BEFORE THE WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

In the Matter of the Petition of VERIZON NORTHWEST INC., For Waiver of WAC 480-120-071(2)(a)	Docket No. UT-011439 OPENING POST HEARING BRIEF OF VERIZON NORTHWEST INC.

I. INTRODUCTION

Chairwoman Showalter pinpointed the central issue of this case in her questioning of Staff witness Tom Spinks on January 24, 2003:

> **Q:** Then do you agree that there is some point at which something is simply too costly in real dollar terms relative to the benefit?
>
> **A:** Yes. A cost benefit analysis shows that all the time . . .

(TR 479)

Line extensions for the Timm Ranch and Taylor locations reach and far exceed that point. Their excessive cost to the general body of Washington ratepayers and to Verizon Northwest Inc. ("Verizon") far outweighs any marginal benefit of wireline service to the eight applicants at those locations. This case demonstrates why the Commission should set limits on the subsidization of wireline service to people who choose to live in remote areas that are enormously costly to serve, particularly when wireless alternatives are available. Other Washington customers should not have to pay for those choices.

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Verizon has demonstrated in this case that a waiver under WAC 480-120-071(7)(a) is warranted. Verizon should be relieved of its obligation to extend its wireline network to the Taylor and Timm Ranch locations under the excessively costly circumstances of this case.

II. BACKGROUND

A. <u>The New Line Extension Rule</u>.

Line extensions for telecommunications are defined as "extensions of company distribution plant to a location that is outside any municipal boundary and where no distribution plant of the extending company exists at the time the extension is requested."[1] The vast majority of Verizon customers never require line extensions. For most of its history, the Commission adopted a policy that divided the cost of extension between the customer and company, with the customer bearing a significant share. The Commission did not want other ratepayers to subsidize line extensions, if possible. (Ex. 32T p.5, 10). Until the new line extension rule took effect on January 1, 2001, Verizon's line extension tariffs reflected that policy by requiring customers to bear the expense of a line extension beyond a free allowance.[2] Verizon's tariff continued until 1999, when Verizon refiled its line extension tariff to mirror U S WEST's provisions, which also required significant customer contributions. That tariff lasted until the Commission's new line extension rule required the company to change it. (Ex. 7T pp. 16-17).

The Commission reevaluated its line extension policy in 1999 and 2000 and decided to materially increase the subsidization of line extensions for residential customers.[3] Under the new rule (WAC 480-120-071), companies were required to file tariffs that would only charge customers

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[1] WAC 480-120-071(1).

[2] The Commission approved the prior GTE line extension tariff in 1983, which provided for a charge of $440 per 1/10 mile for line extensions beyond the ½ mile free allowance. This c harge was intended to recover the entire cost of the added distance. (<u>See</u> Ex. 32T pp. 4, 5; 7T p. 17; 10 and 11).

[3] The Commission has a different policy for facilities extension for energy customers. For instance, Puget Sound Energy charges customers a base cost and a cost per foot to extend facilities. Facilities extensions for energy customers are not as subsidized, if at all, as are telecommunications line extensions under the Commission's new rule, WAC 480-120-071. <u>See</u> Puget Sound Energy Schedule No. 7, WNU-2, Second Revision Sheet 107-E canceling First Revision Sheet No. 107-E available on the Puget Sound Energy website, www.pugetsoundenergy.com.

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maximum initial and final payments of no more than 20 times each for the customer's basic monthly service rate, exclusive of all fees, taxes and other charges. For a Verizon customer this would amount to approximately $500 - $600 in total (TR 555), or just slightly more than the prior tariff charge to construct just one-tenth of a mile.

The Order amending and adopting the new line extension rule (Ex. 211) addressed "groups of people who were without service and people who have little or insufficient access to wireless communications." According to the Commission's web site, the new rule was intended to provide telephone line extensions "for those who live <u>just out of reach</u> of the telephone network." (Ex. 8 (emphasis added)).

The line extension rulemaking was controversial and was considered by the Commission at several open meetings. Commentators and Commissioners themselves recognized that the new line extension rule could not be absolute, requiring line extensions in all circumstances. Commissioner Showalter commented at the April 12, 2000 open meeting:

> I just don't know …to what extent an individual choosing to live very far away should be able to impose a very high price on others. It's the issue. And I recognize the phone is very important…but most people choose to live where such a thing is cheaper and doesn't impose costs on other people.

(Ex. 32T p. 7).

Clearly the Commissioners were concerned about having ratepayers subsidize customer choices. Thus, the waiver provisions of WAC 480-120-071(1) were adopted. The Commission needs the means to serve (as Dr. Danner put it) "as a gatekeeper to protect other customers (and the economy) from unduly costly line extension requests." (Ex. T32 p. 1).

In WAC 480-120-071(7), the Commission set forth seven criteria to consider in ruling on a waiver request. These are not the only considerations for the Commission. At all times the Commission must act in the public interest, which may incorporate considerations other than the

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enumerated waiver criteria. RCW 80.01.040(2).[4] As explained herein, this case presents the Commission with the first opportunity to serve as gatekeeper. Under the new provisions, Verizon has been asked to extend facilities to seven residents and one potential resident at two locations at an initial total cost of at least $1.2 million. The facts and circumstances here – costs, both initial and ongoing, and the availability of wireless service -- demonstrate that the Taylor and Timm Ranch locations' circumstances justify the waiver.

III. FACTUAL BACKGROUND.

The two initial applicants in this case, Kay Taylor and Ike Nelson, live in Douglas and Okanogan Counties in unpopulated, rural areas. The photographs displayed at hearing demonstrate the openness, vastness and rugged terrain of this part of eastern Washington (See photos in Exs. KR-5, KR-6, 12).

A. Taylor Location.

Kay Taylor has lived for 28 years in a residence located at the end of a dirt/gravel road (Hayes Rd.), over two miles from State Highway 17 and seventeen miles from the town of Bridgeport (Amended Petition for Waiver, p. 2). Mrs. Taylor co-owns a janitorial company in Grand Coulee, 28 miles away, which she considers her general community of interest. (Ex. 172 pp. 2-3).

Mrs. Taylor initially contacted Verizon in the spring of 2001 about a line extension to her home and ultimately placed a service order request on December 7, 2001. (Ex. 172 pp. 38, 40).

Mrs. Taylor currently meets her telecommunications needs with cell phone service from Americell Communications and AT&T Wireless Service. RCC Communications cellular service is also available.[5] In addition, Mrs. Taylor pays $79 a month for DirectTV satellite service and has looked into getting Internet access in conjunction with that service. (Ex. 172 pp. 5, 6, 8, 13, 18-20).

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[4] The Commission has stated "'public interest' is a broad concept encompassing the welfare of present and future consumers, stakeholders and the general public." *In the Matter of the Petition of United States Cellular Corporation*, Docket No. UT-970345, Third Supplemental Order ¶ 38 (Jan. 27, 2000).

[5] The RCC service was provided to both Mrs. Taylor and Mr. Nelson as a result of this case to explore its capabilities at each location. Verizon worked with RCC to accomplish this. (TR 191, 271).

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While five residences are on Hayes Road, only four have full-time occupants. (Ex. 172 p.7). Of the four, Verizon received service order requests only from Mrs. Taylor and Mrs. Wendy Schomler, who rents a house owned by Mrs. Taylor, located next to the Taylor house. (Ex. 1T p. 2).

Verizon received a third service order request from Mrs. Ann Nichols, who requested service at 51 Hayes Road for a house she plans to build. She currently lives in Arlington, Washington. (Ex. 1T pp. 2-3).

Another Hayes Road resident, Margarete Weisburn, does not want phone service from Verizon. She meets her needs by use of 2-way radiophone equipment that she purchased. (Ex. 1T p. 3).

Verizon's engineers visited the Taylor location several times and calculated an estimated cost to extend service to the three applicants at the Taylor location. Verizon's total estimated minimum construction costs are $329,839, or $109,946 per applicant. (Exs. 1T p.5; 3). Thus, the amount the applicants would pay under the line extension rule would be only a half of one percent of the actual cost.

Extending service to the Taylor location is so costly because Verizon would have to place copper cable facilities for about 15 miles along State Highway 17 and then over 2 miles along Hayes Road. The actual construction costs may well be higher than estimated because of the anticipated basalt rock common to the area. (Ex. 1T pp. 5-6).

In the normal course of its business operations, Verizon would not extend its network to provide service to the Taylor location, due to the high costs involved and the lack of any forecasted growth in the area. (See Exs. T-7 pp. 7-8; 217c; TR 200-201, Amended Petition for Waiver ¶ 7.) On October 24, 2001 Verizon filed its Petition for Waiver, to be relieved of providing the line extensions requested for the Taylor location.

B. <u>The Timm Ranch Location</u>.

Einar ("Ike") Nelson lives at 224 Timm Road in Okanogan, Washington. A former Qwest employee for more than 42 years, Mr. Nelson and his family own Timm Brothers, Inc., which runs the Timm Ranch, a large cattle ranching operation in Okanogan County. The Timm Ranch consists of about

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10,000 deeded acres and contains five private residences. Four are occupied by Timm family members and the fifth is used for other ranch employees. (Ex. 171 p.9; Ex. 121T pp. 3, 4). In addition, the Timms rent up to 100,000 additional acres for their cow/calf ranching operations. (Ex. 121T p. 4).

Verizon received a Service Order Request on June 15, 2002 from Mr. Nelson and subsequently received four other Service Requests from applicants who lived beyond Mr. Nelson's location on Timm Road, all of whom are either related to the Timm family or work as employees of Timm Ranch, Inc. Mr. Nelson has radiophone service at his residence, which gives him dial tone across the Columbia River from the Qwest Coulee Dam Exchange (Ex. T1 p. 5). Wireless service is also available at his home from RCC Communications. (Ex. 91T p. 9). All of the applicants at the Timm Ranch also currently receive Verizon Wireless cellular service, although they have to go varying distances outside their homes to pick up the signal. This service is also usable at many locations around the Timm Ranch. (Ex. 171 p. 23).

Verizon's engineers went to the Timm Ranch location that lies just within Verizon's Bridgeport exchange area on the north side of the Columbia River. Verizon determined that it would have to construct nearly 30 miles of facilities to reach all of the applicants at the Timm Ranch location (Ex. 1T p. 7). Verizon would install fiber optic facilities and signal boosters in order to provide service to the Timm Ranch. Approximately 23 miles of the route would be along a dirt road. The terrain is extremely rocky, indicating a need for expensive backhoe or rock-cutting equipment in order to place the cable. (Ex. 1T p. 8). Verizon determined it would cost $881,497 to provide service for the five Timm Ranch sites, or a per-applicant cost of $176,299. (Ex. 1T p. 5; 4). Thus, the amount each applicant would pay under the line extension rule would be about a third of one percent of the actual cost.

Given these excessive costs, Verizon filed a petition for a waiver of its obligations under WAC 480-120-071 for the Timm Ranch location with this Commission. [6]

[6] Verizon's original Petition for Waiver, filed on October 24, 2001, covered only line extension requests from Mr. Nelson and Mrs. Taylor. Verizon filed an Amended Petition for Waiver on February 21, 2002 to cover all of the applicants at the Taylor and Timm Ranch locations.

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IV. WAIVER CRITERIA

WAC 480-120-071(7)(b)(ii) lays out seven criteria for determining whether granting a waiver is consistent with the pubic interest. While the rule does not define how to weigh each of the enumerated factors, it is clear that cost can be, as in this case, a compelling reason to grant a waiver. This portion of the brief separately discusses each of the criterion and the related evidence.

A. The Total Direct Cost of the Extension is Disproportionately High by Any Measure.

The first waiver criterion appropriately asks: What is the "direct cost" of the extension?[7] Here, the total cost estimated by Verizon for these extensions is $1,211.336. There is no dispute over the accuracy of Verizon's cost estimates. (TR 618).

By any reasonable, objective economic standard, the Timm and Taylor Ranch costs are too large to justify providing Verizon wireline service. Verizon witness Dr. Carl Danner explained why "these extensions are just not worth the expense, no matter who might end up footing the bill." (Ex. 30T p. 2).

1. System or Societal Costs.

Dr. Danner analyzed the Timm Ranch/Taylor line extension costs from two perspectives. The first was a broader societal viewpoint that concludes that the cost to society as a whole is far greater than any offsetting benefit to the subscribers in question. Dr. Danner explained that building a line extension uses up real resources that could otherwise be used to provide service to a greater number of customers. It makes economic sense to go ahead and consume those resources only when the result is more valuable than what is consumed in achieving it. In other words, if a dollar's worth of resources is consumed to create a product worth two dollars, this is an economic gain. On the other hand, it makes no economic or practical sense to consume a dollar's worth of goods to create something worth only 50 cents to a customer. (Ex. 30T p. 6). In this case, the value of providing line extensions to the Taylor

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[7] The term "direct cost" is not defined in the rule, but the common sense and economically correct meaning is all costs that it will actually incur to provide service at either the Timm or Taylor locations. This includes so-called "reinforcement" and "network upgrade" costs because Verizon would never, in the normal course of operations, incur those costs but for the mandates of the line extension rule and these applications.

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and Timm Ranch locations to the applicants is considerably outweighed by the vast amount of resources consumed to provide line extensions. (Ex. 30T p.12).

The relevant economic question here is: How valuable is wireline service to the applicants at the Taylor and Timm Ranch locations? Clearly it is not valuable enough to them to pay the total direct costs. There is no evidence that Kay Taylor or the Nelsons offered to do so (Exs. 565; 566). Indeed, the evidence shows that neither Mrs. Taylor nor Mr. Nelson valued wireline phone service enough to pay the considerably smaller charges of $23,000 to $40,000 more than 10 years ago to get line extensions.[8] (Exs. 171 p. 13; 172 p. 16). All that the record shows is a willingness to pay the nominal charge of $500 - $600 for a line extension, which is a fraction of one percent of the actual cost.

Dr. Danner explained that there is no reasonable way to conclude that the extensions at issue would create, for instance in the Timm Ranch location, in excess of $150,000 in value for each customer. (Ex. 30T p. 12). Given this conclusion, there is no principled economic reason to consume the vast physical resources involved in providing the line extensions at issue here. The high cost of doing so dwarfs any possible benefit to the customer.

Furthermore, the value to society of adding these locations to the wireline network is disproportionately small in comparison with the cost of doing so. As Dr. Danner explained, the externality value for other customers of having a network that includes the Taylor/Nelson location is quite small, particularly when both have substitute means of connecting to communications networks. (Ex. 30T p. 8-9; TR 262-63). To get this marginal benefit requires the devotion of significant resources – resources that could be devoted to providing line extensions to more customers. Verizon could provide typical line extensions to 120 customers – instead of eight – with the resources at issue in this case.[9]

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[8] Mrs. Taylor and Mr. Nelson did not attend the hearings in this case.

[9] This is premised upon Verizon's experience under the new line extension rule of an average cost of $10,000 per customer. (TR193).

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Dr. Danner concluded "it is not fair to require customers or shareholders to subsidize line extensions that will not benefit them (or anyone) in any way proportional to their costs." (Ex. 30T p. 3).

2. Verizon's Costs For These Locations Would Be Excessive.

Dr. Danner and Kay Ruosch also discussed the real excessive costs that would be incurred by the company unless these waiver petitions are granted.

(a) Initial Construction Costs

The minimum total cost estimated for the Taylor line extension initial construction is $329, 849, or $110,000 per customer. (Ex. 3). Ms. Ruosch testified to an average per customer cost of $10,000 for line extensions under the new rule. (TR193). Thus, the average per-customer cost to provide line extensions to the Taylor location is more than eleven times the average. The per-customer cost for the Timm Ranch location of $176,000 is seventeen times the average. The initial construction cost estimate for this location is $881,497. (Ex. 4).

The total direct costs of $1,211,336 for just eight applicants would consume at least 40% of the 2002 construction budget for the entire Wenatchee District. (Ex. 1T p. 9). These estimates are likely too low, because Verizon will probably encounter conditions during actual construction (e.g., rock conditions) that increase costs. (Ex. 1T pp.6; 10).

(b) Ongoing Maintenance and Replacement Costs

The plant that would be placed for the Taylor and Timm Ranch locations will require maintenance. Given the loop lengths at issue, Verizon realistically anticipates increased maintenance costs. The Timm Ranch line extension would create the only local loop of its kind in the Verizon network in Washington because it would have no customers for a 23-mile stretch. (Ex. 1T p. 10). The average loop length for a Verizon line extension under the new rule is 3,800 feet. (Ex. 7T p.9).

The longer the circuit, the more difficult and costly (in dollars, equipment and man-hours) it is to maintain. (Ex. 1T p. 12-14). Maintenance difficulties are exacerbated by access conditions. For instance, the roads at the Timm Ranch are dirt and/or gravel. Key portions are not plowed in the winter

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by Okanogan County. (Ex. 544). In sum, adding these line extensions will escalate Verizon maintenance costs.

Finally, the Commission cannot ignore replacement costs when this plant wears out. Verizon will ultimately have to replace this plant at the conclusion of its normal lifespan. If the cost in 2003 is $1.2 million, the cost in the future will inevitably surpass this figure, which the Company will not be allowed to recover with reimbursement under the line extension rule.

The facts of this case show that the Taylor and Timm Ranch line extensions would be extraordinary in terms of their length, their construction costs and their ongoing maintenance and replacement costs. The numbers speak for themselves: <u>$1.2 million for eight customers is just too much</u>. No other factor here offsets the consequence of this cost.

Mr. Shirley for the Staff unreasonably suggests such a cost is not too much, but he considers a <u>$100 million</u> cost the outer boundary. (TR686-87). Because these projects are so costly and burdensome, Verizon should not build them under the line extension rule.

B. <u>The Number of Customers to Be Served</u>.

In the Order enacting the line extension rule, the Commission intended to benefit "*groups* of people who are without service." (Ex. 211 p. 4, ¶ 23; emphasis added). The Commission did not intend to enact a rule that would be disproportionately beneficial to only a few customers, as in this case.

With respect to the Taylor location, only <u>two</u> current residents requested line extensions.[10] There is no evidence in the record, or reason to believe, that the Taylor location will experience growth in the number of customers to be served. To the contrary, the forecast for the Bridgeport exchange shows a current negative growth pattern. (Ex. 217c).

The Timm Ranch location involves only five customers spread across a wide area on the Timm Ranch. Again, there is no reason to believe that any additional customer growth will occur on the Timm

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[10] The application for Mrs. Nichols warrants separate consideration because she does not yet live on Hayes Road yet. She currently lives in Arlington, Washington but plans to build a home there in the future. (Ex. 1T pp. 2-3).

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Ranch. Indeed, given the nature of this ranching operation, it seems highly unlikely that additional customers will move to the Timm Ranch location.

Thus, this Commission must decide whether seven actual residents and one potential resident warrant the cost of extending wireline service to them. In the Commission's cost/benefit analysis, the fact that the number of customers is so small favors a waiver rather than spending $1.2 million.

C. The Comparative Price and Capabilities of Radio Communications Service and Other Alternatives Available to Customers.

Kay Taylor currently has telecommunications service from three providers: Americell, AT&T Wireless and RCC Communications. These services work and connect Mrs. Taylor and her family to the outside world. The RCC wireless service connects her to the appropriate 911 public safety answering point. (Ex. 301). In short, Mrs. Taylor has a suitable substitute for landline service and there is no need to force Verizon to provide landline service at such a huge expense.

In addition to her three wireless providers, Mrs. Taylor gets television service through satellite and has investigated, and knows she can get, Internet service through satellite, which is available from many providers. (Exs. 1T pp. 11-12; 172 p. 28).

With respect to price, Mrs. Taylor readily pays $79 a month for cable television service and incurs almost $8,000 a year for her wireless phone bills, which includes business uses. (Ex. 172 pp. 41-42).[11] She testified that she can also use her AT&T Wireless cell phone from her home and that it is more reliable than the Americell phone. (Ex. 172 pp.. 26-27). Finally, Mrs. Taylor's service from RCC appears reasonably satisfactory to her. Ms. Taylor informed RCC that her service "works good." (Ex. 309).

All the applicants at the Timm Ranch have cellular service, which they can use on the ranch. (Ex. 171 p. 23). Mr. Nelson recently built a new home and presumably did so knowing the site's telecommunications capabilities. (Ex. 171 p.13) Mr. Nelson did not cite cost as a reason for

[11] According to Mrs. Taylor, her Americell phone service can be used to call police, fire or ambulance, even though she may have occasional problems, perhaps 2-3 times a year, with that phone service. She now has RCC service available, as well, which also reaches 911. (Exs. 172 pp. 22-23; 301).

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requesting Verizon wireline service under the line extension rule. Wireless service is also available from RCC. RCC tested phone cell system at Mr. Nelson's residence and elsewhere on the Timm Ranch for purposes of determining if RCC's service was workable. RCC's engineers were able to establish that a phone cell system would probably work at the Ike Nelson and Bob Timm residences, but not the other residences on the Timm Ranch with normal equipment. (Ex. 91T p. 9). Because of where the other residences were built, a nearby mountain obstructs existing cell site signals. (Ex. 91 p. 12). However, this does not mean that other technological solutions are not available, or could not be developed in the near future. Kay Ruosch described some of the alternatives available to provide service to the applicants at both the Taylor and Timm Ranch locations. (See Ex. T1 pp. 11-13). Dr. Danner also pointed out that a technological solution to providing better wireless service at the Timm Ranch location may be on the horizon. (TR 269-71). As new equipment is developed, it is possible that this may facilitate more and more alternative means of providing telecommunications services.[12]

The applicants at the Taylor and Timm Ranch locations are not without telecommunications services. Both lead applicants, Kay Taylor and Ike Nelson, have found creative solutions to meet their needs through wireless, satellite or radiophone. These customers will not be left stranded without phone service if this Commission grants Verizon's waiver applications. They can continue with RCC service, which Verizon played a part in providing to them due to its cooperation with RCC. They can investigate satellite and other alternatives. They can explore the ever-increasing technological options offered by niche providers of telecommunications services to highly rural areas.

In short, the present and future availability of multiple wireless communications options at the Taylor and Timm Ranch locations weighs in favor of granting Verizon's requested waiver.

D. <u>Technological Difficulties and Physical Barriers Presented by the Requested Extensions</u>.

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[12] <u>See</u> <u>i.e.</u>, the plans of companies such as EXTEND AMERICA, a new commercial wireless company to provide wireless services to underserved rural markets. Information about this company is available at www.extendamerica.com.

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The line extensions at issue here pose unique technological difficulties and face unique physical barriers, primarily due to the distances involved and the nature of the terrain. These lengths make the Timm Ranch and Taylor projects stand out among other Verizon line extension projects for a number of reasons. Their construction would consume a tremendous amount of equipment and manpower resources, including the prolonged use of one bulldozer, two backhoes, one boring machine, one rock saw cutter, four to five medium trucks, and one fire protection truck. The Taylor job would require 1500 man-hours of work, and the Timm Ranch job would require 2800 man-hours. (*See* Ex. T1 pp. 10-11).

Furthermore, the areas in question appear to be quite rocky. Mr. Nelson acknowledged the presence of basalt conditions. (Ex. 171 p. 19). Such conditions over a long stretch raise costs significantly.

The Columbia River is a huge physical barrier that would require Verizon to serve the Timm Ranch location out of its Brewster exchange, even though the Timm Ranch is technically located within Verizon's Bridgeport exchange. (TR 132; Ex. T1, p. 7). This physical barrier

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requires construction of nearly 30 miles of facilities to reach the Timm Ranch applicants. *Id*. As Ms. Ruosch explained (based on her 25 years of experience), the Taylor and Timm Ranch locations would pose unique and difficult maintenance issues. For instance, the facilities involving the Timm Ranch location would have to be placed along 18 miles of a dirt county road that is not maintained in the winter and would most likely be inaccessible during snowy periods. In any event, increased manpower would be required to detect problems along the unusual loop lengths that would be required for the Taylor and Timm Ranch locations (Ex. T1 pp. 13-14). While Verizon does construct line extensions in the Wenatchee district that might involve dirt roads and rock cutting, none pose the level of technological difficulties and physical barriers that are presented by the Taylor/Timm Ranch extensions. What might be manageable or reasonable for a short distance (i.e., rocky conditions) becomes a significant barrier if encountered for many miles. Again, this factor supports a waiver.

E. <u>The Effect on the Individuals and Communities Involved</u>.

1. <u>Common Impacts</u>

The subsidized construction of these extensions under the Commission's rule would provide a significant financial windfall to the applicants. The value of the remote rural land owned by Mrs. Taylor, Mrs. Nichols and Mr. Nelson and his family, and the other applicants would increase due to the presence of wireline phone service. (TR 266, 282). The Commission will have to consider whether this benefit should come to these applicants at such a low price to them and at such a high price to ratepayers.

2. <u>Taylor Location</u>.

The Taylors have chosen to live on Hayes Road, without landline phone service, for over 28 years. The Taylors have found means to meet their telecommunications needs through a combination of wireless and satellite services. Granting Verizon's waiver request would not leave these individuals without telecommunications services at this time.

Nor would granting the waiver impact any "communities involved." Mrs. Taylor identifies her community of interest as Grand Coulee, 28 miles away. (Ex. 172 p.5). There is no evidence of record

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that shows that lack of wireline phone service impacts that community or Mrs. Taylor's ability to be involved within it. Of the other "neighbors/residents" along Timm Road, only Wendy Schomler, Mrs. Taylor's tenant, wants wireline phone service. Mrs. Weisburn affirmatively does not. None of the other neighbors identified by Kay Taylor have asked for Verizon's wireline service, with the exception of Mrs. Ann Nichols, who is not yet a full-time resident. On balance, a decision to waive Verizon's line extension obligations for the Timm Road will have little to no impact on at least half of the individuals located along that road, and the others acquired their property or took up residence without expectation of receiving subsidized wireline telephone service.

3. Timm Ranch Location.

It is clear that the major impact of requiring Verizon to extend a line to the Timm Ranch location would be to benefit Timm Brothers, Inc., a major cattle ranching operation. Yet, Staff witness Duft described a thriving cattle ranching operation that has been successfully run without the benefit of wireline telephone service for almost 50 years. The value of the cattle alone tops $1.68 million. (TR 541-542; Ex. 554). This clearly is a significant commercial enterprise.

When asked why wireline telephone service was desired, Mr. Nelson stated he intended to use it heavily for the ranching business. "It would get used a lot there, not only in my personal set here, myself, but also for the ranch itself. A lot more business could be transacted out there." (Ex. 171 p. 26 (emphasis supplied)).

No matter how Staff might try to characterize Mr. Nelson's farmhouse as a "qualifying premise," the Commission cannot avoid the inescapable conclusion that it would be subsidizing primarily a commercial operation if it required Verizon's ratepayers to pay $900,000 or more to bring wireline telephone service to Timm Ranch. This is wrong. Even Mr. Shirley admits that businesses – other than cattle ranch businesses -- should "have to pay the full cost of getting an extension to them." (TR 650). The line extension rule by its definition of "premises" expressly excludes subsidizing line extensions for predominantly commercial or industrial uses. As a matter of good regulatory policy, this exclusion

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makes sense. Ratepayers should not be forced to subsidize profit making commercial endeavors, such as Timm Brothers, Inc.

In the Timm Ranch situation, clearly the effect on the individuals and communities involved would be unfairly and disproportionately beneficial to their business.[13] Conversely, granting Verizon's application for a waiver for the Timm Ranch location will not have a negative effect on the individuals and communities involved that would warrant the significant excessive cost. While having wireline phone service may only enhance the commercial operation of Timm Ranch, there is no evidence that the lack of phone service has inhibited the Ranch's ability to develop into a successful operation or that it has deterred the applicants from taking up residence there. Mr. Nelson stated that he and the other residents all have wireless phone service that allows them to connect to their neighboring communities such as Okanogan. (Ex. 171 p.24). Given the nature of a cattle ranching operation, wouldn't a wireless phone would be more beneficial than a wireline phone because the applicants are required to travel regularly around the ranch acreage? Mr. Nelson also meets his needs with a radiophone. In addition, the ranch has the ability to conduct business using cable television service, which enables Mr. Nelson to see Timm Ranch cattle sold over the Internet. Mr. Nelson also indicated in his deposition that he would be willing to further explore satellite or other possibilities for meeting his needs. (Ex. 171 p. 25). Mr. Nelson is a highly capable, resourceful rancher, well versed in telecommunications capabilities. There is no reason to believe, <u>and Staff has presented no evidence to the contrary</u>, that the residents at the Timm Ranch location are so negatively impacted so as to justify an expenditure of $881,447 to bring them wireline service.

Finally, Mr. Nelson's line extension expectations should be framed over the years by his experience as a trustee for the Nespellem Valley Election Co-Op, Inc. That utility gives customers a $1,500 credit for a line extension but charges $7 per foot for any additional costs associated with line

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[13] This case does not involve the policies associated with subsidizing agriculture as an industry.

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extensions. (Ex. 590). Mr. Nelson would have to pay $36,960 a mile for a line extension from this cooperative – not a total cost of between $500-$600.

In sum, the impacts that all of the applicants will receive are disproportionately beneficial to them as opposed to the other customers of this state. This factor favors a waiver.

F. <u>The Effect on the Public Switched Network</u>.

The addition of eight new customers would add *de minimus* value to other subscribers on the public switched network, at a disproportionately high cost to the other subscribers. Dr. Danner explained how the "externality argument" (which relates to the notion that the public switched network is more valuable if more people are added to it) really fails to justify network expansion at any cost. (TR 262-263).

More importantly, a decision to require Verizon to construct <u>these</u> line extensions by implication means that the resources these consume will not be available to expand the public switched network in other areas that would otherwise warrant it. As Ms. Ruosch explained, networks generally expand in relation to projected demand and growth. (TR201). Requiring an expansion where growth and demand does not warrant it is not an efficient economic way to plan and construct the public switched network. Instead, requiring the Taylor/Timm Ranch line extensions would simply add additional new burdens on the public switched network that go beyond mere installation, such as increased maintenance costs and inevitable replacement costs.

In this case, it is difficult to see how the public switched network would benefit at all from the Taylor/Timm Ranch line extensions, but it is uncontroverted that any marginal benefit would outweigh the enormous initial and ongoing costs. Again, in the waiver evaluation process, this factor favors Verizon.

G. <u>The Effect on the Company</u>.

Verizon did not file this petition lightly to avoid a new regulatory burden. To date, Verizon has complied with the greatly increased number of line extension requests it has received since the new rule went into effect. It has constructed 85 line extensions since the line extension rule took effect with the

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exception of the Taylor and Timm Ranch locations. Prior to the new line extension rule, Verizon did one or two line extensions per year. (TR 192). Verizon filed this petition because these applications' extraordinary and enormous costs would negatively impact the company and its customers in financial and operational terms, in both the sort and the long run.

The initial $1.2 million cost would clearly have a negative effect on the company. This amount represents a disproportionate share (40%) of the company's Wenatchee District annual construction budget.[14] (Ex. T1 p. 9). The projects would consume significant equipment and manpower resources both for the construction and ongoing maintenance -- "a significant drain on the company's resources for constructing and maintaining the rest of the network," at best forcing a delay in other projects. (Ex. 1 p. 15).

Moreover, the Staff advocates a position that would significantly limit the amount of initial cost recovery to Verizon under the Commission's rule. Mr. Shirley claims that $309,000 would be excluded from recovery as "normal reinforcement costs." (TR 200-201; Ex. 217c; Ex. T7, pp. 7-8). He also erroneously claims that Verizon has already received or somehow will receive the $309,000 in reinforcement costs for the Timm and Taylor Ranch and that somehow basic rates provide a revenue stream to cover these "normal" reinforcement costs. If the Commission were to adopt his position, obviously the Company would bear an immediate impact of $309,000 to provide phone service to eight applicants – enough to build 30 average line extensions. Even this amount is excessive: $38,600 per customer.[15]

[14] Ms. Ruosch further explained that the company sets its construction budget in advance, but cost recovery under the rule would come in well after these budgets are set.

[15] Staff's positions on "reinforcement costs" and supposed prior or other cost recovery is erroneous and should be rejected by the Commission. None of the direct costs of these projects should be excluded as "reinforcement" because none would ever be incurred but for these line extensions - especially the out-of-exchange construction for the Timm Ranch. No other growth would warrant this construction. (TR 200-201; Ex. 217c; Ex. T7, pp. 7-8). Verizon has not and will not receive any "universal service" reimbursement for these projects, under a "fill factor" or any other theory. (TR 486; Response to Bench Request No. 800).

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In any event, the Company would experience ongoing increased maintenance costs. The Staff belittles these increased burdens, but cannot identify any similar loop of the length and character as would be in place for the Timm Ranch location (TR 448-49). Ms. Ruosch described in detail the problems associated with maintaining such a long loop, because it is placed along dirt country roads that are not maintained in the winter and it faces a number of other potential damages due to natural occurrences, animal activity, and human actions. (Ex. 1T p.14).

Also, the Company would face enormous future costs for the inevitable replacement. (Of course, if demand for service in the Taylor and Timm Ranch locations were to disappear before the end of the plant's service life, the $1.2 million would have been even more of a waste of resources.)

Clearly, Verizon brought this petition because these line extensions would have a serious negative effect on the company's operations in Washington State. It already operates under serious financial constraints because it is earning less than 2% rate of return. (TR 289). Verizon also brought this petition because its customers would be ill served by such a wasteful allocation of what are relatively scarce resources in today's economy. Verizon believes it has an obligation to protect its customers against such economic waste.

H. Verizon is Entitled to a Waiver under WAC 48-120-071.

The intent of the new line extension rule was to address "groups of people who were without service and people who have little or insufficient access to wireless communications,"[16] and who "live just out of reach of the telephone network." (Ex. 8). Clearly this is not the case for these applicants. These isolated locations do not amount to "groups" of people, and, in any event, they have chosen to reside far beyond the reach of the wireline telephone network.

The new line extension rule WAC 480-120-071 does not require line extensions in all circumstances. Its waiver provisions embody a "rule of reason" consistent with the law in this area as expressed in an excerpt from a legal treatise:

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[16] Ex. 211.

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> The right of an inhabitant or group of inhabitants of a community or territory served by a public service company to demand an extension of service for their benefit is not absolute and unqualified but is to be determined by the reasonableness of the demand therefore under the circumstances involved. The duty of a public service company to extend its service facilities, and the reasonableness of a demand for such extension, depends in general upon the need and costs of such extension and the return in revenue that may be expected as a result of the extension; the financial condition of the utility, the advantages to the public from such an extension; and the franchise or charter obligation to make such extension.

64 Am. Jur. *Public Utilities* § 37.

As the above passage illustrates, deciding whether an individual should receive a subsidized line extension involves a balancing of competing interests. While the balance clearly weighs in favor of a waiver in this case, the Commission's decision need not establish a bright line rule for all line extension requests, and Verizon does not ask the Commission to take on this difficult task at this time. Rather, Verizon recognizes that waivers need to be determined based upon the particular facts and circumstances of each case. As Dr. Danner noted, however, whatever decision is reached in this case will send a signal to companies and citizens as to the limits of Washington's new line extension rule and the extent to which the Commission will subsidize those who choose to reside in remote, high cost locations.

Here, there is really no question under the facts of this case as to the appropriateness of a waiver. To summarize --

1. The Cost is Simply Too High.

The total financial and operational costs of constructing the requested line extensions are so disproportionately high in relation to any possible benefits as to warrant a waiver.[17] The $1.2 million cost is not in dispute.

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[17] If no line extension rule existed and Verizon voluntarily incurred these costs, the Commission could well question the prudency of those costs and possible disallow them as unreasonable. While the line extension rule exist, it does not make these costs any less unreasonable or relieve Verizon of its obligations as a public utility to carefully manage its budget so as to avoid incurring unnecessary costs to be recovered in rates. "A public utility will not be permitted to include negligent or wasteful losses among its operating charges, for the purpose of fixing rates… Losses due to unnecessary errors in the construction and equipment of plants, and to lack of ordinary economy, foresight, and efficiency in management, are likewise improper charges to operating expenses." 64 Am.Jur.2d Public Utilities § 131.

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By any measure of reasonableness the direct cost of the Timm Ranch/Taylor line extensions is too great to ask the company and the ratepayers to bear. All parties agree that it is difficult, if not impossible to draw a bright line above which service should not have to be provided (TR 230, 255). Nonetheless, Dr. Danner provided the Commission with one common sense way to consider how far to go in considering the direct cost as a determinant of whether the line extension is to be provided. Dr. Danner testified that he would not go above a $15,000 to $20,000 cost per-customer range and that even this range fails as a matter of simple economics. He said:

> It is clear from a matter of simple economics that most of the line extensions that the rule permits don't pass an economic test. They do cost more than they are worth, but economics is not the sole determinant of the Commission's policy and economics is not the sole determinant of universal service concerns and other things the Commission is responding to in promoting the rule.

(TR 230). However, his figure of $15,000 to $20,000 as the outer limit of acceptable costs is premised on consideration of other values rather than simple economics (*i.e.*, the Commission's desire to help customers in remote places get phone service). Dr. Danner equated the $15,000 to $20,000 range as the equivalent of subsidizing the provision of a new car to a customer. He said, "Is the phone line worth as much as a new car would be? It seems to me that is starting to stretch it."

He posed another similar to view the outer limits, as a matter of social policy, for the subsidization of phone service in rural areas. He theorized that a company could support approximately a $1,600 investment from basic rates on an annual basis and that it might be reasonable to ask other customers to subsidize a capital investment of up to ten times that amount.

> If you say, all right, we're going to have the customer pay for that and we will foot the bill for the rest, $16,000 is about ten times what the basic rate would support in terms of capital recovery. That's another idea for a threshold. (TR. 232)

Dr. Danner's testimony establishes that the costs associated with the Taylor/Timm Ranch line extensions are disproportionately beyond the bounds of a reasonable cost that society, the company and rate payers should be asked to bear. In his view, even a cost of $15,000 to $20,000 is "way past any economic justification for the service" (TR. 261), but that amount includes recognition of some of

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the non-quantifiable factors that need to go into the balancing process in order to determine if a waiver is appropriate.

In contrast, the Staff has provided no guidance to this Commission on how to establish the outer bounds of reasonableness for line extension costs. When pressed by Commissioner Oshie and Chairwoman Showalter, Staff witness Shirley would only admit that the upper bounds of reasonableness would be $100 million for any line extension. (TR686-87). At no point in its written or live testimony did the Staff suggest that any situation would ever warrant a waiver, no matter the cost. Clearly, such an absolutist position completely ignores the importance of the first waiver criteria – consideration of costs. The Staff has not identified any truly strong countervailing reason for requiring this excessive expenditure. Staff does not identify which of the other waiver criteria counteracts the disproportionately high economic costs of these projects. In fact, <u>none</u> of the factors warrant requiring these line extensions, leaving aside the issue of cost.

2. <u>The Costs Exceed the Benefits</u>.

In order to conduct a cost-benefit analysis the Commission should consider what benefits would be derived from requiring these line extensions. According to Dr. Danner, the value of landline phone service to Mr. Nelson or Mrs. Taylor is bounded by the fact they declined the opportunity to get line extensions years ago at an amount much lower than today's costs. At that time, neither Mrs. Taylor nor Mr. Nelson wanted to pay the actual cost of the line extension.

Mrs. Taylor and Mr. Nelson have found alternate ways to substitute for landline service. Accordingly, wireline service would only be an enhancement to the substitute phone service that each applicant has already utilized to date.

In contrast, the Commission should consider what benefit or value to society adding these customers to the wireline network will bring – particularly in comparison to the costs involved to add them to this network. Little value to society is added when a wireline service is provided to a customer that can be reached by wireless capabilities. (TR 477-78).

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The externality value of adding eight new customers to the network is certainly *de minimus* in comparison to the excessive cost of adding them. Clearly these line extensions would add minimal if any benefit or value to our current telecommunication system. Instead they simply provide a really good deal to those applicants who only have to pay a fraction of the cost of receiving phone service.

3. <u>The Ratepayers/Verizon Should Not Subsidize Commercial Operations or the Chosen Life Styles of Customers in Remote Areas</u>.

The clear benefit to Timm Ranch, Inc. of requiring these line extensions cannot be escaped. Requiring these line extensions to a major cattle ranch, subsidized by Washington's ratepayers and/or the company's shareholders, clearly contradicts the purpose of the line extension rule. That rule expressly reflects a policy against subsidizing commercial endeavors.

The Timm Ranch/Taylor requests also raise the legitimate question of whether society should subsidize the choices of citizens who choose to live in remote locations. Mrs. Taylor chose to move to her residence 28 years ago for the benefits of a rural lifestyle for her family. She has, among other things, willingly paid thousands of dollars for wireless telecommunications services in order to maintain her chosen lifestyle. As Ex. 545 demonstrates, people choosing to live in rural areas face different realities and should be expected to have different amenities than those that might be expected in a more populated environment. The Chelan County Code of the West (Ex. 545) advises newcomers: "It is important for you to know that life in the country is different from life in the city." (p.1). It warns "Water, sewer, electric, telephone and other services may be unavailable or may not operate at urban standards" <u>and</u> "It can be very expensive to extend power lines to remote areas." (p.3). This document illustrates that people who choose to live "in the country" do so with the understanding that they make trade-offs that mean they cannot expect the same services at the same costs as their urban counterparts.

V. CONCLUSION

In sum, Verizon requests the Commission to find that it is not reasonable to ask the company and ratepayers to pay $1.2 million up front and significant amounts in the future to bring wireline service

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to these eight customers <u>in this case</u>. From an operational, economic or fairness standpoint, the line extension costs here are not reasonable.

On balance, the factors for establishing waiver have been met. The public interest would be served by finding that the costs in this case do not warrant the requested extensions.

DATED this _____ day of March, 2003.

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