## D. POSITIONS OF THE PARTIES

### 1. IXC Stipulation

The IXC intervenors -- AT&T, MCI, Sprint, and the IAC -- recommend, via a stipulation, that the Commission defer action on the proposed LTR, and that rates for switched access service under the LTR be established in USWC's current general rate case. In the stipulation, they also state agreement on principles that should govern rates for switched access service under the proposed LTR in the rate case:

1. Costs for each element should be established by TSLRIC--or USWC's ASIC (average service incremental cost).

2. Each element should be priced at TSLRIC.

3. Universal service should be addressed in another docket.

4. If the Commission determines that any revenue in excess of TSLRIC should be recovered through access prices, any such amount should be identified and recovered through the CCLC. The other rate elements should be priced at TSLRIC. The CCLC should be phased out over two years, or the same period over which local rates are increased, whichever is shorter. In the event that USWC and GTE are allowed entry in the interLATA market, any remaining CCLC should be eliminated at the date of such entry.

5. Although parties recommend that prices for LTR rate elements not exceed TSLRIC, if the Commission nevertheless determines contribution should be included, the price difference between differing access configurations should reflect only the absolute underlying differences in TSLRIC cost.

### 2. Individual Positions

With regard to the IXCs' requested deferral of consideration of the LTR, USWC argues that a decision on the LTR should not be pushed off to further proceedings. USWC argues that the first step toward rational competitive interconnection policies is to integrate interconnection charges between wireline carriers (IXCs and ALECs). However, USWC argued that the current charges are too high and excessively bundled.

Responding to allegations that it has not properly priced its transport options, USWC argues that pricing involves considerable judgment, and is not black and white. It argues that there are several principles that should be observed:

1. Prices should not be set at incremental cost, unless that is the only price for which there is a demand.

2. No service should be offered for less than the incremental cost.

3. Normally, all services should provide contribution to shared and common costs, as well as the profit of the company.

4. This does not mean that markups need be uniform for all services. They should not be, when market factors are appropriately considered. This is where judgment comes into play, and the company's proposals in a dynamic competitive market should not be second guessed by the Commission unless they are manifestly out of line and will cause clear harm to specific public policies the Commission is charged with protecting.

Regarding allegations that the relationships between USWC's prices for DS1, DS3, and tandem switched transport disadvantages smaller carriers, USWC argues their witness Ms. Wilcox's Exhibit C-47 demonstrates that the critics have incorrectly analyzed the relative contribution levels between services and that contribution levels for the three transport alternatives are comparable, and the rates are not unreasonably or unduly discriminatory.

USWC argues that allegations of discrimination, which it defines as customers in the same class paying different rates for the same service, are not correct as a matter of law. For example, all DS1 customers pay the same rate. USWC argues that the three services being compared are different services, and do not involve different rates for the same thing.

USWC argues that its proposed transport prices are not excessive in the marketplace because 1) they are the same as for equivalent private line services, 2) they are lower than those charged by independent LECs, and 3) they are higher than those charged by USWC's current competitors, as shown by Ex. C-49. Therefore, the Commission should allow USWC to price these services to the dynamic market conditions, in order to maximize its participation.

USWC responds to a Commission Staff recommendation that it double DS3 rates. It contends that the recommendation is arbitrary and makes no sense, that no evidence has been provided to show the rates are under cost or have too little contribution. It argues that the recommendation seems designed only to remove USWC from the dedicated transport market, as dedicated transport is the first service that competitors are targeting. It argues that it is not permissible for the state to use its power to purposely harm USWC's legitimate business, and that intentionally unbalancing the playing field against USWC is not the Commission's role under any of the State's statutes.

Concerning the proposed local switching charge increase, USWC argues that the current $0.0065/minute is among the lowest in the country, and below the $0.008357/minute approved at the federal level; that the increase results in a lower RIC; and that the cost:price relationship is reasonable, especially compared to other switched access rates.

USWC defends its RIC proposal. It argues that the Commission cannot adopt rates in this case that lower the Company's revenues, as the Company is entitled to earn a reasonable return, and there was no evidence presented that earnings are excessive. USWC argues that, as Ms. Wilcox testified (Ex. T-1, p. 31), under the transport restructure its transport revenue will decline from $24 mil to $5 mil. USWC argues that the RIC may be reduced over time as rates are rebalanced.

USWC opposes Commission Staff's proposal that it be ordered not to charge the RIC to companies who do not use USWC's transport facilities. It states several reasons for its opposition to that proposal: 1) It violates USWC's right to revenue neutrality; 2) It would be difficult and expensive to administer; and, 3) It would subject USWC to a competitive disadvantage. USWC argues that, furthermore, the Commission has long followed a policy that IXCs must make significant contribution to the support of the local network, from which those companies gain immense benefit. That absolute level of contribution needs to be reexamined in the rate case, but this is not the appropriate proceeding to reduce that contribution just for those companies that utilize non-USWC transport. Finally, USWC argues that their RIC is not a charge related to transport, that it merely represents a way to make the filing revenue neutral. Staff's recommendation does not serve to further any public policy goals, and its adoption would be improper.

Commission Staff concurs with USWC on the need for local transport restructure, and recommends that the Commission not delay a decision on the LTR. Staff agrees with the general concept of LTR proposed by USWC, but takes issue with several aspects of the Company's proposal, as described below. Staff argues that the suspension date of the present interconnection docket predates the suspension date in the rate case, so the Commission cannot simply defer consideration of these rates to a later date. Staff suggests that the Commission may revisit LTR later.

Regarding transport prices, Commission Staff argues that the relationships between USWC's proposed prices are inappropriate. Staff witness Selwyn testified that it is inappropriate to price LTR transport based on private line prices, as advocated by USWC, because private line and local transport markets are different, and are at different stages of competition. (Selwyn, Ex. T-114, p. 48)

Commission Staff contends that it is inappropriate to price DS3 and DS1 switched transport with varying levels of contribution. Staff advocates a 9.6:1, DS3:DS1 price ratio as the basis for determining if the proposed prices provide an unfair advantage to large IXCs, consistent with the FCC's order in the interstate local transport restructure proceeding, except as to the DS3 entrance facility rate. (Selwyn, Ex. T-114, p. 47) Dr. Selwyn testified that after examining USWC's updated cost studies, all DS3 transport (other than the entrance facility charge) falls significantly short of the 9.6:1 benchmark. (Ex. T-116, p. 3)

Commission Staff recommends that, in order that USWC's proposed prices pass the 9.6:1, DS3:DS1 benchmark, the Commission set all DS3 transport rates (other than the entrance facility charge) at twice the level proposed by USWC. Staff explains that its main

concern is the relative pricing between DS3:DS1, not the absolute levels. It argues that the Company's pending rate case is the proper forum to reexamine the Company's switched access rate levels in general, when both the DS3 and DS1 transport rates could be reduced, while still maintaining an appropriate price ratio.

Staff supports statements by MCI witness Wood that USWC and other LECs should not be in the position to determine the winners and losers among IXC carriers.

Commission Staff urges the Commission to reject the proposed increase in local switching from $0.0065 to $0.0100/minute. Staff contends that USWC has not provided the Commission with any basis for a 57% increase in the local switching charge. It argues that the increase is an attempt to shift substantial amounts of contribution from local transport elements to local switching--a monopoly bottleneck service.

Commission Staff witness Lundquist characterized USWC's proposal to increase its local switching charge as odd, at best. (Ex. T-107, p. 32) Staff argues that USWC's position does not square with USWC witness Harris' testimony that switching costs have been declining dramatically in recent years. Mr. Lundquist performed a comparative analysis of contribution levels, which he testified does not support USWC's claim that the local switching charge provides a relatively low level of contribution. (Ex. T-107, p. 34) Staff argues that Mr. Lundquist's analysis shows that USWC employed contradictory tests for determining the appropriate level of contribution.

Relying on an exhibit showing local switching charges from many jurisdictions, Mr. Lundquist characterized USWC's local switching charge as "...admittedly toward the low end of the pricing spectrum..." but not "out of line" with other jurisdictions. (Ex. T-107, p. 36) Staff argues that USWC's argument lacks any analysis of why other states' charges are lower, or why those would be appropriate and the current charge is not.

Commission Staff supports a RIC, without enthusiasm, as the least objectionable way to achieve revenue neutrality, and because it is temporary until a decision in the general rate case. Dr. Selwyn testified that the RIC results in USWC's proposed LTR rates being no closer to the economies of providing access service than the current access prices and structures. (Ex. T-114, p. 32)

Because it opposes an increase in the local switching rate, Commission Staff proposes a RIC higher than USWC's proposal. Staff calculates that the RIC would be $0.014073/minute, rather than $0.010574/minute proposed by USWC. (Wilson, Ex. T-155, p. 51) A lower switching charge than proposed would necessitate a higher RIC, to maintain revenue neutrality.

Commission Staff strongly objects to USWC's proposal to apply the RIC to all local switched minutes, regardless of whether that traffic is switched to USWC transport or a competitor's transport. It proposes that application of the RIC be limited to traffic switched to USWC transport facilities. Staff argues that applying the RIC to all switched minutes

would inappropriately establish a protectionist policy which would insulate USWC from losses in any competitive local transport business. (Selwyn, Ex. T-114, p. 33) The RIC is to recover $14.8 million, while local transport is $4.3 million. The net effect is to negate USWC's "economically based" rate structure. Staff contends that its proposal could be accomplished by reprogramming the Company's interexchange access billing system. As an alternative, Staff suggests a self-reporting mechanism, which would require IXCs that purchase local switching to certify the percent of total switching minutes being completed on USWC transport facilities. This would be similar to the current percent interstate use factor IXCs use to separate intra and inter state traffic. Staff argues that USWC's allegations that these options would be costly and difficult to implement are unfounded, based on Ms. Wilcox's cross examination testimony that the company had collected no data and done no studies to support these allegations, and that she had no experience in reprogramming the company's billing system.

In response to USWC's contention that applying the RIC only on traffic switched to USWC transport facilities would put the Company at a competitive disadvantage, Staff makes two arguments: 1) Dr. Selwyn testified that Staff's proposal should not limit USWC's ability to compete in the transport market, but USWC's proposal would limit competitors' ability to compete; and, 2) Even if Staff's proposal resulted in a slight loss of market share for USWC, the Company would probably see an absolute gain in business, because competition will probably stimulate demand for telecommunication services. (Selwyn, Ex. T-114, p. 39) Staff also argues that the temporary nature of the RIC would have at most, a minimal impact on the Company.

Regarding USWC's proposal to eliminate its intra-LATA foreign exchange service, Staff recommends that the Commission deny the request. Staff expresses a concern about the revenue impacts of eliminating the service from the switched access tariff. (Wilson, Ex. T-154, p. 20) Mr. Wilson also testified that the Company provided no justification for the change.

Public Counsel generally supports USWC's local transport restructure proposal, except for the proposal to increase the local switching charge. Public Counsel does not argue against revenue neutrality, and agrees that a RIC is appropriate. However, because of opposition to the proposed increase in local switching, Public Counsel generally supports Staff's RIC calculation. While Public Counsel agrees that Staff's proposal to apply the RIC only to traffic switched to USWC transport facilities is a theoretically sound approach, it takes no position on the issue. Finally, Public Counsel recommends that the policy decision on whether the RIC should be maintained indefinitely should be decided in the general rate case.

AT&T contends that the structure of USWC's proposed LTR is a good step, but that the prices are unacceptable. AT&T urges the Commission to reject the revisions proposed for switched access for several reasons. First, all parties agreed that TSLRIC is the proper cost basis for rational pricing. However, given Staff's testimony of its inability to obtain information to review costs, USWC has clearly failed to meet its burden of supporting its

rates. Second, most parties disagree with the fundamental premise of USWC's "revenue neutral" filing. Given that USWC's revenue requirement is before the Commission in the Company's general rate case, the rate case would be the appropriate place to address USWC's switched access rates. (Sumpter, Ex. T-110, p. 13) AT&T also argues that the Commission can adopt local interconnect policies and rates, without changing access rates. Changing those rates for a few months after this case is concluded until the order in the rate case is issued is not an efficient use of resources. The proposed rates are so inequitable that IXCs support the continued application of current access charges. Moreover, unlike local interconnection, there are switched access rates currently in effect.

AT&T contends that USWC has the burden of supporting its rates and has failed to do so. Its cost studies are inadequate. Rather than moving toward TSLRIC prices as USWC contends, its proposal is an obvious attempt to foreclose any competitive alternatives that may emerge for the LTR functions. By doubling its local switching charge, IXCs will still pay USWC the same amount of money; it is just called something different.

AT&T recommends that if the Commission decides to adopt USWC's proposed LTR tariff, it should approve rates put forth by IAC witness Gillan as the rates that best support the approach in the IXC stipulation. AT&T opposes Staff's recommendation to double the proposed DS3 rates, in order to attain a particular contribution ratio with DS1 rates, as it would increase access charges, and is contrary to the record evidence supporting reductions in access rates.

MCI argues that USWC's LTR is driven by entrance of competition into the market for switched access service. MCI witness Wood testified that LTR would have several affects, one of which is that if excessive markups over cost are built into interconnection rates that competing companies pay USWC, customers (both companies and end users) will be denied the benefit of declining prices in a competitive market. (Ex. T-136, p. 31)

Regarding the price relationship between DS3 and DS1 transport rates, MCI argues that USWC's claim that competitive pressures are the impetus for its LTR filing is inconsistent with its proposal. MCI argues that Ms. Wilcox's statement that LTR rates have been set to exceed ADSRC plus contribution is contrary to the result in a competitive market. If USWC actually faced competition, the contribution rate elements should have dropped to slightly above TSLRIC to recover economic overhead associated with the service offering.

MCI argues that Ms. Wilcox admitted that its DS3:DS1 rates are not based on underlying costs, but on "market factors." MCI witness Wood testified that allowing an incumbent to use anticompetitive pricing strategies to eliminate existing competition, or prevent future competition, is indeed a use of market factors, but is a use that should be constrained. (Ex. T-136, p. 41) He testified that price differentials which track differences in cost are not inherently discriminatory, but USWC's proposed prices are discriminatory. (Ex. T-136, p. 42) If USWC is allowed to arbitrarily exaggerate the rate differential in its DS3:DS1 rates as it has proposed to do, it would provide USWC the ability to directly

impact the level of competition by IXCs. MCI argues that this is poor public policy, and would direct rates away from cost based. Therefore, MCI recommends that the Commission adopt Dr. Selwyn's interim recommendation to double USWC's proposed DS3 rates, which should be followed by cost-based rates with proportional contribution based on new cost studies, to be filed within 30 days.

MCI opposes USWC's proposal to increase its local switching charge. MCI argues that USWC did not argue that the existing local switching charge was below TSLRIC, or that local switching costs have increased, and in fact testified that switching costs have been declining dramatically. MCI characterizes USWC's proposed switching charge increase as an attempt to redistribute the severely inflated levels of contribution present in existing switched access rates, which should be rejected.

Finally, MCI urges the Commission to reject USWC's request for revenue neutrality through a RIC. MCI agrees with Commission Staff that the RIC is a protectionist policy, which is not in the interest of long-distance users. Additionally, Mr. Wood testified that providing revenue neutrality through the RIC, when costs, such as switching, are decreasing, actually provides USWC with a guarantee of increasing profits. (Ex. T-136, p. 35) Thus, MCI recommends that the RIC be rejected, and recommends that the Commission proceed with cost-based rates.

Sprint, like AT&T, recommends on brief that the Commission reject USWC's LTR proposal, and set switched access rates in USWC's pending rate case. Sprint also supports the IXC stipulation that switched access elements be priced at TSLRIC, with any contribution flowing through the carrier common line charge, which should be phased out over two years.

Sprint agrees with the other IXCs that USWC's proposed transport rates are discriminatory, and will negatively impact competition. Sprint contends that USWC's cost studies show that per circuit, access cost differences between DS1 and DS3 are almost negligible, which indicates that 90% of the cost advantage bestowed upon large IXCs is unearned. Sprint agrees with IAC witness Gillan that the rates would not only result in diminished competition between large and small IXCs but also would result in fewer competitive options for less densely populated areas.

Sprint argues that contrary to USWC's statement that it is moving toward cost based rates, its LTR rates do not reflect the way costs are incurred, are not cost based, and do not encourage efficient use of the network. Sprint argues that USWC's rates would encourage a company to purchase DS3 service at a point where the customer would utilize less than 20% of the available capacity. (McCanless, Ex. T-99, p. 9)

Sprint shares IAC's concern that USWC's proposal would have an adverse impact on non-urban competition.

The Interexchange Access Coalition (IAC), like the other IXCs, does not oppose the particular rate structure proposed by USWC. IAC does not oppose a revenue neutral component to the rates. However, IAC contends that the rates proposed by USWC for switched access service are unjust, unreasonable, unduly discriminatory, and anticompetitive. IAC further argues that USWC's proposed rates contain so much contribution, and are so discriminatory, that even main beneficiaries of the discrimination--the large IXCs--recommend that the Commission reject the rates as proposed, and accept the IXC stipulation.

IAC argues that while DS1 is generally provided by DS3 transport facilities, such provisioning could impose additional costs on the network. IAC is not opposed to prices reflecting such cost differences. However, IAC contends that USWC's rates are totally out of proportion with those additional costs. By seeking to recover more contribution from DS1 than from DS3 customers (who could bypass USWC's network), USWC is asking small users to subsidize access charge discounts to larger users. IAC argues that USWC did not dispute the fact that its proposed LTR rates would have a disparate impact on IXC competitors, and points to USWC's Owens statement that high volume end users are very sensitive to price. Therefore, argues IAC, USWC's proposed rates are unduly discriminatory, and are counter to the State's policy to promote diversity in the supply of telecommunications services and products in telecommunications markets, under RCW 80.36.300(5).

Responding to USWC's argument that the pricing is not discriminatory, IAC argues that transport is a singular service, regardless of the option selected -- DS1,DS3, or TST. As USWC is proposing to collect differing levels of contribution from the different services, its proposal is discriminatory.

IAC witness Gillan testified that another aspect of the proposed LTR rates is anticompetitive. Mr. Gillan argued that USWC's pricing will make it extremely expensive for IXCs to provide service to non-urban markets, where DS3 and DS1 transports are not economically viable:

> Even for AT&T, the DS3 transport option will be possible primarily in dense urban environments, while the tandem-transport option will typify the access arrangements used in smaller markets. As a result, increasing the price of the tandem transport option will increase relative cost to serve less populous areas. Inflating the cost to serve small markets will ultimately lead to fewer choices in rural areas or lead to de-averaged retail rates that exceed any underlying differences in costs.

(Gillan, Ex. T-95, p. 14)

IAC also argues that USWC's proposed LTR rates would result in inefficient use of the public switched network. IAC contends that use of the network will be efficient only if the price differences between interoffice transport options reflect the underlying cost difference. Thus, USWC's proposed rates create incentives for the inefficient use of the

network, contrary to RCW 80.36.300(2), which states the policy to maintain and advance the efficiency...of the telecommunication service.

IAC argues that in addition to adversely affecting the competition for intrastate toll, USWC's proposal would adversely affect local competition, through the same discriminatory pricing mechanism.

The ALECs contended at hearing that USWC's proposed LTR transport charges, which are incorporated into the LIS, are inaccurately priced, particularly the rate for tandem switched transport. The new entrants are likely to want to interconnect at the USWC tandem for efficiency reasons. They then would not need to connect directly to every USWC end office or to every other LEC and IXC. USWC proposes to price the transport between its tandem and its end offices at private line market rates. The ALECs contend that tandem switched transport should be priced at cost.

MFS urges the Commission to order cost based rates for transport services. MFS characterized the FCC's RIC as a poorly conceived political compromise, with no cost justification, and recommends that the Commission reject all non-cost supported subsidies like the RIC.

TRACER takes issue with Staff's proposal to double USWC's proposed DS3 transport rates. TRACER argues that no party contends DS3 prices are below cost, or that the DS3 price is itself inappropriate. Rather, the complaints are that the contribution per channel is different. TRACER argues this provides a rationale for decreasing DS1 rates, not increasing DS3 rates.

Regarding the relative contribution in rates between DS3 to DS1 rates, TRACER argued that there are legitimate reasons why contribution in DS3 rates might be less than 28 times that in DS1 rates. Dr. Zepp testified:

> When...a large group buys a DS3 they take the risk that they totally fill that DS3 and therefore they are fully paying for it. There is no unused capacity as far as US West is concerned. US West has sold it all and it's fully compensatory, whereas the DS1, US West is taking that risk, and therefore they've got to take that into account when they do the pricing.

[Zepp, TR., p. 2124]

TRACER also argues that an unjustified doubling of the DS3 rate would provide a customer with alternatives to seek other providers. It argues that Staff's proposal to double the DS3 rate is unwarranted and should be rejected.

DOD/FEA characterizes USWC's proposal to increase its local switching charge as an abuse of monopoly power.

## F. COMMISSION DISCUSSION AND DECISION -- LTR

The Commission would have preferred to have dealt with Local Transport Restructure issues in a separate proceeding devoted to LTR, or in the general rate case. LTR will have a significant impact on intrastate toll competition in Washington. We see no legitimate justification for dropping it into a docket that primarily concerns local interconnection.

Based on the record in this proceeding, the Commission identifies five issues which must be decided in this Order:

1. Should and can the Commission defer consideration of the LTR to another proceeding?
2. Are the transport options properly priced?
3. Is the need for and amount of the proposed increase in the local switching charge supported?
4. Is the need for and amount of the RIC supported? If so, should the RIC be imposed only on traffic switched to USWC transport facilities, or on all local switched traffic?
5. Should USWC be permitted to eliminate intraLATA foreign exchange service from its switched access tariff?

We reject USWC's LTR tariff for many reasons described below. We will provide discussion on the topics listed above, and also provide some policy direction concerning how the LTR rates should be approached in USWC's general rate case.

First, we disagree with USWC's basic premise to base LTR rates on existing private party line rates. We agree with Dr. Selwyn that it is inappropriate to price LTR transport based on private line prices. Private line and local transport markets are different, and are at different stages of competition. (Ex. T-114, p. 48) Further, we reject USWC's position that it makes more sense to use the private line prices than to start from scratch. Restructuring USWC's local transport rates will have a large impact on the direction of intrastate toll market. Thus, we would have expected USWC to provide rates based on sound economic and public policy considerations, and have supported those rates with proper, fully supported incremental cost studies. Instead, USWC's proposal is based on rates from services that serve different markets, the proposal uses inappropriate "market factors," and it is not supported by adequate cost studies. The Commission expects USWC to correct these problems in its general rate case.

We agree with AT&T that it would be inefficient to adopt LTR rates in this proceeding. The rates would most likely change in USWC's pending rate case, especially given the magnitude of the RIC. Staff witness Selwyn's testimony (Ex. T-114, p. 32) that the RIC results in USWC's proposed LTR rates being no closer to the economies of providing access service than the current access prices and structures also supports this result. We also find persuasive AT&T's argument that USWC's proposed LTR rates are so inequitable that the IXCs supported the current, bundled rates. Restructuring USWC's access rates in the presence of an economically overwhelming RIC provides no benefits to switched

access customers, as evidenced by the IXC stipulation, and obviously does not benefit the public in general.

The inefficiencies embedded in the LTR rates proposed by USWC are so great, that we find the public interest best served by endorsing the general structure proposed by USWC for its LTR tariff, while rejecting the tariff as filed. We here provide guidance for revisiting the question in USWC's general rate case, where determining specific LTR rates will be economically meaningful.

We agree with USWC that considerable judgment is involved in pricing, that it is neither black nor white. Further, we agree with USWC that the Commission must intervene when a regulated company's proposed rates are manifestly out of line with, and will cause clear harm to, specific public policies the Commission is charged with protecting. USWC's proposed LTR rates clearly contradict two specific public policies the Commission is charged with protecting.

First, several parties convincingly argue that USWC's proposed rates would inappropriately favor large IXCs at the expense of small IXCs, resulting in diminished competition for intrastate toll services. While we are not persuaded by Staff's proposal to double DS3 rates to obtain a 9.6:1 cost ratio to DS1 rates, it is important to note that USWC's rates fail to meet the relative price ratio described in more detail below. As IAC points out, the failure of USWC's rates to meet this relative price ratio is significant because, as USWC witness Owens stated, high volume end users are likely to be very sensitive to price. USWC has proposed to use "market factors" to collect significantly more contribution above TSLRIC from IXCs using lower-level transport options, than those using the DS3 levels. We agree with IAC that this clearly indicates USWC's proposal would have a detrimental effect on smaller IXCs, with no justification other than USWC's "market factors." An added concern is the negative impact USWC's rates would have on services to less populated areas, as described by IAC witness Gillan. We agree with MCI witness Wood that USWC should not be allowed to exercise its market power by applying mark-ups so as to artificially eliminate or prevent competition. Approving a proposal that would result in less intrastate competition, and less competition in less densely populated areas, clearly would be contrary to the "promote diversity" public policy set out in RCW 80.36.300 (5).

Second, Sprint articulates another reason why we should reject USWC's proposal. USWC's proposed pricing for transport options would push carrier customers to purchase DS3 capacity service at a point where it would utilize 20% of the available capacity for that service. If this excess capacity occurred because prices were consistent with price ratios from the underlying TSLRIC relationships, one might argue that the excess is economically efficient. However, this excess capacity is not driven by costs. It is driven by USWC's application of "market factors," which implies the excess capacity is inefficient. Thus, USWC's LTR rates clearly conflict with another telecommunications public policy, RCW 80.36.300 (2): "Maintain and advance the efficiency and availability of telecommunications service."

We provide the following guidance regarding how LTR rates should be established in the Company's rate case. First, the Commission cannot accept rates that would produce the results we have found unacceptable in this proceeding. Second, as discussed above, while Staff's 9.6:1 cost ratio between DS3 and DS1 rates may be useful in gauging rates, we are not persuaded that this ratio should be the basis for setting the rates. The argument is superficial in terms of underlying costs of providing different service levels. It appears that the 9.6:1 cost ratio may avoid some anticompetitive problems from the FCC's perspective, but the approach seems as arbitrary in this proceeding as USWC's "market factor" approach.

With regard to the principles advocated in the IXC stipulation, we agree that costs for each of USWC's LTR elements should be established at TSLRIC, not USWC's surrogate, ADSRC. We believe that TSLRIC is an appropriate price floor for these elements, but at this time do not believe that prices should be established at the bare minimum. We agree with USWC that it has long been the policy of this Commission that interexchange carriers must make significant contribution to the support of the local network, from which they gain immense benefit. Further, we are not persuaded by any evidence on this record that the public interest is best served by abandoning this important policy.

We do not reach the question whether the public interest is better served by spreading the contribution from switched access among the LTR elements (according to some underlying cost justification), placing all of the contribution onto a specific charge (such as the local switching charge), or a combination of those options. However, if prices are to be set higher than TSLRIC (or, in other words, are to include some level of contribution), the relative price ratios between DS3 and DS1 transport elements are important. We are persuaded by the IXCs and Staff that if DS3 to DS1 relative price ratios become too small, it will have inappropriate, negative impact on small IXC competitors and competition to less urbanized areas. The question then becomes what is the appropriate relative price ratio? As mentioned above, the Commission rejects Staff's use of the FCC's 9.6:1 price ratio. General microeconomic theory discusses the importance of relative prices, in that changes in relative prices will affect purchasing decisions, and efficient purchasing decisions would be based on relative incremental costs. Thus, economically efficient purchasing decisions between DS3 and DS1 transport would be based on the underlying TSLRIC ratios of the individual LTR components. Such a price ratio would help to minimize any potential economic distortions from pricing above TSLRIC. If we had confidence in USWC's cost estimates, these relative price ratios could be obtained using Exhibit C-100, by dividing the TSLRIC of each DS3 transport component by the TSLRIC of the corresponding DS1 component. The Commission believes the TSLRIC ratio should be the threshold, below which relative prices between DS3 and DS1 transport components should not fall. This should be the case until such time as the transport market exhibits highly competitive attributes. While the Commission is adopting this relative price ratio as a minimum, we are undecided if the price ratio should be allowed to rise above the relative TSLRIC ratio, and would welcome discussion on this topic in USWC's general rate case, where we assume proper cost estimates will be available.

We are not persuaded by AT&T's argument that interconnection rates for local and long distance should come together and be priced at TSLRIC at some time in the future. It should be clear from the discussion above that we believe IXCs derive significant benefits from having access to local exchange company networks, and thus should contribute a fair share toward the common costs required to provide those networks. Also, at this stage of a rapidly changing market, it is uncertain whether the rates for local and long distance will converge over time. These are different markets, competing in different ways. If, when, and how such rates may converge remains to be seen.

We reject USWC's proposal to increase the local switching element of its switched access charge from $0.0065 to $0.0100/minute. USWC's proposal is a step toward economic inefficiency, which the Commission must be particularly mindful of in an increasingly unbundled and competitive market.

USWC provides no cost justification for increasing the local switching charge by 57%. USWC's arguments in support of increasing the local switching charge element are not persuasive. USWC witness Harris testified that switching costs are declining.[22] His testimony provides justification to decrease the local switching charge, not to increase the rate by 57%.

To support its proposal to increase the local switching charge, USWC argues that the level of contribution from the current local switching charge is too low, relative to contribution the Company seeks to recover from transport functions. In support of this argument, Ms. Wilcox provided Exhibit C-53. This exhibit is a poorly supported chart, based on total contribution rather than contribution from each element. It does not justify the proposed increase. The Commission rejects this argument for several reasons:

First, USWC's assertion that local switching provides less contribution than transport is based on comparisons of prices to ADSRC, rather than to the appropriate TSLRIC costs, which renders the comparison useless. Proper comparisons using TSLRIC were not provided in this case. Even if such comparisons had been presented, we believe any such comparison would be highly suspect. We have very little confidence in the cost studies USWC utilized for its case.

Second, we are especially concerned about USWC's local switching cost estimates. Given Dr. Harris' testimony that local switching costs are declining dramatically, there is a significant risk of an upward bias in the switching cost estimates, which would result in the analysis of contribution from either the current or proposed local switching charge being unreliable.

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[22] Dr. Harris wrote: "The application of transistors, semiconductors, integrated circuits and other microelectronics in telecommunications equipment has dramatically reduced switching and transmission equipment costs...." (Ex. T-10, p. 5)

Third, the Commission finds that USWC has employed contradictory and confusing tests to determine appropriate levels of contribution. USWC witness Wilcox testified that while she does not advocate equal contribution for LTR components, the switching charge should be increased because the differences in contribution levels are too great. (Ex. T-46, p. 28) When we examine Exhibit C-100, we note that the percentage contributions for all transport options exhibit a large range. The contributions from both the current and proposed switching charges lie within that range. Thus, even if the Commission had some confidence in the cost estimates provided, we are left to wonder what upper and lower bounds USWC believes contributions from LTR components (or subsets of components) should lie within, and the theoretical basis for those subsets and boundaries. Without providing these bounds and subsets, and its reasoning for the bounds and groupings, USWC's argument to increase the local switching charge based on relative contributions of other LTR components is, indeed, contradictory.

Fourth, the argument to increase the local switching charge because it provides relatively less contribution than does transport is weak. The Commission finds USWC's testimony that local switching costs are declining dramatically a much stronger argument for what direction the switching charge should be moving.

USWC's final attempt to justify an increase in the local switching charge is a comparison of such charges in other states. It argues that an increase is justified because USWC's local switching charge is lower than switching charges in most other states. Perhaps if USWC had provided some explanation of why several other states have higher local switching charges, and why such charges provide benefits to the citizens of those states, this position would have some meaning. However, we do not find that such a bare comparison in any way justifies any increase, and certainly not an increase of 57%, when the service is exhibiting dramatically decreasing costs.

The Commission's decision to disallow an increase in the local switching charge is for purposes of this proceeding, based on USWC's inadequate demonstration here. We do not rule out raising the local switching charge in the general rate case as a way to obtain contribution from switched access customers. As stated above, IXC carriers derive large benefits from the local network, and should contribute to the financial support of that network.

The final issue regarding LTR is USWC's proposal to eliminate its intraLATA foreign exchange service from the access tariff. Staff recommended that the Commission reject this proposal as the revenue impacts were unknown. (Wilson, Ex. T-154, p. 20) No other intervenor party presented any discussion or recommendation of this proposal. Ms. Wilcox's recommendation that the service be eliminated was based on the LTR being implemented. Since we are rejecting USWC's LTR tariff, there is no basis for accepting the intraLATA foreign exchange service proposal. We agree with Staff that this issue should be addressed in the rate case, where the revenue impacts can be managed in the context of total revenue requirement.

# IV. EXPANDED INTERCONNECTION/ VIRTUAL COLLOCATION

## A. INTRODUCTION

USWC has filed tariff revisions that would make available expanded interconnection and collocation opportunities for the first time on an intrastate basis in Washington. This offering holds the potential for companies to use alternative transport facilities (facilities other than those of the incumbent LECs) and then interconnect to the unbundled portion of the incumbent's network that they wish to use.

USWC envisions that new LECs that self-provision transport to the USWC end office would have to purchase virtual collocation services. This would include an entrance facility charge, an equipment charge and expanded interconnection channel termination.

There are two types of collocation. Physical collocation arrangements allow an interconnector full ownership, access and control of the transmission and circuit termination equipment installed in the incumbent central office for its dedicated use. Under a virtual collocation arrangement, the interconnector requests that the LEC install its desired equipment in the central office and the interconnector is denied direct access to the collocated equipment. Ownership, maintenance, and monitoring of the equipment is controlled by the incumbent.

USWC proposes offering only virtual collocation. USWC argues the Commission has no authority to mandate physical collocation, and that mandates or incentives to USWC to allow physical collocation would be an expropriation of USWC's property.

At least two courts have held that the ordering of physical collocation can violate telecommunications companies' property rights. Bell Atlantic Tel. Co. v. FCC, 24 F.3d 1441 (D.C. Cir. 1994); GTE Northwest Inc. v. PUC of Oregon, 321 Or. 458, 900 P.2d 495 (1995).

Commission Staff recommends that the Commission not consider physical collocation in this docket, because none of the parties who would benefit from it (other than AT&T) argue for it.

AT&T argues that the Commission should order USWC to file tariffs for both physical and virtual collocation. Public Counsel argues that the Commission should not require physical collocation at this time, if for no other reason than to avoid protracted litigation.

Parties have raised other concerns about the specifics of the USWC's tariff, including the tariff's handling of liability, the time frame needed for USWC to respond to requests for new IDE, criteria by which space and requests are accepted or rejected, procedures for

certifying contractors to install and maintain collocated IDE, training of employees and whether the purchase of an expanded interconnection channel termination ("EICT") avoids the application of other switched access rate elements.

### B. COMMISSION DISCUSSION AND DECISION -- EXPANDED INTERCONNECTION/COLLOCATION

The Commission agrees with Public Counsel regarding physical collocation but would like to note that during the development of expanded interconnection rules the Federal Communications Commission concluded that physical collocation was the best means for ensuring a fair basis for competition in the provision of interstate access service because it avoided the operational complications associated with one company relying on a competitor to install, maintain and repair their equipment. (Lundquist, Ex. T-107, p. 9)

We also agree with Public Counsel's argument that there is no reason that virtual collocation should cost any more than physical collocation.

USWC originally proposed virtual collocation rate levels which mirrored its original FCC filing that was suspended by the FCC and later substantially reduced. On rebuttal USWC modified the rates to reflect the same overhead loading factor of 1.2 used to set the Company's interstate rates. The Commission adopts Staff recommendation to accept the loading factor but not the rates USWC proposes. The Commission agrees with Staff that the rates should be reduced further, to reflect total service long run incremental cost results using the recommendations by staff and discussed in greater detail in the next section of this order dealing with cost studies.

USWC also revised its proposal to include a lease back method that would allow inter-connectors to purchase collocation equipment. In addition, the new proposed tariff includes a switched access DS0 EICT upon receipt of a bona fide request. The Commission approves of the USWC modifications but other changes are needed to make the tariff acceptable. During cross examination, USWC's counsel affirmed the company's willingness to negotiate with parties on concerns regarding tariff language, including language dealing with dispute resolution. [TR., p. 1983 ll. 1-3]

The Commission accepts USWC expanded interconnection tariff contingent on the company refiling rates consistent with the 1.2 factor using TSLRIC, consistent with the guidelines established in the next section, and on resolving the tariff language concerns raised by parties in this proceeding.

The Commission is uncertain whether virtual collocation is necessary when local exchange companies interconnect. If meet points are established by mutual agreement, the decision about what equipment resides where will be part of that negotiation, and it is unlikely that the virtual collocation tariff would need to apply.

# V. COST STUDIES AND IMPUTATION

## A. USWC'S COST STUDIES AND POSITIONS OF PARTIES

USWC has submitted cost studies in support of the rates it proposes in this proceeding. The company proposes the use of average direct and shared residual costs (ADSRC) as target price floors. (Farrow, Ex. T-23, p. 9) Several parties disagree with USWC's cost determinations and/or use of costs in this proceeding. They argue that TSLRIC, not ADSRC, is the appropriate measure of cost. See, e.g., Bourgo, Ex. T-127, pp. 4-6. They argue that the company's measurement of costs is inappropriate and inconsistent with previous Commission orders. See, Ex. TC-155 (Wilson). Further, several parties argue that prices should be set at cost, or with small uniform levels of contribution. (Zepp, Ex. T-151, p. 5)

USWC has divided its total company costs into three groups. The groups are: 1) Direct costs of the specific product; these include both fixed and variable costs. 2) Shared residual costs or product family costs. These costs include those non usage sensitive costs related to providing the service for at least two products. 3) General overhead/common costs. These costs represent expenses that cannot be directly tied to a product or family group of products. USWC's studies in this proceeding measure the direct and shared residual costs of providing each product. These costs are unitized to equal the average direct and shared residual costs (ADSRC). ADSRC does not include the common costs of the company. (Farrow, Ex. T-23, p. 7)

Other parties in this proceeding support the use of LRIC (long run incremental cost) or TSLRIC (total service long run incremental cost). As used by these other parties, LRIC and TSLRIC do not include the shared residual costs included within the company's cost studies. LRIC and TSLRIC refer to the costs associated with providing the particular product or service that could be avoided in the long run if the product or service were not offered. A USWC version of TSLRIC is referred to as TSIC, total service incremental costs. (Wood, Ex. T-136, pp. 3, 15) Another term used by USWC is ASIC, average service incremental costs. ASIC is a USWC term which represents the unitized level of TSIC.

The parties that support LRIC or TSLRIC argue that ADSRC, which includes shared residual costs, is not the economic or correct price floor. They argue that shared residual costs included within the company studies cannot be avoided by USWC if the service is not offered. Mr. Wood for MCI-Metro testified that the fundamental concept of cost causation is ignored in the studies performed by USWC using Mr. Farrow's methodology. (Wood, Ex. T-136, pp. 3-5)

USWC argues that there are just three issues on measurement of cost. Those three are cost of money, depreciation, and the level of "fill" (average or objective).[23] The company argues that authorized return has nothing to do with the cost of money on a going forward basis. It argues that the cost of money in a cost study should be the cost of obtaining the money in markets going forward. (Farrow, Ex. T-23, p. 17) The company argues that approved depreciation has nothing to do with the prospective lives. The company also argues that average fill is correct, that the system will never be designed for objective fill, and that spare capacity is a necessity. Further, it argues, the Commission requires USWC to provide service on demand. Without spare capacity, timely implementation would be impossible, and further would be more costly. The company argues that there is no evidence that USWC has improperly invested in any plant.

Several parties argue that the company's studies fail to use Commission approved depreciation, authorized return, and objective fill. The studies were not consistent with Commission orders in Docket No. UT-930957, et al. Public Counsel states that it sees little distinction between SRC and common costs. Staff Witness Wilson testified that the company's use of cost of money and depreciation rates in excess of those authorized overstates the level of costs, and that the use of average fill implies that excess capacity is included within costs, thus increasing costs. (Wilson, Ex. TC-155, p. 6)

Several parties argue that the studies are inappropriately cryptic. In general, they refer to the inability of the parties to review the contents of the studies or to run alternatives. Public Counsel describes this as the "black box". Staff argues that they were not allowed to see costs of some vendors, and that they could not run studies as studies were not available on personal computers. Staff argues that there are no lists of what families are, and there is no justification to assign or allocate spare capacity in a similar fashion to traffic sensitive costs.

USWC argues that cost-based rates do not mean rates at costs. It argues that the precision of the cost studies is not all that relevant unless the Commission accepts the extraordinary assertion that rates for switching and transport be set at cost with no contribution to shared and common costs. They argue that no multi-product firm should be allowed to price any product at incremental cost unless no units would be sold at any higher price. They argue that none of the company's competitors can point to any instance where the competitors price at incremental costs, and that large competitive companies do not strive to price their products at cost.

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[23] It is the Commission's understanding that "fill" represents the utilization of a given capacity (trunking capacity, switching capacity, etc.). Average fill represents the actual usage of the system over an historic period. Average fill tends to be lower than objective fill, which represents the intended level of utilization if the system were operated at its optimum.

Several parties in this proceeding argue that pricing should be based on TSLRIC. Some argue that it is inappropriate for competitors to be required to pay prices that increase another competitor's profits. They argue that ADSRC includes contribution to USWC's overhead and profit. See, e.g., Zepp, Ex. T-151, pp. 16-17.

While Public Counsel states that recovery of shared residual costs through pricing is not improper, it argues that shared residual costs should not be included in costs studies as a basis for pricing. Public Counsel further argues that contribution levels above TSLRIC are appropriate but not in the fashion presented by U S West through use of its ADSRC studies.[24]

## B. COMMISSION DISCUSSION AND DECISION -- COST STUDIES

USWC's presentation is inconsistent with economic theory and inconsistent with previous orders of this Commission. As this Commission has found in the past, and as many witnesses in this proceeding testified, the appropriate measurement of costs is TSLRIC.[25] USWC has not presented TSLRIC cost studies in this proceeding. The ADSRC studies supported by Mr. Farrow include costs that he conceded would not be avoided if the product or service were not offered, and are not the economic price floor but rather U S West target price floors. (Farrow, Ex. T-23, p. 10) The company studies include the components TSIC, and its unitized version, ASIC, which appear to be consistent with the economic theory of TSLRIC. However, the Commission is concerned with the calculation of these costs.

In Docket Nos. UT-93057, UT-931055, and UT-931058, the Commission stated:[26]

> The Commission agrees with Commission Staff and other parties that the company's cost studies on Network Access Channel, Channel Performance, and Transport Mileage were flawed and should be rejected. [footnote omitted] These studies do not provide the Commission a sufficient basis upon which to set cost-based rates.

In that order the Commission rejected the company's use of average fill, non authorized depreciation rates, and a cost of money other than that authorized by the Commission. The order also required the company to use the hypothetical capital structure

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[24] In its brief, Public Counsel states: "So, while the issue of recovery of these so-called 'shared' costs remains an issue to be dealt with in any analysis of appropriate contribution levels ...."

[25] WUTC v. U S WEST Communications, Inc., Docket Nos. UT-930957, 931055, & 931058, Fourth Supplemental Order (September 1994). See, e.g., Ex. T-138 (Wood)

[26] Id., at p. 13.

that was used to develop the authorized return of 10.53% in Consolidated Docket Nos. U-89-2698-F and U-89-3245-P.[27]

The Commission generally continues to hold that view. The Commission does recognize that the cost of money needs to be looked at in a similar forward-looking fashion as other costs in a TSLRIC study. The Commission recognizes that the authorized return is based on embedded costs, particularly with respect to debt rates. The Commission believes that it may be appropriate to take a forward-looking review of the cost of money. However, in this proceeding the company has provided no evidence to support any change in the cost of money, either with respect to cost rates for debt or equity, or with respect to a change in the capital structure. The Commission does not suggest by this order that the company should, with each or any cost study, file revisions to its equity rates or capital structure. These costs levels are more appropriately set in general rate proceedings or separate rate of return proceedings.

The Commission generally agrees with Public Counsel's position on the use of cost studies for pricing. It is not improper to price at a level to recover prudently-incurred shared and common costs. In this proceeding, the level of contribution has been nearly impossible to review. What is an appropriate level of contribution? How much total contribution is needed to recover shared and residual costs? What level of contribution is included within other monopoly and competitive services provided by the company? What costs are direct? And which are shared or common? When looking at exchange service, is the local loop a direct or shared cost? What other policy issues need to be considered in the determination of contribution? The Company has not provided sufficient information for the Commission to be able to answer these questions. Therefore, the Commission is unable to determine the appropriate level of contribution for any service presented to it in this proceeding.

The Commission also notes testimony, including Staff witnesses Wilson and Selwyn, (Exs. T-154 and T-114) and ELI witness Montgomery (Ex. T-84; TR., p. 1139) among others, to the effect that USWC cost studies are difficult to review and to work with. As stated by Public Counsel, the company presented the proverbial "black box", which limits the ability of other parties to review and to independently test and verify the assumptions in the company's cost studies. The Commission adopts Commission Staff's recommendation that it order the company in future cost studies to comply with the recommendations for open access to the company's cost methodology, input data, assumptions, and cost modeling recommended there. These filings should include the full and complete set of work papers and supporting source documents, to be filed simultaneously with the results of the study.

For reasons set out above, the Commission is unable to identify the cost of the various products or offerings in this proceeding. The Commission also is unable to identify the proper level of contribution to be allowed in the prices of these various products or offerings. The Commission orders the company to file future cost studies consistent with this

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[27] Id. at p. 14, footnote 12

order. These studies should be TSLRIC studies, and as such should not include shared residual or common costs. The company should recognize that its protracted inability to produce respectable, auditable, "checkable" cost studies is detrimental to its own self interest. It must do better in this regard if it expects to fare better in persuading the Commission of the rightness of its positions.

## C. IMPUTATION

USWC did not submit an imputation study with its direct case. Other parties including ELI witness Montgomery addressed imputation in their direct cases. Mr. Montgomery's analysis indicated that U S West's proposed interconnection rates did not meet a proper imputation analysis. USWC rebuttal witness Purkey sponsored an imputation study on business exchange rates. His study indicates that the company's business rates do pass an imputation analysis. Other parties responded to this imputation study, suggesting that it was improperly done.

Mr. Purkey's imputation analysis was performed on an average business line as opposed to an individual service. Mr. Purkey indicates that residential service would obviously fail an imputation study since his company contends that residential rates are currently below costs. His imputation study on business exchanges is based on the company's cost studies, using ADSRC. He incorporates a determination of essential services. For these services he inputs the company's proposed pricing. All other elements are priced at cost. The only elements that are considered essential in his studies are: terminating expanded interconnection, terminating local switching, and terminating multiplexer maintenance.

Other parties disagree with Mr. Purkey's studies. They argue that he has misapplied the essential service notion, and that other services such as tandem switching and directory listings should also be considered essential. [Montgomery, TR., p. 1076] They also argue that the study improperly prices out costs such as the proposed universal service charge. [Cornell, TR., p. 2026]] Dr. Cornell's suggested modifications of Mr. Purkey's imputation studies indicate that business exchange does not pass imputation.

Commission Staff, in its brief, argues that the company's imputation studies do not comply with Commission guidelines. Staff also complains that while it is obvious that a imputation study is required, USWC did not provide one in their direct case. Staff objections to the imputation study are related to the averaging of the various business rates in Mr. Purkey's analysis. Staff points to prior Commission orders which require imputation on an individual service basis.

## D. COMMISSION DISCUSSION -- IMPUTATION

The company's failure to present imputation studies in support of its proposed rates in its direct case is unacceptable. The company failed to provide individual service imputation studies despite previous Commission order.[28] In this proceeding the Commission has rejected the company's interim universal service charge and the company's proposed minutes of use interconnection charges, has accepted the use of bill and keep on an interim basis, has modified the expanded interconnection proposal, and has ordered interim number portability at TSLRIC. The Commission sees no need to do an imputation in this interim period of bill and keep.

The Commission expects the company to support future filings made in compliance with this order with imputation studies which support price ceilings for the services offered for interconnection. These studies should be consistent with previous Commission orders. The Commission does recognize several issues which still need to be resolved. The Commission has not yet accepted any cost study for local exchange. There is no determination of what are direct elements of service associated with local service, or the cost of providing these elements of service. Further, the issue of what are essential elements of service has not been determined. The Commission is hopeful that some of these issues may be resolved in the current general rate proceeding.

The Commission would also like to take this chance to note that the simple passing of an imputation study is not sufficient evidence to support the fairness of proposed rates. While it is essential for fair competition that an imputation test be passed, such demonstration does not in and of itself indicate that the rates proposed are fair. The Commission needs to determine that the rates provide a level of contribution that is consistent with the public policy goals of the Commission.

## FINDINGS OF FACT

Having discussed above in detail both the oral and documentary evidence concerning all material matters, and having stated findings and conclusions, the Commission now makes the following summary of these facts. Those portions of the preceding detailed findings pertaining to the ultimate findings are incorporated herein by this reference.

1. The Washington Utilities and Transportation Commission is an agency of the state of Washington, vested by statute with authority to regulate rates, rules, regulations, practices, accounts, securities, and transfers of public service companies, including telecommunications companies.

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[28] In re Pacific Northwest Bell Telephone Company, Docket No. U-88-2052-P, Second Supplemental Order (January 1989).

2. U S WEST Communications, Inc. ("USWC"), GTE Northwest Incorporated ("GTE"), Electric Lightwave, Inc. ("ELI"), and TCG Seattle ("TCG") are each engaged in the business of furnishing telecommunications service within the state of Washington as a public service company.

3. USWC and GTE were, until recently, the exclusive providers of switched local exchange service in their respective Washington exchanges, and currently are the dominant providers of switched local services within their respective Washington exchanges.

4. ELI and TCG presently provide limited switched local exchange service in certain of the exchanges of USWC and of GTE, in competition with those incumbents.

5. To provide switched local exchange service, ELI, TCG, and other alternative local exchange companies ("ALECs") must interconnect with USWC's and GTE's switched networks.

6. The provision of interconnection between two local exchange networks for the purpose of terminating local traffic is an essential service which is not available from any other provider.

7. On November 14, 1994, USWC filed tariff revisions for its switched access service, which included the introduction of local interconnection service and the unbundling of local transport service for switched access. The revisions also included the introduction of expanded interconnection service and expanded interconnection - virtual collocation service for all companies. The stated effective date of the tariff revisions is January 1, 1995. The Commission suspended the tariff filings on December 15, 1994.

8. On November 15, 1994, in Docket No. UT-941465, TCG and Digital Direct of Seattle, Inc. (since acquired by TCG Seattle), filed a complaint against USWC alleging undue prejudice, discrimination, and unjust rates and practices in the provision of interconnection and mutual compensation. USWC answered and counterclaimed. On February 13, 1995, the Commission consolidated Docket Nos. UT-941464 and UT-941465 for discovery and hearing.

9. On February 7, 1995, in Docket No. UT-950146, TCG filed a complaint against GTE alleging undue prejudice, discrimination, and unjust rates and practices in the provision of interconnection and mutual compensation. GTE answered, counterclaimed against TCG, and filed a third party complaint against USWC.

10. On March 1, 1995, in Docket No. UT-950265, ELI filed a complaint against GTE for undue prejudice, discrimination, and unjust rates and practices in the provision of interconnection and mutual compensation.

11. On March 8, 1995, the Commission consolidated Docket Nos. UT-950146 and UT-950265 with Docket Nos. UT-941464 and UT-941465.

12. There is no essential difference between ALEC local traffic and incumbent LEC local traffic within a local calling area, including an EAS area.

13. USWC and GTE currently interconnect with one another and with other incumbent local exchange companies for the exchange of local traffic, including extended area service ("EAS") traffic. They employ a "bill and keep" method of compensating one another for the mutual traffic exchange. Both incumbents refuse to interconnect with ELI or TCG on the same basis, and both require that interconnecting ALECs pay minutes of use-based rates for local call termination.

14. For at least the present, ELI and TCG will establish local calling areas and rate centers conforming to existing USWC and GTE extended area service (EAS) and exchange boundaries.

15. The mutual compensation proposals of both USWC and GTE require the measurement and billing of terminating traffic between companies, which would require additional investment and expense and increase the cost of local exchange service.

16. The minutes of use-based rates proposed by USWC and GTE for terminating the local traffic of ALECs such as ELI and TCG do not properly reflect the structure of costs incurred to provide interconnection service; these costs generally do not vary with the level of traffic being exchanged.

17. The measured use regime proposed by USWC and GTE would undermine the state's public policy of affordable, flat-rated local service by reducing competitive pressure on the incumbents' flat-rated service, increasing the interconnection costs incurred by new entrants, and potentially raising the minimum rate at which incumbents could offer retail service.

18. The mutual traffic exchange or bill and keep compensation mechanism proposed by several parties would provide a simple method for interconnection and compensation for the termination of local exchange traffic.

19. The bill and keep method lacks cost-based price signals that should be included in any long-term compensation mechanism. It is appropriate as an interim mechanism.

20. The cost studies on which USWC bases its rate proposals use improper measures of economic cost and are accompanied by insufficient documentation to enable the Commission to conduct a fair review of the company's costs.

21. The record does not support the need for, or amount of, USWC's proposed interim universal service charge rate element. The record does not demonstrate that universal service in USWC's service territories will be adversely affected if the Commission

does not authorize USWC to collect a charge for the support of universal service in this proceeding.

22. Technically and economically efficient interconnection of incumbent local exchange company (LEC) and new entrant ALEC networks is essential to the development of a competitive local exchange market.

23. Physical interconnection between incumbent local exchange companies and ALECs does not involve any unique technological problems that the incumbent LECs do not face in interconnecting among themselves.

24. Currently USWC, GTE, and other incumbent local exchange companies use separate trunks for exchanging local (EAS) and toll traffic. This presently is a necessary arrangement for distinguishing between local and toll traffic.

25. Until such time as they build ubiquitous networks, new entrants into the switched local exchange service market require the ability to lease customer loops from the incumbent LEC in order to extend their geographical reach throughout a local calling area. The present unavailability, for lease, of incumbent local exchange companies' customer loops is a substantial impediment to the development of competition in the switched local exchange service market.

26. USWC soon will file an unbundled loop service tariff, which will make unbundled customer loops and line side interconnection available to ALECs for resale to end users.

27. The availability of true local service provider number portability is a necessary precondition for effective local service competition. However, true local service number portability is not presently available. USWC's proposed interim number portability measures are appropriate, as a temporary measure, if priced at cost.

28. A unified customer directory database is essential in a competitive switched local exchange service market if local service is to be seamless from the perspective of the consuming public. The lack of a single directory would be a substantial barrier to effective competition in the switched local exchange service market.

29. The complainants have not demonstrated that USWC or GTE will not provide 9-1-1, telecommunications device for the deaf ("TDD"), directory listing and assistance, and other necessary customer services upon interconnection at fair, just, and reasonable rates.

30. USWC's proposed rates for transport have relative price ratios between DS3 and DS1 transport components that are economically inefficient, would result in unfair competitive advantages for large IXCs, and would negatively affect competition to less urbanized parts of the state. An appropriate minimum DS3 to DS1 price ratio is based on