BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION

IN THE MATTER OF THE CONTINUED)
COSTING AND PRICING OF UNBUNDLED)
NETWORK ELEMENTS, TRANSPORT,) Docket No. UT-003013
TERMINATION, AND RESALE) *Part A*

REBUTTAL

TESTIMONY

OF

TERESA K. MILLION

ON BEHALF OF

QWEST CORPORATION
(formerly known as U S WEST)

AUGUST 4, 2000

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

A. My name is Teresa K. Million. I am employed by Qwest Corporation (Qwest), formerly known as U S WEST, as Director – Cost Advocacy. My business address is 1801 California St., Denver, CO.

Q. HAVE YOU PREVIOUSLY FILED TESTIMONY IN THIS PROCEEDING?

A. Yes.

Q. WHAT IS THE PURPOSE OF THIS TESTIMONY?

A. The purpose of this testimony is to rebut the testimonies of Mr. Roy Lathrop representing Worldcom Inc. and Mr. Thomas L. Spinks representing the Washington Utilities and Transportation Commission staff relating to Qwest's Operations Support Systems (OSS) cost studies.

TESTIMONY OF MR. LATHROP

Q. DOES MR. LATHROP APPLY THE CORRECT STANDARD TO RECOVERY OF OSS COSTS?

A. No. Mr. Lathrop carries on a lengthy discussion about forward-looking, efficient systems and says that proper cost would be de minimus because a forward-looking system would only need "new features" and, presumably, would not need to be modified for a multi-provider environment. Mr. Lathrop does not say what the "new features" are for which Qwest should receive cost recovery. He then goes so far as to imply that Qwest's OSS expenditures prior to the Act may have been made in order to purposely complicate its legacy systems. This is an untrue allegation and, like most of Mr. Lathrop's testimony, is totally unsupported and results in an untrue allegation.

Q. WHAT IS THE APPROPRIATE STANDARD FOR RECOVERY OF OSS COSTS?

A. The Eighth Circuit Court of Appeals recently affirmed that the costs for UNEs should be forward-looking, but it vacated the requirement that they be based on the most efficient, least cost configuration.[1] The Court's decision is discussed more completely in the rebuttal testimony of Mr. Jerrold L. Thompson. As a result of the Court's action, it is clear that cost recovery of UNEs should be based on the actual costs of providing the UNEs, and not some unrealistic, unachievable or hypothetical substitute for the actual items or elements. Qwest believes that this decision supports a method where actual, identifiable expenditures are tracked and charged to the cost causers. In the case of OSS, this includes the costs Qwest has expended to develop, modify and enhance its systems for the benefit of the CLECs that form the basis for OSS cost recovery.

Q. IS MR. LATHROP CORRECT THAT QWEST'S OSS COSTS HAVE BEEN INCLUDED IN ITS RATES?

A. No. Mr. Lathrop is unclear whether he means the OSS costs have been included in Qwest's wholesale rates or its retail rates, or both. However, my direct testimony from page 8 through page 14 "clearly" explains that the OSS costs for which Qwest seeks recovery are not included in the overheads and cost factors for either wholesale or retail rates. This is because the OSS costs included in this cost docket were expended <u>after</u> the time period in which the overheads and cost factors were

[1] *Iowa Utilities Board, et al., Petitioners, v. Federal Communications Commission and the United States of America, Respondents, On Petitions for Review of an Order of the Federal Communications Commission.* (Decision No. 96-3321).

developed. Nevertheless, to ensure that the costs did not duplicate costs recovered elsewhere, I made an adjustment reducing the OSS costs to reflect only the incremental costs that could not have been recovered previously. Please see my direct testimony, page 12, for a detailed explanation of the adjustment.

Q. IS MR. LATHROP CORRECT THAT QWEST'S "ONGOING" CHARGES ARE PER LINE PER MONTH?

A. No. The ongoing charges in Qwest's OSS cost study have been clearly labeled as being "per order." This means the ongoing maintenance charge applies once, each time a CLEC places a service order, and not on a monthly basis per line.

TESTIMONY OF MR. SPINKS

IS MR. SPINKS CONCERN ABOUT THE DIFFERENCE IN ESTIMATED VERSUS ACTUAL EXPENSES FOR 1999 VALID?

A. No. Mr. Spinks points out that Qwest estimated a total of $979 million in Information Technologies expenses for 1999, but only reported $632 million to Account 6724 in 1999. As shown in response to staff data request number 27b, and again in response to number 37b, the total actual Information Technologies expenditures in 1999 were $950 million. This is a difference of $29 million between the estimated and actual expenditures, not $367 million as Mr. Spinks suggests. Due to the implementation of the Software SOP 98-1, only $632 million of those expenditures were reported in Account 6724, while the remaining $318 million were reclassified to capital accounts. Therefore, if 1999 dollars had been booked on the same basis as in prior years, Qwest would have reported the entire $950 million in Account 6724.

Q. DO YOU AGREE WITH MR. SPINKS THAT QWEST IS NOT ENTITLED TO SEEK RECOVERY OF "DIRECTLY ATTRIBUTABLE" COSTS OF ITS OSS STARTUP COSTS?

A. No. AT&T made this same argument previously in Docket No. UT-960369 et al., specifically with regard to OSS and other nonrecurring charges. The Commission ruled at paragraph 126 of the Twenty-fifth Supplemental Order that it is appropriate to use "administrative, product management, and business fee loaders in U S WEST's (Qwest's) TELRIC studies."

Q. IS MR. SPINKS CORRECT THAT THE CAPITAL AMOUNT ON LINE 76 OF ATTACHMENT B, PAGE 22, IS INCLUDED IN THE AMOUNT OF TOTAL EXPENSES ON LINE 80?

A. No. As is shown on page 20 of Attachment B, as well as on page 22, the capital and expense amounts are calculated separately in the OSS cost study. The expense amounts that are represented on line 80 of page 22 are the sum of cells B10, B21 and B32 from page 20, while the capital amounts on line 76 of page 22 are the sum of cells E5, E16, and E27 from page 20. These amounts are developed separately, and do not overlap. Therefore, none of the capital costs from line 76 of Attachment B, page 22, are included in the amount labeled as "Total Expenses to be Recovered" on line 80 of the same page.

Q. PLEASE ADDRESS MR. SPINKS CONCERN OVER QWEST'S PRESENT WORTH CALCULATIONS.

A. The reason for the calculation in the OSS cost study that place both demand and the OSS costs on a present value basis is so that the resulting rate recovers the costs appropriately. In other words, because the demand represents a future number, and the cost represents a past number, both the numerator (cost) and denominator (demand) must be calculated on the basis of their present worth in order for charges in the future to recover costs that have already been expended. Please see Exhibit TKM-6 for proof that the resulting rate times the forecasted demand equals the costs that Qwest seeks to recover for 1997, 1998 and 1999.

Q. IS MR. SPINKS CORRECT THAT THE TREND ANALYSIS PROVIDED IN EXHIBIT TKM-3 DOES NOT SUPPORT THE LEVEL OF OSS COSTS FOR WHICH QWEST SEEKS RECOVERY?

A. No. Qwest provided a trend analysis showing the dramatic increase in expenditures in the three years since the passage of Act in my direct testimony. This analysis clearly supports the level of OSS costs for which Qwest seeks recovery. In addition, Qwest has provided further information to support this analysis in response to staff data request numbers 27, 35, 36 and 37.

As explained above, Mr. Spinks is incorrect in his conclusion that the 1999 expenses used in the analysis were overstated by $367 million. Actual expenditures for 1999 on an equivalent basis to earlier years, prior to implementation of SOP 98-1, were $950 million. Qwest has also provided further information regarding its Y2K expenditures during the three years since passage of the Act. Mr. Spinks is also incorrect when he states that Qwest did not provide the Y2K amounts that were booked to Account 6724 for 1997, 1998 and 1999. In response to staff data request number 37, Qwest reported Y2K amounts of $153.7 million for total Qwest, with $23.5 million reported in Washington. As predicted in footnote 12 of my direct testimony, this amount is less than the Y2K estimate of $175 million that I used in my analysis, thus affirming my conclusion that the trend in Information Technologies expenditures supports the level of OSS costs that Qwest seeks to recover.

Q. DO YOU AGREE WITH MR. SPINKS CALCULATION OF OSS STARTUP COSTS FOR QWEST-WASHINTON?

A. No. First, Mr. Spinks is trying to put the OSS expenditure on a Washington only basis. As Qwest has repeatedly explained, these costs are not incurred on a state specific basis, but are incurred at a company level. Therefore, any attempt to assign costs to Washington must be accomplished with an allocation, which Mr. Spinks has assumed to be 14.5%. The data that Qwest has provided in response to staff data request number 27 shows a Washington allocation percentage that has ranged from a low of 14.5% in 1999 to a high of 16.2% in 1993. It is inappropriate to arbitrarily use 14.5% to allocate amounts in the earlier years, especially since Mr. Spinks has those percentages available to him.

Second, Mr. Spinks does not acknowledge that the costs he has calculated for Washington from Attachment B pages 17 and 18 are merely inputs to Qwest's

WINPC3 program which are used to develop the appropriate TELRIC amounts, i.e., with loadings applied. In order to calculate the Washington specific amount correctly, Mr. Spinks should have started with the company-total dollars after loadings have been applied, not with the input dollars. The capital amount is arrived at by multiplying the company-total number from Attachment B, page 22, line 76 ($23.5 million) by the average allocation percentage for 1997, 1998 and 1999 (14.87%). The expense amount is arrived at by adjusting the company-total number from Attachment B, page 22, line 80 ($121.8 million) to account for the difference between estimated and actual expenditures in Account 6724 ($950 million/$979 million, or 97%) for 1999. The result ($119.5 million) is then multiplied by the average allocation percentage (14.87%). Thus, even using Mr. Spinks' simple allocation approach, but after loadings have been applied, the amount of Capital to be Recovered would be $3.5 million, and the amount of Expense to be Recovered would be $17.7 million when calculated correctly on a Washington specific basis for 1997, 1998 and 1999.

Finally, in order to calculate a rate for Washington-only OSS costs the demand for service orders would need to be estimated for Washington, as well. It would be inappropriate to use Washington specific dollars, and Qwest company-total demand to calculate a Washington rate for OSS startup costs. However, as Qwest indicated in its responses to staff data request numbers 28 and 29, forecasts for service orders are not generally estimated or tracked at a state level, thus it would be difficult to develop a Washington specific rate for OSS.

Q. IS THERE A WAY TO ADDRESS MR. SPINKS' CONCERN THAT QWEST NOT BE ALLOWED TO OVER-RECOVER OSS COSTS IN WASHINGTON?

A. Yes. Using the correct approach described above, it is possible to identify the total amount of Washington specific OSS startup costs to be recovered for 1997, 1998 and 1999. The Commission could approve the rates Qwest has developed on a company-wide basis, and set a limit on the amount of startup cost to be recovered in Washington. According to my estimate, calculated above, the Washington specific costs are approximately $21.2 million for 1997, 1998 and 1999. Qwest could track the OSS amounts collected in the state, and discontinue collecting the OSS startup costs once the limit was reached. This would eliminate the need to develop a Washington specific OSS rate and at the same time ensure that CLECs competing in Washington do not pay for OSS startup costs appropriately allocated to other states.

Q. DO YOU AGREE WITH MR. SPINKS THAT THE COMMISSION SHOULD CONSIDER ALTERNATIVES TO A "PER ORDER" CHARGE FOR RECOVERY OF OSS COSTS?

A. Qwest has repeatedly stated that it would be willing to entertain alternatives to the "per order" charge for OSS cost recovery. Several of the intervenors, including the Commission staff, have objected to recovery of OSS on a "per order" basis because service orders themselves did not cause the underlying OSS costs. However, none of the parties who have criticized Qwest's proposed method have offered an alternative method. Nor has anyone suggested rates that actually allow Qwest to recover its costs. Regardless of what vehicle is chosen for recovering the OSS costs, the total amount that Qwest seeks to recover from the CLECs will not change.

These same parties insist that each CLEC should bear only its fair share of the costs Qwest has incurred to modify the OSS on its behalf. Qwest believes that using service orders is an appropriate way to determine which CLECs are accessing the OSS to provide service to their customers, and thus, which CLECs are benefiting from the enhancements and modifications that Qwest has made to its OSS. Nevertheless, Qwest has considered using substitutes for service orders to recover its OSS. For example, it would be possible, although more difficult, to project demand on the basis of the number of products that the CLECs will order. This would associate an OSS charge with each wholesale product purchased by a CLEC and would accomplish the allocation of costs in a manner similar to a "per order" charge, but at a lower level of detail. Perhaps this would result in spreading the costs among the CLECs more fairly and accurately. Again, as long as Qwest is able to recover the costs it has incurred to modify its OSS for the benefit of the CLECs, it is willing to entertain alternative methods of recovery.

Q. PLEASE COMMENT ON MR. SPINKS PROPOSAL REGARDING HOW ILECS SHOULD RECOVER OSS STARTUP COSTS.

A. Mr. Spinks spends several pages discussing what he contends is the appropriate way to develop OSS startup costs, and then on page 6 arbitrarily recommends a $5.00 rate for recovery of OSS. While I do not agree with his approach to developing OSS startup costs, as explained above, I am at a loss to understand how he intends to support the validity of an arbitrary $5.00 rate. As this Commission has already determined, Qwest is entitled to recover its costs to modify and enhance its OSS for the benefit of the CLECs. In addition, the recent decision by the Eighth Circuit Court affirms, that Qwest is entitled to recover its actual costs, based in reality, for providing UNEs. Therefore, it makes no sense to propose an arbitrary rate simply because the real cost of OSS might disincent CLECs from competing in Washington. To put such a justification in perspective, it is important to remember that by paying to access Qwest's OSS, the CLECs are able to compete at a considerable savings because they are spared having to first duplicate 100 years worth of ILEC legacy systems and data.

Q. IS MR. SPINKS' DISCUSSION OF RETAIL RATES IN RELATION TO OSS COST RECOVERY APPROPRIATE?

A. No. As discussed in my direct testimony at page 13, OSS is a UNE. Therefore, discussion of recovery through retail rates, and the potential for rebates to retail customers, should not be part of this wholesale cost docket. Both Mr. Mark Reynolds and Mr. Carl Inouye discuss this issue in more detail in their testimonies.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.