

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,

Complainant,

v.

VERIZON NORTHWEST INC.,

Respondent.

DOCKET NO. UT-040788

RATE DESIGN TESTIMONY

OF

REX KNOWLES

On Behalf of

XO Washington, Inc.

December 15, 2004

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

2 A. My name is Rex Knowles. I am a Regional Vice President of Regulatory and External
3 Affairs for XO Communications, 111 East Broadway, Suite 1000, Salt Lake City, Utah
4 84111.

5 **BACKGROUND**

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

8
9 A. I am testifying on behalf of XO Washington, Inc. ("XO"), a competitive local exchange
10 company ("CLEC") that provides facilities-based local and long distance
11 telecommunications services in Washington in competition with Verizon Northwest Inc.
12 ("Verizon").

13 Q. WHAT ARE YOUR RESPONSIBILITIES?
14

15 A. I am responsible for all regulatory, legislative, municipal, and incumbent local exchange
16 carrier ("ILEC") initiatives on behalf of XO and other affiliates in several western states,
17 including Washington.

18 Q. WHAT IS YOUR BUSINESS AND EDUCATION BACKGROUND?

19 A. I graduated from Portland State University in Portland, Oregon, with a degree in Business
20 Administration/Finance Law in 1989. I was employed by United Telephone of the
21 Northwest from 1989 to 1993 as a regulatory staff assistant and product manager
22 responsible for incremental cost studies and creation and implementation of extended
23 area service ("EAS") and 911. From 1993 to 1996, I was employed by Central Telephone
24 of Nevada as manager of revenue planning and research and was responsible for

1 supervising cost study preparation and developing and implementing regulatory reform,
2 including opening the local exchange market to competition and alternative forms of
3 regulation for ILECs. I joined the XO organization in the Spring of 1996.

4 **Q. HAVE YOU PREVIOUSLY TESTIFIED IN OTHER REGULATORY**
5 **PROCEEDINGS BEFORE THE COMMISSION?**

6
7 A. Yes, I have provided testimony in several Commission proceedings, including the
8 Commission's generic costing and pricing and universal service proceedings.

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

10 A. The purpose of my testimony is to propose rates for Verizon intrastate services of
11 particular interest to XO and other facilities-based CLECs. Specifically, XO proposes
12 that the Commission adopt rates for Verizon DS1 and DS3 wholesale special access
13 services that are the same as, or comparable to, the rates that the Commission has
14 established or will establish for Verizon's DS1 and DS3 unbundled loops and transport.
15 As I discuss below, adopting these rates would likely increase Verizon's intrastate
16 revenues and will help to assure the availability of the wholesale high capacity services
17 that facilities-based CLECs need to be able to provide effectively competitive alternatives
18 to Verizon's local exchange services in Washington.

19 **RATE DESIGN PROPOSAL**

20 **Q. FOR WHICH VERIZON SERVICES DOES XO PROPOSE THAT THE**
21 **COMMISSION ADOPT SPECIFIC RATES?**

22
23 A. XO proposes rates for the intrastate special access services that Verizon provides to
24 wholesale customers at a DS1 or DS3 level. These services include DS1 and DS3 Special

1 Access Lines and Special Transport. Verizon has proposed rates only for its DS1 special
2 access services, explaining in response to a data request that it has not proposed rate
3 increases for DS3 services “due to the small number of current units for DS3 and, thus,
4 the revenue generating potential associated with a price increase.” Verizon Response to
5 TWTC/XO Data Request No. 1-001. A copy of Verizon’s responses to this set of data
6 requests is attached as Exhibit ____ (RK-2).

7 **Q. DOES VERIZON CURRENTLY HAVE SEPARATE SPECIAL ACCESS RATES**
8 **FOR WHOLESALE CUSTOMERS?**

9
10 A. No, it does not. Verizon has a single rate for all customers, and therein lies one of the
11 two principal problems with Verizon’s existing special access pricing. Verizon charges
12 competitors the same prices for intrastate special access services that Verizon charges to
13 its end user customers. A CLEC obviously cannot effectively serve customers using
14 Verizon intrastate special access circuits under these circumstances because the CLEC’s
15 costs to obtain the circuits to provide a competing service (without considering a CLEC’s
16 other costs) are the same or comparable to Verizon’s retail rate, even after considering
17 any applicable discounts.

18 **Q. WHAT IS THE OTHER PRINCIPAL PROBLEM WITH VERIZON’S CURRENT**
19 **SPECIAL ACCESS PRICING?**

20
21 A The other problem is that Verizon’s special access pricing vastly exceeds the costs that
22 the Commission previously has determined that Verizon incurs to provide high capacity
23 circuits. Verizon’s current cost-based DS1 unbundled loop rate in the highest density
24 zone is \$73.92, less than half of Verizon’s current intrastate special access line rate of

1 \$150.00 (which Verizon proposes to increase to \$187.50). Verizon's current DS3 special
2 access recurring monthly rate of \$2,450.00 for a one-year term commitment is almost
3 *three* times higher than Verizon's cost-based unbundled DS3 loop rate of \$791.97. Not
4 surprisingly, Verizon sells only a small fraction of its high capacity intrastate special
5 access services to wholesale service providers. See Exhibit ___ (RK-3C) (Confidential
6 attachment to Verizon Response to TWTC/XO Data Request No. 1-006).

7 **Q. THEN WHY DON'T CLECS SIMPLY ORDER UNBUNDLED NETWORK**
8 **ELEMENTS?**

9
10 A. There are several reasons, all of which boil down to the fact that Verizon and other ILECs
11 simply do not want to provide high capacity unbundled network elements ("UNEs").
12 ILECs have consistently refused to undertake the routine network modifications needed
13 to provision many high capacity circuits when those circuits are ordered as UNEs. As a
14 result, CLEC UNE orders have often been denied because of an alleged lack of facilities,
15 requiring that the CLEC either deny their own customers' service requests or order the
16 same facility out of the ILEC's special access tariff. ILECs have also refused to permit
17 "commingling," the combination of special access services and UNEs. Thus if a CLEC
18 already has interoffice transport that it has purchased as a special access service and
19 wants to connect a loop to that transport, the CLEC's only alternative is to purchase the
20 loop out of the special access tariff. CLECs must be responsive to customer needs if they
21 want to survive in the current market dominated by the ILECs, and purchasing special
22 access circuits is generally much easier, faster, and more reliable (even though much
23 more expensive) than trying to obtain the same circuits as UNEs.

1 **Q. DIDN'T THE FCC'S TRIENNIAL REVIEW ORDER ("TRO") REQUIRE**
2 **VERIZON AND OTHER ILECS TO UNDERTAKE ROUTINE NETWORK**
3 **MODIFICATIONS AND PERMIT COMMINGLING?**
4

5 A. Yes, but Verizon has yet to implement those requirements for CLECs other than the
6 carriers willing to accept Verizon's unilateral terms and conditions. Verizon has
7 specifically notified CLECs, for example, that Verizon will make routine network
8 modifications available only if the CLECs have executed a TRO Amendment to their
9 interconnection agreements ("ICAs"). Verizon, however, filed an arbitration petition
10 against every CLEC with which Verizon has an interconnection agreement in Washington
11 to arbitrate an appropriate TRO Amendment. That petition is currently pending before
12 the Commission in Docket No. UT-043013, with a final resolution not expected until the
13 second quarter of 2005. Routine network modifications and commingling, moreover, are
14 among the issues that Verizon proposes be handled *later* in a second phase of the
15 proceeding, which could delay a final resolution of those issues indefinitely.

16
17 Verizon's refusal to implement, and attempts to delay resolution of, routine network
18 modification and commingling issues stands in sharp contrast to Verizon's position on
19 implementation of other aspects of the TRO and subsequent federal law that *benefit*
20 Verizon. With respect to those issues, Verizon has taken the position that its current
21 ICAs automatically incorporate changes in the law and thus authorize Verizon
22 immediately to discontinue providing certain UNEs. The Administrative Law Judge in
23 Docket No. UT-043013 apparently agreed that language in Verizon's ICAs should be

1 interpreted to “allow Verizon to take unilateral action under the agreements upon certain
2 changes in law, and the parties may subsequently amend the agreements to address the
3 changes in law.” Order No. 12, paragraph 71. Yet, Verizon refuses to implement TRO
4 requirements that benefit CLECs without *first* executing a written amendment to the
5 ICAs. If Verizon had acted consistent with its own interpretation of its ICAs, Verizon
6 would have made routine network modifications and commingling available over one
7 year ago. Because Verizon selectively applies the “automatically supercede” language
8 only to changes in law that benefit Verizon, Verizon cannot be expected to comply with
9 the FCC’s routine network modification and commingling requirements for the
10 foreseeable future.

11 **Q. IS VERIZON’S REFUSAL TO IMPLEMENT FCC REQUIREMENTS ON**
12 **ROUTINE NETWORK MODIFICATIONS AND COMMINGLING THE ONLY**
13 **LIMITATION ON THE AVAILABILITY OF HIGH CAPACITY UNES?**
14

15 **A.** In all likelihood, no. Verizon has been the most aggressive ILEC challenging the FCC’s
16 unbundling rules, and Verizon can be expected to appeal virtually any obligation to
17 unbundle high capacity circuits that the FCC adopts as part of its latest rulemaking
18 proceeding. The FCC, moreover, has steadily reduced the ILECs’ unbundling obligations
19 with each successive remand of these issues by the D.C. Circuit Court of Appeals. In a
20 News Release issued today, the FCC announced that it will eliminate high capacity and
21 dark fiber transport and loops that are served out of ILEC central offices that serve as few
22 as 24,000 business access lines or have as few as three fiber-based collocators. A copy of
23 the News Release is attached as Exhibit ___ (RK-4). The effect on Verizon’s service

1 territory in Washington is unclear at this point, but at a minimum, the continued
2 availability of high capacity UNEs, even in theory, is in serious question.

3 **Q. WHAT CAN THE COMMISSION DO IN THIS PROCEEDING?**

4
5 A. The Commission cannot control federal law, or more specifically how the FCC
6 implements Section 251 of the Telecommunications Act of 1996. The Commission,
7 however, regulates the intrastate services that Verizon provides in Washington, including
8 DS1 and DS3 special access services. By establishing cost-based rates for these services
9 when they are provided to CLECs, the Commission can take an important step toward
10 furthering its and the Legislature's goal of fostering the development of effective local
11 exchange competition in Washington. Commission Staff witness Thomas Spinks
12 calculated in the pending Verizon cost docket, Docket No. UT-023003, that Verizon
13 enjoys a 97% share of the local exchange market in its service territories in Washington.
14 This virtual nonexistence of competition in Verizon territory will not change if CLECs
15 continue to be denied access to Verizon's high capacity circuits at reasonable prices.

16 **Q. IS PRICING THE ONLY OBSTACLE TO CLECS' USE OF VERIZON'S**
17 **INTRASTATE SPECIAL ACCESS SERVICES?**

18
19 A. Unfortunately, no. Verizon likely will do everything it can to protect its monopoly by
20 erecting as many obstacles as possible to CLECs' ability to use these services to compete
21 with Verizon. Those, however, are battles for another day and another case. Here and
22 now, the Commission can begin to decrease its increasingly shaky reliance on the FCC
23 and Congress and take the steps necessary to encourage local exchange competition in
24 Washington by establishing reasonable, cost-based rates for the high capacity circuits that

1 facilities-based CLECs need to offer an effective alternative to Verizon's local exchange
2 services in this state.

3 **RECOMMENDATION**

4 **Q. WHAT DOES XO RECOMMEND?**

5
6 A. XO recommends that the Commission establish wholesale prices for DS1 and DS3
7 special access services at the levels the Commission has established (or will establish in
8 the current Verizon cost proceeding, Docket No. UT-023003) for DS1 and DS3 UNE
9 loops and transport. Verizon estimates a higher cost to provide these UNEs than to
10 provide corresponding special access services, so establishing the prices for these services
11 at UNE cost levels ensures that the revenues generated will significantly exceed the costs
12 that Verizon incurs to provide the services. See Exhibit ___ (RK-2) at Verizon Response
13 to TWTC/XO Data Request No. 1-003.

14 **Q. WHAT EFFECT WILL SUCH A PRICE DECREASE HAVE ON VERIZON'S**
15 **INTRASTATE REVENUES?**

16 A. The effect, if any, should be minimal. Even if the number of high capacity circuits that
17 Verizon currently provides as intrastate special access services to wholesale customers
18 remains unchanged, it is a small fraction of the total number of such circuits that Verizon
19 provides to its retail customers. See Exhibit ___ (RK-3C) (Confidential Attachment to
20 Verizon Response to TWTC/XO Data Request No. 1-006). In all likelihood, however,
21 the reduced prices should encourage facilities-based CLECs to purchase more intrastate
22 high capacity services, potentially *increasing* Verizon's intrastate revenues for these
23 services. In any event, the benefits to Washington consumers who are presently deprived

1 of an effective alternative to Verizon's local exchange services certainly outweigh the
2 revenue impacts of XO's recommendation.

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

4 **A.** Yes, it does.