BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

AT&T COMMUNICATIONS OF THE PACIFIC NORTHWEST, INC. Complainant, v. VERIZON NORTHWEST INC., Respondent.	)	Docket No. UT-020406

ANSWERING POST-HEARING BRIEF OF

AT&T COMMUNICATIONS OF THE PACIFIC NORTHWEST, INC.

June 17, 2003

TABLE OF CONTENTS

I. INTRODUCTION

1. The Commission has repeatedly indicated its desire to consider the merits of the Complaint filed by AT&T Communications of the Pacific Northwest, Inc. ("AT&T") – most recently by requiring the parties to address the issues of appropriate access charges for Verizon Northwest Inc. ("Verizon") and how to implement any rate change. Verizon has consistently ignored and resisted this Commission desire, and Verizon's Opening Brief ("Verizon Brief") is no exception. Verizon virtually concedes the need to change its excessive originating access charges but devotes the majority of its brief to arguing why the Commission cannot consider doing so. Indeed, Verizon does not even attempt to justify these charges except as an allegedly necessary source of intrastate revenues. Verizon's arguments do not come close to being convincing.

2. AT&T and Commission Staff ("Staff") have presented substantial and reliable testimony demonstrating the unrebutted need to reduce Verizon's access charges to cost-based levels. AT&T and Staff may not be in complete agreement on the precise amount of that reduction, but they agree that Verizon's current rates are unlawful, unfair, unjust, and unreasonable. Accordingly, AT&T urges the Commission to find in favor of AT&T on the allegations in AT&T's Complaint and to grant the relief that AT&T has requested.

II. DISCUSSION

A. WHAT SHOULD VERIZON'S ACCESS CHARGES BE, AND WHY?

3. Verizon's access charges, like its local interconnection rates, should be based on Verizon's forward-looking costs to provide the service. Verizon, however, advocates retaining its existing rates, based largely on a decision the Commission made almost 20 years ago in Docket No. U-85-23. Verizon apparently lives in the past, despite that fact that the company was formed only three years ago in the wake of the merger between BellAtlantic and GTE. Verizon

undoubtedly would like to turn the clock back to the days when competition in the intraLATA toll and local markets was nothing more than an heretical idea, and Verizon was earning in excess of its authorized rate of return. While Verizon's attitudes toward competition and its earnings have not changed, the rest of the world has.

4. The Commission and Washington intraLATA toll markets have moved far beyond the circumstances that existed in 1985. Rather than viewing access charges as a cash cow for incumbent local exchange carriers ("ILECs"), the Commission now realizes that consumers receive greater benefits when toll services are effectively competitive. The Commission also understands that such competition cannot develop when access charges vary dramatically from local interconnection rates. The Commission took its latest step toward access charge reform in the rulemaking that resulted in WAC 480-120-540. Verizon, not surprisingly, almost single-handedly prevented that rule from taking effect for almost six years, ostensibly arguing that access charges should be set in carrier-specific proceedings, rather than pursuant to a rule. Now in a complete about-face, Verizon claims that the Commission should rely solely on the rule, rather than this Verizon-specific proceeding, to conclude that Verizon's access charges are invulnerable from challenge. Verizon will make whatever arguments it believes will delay the advent of more effective competition, regardless of the inconsistency of its advocacy.

5. Neither AT&T nor Staff needs to file a petition to alter the Commission's decision in Docket No. U-85-23. The Commission effectively has done so itself long ago. Nor does the Commission need to alter WAC 480-120-540. That rule requires cost-based access charges, and none of the exceptions it provides apply to Verizon. AT&T is not attacking the Commission's access charge rules and policy but is attempting to use them to demonstrate to the Commission the need to take at least the next step toward access charge reform by eliminating

the $40 million problem that Verizon's access rates create in Washington intraLATA toll markets. The means exist to remedy that problem. AT&T urges the Commission to use those means.

1. Terminating Rates (including ITAC)

6. Verizon's terminating access rate should be equal to the forward-looking costs of providing that service, *i.e.*, the same as its local interconnection rate. Verizon points out that its current rates include those costs, as well as an interim universal service subsidy rate element ("ITAC") authorized under WAC 480-120-540, and Verizon thus claims that its terminating access charges are consistent with applicable law. As AT&T discusses below and in its Opening Brief,[1] the ITAC is inconsistent with federal law and should be eliminated.[2] If the Commission continues to authorize Verizon to charge that rate element, however, the Commission should adopt the ITAC that Staff has calculated.[3]

2. Originating Rates

7. Verizon's charges for originating access, like its terminating access rates, should be based on forward-looking costs. Rather than address the merits of AT&T's claims, Verizon devotes the section of its brief discussing this issue to procedural reasons why the Commission

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[1] Section C, *infra*; AT&T Opening Brief at 22-23.

[2] Verizon asserts that AT&T has waived this claim because an exhibit to Dr. Selwyn's testimony includes ITAC revenues when calculating the impact on Verizon's revenues if the Commission adopts AT&T's proposed access charges. Verizon's assertion is not even facially plausible. Dr. Selwyn, as a fact witness, cannot waive one of AT&T's legal claims. Verizon, moreover, never asked Dr. Selwyn about this exhibit or made any allegation, much less demonstration, in its testimony or during the hearings that the exhibit is inconsistent with Dr. Selwyn's frequently stated position that Verizon's access charges should be based on forward-looking costs. Verizon cannot raise such factual claims for the first time in its post-hearing brief. *See In re Continued Costing and Pricing of UNEs*, Docket No. UT-003013, Thirteenth Supp. Order (Part A Order), ¶ 387 (Jan. 2001) ("parties may not raise factual disputes for the first time in their post-hearing briefs").

[3] Exs. 100-107C (Staff Zawislak testimony and exhibits).

should not consider those claims. Indeed, Verizon virtually concedes that its originating access charges are excessive but contends that there is nothing the Commission can do about them without Verizon's consent. The Commission is not so limited and should reject Verizon's novel and self-serving position.

8. Verizon first resurrects its arguments that AT&T's Complaint represents single issue ratemaking and is not authorized by the complaint statute.[4] The Commission has already rejected these arguments in this case. Verizon cites no change in governing law or fact that would justify a different decision. The Commission, therefore, should once again reject Verizon's arguments.

9. Verizon then claims that AT&T's and Staff's proposals to reduce Verizon's access charges are impermissible collateral attacks on the Commission's access and imputation rules.[5] As discussed in more detail below,[6] AT&T is not attacking WAC 480-120-540 and WAC 480-80-204(6) but is seeking to enforce them, along with other provisions of applicable law. Verizon's creative interpretation of these rules and mischaracterizations of AT&T's claims do not provide any basis on which the Commission should refuse to consider AT&T's and Staff's proposals to reduce Verizon's excessive access charges.

10. Finally, Verizon maintains that the Commission cannot reduce Verizon's access charges without simultaneously increasing other rates on a revenue neutral basis.[7] Verizon cites no authority for this position, and AT&T is aware of none. Indeed, Verizon's own witness acknowledged that Verizon can be required to reduce its access charges if those charges violate

[4] Verizon Brief at 14.

[5] *Id*. at 15.

[6] Section E, *infra*.

[7] Verizon Brief at 15-16.

applicable law.[8] AT&T and Staff have produced more than sufficient evidence to demonstrate that Verizon's access charges are unlawful, unfair, unjust, and unreasonable. The Commission, therefore, has both the authority and the obligation to remedy Verizon's violation of applicable law by requiring Verizon to reduce its switched access rates. Verizon certainly may seek Commission permission to generate offsetting revenues from other sources, but those issues should be addressed in a separate proceeding initiated by Verizon, not in this docket.

B. IMPUTATION ISSUES

11. Verizon, both directly and indirectly through its affiliate Verizon Long Distance ("VLD"), prices its intraLATA toll services below a reasonable estimate of Verizon's price floor. Verizon disagrees, claiming that all of its toll services pass imputation based on a comparison between its retail rates and a price floor that Verizon contends is the only one that is calculated consistent with Commission requirements. Of course, the Commission would have to take Verizon's word for the accuracy and propriety of Verizon's calculations in light of the fact that Verizon failed to produce *any* evidence identifying, much less explaining or justifying, how Verizon calculated its price floor. The Commission, however, should review the record evidence, which demonstrates that Verizon's calculations are unrealistically low. The price floor developed by Dr. Selwyn is a conservative and reasonable estimate of Verizon's costs to provide intraLATA toll service and is considerably higher than Verizon's (and VLD's) retail toll rates.

1. Access Costs (including the Conversion Factor)

12. Dr. Selwyn calculated a reasonable estimate of Verizon's access costs as part of his direct testimony.[9] Verizon takes issue with Dr. Selwyn's calculations, claiming that (1) he failed to use Verizon's updated traffic distribution figures, and (2) his rebuttal testimony

[8] Tr. at 692-93 (Verizon Danner).

criticizes Verizon access charge calculations that comply with statements he made in his direct testimony. The record evidence provides no support for Verizon's claims, which should have been made long before Verizon filed its post-hearing brief.

13. Verizon provided only its proposed lump sum price floor in its testimony.[10] No Verizon witness ever identified the amount of that price floor that is comprised of access costs, much less explained how Verizon calculated those costs. Nor did Verizon's prefiled testimony address, much less take issue with, Dr. Selwyn's access cost calculations,[11] despite Dr. Selwyn's virtual invitation to do so.[12] Not until its post-hearing brief did Verizon dispute Dr. Selwyn's access charge calculations,[13] and not surprisingly, Verizon's brief cites no record evidence in support of its factual assertions on how Verizon calculated its access costs.[14] Verizon's criticisms not only lack evidentiary support, they come far too late to be considered by the

[9] Ex. T1 (AT&T Selwyn Direct) at 32-34 and Attachment 3.

[10] Ex. 231C (Verizon Imputation Analysis) at col. (k).

[11] *See, e.g.*, Ex. T3-R (AT&T Selwyn Rebuttal) at 18 ("Verizon offered no criticism of my calculations of the access costs attributable to Verizon in the provision of toll service, despite the fact that the Company's calculation of these costs is different.").

[12] *See* Ex. T1 (AT&T Selwyn Direct) at 34 n.48 (observing methodological changes in Verizon's calculations in an updated data request response provided shortly before the testimony was filed and noting, "It is likely that these new methodologies will be addressed in Verizon's responsive testimony, in which event I will consider their appropriateness and accuracy, and respond accordingly in my rebuttal testimony.").

[13] Verizon attempted to address Dr. Selwyn's access cost calculations in surrebuttal testimony, but the Commission struck that testimony for addressing issues that Verizon should have addressed in its responsive testimony. Verizon, however, never attempted to question Dr. Selwyn during the hearings on the alleged inconsistency between his direct and rebuttal testimony.

[14] *See* Verizon Brief at 21-22. Indeed, Verizon cites to *Staff* testimony to identify Verizon's access cost calculations. *Id*. at 22.

Commission.[15] The Commission, therefore, should adopt Dr. Selwyn's calculation of Verizon's access costs.

2. Billing and Collection Costs

14. Dr. Selwyn conservatively estimated that Verizon's billing and collection costs are $0.0155 per minute of use. Verizon's criticisms of that estimate are devoid of merit, as is Verizon's attempt to justify its own fatally flawed billing and collection cost study.

15. Verizon first contends that WAC 480-80-240(6) requires that Verizon's price floor be calculated using the long-run incremental cost ("LRIC") of billing and collection, and thus "Dr. Selwyn is attempting to re-write the Commission's price floor policy and imputation test as embodied in analysis conflicts with the Commission's imputation rule."[16] Verizon, however, conveniently ignores the plain language of the rule, which provides in relevant part:

> The rates, charges, and prices of services classified as competitive under RCW 80.36.330 must cover the cost of providing the service. Costs must be determined using a long-run incremental cost analysis, including as part of the incremental cost, the price charged by the offering company to other telecommunications companies for any essential function used to provide the service, ***or any other commission-approved cost method***.[17]

This express language permits the Commission to consider and adopt a cost methodology other than LRIC. A LRIC analysis, moreover, does not require the Commission to consider billing and collection for toll services as "incremental" to local service. As Dr. Selwyn explained, the reverse assumption – that local service billing and collection be considered "incremental" to toll

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[15] *See In re Continued Costing and Pricing of UNEs*, Docket No. UT-003013, Thirteenth Supp. Order (Part A Order), ¶ 387 (Jan. 2001) ("parties may not raise factual disputes for the first time in their post-hearing briefs").

[16] Verizon Brief at 24.

[17] WAC 480-80-240(6) (emphasis added).

billing – is more appropriate under the circumstances presented here.[18] Dr. Selwyn's approach thus is fully consistent with both the letter and the spirit of WAC 480-80-204(6).

16. Verizon also claims that Dr. Selwyn miscalculated the amounts that VLD pays Verizon for billing and collection. Verizon had every opportunity to make that point – and provide evidence to support it – in its testimony or even in its cross-examination of Dr. Selwyn. Verizon failed to do so, and it cannot attempt to do so for the first time in its post-hearing brief.[19] Even were that not the case, the record evidence supports Dr. Selwyn's calculations.[20]

17. The evidence also supports the applicability of those calculations to a proper estimate of Verizon's intraLATA toll price floor. Verizon observes that its charges to VLD for billing and collection must be the higher of either Verizon's booked costs or the fair market value of the service provided. Verizon indicated in a response to an AT&T data request that its

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[18] Tr. at 503 (AT&T Selwyn); Ex. T1 (AT&T Selwyn Direct) at 36. Verizon also unsuccessfully attempts to attack Dr. Selwyn's testimony by focusing on his use of the terms "regulated" and "unregulated." The context of his testimony makes clear, however, that Dr. Selwyn refers to noncompetitive local service as "regulated" and competitively classified services as "unregulated." Verizon fails to address, much less rebut, Dr. Selwyn's fundamental point that Verizon proposes to use facilities funded by captive ratepayers to cross-subsidize Verizon's competitively classified intraLATA toll services.

[19] *See In re Continued Costing and Pricing of UNEs*, Docket No. UT-003013, Thirteenth Supp. Order (Part A Order), ¶ 387 (Jan. 2001) ("parties may not raise factual disputes for the first time in their post-hearing briefs"). Similarly, Verizon contends that Dr. Selwyn's testimony is inconsistent with a selective quote from testimony provided by a different witness who testified on behalf of AT&T in the Qwest (then US WEST) rate case. Verizon Brief at 19-20. Verizon never attempted to introduce that testimony into the record in this proceeding, much less provide Dr. Selwyn an opportunity to address any alleged inconsistency. Such "attack by brief" is inappropriate and should be disregarded.

[20] Verizon's figure of "$1.10 per account (excluding discounts)" is not contained in Exhibit 217, as Verizon states, nor did Verizon present any billing and collection contracts to substantiate, much less quantify, any discounts Verizon provides to VLD. The record evidence, moreover, demonstrates that the average wireline long distance minutes of use per subscriber in 2003 is 73 minutes (Dr. Selwyn used 74), rendering irrelevant the 116 minute figure for 2000 that Verizon cites. *See* Ex. 265 (Credit Suisse First Boston Report) at 3. No record evidence supports Verizon's contentions that these figures are specific to residential service or that business toll service usage per subscriber is higher than residential usage.

billing and collection charges to VLD are set at the prevailing market rate.[21] That rate thus reflects the value of those services, which should be the compensation that Verizon pays to captive ratepayers for funding Verizon's toll billing and collection.[22] Even if Verizon's billing and collection charges to VLD were set at Verizon's booked costs, those charges would reflect the costs that Verizon actually incurs to provide billing and collection for toll services. Under either alternative, the price that VLD pays to Verizon for providing billing and collection provides a far more accurate estimate of Verizon's costs than Verizon's cost study.

18. Verizon attempts to support its billing and collection cost study by pointing out that this was the same study that Verizon filed in the cost docket and that Mr. Tucek testified that computer costs have decreased since the study was conducted in 1998. Neither of these observations resuscitates Verizon's deficient study. The Commission did not adopt or endorse Verizon's ICM in the cost docket, but "reluctantly" agreed to its use for determining UNE rates in that proceeding.[23] The Commission did not even consider billing and collection costs for retail services in the cost docket. The Commission, however, did find Verizon's cost studies to be seriously flawed and concluded that cost studies based on the opinion of subject matter experts are unreliable.[24] Verizon's billing and collection cost study is based almost entirely on the opinion of unidentified "key personnel."[25] And while computer costs undoubtedly have

[21] Ex. 218C (Verizon Response to AT&T DR No. 70), third page.

[22] *See* Tr. at 471-74 (AT&T Selwyn); Ex. 56 (AT&T Response to Verizon DR No. 45).

[23] *In re Continued Costing and Pricing of UNEs*, Docket No. UT-003013, 32nd Supp. Order (Part B Order), ¶ 344 (June 21, 2002).

[24] *Id*. 41st Supp. Order, ¶ 319 & 45th Supp. Order, ¶ 216.

[25] Ex. 228C (Billing and Collection excerpts from ICM); Tr. at 761-62 (Verizon Tucek).

declined in the last six years, other costs have just as undoubtedly increased.[26] Mr. Tucek, moreover, did not have any involvement in the preparation of Verizon's cost studies, and thus he has no basis on which to opine on what impact the passage of time has had on the level of Verizon's billing and collection costs.

19. Interestingly, Verizon ignores the Commission's prior determination that the costs of billing and collection – calculated on a LRIC basis – for Verizon and other independent ILECs is $0.0346 per minute.[27] If Verizon truly believes in its own advocacy that Commission determinations remain valid in perpetuity, Verizon should agree that its LRIC for billing and collection is the $0.0346 amount that the Commission previously established because that is the last amount that the Commission has adopted. AT&T has proposed a much more conservative billing and collection cost of $0.0155, which is the bare minimum amount that the Commission should use.

3. Retailing/Marketing Costs

20. Dr. Selwyn estimated the retailing and marketing costs that Verizon incurs in the provision of intraLATA toll services based on the publicly available sources. Verizon criticizes that estimate of $0.03 per minute of use as being based on nation-wide, rather than Verizon-specific, costs with insufficient supporting documentation.[28] Dr. Selwyn, however, relied primarily on a cost estimate provided by Dr. William Taylor in testimony he filed on behalf of

[26] For example, the Commission should take official notice of the fact that first class postage rates have increased over 15% since 1997 (from $0.32 to $0.37 for the first ounce).

[27] Ex. T1 (AT&T Selwyn Direct) at 37.

[28] Verizon also criticizes Dr. Selwyn's estimate as not being consistent with LRIC, which fails to undermine Dr. Selwyn's analysis for the same reasons discussed above (and in AT&T's Opening Brief) with respect to billing and collection costs.

Qwest Corporation in Minnesota.[29] As a frequent Verizon witness, Verizon should not dispute his credibility or the reliability of the sources of his cost estimates. The nature of publicly available cost data, moreover, is that it often is not company or state specific. Dr. Selwyn used the best data available, which is the only data to which he had access. Indeed, AT&T tried to obtain more specific data from Verizon through discovery, but even after the Commission ordered Verizon to respond to AT&T's requests, Verizon did not provide sufficient information to calculate Verizon's marketing costs in Washington.[30]

21. Verizon also criticizes Dr. Selwyn for not seeking retailing and marketing data from AT&T. As AT&T and the Commission have repeatedly reminded Verizon, however, this case is about Verizon's costs and prices, not AT&T's costs. Verizon nevertheless produced publicly available information about AT&T's costs allegedly to refute Dr. Selwyn's testimony.[31] Verizon ignores this evidence in its Brief, no doubt because that evidence indicates that the cost of customer acquisition (excluding customer care) costs is $0.0257 per toll minute of use, which supports Dr. Selwyn's reliance on Dr. Taylor's retailing and marketing cost estimate.[32]

22. Verizon, of course, advocates its own retailing and marketing cost study, claiming that it is "based on the costs associated with Verizon's actual and verifiable retailing/marketing

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[29] *Id*. at 37-38. As Verizon notes, Dr. Taylor used the same figure in an FCC filing on behalf of Verizon. Verizon Brief at 27. Verizon further observes that Dr. Taylor noted in his FCC affidavit that his figure was a national average, but Dr. Taylor nevertheless applied that same figure to retailing and marketing costs that Qwest would likely incur in Minnesota. Dr. Taylor thus apparently believes that this figure is equally applicable on a state-specific basis.

[30] *See, e.g.*, Ex. 218C (Verizon Response to AT&T DR No. 70) (providing aggregate sales and marketing data for Washington, Oregon, and Idaho combined, rather than the Washington-specific data requested).

[31] Ex. 262 (Verizon Danner Surrebuttal) at 26; Ex. 265 (Credit Suisse First Boston Report).

[32] Tr. at 679-83 (Verizon Danner); Ex. 265 (Credit Suisse First Boston Report) at 3 & 8; AT&T Opening Brief at 11.

activity in Washington for its intraLATA toll services."[33] Verizon produced no evidence by which the Commission or any of the parties could verify any such activity. Rather, as AT&T explained in its Opening Brief, Verizon's cost study is based on unidentified Verizon employees' manipulation of a 1997 mid-year budget, without any reliance on "actual" costs or retailing or marketing activities.[34] Particularly in the absence of any evidence of Verizon's retailing and marketing costs – either "actual" or LRIC – AT&T has produced the most reliable estimate of the retailing and marketing costs Verizon incurs to provide intraLATA toll services in Washington.

4. Other Costs

23. Verizon contends that no other costs should be included in its toll price floor, confirming that its imputation analysis does not include costs for intertandem transport. As AT&T discussed in its Opening Brief, Verizon incurs such costs, and they should be included in a proper imputation analysis.

5. Applicability to Verizon Affiliates

24. AT&T demonstrated that Verizon and VLD are effectively a single company for purposes of providing intraLATA toll service in Washington and thus should be treated the same for imputation purposes.[35] Verizon contends that if AT&T believes that VLD is in violation of the law, AT&T should have named VLD in its Complaint. Verizon misses the point. Verizon's inflated switched access charges enable Verizon and its affiliates to price intraLATA toll services below not only Verizon's price floor (even using Verizon's calculation) but below

[33] Verizon Brief at 29.

[34] AT&T Opening Brief at 11-12.

[35] AT&T Opening Brief at 15-17.

Verizon's own access cost calculations. Suing Charlie McCarthy cannot redress a grievance against Edgar Bergen.

25. Verizon further claims that "AT&T has offered *no* evidence of VLD's total costs of providing services to Washington consumers."[36] Verizon apparently is not too familiar with the record in this proceeding. Verizon's responses to AT&T's data requests and Verizon's own witness confirmed the price that VLD pays Verizon to resell intraLATA toll services, as well as the amount that VLD pays Verizon for billing and collection, joint marketing (excluding advertising), and other services.[37] AT&T agrees that these do not represent all of the costs that VLD incurs to provide intraLATA toll services in Washington, but in light of the undisputable fact that the amounts VLD is paying to Verizon are substantially higher than the intraLATA toll rates in the VLD price list, evidence of those additional costs would be superfluous.

26. Finally, Verizon attempts to defend its actions by claiming that federal law authorizes Verizon to jointly market services with its affiliates. Federal law, however, does not authorize Verizon to provide intraLATA toll services through an affiliate at rates that are below Verizon's own imputed costs. Verizon and VLD's joint development and marketing of package services simply provides additional evidence that Verizon and VLD are effectively the same company and should be treated as such for purposes of the Commission's imputation requirements.

6. Whether there is a price squeeze/remedies

27. Verizon, directly and indirectly through VLD, is pricing its intraLATA toll services below a properly calculated price floor and, in some cases, below even Verizon's

[36] Verizon Brief at 30 (emphasis in original).

calculation of its access costs. Verizon nevertheless maintains that there is no price squeeze because "AT&T has failed to list even one of its toll plans that is currently being 'squeezed' by Verizon."[38] Verizon's argument represents a fundamental misunderstanding of the intraLATA toll market in Washington and how Verizon's excessive access charges distort that market.

28. The Commission requires toll providers to provide service at state-wide averaged rates.[39] AT&T specifically must charge "geographically uniform rates," and AT&T is the only toll provider that is required to provide toll services "in all areas of the state."[40] Verizon is not required to provide intraLATA toll service outside of it local service territory and does not do so.[41] At least one reason why Verizon does not provide intraLATA toll service to customers to whom Verizon does not provide local service is that Verizon must impute its originating access charges into its toll rates, and the resulting rates are not competitive with Qwest's rates, which impute Qwest's much smaller originating access charges. Qwest, on the other hand, has minimized or withdrawn from providing toll service to customers located in the local service territories of Verizon and other independent ILECs because it would have to raise its toll rates

[37] Exs. 218C, 219C & 403C (Verizon Responses to AT&T DR Nos. 70, 71 & 16); Tr. at 832-38 (Verizon Fulp); *see* Ex. T1 (AT&T Selwyn Direct) at 35-37 (calculating VLD payments to Verizon for billing and collection on a per minute of use basis).

[38] Verizon Brief at 31. Verizon also argues that AT&T has somehow waived its price squeeze claims by representing to the Commission that it was not claiming to have suffered losses in providing toll service in Washington. As discussed further below, however, Verizon's arguments miss the mark. Whether AT&T's intraLATA toll services are profitable is an entirely separate (and irrelevant) issue from whether toll carriers in general are suffering a price squeeze.

[39] *See* RCW 80.36.183.

[40] *In re Petition of AT&T for Classification as a Competitive Telecommunications Company*, Cause No. U-86-113, Fourth Supp. Order Granting Petition With Conditions at 19 (June 5, 1987).

[41] Ex. 206 (Verizon Response to AT&T DR No. 19).

(or provide less profitable service) to pay those carriers' high originating access charges.[42] AT&T alone, therefore, must compete with both Qwest and Verizon, attempting to set uniform rates that recover Verizon's excessive access charges but are competitive with Qwest rates that are based on significantly lower access costs.[43]

29. Verizon's access charges thus create at least three different types of price squeeze. First, AT&T is squeezed between Qwest's toll rates and the excessive access costs imposed by Verizon. AT&T cannot fully compete with Qwest because AT&T must establish statewide averaged rates that enable AT&T to pay Verizon's originating access charges, costs which Qwest can avoid by not serving customers in Verizon's local service territory. Verizon increases the pressure on AT&T by pricing its toll services (particularly the services offered under VLD's price list) below Verizon's access costs. The second type of squeeze squeezes Qwest and other wireline toll providers who are not required to provide service statewide out of the market in Verizon local service territory. Qwest is a much more effective and profitable competitor when it provides toll service to its own local exchange customers because it pays only its own costs, not the artificial originating access charges imposed by Verizon. The third type of price squeeze squeezes Verizon out of the intraLATA toll market outside of its own local service area. Verizon's toll rates are not competitive outside of Verizon's local service territory because those rates must cover Verizon's imputed access costs, which are much higher than Qwest's access charges.

[42] Qwest, for example, has withdrawn as the primary toll carrier for most, if not all, independent ILECs.

[43] To the extent that MCI, Sprint, and other toll providers *choose* to serve customers in all geographic areas in Washington, they face the same dilemma.

30. Dr. Blackmon made this same point in his testimony.[44] While he did not refer to these circumstances as a price squeeze, the concept is the same. Verizon's excessive access charges are squeezing carriers out of intraLATA toll markets in Washington, and the only effective remedy is to reduce those charges. Indeed, while raising Verizon's toll rates (including the rates of services provided under VLD's price list) may theoretically reduce the price squeeze on AT&T and other statewide carriers, such an increase would not have any impact on the ability of Verizon to enter the interLATA toll market in Qwest local service territory or vice versa.[45] The Commission should resolve *all* of the market distortions and inequities caused by Verizon's access charges by requiring Verizon to charge only forward-looking cost-based rates.

C. DO VERIZON'S ACCESS CHARGES VIOLATE STATE OR FEDERAL LAW AS ALLEGED IN AT&T'S COMPLAINT?

31. Verizon's access charges violate both state and federal law, as AT&T explained in its Opening Brief.[46] Verizon does not provide the Commission with any analysis or substantive discussion of the state statutes that AT&T cited in its Complaint. Instead, Verizon parrots Commission decisions from 1997 concluding that access charges need not be set at

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[44] Ex. T130 (Staff Blackmon Direct) at 5-6.

[45] Verizon's further argument that it has lost intraLATA toll market share within its local service territory thus fails to address the impact of Verizon's excessive access charges on intraLATA toll markets as a whole. Verizon's market share figures are also inaccurate. Specifically, the market share that Verizon calculates for VLD is understated because Verizon apparently calculated it by comparing the number of VLD *customers* to the number of Verizon *lines*. *See* Ex. 205C (Verizon Response to AT&T DR No. 17). Customers are not equivalent to lines. To the contrary, the Commission adopted a 1.25 lines per household assumption in the first cost docket. *In re Pricing Proceeding*, Docket Nos. UT-960369, *et al*., Eighth Supp. Order at 40 (April 16, 1998) (the Commission adopted this figure for Qwest but made a comparable adjustment to Verizon's cost estimates). Multiplying 1.25 by the number of VLD customers to approximate the number of lines VLD serves would substantially raise Verizon/VLD's share of the intraLATA toll market in Verizon's local service territory.

[46] AT&T Opening Brief at 19-24.

forward-looking cost.[47] Six years have passed since the Commission issued those decisions, and in those six years, wireless intraLATA calling has overtaken "stagnant" wireline competition,[48] which has only become more Balkanized as the largest intraLATA toll providers, Qwest and Verizon, have merged with other companies and withdrawn to their own local service territories to provide intraLATA toll service. The time has long since come for the Commission to reevaluate its past determinations in light of current circumstances.

32. With respect to federal law, Verizon primarily responds to an argument that AT&T has not made. AT&T does not contend that federal law requires that Verizon's intrastate access charges be cost-based. Rather as discussed in its Opening Brief, AT&T's position is that Verizon's intrastate access charges violate federal law by including implicit universal service support subsidies.[49] Most of Verizon's federal law arguments thus are irrelevant.

33. In response to the federal law claims that AT&T *is* making, Verizon contends that the Congressional requirement that universal service support must be explicit does not apply to state commissions. The language of the Act is to the contrary. State commission regulations governing universal service support must be consistent with FCC rules.[50] If FCC rules cannot require or permit ILECs to recover universal service support through access charges, neither can state commission rules. Verizon quotes a *recommended* decision by the Federal-State Board on Universal Service, but that entity is not a decision-making body, much less empowered to establish binding interpretations of federal law.

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[47] Verizon Brief at 32-33. Verizon also cites the Commission's order approving the settlement agreement in the BellAtlantic/GTE merger proceeding, but the Commission did not even address how access charges should be priced in that order, much less determine that access charges need not be cost-based.

[48] Tr. at 554 (Staff Blackmon).

[49] AT&T Opening Brief at 22-23.

34. Verizon then argues that even if Congress meant what it said, state commissions can indefinitely delay removing implicit universal service support subsidies from access charges. The cases that Verizon cites do not support this proposition. The Fifth Circuit merely stated that FCC orders intended to be transitional in the shift from monopoly to competitive regulation were entitled to special deference.[51] No such "transitional" orders are at issue here. The Fifth Circuit, moreover, was evaluating FCC orders promulgated in 1997 and 1998, shortly after passage of the Act. The Commission has not promulgated any orders to remove the implicit universal service support subsidies from ILEC access charges, and Verizon has maintained the same level of access charges since 1999. Nothing in the Fifth Circuit's opinions supports providing special deference under these circumstances. Indeed, there is no Commission decision to which a court could defer. The Commission, therefore, has no basis on which it should further delay compliance with Congressional limitations on funding universal service support.

D. VERIZON EARNINGS ISSUES

35. Verizon's earnings are irrelevant, and Verizon's efforts to inject earnings issues into this proceeding do not change that fact. State statutes prohibiting rate discrimination and anticompetitive conduct, as well as federal law prohibiting implicit universal service support in access rates, include no provision that would rescind those prohibitions if the company needs the revenues from the unlawful rates to generate its authorized rate of return. As discussed above and in AT&T's Opening Brief, Verizon's access charges are unlawful, and Verizon is not entitled to maintain unlawful rates, regardless of the extent to which those rates contribute to Verizon's intrastate earnings.

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[50] 47 U.S.C. § 254(f).

[51] *Alenco Comm., Inc. v. FCC*, 201 F.3d 608, 616 (5th Cir. 2000).

36. Even if the Commission chose to consider data on Verizon's earnings, Dr. Selwyn and Ms. Erdahl more than adequately explained that even the high-level adjustments they proposed to the superficial earnings data that Verizon provided collectively demonstrate that Verizon is earning in excess of its authorized rate of return.[52] Verizon's hyperbolic claims that these adjustments are unreasonable or unlawful do not disguise the fact that Verizon does not believe its own figures, finding insufficient reason to seek rate increases or rebalancing in the face of Verizon's claims to be suffering annual shortfalls of $105 million and a threatened additional revenue reduction of $40 million.[53]

37. Verizon has been free to file a rate case since at least July 1, 2002. Verizon retains that option if Verizon truly believes that a reduction in its access charges to lawful and reasonable levels would preclude it from generating revenues sufficient to earn its authorized rate of return. A rate case, rather than this complaint proceeding, represents the appropriate forum for addressing Verizon's earnings issues.

E. WHAT IS THE IMPACT OF WAC 480-120-540 OR OTHER COMMISSION ORDERS?

38. Neither the access charge rule nor the imputation rule precludes AT&T's Complaint. To the contrary, both rules largely support granting the relief that AT&T has requested.

39. Verizon erroneously claims that "[n]o party disputes the fact that Verizon's current access charges comply with the Commission access charge rule."[54] AT&T disputes that Verizon's current access charges comply with WAC 480-120-540. The rule requires that

[52] Exs. T150-154C (Staff Erdahl Rebuttal and Exhibits); Exs. T3R & T4C-R (AT&T Selwyn Rebuttal) at 28-39; Exs.7C-10 (AT&T Selwyn Rebuttal Exhibits).

[53] *See, e.g.*, Tr. at 875-76 (Verizon Fulp).

[54] Verizon Brief at 51.

terminating access charges "not exceed the lowest rate charged by the local exchange company for the comparable local exchange service" or in the absence of any such rates, "the total service long-run incremental cost of terminating access service plus a reasonable contribution to common or overhead costs."[55] The rule also permits imposition of an ITAC "[i]f a local exchange company is authorized by the commission to recover any costs for support of universal service *through access charges*."[56] As discussed above, federal law prohibits Verizon from recovering universal service support through access charges. Accordingly, the rule does not authorize Verizon to violate federal law, and Verizon's terminating access charges thus are not in compliance with WAC 480-120-540.

40. A similar analysis applies to Verizon's originating access charges. The rule does not prescribe a rate design for originating access charges,[57] but addresses these charges in only two contexts. First, "nothing in this rule prohibits recovery of local loop costs through originating access charges,"[58] but nothing in the rule requires or even authorizes such recovery. Second, the rule permits Verizon to file tariffs transferring to its originating access charges the amounts in excess of forward-looking cost that Verizon previously included in terminating

[55] WAC 480-120-540(1) & (2).

[56] WAC 480-120-540(3) (emphasis added).

[57] Contrary to Verizon's interpretation, the Commission itself stated that in the access charge rule, "we prescribe only the rate design for terminating access and allow competition and customer choices (i.e., 'the Market') to determine the sustainability of originating access charges." Ex. 131 (General Order No. R-450, Docket No. UT-970325) at 18. The Commission further explained, "We remain open to dealing with individual company responses and proposals on a case-by-case basis given the underlying circumstances of each." *Id*. Again in contrast to Verizon's advocacy, the Commission did not forgo consideration of access charge rate issues on an individual case basis but adopted the rule to provide general guidance when examining individual company-specific issues.

[58] WAC 480-120-540(2).

access charges.[59] Any such transfer, however, must be "in the public interest."[60] Increasing already bloated originating access charges that are discriminatory and anticompetitive in violation of state law is not in the public interest. Indeed, originating access charges in excess of forward-looking cost violate state and federal law, as discussed above, and thus are not in compliance with the Commission rule.

41. AT&T is not attacking the Commission's access charge rule, as Verizon contends, because no attack is necessary. The rule requires that terminating access charges be equivalent to a LEC's lowest local interconnection rate, which is precisely the level for Verizon's access charges that AT&T has advocated that the Commission adopt in this proceeding. The possible adjustments to originating and terminating access authorized in the rule are inapplicable, and nothing in the rule precludes the Commission from setting originating access charges at the same forward-looking cost-based level as terminating access charges. AT&T, therefore, requests that the Commission enforce its access rule, as well as other applicable statutes and rules.

42. One of those other rules is WAC 480-80-204(6), to which Verizon refers as the Commission's imputation rule. Verizon argues that AT&T is collaterally attacking that rule by requesting that the Commission lower Verizon's access rates rather than increase Verizon's toll prices. Verizon's argument can charitably be characterized as nonsense. The rule requires only that the rates of competitively classified services must cover the cost of providing the service. The rule does not specify a remedy for its violation, much less preclude AT&T from requesting (or the Commission from granting) relief in the form of lower costs, rather than higher prices. Again, far from challenging the rule, AT&T seeks its enforcement, along with enforcement of other applicable provisions of Washington law.

[59] WAC 480-120-540(6).

43. Verizon's final contention on this issue is that "the access charge rule and the imputation rule reflect the Commission's long-standing policy of requiring regulated carriers to recover significant portions of their costs through access charges."[61] The Commission has no such policy, nor can these rules reasonably be construed to embody such a policy. The "imputation" rule does not even mention access charges, while the access charge rule requires *reductions* to access charges. Indeed, this rule and other Commission decisions issued after Verizon's last rate case over 20 years ago – including the orders in Qwest's most recent rate case[62] and the BellAtlantic/GTE merger – have established a Commission policy to bring access charges closer to cost and to require ILECs to recover more of their costs from their retail customers, rather than from their competitors. The Commission should further promote this policy by granting the relief that AT&T has requested.

F. HOW SHOULD AN ACCESS CHARGE REDUCTION BE IMPLEMENTED, IF THE COMMISSION DECIDES THAT SUCH A REDUCTION IS APPROPRIATE?

44. The Commission should immediately require Verizon to reduce its originating and terminating access charges to forward-looking cost-based levels. Verizon continues to advocate a revenue neutral solution in which reductions in access charges would be offset by increases in other rates. Verizon has had almost one year to initiate an appropriate proceeding to do just that and has refused to do so. Nor does Verizon have any plans to initiate such a proceeding in the future. Verizon's actions speak louder than its words. Verizon is interested only in maintaining the status quo and delaying any relief to those suffering from Verizon's excessive access charges.

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[60] *Id*.

[61] Verizon Brief at 57.

[62] Docket No. UT-950200, Fifteenth Supp. Order.

45. None of the three options that Verizon proposes, moreover, are viable, much less effective in providing appropriate relief. Verizon first suggests that the Commission order the parties to reach a settlement. Commission abdication of its responsibility to resolve the disputed issues is not an option that the Commission should consider, even if that option were available under applicable law. The parties, moreover, have already unsuccessfully tried to settle these issues and further efforts would be fruitless, as Verizon well knows. Verizon, of course, has no suggestion for a procedure when settlement negotiations inevitably fail, reinforcing Verizon's actual goal of further delaying resolution of the issues.

46. Verizon's second proposal is that the Commission re-open U-85-23 or the access charge rulemaking to "establish a procedure for revenue-neutral rate rebalancing."[63] Verizon never explains what type of "procedure" it has in mind or how any such "procedure" would address Verizon's contention that this or any other option "requires the Commission to consider Verizon's overall earnings."[64] It also cannot have escaped Verizon's notice that the Commission's access charge rulemaking began in 1997 and the resulting rule became effective in March of this year – over 5 years later – after Verizon had finally exhausted its appeals. While Verizon may be happy to delay resolution of the issues in this case until 2009, intraLATA toll markets should not be held hostage to Verizon's unlawful and unreasonable access charges for another six days, much less six years.

47. Third, Verizon proposes that the Commission open a separate phase of this docket to address the issue of rate increases to offset access charge reductions. As Public Counsel and retail ratepayer intervenors have pointed out, however, any consideration of an increase to local rates outside the context of a general rate case raises serious procedural, as well as substantive,

[63] Verizon Brief at 58.

concerns. Even if such issues could be addressed in this docket, the type of review required (and participation in that review by all potentially affected parties) would be indistinguishable from a general rate case. Verizon is not entitled to hijack this proceeding and indefinitely postpone the remedy for Verizon's unlawful access rates so that a different set of parties can consider retail rate issues that AT&T never raised and that are unrelated to any claim in AT&T's Complaint.

48. IntraLATA toll providers (other than Verizon and its affiliates) and their customers are entitled to a remedy now, not years from now. Reducing Verizon's access charges immediately will not *require* Verizon to take any other action whatsoever. The availability of a separate Verizon filing to raise or rebalance its rates in the wake of an ordered reduction in access charges "is not a mandate, but an opportunity to exercise choice."[65] Verizon's own witness testified that Verizon considers a rate case filing under those circumstances only to be a "possibility."[66] Verizon can initiate any proceeding it believes is appropriate to seek to raise additional revenues, including a general rate case or a retail access charge as Staff originally proposed.[67] What Verizon should not be permitted to do is to further delay appropriate relief for Verizon's unlawful and unreasonable access rates.

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[64] *Id*. at 59.

[65] Ex. 131 (General Order No. R-450, Docket No. 970325) at 13.

[66] Tr. at 829 (Verizon Fulp).

[67] AT&T in its Opening Brief supported Staff's original proposal for a retail access charge, AT&T Opening Brief at 28, but did not clearly state that in light of the Commission's Fifth Supplemental Order striking testimony on Staff's proposal, the Commission should entertain that proposal in a separate proceeding after granting the appropriate relief in this docket. AT&T continues to believe that Staff's proposal has merit and would provide Verizon with the opportunity to raise additional revenue, including interim universal service support, without raising local service rates. While not an issue to be addressed substantively in this proceeding, the Commission order resolving AT&T's Complaint could authorize Verizon, after the carrier access charge reduction is effective, to make a separate tariff filing that creates a retail access charge, subject to appropriate additional proceedings in the separate docket initiated by that tariff filing.

III. CONCLUSION

49. AT&T has carried its burden to prove that Verizon's switched access rates are unlawful, unfair, unjust, and unreasonable as AT&T alleged in its Complaint. Accordingly, the Commission should grant the relief that AT&T requested and should require Verizon immediately to reduce its switched access rates to forward-looking cost based levels.

RESPECTFULLY SUBMITTED this 17th day of June, 2003.

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