a "point of presence", usually the IXC's central office location.

Incumbent LECs generally interconnect with one another at mutually agreed upon "meet points," such as a manhole on the boundary between their service territories, using relatively simple methods such as the splicing together of trunks.

Alternative Local Exchange Companies ("ALECs"). New competitors of historical LECs in the local exchange service market, as described in the background below, are called by various names. In addition to "ALECs," they are referred to as "alternative exchange carriers" ("AECs"), "competitive local exchange companies" ("CLECs"), and "new LECs."

## B. BACKGROUND

In 1985, the Washington Legislature declared it the policy of the state to "promote diversity in the supply of telecommunications services and products in telecommunications markets throughout the state." RCW 80.36.300. However, until 1993, a divided Commission interpreted its statutes as providing for quasi-exclusive local service territories. A Superior Court decision in November 1992[3] caused the Commission majority to change its interpretation of the statutes, and to begin authorizing competition in the local exchanges. The Supreme Court of Washington affirmed the Superior Court's judgment, in In re Electric Lightwave, Inc., 123 Wn.2d 530, 869 P.2d 1045 (1994), as amended on denial of reconsideration. In that decision, the Supreme Court stated:

> RCW 80.36.300(5) notes it is the state's policy to "[p]romote diversity in the supply of telecommunications services and products in telecommunications markets through out the state." Recognizing an implicit authority to grant monopolies would frustrate the express legislative goal of assuring diversity. 123 Wn.2d at 538-539

Several telecommunications companies, including ELI and TCG, have begun to construct local networks and to provide local exchange service, on a limited basis, in competition with incumbent LECs. Three other companies also have been granted authority to provide competitive local exchange service. In this order, these new local service competitors will be referred to as "alternative local exchange companies" or "ALECs."

In order to provide complete local exchange service, the ALECs must be able to interconnect their networks with those of the incumbent LECs. Establishing the terms of interconnection of competing local switched networks is the principal focus of this proceeding. This proceeding involves several complex issues, including the physical terms of interconnection; compensation for terminating traffic that originates on a competitor's network; the possible "unbundling" of services; number portability; use of existing directory assistance databases; unified white pages directory listings; the pricing of services and unbundled network components; and other issues.

USWC, in its tariff filing, and GTE have proposed local interconnection mechanisms that are modeled on mechanisms established during the 1980s for interconnecting with IXCs. Whether these mechanisms are appropriate for local interconnection, whether the incumbent LECs' specific proposals adequately address the state's policy goals, and whether there are alternatives that are more appropriate in terms of meeting the state's telecommunications policies, are matters to be determined in this proceeding.

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[3] On November 13, 1992, the Superior Court of the State of Washington for King County entered a decision which reversed a Commission decision that LECs had quasi-exclusive rights to provide service in an exchange area under RCW 80.36.230.

## C. OVERVIEW OF USWC'S TARIFF FILING

USWC proposes that both the physical and compensation terms of local interconnection be modeled on its access tariff for IXCs. The tariff filing proposes a restructure of access service for IXCs by bringing that service into conformity with an FCC-ordered restructure of the local transport component of interstate switched access service.[4] At the same time, it would bring the ALECs into the access charge structure, creating a unified access structure for both groups of carriers.

USWC currently assesses IXCs time and distance-sensitive charges for providing the originating or terminating leg of a long distance call. The access charge has several rate elements, including charges for local switching (switching at the end office); local transport (a charge for use of trunk lines that connect USWC's central offices, including transport via its tandem switch); a carrier common line charge as a contribution to the cost of the wire loop that connects to the customer's premises; and a universal service fund charge.

USWC refers to its proposed restructure of IXC switched access service as the "local transport restructure" ("LTR"). In the tariff revisions, the current charge for "transport" would be "unbundled" from the access charge, and transport would be split into several elements which would be individually priced and offered. The unbundling of transport would make use of USWC's transport service optional: an IXC could bypass USWC's transport facilities by providing its own transport to USWC switches or obtaining transport trunks from third parties. USWC would make available alternative transport options either through direct trunked transport or tandem switched transport. The remaining access charges would be modified to increase the switching charge from $0.0065/minute to $0.01/minute, and, in order to make the filing revenue neutral, add a temporary rate element that USWC calls a "residual interconnection charge ("RIC"). The new LTR access charges would apply to all toll traffic, including long distance traffic delivered by ALECs.

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[4] See, CC Docket No. 91-213.

For local interconnection, USWC's tariff filing creates a new "local interconnection service ("LIS") section of its Access Services tariff. The LIS incorporates the transport options and switching charge from the restructured switched access tariff,[5] and creates a new access rate element for local interconnection called an "interim universal service charge" ("I-USC"). The I-USC is applicable to LIS customers that market mostly to business customers and high density service areas. The I-USC would be in the same amount as the carrier common line charge, $0.0228/local switching minute. Thus, for local traffic that it delivers to USWC for termination, an ALEC would be assessed a local switching charge of $0.01/minute, an interim universal service charge (I-USC) of $0.0228/minute, and transport charges for transport services used.

USWC contends that the I-USC is necessary as a *contribution* to USWC for bearing the burden of providing "universal service" (ubiquitous service with affordable residential rates).

The LIS would require the establishment of a formal tracking, measurement, and billing mechanism for local call termination.

As part of its tariff filing, USWC proposes an expanded interconnection service for companies that wish to avoid USWC transport charges by providing their own transport to USWC end office or tandem switches. The FCC has ordered expanded interconnection for IXCs. Expanded interconnection would allow interconnection at USWC tandem and local switches. It would use a co-location ("collocation") arrangement whereby companies interconnect with USWC's network on USWC's premises, with USWC providing space for the interconnector to locate its terminating equipment. USWC's tariff specifies facilities that the interconnector must use, and specifies a number of charges for the service. Expanded interconnection would be offered to ALECs as well as IXCs.

USWC has rejected the ALECs' requests to interconnect with USWC's network at any convenient "meet point," or in the same manner it interconnects with incumbent LECs for the exchange of EAS traffic. USWC would permit an ALEC to interconnect only inside or just outside the ALEC's central office, using a USWC entrance facility, or just outside a USWC central office, via virtual collocation.

USWC proposes to offer several services that would make it easier for USWC's customers and the ALECs' customers to reach one another. These other services include white pages directory listing; directory assistance services; use of USWC's line identification data base (LIDB) which facilitates billing for third-party, collect, and calling card calls; a channel to the customer's premises; and interim solutions to number portability while permanent solutions are being developed. For the most part, these services would be provided through USWC's existing tariffs at already established rates.

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[5] The LIS does not incorporate the common carrier line charge or the RIC from the LTR.

## D. THE COMPLAINTS

The complaints by ELI and TCG allege generally that USWC and GTE refuse to enter into interconnection and mutual compensation arrangements with complainants that are equivalent to the arrangements the incumbents have made with other LECs for the exchange of local/EAS traffic. Further, the incumbents propose to charge the complainants for interconnection at rates well in excess of rates they charge their own customers for comparable local exchange services, thereby subjecting the complainants to unreasonable prejudice, discrimination, and disadvantage. The complaints also allege that the incumbents' proposed charges for network interconnection are unfair, unjust, unreasonable, and anticompetitive. They ask the Commission for orders pursuant to RCW 80.36.140 and 80.36.160 requiring the incumbents to interconnect their networks with the complainants' networks, establishing a fair, just, reasonable, and nondiscriminatory reciprocal compensation arrangement for that interconnection, and requiring the incumbents to provide 9-1-1, directory listings and assistance, and other vital customer services upon interconnection at fair, just, and reasonable rates. The complaints are described in greater detail in section II.G. of this order.

GTE also has brought a third party complaint against USWC, claiming that USWC is handing off to GTE, for termination, traffic that originated on TCG's network that GTE is entitled to be compensated for terminating, without identifying the traffic so that GTE can bill for it. The reference is to traffic that would be EAS traffic if it originated on USWC's network.

## E. OVERVIEW OF POSITIONS OF PARTIES

With respect to local interconnection, the parties generally split into two groups. All parties except the incumbent LECs generally oppose USWC's tariff proposals and GTE's proposed rates as requiring unnecessary and inefficient architecture, as unproven, as unfair and unreasonable, as discriminatory, and as anticompetitive.

With regard to compensation for terminating an ALEC's traffic, the opponents of USWC's proposal are particularly critical of the proposed I-USC. All urge the Commission to defer consideration of universal service to another proceeding.

All of these parties, except one (AT&T), oppose the compensation mechanism the incumbents propose for the mutual termination of local traffic -- measured usage rates. They, as well as AT&T, argue that the appropriate compensation arrangement for the mutual termination of local traffic between competing LECs, at least until barriers to competition are removed, is "mutual traffic exchange" known as "bill and keep," the compensation arrangement that the incumbent LECs presently utilize for the exchange of EAS traffic. The complaints, in fact, allege that it is discriminatory for the incumbents to adopt any other compensation mechanism while they have a bill and keep arrangement among themselves.

The ALECs argue that USWC's proposal to restrict physical interconnection to three points and via specified facilities is unreasonable and anticompetitive, and urge the Commission to order USWC to allow them to physically interconnect with USWC's network at meet points similar to those established between incumbent LECs.

They also argue that competition will develop more quickly if they are able to purchase and resell unbundled parts of the incumbents' networks, although they differ over the degree of unbundling that is necessary. These parties agree that at a minimum they should be able to lease the customer loop (the link between a customer's residence or place of business and the end office switch) from an incumbent LEC for resale to end users, so that the competitors can provide service without the need to duplicate the loop to every end user's premises. They contend that the Commission must establish other terms of interconnection that are necessary to effective competition.

Allied on the other side are the incumbent LECs -- USWC, GTE, and the Washington Independent Telephone Association (WITA). They generally take the position that the Commission's authority with respect to interconnection is limited to ordering the incumbents to interconnect, and regulating the fairness and sufficiency of the rates for the interconnection services the incumbents choose to offer. They contend that bill and keep, additional physical interconnection options, greater unbundling than the LECs are willing to offer, and other solutions proposed by the other parties are beyond the Commission's authority to order and that ordering them would constitute confiscation of the incumbent LECs' property. They contend that very few of the services and facilities their opponents request are necessary for effective competition, and that their competitors are asking the Commission for competitive assistance and advantage. USWC opposes deferral of the universal service question on policy and legal grounds, and the other incumbents support its contention that it is entitled to an I-USC element in its access charge. WITA contends that unbundling may not be cost effective for small LECs.

Responding to the complaints, USWC contends that the complaints raise no issues not also raised in USWC's direct case and presented by USWC for resolution, and should be dismissed as moot. GTE contends that the complaints against it must be dismissed because the complainants have not stated actionable claims or proven their case, and contends that because the complaints must be dismissed, the Commission cannot enter an order regarding GTE's rates in this proceeding.

GTE contends that several issues in USWC's tariff proceeding, including unbundling, universal service, and collocation, were not raised in the complaints against GTE, and that the Commission cannot enter any order with respect to GTE on such issues.

With respect to the LTR, the IXCs, which are particularly dependent on incumbent LEC transport and switching for the local leg of long distance calls, support the LTR's separation of transport from other elements of access service, and support the component elements of transport that USWC has identified, but strongly oppose the LTR's proposed pricing of the transport

elements, the proposed increase in local switching charge, and proposed residual interconnection charge (RIC).

The IXCs that are parties -- AT&T, MCI, Sprint, and IAC -- take the common position, via a stipulation, that revisions to the switched access tariff (i.e., the LTR) should be resolved in another proceeding that currently is pending before the Commission: the USWC general rate case (Docket No. UT-950200).

In addition to the ALEC objections to USWC's requirement that interconnection at USWC end offices may be only via USWC's virtual collocation service, several parties raise concerns about the charges USWC proposes to impose for virtual expanded interconnection services, and USWC's proposal to price other elements of ALECs' charges on an Individual Cases Basis ("ICB").

A number of parties analyze the cost studies on which USWC bases its rate proposals, and are highly critical of them. They contend that the studies use improper measures of economic cost, are unnecessarily cryptic, contain strategically differentiated markups over cost, and are accompanied by insufficient documentation to enable them to conduct a fair review of the company's costs. All parties except the incumbent LECs are critical of USWC's proposed prices for both competitive and monopoly services.

## F. COMMISSION'S JURISDICTION

USWC takes an extremely legalistic approach in support of its tariff proposals and in opposition to the proposals of the ALECs and IXCs. Essentially, it contends that the Commission's authority is limited to ordering interconnection between incumbent LECs and other wireline carriers,[6] and reviewing for fairness and sufficiency the rates for the interconnection services it offers.

USWC makes a detailed analysis of the Commission's statutes. It argues, based on its analysis, that:

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[6] None of the LECs deny that they must interconnect with local exchange service competitors for the exchange of traffic. USWC notes that Const. art. 12, § 19 requires it to interconnect. WITA notes that 80.36.350 empowers the Commission to authorize the entry of new companies, and that once operating, 80.36.200 provides that a new company's messages must be received, transmitted, and delivered by other telecommunications companies without discrimination or delay.

(1) The Commission must approve access or interconnection charges (as in the current interexchange model) for local interconnection. Commission statutes do not allow the prescription of no rates, or bill and keep. Commission statutes all contemplate that remunerative rates will be charged.

(2) Although incumbent LECs exchange EAS traffic on a bill and keep basis, the Commission has no authority to require companies to provide intercompany EAS on a bill and keep basis.

(3) Given the state's telecommunications policies, the Commission has no choice but to approve an access charge structure for local interconnection with a universal service charge element. Failure to approve USWC's proposed I-USC would either undermine affordable universal service, which is the state's paramount public policy under RCW 80.36.300, or would illegally deprive USWC of the ability to cover its authorized revenue requirement.

(4) The Commission only has authority to order a company to provide telecommunications services to another. It has no authority to order a company to provide bare facilities, such as loops or subparts of loops. It cannot order unbundling.

(5) The Commission's jurisdiction to regulate in terms of competitive fairness applies only to rates for telecommunications services. It does not provide authority to order charges for or access to bare facilities, real estate, or non-telecommunications products or services such as telephone directories.

The other incumbent LECs (GTE and WITA) make many of the same arguments.

The Commission is mindful that it is a creature of the Legislature without inherent or common-law powers, and that it may exercise only those powers conferred on it either expressly or by necessary implication. Cole v. Wn. Util. & Transp. Comm'n, 79 Wn. 2d 302, 306, 485 P.2d 71 (1971).

The Commission believes that the telecommunications industry itself should assume primary responsibility for reaching consensus on reasonable solutions to many of the local interconnection issues. However, we realize that the industry necessarily and appropriately looks to the Commission to provide some leadership and direction during the transition to a competitive industry structure. If members of the industry fail to reach agreement necessary to resolve these critical issues, the Commission is prepared to take a more directive role as needed to establish terms for fair interconnection among competing providers of local exchange services.

The Commission has carefully and thoroughly considered the incumbent LECs' arguments that we lack authority to order any interconnection terms or conditions other than those they are offering. We believe that the incumbent LECs' interpretation of the Commission's authority, and USWC's interpretation in particular, are unreasonably restrictive. The Commission has broad authority to regulate the rates, services, facilities, and practices of

telecommunications companies in the public interest. See, POWER v. Utilities & Transp. Comm'n, 104 Wn.2d 798, 808, 711 P.2d 319 (1985); State ex rel. American Telechronometer Co. v. Baker, 164 Wash. 483, 491-96, 2 P.2d 1099 (1931); State ex rel. Public Service Commission v. Skagit River Telephone & Telegraph Co., 85 Wash. 29, 36, 147 P. 885 (1915).

Under RCW 80.01.040(3), the Commission is authorized to regulate in the public interest the rates, services, facilities, and practices of public utilities, including telecommunications companies.

RCW 80.36.080 gives the Commission broad power to regulate the rates, tolls, contracts and charges, rules, and regulations of telecommunications companies for services rendered and equipment and facilities supplied, as to fairness, justness, reasonableness, and sufficiency.

RCW 80.36.140 gives the Commission broad authority over rates and over rules and practices affecting rates, and broad authority over practices, facilities, and services:

> Whenever the commission shall find, after a hearing had upon its own motion or upon complaint, that the rates, charges, tolls or rentals demanded, exacted, charged or collected by any telecommunications company for the transmission of messages by telecommunications, or for the rental or use of any telecommunications line, instrument, wire, appliance, apparatus or device or any telecommunications receiver, transmitter, instrument, wire, cable, apparatus, conduit, machine, appliance or device, or any telecommunications extension or extension system, or that the rules, regulations or practices of any telecommunications company affecting such rates, charges, tolls, rentals or service are unjust, unreasonable, unjustly discriminatory or unduly preferential, or in anywise in violation of law, or that such rates, charges, tolls or rentals are insufficient to yield reasonable compensation for the service rendered, the commission shall determine the just and reasonable rates, charges, tolls or rentals to be thereafter observed and in force, and fix the same by order as provided in this title.
>
> Whenever the commission shall find, after such hearing that the rules, regulations or practices of any telecommunications company are unjust or unreasonable, or that the equipment, facilities or service of any telecommunications company is inadequate, inefficient, improper or insufficient, the commission shall determine the just, reasonable, proper, adequate and efficient rules, regulations, practices, equipment, facilities and service to be thereafter installed, observed and used, and fix the same by order or rule as provided in this title.

Under RCW 80.04.110, the Commission may consider complaints by one competitor against another alleging that the rates, charges, rules, regulations, or practices of the other are unreasonable, unremunerative, discriminatory, illegal, unfair, or intending or tending to oppress

the complainant, to stifle competition, or to create or encourage the creation of monopoly, and to correct abuses complained of by establishing uniform rates, charges, rules, regulations, or practices in lieu of those complained of.

RCW 80.36.160 gives the Commission authority to order physical connections, prescribe routing, and establish joint rates for toll telephone service.

Finally, the Commission has broad powers to protect consumers and competitors from unreasonable preference, advantage, or discrimination under RCW 80.36.170, .180, and .186.

Our analyses of the incumbent LECs' specific legal arguments concerning bill and keep, EAS, unbundling, and making available other services and facilities, are set out later, in appropriate sections of this decision. We have concluded that the Commission's authority is sufficiently broad for it to order compensation arrangements (including "bill and keep") and other terms and conditions for local interconnection that differ from those the incumbents propose. In deciding which arrangements, terms, and conditions to approve and order, the Commission will endeavor to identify solutions that are consistent with the state's telecommunications policies and otherwise in the public interest.

## II. LOCAL INTERCONNECTION

### A. POLICY

The Commission requested that the parties address policy considerations in their testimony and in their briefs. We appreciate the considerable thought and effort the parties put into their discussions.

USWC's policy discussion is largely restricted to its various legal challenges to the Commission's authority to do anything more than review the fairness and remunerativeness of the rates it proposes, summarized in the previous section. USWC's view would permit the Commission virtually no policy role.

The incumbent LECs suggest that the Commission take care not to promote competition solely for the sake of competition. Competition already is developing rapidly on its own, they argue, and many of the measures that the new entrant ALECs seek in this proceeding are unnecessary and would distort competition. The incumbent LECs argue that the ALECs should not be allowed to use the Commission's regulatory authority to gain an unfair advantage in their competition with them.

USWC argues that the Legislature has declared preservation of affordable universal telecommunications service to be the paramount public policy. Other objectives, such as promoting diversity of supply in telecommunications services, are subservient to universal service. USWC maintains that the Commission cannot promote local exchange competition at the expense of affordable universal service and the right of regulated companies to reasonable and sufficient rates for services rendered.

GTE argues that the Commission's overall policy should be to allow the fair and natural development of competition under symmetrical regulatory rules. It should not attempt to create "pseudo-competition," and it should not mandate that some firms aid and provide an advantage to their competitors. GTE argues for interconnection rates that are consistent with sound economic principles and facilitate movement toward an integrated, unified rate structure for all traffic between carriers, be they incumbent LECs, ALECs, or interexchange carriers.

WITA's position stresses the need to avoid delay in defining standards for local exchange competition, because the development of competition in this market is already explosive. According to WITA, the Commission should recognize the conditions claimed by ALECs as requirements for competition as mere illusion, designed to gain a competitive advantage. WITA argues that each new entrant could, if it so chooses, completely duplicate the existing network of the incumbents or use existing wireless or cable infrastructure.

Other parties in this proceeding generally argue that the paramount policy of the Commission should be to permit and encourage the development of effective competition in the local exchange market. Commission policy should support arrangements that are consistent with competitive markets and that promote the development of efficient, low-cost services for consumers. Competition, they argue, promotes the public policies declared by the Legislature in RCW 80.36.300, such as universal service and diversity of supply.

The other parties offer recommended sets of policies that differ in scope and detail but generally resemble each other in comparison to the incumbent LEC positions. For example, Commission Staff offers a series of principles and objectives intended to move toward a long term goal of establishing the marketplace as the regulator of local rates and services. These include policies to promote effective competition, treat all market participants as "co-carriers," require that dominant incumbents make available to ALECs non-competitive services at non-discriminatory, cost-based, unbundled rates, recognize the lack of "effective competition" in defining "essential services," require that prices for basic network functions be cost-based without contribution to the profits of the incumbent, and use total service long run incremental costs (TSLRIC) as the cost basis for pricing decisions.

The Commission concludes that the decisions in this case must be guided primarily by the specific public policies declared by the Legislature in RCW 80.36.300:

(1) Preserve affordable universal telecommunications service;

(2) Maintain and advance the efficiency and supply of telecommunications service;
(3) Ensure that customers pay only reasonable charges for telecommunications service;
(4) Ensure that rates for noncompetitive telecommunications services do not subsidize the competitive ventures of regulated telecommunications companies;
(5) Promote diversity in the supply of telecommunications services and products in telecommunications markets throughout the state; and
(6) Permit flexible regulation of competitive telecommunications companies and services.

These legislative policies are, in turn, guided by provisions of the state constitution that protect the rights of all companies to provide telecommunications services (Const. art. 12, § 19) and declare the state's abhorrence of monopolies (Const. art. 12, § 22). See, In re Electric Lightwave, Inc., supra, 123 Wn.2d at 538-39.

The policy goals of preserving universal service and promoting competitive markets are not at odds. Competition can make telecommunications services more affordable by encouraging firms to be more efficient and more innovative. It also can promote affordable service by imposing "market discipline" on the prices of incumbent LECs in other words, the prospect of competition can encourage incumbents to hold down rates.

As the Commission moves forward in establishing the conditions for competition (as presented to us in this docket), we must be vigilant in regards to consumer protection and universal service goals. To this end, the Commission concurs with the principles advocated by Public Counsel, at pages 3-4 of its brief:

> The first policy is that the Commission should guarantee that the benefits of competition -- including lower rates, more and better service options, and more rapid deployment of technological advances -- flow to all customers, not just large business customers.
>
> The second, and corollary policy is that the Commission assure that residential and small business customers do not become the "guarantors" of US WEST's revenue stream at a time when competitive pressures would otherwise force the Company to become more efficient to maintain its levels of profitability.
>
> The third policy is that new entrants be recognized as co-carriers and treated accordingly. The Commission should dismantle any remaining barriers to entry and avoid constructing (or authorizing incumbents to construct) any new barriers through decisions on interconnection issues.

The Commission adds the additional principle that rates and conditions should reflect costs. The Commission continues to be mindful of the statutory requirement that rates be fair,

just, reasonable and sufficient. It would not be in the public interest to allow rates which do not meet this test.

## B. COMPENSATION

### 1. Introduction

The crux of this case deals with inter-company compensation for the termination of local calls. Little would be gained from granting new firms the opportunity to interconnect with the existing network but allowing the incumbents to charge excessive rates for that access. Yet it also would not be in the public interest to establish a compensation mechanism that failed to compensate companies for the use of their facilities, that allowed new entrants to impose excessive costs on incumbents' networks, or that created incentives for uneconomic investment.

In evaluating alternative compensation mechanisms we have sought to maintain a balance between the objective of promoting diversity in the supply of telecommunications services and the responsibility to ensure that companies are fairly compensated for their services. It is not the Commission's responsibility to protect incumbents from competition; indeed, it is our responsibility to ensure that new entrants have a reasonable opportunity to compete. We emphasize our agreement with the incumbent LECs that we should not encourage competition merely for the sake of competition. We seek to ensure the development of effectively competitive markets in order to satisfy consumer demand and promote economic efficiency.

### 2. Options Presented

The parties have put forward three different approaches for compensating local service providers for terminating a competitor's local calls: (1) a variable charge based on minutes of use of the terminating company's transport and switching network; (2) compensation in the form of mutual traffic exchange, or "bill and keep"; and (3) a port charge based on peak use of interconnection capacity.

USWC in its tariff filing and GTE in the rates it has offered to the complainants, take a common approach of a per-minute charge mechanism. This proposed compensation mechanism is an access charge structure modeled on the one adopted in the 1980s for interconnection with IXCs.

Mutual traffic exchange, or bill and keep, is the preferred alternative of nearly all the other parties, at least as an interim approach until barriers to competition are removed. Bill and keep is a compensation mechanism in which each local exchange company would pay for the calls it terminates on other companies' networks by, in return, terminating those other companies' calls on its own network.[7]

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[7] TCG favors bill and keep for end office interconnection only; it proposes that interconnection at tandem switches be compensated with port charges.

The flat-rated port charge was proposed by several parties as an alternative to per-minute charges, should the Commission reject a bill and keep mechanism.

**a. Per-minute charge**

In the tariff revisions filed in this proceeding, USWC proposes to charge essentially the same unbundled rates for transporting and terminating calls from local competitors as it would charge IXCs for switched access (long-distance) transport and call termination. The local interconnection service (LIS) section of USWC's Access Services tariff would incorporate transport rates and a switching rate element from the company's restructured switched access tariff for IXCs, and would add an interim universal service charge (I-USC) rate element.

For local traffic that an ALEC delivers to USWC for termination, USWC would assess the ALEC transport charges for USWC transport services the termination requires, a local switching charge of $0.01/minute for use of the end office switch, and an I-USC of $0.0228/minute applicable to ALECs that do not meet a set of requirements that includes serving the same ratio of residence to business customers as USWC. USWC proposes the I-USC as a contribution to the support of USWC's statewide averaged residential rates.

USWC's LIS would require that local traffic be measured. USWC presently is not capable of measuring terminating local traffic, but is developing new technology that can generate the necessary call records for such measurement. It proposes interim measurement arrangements whereby each local exchange company would measure the traffic it delivers to another, and the receiving company would rely on those measurements to bill its terminating access charges. USWC presently bases IXC access charges on a delivered-traffic reporting system similar to the interim system it proposes for ALECs.

USWC proposes that local interconnection access charges be reciprocal. The ALECs could charge USWC access charges for traffic that USWC delivers to them for termination to ALEC customers based on the ALECs' access tariffs or price lists. An exception to this position is USWC's proposed I-USC. It would be strictly a one-way charge.

GTE has proposed usage-based mutual compensation for terminating ALECs' "local-like" and "EAS-like" traffic based upon GTE's switched access tariff rates, except for the common carrier line charge and the information surcharge elements.[8] Its proposed contract rate for local termination is $0.0295291 per minute, which is derived from its switched access tariff. In cross-

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[8] GTE does not have a tariff for local interconnection service, either existing or proposed. GTE is a party in this proceeding because of complaints filed against it by TCG and ELI. In negotiations with GTE, TCG and ELI requested that GTE interconnect with them on the same basis it interconnects with incumbent LECs for the exchange of EAS traffic, including employing a bill and keep method of mutual compensation for the exchange of local traffic. GTE refused that request.

examination, GTE witness Beauvais recommended that the Commission should direct GTE to impose rates for inter-company compensation at a level similar to what is paid currently for local measured service, approximately $0.01 to $0.015/minute. [Beauvais, TR., pp. 1789 and 1802] GTE has not proposed to unbundle transportation from its access charge.

There were several basic issues cited by parties in their support for or opposition to a measured use structure. The major issues were whether: (1) the local access rate structure should be consistent with the existing toll access rate structure; (2) a per-minute charge would send correct economic signals to actual and potential participants in the market; and (3) measured use rates would impose unnecessary costs on market participants.[9]

(1) Consistency of local and toll access rate structures.

USWC argues that there is no basis for having a different compensation mechanism for local traffic than the one already in place for interexchange traffic. Local interconnection is no different technically and conceptually from any other kind of interconnection. GTE concurs in this argument, contending that differentiation of traffic "types" will succumb to the proliferation of technologies, service providers, and service packages. A common rate structure would obviate the need to use separate trunking or specialized measuring and billing systems, provide equal treatment to all originating companies, and eliminate the incentive to arbitrage any difference between different rates. In addition, WITA argues that measured use rates for local interconnection build on existing models and are easy and efficient to administer.

In opposition, Public Counsel argues that the historical existence of such a structure for toll access does not make it an appropriate model for local access. DOD/FEA notes that the idea of consistency is superficially attractive but contends that the relationship between an incumbent LEC and a toll carrier is altogether different than the relationship between two incumbent LECs or between an incumbent LEC and a new entrant ALEC.

(2) Economic signals to market participants.

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[9] The parties also disagree about the amount that would be charged per minute for call termination. USWC contends that interconnection rates should be set above incremental cost to provide a contribution to the common costs of the existing network. Several other parties argue that rates should be set at incremental cost to promote competition. Markups on services provided to competitors would allow the incumbent to block meaningful competition, they argue.

GTE argues that measured use rates for local and EAS traffic send appropriate economic signals to the market. Local exchange companies incur costs to terminate each other's traffic, and this cost should be reflected in rates. The per-minute rate is superior to bill and keep, GTE argues, because bill and keep sends an incorrect economic signal that traffic termination has no cost. USWC also argues that per-minute measured use rates are warranted by the need to send accurate price signals. WITA contends that access-like charges will ensure entry on an economically sound basis and allow rural LECs an opportunity to recover network costs for serving all of the rural service area.

ELI argues that interconnection costs are not sensitive to the number of minutes used but rather are a function of the potential demand for peak network capacity. (Montgomery, Ex. T-84, pp. 47-48)

Public Counsel contends that a measured rate structure has the potential to place irresistible pressure toward provision of retail service on a measured basis. It cites the testimony of GTE witness Beauvais, that "if compensation costs are on a minute of use or per call basis, it is desirable that the end user see a rate structure reflecting those cost characteristics..." (Ex. T-130, p. 12) MCI argues that adopting a per-minute charge, even at cost, would result in a cost floor for local exchange services much higher than the floor that would apply under mutual traffic exchange.

GTE does not accept that usage based charges would result in mandatory local measured service. GTE does not have the goal of imposing mandatory measured service, and its proposed integrated rate structure would accommodate flat rate service offerings. GTE argues that such concerns should not distract from the real issues of sound economic, forward-looking prices. [Beauvais, TR., p. 1786]

(3) <u>Imposition of unnecessary costs with a per-minute structure.</u>

Finally, the parties disagree on whether the proposed rate structure would unnecessarily raise costs for various firms, either by creating measurement and billing costs or by distorting choices in network architecture and technology. USWC contends that the investment necessary to measure terminating traffic is necessary for companies to manage their networks in a competitive manner and that the additional cost of local measurement capability for companies who already must measure toll traffic is modest and incremental. GTE argues that any factual basis for the claim that measuring costs are high are based only on USWC's costs, citing evidence that it can and is measuring and billing for terminating traffic using existing capabilities at a low cost. WITA suggests that costs could be very low if companies used the Data Distribution Center to exchange billing system records.

Many opponents of USWC's proposed rate structure cite measurement costs as a disadvantage of that proposal. TRACER presented testimony that USWC's assumed costs for measuring, billing, and collecting would account for almost half the costs for terminating local

calls. (Zepp, Ex. T-151, 22-23) The technology used to measure local traffic is three times as costly as that used to measure IXC traffic. (Wilson, Ex. T-154, p. 32) Measurement costs will be wasted if traffic is in balance, TCG argues, and even if the traffic is out of balance, the total cost of measurement must be justified by the amount of the imbalance. Sprint, ELI, MCI, and Public Counsel argue that requiring new entrants to adopt technologies that permit measurement of terminating minutes would distort technology and architecture choices and raise entry costs.

**b. <u>Mutual traffic exchange</u>**

Mutual traffic exchange, also known as "bill and keep," is the compensation mechanism supported by most parties other than the incumbent local exchange companies. Under this mechanism, traffic is exchanged among companies on a reciprocal basis. Each company terminates the traffic originating from other companies in exchange for the right to terminate its traffic on that company's network.

Proponents focus primarily on the reciprocal nature of mutual traffic exchange and the "co-carrier" treatment it affords incumbent LECs and new entrant ALECs. Commission Staff argues that it is appropriate to treat ALECs as co-carriers of local traffic, along with USWC and other LEC incumbents. The new entrants will provide the same local exchange services to their customers as does USWC to its customers. Staff cites as an example the independent LECs, which have used a bill and keep arrangement with USWC for several years. This relationship is in contrast to the IXCs, which are customers of USWC and have historically provided profits to USWC through access charges. ELI, MCI, Public Counsel, AT&T, and TRACER also argue that the reciprocal nature of bill and keep is appropriate because it treats incumbents and entrants as equals in the local exchange market. These parties contend that the reciprocal nature of bill and keep means that companies do not use the networks of another for free. Consideration takes the form of a payment in kind.

A second argument made by proponents of bill and keep is that it is efficient and simple to administer. Commission Staff, TCG, ELI, Public Counsel, and MFS argue that under this mechanism, neither party incurs measurement and billing expenses, and each company has a strong incentive to minimize its costs and improve the efficiency of its network. AT&T notes that cost studies are avoided. MCI cites the use of mutual traffic exchange among non-competing LECs for terminating EAS traffic as evidence of the efficiency of this compensation structure. It argues that in these situations, where competitive advantage is not sought, adjacent incumbent LECs have chosen bill and keep as the most efficient mechanism.

A third argument made by proponents of bill and keep, including MFS, TRACER, and DOD/FEA, is that it eliminates incentives to perpetuate traffic imbalances. This argument holds that an incumbent LEC would have an incentive under a measured use scheme to delay implementation of local number portability since without number portability, customers are less likely to switch their incoming lines to a new service provider. A bill and keep arrangement would give incumbents an incentive to negotiate better long-term solutions and to develop a workable system of number portability.

The incumbent local exchange companies oppose a bill and keep compensation structure, arguing that it would fail to compensate them for use of their networks by competitors. GTE refers to this arrangement as "forced barter" and argues that it does not satisfy the obligation to make just compensation. USWC similarly argues that "every carrier is absolutely entitled to reasonable and sufficient rates for services rendered" and that the bill and keep arrangement does not provide that compensation.

GTE further argues that full and just compensation would not result under bill and keep unless there were an exchange of equal value and that this is unlikely under bill and keep. Exchange of equal value would require that traffic between two companies be perfectly in balance, and there is no evidence that this would be the case, according to GTE.

Another argument raised by opponents is that the bill and keep structure would invite arbitrage of the differences in rate structure between toll and local access. WITA argues that bill and keep would give even small customers an incentive to establish their own local exchange company. Rather than pay the incumbent LEC for PBX trunks, the customer could obtain bill and keep interconnection service.

The bill and keep structure also is criticized for sending price signals that are inconsistent with the development of an efficient competitive telecommunications market. GTE argues that prices should reflect costs. Bill and keep sets a zero price for terminating local traffic, when that service has a cost. (Beauvais, Ex. T-133, p. 10) WITA makes a similar argument, quoting USWC witness Harris that "the central tenet of economics is that prices pay a critically important role in the allocation and distribution of goods and services in a market economy. Bill and keep violates that principle." (Ex. T-31, p. 9)

### c. Flat-rated port charge

Besides mutual traffic exchange, the other alternative to the per-minute regime proposed by USWC and GTE is a "flat-rated port charge" for interconnection.[10] As described by TRACER witness Zepp, companies would pay a charge for each port interconnecting the other. In effect, the total cost of each port would be allocated based upon use of that port during the period of peak demand. The company with the greater number of terminating minutes during the busy hour would pay an amount based on the difference in minutes and the cost of the

[10] While this option is styled a "flat-rated charge," it would be more accurate to describe it as a peak use charge. If the charge were truly "flat-rated," it would not vary with a carrier's use of peak capacity. For instance, flat-rated local telephone service in this state means that a customer pays a flat monthly rate whether or not they make local calls. The port charge proposed in this case is a charge based upon use, but only use during the period of peak demand.

interconnection.[11] (Ex. T-151, pp. 19-20) Commission Staff witness Wilson also supported this formulation of a port charge as an alternative to "bill and keep." (Ex. T-155, p. 31)

Commission Staff, TRACER, and ELI support mutual traffic exchange as the preferred compensation mechanism but argue for a port charge as the second-best alternative. TCG advocates a hybrid approach using bill and keep for end office interconnections and a port charge for tandem interconnections. However, no party offers a port charge as its preferred method of structuring compensation.

The record in this proceeding is, to put it euphemistically, rich with argument and evidence on the advantages and disadvantages of the per-minute charge and bill and keep alternatives. Very little information has been provided by the parties on the merits and demerits of a port charge. In support of a port charge over a per-minute charge, Commission Staff and ELI contend that a port charge would result in cost-based rates that are more competitively neutral than per-minute charges. Another suggested advantage of port charges, compared to per-minute charges, is that this mechanism would avoid many of the expenses of metering, billing, and auditing every minute of use. Charges would be based on peak traffic instead.

In addition, contend Commission Staff and ELI, a port charge is economically efficient, in that it recognizes that interconnection costs are determined primarily by demand for peak network capacity and that off-peak use has very little cost. TRACER and ELI argue that port charges also allow new entrant ALECs more flexibility (relative to measured use rates) to experiment with their own pricing plans. Finally, TCG argues that port charges allow each company to obtain compensation for the costs of interconnection on a basis that parallels flat-rated retail pricing.

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[11] The proposed port charge formula is

$$\text{Price/Port} = 9{,}000 \times (F_{ALEC} - F_{USWC}) \times (\text{TSLRIC-X})$$

where:

$F_{ALEC}$= the fraction of traffic a typical ALEC terminates on USWC during the busy hour, plus or minus 5%,

$F_{USWC}$= the fraction of traffic that USWC typically terminates on a ALEC during the busy hour, plus or minus 5%, and
(TSLRIC-X)= the TSLRIC (minus an adjustment factor), expressed in dollars per minute. The per-minute rate is multiplied by 9,000 minutes per month to arrive at a monthly rate.

### 3. Commission Discussion and Decision -- Compensation

The structure of a compensation mechanism, as well as the level of interconnection rates, has been argued and examined in great detail in this proceeding. The Commission finds itself impressed with the weaknesses of both USWC's proposed per-minute charge and the mutual traffic exchange mechanism offered by other parties. The record demonstrates that neither mechanism would provide a long-term compensation structure that meets the policies and objectives discussed earlier in this order. This discussion will explain that conclusion, provide for an interim compensation mechanism, and provide the parties with direction on how a long-term compensation structure should be developed.

#### a. The proposed minutes-of-use structure

The Commission rejects USWC's proposal to impose toll-type access charges on each minute of local interconnection. Neither the structure of the proposed mechanism nor the specific rates proposed can be considered to be fair, just, and reasonable. Adoption of a minutes-of-use scheme would either impose extremely high barriers to entry or substantially increase the retail price of local service. Either result would conflict with state policy goals. Our rejection of the proposed minutes-of-use structure and rate is based on three basic factors:

(1) Attempting to unify rate structures in the toll and local access markets by imposing toll-type charges on local access is misguided and unnecessary.

The incumbent LECs look to their existing relationships with the interexchange carriers as a model for their future relationships with competitive alternative local exchange companies. USWC argues that one of two fundamental principles supporting its usage-based pricing structure is that "local interconnection is no different technically and conceptually from any other kind of interconnection" (USWC brief, p. 29). Since local and toll access are technically similar, it is argued that rates structures should be the same. With the IXC rate structure already in place, the incumbent LECs appear to believe the best strategy is to apply that structure to the new entrant ALECs.

The Commission believes it would be a fundamentally misguided strategy to emulate the toll access structure in local exchange interconnection or to make consistency between toll and local access rates an objective in developing an interconnection compensation structure. It should be recalled that toll access rates were developed in a regulatory setting to provide consistency between retail toll rates and wholesale toll access rates. It remains unclear whether the use of measured toll access rates to recover non-traffic-sensitive costs will be competitively sustainable and economically efficient over the long term.

Since the toll access charge regime reflects retail rate structures in wholesale rates, following the toll example means developing a local interconnection regime that reflects the structure of retail local rates. In concrete terms, this means that local interconnection would be

available on a flat-rated basis. It would not preclude a measured service option, but it would preclude mandatory measured service at the wholesale level.

(2) Measured use interconnection rates are not cost-based, because the costs of interconnection generally do not vary with the level of traffic being exchanged.

USWC's second "fundamental principle" underlying its usage-based compensation scheme is that "interconnection rates should be cost based." USWC brief, p. 29. According to the incumbent, "the monopoly era approach of allocating large amounts of revenue requirement to interconnection rates to keep all residential rates below cost is not viable going forward." Id., p. 30.

That argument, whatever its merits, speaks to the *level* of interconnection rates and says nothing about the *structure* of rates. On the issue of rate structure, USWC's brief cites its witness, Mr. Owens, who testifies that one implication of this principle of movement toward economically rational pricing was "the adoption of interconnection rate structures that are reflective of how costs are incurred." (Ex. T-10, p. 5) He then concludes:

> Thus, local switching costs imposed by the termination of traffic on a USWC switch from an alternative exchange carrier are appropriately recovered through usage sensitive charges -- not through bill and keep or flat-rated port charges. (Ex. T-10, p. 5)

Missing from USWC's case is the evidence that shows usage-based rates are "reflective of how costs are incurred." By USWC's reasoning, only if costs are primarily traffic sensitive would USWC's support of usage-based rates be consistent with its principle that rate structures reflect how costs are incurred. The record does not support USWC on this point.

Instead, the record shows that usage-based prices are anything but consistent with the underlying costs. Call termination costs are primarily a function of the capacity required to meet peak demands. Once that level of capacity is installed, costs do not vary significantly with the level of traffic. (Montgomery, Ex. T-84, pp. 47-48; Montgomery, Ex. T-86, p. 23; Wilson, Ex. T-155, p. 33; Andreassi, Ex. T-83, p. 27; Zepp, Ex. T-153; King, Ex. T-104, pp. 27-30) Each firm should be responsible for the costs that it imposes on others; usage-based rates provide no assurance that this will happen. A company whose outgoing traffic, for instance, is primarily during the busiest hours would contribute much more to costs than it would pay in interconnection charges under a minutes-of-use regime. That would encourage uneconomic entry and be unfair to the terminating company.

(3) A measured use regime would threaten the state's public policy of affordable, flat-rated local service.

The final strike against a mandatory measured-use compensation structure is that it conflicts with and could ultimately undermine the state's policy in favor of providing telephone

customers with the option of flat-rated local service. Adopting mandatory measured service at the wholesale level makes it impossible to adopt a retail rate structure that reflects the wholesale price structure without violating the statutory ban on mandatory measured service. (Murray, Ex. T-135, p. 6; Beauvais, Ex. T-130, p. 12; Zepp, Ex. T-153, p. 5)

USWC's proposed minutes of use rate likely would price new entrant ALECs out of the market for flat-rated local service, thereby insulating incumbents from competition for those customers who want flat-rated service -- a group that would appear to include most customers. USWC argues that any of its competitors would be free to sell at retail flat-rated services that it was buying from USWC at wholesale on a measured basis, and we do not disagree. But that does not mean that such a strategy would be competitively viable. (Montgomery, Ex. T-84, p. 48) The costs of USWC's competitors would be higher by the amount of the access charge, thereby reducing pressure on USWC to maintain low rates. Any firm charging flat rates while paying measured rates for access would be vulnerable to a price squeeze as calling volume increased. (Zepp, Ex. T-151, pp. 13-14; Wilson, Ex. T-155, p. 26)

The minutes of use plan would not only raise costs of competitors but also directly place upward pressure on the incumbents' flat-rated local service, both because of the additional expenses associated with measurement and billing, and the potential that retail rates would have to be raised when the access charges are included in an imputation calculation. (Cornell, Ex. T-140, p. 34; Smith, Ex. T-157, p. 20; Smith, TR., pp. 2330-31; Murray, Ex. T-135, p. 6; Murray, TR., p. 1962; Beauvais, Ex. T-130, p. 12)

In summary, USWC has proposed mandatory measured use as the exclusive compensation mechanism and at a rate that is excessive in relation to the service's cost. Adopting that proposal would throttle the nascent competition in the local exchange market, foreclose the potential benefits that consumers might enjoy from being able to choose among local exchange companies competing for business on the basis of price, service, and technology. Even as it restricted access to competitive options, a mandatory measured rate regime for local interconnection could, through imputation requirements, drive up the incumbent's local rates and undermine flat-rated local service at the retail level. Adopting such a compensation structure is not in the public interest.

**b. Bill and keep as an interim measure**

The Commission will adopt, as an interim measure, the mutual traffic exchange or bill and keep mechanism for compensating local exchange companies for terminating traffic from other LECs. Bill and keep is a simple method for companies to interconnect with one another and exchange services in a way that benefits their customers. It is already in use by the industry for exchange of EAS traffic. In those circumstances where companies with similar technologies interconnect and maintain balanced traffic, bill and keep produces the same result, i.e., no exchange of money, as would the alternatives that rely on specific rates.

This decision to rely on mutual traffic exchange as an interim measure is driven in part by the fact that all price-based compensation approaches developed in this record suffer serious deficiencies as a basis for efficient and fair interconnection. Bill and keep is, to put it simply, the least deficient of the alternatives offered. The Commission is persuaded that, while bill and keep lacks the appropriate price signals that are essential to an efficient competitive telecommunications market, incumbents will not be financially harmed by adopting bill and keep on an interim basis. Any potential harm would not occur until current barriers to competition are eliminated and competitors gain more than a de minimus market share. This order explicitly links the transition from bill and keep to a price-based structure to the implementation of true local number portability and the removal of other competitive barriers.

The primary advantage of mutual traffic exchange as a compensation structure is that, in the near term, it provides a simple and reasonable way for two competing companies to interconnect and terminate each other's calls. Adopting a bill and keep compensation mechanism will let the incumbents and the new entrants focus on the technical aspects of efficient interconnection without concerns over costly measurement or accounting procedures and without having to revisit existing interconnection agreements for EAS. Bill and keep offers the best opportunity to get new entrants up and running, with a minimum disruption to customers and existing companies. (Zepp, Ex. T-151, p. 13)

Beyond the inherent simplicity of bill and keep, it has the advantage of avoiding the pricing issue because in many situations it results in little or no money changing hands. Interconnection is a reciprocal relationship; otherwise, it would be "connection" instead of "interconnection." One company is providing call termination to a second who, in turn, is providing call termination to the first. Regardless of the pricing structure or the prices themselves, no net money would change hands in those situations where two companies are obtaining identical services from one another.[12] (Cornell, Ex. T-140, p. 26; Beauvais, TR., pp. 1805-06)

We would not adopt bill and keep if it appeared that new entrant ALECs would be imposing more costs on the incumbents than they would be incurring by terminating incumbents' traffic.[13] This might happen if all traffic were from the ALECs to the incumbent LECs. Both would incur the cost of establishing an interconnection, but with no traffic going to the new entrant, the cost incurred by the incumbent provides it no benefit. However, the opponents of bill

[12] This is not to suggest that prices are irrelevant when traffic is in balance and no money is changing hands. The structure and level of prices would affect companies' incentives and decisions in many areas, including investment in new capacity, retail rate structure, and marketing strategies. We conclude that limiting bill and keep to an interim period minimizes the adverse effects posited by such incentives and long-term decisions.

[13] This condition is frequently referred to in the record as a "traffic balance." However, since the interconnection costs are primarily fixed (non traffic-sensitive), the most relevant measure of balance is not the volume of traffic but capacity to carry traffic.

and keep have not demonstrated that this situation is likely to occur, at least in the near term when bill and keep will be in place. To the contrary, the only evidence on the record favors the theory that traffic will be close to balance.[14] (Wilson, Ex. T-155, pp. 23-25; Montgomery, Ex. T-84, p. 44; Montgomery, Ex. T-86, p. 21; Cornell, Ex. T-140, p. 28)

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[14] If ALECs develop more than a de minimus market share, and the incumbent LECs have evidence that this interim "bill and keep" requirement causes the incumbents competitive harm, they, of course, can file appropriate tariff revisions designed to correct that development.

It is impossible to say exactly what will occur once competition ensues, but every indication at this point is that the new entrant ALECs will be seeking to provide full-service telecommunications. Their customers can be expected to receive calls as well as make calls. Incumbent and entrant, each seeking to satisfy the demands of its own customers, will have the same need for interconnection.[15] We find little potential harm and much potential gain to having competition begin under an interim bill and keep arrangement.

**c. Future structures for compensation**

Adopting bill and keep as an interim measure raises the question of what structure compensation should take over the long term. Specifically, what will follow bill and keep? The Commission expects that future interconnection arrangements will be negotiated with mutually acceptable results once the bargaining position between incumbents and new entrants becomes more balanced. As technical problems such as number portability are resolved and competition becomes more pervasive, compensation -- like every other aspect of interconnection -- will usually be negotiated to the mutual satisfaction of the interconnecting companies. We would be

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[15] This prospect of balanced demand for interconnection may not be realized if companies are unable to develop a way to make telephone numbers portable among companies, so that a customer can switch companies without changing telephone numbers. The primary concern about a lack of number portability is its effect on competition. The costs of switching numbers would discourage customers from changing companies and thereby allow the incumbent to maintain above-market prices. However, a secondary concern is that, to the extent new ALEC entrants do attract customers, the traffic might be out of balance. A customer might keep its USWC line (and number) for incoming calls and use an ALEC's line for outgoing calls. The result would be an imbalance of traffic on the ALEC-USWC interconnection, even though the customer's total traffic is in balance. In this example the interconnection imbalance exists only because of a lack of number portability and likely would not continue once numbers become portable.

very surprised if every negotiation ended with a bill and keep structure. It certainly is not the Commission's intent in this order to require such a result.

As the number and types of interconnection arrangements increase, bill and keep as a standard interconnection framework is likely to become less and less workable as an exclusive structure for compensation. Situations are likely to arise where two competitors do not want or need exactly the same services, measured in either quantity or quality, from one another. One company might desire to terminate all traffic to another on that company's tandem, but the second may prefer to terminate its traffic at each of the first company's end offices. [Owens,TR., p. 355] These decisions will be made by each company based on economics, technology, and the demands of its customers for quality service and low prices. A bill and keep arrangement that presumes mutual exchange of services will not, over the long term, provide the flexibility to accommodate the diversity that is likely to result from competing local exchange companies, though it may well be used in some situations.

Beyond the near term, competitive local exchange markets will require prices such that companies can both obtain the services they need from each other and receive the compensation that they deserve and require. With price tags attached to various interconnection services, LECs can choose and pay for the services that they need to satisfy their own customers. The services that competing companies seek to offer, the markets that they seek to serve, and the technologies they use in the process are all likely to vary among companies.

Price-based mechanisms were proposed in this case, but we are not satisfied that the record here provides a basis to adopt any cost-based interconnection rate. For instance, the costs underlying interconnection are primarily fixed in nature, yet the prices proposed by various parties included usage elements. The USWC proposal departs most from cost in this regard, since it would recover costs through a charge on every minute of use. Even the so-called flat-rated port charge offered as an alternative to bill and keep falls short, in that the charges depend upon a company's use during peak hours. If interconnection costs are fixed, they do not go away if a company does not use the capacity made available by the interconnecting company.

We expect that the telecommunications industry will develop other compensation mechanisms that fit in circumstances where bill and keep does not. To do so, incumbent LECs and new entrant ALECs need to develop further the cost basis for specific rates. Each company has the responsibility to demonstrate that the interconnection rate it would charge is fair, just, and reasonable. At a minimum, the rate should cover the total service long-run incremental cost, or TSLRIC, of the service. The estimates of TSLRIC in this case, however, have been insufficient (see the Cost Studies section of this order). If rates are to be set by the Commission (rather than through good-faith negotiations of market participants, as we would prefer), complete and accurate cost data must be provided. Our lack of confidence in the calculations of USWC's TSLRIC in this case is one factor in our decision to adopt, at least for an interim period, the mutual traffic exchange compensation mechanism.

Any interconnection rates proposed as a replacement for bill and keep also need to reflect the cost structure of the service being provided and in particular the cost structure that is likely to obtain in the future:

> The new technologies are less sensitive to call distances and to call usage. Whereas usage rate structures measure only these factors, the underlying costs are becoming relatively more sensitive to the capacity demanded, rather like the "demand charge" in kilowatts in an electric service pricing structure compared to the usage sensitive kilowatt-hours. (Montgomery, Ex. T-84, p. 48)

Charging a use-based rate to recover costs that are primarily fixed in nature is likely to discriminate against certain groups of customers, distort incentives to enter the competitive market, discourage economic efficiency in the design of networks, and prove unsustainable under competition. Use-based rates may be reasonable when customers also have the option of a flat rate, but nothing in this record suggests a circumstance where mandatory measured service interconnection rates would serve the public interest.

In addition, further exploration is required whether TSLRIC is appropriate as a price for interconnection services. It has been argued that interconnection rates should be set at TSLRIC because an incumbent LEC should not be permitted to earn profits from services it provides its competitors. We are not prepared to accept that argument, though we do not reject it at this point. To illustrate that it may be appropriate for rates to exceed TSLRIC, consider the extreme case where every customer is served by an ALEC: Would the backbone network still be provided by the incumbent LEC? Would rates based on the TSLRIC of interconnection be sufficient to pay the costs of that network?[16] These questions are not resolved by the record in this case, and they need to be before reasonable, cost-based interconnection rates can be established.

Elsewhere in this order, we direct both the incumbent and entrant local exchange companies to develop a plan for implementation of local number portability and present that plan to the Commission within nine months of the date of this order. The Commission believes that is an appropriate time to revisit the interim compensation mechanism adopted in this order. We expect that by that time the industry will have negotiated a replacement for the bill and keep mechanism, a replacement that sets prices for services based on the costs of those services. Failing such an agreement, we expect the incumbent LECs to propose a capacity charge that is cost-based, that is supported by reasonable cost studies, and, if proposed interconnection rates provide a contribution above TSLRIC, that justify the existence and magnitude of that contribution.

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[16] The question, viewed from another perspective, is: Would the new entrant ALECs compete with the incumbent LEC in every aspect and component of its service? Or, does there exist a core network integration function that new entrants cannot be expected to provide? If so, the cost of that function would appear to be one that should be recovered in an interconnection rate that exceeds TSLRIC.

### 4. Legal Arguments Raised by Incumbent LECs on Compensation Issues

As noted in the above discussion of the Commission's authority, the incumbent LECs have taken a very legalistic approach in arguments supporting their interconnection proposals. With regard to compensation for the termination of another LEC's local traffic, they argue that the Commission's authority to set rates is extremely limited. They take the position that the Commission cannot order bill and keep, for either intraexchange traffic or ALECs' EAS traffic. They argue that the Commission must approve their proposed interconnection compensation mechanism, and that the Commission's authority is limited to regulating the fairness and sufficiency of the rates of the services they choose to offer. USWC argues that the Commission has no choice but to approve local interconnection access charges which include an interim universal service charge element, because failure to do so will result in a deprivation of USWC's right to an opportunity to earn a fair rate of return.

The Commission has thoroughly considered the incumbents' legal arguments related to compensation. It concludes that it has the authority to order bill and keep as an interim compensation mechanism. It concludes that it has the authority to order all companies to adopt the same compensation mechanism for all local interconnection, including EAS traffic. It concludes that USWC has not demonstrated a need for, or the amount of, an interim universal service charge. The parties' positions, and the Commission's discussion and decisions on these issues, follow.

#### a. The Commission's legal authority to order bill and keep.

##### (1) Positions of parties

USWC argues the Commission's statutory authority contemplates that sufficient and remunerative rates will be charged for services, and that no statute gives the Commission authority to prescribe *no* rates for a proffered telecommunications service, that is "bill and keep." Specifically,

- RCW 80.36.080 gives the Commission the power to regulate rates for telecommunications services for fairness, reasonableness, and sufficiency. This is not authority to charge "no rates."

- RCW 80.36.160 and 80.36.855 are the Commission's only specific authority over interconnection, and, read together with 80.36.080, give the Commission authority only to review intercompany interconnection service rates for reasonableness and <u>sufficiency</u>.

- RCW 80.04.110 gives the Commission jurisdiction over complaints by competing telecommunications companies against the rates or regulations of another if they are "unreasonable, <u>unremunerative</u>, discriminatory, illegal, unfair or intending or tending to

oppress the complainant, to stifle competition or to create or encourage the creation of a monopoly." [Emphasis supplied.] The Commission's remedy is limited to establishing remunerative rates to be observed by all companies. "Thus, once again it is seen that rates must be charged that are remunerative, or in excess of costs, in order to be competitively fair, and all competing carriers must charge such rates."

- RCW 80.36.330(3) provides: "Prices or rates charged for competitive telecommunications services shall cover their costs." That sufficient rates for services are rates that are above costs, unless the Commission has a compelling record to require higher than otherwise necessary rates to some class of customer in order to subsidize the rates of others, in the furtherance of a mandated public policy, like universal service.

- RCW 80.36.180, which allows the Commission to find that rates charged for or access to a noncompetitive service, such as carrier access service, grants an "undue or unreasonable preference or advantage" to the offering company or another vis-a-vis the complaining company, at most would permit the Commission to utilize an imputation test for local exchange service.

USWC argues that every company is absolutely entitled to reasonable and sufficient rates for services rendered; otherwise its property is being confiscated for the benefit of another, contrary to fundamental constitutional and public utility law.

GTE echoes the argument that if the Commission orders a compensation mechanism that does not provide full and just compensation for the service provided, there will be an "unconstitutional taking" of the incumbents' property. It cites State Ex Rel. Pub. Serv. Co. v. Skagit River Tel. & Tel. Co., 85 Wash. 29, 49 (1915).

To other parties' arguments that there is compensation with bill and keep, "in-kind" rather than "in cash," GTE responds that "neither the state nor federal constitution provides that the obligation to make just compensation may be satisfied by "in kind" compensation, i.e., "forced barter."

GTE argues that compensation must be full and just, that this would not occur under bill and keep unless the exchange of value were equal, that for bill and keep to result in exchange of equal value traffic must be perfectly in balance, and that there is no evidence that this would be the case under the ALECs' proposal.

**(2) Commission discussion**

The Commission rejects the argument that it lacks authority to order bill and keep. Bill and keep is not a system of interconnection "for free." Bill and keep is compensatory. There is a reciprocal exchange of traffic in which each company receives something of value. As Dr. Cornell persuasively testified:

> It is important to remember that rival local exchange carriers are not customers, but co-carriers. That means, whenever the rival has acquired a single customer, traffic will flow both ways. Mutual traffic exchange simply involves each carrier "paying" for the other to terminate local calls originated by its subscribers by mutually terminating local calls originated by the customers of the other carrier. That is why I referred to it as payment "in kind" rather than "in cash." (Ex. T-140, p. 26)

Moreover, as DOD/FEA argues, bill and keep is more consistent with the structure of cost occurrence than are the access charges that the incumbents propose. The reason that local exchange services are flat rated is that most of the cost of local service is not sensitive with traffic volume but is related to access to the public switched network. The principal cost of terminating calls relates to the provision of the line to the subscriber's premise. The cost of this line is largely insensitive to the volume and duration of calling. Even end-office switching costs have a large non-traffic sensitive component. It is thus simply wrong to suggest that the bill and keep procedure means that calls are being terminated "for free." The termination function is paid for, not by the originating company, but by the end-use customer in his flat monthly charge. That charge covers all access to and from the public switched network. Under bill and keep, a company is fully compensated for most call terminations by its own customer.

It also should be kept in mind that confiscation in this context is measured not by any particular element of a rate structure, but by whether the end result of the entire process results in sufficient rates overall. FPC v. Hope Natural Gas Co., 320 U.S. 591, 64 S.Ct. 281, 88 L.Ed. 333 (1944); POWER, supra, 104 Wn.2d at 811.

The record does not support the incumbents' argument that they would not be fairly compensated because traffic may not be "in balance." USWC concedes that it has no traffic studies indicating the likelihood of any traffic imbalance. (Owens, TR., p. 212; Montgomery, Ex. T-84, p. 44) To the extent Washington traffic patterns could be analyzed by Commission Staff, their analysis of EAS traffic supports the position that traffic will be in balance, within ten percent. (Wilson, Ex. T-155, p. 24) The only evidence in the record on local traffic balance between incumbents and ALECs relates to MFS's experience in New York, in which traffic between MFS and NYNEX has been in balance or has favored NYNEX. (Schultz, Ex. T-126, p. 16)

Moreover, as ELI witness Montgomery persuasively testified, in a competitive co-carrier environment, traffic imbalances are unlikely because the ALEC serves the same community of interest area. Thus, unless the ALEC's incentives concerning which customers to serve are artificially distorted by discriminatory compensation rules and the absence of full local interconnection including number portability, the ALEC should see calling characteristics that are highly similar to the dominant incumbent LEC serving the same area. Thus, traffic flows for the ALEC are likely to be in balance. (Ex. T-84, pp. 44-45)

To the argument that bill and keep is not fair or compensatory unless traffic is perfectly in balance, the Commission notes that the parties cannot even agree on whether "balance" should be

measured in terms of amount of traffic delivered for termination or costs to the companies of handling the traffic that is delivered for termination. Also, no compensation mechanism guarantees "perfect" compensation, as the extensive testimony regarding USWC billing errors and auditing difficulties related to minutes of use compensation attests.

That bill and keep is a fair compensation method is evident from the fact that it is the dominant current practice between adjacent LECs around the country, including the state of Washington, for terminating local (EAS) traffic between adjacent exchanges. Where there is no gain to be achieved from anticompetitive or inefficient behavior, companies have elected bill and keep because of its inherent simplicity and efficiencies. As Dr. Zepp stated: "This intercompany compensation method has been used . . . to establish intercompany compensation between local co-carriers who are neighbors. It is just as appropriate for local co-carriers who are competitors." (Ex. T-151, p. 11 (emphasis in original))

Finally, the Commission notes that several other Commissions have ordered bill and keep on an interim basis. In a decision adopted July 24, 1995, the California Public Utilities Commission ordered bill and keep to be implemented for one year, for the termination of calls between ALECs and the incumbent LECs. Orders Instituting Rulemaking and Investigation on the Commission's Own Motion into Competition for Local Exchange Service, Docket Nos. R. 95-04-043 and I. 95-04-044, at p. 47 (1995). An initial decision of the administrative law judge for the Pennsylvania Public Utility Commission likewise ordered the use of bill and keep, for an undetermined period, for the termination of local calls between the ALEC and the incumbent LEC. Application of MFS Intelenet of Pennsylvania, Initial Decision, Docket No. A-310203F0002, at p. 67 (June 6, 1995). The Michigan Public Utilities Commission adopted a modified bill and keep methodology, authorizing assessment of a per-minute charge for local interconnection only if there is a traffic imbalance of greater than plus or minus five percent. Otherwise, bill and keep will apply. Re City Signal, Inc., 159 PUR 4th 532, 543-48, 577 (February 23, 1995).

### b. The Commission's ability to defer a decision on funding universal service.

#### (1) Positions of parties

USWC argues that an I-USC is needed now, and cannot be put off, for both policy and legal reasons. It argues that there is every expectation that USWC's large, powerful competitors will quickly gain significant market share in the Seattle business market, where USWC's business revenues are concentrated, which will imperil USWC's ability to maintain its responsibilities for customers and areas of the state which competitors choose not to serve.

USWC argues that it is important to realize that this Commission has no authority to fund universal service except through access charges to interconnecting carriers. It cannot fund universal service by forcing USWC to maintain a rate structure that does not allow it to earn a fair rate of return on its investment. It argues that this is exactly what will happen if the

Commission defers consideration of universal service. Competitors with no responsibilities will steal off large portions of USWC's revenues, while USWC is not allowed to withdraw from residential or rural service or otherwise take steps to protect its earnings.

USWC argues that because USWC's business and residential service rates are not at issue in this proceeding, USWC cannot protect itself from the loss of revenue that will result from the imbalance in those rates by rebalancing them. The Commission will be denying USWC the right to a fair return on its investment if it fails to order an I-USC to make up for the revenue loss caused by the imbalance.

USWC argues that until the Legislature approves a competitively neutral funding mechanism to make rates affordable in low density and low income market segments, the industry and the Commission presently must use the interconnection charges as needed to preserve universal service.

**(2) Commission discussion and decision**

The Commission is not persuaded that there is an immediate need to deal with the universal service issue, or to grant USWC some sort of interim universal service charge. As Dr. Cornell demonstrated, it will be some time before new entrants have any genuine effect on the revenues of incumbent LECs. She described how previous experiences with telecommunications competition have shown that market shares change slowly even when changing providers is relatively easy for consumers, as is the case in the long distance services market. Moreover, it will be difficult for customers to change local exchange providers in the near future. Most will not even have the option, because networks take time to construct.

Public Counsel witness Murray also testified persuasively that no harm is likely to result to universal service from deferring this issue, because competition is so new and the financial impact of competition on incumbent LECs is likely to be small. (Ex. T-135, p. 3) Her position was unshaken on cross-examination.

Universal service presently is under review in a Washington Exchange Carriers Association investigation, Docket 95-01. We believe that proceeding, and USWC's pending general rate case, are appropriate forums for addressing universal service issues.

We also agree with Public Counsel's argument that a difference in obligation to serve between USWC and ALECs, to the extent it exists, is no reason to adopt the I-USC. Being the ubiquitous provider confers substantial benefits on USWC. As Dr. Montgomery pointed out, even if access revenues from some residential customers may be below the incremental cost as calculated by USWC, that does not correlate to an overall below cost of service, when one considers the entire residential class, including all the intraLATA toll usage, CLASS services (e.g., call waiting, call forwarding, etc.), and other services. (Ex. T-84, pp. 16-19) As ELI and TRACER argue, the market shows that being the ubiquitous provider of telephone network

access is an asset rather than a liability. Access lines are what provide economies of scope; many services can be provided once access is available but not without it. (Zepp, Ex. T-151, p. 28)

Moreover, USWC's proposed I-USC is an entirely arbitrary, non-cost-based assessment. [See, Owens, TR., pp. 236-237] The company has not quantified any "interim" losses that may occur as a result of interconnection, has not quantified what support is needed to protect universal service, has not tried to prove the revenue effects of its being a "carrier of last resort", has not quantified the costs of its carrier of last resort status, and has not quantified the amount of any "subsidy" to residential service. (E.g., Murray, Ex. T-134, p. 8; Murray, TR., p. 1901; Wilson, TR. p. 2176; Cornell, Ex. T-140, pp. 32-33; Montgomery, Ex. T-84, pp. 16-19) USWC has not provided any guarantee that the funds would be used to protect universal service. [Owens, TR., pp. 239-240] The I-USC merely compensates one competitor for lost revenues -- both current and future -- resulting from a former or potential customer's decision to obtain service from another provider. It is simply a device to protect USWC from revenue losses and provide it with an opportunity to impose a price squeeze on ALECs.

Commission Staff's analysis of USWC's justification for the $0.0228/minute shows that the amount is entirely arbitrary. It mimics the carrier common line charge while having nothing in common with it. As Staff notes, USWC witness Owens admitted on cross that the company's figure was arbitrary. [TR., pp. 221-225] As Staff argues, the only certainty about this charge is that, if approved, it will effectively prevent any competition for local exchange services from occurring at all.

As Public Counsel points out, cost studies upon which Mr. Farrow relies for his "subsidy" argument, which were not even filed in this proceeding, do not reflect the Commission-prescribed fill factors, depreciation rates, or cost of capital (Farrow, TR., pp. 705-707), inconsistent with the policy established in the recent "terminal loops case."[17] The studies are inconsistent with USWC's own testimony [Harris, TR. 173] on what is "forward-looking" technology. Finally, the residential cost study contains a basic flaw: USWC improperly allocates 100% of the local loop to residential service, and 0% to services that rely and depend on the use of that facility. The Commission in the past has addressed this issue and found it appropriate to allocate a portion of the loop costs to toll and other services. See, Eighteenth Supplemental Order, Cause No. U-85-23, et al (December 1986). Vertical services such as call waiting, or any other services that use the loop, should receive an allocation of the loop's costs.

We also agree with Public Counsel's argument that the I-USC is likely to vastly overcompensate USWC for whatever problem USWC is trying to solve. It would apply to every line the ALEC installs, if USWC terminating access is provided, including residential lines served by the ALEC which are not imposing a burden on USWC at all. (Owens, Ex. T-32, p. 11; Owens, TR., p. 461) Also, the I-USC would apply even to ALEC lines that a customer wants for

[17] WUTC v. U S WEST Communications, Inc., Docket Nos. UT-930957, UT-931055, and UT-931058, Fourth Supplemental Order (September 1994).

purposes of service redundancy, and apply to new lines obtained when a customer opens a new location. [Owens, TR., p. 461; Owens, TR., pp. 461-462]

Finally, as Public Counsel points out, USWC has not and is not being forced by this Commission to serve areas it does not wish to serve. It recently sold approximately 28 rural exchanges to Telephone Utilities of Washington, Inc. d/b/a Pacific Telecom.[18]

**c. Whether all companies must adopt the same compensation mechanism for all local interconnection, including EAS traffic.**

**(1) Positions of parties**

The complaints of TCG and ELI essentially allege that any compensation arrangement other than bill and keep subjects the complainants to unreasonable prejudice or disadvantage and is discriminatory. The complaints allege that the incumbents employ a bill and keep method of mutual compensation with one another for the exchange of local traffic (i.e., EAS traffic), and that their refusal to offer a bill and keep mechanism to the complainants for the exchange of local traffic subjects the complainants to unreasonable prejudice or disadvantage and is discriminatory.

The ALECs argue that the Commission should order that all companies must adopt the same compensation mechanism for all local interconnection, including EAS traffic.

The incumbent LECs contend that the compensation mechanism that they have adopted for the exchange of EAS traffic has no bearing on the question of what is the appropriate compensation mechanism for their exchange of either "local-like" or "EAS-like" traffic with ALECs.

GTE argues that it currently provides no interconnection service to incumbent LECs for local traffic, because EAS traffic is not "local" traffic, despite its similarity from an end user billing point of view. It argues that therefore the contract rate at which it has offered to terminate ALECs' local traffic cannot be discriminatory, because there is no intercompany local traffic among incumbent LECs. GTE further argues that while its proposed interconnection rate "treats" ALECs' "local-like" and "EAS-like" traffic the same, the Commission has no authority to order it to do so in this proceeding.

[18] See, Third Supplemental Order Accepting Settlement, Docket Nos. UT-940700,-940701 (June 1995).

GTE argues that the complainants' claim that denying them bill and keep for their traffic on existing EAS routes would be discriminatory has no merit. It argues that undue discrimination can exist only as to "like and contemporaneous service . . . under the same or substantially the same circumstances and conditions" (quoting from RCW 80.36.180), and that there is significant uncontroverted evidence on the record that the existing intercompany EAS compensation situation is substantially different from complainants' situation: 1) the participants in the current arrangement are LECs which do not have overlapping territories and which were not in competition for the provision of local exchange and other services when the arrangement was implemented; and 2) the EAS compensation mechanisms are based on cost studies specific to each EAS route.

GTE argues that the Commission does not have the authority in this proceeding to prescribe the compensation arrangements between incumbent LECs and new entrant ALECs for the exchange of traffic on existing EAS routes. It argues that the EAS designations apply only to companies that are parties to an EAS proceeding under the Commission's EAS rules. The statute clearly requires a specific EAS hearing procedure. Thus, if complainants wish to be formally integrated into the current intercompany EAS compensation arrangement, they must proceed through that statutory procedure.

WITA argues that EAS does not represent an industry standard for local interconnection. First, local interconnection is not EAS, which is a toll substitute. Second, as described by WITA witness Smith, bill and keep in the EAS environment is a recent phenomenon; it is a compromise involving an entire package of EAS rules. WITA argues that the ALECs grudgingly admitted on cross-examination their mischaracterization of bill and keep as the industry standard for EAS.

ELI argues that the entire purpose of the Commission's EAS rules is to establish rational "local" calling routes between "communities of interest." The specific identity of the companies involved is irrelevant. To avoid getting bogged down in legal distinctions about which companies are "privy" to existing contracts or covered by existing rules, the Commission, as a matter of competitive policy, should declare that existing local calling areas (i.e., EAS routes) apply to ALECs for purpose of distinguishing between local and toll calling.

TCG argues that EAS should be treated the same for all companies. It argues that EAS areas are established for the benefit of consumers within a community of interest that does not correspond to the LEC-established exchange boundaries. Customers who make calls within that area should be treated the same, not subject to higher charges simply because they choose service from a company other than one of the original EAS companies. TCG recommends that the Commission adopt the same compensation mechanism for all local interconnection, including EAS traffic.

Public Counsel argues that the discrimination complaints of the ALECs present a close legal and factual question. "Their claims are likely meritorious, providing further justification for a bill and keep compensation arrangement." Public Counsel's argument is more fully set out below in the discussion of the TCG and ELI complaints.

Public Counsel argues that:

> It is true that significant public policies are at work in creation of EAS routes, and such routes are set as between specific companies. It is also true that "obligation to serve" may be somewhat different between new LECs and incumbents. But the public policy is to respond to customer needs and demands for local, flat-rated calling within their community of interest. The focus for discrimination should likewise be placed on the customer interest in the situation. The new entrant must attempt to attract the same customers as the incumbents, yet without the same compensation system. As WITA's witness concluded, an access, or usage based cost compensation "will lead to a shift from flat rate to measured service." (Smith, Ex. T-157, p. 17). Incumbent LECs do not face this pressure in the bill and keep environment they enjoy.

MFS argues that if ALECs are required to pay rates higher than EAS rates, incumbent LECs would be engaging in blatant discrimination against the new entrants. It contends that USWC's proposal to migrate its present EAS bill and keep compensation to new charges based upon "costs" is a transparent attempt to support the LECs' efforts to impose high switched access rates which will serve as barriers to entry on the ALECs.

MCI argues that there is no justification for WITA's argument that the Commission should leave the incumbents' EAS routes intact, but that such routes should not be available to new entrants who are not privy to the routes created under Commission rules. EAS routes are established to reflect the community of interest between two areas. A change of provider serving the involved areas does not change their community of interest.

AT&T urges the Commission to reject out of hand the contention by the incumbents that EAS calls will constitute toll traffic when originated by a new entrant and, as such, incur switched access charges. It argues that customers will expect the new entrants to offer the same local calling areas as the incumbents. AT&T supports the suggestion of Public Counsel's witness that, for the interim period, the ALECs should adopt the existing EAS boundaries but that the Commission should re-examine this issue.

TRACER agrees with ELI witness Montgomery. Dr. Zepp also testified that the Commission should allow all providers to participate in EAS routes on equal terms and conditions. EAS routes are established for the benefit of <u>residents</u> of the various communities, not telephone companies. The Commission's order should recognize that a local calling area's "community of interest" will remain a community of interest regardless of the number or identities of firms providing service.

**(2) <u>Commission discussion and decision -- EAS</u>**

The Commission rejects the incumbents' analysis. It adopts the ALECs' position that it should order that all companies must adopt the same compensation mechanism for all local interconnection, including EAS traffic.

Existing exchange and most EAS boundaries were adopted during an era of monopoly local service. Establishing them required a proceeding to determine whether there was a community of interest in the proposed territory, and to determine the engineering costs and lost toll revenues that would result from converting the multiple exchanges into a single local calling area with flat rates. That the determinations involved specific LECs is merely an historical circumstance. Those were the only local service providers at the time.

In established EAS territories, the old exchange boundaries no longer define what is "local service." The "local calling area" now is defined by the EAS boundaries. One has only to open a USWC directory to see that USWC defines its customer's "local calling area" as its EAS territory, not in relation to old exchange boundaries.

The ALECs have stated that they will establish local calling areas and rate centers conforming to existing LEC EAS and exchanges boundaries. So long as that is the case, no possible purpose would be served by requiring ALECs to go through an EAS procedure to establish the local calling areas for their customers. That the existing EAS boundaries define a community of interest is already established. The ALECs do not have to re-engineer existing systems in order to adopt the present EAS territories. The ALECs also have no need to study the effect of the present boundaries on their toll revenues, because they have never had toll revenues from calls between points within the EAS territories.

The Commission finds persuasive on this issue the testimony of TRACER witness Zepp (Ex. T-153, pp. 9-11); the testimony of ELI witness Montgomery (Ex. T-87, p. 7); the testimony of Commission Staff witness Wilson (Ex. T-155, p. 34-36); and the analysis and the arguments of Public Counsel, ELI, TCG, MFS, MCI, AT&T, and TRACER, summarized above. The Commission concludes that EAS traffic is local traffic for purposes of compensation for local interconnection, and orders all parties to enter into compensation arrangements for local interconnection consistent with this conclusion.

The Commission recognizes that as companies transition from bill and keep to other compensation mechanisms for local interconnection, the new mechanisms may also apply to existing EAS traffic.

An issue that will have to await future resolution is what compensation arrangements are appropriate when, as is likely to happen, LECs, including the both incumbents and new entrants, seek to establish different local calling areas than those that presently exist, as a means of attracting customers.

### C. TERMS OF PHYSICAL INTERCONNECTION

### 1. USWC's Proposal

USWC proposes to allow ALECs to interconnect with USWC's network only at three points, using USWC-specified facilities. ALECs could interconnect inside or just outside their own central offices, using USWC entrance facilities. In that case, they would have to use USWC transport to USWC end offices. The ALEC also may interconnect at a USWC central office, using USWC's expanded interconnection service. In that case, it may provision its own transport. USWC is not willing to interconnect ALECs at something comparable to a "meet point" as it does with other incumbent LECs. [Owens, TR., pp. 351-2]

### 2. The Complaints Against GTE

The complaints against GTE do not address the terms of physical connection that GTE has offered, other than GTE's requirement that interconnecting ALECs use separate trunk groups for toll and local/EAS traffic. The complaints allege that this requirement is inefficient and discriminatory. They allege that GTE and other LECs do not require such arrangements of each other for the termination of local traffic.

### 3. Positions of Parties

USWC contends that the company on whose network the traffic originates should define the point of interconnection, and that the originating company should compensate the terminating company for transport if the point of interconnection is near the originating switch, or pay virtual collocation charges if the originating company chooses to provide its own transport to the terminating end office.

USWC states that its preference is to minimize the number of interconnection points with ALECS. [Owens, TR., p. 511, ll. 10-12] In its brief, USWC contends that there are no major disputes between the parties in arranging physical interconnection.

GTE contends that there is no dispute as to whether GTE will directly interconnect with ALECs. GTE witness Beauvais testified that GTE would be willing to have meet points at mutually agreeable locations. [Beauvais, TR., p. 1822]

GTE argues that while some parties expressed concern about two-trunk interconnection, only TCG specifically had concerns about separating toll and local. Dr. Beauvais testified that GTE needs separate trunk groups for local and toll because it needs to distinguish between toll and local traffic. The practice is necessary given the different rates and compensation arrangements applied to toll and EAS. WITA also recommends that toll and local traffic be exchanged on separate trunks. WITA and GTE state that currently incumbent LECs use separate trunks for exchanging local and toll traffic. Toll traffic is handled through a toll trunk group that goes to a toll tandem switch. EAS traffic is handled on an EAS trunk group.

WITA argues that independent telephone companies presently cannot unilaterally designate interconnection points. Rather, the points of interconnection are negotiated between the interconnecting companies. WITA also argues that there is nothing in this record that demonstrates the need for multiple points of interconnection. WITA further contends that the Commission has no authority to prescribe the points of interconnection for local traffic -- RCW 80.36.200 allows the Commission to order that messages be delivered, not to specify the manner in which they must be delivered, and RCW 80.36.160 gives the Commission the authority to prescribe the routing of toll messages only, not local service.

WITA recommends that ALECs connect to the incumbents at mutually agreed meet points. Public Counsel makes a similar recommendation.

TCG, ELI, and MCI argue for interconnection at any technically feasible meet points similar to meet points established between incumbent LECs. Such meet points are usually at or near the traditional boundary separating incumbent LECs. The LEC and ALEC would share the physical cost of interconnection.

TCG recommends that meet points be determined through good faith negotiations, and that all costs associated with construction of facilities to the meet point be shared equally. TCG requests interconnection using two-way DS1 trunks.

MFS argues that the new ALECs should determine the interconnection point. TRACER agrees, contending that the new entrant is motivated solely by desire to minimize costs whereas the incumbent has an incentive to insist on more costly means of interconnection. TRACER argues further that USWC is not suggesting that existing meet points with incumbent companies be abolished.

MCI argues the USWC proposal is unfair, because the result is that ALECs bear most of the cost of interconnection and transport to the incumbent's switch. In addition, by having the originating company select the point of interconnection, there might be two different points of interconnection for the same route, resulting in the inefficient use of trunks. MCI argues that inefficient interconnection harms new entrants more than it does incumbents since interconnection costs represent a more substantial part of a new entrant's cost of doing business.

### 4. Commission Discussion and Decision

Technically and economically efficient interconnection of the incumbent LEC and new entrant ALEC networks is essential to the emergence of a competitive local exchange market. Denial of technically and economically efficient interconnection arrangements creates a barrier to entry. The Commission is persuaded that ALECs should have considerable flexibility to configure their networks in a manner they deem suitable.

Based upon the record, it does not appear that physical interconnection between incumbent LECs and ALECs involves any unique technological problems that the incumbents do

not already face when interconnecting among themselves. The unresolved issues of physical interconnection concern how interconnection meet points shall be established, how interconnection disputes will be settled efficiently and fairly, and whether separate trunks are required for toll and local.

During cross-examination, witnesses for two ALECs (TCG and ELI) testified that they have achieved interconnection with USWC and that USWC has provided the interconnection facilities that they requested. [TR., p. 988; TR., p. 1260] In direct testimony, ELI indicated that the fact it had trunk-side interconnection with GTE was evidence that there were no technical barriers to overcome. (Cook, Ex. T-88, pp. 2-3) AT&T witness Waddell, however, testified that the process of getting interconnected with USWC was not free of some frustrations and setbacks.

The Commission shares the concerns of USWC and WITA that interconnection costs be minimized. As competition develops and the number of competitors increase, it is particularly important that the cost of interconnection not burden customers who have yet to realize the benefits of competition.

The Commission also shares the concern of ELI witness Cook that USWC (and other incumbent LECs) not be in a position to require that ALECs construct facilities that would make their service offerings not cost-effective. [TR., p. 1176] Interconnection rules should not force one company to adopt the architecture of the other or to incur costs over and beyond what is necessary to interconnect with a competitor.

The Commission adopts the recommendations by Public Counsel, WITA and TCG that companies establish mutually agreed upon meet points for purposes of exchanging local and toll traffic.

Such meet points should be established, upon request, for each company registered to provide local exchange service in a given area. USWC and other incumbents may establish, through negotiations, separate meet points for each company or negotiate a common hub by which multiple companies can come together efficiently. Each company shall be responsible for building and maintaining its own facilities up to the meet point. In addition, each company is responsible for the traffic that originates on its network up to the meet point, and for the terminating traffic handed off at the meet point to the call's destination. (Cook, Ex. T-87, p. 3)

In their briefs, USWC and WITA raise the question of the Commission's authority to order additional meet points (meet points in addition to those the incumbents are willing to offer). Given the experiences related by TCG and ELI, negotiating additional meet points does not appear to be a serious problem requiring a determination of the Commission's authority. The Commission expects incumbents and new entrants to negotiate in good faith as co-carriers. If allowing the industry to negotiate their own agreements results in litigation which delays the development of competition, the Commission may need to revisit the issue.

The Commission notes that GTE and USWC currently provision their EAS and toll traffic over separate trunks. [TR., p. 2212, ll. 21-23] We accept WITA's argument that unless

the Data Distribution Center is used, the only way that toll traffic can be segregated for billing of terminating access is if local and toll traffic are routed over separate trunk groups. The Commission finds against TCG on its complaint that the imposition of separate trunks for toll and local is unreasonable or discriminatory.

This order requires that, for intercompany compensation reasons, there remains a need to distinguish between toll and local traffic (which includes EAS). Companies should establish an efficient means, either through engineering (separate trunks) or accounting methods (Data Distribution Center), to distinguish between toll and local traffic.

In summary, the Commission agrees with USWC and GTE that there are no major disputes over physical interconnection. It is not surprising that the first interconnections with competitive companies have been beset by glitches and setbacks. However, we do expect that as competition develops, interconnection between companies will become more routine.

To facilitate the process, the Commission believes that it would be appropriate for the industry, Commission Staff, and other interested persons to establish a process for settling disputes as suggested by ELI in its brief. Staff shall hold a workshop with interested persons to explore how mediation or alternative dispute resolution can be used to settle differences regarding the terms of physical interconnection. Staff shall report back to the Commission on whether an industry consensus has emerged, and on any other recommendations Staff may have for resolving disputes, within nine months of the date of this order.

## D. UNBUNDLING/RESALE

### 1. Introduction

Unbundling is the identification and disaggregation of physical components of the local exchange network into a set of "piece parts" which can be separately provisioned, cost supported, priced, and combined in such a way as to provision all service offerings, including those offered by the LEC. (vanMidde, Ex. T-111, p. 2)

Resale refers to the ability of competitors and other wholesale purchasers to resell, to end users, services and facilities they purchase from the incumbent LECs. Tariffs often have been user-specific, containing restrictions on how a service can be used and its resale.

Unbundling network functions and permitting their resale allow new entrant ALECs to be able to combine their facilities and those of the incumbent LEC to offer a complete telecommunications service. Unbundling would enable the ALECs to extend their geographical reach by purchasing facilities from the incumbent LEC rather than constructing all of their own facilities. It also would enable them to assemble the most cost-effective combination of existing network elements and self-provisioned elements.

### 2. Positions of Parties

The incumbent LECs argue that the Commission has no authority to order unbundling or changes in tariff resale provisions. They contend that it can only order interconnection and regulate the fairness and sufficiency of the rates for the interconnection services and the unbundled facilities the LECs choose to make available.

GTE argues that unbundling is the creation of new services, and that the Commission has no authority to mandate new services.

USWC also argues that the Commission has no authority to order a company to make non-essential services or facilities available to a competitor, and that nothing that USWC is refusing to unbundle is essential. It argues that the Commission should use the "essential facilities" doctrine applied in antitrust law to determine, on a factual basis, whether a facility is essential. It cites a number of court decisions, including United States v. Terminal Railroad Ass'n., 224 U.S. 383 (1912); Otter Tail Power Co. v. United States, 410 U.S. 366 (1973); City of Anaheim v. Southern Cal. Edison Co., 955 F.2d 1373 (9th Cir. 1992); and Alaska Airlines, Inc. v. United Airlines, Inc., 948 F.2d 536 (9th Cir. 1991). Its argument is that an essential facilities claim should not be granted unless it is impractical for the competitor to duplicate the facility, and the monopolist refuses to make the service available to competitors. It contends that if it offers a finished service, it is not refusing to make its facilities available: "Properly analyzed, none of USWC's services are truly essential to competitors so long as interconnection of networks is offered on reasonable terms and conditions." (USWC Brief, p. 43) It also contends that its current competitors are large companies that "are capable of providing their own services needed to provide in turn a complete local service." (USWC Brief, pp. 43-44)

USWC contends that its local transport restructure, virtual collocation service and its unbundled loop service, which it intends to file, represent extensive unbundling.

USWC questions the fairness of resale in the absence of rate rebalancing and continued interLATA toll business restrictions. Also, USWC cautions that resale should not be used to avoid toll access charges.

On rebuttal, USWC indicates that it will file a tariff for "an unbundled loop service." According to USWC, this service will provide a two-wire connection from an end user's premise to the USWC central office main frame, which can be interconnected to the ALEC's virtual collocation equipment or to USWC's private line transport service for delivery to the ALEC.

GTE argues that unbundling involves a multitude of issues, but the record does not provide a sufficient basis for resolving them.

WITA argues that if the Commission does have authority, it should only require unbundling on a bona fide request basis and only when economically and technically feasible.

Commission Staff argues that the authority for unbundling may be found in RCW 80.36.140, second paragraph, which allows the Commission to determine the just, reasonable, proper, adequate and efficient practices to be observed and used, if it determines after hearing that a company's practices are unjust or unreasonable. It argues that the term "practice" is clearly broad enough to cover the offering of services on a bundled or unbundled basis, and, moreover, that the practice of bundling could be "unjust or unreasonable" in a competitive environment.

Commission Staff recommends the Commission order unbundled loops and line side interconnection. Other basic network functions should be unbundled later and a process should be developed to address unbundling requests. Staff witness Selwyn outlined a bona fide request process which could serve as an alternative to a second phase of unbundling. WITA, while concerned about the cost of applying unbundling to smaller companies, appears to support such a bona fide request process for unbundling.

Public Counsel finds authority for unbundling and resale in the declaration in RCW 80.36.300(5) that it is state policy to promote diversity in the supply of telecommunications services and products. Public Counsel argues that the record is clear that unbundling and resale are key elements in fostering diversity in supply of services and products.

Public Counsel witness Murray testified that the high cost of constructing duplicate loop facilities makes it prohibitive for new entrants to provide services to lower-volume customers. But if provided access to cost-based unbundled loop services, competitors may be able to service residential and small business customers at a lower total cost than the incumbent by providing their own switching, trunking, and administrative services in combination with the incumbent's loop.

ELI argues that USWC's definition of what is "essential" is unrealistic. ELI argues that the economics of trying to rapidly build the facilities as extensive as USWC's full network are prohibitive, which is why ALECs must use the incumbent's facilities and why a service or facility therefore can be essential even if there exists the possibility that the facility can over time be duplicated by a competitor. As a general matter, ELI believes essential services should be priced at TSLRIC.

ELI supports MCI witness Cornell's list of 34 monopoly functions or elements necessary for local exchange competition to have its greatest benefits to consumers, which should be unbundled immediately and made available at prices based upon their total service long run incremental cost (TSLRIC). ELI differs from MCI in that it believes that the loop need not be unbundled into the feeder and distribution portions at this time. TRACER also supports MCI's position, as modified by ELI.

ELI argues that, under the present USWC proposal, interconnection of a stand-alone Network Access Channel (NAC) to an ALEC's interconnector equipment would require purchase of an expanded interconnection channel termination ("EICT") element, which provides for the path from the interconnector equipment to a USWC private line within the same wire center.

ELI's engineer witness Cook argues that all that is actually required is a two-wire jumper providing a path from the USWC main distribution frame to the ALEC's interconnector equipment; USWC's EICT element includes equipment that is not required. (Ex. T-87, p. 16)

TCG recommends that the Commission order USWC and GTE to provide unbundled subscriber loops and line-side interconnection as described in Mr. Cook's testimony (Ex. T-87, pp. 11-16). Other LEC network functions also may need to be unbundled. Such unbundling raises issues of technical feasibility, cost, and pricing that have not been fully explored in these proceedings. TCG recommends that the Commission order that network functions other than the local loop be unbundled and made available to competitors upon bona fide request and at rates, terms, and conditions established through good faith negotiations.

MFS also argues that unbundling of the local loop is necessary to remove a significant barrier to competition. The incumbents were able to construct their ubiquitous networks under the protection of their monopoly status, with the advantage of favorable government franchises, access to rights-of-way, and other government assistance. MFS argues that replication of the existing LEC loop network would be cost-prohibitive and accomplished on less favorable terms than the incumbents enjoyed. MFS recommends that the Commission require that incumbent LECs offer unbundled local loops priced on a reasonable cost basis using the TSLRIC method of determining costs.

MCI argues that because of the long-standing historical monopoly in local exchange service provision, the only available supplier of "parts" of the network needed to supply service is the incumbent LEC. These components must come from unbundling and the removal of resale restrictions. Not to require unbundling and resale would allow the incumbent to use its past government-granted monopoly to create unnecessary barriers to entry. It argues that unbundling and resale were how competition was able to develop in the long distance market.

MCI argues that USWC should be required to price the unbundled functions on a TSLRIC basis. Dr. Cornell describes how an unbundled functionality incorrectly priced will also impedes competition. (Ex. T-140, p. 85)

AT&T contends that the Commission should order USWC and GTE to provide an unbundled loop and a switch port, to be tariffed within 30 days of the order in this case. The prices for these services should be at TSLRIC; in no event should the total of the unbundled elements exceed the price for the bundled services (local exchange residential and local exchange business) offered by the incumbent LECs. It also argues that the testimony of Public Counsel witness Murray supports more extensive unbundling. It urges the Commission to order the level of unbundling described by AT&T witness vanMidde (Ex. 111, pp. 5-6) -- eleven basic network functions, with two of those (switching and tandem switching) being further unbundled.

The non-LEC parties support elimination of resale restrictions, with the exception that where residential service is determined to be priced below cost, resellers should not be able to resell to other than residential customers.

### 3. Commission Discussion and Decision

The record clearly establishes that unbundling of the local loop is essential to the rapid geographic dispersion of competitive benefits to consumers and is in the public interest. Unbundling allows customers greater opportunity to choose between a diversity of products, services, and companies. Unbundling also allows for efficient use of the public switched network, reduces the likelihood of inefficient network over-building, and ensures that competition is not held hostage by being bundled with bottleneck functions.

The Commission agrees with Public Counsel's argument that facility-based competition may be the preferred future, but the record supports the conclusion that retail competition through a strong resale market may indeed be an important step in the long term development of local competition.

The Commission also is persuaded by Dr. Cornell's testimony that no one can be certain how much of the local exchange can be supplied competitively. (Ex. T-140, p. 72) Allowing for the access to and resale of unbundled parts of the incumbent's network allows for those parts of the local exchange market that can support competition to move forward with competition without being held back by those parts of the market still characterized by monopoly.

Unbundling also holds the prospect of speeding the delivery of advanced network services such as ISDN (integrated services digital network) to customers who are not yet located along an ALEC's network. See, Cook, Ex. T-87, p. 16.

The incumbent LECs have focused their arguments against unbundling on legal, rather than policy grounds. The Commission has authority to order unbundling pursuant to RCW 80.36.140, which states in part:

> Whenever the commission shall find, after such hearing that the rules, regulations or practices of any telecommunications company are unjust or unreasonable, or that the equipment, facilities or service of any telecommunications company is inadequate, inefficient, improper or insufficient, the commission shall determine the just, reasonable, proper, adequate and efficient rules, regulations, practices, equipment, facilities and service to be thereafter installed, observed and used, and fix the same by order or rule as provided in this title.

(Emphasis added.)

The first paragraph of RCW 80.36.140 (quoted in the Commission Jurisdiction section of this order) gives the Commission broad authority over rates. The second paragraph, quoted above, gives the Commission broad authority over practices and services as well. The way in which services are offered, on a bundled or unbundled basis, certainly falls within the scope of the second paragraph. See, e.g., State ex rel. American Telechronometer Co. v. Baker, 164 Wash. 483, 491-96, 2 P.2d 1099 (1931) (citing earlier version of above quoted provision); State ex rel. Public Service Commission v. Skagit River Telephone & Telegraph Co., 85 Wash. 29, 36, 147 P. 885 (1915)(describing Commission's power to regulate public utilities as "plenary").

The Commission also agrees with Public Counsel that the declaration at RCW 80.36.300(5) that state policy promoting diversity in the supply of telecommunications services and products provides authority to order unbundling and resale. It is clear from this record that unbundling and resale are key elements in fostering diversity in supply of services and products.

The Commission does not agree with USWC's argument that the "essential facilities" doctrine applied in antitrust law is applicable in the context of Commission regulation of telecommunications companies' practices. This Commission is charged by statute to determine adequate and efficient practices to be observed by telecommunications companies, and to correct practices that tend to stifle competition, RCW 80.04.110. While reference to antitrust law by analogy may be useful in some future cases, we are not here applying the antitrust statutes. There is ample testimony in this record that requiring new entrants to duplicate all of the facilities of existing LECs is highly inefficient, and that it tends to stifle competition.

However, it appears that the Commission need not order unbundling at this time, given USWC's representation that it will file an unbundled loop tariff, and the apparent lack of an immediate need for more extensive unbundling. At this time, the Commission is satisfied with a first level of unbundling that includes an unbundled loop and an efficient line-side interconnection.

USWC shall file a tariff within 30 days of this order that offers access to a two-wire connection from an end user's premise to the USWC central office and provides for line-side interconnection -- the transmission path between the incumbent LEC's main distribution frame and the new entrant ALEC's collocated equipment. This tariff should be unbundled from redundant elements such as channel performance, remote testing, and conditioning. In addition, the line side interconnection should be equally efficient, as suggested by ELI witness Cook in his direct and rebuttal testimony. Line side interconnection involves running a two-wire jumper between the vertical and horizontal sides of the main distribution frame, cross-connecting the appropriate wire pair on the horizontal side to the alternative company's collocated equipment. (Ex. T-88, p. 6)

In support of its tariff, USWC should file a TSLRIC (total service long run incremental cost) study consistent with the cost methodology, input data, assumptions, and cost modeling recommended by Commission Staff and discussed in greater detail in the cost section of this order (Section V.). The Commission is leaving open the question of what level of contribution

should be established above TSLRIC but wishes to make clear that the starting point for such discussions should be TSLRIC.

Further unbundling, beyond the unbundled loop and line-side interconnection, will likely be necessary, particularly in areas where complications with right-of-way and conduit access makes duplicating the incumbent's network not only economically, but technically, impossible. In Docket No. U-86-86, the Commission instructed USWC that it expected the company to move in the direction of unbundling monopoly and competitive elements as much as possible. In re Pacific Northwest Bell Telephone Company, Docket Nos. U-86-34, U-86-35, U-86-36, U-86-86, & U-86-90, Fourth Supplemental Order (April 1987). That continues to be the Commission's policy. See, WUTC v. U S WEST Communications, Inc., Docket Nos. UT-911488,-911490,-920252, Fourth Supplemental Order (November 1993).

The ability of an incumbent company to successfully acquire pricing flexibility, either through seeking competitive service classification or through an alternative form of regulation, could rest on the extent to which it has freed up its potentially competitive services from its bottleneck and monopoly services. This case confirms the Commission's belief that incumbent LECs will see the benefit to unbundling, not only for advantages associated with freeing itself up to compete more effectively but also in maximizing the use of its network and the resulting revenues associated from that use.

Thus, while we would prefer that companies step forth with unbundling tariffs, for now the Commission supports a bona fide request procedure proposed by Commission Staff witness Selwyn, and endorsed by WITA.

Resale is a significant issue in the case of extensive unbundling. The Commission is not ordering extensive unbundling. USWC shall allow resale of unbundled loop and other transport service, except that residential service may not be resold as business service and local call termination may not be used to deliver toll traffic.

## E. NUMBER PORTABILITY

### 1. Introduction

Number portability is the ability to retain a telephone number when a subscriber changes from one service provider to another (service provider portability), or when moving from one geographic location to another (geographic portability). With true number portability, the change of provider or location would be seamless, allowing users to be able to perform the same functions they were able to do previously. USWC is proposing an interim solution, using its existing service options at existing tariffed rates, until true portability can be established.

In its rebuttal testimony, USWC proposed to offer two forms of interim number portability, using remote call forwarding and direct number route indexing. The company

intends to price the service at about $4 a month, plus two non-recurring charges. (Owens, Ex. T-32, p. 67)

**2. Positions of the Parties**

USWC argues that number portability is not an absolute prerequisite for effective competition, but agrees that number portability could provide benefits to consumers generally, and states that it will continue to pursue workable solutions. USWC argues the Commission should approve the company's interim approach on this issue, and allow USWC to file its proposed tariff for review and implementation.

GTE states that it is an active participant in current industry trials and that ELI did not prove that GTE is unwilling to provide number portability.

WITA agrees with ELI witness Ackley that number portability is an important element of intraexchange competition, and that the Commission should establish a timeline for the industry to develop a service provider number portability solution and report back to the Commission. It also recommends that the Commission establish a series of deadlines for the existing Washington Exchange Carrier Association docket considering number portability.

Commission Staff recommends that Market Expansion Line and Direct Inward Dialing be made available by USWC to interconnecting service providers at rates which reflect USWC's TSLRIC or ASIC (average service incremental cost, discussed infra) of those services, set out on confidential page 45 of Commission Staff witness Wilson's rebuttal testimony (Ex. T-155). Public Counsel supports Staff's recommendation.

TCG concedes that true service number portability is not yet feasible. The lack of number portability, however, has a profound impact on the ability of TCG and other ALECs to market their services to existing LEC customers. Most customers are unwilling to change providers if they cannot keep their numbers. Interim solutions have serious and substantial flaws. TCG therefore argues that incumbent LECs should be required to provide interim number solutions for their former customers who change service providers without charge, until a permanent number portability solution has been developed and deployed. Alternately, the service should be available at TSLRIC. TCG argues that the lack of number portability arises because of the way LEC networks were originally configured, and that LECs should not be directly compensated for more than their costs of mitigating a barrier to competition -- a barrier from which they benefit and for which they are responsible.

ELI argues that the availability of true local service provider number portability is a necessary precondition for effective local service competition. ELI witness Ackley testified that 86% of ELI's sales contacts terminated as soon as the customer found out they had to change their telephone number. [TR., p. 1227, ll. 18-21] ELI recommends that the Commission order the parties to cooperate to develop a permanent solution, and report to the Commission within six

months. ELI endorses the USWC offering but believes the service should be at the lowest possible price to mitigate for the technical deficiencies and the economic penalty imposed on an ALEC for not being able to efficiently offer its customer the ability to retain its telephone number when switching service providers.

MFS witness Schultz testified to similar marketing problems caused by the lack of number portability. MFS argues that the Commission should order the incumbents, on an interim basis, to provide ALECs with Co-Carrier Call Forwarding ("CCF") as a form of number portability. It argues that the New York Public Service Commission has ordered CCF, and that CCF, as Mr. Schultz described, has numerous advantages over "Flexible DID" and other remote call forwarding alternatives. It argues that USWC provides a conceptually similar service, "call forwarding - variable," and that the Commission should order USWC to provide this service to ALECs at cost. However, MFS also believes that a $4.00 monthly recurring fee per redirected business line (the negotiated interim rate in New York) is an acceptable interim solution.

MCI also argues that the availability of local number portability is essential to the development of effective competition. Their witness Mr. Traylor testified about a Gallup survey performed for MCI on a national basis that showed that 83% of those surveyed considered it important to retain their telephone numbers when changing service providers. [TR., p. 1683] MCI witness Cornell testified that allowing USWC to charge retail rates for its interim solutions would create an incentive for it to try to delay provisioning true service provider number portability, because it benefits commercially from the sales and because delay will impede entry. Dr. Cornell recommends that the cost of USWC's interim proposals be recovered either by setting the price at cost (TSLRIC), with no markup, or by a surcharge on all telephone numbers.

### 3. Commission Discussion and Decision

The Commission is persuaded that true number portability is an essential condition for effective local exchange competition just as it has been for the "800" number services market. The Commission also believes that in the interim, less than perfect number portability needs to be available. USWC's offer of its two services is appropriate.
However, the rate for those services should be set at the company's incremental costs. Interim number portability is a stopgap measure until permanent number portability can be established. Thus, there is no reason for USWC to recover common costs from this service. USWC shall file its interim number portability tariff within 30 days of the date of this order. In the absence of an incremental cost study for interim number portability services, the Commission will accept the rates set forth by Commission Staff witness Wilson. (Ex. T-155, p. 45)

All parties on brief indicate a willingness to work on a permanent true number portability solution. The Commission asks that the parties, through the WECA docket and other forums, review the various trials around the country and to return to the Commission with a recommendation by July 1, 1996, for immediate implementation and funding of a true local number portability solution.

## F. DIRECTORY LISTINGS, DIRECTORY ASSISTANCE, OTHER DATA BASES

### 1. Positions of the Parties

USWC suggests that ALECs have several options for listing their customers' information in the U S West Direct directory, including negotiating with U S West Direct and purchasing USWC's listing services. (Owens, Ex. T-10, p. 50) This new listing service provides for a listing in USWC's voice and electronic directory assistance databases at a price of $0.75/month per business listing and $0.60/month per residential listing, plus a $5.00 non-recurring charge for each listing added or changed. (Ex. T-32, p. 56) USWC further argues that directory assistance and listings in directory databases and publications are not essential facilities because there are alternative providers.

GTE states that it plans to include new LEC customers in its directories and directory assistance databases because of the value that more complete information provides its customers. [Beauvais, TR., p. 1872, ll. 1-3]] GTE indicates that it is willing to enter into contracts with ALECs regarding the specifics of directory listings and the provision of directories.

The ALECs argue that its not economical to produce a separate published directory. They want their customers to be included in database, white pages, and simple listings in yellow pages, plus they want USWC and GTE to supply copies of the directories for distribution. These services should be provided free or at avoided costs. These parties, as well as Commission Staff, believe that USWC and GTE should provide directory assistance on the same terms and conditions that they provide directory assistance to other incumbent LECs.

Public Counsel wants consumers to have seamless access to directory assistance and white pages. Public Counsel recommends that the Commission mandate a unified white pages directory and ensure that USWC makes published directories available on an incremental cost basis.

MFS argues that directory listings should be free because incumbent LECs gain value in having a complete listing. USWC appears to agree with the notion that listings add value when it represented that U S WEST Direct's goal is to have complete and accurate listings of all of the consumers and businesses covered by its directories, regardless of whether a particular customer is served by USWC or an ALEC." (Owens, Ex. T-10, p. 50)

WITA states that the independent LECs are required to publish directories, and that all customers should be included in white page listings. It argues that access to directory assistance and data bases and the duty to publish one's own directory are items that should be competitively neutral, implying that they should be offered on the same terms and conditions.

## 2. Commission Discussion and Decision

Commission rule requires that a telephone directory be regularly published for each exchange, listing the name, address, and telephone number of the subscribers who can be called in that exchange. Additionally, the rule requires that subscribers be furnished with the directory or directories that contain listings for all subscribers who can be called toll free from that exchange. WAC 480-120-042

The Commission agrees that there are alternatives to published directories and directory assistance. However, there is a strong public and consumer interest in having a complete listing of subscribers for each local calling area available to subscribers. Commission rules enforce this interest by requiring that subscribers be provided the directories necessary to access all numbers within a local calling area. In the absence of a complete, unified listing, the incumbent LECs would have to acquire directories from every other telephone company providing service in that calling area and provide each subscriber with a set of such directories. USWC witness Owens agreed in cross examination that independent directories published by each ALEC will cause "some customer confusion." [TR., p. 341, ll. 15-16] We do not believe that a situation where multiple companies distribute different kinds of directories to all telephone customers in a calling area is practical, economically feasible, or desirable. Thus, while USWC may argue somewhat persuasively that directories and directory assistance are not essential, we do believe a unified directory database is essential.

To ensure that USWC, GTE, and all other LECs can continue to be in compliance with WAC 480-120-042, USWC and GTE must include all listings of telephone subscribers submitted to them by companies serving the same area served by the directory or database. This database of directory listings shall be the same that is provided to the company's directory publishing subsidiaries and other directory publishers. The Commission has no basis to determine if the rates for listings put forth by USWC are fair, just, and reasonable. When asked, the USWC witness did not know the incremental cost of the service. [Owens, TR., p. 278, l. 20] However, given that there is value associated with a complete listing and that USWC and GTE are required to provide complete listings to its subscribers, the Commission believes that simple listings in the published directories should be provided, without additional charge, as "in kind" compensation to the company providing the subscriber information. The Commission will not require GTE and USWC to supply extra copies of their directories to the ALECs or their customers. However, given that these directories also contain extensive advertisements, GTE and USWC have every incentive to ensure broad distribution of their publications.

Other directory assistance, line identification data base (LIDB), and operator services should be provided by USWC and GTE to ALECs on the same terms and conditions as they are provided to other incumbent LECs.

## G. THE COMPLAINTS

Three complaints are consolidated with USWC's tariff filing. TCG filed a complaint against USWC, and TCG and ELI separately filed complaints against GTE. The three complaints are nearly identical.

### 1. Allegations and Relief Sought

The complaints allege two causes of action, one claiming unreasonable prejudice, disadvantage, and discrimination, and the second claiming unreasonable and anticompetitive rates and practices.

#### a. Factual Allegations

The principal factual allegations are:

1. The incumbents are currently the de facto monopoly providers of switched local services within their Washington exchanges.

2. To provide switched local exchange service, the complainants must interconnect with the incumbents' switched networks and have mutual compensation arrangements with the incumbents for the interconnection.

3. During the summer of 1994, the complainants approached the incumbents to negotiate agreements for interconnection of the networks. The complainants proposed "bill and keep" at the end office as a means of mutual compensation for the interconnection.

4. [Re: USWC] USWC rejected TCG's proposal and offered the following counter-proposal:

a) TCG would pay USWC more to complete a call on USWC's network than USWC would pay TCG to complete a call on its network;

b) TCG would pay USWC switched access rates of approximately $0.021/minute of use, plus a $0.032/minute "lost contribution charge" to complete local calls, which creates a charge for local interconnection which is higher than USWC's current IXC access charges;

c) The $0.032/minute charge is designed to compensate USWC for lost profits on the sale of complex business line service, regardless of whether USWC's sales of that service actually decline; and

d) the $0.032/minute charge would be reduced only if USWC is allowed to increase residential rates, and would be eliminated entirely only when USWC is allowed to increase residential rates by 250%.

4. [Re: GTE] GTE rejected each complainant's proposal and offered the following counter-proposal:

> a) GTE and TCG would establish two separate trunk groups between their respective switching centers using Feature Group D signalling for the interchange of switched traffic -- one group would transport only toll traffic while the other group would transport only what GTE refers to as "local-like" and "EAS-like" traffic (alleged by TCG only);
>
> b) For intrastate "local-like" and "EAS-like" traffic, GTE would bill the complainants for terminating local (including EAS) calls based on GTE's access tariff or price list on file with the Commission, except that GTE would not bill the information surcharge and Carrier Common Line Charge (CCLC) rate elements; GTE calculates its rate at $0.0295291/minute. The complainants would bill GTE for terminating such traffic based on the complainants' access tariffs or price lists on file with the Commission (alleged by both TCG and ELI).
>
> c) The usage for "local-like" and "EAS-like" traffic would be measured where technical capability exists; otherwise, usage per port would be determined based on periodic studies of the quantity and direction of traffic, and billing would be based on those determinations (alleged by both TCG and ELI).

5. [Re: USWC] Despite further negotiations, USWC has refused to modify its proposal.

5. [Re: GTE] GTE and the complainants have been unable to reach agreement on the arrangements, terms, and conditions for interconnection.

6. The incumbents employ a "bill and keep" method of mutual compensation with other incumbent LECs for the exchange of local traffic.

7. The incumbents refuse to offer a "bill and keep" method of mutual compensation to complainants for the exchange of local traffic.

8. The incumbents' provision of interconnection with their networks for the purpose of terminating local traffic currently is a noncompetitive service.

9. The incumbents have proposed to charge the complainants more to complete local calls to complainants' customers than the incumbents charge other incumbent LECs.

10. [Re: USWC only] USWC refuses to pay TCG the $0.032 "lost contribution charge" to terminate traffic on TCG's network.

11. The incumbents offer many other local services, such as DSS or Centrex, some of the elements of which are comparable to the interconnection with their networks that the incumbents would provide the complainants.
12. The rate the incumbents propose to charge the complainants for interconnection exceeds the retail rate for the entire services of which these elements are only a part.

13. The rates the incumbents have offered to charge the complainants to terminate traffic on the incumbents' networks are far above the long run incremental cost of providing that service.

14. The incumbents have indicated that they would provide 9-1-1, TDD (telecommunications devices for the deaf) services, and directory listings and assistance, but have not made any proposal to the complainants regarding provision of these and other services that must be available upon interconnection and the exchange of local traffic.

**b. Causes of Action**

The complaints allege that the incumbents' refusal to offer "bill and keep" to the complainants subject them to undue or unreasonable prejudice or disadvantage in violation of RCW 80.36.170 and RCW 80.36.186.

The complaints allege that the following subject the complainants to undue or unreasonable prejudice or disadvantage in violation of RCW 80.36.170 and RCW 80.36.186 and are discriminatory in violation of RCW 80.36.180:

a) The incumbents' proposed mutual compensation for interconnection with the complainants.

b) The incumbents' interconnection rate disparity vis-a-vis services such as DSS or Centrex.

c) USWC's refusal to pay a $0.032 "lost contribution charge" while insisting on charging TCG that same charge.

d) GTE's requirement that local and EAS traffic be measured.

e) GTE's requirements for separate local and toll trunk groups for local and EAS traffic (alleged by TCG only).

f) GTE's refusal to provide "transiting" tandem switching services for EAS traffic that it provides to other local exchange companies (alleged by ELI only).

The complaints allege that the following are unfair, unjust, and unreasonable in violation of RCW 80.36.080:

a) The incumbents' proposed charges for network interconnection.

b) The rates the incumbents have proposed to charge the complainants to terminate traffic on the incumbents' networks.

c) The incumbents' refusal to provision 9-1-1, TDD, directory listings and assistance, and all other necessary services at existing rates.

The complaints allege that the following are anticompetitive:

a) The incumbents' proposals for use of excessive switched access rates.

b) USWC's proposal that TCG compensate USWC for the mere possibility of a $0.032/minute lost margin, i.e., that TCG insulate USWC from any effects of competition.

**c. Relief sought**

Each complaint prays for relief as follows:

An order from the Commission pursuant to RCW 80.36.140 and 80.36.160:

(1) ordering the incumbent to interconnect its network with the complainant's network in an efficient and cost-effective manner,

(2) establishing a fair, just, reasonable and nondiscriminatory reciprocal compensation arrangement for that interconnection, and

(3) requiring the incumbent to provide 9-1-1, TDD, directory listing and assistance, and other vital customer services upon interconnection at fair, just, and reasonable rates.

**d. Counterclaims and Third Party Complaint**

USWC and GTE deny the material allegations of the complaints and counterclaim for access charges.

GTE also brought a third party complaint against USWC, claiming that USWC is handing off to GTE for termination, traffic that originated on TCG's network that GTE is entitled to be compensated for terminating under its access tariff, and that USWC is not identifying the traffic so that GTE can bill for it. The reference is to traffic that would be EAS traffic if it originated on USWC's network.

**2. Positions of the Parties**

USWC contends that the complaints raise no issues not raised in USWC's direct case and presented by USWC for resolution. It argues that procedurally the Commission should dismiss the complaints as moot because the order on the issues raised by USWC in its direct case in support of its tariff filling will have addressed any issues presented by the complaints.

Regarding GTE's third party complaint, USWC argues that GTE offered no proof of any amounts owed by USWC and apparently wants the issue resolved going forward. USWC has no objection to the Commission resolving the principle.

GTE contends that the complainants have no standing to contest the reasonableness of the rate level which GTE proposes to charge for the termination of complainants' local or EAS traffic, and therefore the Commission has no authority to declare the rate level unreasonable and reset it. GTE reasons that while the Commission has authority under RCW 80.36.140 to determine upon complaint that a company's rates are unreasonable or discriminatory, RCW 80.04.110 specifically limits the Commission, in the case of private complaints as to the reasonableness of rates, to entertaining complaints which are signed by specified municipal officials or by a specified percentage of ratepayers. It argues that the complainants clearly do not comply with this requirement.

GTE contends that due to the procedural posture of this case and the complainants' lack of standing to complain about the reasonableness of rates, the Commission may reset GTE's contract local/EAS rate only if it finds that GTE's application of that rate is unduly discriminatory.

GTE contends that complainants have presented virtually no evidence in support of their allegations that GTE's local/EAS interconnection rate is unduly discriminatory. It argues that GTE currently provides no interconnection service to incumbent LECs for local traffic, because there is no intercompany local traffic among the incumbent LECs. "Thus, the contract rate at which GTE has offered to terminate complainants' local traffic cannot be discriminatory."

GTE argues that the only issue is whether its refusal to apply its EAS compensation arrangement to a situation outside the Commission's EAS orders constitutes undue discrimination. It argues that it does not. It argues that undue discrimination can exist only as to "like and contemporaneous service . . . under the same or substantially the same circumstances and conditions" (quoting from RCW 80.36.180), and that there is significant uncontroverted evidence on the record that the existing intercompany EAS compensation situation is substantially different from complainants' situation because 1) the participants in the current arrangement are LECs which do not have overlapping territories and which were not in competition for the provision of local exchange and other services when the arrangement was implemented, and 2) the EAS compensation mechanisms are based upon engineering cost studies specific to each EAS route.

GTE argues that issues of universal service and collocation were not raised in the complaints against it. It argues that unbundling and resale are not issues that were raised in the

complaints against it, and therefore no order may be issued in this case which directs GTE to unbundle any services or modify any of its tariffs' resale provisions.

GTE contends that ELI did not prove that GTE is unwilling to provide number portability. It contends that ELI's request that the Commission compel GTE to provide directory listings and assistance is a non-issue, because GTE plans to include ALECs' customers in its directory and directory assistance, and further, there is no legal basis for compelling GTE to provide those services to ALEC customers. It contends that complainants' testimony is devoid of any evidence to support the allegations that GTE has refused to provide them 9-1-1, TDD, and other services.

GTE argues that the only interconnection issues that are raised against it are compensation (discussed above), measurement of traffic (raised by both complainants), the use of separate toll and local/EAS trunk groups (raised only by TCG), and transiting tandem services (raised only by ELI). It contends that the complainants failed to prove their allegations on any of these points. It argues that the record establishes that GTE's use of measured rates would not unduly disadvantage the complainants. It argues that the record is clear that GTE and other incumbent LECs do not interchange local traffic, so no discrimination can be proved, and in any event, it is clear that GTE and other incumbent LECs utilize separate trunks for the toll and EAS traffic that they exchange, and that the use of separate trunks is reasonable.

ELI describes its complaint against GTE as a "friendly complaint" that "was brought primarily to ensure that the Commission had sufficient procedural basis to decide how local interconnection between GTE's network and the networks of the new entrants should be handled." It argues that its discussions of generic issues sufficiently addresses "all of the issues regarding GTNW that need to be addressed."

TCG argues that the record overwhelmingly supports the allegations of its complaints, that it has carried its burden of proof and is entitled to the relief requested in the complaints and recommended through its and other parties' testimony and in its brief.

As noted above, ELI and TCG both argue that the Commission, as a matter of competitive policy, should declare that existing local calling areas (i.e., EAS territories) apply to ALECs for purpose of distinguishing between local and toll calling.

Public Counsel is the only other party that specifically addresses the complaints and counterclaims. Public Counsel argues that the discrimination/preference/competition-based complaints of the ALECs present a close legal and factual question. It contends: "Their claims are likely meritorious, providing further justification for a bill and keep compensation arrangement."

Public Counsel analyzes the factual basis for the claim and the relevant statutes: RCW 80.36.170,.180,.186. It argues that what is "undue" discrimination or "undue" preference is at one level a policy issue to be decided by the Commission.

Public Counsel argues that the discrimination issue should be analyzed in the context of local calling areas prescribed or not prescribed by the Commission. It reviews how the Commission historically has established both local exchange areas and EAS routes. In both cases, the Commission focused on a community of interest, and created local exchange and EAS territories on a company specific basis. This made sense in an environment where companies operated in mutually exclusive service areas, but in the post-Electric Lightwave competitive environment, the Commission may wish to prescribe local calling areas for all telecommunications companies operating in a particular area.

It argues that in any event, since it is not mandatory under RCW 80.36.230 that the Commission prescribe exchange areas, and since it appears the new ALECs intend to voluntarily establish local calling areas consistent with those prescribed for others under RCW 80.36.230 and the EAS rule, the issue is neatly stated:

> May a telecommunications company maintain one compensation scheme with one telecommunications company relating to traffic it does not compete for, and another compensation scheme for a different telecommunications company relating to traffic it does compete for?

Public Counsel argues, at page 54 of its brief: "This is a close legal question. We conclude that different treatment of competitors compared to those who are not competitors could well be unlawfully discriminatory or unduly preferential or prejudicial. This is so for three primary reasons:

- The Legislature added RCW 80.36.186 in 1989, which has the effect of further emphasizing the general prohibition against discrimination and preference in other statutes, in a specific application to telecommunications companies which sell non-competitive services to each other.

- Requiring new LECs to use the LECs' access charge (i.e., usage) payment scheme when non-competing LECs use bill and keep puts unfair pressure on new LECs to price on a usage basis when their competitors have no cost reason to do so.

- There is no essential difference between new LEC "local traffic" and LEC "local traffic within a local calling area, including an EAS area."

Public Counsel also argues that "[i]t is true that significant public policies are at work in creation of EAS routes, and such routes are set as between specific companies. It is also true that 'obligation to serve' may be somewhat different between new LECs and incumbents. But the

public policy is to respond to customer needs and demands for local, flat-rated calling within their community of interest. The focus for discrimination should likewise be placed on the customer interest in the situation. The new entrants must attempt to attract the same customers as the incumbents, yet without the same compensation system. As WITA's witness concluded, an access, or usage based cost compensation `will lead to a shift from flat rate to measured service.' (Smith, Ex. T-157, p. 17) Incumbent LECs do not face this pressure in the bill and keep environment they enjoy."

### 3. Commission Discussion and Decision

#### a. The Complainants Have Standing to Complain of the Reasonableness of GTE's Rates.

The Commission finds GTE's standing analysis flawed. Its argument overlooks the "PROVIDED FURTHER" provision of RCW 80.04.110, which allows for complaints brought by competitors.[19]

#### b. The issues in the complaint against USWC are present in the tariff filing.

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[19] PROVIDED, FURTHER, That when two or more public service corporations, (meaning to exclude municipal and other public corporations) are engaged in competition in any locality or localities in the state, either may make complaint against the other or others that the rates, charges, rules, regulations or practices of such other or others with or in respect to which the complainant is in competition, are unreasonable, unremunerative, discriminatory, illegal, unfair or intending or tending to oppress the complainant, to stifle competition, or to create or encourage the creation of monopoly, and upon such complaint or upon complaint of the commission upon its own motion, the commission shall have power, after notice and hearing as in other cases, to, by its order, subject to appeal as in other cases, correct the abuse complained of by establishing such uniform rates, charges, rules, regulations or practices in lieu of those complained of, to be observed by all of such competing public service corporations in the locality or localities specified as shall be found reasonable, remunerative, nondiscriminatory, legal, and fair or tending to prevent oppression or monopoly or to encourage competition, and upon any such hearing it shall be proper for the commission to take into consideration the rates, charges, rules, regulations and practices of the public service corporation or corporations complained of in any other locality or localities in the state.

The issues raised in TCG's complaint against USWC are present in the tariff filing. The Commission's decisions on the tariff filing appear to resolve all issues in the complaint.

#### c. **The complaints against GTE are granted, in part.**

We grant the complaints against GTE as to the issue of compensation for the exchange of local traffic. We order GTE to interconnect with TCG, ELI, and other ALECs on a bill and keep basis, pursuant to the terms of this order.

The Commission's objections to any minutes of use compensation scheme, set out above, apply equally to the proposals of both GTE and USWC. Measured use interconnection rates are not cost based, require unnecessary and inefficient measurement, create a barrier to entry, and would threaten the state's public policy of affordable, flat-rated local service.

As is discussed above (at pages 40-43), the Commission also agrees with Public Counsel that it is discriminatory for GTE to exchange EAS traffic with incumbent LECs on a bill and keep basis and to refuse to exchange local traffic with ALECs on a bill and keep basis.

The Commission denies TCG's complaint with respect to GTE's requirement that TCG and GTE establish two separate trunk groups between their respective switching centers. It appears that the practice GTE proposes currently is necessary given the different rates and compensation arrangements applied to toll and EAS. Currently, incumbent LECs use separate trunks for exchanging local/EAS and toll traffic.

Regarding the complaints' allegations that GTE has failed to offer provision of 9-1-1, TDD, directory listings and assistance, transiting tandem services, and all other necessary services at existing rates, the record is insufficiently developed for the Commission to determine the merits of the allegations.

#### d. **The counterclaims and GTE's Third Party Claim against USWC are dismissed.**

We dismiss the counterclaims and GTE's third-party complaint against USWC. Our ordering bill and keep compensation and our determination that EAS traffic is local traffic for compensation purposes, render those claims moot.

# III. LOCAL TRANSPORT RESTRUCTURE

## A. INTRODUCTION

The local transport restructure, ("LTR"), is the term applied to USWC's proposed restructure of its access services tariff for interexchange carriers. It includes an unbundling of transport from the company's switched access charge, an increase in the local switching element

of the access charge, and a residual interconnection charge ("RIC") on switched access to make the filing revenue neutral.

Under the proposal, transport would be priced separately, and several transport options would be available to interconnecting carriers that chose to use USWC's transport. The local switching rate element will be increased from $0.0065/minute to $0.0100/minute. The RIC would be $0.0106/minute on every minute of local switched traffic.

As is noted above, USWC's proposed local interconnection service ("LIS") for local service competitors would incorporate the LTR's local transport options and local switching rate element.

The impetus for the LTR is a modification of interstate switched access service ordered by the Federal Communications Commission (FCC).[20]

## B. FCC DEVELOPMENTS

Switched access service was initiated in 1984 upon the breakup of the Bell System. The FCC established switched access charges to compensate the LECs for the cost of switching and transport, and to provide a contribution to the general revenue requirement of the LECs' local operations. Switched access rates are based on minutes of use and distance. From their inception, switched access charges have been a very large portion (40-50%) of an IXC's cost of doing business. (Wilcox, Ex. T-1, p. 17)

In Washington State, USWC filed and gained WUTC approval for intrastate switched access rates that mirrored the first interstate tariffed rates. According to USWC witness Wilcox (Ex. T-1, p. 17), the company's present switched access rates contain a very large amount of contribution to USWC's revenues above the cost of providing the service.

In 1992, the FCC began an investigation into whether there was a need to restructure interstate access rates. An FCC order released in October 1992 established an interim local transport structure that is set to expire at the end of 1995. That order unbundled local transport from the switched access charge. It identified and set interstate rates for different types of transport configurations. LTR provides separate charges for LEC entrance facilities (the splice and cable used to link the IXC's trunk to USWC's serving wire center), for direct trunked

[20] See, Transport Rate Structure and Pricing, Report and Order and Further Notice of Proposed Rulemaking, CC Docket No. 91-213, 7 FCC Rcd 7006 (1992) (Transport Order); Transport Rate Structure and Pricing, CC Docket No. 91-213, FCC 93-366, First Memorandum Opinion & Order on Reconsideration, released July 21, 1993 (First Reconsideration Order); and Transport Rate Structure and Pricing, CC Docket No. 91-213, FCC 93-403, Second Memorandum Order and Order on Reconsideration, released August 18, 1993 (Second Reconsideration Order).

transport between the service wire center and LEC end offices (at flat rates), and for tandem switched transport (at usage-sensitive rates). Both entrance facilities and direct trunked transport are provided at different capacity levels -- DS0, DS1, and DS3.

In an August 1993 order in FCC Docket 91-141, on expanded interconnection, the FCC adopted rules for switched transport collocation, allowing interconnection at LEC central offices. That change, together with the unbundling of transport, allowed IXCs to self provision all or part of the transport they need to reach LEC end offices and thereby avoid or reduce the transport charges they must pay the LEC.

The FCC's transport restructure results in an overall reduction in the revenues produced by the transport portion of the LECs' switched access service. The FCC introduced a transitional, residually-priced rate element called the "interconnection charge" to make up for the lost revenues. The FCC has indicated that this charge should be phased out over time in the interstate jurisdiction, allowing the industry to transition from its present configuration to one fully driven by competitive market forces.

## C. USWC'S LTR PROPOSAL

USWC proposes that the Commission allow it to adopt, on an intrastate basis, local transport restructure and a pricing structure for IXC switched access service that mirrors the FCC structure.

### 1. Transport Options

New transport charges, for carriers that choose to use USWC's transport, would fall into four categories:

1. Entrance facilities--to recover costs for the physical interconnection and cable USWC uses to link an IXC's premises to USWC's serving wire center (the USWC switching office closest to the IXC's Point of Presence). Entrance facilities would be available at DS0, DS1, and DS3 capacities. Entrance facility rates would be flat rates equal to existing market rates USWC charges for the comparable private line network access channel.

2. Direct trunked transport (DTT) option for interoffice transport between the serving wire center and USWC end offices. DTT is dedicated transport that reserves specific transmission capacity for the exclusive use of a single company. DTT would also be available at DS0, DS1, and DS3 capacities.

   USWC proposes to price DTT on a flat rate basis. There would be two rate elements for DTT: a fixed monthly rate, plus a "variable" charge per mile per month. USWC would charge rates that are the same as existing market rates charged for comparable private line services. The price relationships for the different dedicated transport services would not

be tied to the cost relationships for those services, but would take into account "market factors".

3. Tandem switched transport ("TST") option for interoffice transport. TST would carry calls between the serving wire center and USWC's end offices via USWC's tandem switch and common transport network.

   A TST customer could purchase DTT for the portion of the transport between the serving wire center and the tandem switch.

   TST generally would be used by low volume carriers that do not have sufficient traffic volume to any LEC end office to justify reserving individual trunk groups. Large IXCs likely would reserve individual (dedicated) circuit groups to the LEC end offices with large concentrations of long distance calling, but they also might rely upon TST for overflow.

   USWC has proposed to price TST on a usage sensitive basis, with separate charges for transmission and tandem switching. The two rate categories are:

   a) tandem transmission charges, which would be usage and distance sensitive. For each mileage band there would be fixed charges per minute of use plus "variable" charges for each mile per minute of use. USWC's proposal derives the rates from the DS1 and DS3 trunk transport rates (i.e., rates equal to comparable private line services); and

   b) tandem switching charge, which would be assessed on a per minute of use, and would be priced at ADSRC (average direct and shared residual cost) plus a contribution that USWC describes as "modest".

   USWC's pricing of tandem switching at LRIC (long run incremental cost) plus a contribution to USWC's common costs is a different approach than the approach taken by the FCC for initial tandem switching prices. The FCC ruled that the initial tandem switching price should be set to recover 20% of the tandem switching revenue requirement. Ms. Wilcox testified that USWC is taking a different approach because the FCC's approach produces an initial price that is below the long run incremental cost of the tandem switching function, tandem switching has now become a competitive function, with the FCC's unbundling of tandem switching elements, and USWC will be in an untenable position if it has to price a competitive service below cost. (Ex. T-1, pp. 29-30)

4. Multiplexer charge. Multiplexers put multiple voice or data channels over a single transmission medium (line or frequency), increasing the capacity of the transmission medium. Multiplexers also would be available at DS0, DS1, and DS3 capacity levels,

and would be priced at a flat monthly rate for Voice Grade-DS1 and DS1-DS3 connections. The prices are equal to existing private line rates for multiplexers.

Ms. Wilcox testified that USWC's pricing approach is consistent with the FCC's directive to base the dedicated facilities prices on special access (private line) prices. She stated that the rate relationships for the different dedicated transport services are not tied to the cost relationships for these services. The rate relationships are based on the underlying average direct and shared residual costs (ADSRC) plus a contribution to common costs, so that the prices in all cases cover costs, and the services that cost more are priced higher than those that have lower costs. She opined that it would be a mistake to price strictly in accordance with costs, as that would fail to take into account "market factors" that are equally important in setting an appropriate price. (Ex. T-1, pp. 27-8)

### 2. Increase in Local Switching Charge Element of Switched Access Rate

As part of the switched access charge restructure, USWC proposes to increase the local switching charge from $0.0065/minute to $0.0100/minute for all IXC traffic that originates or terminates on USWC's network. USWC witness Wilcox testified (Ex. T-1, p. 22) that the current charge of $0.0065/minute is among the lowest in the country, and provides a relatively low level of contribution to common costs of the firm in comparison to switched access service on the whole.[21] She also testified that increasing the switching element results in a lower RIC.

### 3. Introduction of the RIC

Ms. Wilcox testified (Ex. T-1, p. 31) that the transport restructure will cause a decline in transport revenues from $24 million to $5 million. Even with the proposed increase in local switching charge, USWC's LTR proposal would result in a negative impact on revenue requirements. To make the LTR revenue neutral, USWC proposes to introduce a "residual interconnection charge" element of its switched access charge. USWC would charge a RIC of $0.010243/minute on every minute of switched traffic. Ms. Wilcox testified (Ex. T-46, p. 31) that the RIC could disappear over time, and suggested that the time table for reducing the RIC and reducing other contributory elements could be determined in the company's pending rate case.

### 4. Elimination of Intra-LATA Foreign Exchange Service from Access Tariff

[21] On rebuttal, Ms. Wilcox testified that total transport contribution is nearly double the percentage contribution in the current local switching charge, and provided Exhibit C-47 in support of this statement.

Finally, USWC proposes to eliminate its intra-LATA foreign exchange service from the access tariff. Intra-LATA foreign exchange service allows a customer to draw a dial tone and telephone number from an exchange outside the customer's local calling area, but within the same LATA. Ms. Wilcox made several arguments in support of removing this tariff. First, she stated that intra-LATA foreign exchange service is not an access service. Second, she stated that this same service is available in the basic exchange tariff, and removal of the service in this tariff will eliminate offering the same service for different prices. Lastly, Ms. Wilcox stated that LTR will have a significant impact on these customers' rates, so eliminating the service should be done now, in conjunction with LTR. (Ex.T-1, pp. 23-24)

## D. POSITIONS OF THE PARTIES

### 1. IXC Stipulation

The IXC intervenors -- AT&T, MCI, Sprint, and the IAC -- recommend, via a stipulation, that the Commission defer action on the proposed LTR, and that rates for switched access service under the LTR be established in USWC's current general rate case. In the stipulation, they also state agreement on principles that should govern rates for switched access service under the proposed LTR in the rate case:

1. Costs for each element should be established by TSLRIC--or USWC's ASIC (average service incremental cost).

2. Each element should be priced at TSLRIC.

3. Universal service should be addressed in another docket.

4. If the Commission determines that any revenue in excess of TSLRIC should be recovered through access prices, any such amount should be identified and recovered through the CCLC. The other rate elements should be priced at TSLRIC. The CCLC should be phased out over two years, or the same period over which local rates are increased, whichever is shorter. In the event that USWC and GTE are allowed entry in the interLATA market, any remaining CCLC should be eliminated at the date of such entry.

5. Although parties recommend that prices for LTR rate elements not exceed TSLRIC, if the Commission nevertheless determines contribution should be included, the price difference between differing access configurations should reflect only the absolute underlying differences in TSLRIC cost.

### 2. Individual Positions

With regard to the IXCs' requested deferral of consideration of the LTR, USWC argues that a decision on the LTR should not be pushed off to further proceedings. USWC argues that the first step toward rational competitive interconnection policies is to integrate interconnection charges between wireline carriers (IXCs and ALECs). However, USWC argued that the current charges are too high and excessively bundled.

Responding to allegations that it has not properly priced its transport options, USWC argues that pricing involves considerable judgment, and is not black and white. It argues that there are several principles that should be observed:

1. Prices should not be set at incremental cost, unless that is the only price for which there is a demand.

2. No service should be offered for less than the incremental cost.

3. Normally, all services should provide contribution to shared and common costs, as well as the profit of the company.

4. This does not mean that markups need be uniform for all services. They should not be, when market factors are appropriately considered. This is where judgment comes into play, and the company's proposals in a dynamic competitive market should not be second guessed by the Commission unless they are manifestly out of line and will cause clear harm to specific public policies the Commission is charged with protecting.

Regarding allegations that the relationships between USWC's prices for DS1, DS3, and tandem switched transport disadvantages smaller carriers, USWC argues their witness Ms. Wilcox's Exhibit C-47 demonstrates that the critics have incorrectly analyzed the relative contribution levels between services and that contribution levels for the three transport alternatives are comparable, and the rates are not unreasonably or unduly discriminatory.

USWC argues that allegations of discrimination, which it defines as customers in the same class paying different rates for the same service, are not correct as a matter of law. For example, all DS1 customers pay the same rate. USWC argues that the three services being compared are different services, and do not involve different rates for the same thing.

USWC argues that its proposed transport prices are not excessive in the marketplace because 1) they are the same as for equivalent private line services, 2) they are lower than those charged by independent LECs, and 3) they are higher than those charged by USWC's current competitors, as shown by Ex. C-49. Therefore, the Commission should allow USWC to price these services to the dynamic market conditions, in order to maximize its participation.

USWC responds to a Commission Staff recommendation that it double DS3 rates. It contends that the recommendation is arbitrary and makes no sense, that no evidence has been provided to show the rates are under cost or have too little contribution. It argues that the

recommendation seems designed only to remove USWC from the dedicated transport market, as dedicated transport is the first service that competitors are targeting. It argues that it is not permissible for the state to use its power to purposely harm USWC's legitimate business, and that intentionally unbalancing the playing field against USWC is not the Commission's role under any of the State's statutes.

Concerning the proposed local switching charge increase, USWC argues that the current $0.0065/minute is among the lowest in the country, and below the $0.008357/minute approved at the federal level; that the increase results in a lower RIC; and that the cost:price relationship is reasonable, especially compared to other switched access rates.

USWC defends its RIC proposal. It argues that the Commission cannot adopt rates in this case that lower the Company's revenues, as the Company is entitled to earn a reasonable return, and there was no evidence presented that earnings are excessive. USWC argues that, as Ms. Wilcox testified (Ex. T-1, p. 31), under the transport restructure its transport revenue will decline from $24 mil to $5 mil. USWC argues that the RIC may be reduced over time as rates are rebalanced.

USWC opposes Commission Staff's proposal that it be ordered not to charge the RIC to companies who do not use USWC's transport facilities. It states several reasons for its opposition to that proposal: 1) It violates USWC's right to revenue neutrality; 2) It would be difficult and expensive to administer; and, 3) It would subject USWC to a competitive disadvantage. USWC argues that, furthermore, the Commission has long followed a policy that IXCs must make significant contribution to the support of the local network, from which those companies gain immense benefit. That absolute level of contribution needs to be reexamined in the rate case, but this is not the appropriate proceeding to reduce that contribution just for those companies that utilize non-USWC transport. Finally, USWC argues that their RIC is not a charge related to transport, that it merely represents a way to make the filing revenue neutral. Staff's recommendation does not serve to further any public policy goals, and its adoption would be improper.

Commission Staff concurs with USWC on the need for local transport restructure, and recommends that the Commission not delay a decision on the LTR. Staff agrees with the general concept of LTR proposed by USWC, but takes issue with several aspects of the Company's proposal, as described below. Staff argues that the suspension date of the present interconnection docket predates the suspension date in the rate case, so the Commission cannot simply defer consideration of these rates to a later date. Staff suggests that the Commission may revisit LTR later.

Regarding transport prices, Commission Staff argues that the relationships between USWC's proposed prices are inappropriate. Staff witness Selwyn testified that it is inappropriate to price LTR transport based on private line prices, as advocated by USWC, because private line and local transport markets are different, and are at different stages of competition. (Selwyn, Ex. T-114, p. 48)

Commission Staff contends that it is inappropriate to price DS3 and DS1 switched transport with varying levels of contribution. Staff advocates a 9.6:1, DS3:DS1 price ratio as the basis for determining if the proposed prices provide an unfair advantage to large IXCs, consistent with the FCC's order in the interstate local transport restructure proceeding, except as to the DS3 entrance facility rate. (Selwyn, Ex. T-114, p. 47) Dr. Selwyn testified that after examining USWC's updated cost studies, all DS3 transport (other than the entrance facility charge) falls significantly short of the 9.6:1 benchmark. (Ex. T-116, p. 3)

Commission Staff recommends that, in order that USWC's proposed prices pass the 9.6:1, DS3:DS1 benchmark, the Commission set all DS3 transport rates (other than the entrance facility charge) at twice the level proposed by USWC. Staff explains that its main concern is the relative pricing between DS3:DS1, not the absolute levels. It argues that the Company's pending rate case is the proper forum to reexamine the Company's switched access rate levels in general, when both the DS3 and DS1 transport rates could be reduced, while still maintaining an appropriate price ratio.

Staff supports statements by MCI witness Wood that USWC and other LECs should not be in the position to determine the winners and losers among IXC carriers.

Commission Staff urges the Commission to reject the proposed increase in local switching from $0.0065 to $0.0100/minute. Staff contends that USWC has not provided the Commission with any basis for a 57% increase in the local switching charge. It argues that the increase is an attempt to shift substantial amounts of contribution from local transport elements to local switching--a monopoly bottleneck service.

Commission Staff witness Lundquist characterized USWC's proposal to increase its local switching charge as odd, at best. (Ex. T-107, p. 32) Staff argues that USWC's position does not square with USWC witness Harris' testimony that switching costs have been declining dramatically in recent years. Mr. Lundquist performed a comparative analysis of contribution levels, which he testified does not support USWC's claim that the local switching charge provides a relatively low level of contribution. (Ex. T-107, p. 34) Staff argues that Mr. Lundquist's analysis shows that USWC employed contradictory tests for determining the appropriate level of contribution.

Relying on an exhibit showing local switching charges from many jurisdictions, Mr. Lundquist characterized USWC's local switching charge as "...admittedly toward the low end of the pricing spectrum..." but not "out of line" with other jurisdictions. (Ex. T-107, p. 36) Staff argues that USWC's argument lacks any analysis of why other states' charges are lower, or why those would be appropriate and the current charge is not.

Commission Staff supports a RIC, without enthusiasm, as the least objectionable way to achieve revenue neutrality, and because it is temporary until a decision in the general rate case. Dr. Selwyn testified that the RIC results in USWC's proposed LTR rates being no closer to the

economies of providing access service than the current access prices and structures. (Ex. T-114, p. 32)

Because it opposes an increase in the local switching rate, Commission Staff proposes a RIC higher than USWC's proposal. Staff calculates that the RIC would be $0.014073/minute, rather than $0.010574/minute proposed by USWC. (Wilson, Ex. T-155, p. 51) A lower switching charge than proposed would necessitate a higher RIC, to maintain revenue neutrality.

Commission Staff strongly objects to USWC's proposal to apply the RIC to all local switched minutes, regardless of whether that traffic is switched to USWC transport or a competitor's transport. It proposes that application of the RIC be limited to traffic switched to USWC transport facilities. Staff argues that applying the RIC to all switched minutes would inappropriately establish a protectionist policy which would insulate USWC from losses in any competitive local transport business. (Selwyn, Ex. T-114, p. 33) The RIC is to recover $14.8 million, while local transport is $4.3 million. The net effect is to negate USWC's "economically based" rate structure. Staff contends that its proposal could be accomplished by reprogramming the Company's interexchange access billing system. As an alternative, Staff suggests a self-reporting mechanism, which would require IXCs that purchase local switching to certify the percent of total switching minutes being completed on USWC transport facilities. This would be similar to the current percent interstate use factor IXCs use to separate intra and inter state traffic. Staff argues that USWC's allegations that these options would be costly and difficult to implement are unfounded, based on Ms. Wilcox's cross examination testimony that the company had collected no data and done no studies to support these allegations, and that she had no experience in reprogramming the company's billing system.

In response to USWC's contention that applying the RIC only on traffic switched to USWC transport facilities would put the Company at a competitive disadvantage, Staff makes two arguments: 1) Dr. Selwyn testified that Staff's proposal should not limit USWC's ability to compete in the transport market, but USWC's proposal would limit competitors' ability to compete; and, 2) Even if Staff's proposal resulted in a slight loss of market share for USWC, the Company would probably see an absolute gain in business, because competition will probably stimulate demand for telecommunication services. (Selwyn, Ex. T-114, p. 39) Staff also argues that the temporary nature of the RIC would have at most, a minimal impact on the Company.

Regarding USWC's proposal to eliminate its intra-LATA foreign exchange service, Staff recommends that the Commission deny the request. Staff expresses a concern about the revenue impacts of eliminating the service from the switched access tariff. (Wilson, Ex. T-154, p. 20) Mr. Wilson also testified that the Company provided no justification for the change.

Public Counsel generally supports USWC's local transport restructure proposal, except for the proposal to increase the local switching charge. Public Counsel does not argue against revenue neutrality, and agrees that a RIC is appropriate. However, because of opposition to the proposed increase in local switching, Public Counsel generally supports Staff's RIC calculation. While Public Counsel agrees that Staff's proposal to apply the RIC only to traffic switched to

USWC transport facilities is a theoretically sound approach, it takes no position on the issue. Finally, Public Counsel recommends that the policy decision on whether the RIC should be maintained indefinitely should be decided in the general rate case.

AT&T contends that the structure of USWC's proposed LTR is a good step, but that the prices are unacceptable. AT&T urges the Commission to reject the revisions proposed for switched access for several reasons. First, all parties agreed that TSLRIC is the proper cost basis for rational pricing. However, given Staff's testimony of its inability to obtain information to review costs, USWC has clearly failed to meet its burden of supporting its rates. Second, most parties disagree with the fundamental premise of USWC's "revenue neutral" filing. Given that USWC's revenue requirement is before the Commission in the Company's general rate case, the rate case would be the appropriate place to address USWC's switched access rates. (Sumpter, Ex. T-110, p. 13) AT&T also argues that the Commission can adopt local interconnect policies and rates, without changing access rates. Changing those rates for a few months after this case is concluded until the order in the rate case is issued is not an efficient use of resources. The proposed rates are so inequitable that IXCs support the continued application of current access charges. Moreover, unlike local interconnection, there are switched access rates currently in effect.

AT&T contends that USWC has the burden of supporting its rates and has failed to do so. Its cost studies are inadequate. Rather than moving toward TSLRIC prices as USWC contends, its proposal is an obvious attempt to foreclose any competitive alternatives that may emerge for the LTR functions. By doubling its local switching charge, IXCs will still pay USWC the same amount of money; it is just called something different.

AT&T recommends that if the Commission decides to adopt USWC's proposed LTR tariff, it should approve rates put forth by IAC witness Gillan as the rates that best support the approach in the IXC stipulation. AT&T opposes Staff's recommendation to double the proposed DS3 rates, in order to attain a particular contribution ratio with DS1 rates, as it would increase access charges, and is contrary to the record evidence supporting reductions in access rates.

MCI argues that USWC's LTR is driven by entrance of competition into the market for switched access service. MCI witness Wood testified that LTR would have several affects, one of which is that if excessive markups over cost are built into interconnection rates that competing companies pay USWC, customers (both companies and end users) will be denied the benefit of declining prices in a competitive market. (Ex. T-136, p. 31)

Regarding the price relationship between DS3 and DS1 transport rates, MCI argues that USWC's claim that competitive pressures are the impetus for its LTR filing is inconsistent with its proposal. MCI argues that Ms. Wilcox's statement that LTR rates have been set to exceed ADSRC plus contribution is contrary to the result in a competitive market. If USWC actually faced competition, the contribution rate elements should have dropped to slightly above TSLRIC to recover economic overhead associated with the service offering.

MCI argues that Ms. Wilcox admitted that its DS3:DS1 rates are not based on underlying costs, but on "market factors." MCI witness Wood testified that allowing an incumbent to use anticompetitive pricing strategies to eliminate existing competition, or prevent future competition, is indeed a use of market factors, but is a use that should be constrained. (Ex. T-136, p. 41) He testified that price differentials which track differences in cost are not inherently discriminatory, but USWC's proposed prices are discriminatory. (Ex. T-136, p. 42) If USWC is allowed to arbitrarily exaggerate the rate differential in its DS3:DS1 rates as it has proposed to do, it would provide USWC the ability to directly impact the level of competition by IXCs. MCI argues that this is poor public policy, and would direct rates away from cost based. Therefore, MCI recommends that the Commission adopt Dr. Selwyn's interim recommendation to double USWC's proposed DS3 rates, which should be followed by cost-based rates with proportional contribution based on new cost studies, to be filed within 30 days.

MCI opposes USWC's proposal to increase its local switching charge. MCI argues that USWC did not argue that the existing local switching charge was below TSLRIC, or that local switching costs have increased, and in fact testified that switching costs have been declining dramatically. MCI characterizes USWC's proposed switching charge increase as an attempt to redistribute the severely inflated levels of contribution present in existing switched access rates, which should be rejected.

Finally, MCI urges the Commission to reject USWC's request for revenue neutrality through a RIC. MCI agrees with Commission Staff that the RIC is a protectionist policy, which is not in the interest of long-distance users. Additionally, Mr. Wood testified that providing revenue neutrality through the RIC, when costs, such as switching, are decreasing, actually provides USWC with a guarantee of increasing profits. (Ex. T-136, p. 35) Thus, MCI recommends that the RIC be rejected, and recommends that the Commission proceed with cost-based rates.

Sprint, like AT&T, recommends on brief that the Commission reject USWC's LTR proposal, and set switched access rates in USWC's pending rate case. Sprint also supports the IXC stipulation that switched access elements be priced at TSLRIC, with any contribution flowing through the carrier common line charge, which should be phased out over two years.

Sprint agrees with the other IXCs that USWC's proposed transport rates are discriminatory, and will negatively impact competition. Sprint contends that USWC's cost studies show that per circuit, access cost differences between DS1 and DS3 are almost negligible, which indicates that 90% of the cost advantage bestowed upon large IXCs is unearned. Sprint agrees with IAC witness Gillan that the rates would not only result in diminished competition between large and small IXCs but also would result in fewer competitive options for less densely populated areas.

Sprint argues that contrary to USWC's statement that it is moving toward cost based rates, its LTR rates do not reflect the way costs are incurred, are not cost based, and do not encourage efficient use of the network. Sprint argues that USWC's rates would encourage a company to

purchase DS3 service at a point where the customer would utilize less than 20% of the available capacity. (McCanless, Ex. T-99, p. 9)

Sprint shares IAC's concern that USWC's proposal would have an adverse impact on non-urban competition.

The Interexchange Access Coalition (IAC), like the other IXCs, does not oppose the particular rate structure proposed by USWC. IAC does not oppose a revenue neutral component to the rates. However, IAC contends that the rates proposed by USWC for switched access service are unjust, unreasonable, unduly discriminatory, and anticompetitive. IAC further argues that USWC's proposed rates contain so much contribution, and are so discriminatory, that even main beneficiaries of the discrimination--the large IXCs--recommend that the Commission reject the rates as proposed, and accept the IXC stipulation.

IAC argues that while DS1 is generally provided by DS3 transport facilities, such provisioning could impose additional costs on the network. IAC is not opposed to prices reflecting such cost differences. However, IAC contends that USWC's rates are totally out of proportion with those additional costs. By seeking to recover more contribution from DS1 than from DS3 customers (who could bypass USWC's network), USWC is asking small users to subsidize access charge discounts to larger users. IAC argues that USWC did not dispute the fact that its proposed LTR rates would have a disparate impact on IXC competitors, and points to USWC's Owens statement that high volume end users are very sensitive to price. Therefore, argues IAC, USWC's proposed rates are unduly discriminatory, and are counter to the State's policy to promote diversity in the supply of telecommunications services and products in telecommunications markets, under RCW 80.36.300(5).

Responding to USWC's argument that the pricing is not discriminatory, IAC argues that transport is a singular service, regardless of the option selected -- DS1,DS3, or TST. As USWC is proposing to collect differing levels of contribution from the different services, its proposal is discriminatory.

IAC witness Gillan testified that another aspect of the proposed LTR rates is anticompetitive. Mr. Gillan argued that USWC's pricing will make it extremely expensive for IXCs to provide service to non-urban markets, where DS3 and DS1 transports are not economically viable:

> Even for AT&T, the DS3 transport option will be possible primarily in dense urban environments, while the tandem-transport option will typify the access arrangements used in smaller markets. As a result, increasing the price of the tandem transport option will increase relative cost to serve less populous areas. Inflating the cost to serve small markets will ultimately lead to fewer choices in rural areas or lead to de-averaged retail rates that exceed any underlying differences in costs.

(Gillan, Ex. T-95, p. 14)

IAC also argues that USWC's proposed LTR rates would result in inefficient use of the public switched network. IAC contends that use of the network will be efficient only if the price differences between interoffice transport options reflect the underlying cost difference. Thus, USWC's proposed rates create incentives for the inefficient use of the network, contrary to RCW 80.36.300(2), which states the policy to maintain and advance the efficiency...of the telecommunication service.

IAC argues that in addition to adversely affecting the competition for intrastate toll, USWC's proposal would adversely affect local competition, through the same discriminatory pricing mechanism.

The ALECs contended at hearing that USWC's proposed LTR transport charges, which are incorporated into the LIS, are inaccurately priced, particularly the rate for tandem switched transport. The new entrants are likely to want to interconnect at the USWC tandem for efficiency reasons. They then would not need to connect directly to every USWC end office or to every other LEC and IXC. USWC proposes to price the transport between its tandem and its end offices at private line market rates. The ALECs contend that tandem switched transport should be priced at cost.

MFS urges the Commission to order cost based rates for transport services. MFS characterized the FCC's RIC as a poorly conceived political compromise, with no cost justification, and recommends that the Commission reject all non-cost supported subsidies like the RIC.

TRACER takes issue with Staff's proposal to double USWC's proposed DS3 transport rates. TRACER argues that no party contends DS3 prices are below cost, or that the DS3 price is itself inappropriate. Rather, the complaints are that the contribution per channel is different. TRACER argues this provides a rationale for decreasing DS1 rates, not increasing DS3 rates.

Regarding the relative contribution in rates between DS3 to DS1 rates, TRACER argued that there are legitimate reasons why contribution in DS3 rates might be less than 28 times that in DS1 rates. Dr. Zepp testified:

> When...a large group buys a DS3 they take the risk that they totally fill that DS3 and therefore they are fully paying for it. There is no unused capacity as far as US West is concerned. US West has sold it all and it's fully compensatory, whereas the DS1, US West is taking that risk, and therefore they've got to take that into account when they do the pricing.

[Zepp, TR., p. 2124]

TRACER also argues that an unjustified doubling of the DS3 rate would provide a customer with alternatives to seek other providers. It argues that Staff's proposal to double the DS3 rate is unwarranted and should be rejected.

DOD/FEA characterizes USWC's proposal to increase its local switching charge as an abuse of monopoly power.

## F. COMMISSION DISCUSSION AND DECISION -- LTR

The Commission would have preferred to have dealt with Local Transport Restructure issues in a separate proceeding devoted to LTR, or in the general rate case. LTR will have a significant impact on intrastate toll competition in Washington. We see no legitimate justification for dropping it into a docket that primarily concerns local interconnection.

Based on the record in this proceeding, the Commission identifies five issues which must be decided in this Order:

1. Should and can the Commission defer consideration of the LTR to another proceeding?
2. Are the transport options properly priced?
3. Is the need for and amount of the proposed increase in the local switching charge supported?
4. Is the need for and amount of the RIC supported? If so, should the RIC be imposed only on traffic switched to USWC transport facilities, or on all local switched traffic?
5. Should USWC be permitted to eliminate intraLATA foreign exchange service from its switched access tariff?

We reject USWC's LTR tariff for many reasons described below. We will provide discussion on the topics listed above, and also provide some policy direction concerning how the LTR rates should be approached in USWC's general rate case.

First, we disagree with USWC's basic premise to base LTR rates on existing private party line rates. We agree with Dr. Selwyn that it is inappropriate to price LTR transport based on private line prices. Private line and local transport markets are different, and are at different stages of competition. (Ex. T-114, p. 48) Further, we reject USWC's position that it makes more sense to use the private line prices than to start from scratch. Restructuring USWC's local transport rates will have a large impact on the direction of intrastate toll market. Thus, we would have expected USWC to provide rates based on sound economic and public policy considerations, and have supported those rates with proper, fully supported incremental cost studies. Instead, USWC's proposal is based on rates from services that serve different markets, the proposal uses inappropriate "market factors," and it is not supported by adequate cost studies. The Commission expects USWC to correct these problems in its general rate case.

We agree with AT&T that it would be inefficient to adopt LTR rates in this proceeding. The rates would most likely change in USWC's pending rate case, especially given the magnitude of the RIC. Staff witness Selwyn's testimony (Ex. T-114, p. 32) that the RIC results in USWC's proposed LTR rates being no closer to the economies of providing access service than the current access prices and structures also supports this result. We also find persuasive AT&T's argument that USWC's proposed LTR rates are so inequitable that the IXCs supported the current, bundled rates. Restructuring USWC's access rates in the presence of an economically overwhelming RIC provides no benefits to switched access customers, as evidenced by the IXC stipulation, and obviously does not benefit the public in general.

The inefficiencies embedded in the LTR rates proposed by USWC are so great, that we find the public interest best served by endorsing the general structure proposed by USWC for its LTR tariff, while rejecting the tariff as filed. We here provide guidance for revisiting the question in USWC's general rate case, where determining specific LTR rates will be economically meaningful.

We agree with USWC that considerable judgment is involved in pricing, that it is neither black nor white. Further, we agree with USWC that the Commission must intervene when a regulated company's proposed rates are manifestly out of line with, and will cause clear harm to, specific public policies the Commission is charged with protecting. USWC's proposed LTR rates clearly contradict two specific public policies the Commission is charged with protecting.

First, several parties convincingly argue that USWC's proposed rates would inappropriately favor large IXCs at the expense of small IXCs, resulting in diminished competition for intrastate toll services. While we are not persuaded by Staff's proposal to double DS3 rates to obtain a 9.6:1 cost ratio to DS1 rates, it is important to note that USWC's rates fail to meet the relative price ratio described in more detail below. As IAC points out, the failure of USWC's rates to meet this relative price ratio is significant because, as USWC witness Owens stated, high volume end users are likely to be very sensitive to price. USWC has proposed to use "market factors" to collect significantly more contribution above TSLRIC from IXCs using lower-level transport options, than those using the DS3 levels. We agree with IAC that this clearly indicates USWC's proposal would have a detrimental effect on smaller IXCs, with no justification other than USWC's "market factors." An added concern is the negative impact USWC's rates would have on services to less populated areas, as described by IAC witness Gillan. We agree with MCI witness Wood that USWC should not be allowed to exercise its market power by applying mark-ups so as to artificially eliminate or prevent competition. Approving a proposal that would result in less intrastate competition, and less competition in less densely populated areas, clearly would be contrary to the "promote diversity" public policy set out in RCW 80.36.300 (5).

Second, Sprint articulates another reason why we should reject USWC's proposal. USWC's proposed pricing for transport options would push carrier customers to purchase DS3 capacity service at a point where it would utilize 20% of the available capacity for that service. If this excess capacity occurred because prices were consistent with price ratios from the underlying TSLRIC relationships, one might argue that the excess is economically efficient. However, this

excess capacity is not driven by costs. It is driven by USWC's application of "market factors," which implies the excess capacity is inefficient. Thus, USWC's LTR rates clearly conflict with another telecommunications public policy, RCW 80.36.300 (2): "Maintain and advance the efficiency and availability of telecommunications service."

We provide the following guidance regarding how LTR rates should be established in the Company's rate case. First, the Commission cannot accept rates that would produce the results we have found unacceptable in this proceeding. Second, as discussed above, while Staff's 9.6:1 cost ratio between DS3 and DS1 rates may be useful in gauging rates, we are not persuaded that this ratio should be the basis for setting the rates. The argument is superficial in terms of underlying costs of providing different service levels. It appears that the 9.6:1 cost ratio may avoid some anticompetitive problems from the FCC's perspective, but the approach seems as arbitrary in this proceeding as USWC's "market factor" approach.

With regard to the principles advocated in the IXC stipulation, we agree that costs for each of USWC's LTR elements should be established at TSLRIC, not USWC's surrogate, ADSRC. We believe that TSLRIC is an appropriate price floor for these elements, but at this time do not believe that prices should be established at the bare minimum. We agree with USWC that it has long been the policy of this Commission that interexchange carriers must make significant contribution to the support of the local network, from which they gain immense benefit. Further, we are not persuaded by any evidence on this record that the public interest is best served by abandoning this important policy.

We do not reach the question whether the public interest is better served by spreading the contribution from switched access among the LTR elements (according to some underlying cost justification), placing all of the contribution onto a specific charge (such as the local switching charge), or a combination of those options. However, if prices are to be set higher than TSLRIC (or, in other words, are to include some level of contribution), the relative price ratios between DS3 and DS1 transport elements are important. We are persuaded by the IXCs and Staff that if DS3 to DS1 relative price ratios become too small, it will have inappropriate, negative impact on small IXC competitors and competition to less urbanized areas. The question then becomes what is the appropriate relative price ratio? As mentioned above, the Commission rejects Staff's use of the FCC's 9.6:1 price ratio. General microeconomic theory discusses the importance of relative prices, in that changes in relative prices will affect purchasing decisions, and efficient purchasing decisions would be based on relative incremental costs. Thus, economically efficient purchasing decisions between DS3 and DS1 transport would be based on the underlying TSLRIC ratios of the individual LTR components. Such a price ratio would help to minimize any potential economic distortions from pricing above TSLRIC. If we had confidence in USWC's cost estimates, these relative price ratios could be obtained using Exhibit C-100, by dividing the TSLRIC of each DS3 transport component by the TSLRIC of the corresponding DS1 component. The Commission believes the TSLRIC ratio should be the threshold, below which relative prices between DS3 and DS1 transport components should not fall. This should be the case until such time as the transport market exhibits highly competitive attributes. While the Commission is adopting this relative price ratio as a minimum, we are undecided if the price ratio should be

allowed to rise above the relative TSLRIC ratio, and would welcome discussion on this topic in USWC's general rate case, where we assume proper cost estimates will be available.

We are not persuaded by AT&T's argument that interconnection rates for local and long distance should come together and be priced at TSLRIC at some time in the future. It should be clear from the discussion above that we believe IXCs derive significant benefits from having access to local exchange company networks, and thus should contribute a fair share toward the common costs required to provide those networks. Also, at this stage of a rapidly changing market, it is uncertain whether the rates for local and long distance will converge over time. These are different markets, competing in different ways. If, when, and how such rates may converge remains to be seen.

We reject USWC's proposal to increase the local switching element of its switched access charge from $0.0065 to $0.0100/minute. USWC's proposal is a step toward economic inefficiency, which the Commission must be particularly mindful of in an increasingly unbundled and competitive market.

USWC provides no cost justification for increasing the local switching charge by 57%. USWC's arguments in support of increasing the local switching charge element are not persuasive. USWC witness Harris testified that switching costs are declining.[22] His testimony provides justification to decrease the local switching charge, not to increase the rate by 57%.

To support its proposal to increase the local switching charge, USWC argues that the level of contribution from the current local switching charge is too low, relative to contribution the Company seeks to recover from transport functions. In support of this argument, Ms. Wilcox provided Exhibit C-53. This exhibit is a poorly supported chart, based on total contribution rather than contribution from each element. It does not justify the proposed increase. The Commission rejects this argument for several reasons:

First, USWC's assertion that local switching provides less contribution than transport is based on comparisons of prices to ADSRC, rather than to the appropriate TSLRIC costs, which renders the comparison useless. Proper comparisons using TSLRIC were not provided in this case. Even if such comparisons had been presented, we believe any such comparison would be highly suspect. We have very little confidence in the cost studies USWC utilized for its case.

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[22] Dr. Harris wrote: "The application of transistors, semiconductors, integrated circuits and other microelectronics in telecommunications equipment has dramatically reduced switching and transmission equipment costs...." (Ex. T-10, p. 5)

Second, we are especially concerned about USWC's local switching cost estimates. Given Dr. Harris' testimony that local switching costs are declining dramatically, there is a significant risk of an upward bias in the switching cost estimates, which would result in the analysis of contribution from either the current or proposed local switching charge being unreliable.

Third, the Commission finds that USWC has employed contradictory and confusing tests to determine appropriate levels of contribution. USWC witness Wilcox testified that while she does not advocate equal contribution for LTR components, the switching charge should be increased because the differences in contribution levels are too great. (Ex. T-46, p. 28) When we examine Exhibit C-100, we note that the percentage contributions for all transport options exhibit a large range. The contributions from both the current and proposed switching charges lie within that range. Thus, even if the Commission had some confidence in the cost estimates provided, we are left to wonder what upper and lower bounds USWC believes contributions from LTR components (or subsets of components) should lie within, and the theoretical basis for those subsets and boundaries. Without providing these bounds and subsets, and its reasoning for the bounds and groupings, USWC's argument to increase the local switching charge based on relative contributions of other LTR components is, indeed, contradictory.

Fourth, the argument to increase the local switching charge because it provides relatively less contribution than does transport is weak. The Commission finds USWC's testimony that local switching costs are declining dramatically a much stronger argument for what direction the switching charge should be moving.

USWC's final attempt to justify an increase in the local switching charge is a comparison of such charges in other states. It argues that an increase is justified because USWC's local switching charge is lower than switching charges in most other states. Perhaps if USWC had provided some explanation of why several other states have higher local switching charges, and why such charges provide benefits to the citizens of those states, this position would have some meaning. However, we do not find that such a bare comparison in any way justifies any increase, and certainly not an increase of 57%, when the service is exhibiting dramatically decreasing costs.

The Commission's decision to disallow an increase in the local switching charge is for purposes of this proceeding, based on USWC's inadequate demonstration here. We do not rule out raising the local switching charge in the general rate case as a way to obtain contribution from switched access customers. As stated above, IXC carriers derive large benefits from the local network, and should contribute to the financial support of that network.

The final issue regarding LTR is USWC's proposal to eliminate its intraLATA foreign exchange service from the access tariff. Staff recommended that the Commission reject this proposal as the revenue impacts were unknown. (Wilson, Ex. T-154, p. 20) No other intervenor party presented any discussion or recommendation of this proposal. Ms. Wilcox's

recommendation that the service be eliminated was based on the LTR being implemented. Since we are rejecting USWC's LTR tariff, there is no basis for accepting the intraLATA foreign exchange service proposal. We agree with Staff that this issue should be addressed in the rate case, where the revenue impacts can be managed in the context of total revenue requirement.

## IV. EXPANDED INTERCONNECTION/ VIRTUAL COLLOCATION

### A. INTRODUCTION

USWC has filed tariff revisions that would make available expanded interconnection and collocation opportunities for the first time on an intrastate basis in Washington. This offering holds the potential for companies to use alternative transport facilities (facilities other than those of the incumbent LECs) and then interconnect to the unbundled portion of the incumbent's network that they wish to use.

USWC envisions that new LECs that self-provision transport to the USWC end office would have to purchase virtual collocation services. This would include an entrance facility charge, an equipment charge and expanded interconnection channel termination.

There are two types of collocation. Physical collocation arrangements allow an interconnector full ownership, access and control of the transmission and circuit termination equipment installed in the incumbent central office for its dedicated use. Under a virtual collocation arrangement, the interconnector requests that the LEC install its desired equipment in the central office and the interconnector is denied direct access to the collocated equipment. Ownership, maintenance, and monitoring of the equipment is controlled by the incumbent.

USWC proposes offering only virtual collocation. USWC argues the Commission has no authority to mandate physical collocation, and that mandates or incentives to USWC to allow physical collocation would be an expropriation of USWC's property.

At least two courts have held that the ordering of physical collocation can violate telecommunications companies' property rights. Bell Atlantic Tel. Co. v. FCC, 24 F.3d 1441 (D.C. Cir. 1994); GTE Northwest Inc. v. PUC of Oregon, 321 Or. 458, 900 P.2d 495 (1995).

Commission Staff recommends that the Commission not consider physical collocation in this docket, because none of the parties who would benefit from it (other than AT&T) argue for it.

AT&T argues that the Commission should order USWC to file tariffs for both physical and virtual collocation. Public Counsel argues that the Commission should not require physical collocation at this time, if for no other reason than to avoid protracted litigation.

Parties have raised other concerns about the specifics of the USWC's tariff, including the tariff's handling of liability, the time frame needed for USWC to respond to requests for new IDE, criteria by which space and requests are accepted or rejected, procedures for certifying contractors to install and maintain collocated IDE, training of employees and whether the purchase of an expanded interconnection channel termination ("EICT") avoids the application of other switched access rate elements.

### B. COMMISSION DISCUSSION AND DECISION -- EXPANDED INTERCONNECTION/COLLOCATION

The Commission agrees with Public Counsel regarding physical collocation but would like to note that during the development of expanded interconnection rules the Federal Communications Commission concluded that physical collocation was the best means for ensuring a fair basis for competition in the provision of interstate access service because it avoided the operational complications associated with one company relying on a competitor to install, maintain and repair their equipment. (Lundquist, Ex. T-107, p. 9)

We also agree with Public Counsel's argument that there is no reason that virtual collocation should cost any more than physical collocation.

USWC originally proposed virtual collocation rate levels which mirrored its original FCC filing that was suspended by the FCC and later substantially reduced. On rebuttal USWC modified the rates to reflect the same overhead loading factor of 1.2 used to set the Company's interstate rates. The Commission adopts Staff recommendation to accept the loading factor but not the rates USWC proposes. The Commission agrees with Staff that the rates should be reduced further, to reflect total service long run incremental cost results using the recommendations by staff and discussed in greater detail in the next section of this order dealing with cost studies.

USWC also revised its proposal to include a lease back method that would allow inter-connectors to purchase collocation equipment. In addition, the new proposed tariff includes a switched access DS0 EICT upon receipt of a bona fide request. The Commission approves of the USWC modifications but other changes are needed to make the tariff acceptable. During cross examination, USWC's counsel affirmed the company's willingness to negotiate with parties on concerns regarding tariff language, including language dealing with dispute resolution. [TR., p. 1983 ll. 1-3]

The Commission accepts USWC expanded interconnection tariff contingent on the company refiling rates consistent with the 1.2 factor using TSLRIC, consistent with the guidelines established in the next section, and on resolving the tariff language concerns raised by parties in this proceeding.

The Commission is uncertain whether virtual collocation is necessary when local exchange companies interconnect. If meet points are established by mutual agreement, the

decision about what equipment resides where will be part of that negotiation, and it is unlikely that the virtual collocation tariff would need to apply.

## V. COST STUDIES AND IMPUTATION

### A. USWC'S COST STUDIES AND POSITIONS OF PARTIES

USWC has submitted cost studies in support of the rates it proposes in this proceeding. The company proposes the use of average direct and shared residual costs (ADSRC) as target price floors. (Farrow, Ex. T-23, p. 9) Several parties disagree with USWC's cost determinations and/or use of costs in this proceeding. They argue that TSLRIC, not ADSRC, is the appropriate measure of cost. See, e.g., Bourgo, Ex. T-127, pp. 4-6. They argue that the company's measurement of costs is inappropriate and inconsistent with previous Commission orders. See, Ex. TC-155 (Wilson). Further, several parties argue that prices should be set at cost, or with small uniform levels of contribution. (Zepp, Ex. T-151, p. 5)

USWC has divided its total company costs into three groups. The groups are: 1) Direct costs of the specific product; these include both fixed and variable costs. 2) Shared residual costs or product family costs. These costs include those non usage sensitive costs related to providing the service for at least two products. 3) General overhead/common costs. These costs represent expenses that cannot be directly tied to a product or family group of products. USWC's studies in this proceeding measure the direct and shared residual costs of providing each product. These costs are unitized to equal the average direct and shared residual costs (ADSRC). ADSRC does not include the common costs of the company. (Farrow, Ex. T-23, p. 7)

Other parties in this proceeding support the use of LRIC (long run incremental cost) or TSLRIC (total service long run incremental cost). As used by these other parties, LRIC and TSLRIC do not include the shared residual costs included within the company's cost studies. LRIC and TSLRIC refer to the costs associated with providing the particular product or service that could be avoided in the long run if the product or service were not offered. A USWC version of TSLRIC is referred to as TSIC, total service incremental costs. (Wood, Ex. T-136, pp. 3, 15) Another term used by USWC is ASIC, average service incremental costs. ASIC is a USWC term which represents the unitized level of TSIC.

The parties that support LRIC or TSLRIC argue that ADSRC, which includes shared residual costs, is not the economic or correct price floor. They argue that shared residual costs included within the company studies cannot be avoided by USWC if the service is not offered. Mr. Wood for MCI-Metro testified that the fundamental concept of cost causation is ignored in the studies performed by USWC using Mr. Farrow's methodology. (Wood, Ex. T-136, pp. 3-5)

USWC argues that there are just three issues on measurement of cost. Those three are cost of money, depreciation, and the level of "fill" (average or objective).[23] The company argues

[23] It is the Commission's understanding that "fill" represents the utilization of a given capacity

that authorized return has nothing to do with the cost of money on a going forward basis. It argues that the cost of money in a cost study should be the cost of obtaining the money in markets going forward. (Farrow, Ex. T-23, p. 17) The company argues that approved depreciation has nothing to do with the prospective lives. The company also argues that average fill is correct, that the system will never be designed for objective fill, and that spare capacity is a necessity. Further, it argues, the Commission requires USWC to provide service on demand. Without spare capacity, timely implementation would be impossible, and further would be more costly. The company argues that there is no evidence that USWC has improperly invested in any plant.

Several parties argue that the company's studies fail to use Commission approved depreciation, authorized return, and objective fill. The studies were not consistent with Commission orders in Docket No. UT-930957, et al. Public Counsel states that it sees little distinction between SRC and common costs. Staff Witness Wilson testified that the company's use of cost of money and depreciation rates in excess of those authorized overstates the level of costs, and that the use of average fill implies that excess capacity is included within costs, thus increasing costs. (Wilson, Ex. TC-155, p. 6)

Several parties argue that the studies are inappropriately cryptic. In general, they refer to the inability of the parties to review the contents of the studies or to run alternatives. Public Counsel describes this as the "black box". Staff argues that they were not allowed to see costs of some vendors, and that they could not run studies as studies were not available on personal computers. Staff argues that there are no lists of what families are, and there is no justification to assign or allocate spare capacity in a similar fashion to traffic sensitive costs.

USWC argues that cost-based rates do not mean rates at costs. It argues that the precision of the cost studies is not all that relevant unless the Commission accepts the extraordinary assertion that rates for switching and transport be set at cost with no contribution to shared and common costs. They argue that no multi-product firm should be allowed to price any product at incremental cost unless no units would be sold at any higher price. They argue that none of the company's competitors can point to any instance where the competitors price at incremental costs, and that large competitive companies do not strive to price their products at cost.

Several parties in this proceeding argue that pricing should be based on TSLRIC. Some argue that it is inappropriate for competitors to be required to pay prices that increase another

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(trunking capacity, switching capacity, etc.). Average fill represents the actual usage of the system over an historic period. Average fill tends to be lower than objective fill, which represents the intended level of utilization if the system were operated at its optimum.

competitor's profits. They argue that ADSRC includes contribution to USWC's overhead and profit. See, e.g., Zepp, Ex. T-151, pp. 16-17.

While Public Counsel states that recovery of shared residual costs through pricing is not improper, it argues that shared residual costs should not be included in costs studies as a basis for pricing. Public Counsel further argues that contribution levels above TSLRIC are appropriate but not in the fashion presented by U S West through use of its ADSRC studies.[24]

## B. COMMISSION DISCUSSION AND DECISION -- COST STUDIES

USWC's presentation is inconsistent with economic theory and inconsistent with previous orders of this Commission. As this Commission has found in the past, and as many witnesses in this proceeding testified, the appropriate measurement of costs is TSLRIC.[25] USWC has not presented TSLRIC cost studies in this proceeding. The ADSRC studies supported by Mr. Farrow include costs that he conceded would not be avoided if the product or service were not offered, and are not the economic price floor but rather U S West target price floors. (Farrow, Ex. T-23, p. 10) The company studies include the components TSIC, and its unitized version, ASIC, which appear to be consistent with the economic theory of TSLRIC. However, the Commission is concerned with the calculation of these costs.

In Docket Nos. UT-93057, UT-931055, and UT-931058, the Commission stated:[26]

> The Commission agrees with Commission Staff and other parties that the company's cost studies on Network Access Channel, Channel Performance, and Transport Mileage were flawed and should be rejected. [footnote omitted] These

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[24] In its brief, Public Counsel states: "So, while the issue of recovery of these so-called `shared' costs remains an issue to be dealt with in any analysis of appropriate contribution levels ...."

[25] WUTC v. U S WEST Communications, Inc., Docket Nos. UT-930957, 931055, & 931058, Fourth Supplemental Order (September 1994). See, e.g., Ex. T-138 (Wood)

[26] Id., at p. 13.

> studies do not provide the Commission a sufficient basis upon which to set cost-based rates.

In that order the Commission rejected the company's use of average fill, non authorized depreciation rates, and a cost of money other than that authorized by the Commission. The order also required the company to use the hypothetical capital structure that was used to develop the authorized return of 10.53% in Consolidated Docket Nos. U-89-2698-F and U-89-3245-P.[27]

The Commission generally continues to hold that view. The Commission does recognize that the cost of money needs to be looked at in a similar forward-looking fashion as other costs in a TSLRIC study. The Commission recognizes that the authorized return is based on embedded costs, particularly with respect to debt rates. The Commission believes that it may be appropriate to take a forward-looking review of the cost of money. However, in this proceeding the company has provided no evidence to support any change in the cost of money, either with respect to cost rates for debt or equity, or with respect to a change in the capital structure. The Commission does not suggest by this order that the company should, with each or any cost study, file revisions to its equity rates or capital structure. These costs levels are more appropriately set in general rate proceedings or separate rate of return proceedings.

The Commission generally agrees with Public Counsel's position on the use of cost studies for pricing. It is not improper to price at a level to recover prudently-incurred shared and common costs. In this proceeding, the level of contribution has been nearly impossible to review. What is an appropriate level of contribution? How much total contribution is needed to recover shared and residual costs? What level of contribution is included within other monopoly and competitive services provided by the company? What costs are direct? And which are shared or common? When looking at exchange service, is the local loop a direct or shared cost? What other policy issues need to be considered in the determination of contribution? The Company has not provided sufficient information for the Commission to be able to answer these questions. Therefore, the Commission is unable to determine the appropriate level of contribution for any service presented to it in this proceeding.

The Commission also notes testimony, including Staff witnesses Wilson and Selwyn, (Exs. T-154 and T-114) and ELI witness Montgomery (Ex. T-84; TR., p. 1139) among others, to the effect that USWC cost studies are difficult to review and to work with. As stated by Public Counsel, the company presented the proverbial "black box", which limits the ability of other parties to review and to independently test and verify the assumptions in the company's cost studies. The Commission adopts Commission Staff's recommendation that it order the company in future cost studies to comply with the recommendations for open access to the company's cost methodology, input data, assumptions, and cost modeling recommended there. These filings

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[27] Id. at p. 14, footnote 12

should include the full and complete set of work papers and supporting source documents, to be filed simultaneously with the results of the study.

For reasons set out above, the Commission is unable to identify the cost of the various products or offerings in this proceeding. The Commission also is unable to identify the proper level of contribution to be allowed in the prices of these various products or offerings. The Commission orders the company to file future cost studies consistent with this order. These studies should be TSLRIC studies, and as such should not include shared residual or common costs. The company should recognize that its protracted inability to produce respectable, auditable, "checkable" cost studies is detrimental to its own self interest. It must do better in this regard if it expects to fare better in persuading the Commission of the rightness of its positions.

## C. IMPUTATION

USWC did not submit an imputation study with its direct case. Other parties including ELI witness Montgomery addressed imputation in their direct cases. Mr. Montgomery's analysis indicated that U S West's proposed interconnection rates did not meet a proper imputation analysis. USWC rebuttal witness Purkey sponsored an imputation study on business exchange rates. His study indicates that the company's business rates do pass an imputation analysis. Other parties responded to this imputation study, suggesting that it was improperly done.

Mr. Purkey's imputation analysis was performed on an average business line as opposed to an individual service. Mr. Purkey indicates that residential service would obviously fail an imputation study since his company contends that residential rates are currently below costs. His imputation study on business exchanges is based on the company's cost studies, using ADSRC. He incorporates a determination of essential services. For these services he inputs the company's proposed pricing. All other elements are priced at cost. The only elements that are considered essential in his studies are: terminating expanded interconnection, terminating local switching, and terminating multiplexer maintenance.

Other parties disagree with Mr. Purkey's studies. They argue that he has misapplied the essential service notion, and that other services such as tandem switching and directory listings should also be considered essential. [Montgomery, TR., p. 1076] They also argue that the study improperly prices out costs such as the proposed universal service charge. [Cornell, TR., p. 2026]] Dr. Cornell's suggested modifications of Mr. Purkey's imputation studies indicate that business exchange does not pass imputation.

Commission Staff, in its brief, argues that the company's imputation studies do not comply with Commission guidelines. Staff also complains that while it is obvious that a imputation study is required, USWC did not provide one in their direct case. Staff objections to the imputation study are related to the averaging of the various business rates in Mr. Purkey's analysis. Staff points to prior Commission orders which require imputation on an individual service basis.

## D. COMMISSION DISCUSSION -- IMPUTATION

The company's failure to present imputation studies in support of its proposed rates in its direct case is unacceptable. The company failed to provide individual service imputation studies despite previous Commission order.[28] In this proceeding the Commission has rejected the company's interim universal service charge and the company's proposed minutes of use interconnection charges, has accepted the use of bill and keep on an interim basis, has modified the expanded interconnection proposal, and has ordered interim number portability at TSLRIC. The Commission sees no need to do an imputation in this interim period of bill and keep.

The Commission expects the company to support future filings made in compliance with this order with imputation studies which support price ceilings for the services offered for interconnection. These studies should be consistent with previous Commission orders. The Commission does recognize several issues which still need to be resolved. The Commission has not yet accepted any cost study for local exchange. There is no determination of what are direct elements of service associated with local service, or the cost of providing these elements of service. Further, the issue of what are essential elements of service has not been determined. The Commission is hopeful that some of these issues may be resolved in the current general rate proceeding.

The Commission would also like to take this chance to note that the simple passing of an imputation study is not sufficient evidence to support the fairness of proposed rates. While it is essential for fair competition that an imputation test be passed, such demonstration does not in and of itself indicate that the rates proposed are fair. The Commission needs to determine that the rates provide a level of contribution that is consistent with the public policy goals of the Commission.

### FINDINGS OF FACT

Having discussed above in detail both the oral and documentary evidence concerning all material matters, and having stated findings and conclusions, the Commission now makes the following summary of these facts. Those portions of the preceding detailed findings pertaining to the ultimate findings are incorporated herein by this reference.

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[28] In re Pacific Northwest Bell Telephone Company, Docket No. U-88-2052-P, Second Supplemental Order (January 1989).

1. The Washington Utilities and Transportation Commission is an agency of the state of Washington, vested by statute with authority to regulate rates, rules, regulations, practices, accounts, securities, and transfers of public service companies, including telecommunications companies.

2. U S WEST Communications, Inc. ("USWC"), GTE Northwest Incorporated ("GTE"), Electric Lightwave, Inc. ("ELI"), and TCG Seattle ("TCG") are each engaged in the business of furnishing telecommunications service within the state of Washington as a public service company.

3. USWC and GTE were, until recently, the exclusive providers of switched local exchange service in their respective Washington exchanges, and currently are the dominant providers of switched local services within their respective Washington exchanges.

4. ELI and TCG presently provide limited switched local exchange service in certain of the exchanges of USWC and of GTE, in competition with those incumbents.

5. To provide switched local exchange service, ELI, TCG, and other alternative local exchange companies ("ALECs") must interconnect with USWC's and GTE's switched networks.

6. The provision of interconnection between two local exchange networks for the purpose of terminating local traffic is an essential service which is not available from any other provider.

7. On November 14, 1994, USWC filed tariff revisions for its switched access service, which included the introduction of local interconnection service and the unbundling of local transport service for switched access. The revisions also included the introduction of expanded interconnection service and expanded interconnection - virtual collocation service for all companies. The stated effective date of the tariff revisions is January 1, 1995. The Commission suspended the tariff filings on December 15, 1994.

8. On November 15, 1994, in Docket No. UT-941465, TCG and Digital Direct of Seattle, Inc. (since acquired by TCG Seattle), filed a complaint against USWC alleging undue prejudice, discrimination, and unjust rates and practices in the provision of interconnection and mutual compensation. USWC answered and counterclaimed. On February 13, 1995, the Commission consolidated Docket Nos. UT-941464 and UT-941465 for discovery and hearing.

9. On February 7, 1995, in Docket No. UT-950146, TCG filed a complaint against GTE alleging undue prejudice, discrimination, and unjust rates and practices in the provision of interconnection and mutual compensation. GTE answered, counterclaimed against TCG, and filed a third party complaint against USWC.

10. On March 1, 1995, in Docket No. UT-950265, ELI filed a complaint against GTE for undue prejudice, discrimination, and unjust rates and practices in the provision of interconnection and mutual compensation.

11. On March 8, 1995, the Commission consolidated Docket Nos. UT-950146 and UT-950265 with Docket Nos. UT-941464 and UT-941465.

12. There is no essential difference between ALEC local traffic and incumbent LEC local traffic within a local calling area, including an EAS area.

13. USWC and GTE currently interconnect with one another and with other incumbent local exchange companies for the exchange of local traffic, including extended area service ("EAS") traffic. They employ a "bill and keep" method of compensating one another for the mutual traffic exchange. Both incumbents refuse to interconnect with ELI or TCG on the same basis, and both require that interconnecting ALECs pay minutes of use-based rates for local call termination.

14. For at least the present, ELI and TCG will establish local calling areas and rate centers conforming to existing USWC and GTE extended area service (EAS) and exchange boundaries.

15. The mutual compensation proposals of both USWC and GTE require the measurement and billing of terminating traffic between companies, which would require additional investment and expense and increase the cost of local exchange service.

16. The minutes of use-based rates proposed by USWC and GTE for terminating the local traffic of ALECs such as ELI and TCG do not properly reflect the structure of costs incurred to provide interconnection service; these costs generally do not vary with the level of traffic being exchanged.

17. The measured use regime proposed by USWC and GTE would undermine the state's public policy of affordable, flat-rated local service by reducing competitive pressure on the incumbents' flat-rated service, increasing the interconnection costs incurred by new entrants, and potentially raising the minimum rate at which incumbents could offer retail service.

18. The mutual traffic exchange or bill and keep compensation mechanism proposed by several parties would provide a simple method for interconnection and compensation for the termination of local exchange traffic.

19. The bill and keep method lacks cost-based price signals that should be included in any long-term compensation mechanism. It is appropriate as an interim mechanism.

20. The cost studies on which USWC bases its rate proposals use improper measures of economic cost and are accompanied by insufficient documentation to enable the Commission to conduct a fair review of the company's costs.

21. The record does not support the need for, or amount of, USWC's proposed interim universal service charge rate element. The record does not demonstrate that universal service in USWC's service territories will be adversely affected if the Commission does not authorize USWC to collect a charge for the support of universal service in this proceeding.

22. Technically and economically efficient interconnection of incumbent local exchange company (LEC) and new entrant ALEC networks is essential to the development of a competitive local exchange market.

23. Physical interconnection between incumbent local exchange companies and ALECs does not involve any unique technological problems that the incumbent LECs do not face in interconnecting among themselves.

24. Currently USWC, GTE, and other incumbent local exchange companies use separate trunks for exchanging local (EAS) and toll traffic. This presently is a necessary arrangement for distinguishing between local and toll traffic.

25. Until such time as they build ubiquitous networks, new entrants into the switched local exchange service market require the ability to lease customer loops from the incumbent LEC in order to extend their geographical reach throughout a local calling area. The present unavailability, for lease, of incumbent local exchange companies' customer loops is a substantial impediment to the development of competition in the switched local exchange service market.

26. USWC soon will file an unbundled loop service tariff, which will make unbundled customer loops and line side interconnection available to ALECs for resale to end users.

27. The availability of true local service provider number portability is a necessary precondition for effective local service competition. However, true local service number portability is not presently available. USWC's proposed interim number portability measures are appropriate, as a temporary measure, if priced at cost.

28. A unified customer directory database is essential in a competitive switched local exchange service market if local service is to be seamless from the perspective of the consuming public. The lack of a single directory would be a substantial barrier to effective competition in the switched local exchange service market.

29. The complainants have not demonstrated that USWC or GTE will not provide 9-1-1, telecommunications device for the deaf ("TDD"), directory listing and assistance, and other necessary customer services upon interconnection at fair, just, and reasonable rates.

30. USWC's proposed rates for transport have relative price ratios between DS3 and DS1 transport components that are economically inefficient, would result in unfair competitive advantages for large IXCs, and would negatively affect competition to less urbanized parts of the state. An appropriate minimum DS3 to DS1 price ratio is based on the underlying, and properly estimated, total service long run incremental cost ratios for those transport components.

31. Local switching costs have been declining dramatically in recent years. USWC has not provided a solid evidentiary foundation for increasing its local switching charge, in view of such cost declines.

32. Revenue neutrality associated with local transport restructure ("LTR") in this proceeding would result in a residual interconnection charge so large it would render LTR economically meaningless in this proceeding. Local transport restructure is an issue appropriately addressed in USWC's pending general rate increase case.

33. USWC's proposal to omit its intra-LATA foreign exchange service from the access tariff was based on implementing LTR in this proceeding. Since the Commission rejects the LTR tariff filing in this proceeding, eliminating the intra-LATA foreign exchange service from its access tariff should be addressed in USWC's general rate increase case.

34. USWC's EICT proposal does not fully specify how the EICT substitutes for the restructured switched access rate elements that would otherwise apply. Another deficiency in USWC's proposal is that virtual collocation rate elements are not based on long run incremental cost studies.

## CONCLUSIONS OF LAW

1. The Washington Utilities and Transportation Commission has jurisdiction over the subject matter of these proceedings and the parties.

2. USWC's proposed tariff revisions filed in Docket No. UT-941464 state rates, charges, and practices that are not shown to be fair, just, and reasonable, and are shown to be unjustly discriminatory and unduly preferential.

3. The Commission should reject the tariff revisions filed in Docket No. UT-941464.

4. The rates GTE has offered ELI and TCG to terminate local (including EAS) traffic on GTE's network are not fair, just, or reasonable, and are anticompetitive.

5. The terms for local interconnection that GTE has offered ELI and TCG are anticompetitive and subject ELI and TCG to undue or unreasonable prejudice or disadvantage in violation of RCW 80.36.170 and RCW 80.36.186, and are discriminatory in violation of RCW 80.36.180.

6. The Commission should grant the complaints of TCG and ELI, in part, and should order GTE to interconnect with ELI and TCG on the same terms and conditions as it interconnects with USWC and other incumbent LECs. It should order GTE to file a local interconnection tariff providing for the exchange of local (including EAS) traffic with ELI and TCG on a bill and keep basis.

7. The use of mutual traffic exchange or bill and keep compensation structure on an interim basis results in compensation to local exchange companies that is fair, just, reasonable, and sufficient.

8. The Commission should direct USWC, GTE, TCG, and ELI to develop a plan for the implementation of true number portability and return to the Commission with a recommendation by July 1, 1996.

9. The Commission should direct USWC and GTE to file tariff revisions proposing a replacement for bill and keep by July 1, 1996.

10. Commission Staff and interested persons should hold a workshop (which should include a Commission facilitator) to explore how mediation or alternative dispute resolution can be used to settle differences regarding the terms of physical interconnection. Staff should report back to the Commission on whether an industry consensus has emerged, and on any other recommendations Staff or other participants may have for resolving disputes, by July 1, 1996.

11. The Commission should dismiss the counterclaim of USWC in Docket No. UT-941465, and should dismiss the counterclaim of GTE in Docket No. UT-950146.

12. The Commission should dismiss the third party complaint of GTE in Docket No. UT-950146.

13. All motions made in the course of this proceeding which are consistent with findings and conclusions made in this Order should be deemed granted and those inconsistent should be deemed denied.

## ORDER

THE COMMISSION ORDERS:

1. The tariff revisions filed in Docket No. UT-941464 are rejected in their entirety. USWC is ordered to file tariff revisions, which also shall include terms and conditions for bill and keep on an interim basis, in the form found to be appropriate in the body of this order.

2. The local transport restructure is removed to USWC's general rate increase case; appropriate portions of the record evidence relating to that issue will be incorporated into the record in that proceeding.

3. The complaint of TCG Seattle filed against GTE in Docket No. UT-950146 is granted, in part. GTE is ordered to interconnect with TCG on the same terms and conditions as it interconnects with USWC and other incumbent LECs, including, on a transitional basis, terminating the local (including EAS) traffic of TCG on a bill and keep basis.

4. The complaint of Electric Lightwave, Inc., filed against GTE in Docket No. UT-950265 is granted, in part. GTE is ordered to interconnect with ELI on the same terms and conditions as it interconnects with USWC and other incumbent LECs, including, on a transitional basis, terminating the local (including EAS) traffic of ELI on a bill and keep basis.

5. GTE is ordered to offer 9-1-1, TDD, directory listings, operator services, and directory assistance to TCG and ELI on the same rates, terms, and conditions as it offers those services to other incumbent local exchange companies.

6. GTE is ordered to file a local interconnection tariff pursuant to the terms of this order.

7. The counterclaim of USWC in Docket No. UT-941465 is dismissed.

8. The counterclaim of GTE in Docket No. UT-950146 is dismissed.

9. The third party complaint of GTE against USWC in Docket No. UT-950146 is dismissed.

10. The interconnection arrangements required by this order shall be tariffed and filed no later than 20 days after entry of this order, with a stated effective date at least ten working days after the filing date.

11. The refiled tariff pages shall bear the notation that the tariffs are filed authority of the Commission's FOURTH SUPPLEMENTAL ORDER IN DOCKET NOS. UT-941464, et al.

12. The compliance filing required by this order is strictly limited in scope to effectuate the terms of the Commission's decision and order.

13. USWC, GTE, TCG, and ELI are ordered to develop a plan for implementation of true number portability, in consultation with one another (and with other members of the industry, if they so choose), and return to the Commission with a recommendation no later than July 1, 1996.

14. USWC and GTE both are ordered to file tariff revisions proposing a replacement for bill and keep, no sooner that July 1, 1996, and no later than July 15, 1996.

15. Commission Staff shall convene a workshop to explore with interested persons use of mediation or alternative dispute resolution to settle differences regarding the terms of physical interconnection. Staff shall report back to the Commission on whether an industry consensus has emerged, and on any other recommendations Staff or other participants may have for resolving disputes, by July 1, 1996.

16. The Commission retains jurisdiction over the subject matter and the parties to effectuate the provisions of this order.

17. All outstanding motions consistent with this order are deemed granted. Those inconsistent with this order are deemed denied.

DATED at Olympia, Washington, and effective this
day of October 1995.

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

SHARON L. NELSON, Chairman

RICHARD HEMSTAD, Commissioner

WILLIAM R. GILLIS, Commissioner

**NOTICE TO PARTIES:**

**This is a final order of the Commission. In addition to judicial review, administrative relief may be available through a petition for reconsideration, filed within 10 days of the service of this order pursuant to RCW 34.05.470 and WAC 480-09-810, or a petition for rehearing pursuant to RCW 80.04.200 and WAC 480-09-820(1).**