Q. **PLEASE STATE YOUR NAME, EMPLOYER, AND BUSINESS ADDRESS**.

A. My name is Thomas L. Spinks. I am employed by the Washington Utilities and Transportation Commission. My business address is 1300 South Evergreen Park Dr SW, P.O. Box 47250, Olympia, Washington, 98504.

Q. **IN WHAT CAPACITY ARE YOU EMPLOYED?**

A. I am employed as a Regulatory Consultant.

Q. **HAVE YOU PREPARED A STATEMENT OF YOUR QUALIFICATIONS?**

A. Yes. A summary of my education and experience is provided as Exhibit ___ (TLS-2).

Q. **WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

A. The purpose of my testimony is to address a number of issues regarding the Qwest and Verizon proposals relating to the amount and recovery of OSS and line sharing costs.

RECOVERY OF OSS STARTUP COSTS

Q. **WHAT GUIDANCE HAS THE COMMISSION PROVIDED REGARDING THE RECOVERY OF OSS COSTS?**

A. In its 17th Supplemental Order in Docket Nos. UT-960369, *et al.*, the Commission determined that incumbent local exchange carriers (ILECs) are entitled to recover the costs of OSS from competitive local exchange companies (CLECs) and established certain criteria that would be followed in this proceeding.[1] The criteria include a requirement that ILECs file new cost studies demonstrating that OSS costs are not already being recovered through their expense factors and provide evidence of the level of expenditures for OSS demonstrating that such expenditures were incurred in order to provide OSS to CLECs. *See* 17th Supp. Order, ¶¶ 98-112. The ILECs also must provide detailed cost support for any request to recover shared or common costs and address and defend their determination of the degree to which these costs already have been recovered through their retail rates. *Id.* at ¶ 110. Staff's review of the testimony and cost studies filed by the ILECs raises a number of concerns.

Q. **WHAT ARE STAFF'S CONCERNS WITH THE QWEST OSS STARTUP COST RECOVERY PROPOSAL?**

A. Staff has concerns with how Qwest developed the amount of cost to be recovered and the proposed mechanisms for recovering the costs from CLECs. Qwest proposes to charge $9.58 per order for EDI access and $14.19 per order for IMA access to recover the startup costs. Verizon proposes to charge $4.28 per order for EDI orders.

Q. **WHAT ARE STAFF'S CONCERNS WITH THE DEVELOPMENT OF THE AMOUNT OF OSS STARTUP COST TO BE RECOVERED FROM CLECS?**

A. The first concern is that Qwest's estimate of OSS startup cost relies on estimates of 1999

[1]*See In the Matter of the Pricing Proceeding for Interconnection, Unbundled Elements, Transport and Termination, and Resale,*17th Supplemental Order, Docket Nos. UT-950369, *et al.* (Sept. 23, 1999).

expenses rather than actual expenses. For instance, Exhibit ____ (TKM-3) shows 1999 estimated Account 6724 expenses of $979 million. However, its 1999 ARMIS report shows the company actually booked $632 million to the Account in 1999. As discussed later in this testimony, Qwest updated the trend exhibit for Account 6724 but did not provide 1999 OSS startup costs allocated to Washington. Qwest still needs to provide the 1999 Washington OSS startup expenses.

The second concern is with the cost study supporting the development of the OSS cost recovery charge. Exhibit ___ (TKM-1), Attachment A, page 17, shows the amounts of investment and expense that the company seeks to recover before subsequent adjustments. The amounts shown on page 17 are increased substantially to include what the company terms “directly attributable” costs to arrive at the $121.8 million the company seeks to recover.[2] Direct Testimony of Teresa Million, page 3, line 7. The “directly attributable” cost categories are business fees, product management costs, administrative costs, and attributed costs. These additional costs are typically applied to investments and recurring costs in cost studies, not one time startup expenses. The additional costs associated with expenses should be removed from the study.

Also, in developing the proposed recovery charge in Exhibit ____ (TKM-1), page 22, Attachment B, the company appears to include recovery of the investment portion of the OSS startup costs twice. The present value of the investment is included at column F, line 76, while the actual investment amount is also included in the “Total

[2]In contrast, Verizon is only requesting recovery of the expense without additional markups.

Expenses to be Recovered" amount shown in column F, line 80. The amount at line 76 should not be included in the calculation because the investment is included at line 80.

Finally, the per order charge is calculated using projections of future service orders that are discounted to their present value[3] as well as including an investment amount that has been increased to represent its present worth over the six year recovery period.

Q. **DOES THE TREND ANALYSIS PROVIDED IN EXHIBIT ____ (TKM-3) SUPPORT THE LEVEL OF OSS COSTS FOR WHICH QWEST SEEKS RECOVERY?**

A. No. The testimony of Ms. Million discusses the fact that expenses in the Account about doubled in the six years prior to passage of the Act, and have nearly doubled again in the three years preceding the Act. T. Million, Direct Testimony, pages 10 and 11, lines 1-11. The subsequent analysis purports to show that the claimed amount of OSS expense is reasonable. The problem is that the analysis relied on an estimate of 1999 expenses that turned out to be overstated by some $367 million. Staff attempted to perform its own trend analysis and asked for, in staff data request number 37, the 1997, 1998, 1999, and Year 2000 expenses that were included in the Account. However, the company did not provide the requested information.

---

[3] *See* Attachment B, page 21, line 52.

Q. **HAS STAFF ESTIMATED QWEST'S OSS STARTUP COSTS?**

A. Based on the costs provided in Exhibit ____ (TKM-1), Attachment B, staff estimates the 1997-1998 OSS startup costs for Qwest-Washington to be $5.3 million.[4] In response to staff data request number 27, Qwest provided an Account 6724 trend analysis for Washington with non-OSS expenses removed from historical costs, and in response to staff data request number 35, Qwest provided an update to the earlier data request but did not provide the 1999 Washington expense. The responses are provided as Confidential Exhibit C-___ (TLS-3C). The difference in the expenses between the staff estimate and the estimate provided in response to staff data request number 27 need to be reconciled because the company states in response to staff data request number 35 that the amounts provided for Washington included only "those operational support systems defined generally by the FCC as a UNE, and for which Qwest seeks cost recovery . . . ." The probable source of the difference is the expense factor adjustment discussed in Ms. Million's testimony at page 12, lines 16-18. The company needs to clarify the level of Washington expense it seeks to recover.

Q. **WHAT ARE THE CONCERNS WITH THE ILECS' PROPOSED METHOD OF RECOVERY?**

A. The ILECs propose to establish a per order service charge to recover OSS startup costs

[4] *See* Exhibit ____ (TKM-1), Attachment B, page 17, line 49, columns C and D, and page 18, line 88, columns C and D, which were summed and multiplied by 14.5 percent, the approximate allocation factor for Washington.

that relies on system-wide forecasts of service orders placed by CLECs, and is based on system-wide costs rather than Washington specific costs. The ILECs allocate corporate level costs such as the OSS startup costs between the states for accounting and ratemaking purposes, so state specific costs can and should be identified and used. This is necessary so that the costs allocated to Washington are fully recovered by charges to CLECs for competitive activity in Washington.[5] If Washington-specific costs are not used in the recovery calculation, OSS startup costs allocated to other states could be paid for by CLEC activity in Washington. Using state specific costs will also make it easier to track and audit the recovery of OSS startup costs. The Commission already has ordered the ILECs to establish true-up procedures to ensure accurate cost recovery of interim charges. Staff also believes that because forecasts of projected order activity are highly speculative at this time, and likely to be understated,[6] the Commission should consider alternative cost recovery proposals.

Q. **HOW SHOULD ILECS RECOVER THE OSS STARTUP COSTS?**

A. The OSS startup costs should be recovered by identifying the amount of OSS expense attributable to Washington and establishing a transaction or per order charge of $5.00 or less to recover the OSS startup costs. Under this approach, Verizon’s proposed charge of $4.28 appears reasonable. Both ILECs should report periodically to the Commission the

[5]Verizon identifies the amount of Washington specific cost of $1,962,463 in its non-confidential section of cost support, Tab 5, OSS 5-WA3.

[6]The direct testimony of AT&T witness Joseph Gillian in this case discusses the use of the UNE platform for mass marketing.

amount collected and the amount remaining to be collected from the CLECs until the costs are fully recovered.

If the Commission still wants to have separate rates for EDI and IMA access,[7] a lower charge of $3.00 could be established for the EDI access and the $5.00 charge would apply to IMA access. Staff is concerned that charging a higher rate to recover the OSS startup costs may create a disincentive for CLECs to compete in Washington until after the charge is recovered and eliminated.

Q. **HOW DO THE ILECS ADDRESS THE QUESTION OF WHETHER OSS COSTS HAVE ALREADY BEEN RECOVERED IN RETAIL RATES?**

A. Verizon witness Robert Tanimura states that OSS costs are not included in retail rates because "GTENW's last rate case was in 1985." R. Tanimura, Direct Testimony, page 8, line 14. Qwest witness Teresa Million also denies that OSS development costs have been recovered through retail rates "because the retail rates in Washington are based on a 1997 rate case . . . ." T. Million, Direct Testimony, page 13, line 8. This testimony indicates that the ILECs have taken the position that unless there has been a rate case that specifically included OSS costs, the costs have not been recovered in retail rates.

Q. **ARE ILECS ALREADY RECOVERING OSS COSTS IN RETAIL RATES?**

A. Yes. While a recent rate case is certainly one way to demonstrate what expenses are

---

[7]The supplemental testimony of Qwest witness T. Million indicates that there is a relatively small difference in costs between EDI and IMA access.

included in retail rates, the question of whether current retail rates have recovered current OSS expenses cannot be answered by whether or not a company has had a recent rate case. In staff's view, expenses that are incurred after a rate case would be covered by revenues if rate levels are considered in conjunction with other proceedings, such as a merger proceeding, or if current levels of revenues and expenses are such that a company met or exceeded its authorized rate of return. If an ILEC meets or exceeds its authorized return, it means that revenues have grown faster than expenses and the additional revenue growth was sufficient to permit recovery of OSS implementation costs in retail rates.

Q. **WHEN WERE VERIZON'S RATE LEVELS LAST CONSIDERED BY THE COMMISSION?**

A. Verizon rate levels were reviewed by staff and reset in the merger settlement, Docket No. UT-981367, which also resolved the earnings complaint filed in Docket No. UT-991164. The staff earnings complaint analysis for Verizon used a 1998 test year and formed the basis for staff's position on the rate reductions agreed to by the company in the merger settlement.[8] Because Verizon's OSS startup expenses for which it is requesting recovery were incurred through 1998, staff believes all OSS startup costs, including subsequent 1999 expenses, have already been recovered in current retail rates.

---

[8]Staff acknowledges that Verizon did not concede that it was overearning in the merger settlement.

Q. **WHEN WERE QWEST'S RATE LEVELS LAST CONSIDERED BY THE COMMISSION?**

A. Qwest rate levels were last set by the Commission in Docket No. UT-970766, and used a 1996 test year. Qwest appears to have excluded the 1996 OSS expenses from the amount of OSS startup cost requested for recovery in this case.

Q. **DO QWEST'S EARNINGS CURRENTLY MEET OR EXCEED THE AUTHORIZED RATE OF RETURN?**

A. Yes. Qwest is required to report revenues and expenses periodically on a Washington intrastate basis and the reports must contain various ratemaking adjustments ordered by the Commission. The company's reported earnings for 1998 and 1999, on a Commission basis, were 12.56 and 12.67 percent, respectively. The current authorized return is 9.36 percent. Staff acknowledges that the Commission basis earnings levels for 1998 and 1999 would need to be adjusted for ratemaking purposes to properly reflect certain expense and/or revenues booked in other years. However, because the amount of overearnings for 1999 is approximately $72 million, staff believes it is highly unlikely that the company could demonstrate that its Commission basis earnings levels for 1998 and 1999 were not at least at the authorized level. Therefore, staff believes that Qwest's OSS expenses allocated to Washington have been recovered in retail rates. Neither Verizon or Qwest have demonstrated in their testimony that the OSS startup costs were not recovered by the additional revenues. Since the Commission has already determined that CLECs are responsible for paying for the OSS startup costs, if no action is taken, ILECs will recover the startup costs twice.

Q. **WHAT OPTIONS ARE OPEN TO THE COMMISSION FOR ENSURING THERE IS NO DOUBLE RECOVERY OF THE OSS STARTUP COSTS?**

A. The Commission could direct the ILECs to make offsetting retail rate reductions or reductions to other OSS rate elements. Staff believes the latter option of reducing other OSS rates may be preferable because the lower rates would encourage more rapid competitive entry into Washington telecommunications markets, which in turn would benefit all Washington telecommunications customers.

Q. **IF THE COMMISSION CHOOSES TO REDUCE RETAIL RATES, WHAT RATES SHOULD THE COMMISSION CONSIDER?**

A. One potential retail rate reduction would be to the number portability charge that is assessed on access lines for the purpose of recovering part of the cost of establishing number portability. Qwest charges $0.43 per access line per month. The Verizon charge is $0.36 per month. The number portability charge is imposed by the FCC and cannot be eliminated. Under the staff proposal, the companies would provide an intrastate bill credit and explain that the credit is to offset the interstate number portability charge. The offset to the number portability charge would not be permanent because the cost recovery period for the charge exceeds the amount of revenue that would be available.

Q. **IF THE COMMISSION CHOOSES TO REDUCE OTHER OSS RATES, WHAT RATES SHOULD THE COMMISSION CONSIDER?**

A. The Commission could use the OSS costs already recovered in retail rates to offset non-recurring costs for collocation or reduce UNE monthly recurring rates. If monthly recurring rate reductions are considered, they should not be reduced below the direct cost of providing the UNE.

<u>LINE SHARING ISSUES</u>

Q. **WHAT ARE STAFF'S CONCERNS WITH THE ILEC PROPOSALS FOR LINE SHARING?**

A. The concern with the Qwest proposal is the proposed $9.08 loop allocation charge to CLECs. Verizon has not proposed a line sharing charge for the loop. Staff also has concerns with the ILEC proposals for a separate line sharing OSS cost recovery element.

Q. **WHAT ARE THE CONCERNS WITH THE QWEST LOOP ALLOCATION PROPOSAL?**

A The concerns are: (1) the proposed allocation of 50 percent of the loop cost to line sharing, which appears excessive because many services share the loop and contribute to the recovery of the loop cost; (2) the proposed $9.08 charge does not appear to recognize the geographically deaveraged zones recently ordered by the Commission; and (3) because line sharing is simply another form of sub-loop unbundling, any line sharing charge should be offset by a reduction in the rate for the rest of the unbundled loop. Qwest has not proposed any offset to the UNE loop cost.

Q. **WHAT DOES STAFF PROPOSE FOR A LINE SHARING CHARGE?**

A Staff recommends that the line sharing charge be set at zero. If the Commission concludes that some charge is appropriate, staff recommends that it not exceed $.96 per month.

Q. **WHY SHOULD THE LINE SHARING CHARGE BE ZERO?**

A. When Qwest filed its proposed tariff for Mega-Bit service in Washington, staff inquired as to why loop costs were not included in the cost support for the service. The company position was that the cost of the loop was already being recovered in the rates for other services. Staff accepted this explanation and, consistent with that acceptance, notes that it would now place CLECs at a competitive disadvantage to allow a charge for the loop to be made for their use of the same functionality for which Qwest charges itself nothing.

Q. **WHAT IS THE BASIS FOR RECOMMENDING THAT IF THE COMMISSION CONCLUDES SOME CHARGE IS APPROPRIATE, THAT IT NOT EXCEED $.96 PER MONTH?**

A. Line sharing has been determined by the FCC to be a UNE and, therefore, like other UNEs is subject to the "TELRIC plus a reasonable share of common/overhead cost" criteria that is required for pricing UNEs. In developing a charge for this UNE, staff notes that the TELRIC for line sharing is zero; the only question is what is a reasonable share of common and overhead cost to use for line sharing.

Q. **WHAT ARE THE APPLICABLE COMMON AND OVERHEAD COSTS TO CONSIDER IN DEVELOPING A PROPOSED RATE FOR LINE SHARING?**

A. In staff's view, the applicable common and overhead costs to consider for line sharing depend on whether line sharing is a service that uses the loop in common with other services or whether line sharing is a form of sub-loop unbundling. Under the former, the loop would be a common cost to be recovered from all services, while under the latter the common cost to consider is the common cost attributable to the UNE-loop. The reason that the loop common costs are appropriate to consider in pricing the UNE line sharing is because, in the context of UNEs, the CLEC is not buying the UNE loop, rather, the CLEC is buying access to the high-frequency portion of the loop spectrum. The cost of that access is recovered in the non-recurring cost of line sharing. There are no recurring costs associated with that access and the only common and overhead cost that is relevant to line sharing is the common cost associated with the loop itself. For example, if the $.36 Verizon charge applied to 750,000 access lines, the charge could be offset for a seven month period.

Q. **WHAT IS THE AMOUNT OF COMMON COST INCLUDED IN THE PRICE OF THE LOOP?**

A. The amount of common cost already included in the UNE loop cost today is $1.91.[9] 17th Supp. Order, Docket Nos. UT-960369, et al., ¶ 205. Staff believes that allocating no more than 50 percent of $1.91, which is $.96, would be a rational and reasonable TELRIC-based monthly charge for line sharing.

Q. **HOW SHOULD A LINE SHARING CHARGE, IF ANY, BE APPLIED TO GEOGRAPHIC ZONE BASED UNE LOOPS?**

A. If the Commission adopted the Qwest proposal of $9.08, which is 50 percent of the statewide average rate, the charge should be applied in Zone 1 as 50 percent of the Zone 1 rate, or $3.75. The reason for using a percentage is that Qwest is proposing to allocate the loop cost and that cost varies by zone. Under the staff proposal, if any charge is permitted, the charge would apply equally in any zone because the common/overhead portion of the loop cost does not vary by zone. In either case, loops not equipped with line sharing would have a rate equal to the zone rate less the line sharing rate.

Q. **WHY IS LINE SHARING A FORM OF SUB-LOOP UNBUNDLING?**

A. Sub-loop unbundling is generally thought of in terms of providing access to only the portion of the loop that would be needed by the CLEC given some caveats regarding the

[9] $18.16 less the $16.25 cost floor equals $1.91.

feasibility of access. So the framework for discussing unbundling the loop has encompassed using points of access such as the feeder/distribution interface or the drop. The analogy would be to taking a straw and cutting a piece off - maybe at the halfway point or maybe closer to the end - depending on how much you need. Line sharing is like taking the straw and slicing it down the length of the straw. So long as access is feasible, and it is, line sharing is simply a different way of splitting the loop and is a form of sub-loop unbundling. However, unlike costing for other forms of sub-loop unbundling which can rely on relative amounts of investment for each portion of the loop being unbundled, line sharing uses one portion of the loop bandwidth without avoiding the cost of the other portions.

Q. **DOES STAFF HAVE A CONCERN WITH THE ILEC PROPOSAL FOR A SEPARATE LINE SHARING OSS COST RECOVERY CHARGE?**

A. Yes. The concern is that there is simply no need to treat the line sharing UNE startup costs any differently from the startup costs for other UNEs. Any additional costs incurred by the ILECs to provide OSS access for line sharing should be added to the pool of OSS costs designated for recovery by the per service order charge as discussed earlier in my testimony.

Q. **DOES STAFF HAVE ANY CONCERNS WITH THE QWEST PROPOSAL FOR AN OSS ONGOING MAINTENANCE CHARGE?**

A. The main concern with the OSS ongoing maintenance charge is that it applies on a per order basis and relies on the likely understated and discounted CLEC order projections discussed earlier in this testimony. Any charge for ongoing maintenance should be a monthly recurring charge because the expenses do not depend on the level of order activity.

Q. **DOES THIS COMPLETE YOUR TESTIMONY?**

A. Yes.