

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the)
) Docket No. UT-003013
Continued Costing and Pricing of)
Unbundled Network Elements, Transport,)
Termination, and Resale)
_____)

PART A DIRECT TESTIMONY

OF

REX KNOWLES

On Behalf of

NEXTLINK Washington, Inc.

May 19, 2000

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

2 A. My name is Rex Knowles. I am a Vice President Regulatory for NEXTLINK, 111 East
3 Broadway, Suite 1000, Salt Lake City, Utah 84111.

4 **I. BACKGROUND**

5 **Q. PLEASE IDENTIFY AND DESCRIBE THE PARTY ON WHOSE BEHALF YOU**
6 **ARE TESTIFYING.**

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8 A. I am testifying on behalf of NEXTLINK Washington, Inc. ("NEXTLINK"), a competitive
9 local exchange company ("CLEC") that provides facilities-based local and long distance
10 telecommunications services in Washington in competition with U S WEST
11 Communications, Inc. ("U S WEST") and GTE Northwest Incorporated ("GTE").

12 **Q. WHAT ARE YOUR RESPONSIBILITIES?**

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14 A. I am responsible for all regulatory, legislative, municipal, and incumbent local exchange
15 carrier ("ILEC") initiatives on behalf of NEXTLINK and other affiliates in several
16 western states, including Washington and other states in the U S WEST region.

17 **Q. WHAT IS YOUR BUSINESS AND EDUCATION BACKGROUND?**

18 A. I graduated from Portland State University in Portland, Oregon, with a degree in Business
19 Administration/Finance Law in 1989. I was employed by United Telephone of the
20 Northwest from 1989 to 1993 as a regulatory staff assistant and product manager
21 responsible for incremental cost studies and creation and implementation of extended

1 area service ("EAS") and 911. From 1993 to 1996, I was employed by Central Telephone
2 of Nevada as manager of revenue planning and research and was responsible for
3 supervising cost study preparation and developing and implementing regulatory reform,
4 including opening the local exchange market to competition and alternative forms of
5 regulation for ILECs. I joined the NEXTLINK organization in the Spring of 1996.

6 **Q. HAVE YOU PREVIOUSLY TESTIFIED IN OTHER REGULATORY**
7 **PROCEEDINGS BEFORE THE COMMISSION?**

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9 A. Yes, I have provided testimony on costing, pricing, and policy issues in the Commission's
10 generic costing and pricing proceeding, Docket Nos. UT-960369, *et al.*, in the universal
11 service case, Docket No. UT-980311(a), and in the U S WEST-Qwest merger review,
12 Docket No. UT-991358.

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

14 A. The purpose of my testimony is to discuss the general principles applicable to cost
15 recovery for competing local exchange company ("CLEC") access to incumbent local
16 exchange company ("ILEC") operations support systems ("OSS"). I also discuss
17 NEXTLINK's approach to developing costs for collocation, nonrecurring charges, and
18 line sharing.

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20 **II. OPERATIONS SUPPORT SYSTEMS**

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Q. WHAT ARE THE GENERAL PRINCIPLES APPLICABLE TO COST RECOVERY FOR CLEC ACCESS TO ILEC OSS?

A. There are four general principles applicable to cost recovery for CLEC access to ILEC OSS:

1. Cost recovery for OSS as an unbundled network element is limited to total element long-run incremental cost (“TELRIC”) plus a reasonable share of forward-looking common costs;
2. To the extent that ILECs incur non-TELRIC costs to make OSS access available, the ILECs should recover those costs from all customers, not from CLECs alone;
3. CLECs also incur costs to comply with federal legal requirements, and CLECs should be entitled to recover their costs from the ILECs to the same extent that the ILECs are authorized to recover those costs from the CLECs; and
4. Any authorized OSS cost recovery should ensure that each entity contributing to that cost recovery is responsible only for the costs attributable to that entity’s use of other carrier’s OSS.

Q. PLEASE EXPLAIN THE FIRST PRINCIPLE YOU IDENTIFIED.

A. The most fundamental general principle applicable to OSS cost recovery is that as an unbundled network element, OSS access pricing must be based on TELRIC. The FCC has defined “TELRIC” in paragraphs 674-92 of its August 8, 1996 *Local Competition*

1 *Order* as a forward-looking methodology for estimating costs, as opposed to an
2 embedded approach that determines “costs that firms incurred in the past for providing a
3 good or service and are recorded as past operating expenses and depreciation” (paragraph
4 675). More specifically, the FCC stated in paragraphs 683 and 685, “Forward-looking
5 cost methodologies, like TELRIC, are intended to consider the costs that a carrier would
6 incur in the future,” and TELRIC is “based on the least-cost, most efficient network
7 configuration and technology currently available.”

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9 TELRIC, however, by definition does not include costs that an ILEC incurs to modify its
10 existing network to achieve the least cost, most efficient network configuration and
11 technology currently available. TELRIC already assumes a multi-provider environment.
12 As the FCC explained in paragraph 679 of the *Local Competition Order*, “Adopting a
13 pricing methodology based on forward-looking, economic costs best replicates, to the
14 extent possible, the conditions of a competitive market.” The ILECs cannot logically
15 claim that costs they have incurred in the past to *transition* from a monopoly to a multi-
16 provider environment are forward-looking costs that simulate the conditions in a market
17 that is *already* competitive. Accordingly, one-time costs incurred to modify or develop
18 access to ILEC OSS to accommodate competition should not be included in any TELRIC-

1 based rates CLECs pay for access to OSS and an unbundled network element.

2 **Q. ARE ILECS ENTITLED TO RECOVER THE NON-TELRIC BASED THEY**
3 **INCUR TO MODIFY OR DEVELOP ACCESS TO THEIR OSS TO**
4 **ACCOMMODATE COMPETITION?**

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6 A Yes, but only to the same extent that they are authorized to recover other prudently
7 incurred embedded costs – as part of the rate base on which the Commission establishes
8 retail prices. Thus the second principle of OSS cost recovery is that ILECs are not
9 entitled to recover non-TELRIC costs from CLECs alone.

10 **Q. DON'T CLECS CAUSE THE ILECS TO INCUR THESE COSTS AND**
11 **ULTIMATELY BENEFIT FROM OBTAINING ACCESS TO ILEC OSS?**

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13 A. No, at least not in the sense that CLECs can be considered the “cost causers” for
14 ratemaking purposes. Congress and the FCC have determined as a matter of public
15 policy that formerly monopoly local exchange markets should be opened to competition,
16 and the only way effective competition can develop is if the ILECs provide
17 nondiscriminatory access to, and interconnection with, their networks to competitors.
18 This represents a transition from exclusively using government agencies to regulate
19 telecommunications services to relying more on market constraints to discipline pricing
20 and service quality. The objective, however, remains the same – to ensure that such
21 services are generally available at reasonable rates, terms, and conditions. The public
22 interest – more specifically all telecommunications ratepayers – “caused” the costs

1 associated with making this transition. Accordingly, ratepayers as a whole benefits from
2 the resulting development of competition, and ratepayers as a whole should be
3 responsible for the attendant costs.

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5 Analogous circumstances are presented by federal and state requirements that building
6 owners make their buildings accessible to physically disabled persons. Such
7 requirements represent a public policy determination that disabled persons are entitled to
8 obtain access to, and use of, buildings on a basis that is equivalent to the access and use
9 enjoyed by the general public. These requirements, however, require building owners to
10 modify existing buildings, including installing ramps, elevators, and special restroom
11 facilities. Persons with disabilities use these facilities, but they are not the “cost causers”
12 of the building modifications they use. The general public is the “cost causer” because
13 the public’s elected representatives determined that society is better if all persons,
14 regardless of their physical abilities, can have equivalent access to the same places. That
15 goal would be substantially undermined if building owners were authorized to impose a
16 charge applicable only to the disabled in order to recover the costs of the necessary
17 building modifications.

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1 Similarly here, Congress intends that *all* customers – both CLEC and ILEC customers –
2 benefit from the development of effective local exchange competition. Only if CLECs
3 can timely and efficiently obtain facilities and services from the ILECs can customers
4 have an effective choice among service providers. Effective choice, in turn, imposes
5 market discipline to improve the quality and price of service both to obtain and retain
6 customers. Existing ILEC customers, therefore, benefit from the advent of effective local
7 exchange competition either by choosing an alternate carrier that can provide better
8 service at a better price than the ILEC, or by remaining with their current provider
9 because the ILEC has improved its service to win, not simply expect, customer loyalty.
10 Accordingly, all customers, not just CLECs, should pay the costs of the ILECs' transition
11 from a monopoly to a multi-provider environment.

12 **Q. ARE ILECS THE ONLY ONES TO INCUR COSTS IN COMPLIANCE WITH**
13 **FEDERAL AND FCC REQUIREMENTS?**

14 A. Certainly not. The third principle of OSS cost recovery is that CLECs also incur costs to
15 comply with federal legal requirements. The Act requires *all* local exchange companies –
16 including CLECs – to interconnect their networks and exchange local traffic. CLECs,
17 therefore, must order, construct, or otherwise establish interconnection trunks, as well as
18 monitor and measure the traffic exchanged with other carriers. To the extent that the
19 ILECs seek to recover costs to enable them to perform these functions, the CLECs should
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1 be entitled to recover those same costs.

2
3 The FCC has also authorized the ILECs to require an interface that CLECs must use to
4 access the ILECs' OSS, rather than allowing CLECs to have the same direct access to
5 those systems that the ILECs have. The CLECs, however, must incur costs to use those
6 interfaces that the CLECs would not incur if they were permitted direct access.

7 Specifically, CLECs seeking to use an electronic data interface ("EDI") must construct
8 their own gateway to obtain electronic access to the ILECs OSS. Again, these costs are
9 incurred pursuant to a legal requirement, and if the ILECs are entitled to recover their
10 costs to construct a gateway and otherwise modify CLECs' access to the OSS, CLECs
11 should be entitled to recover those same costs.

12 **Q. HOW DO YOU PROPOSE THAT CLECS RECOVER THOSE COSTS?**

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14 A. First, let me repeat that NEXTLINK strongly believes that no carrier should recover such
15 costs solely from other carriers and that each carrier should recover the costs it incurs to
16 comply with legal requirements to open markets to competition from all of its customers
17 as a cost of doing business. Only if the Commission authorizes the ILECs to impose a
18 separate charge on CLECs to recover non-TELRIC expenditures should NEXTLINK and
19 other CLECs similarly be authorized to recover such costs.

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2 If carriers are authorized to recover these costs from each other, the FCC has provided
3 some guidance in estimating the costs CLECs should be entitled to recover. The FCC, in
4 its *Local Competition Order* and attendant rules, determined with respect to costs to be
5 recovered through reciprocal compensation for exchange of traffic that a CLEC's costs
6 are presumed to be the same as the ILEC's costs unless the CLEC can demonstrate that its
7 costs are higher. These were the only circumstances in which the FCC addressed CLEC
8 cost recovery, but the same principle should apply to all instances in which ILECs and
9 CLECs are entitled to recover from each other costs incurred for the same service or
10 network functionality they provide pursuant to federal mandates. Thus, to the extent that
11 ILECs are entitled to recover their OSS development costs from CLECs alone, CLECs
12 should be entitled to recover the same costs from the ILECs.

13 **Q. SHOULD ALL CLECS RECOVER THE SAME COSTS FROM THE ILECS?**

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15 A. Not necessarily, which leads to the fourth and final OSS cost recovery principle I have
16 identified. Any non-TELRIC OSS cost recovery structure involving intercarrier charges
17 should ensure that carriers pay only for their proportionate use of the others' OSS. A
18 CLEC that does not resell ILEC retail services, for example, should not be responsible for
19 any costs associated with OSS used to order or provision resold services. Similarly, a

1 CLEC that does not exchange local traffic with an ILEC (such as carriers that offer only
2 resold or data services) should neither pay, nor receive payment, for OSS costs associated
3 with interconnection and local traffic exchange. Whatever rate structure the Commission
4 develops – if it insists on authorizing intercarrier payments for non-TELRIC OSS cost
5 recovery – should be consistent with this principle.

6 **Q. WHAT ABOUT TELRIC-BASED PRICES FOR OSS ACCESS?**

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8 A. TELRIC-based prices should adhere to this same principle. A CLEC obtaining an
9 unbundled loop, for example, is not required to pay for switching as well. Similarly, a
10 CLEC using the ILEC OSS to order an unbundled loop should not have to pay for costs
11 associated with OSS used to order and provision resold services. The Commission has
12 implicitly recognized this principle by requiring different rates for electronic and manual
13 order processing. The FCC similarly has defined TELRIC, in part, by contrasting it with
14 total *service* long-run incremental cost (“TSLRIC”). The FCC explained in paragraph
15 678 of the *Local Competition Order* that “separate telecommunications services are
16 typically provided over shared network facilities, the costs of which may be joint or
17 common with respect to some services,” but network elements “largely correspond to
18 distinct network facilities” and thus “the amount of joint and common costs that must be
19 allocated among separate offerings is likely to be much smaller using a TELRIC

1 methodology rather than a TSLRIC approach that measures the costs of conventional
2 services.” The TELRIC-based rates for OSS access the Commission establishes in this
3 docket, therefore, should be specific to the OSS functionality used (and corresponding
4 costs generated) by the CLEC.
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6 III. OTHER PART A ISSUES

7 **Q. HAS NEXTLINK DEVELOPED A PROPOSAL FOR COLLOCATION COSTING**
8 **AND PRICING?**
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10 A. No. Following the Commission’s decision on collocation in the earlier costing and
11 pricing proceeding, NEXTLINK reviewed the evidence submitted by the various parties
12 in that proceeding, as well as the testimony and cost study U S WEST subsequently filed
13 with revised cost and price estimates for collocation. Other NEXTLINK representatives
14 and I have also been participating in collocation workshops sponsored by the Division of
15 Public Utilities in Utah to examine collocation cost development. The conclusion we
16 reached was that the assumptions underlying the cost calculations have the greatest
17 impact on collocation cost estimates. Rather than devote substantial resources to
18 developing and defending a different collocation cost model, therefore, NEXTLINK
19 decided to use the models proposed by U S WEST and GTE. Accordingly, NEXTLINK
20 will examine the inputs and assumptions included in the cost studies and supporting

1 direct testimony that U S WEST and GTE file and will provide responsive testimony
2 detailing our analysis and proposing revisions.

3 **Q. WHAT ABOUT NONRECURRING CHARGES AND LINE SHARING?**

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5 A. Again, NEXTLINK is willing to work with whatever model U S WEST and GTE use to
6 estimate nonrecurring charges in light of NEXTLINK's experience that the inputs and
7 assumptions, rather than the model, account for the greatest discrepancy in cost estimates.
8 NEXTLINK will also respond, as necessary, to the line sharing proposals sponsored by U
9 S WEST, GTE, and any other party.

10 **Q. DOES THAT CONCLUDE YOUR TESTIMONY?**

11 A. Yes, it does.