

PUBLIC VERSION

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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 In the Matter of)
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 Long-Term Telephone Number Portability)
 Tariff Filings)
)
 Ameritech Tariff F.C.C. No. 2,)
 Transmittal No. 1186)
)
 GTE System Telephone Companies Tariff)
 F.C.C. No. 1, Transmittal Nos. 1190, 1999)
)
 GTE Telephone Operating Companies)
 Tariff F.C.C. No. 1,)
 Transmittal Nos. 1190, 1999)
)
 Pacific Bell Tariff F.C.C. No. 128,)
 Transmittal No. 2029)
)
 Southwestern Bell Tariff F.C.C. No. 73,)
 Transmittal No. 2745)
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CC Docket No. 95-116
RM 8535

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FEDERAL COMMUNICATIONS COMMISSION
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AT&T CORP. OPPOSITION TO DIRECT CASES

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SUMMARY

The tariffs at issue in this investigation seek to establish LNP surcharge and query rates that are based not on the Commission's rules, but on the rules as the ILECs argue they should be. The bulk of the direct cases does not even attempt to carry the ILECs' burden of proof that their tariffs are lawful, but rather attack the requirements established by the LNP Cost Recovery Order and LNP Cost Classification Order. It is both unavailing and patently improper for the ILECs to contend in this proceeding that the Commission should amend its existing LNP cost recovery rules. Even if their claims were cognizable in this tariff investigation (as they are not), the very arguments they seek to offer here have already been considered and rejected by the Commission.

The direct cases confirm that all of the tariffs at issue seek to recover significant costs relating to OSS modifications that, by the ILECs' own admission, do not satisfy the two-part test established in the LNP Cost Classification Order. That order made clear that such costs were recoverable in LNP tariffs only if they (1) would not have been incurred by the carrier "but for" the implementation of number portability, and (2) were incurred "for the provision of" number portability service. Disregarding these unequivocal requirements, the ILECs seek to recover myriad costs that satisfy only the first prong of this test.

Ameritech, SWBT and Pacific devote much of their direct cases to attacking the Commission's ruling that ILECs may recover through their LNP tariffs only their incremental costs of implementing LNP. These claims are irrelevant to the instant proceeding, which may properly address only the ILECs' compliance with existing requirements, but are meritless in all events. Average cost models such as Ameritech's are a potentially reasonable approach when the prices of all the goods and services that utilize the inputs in question are taken into account.

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Ameritech and the SBC ILECs propose, however, to continue to charge their current rates for services other than LNP -- rates which permit them to recover the full costs of their existing systems and network -- while also recovering a portion of those same embedded costs via their LNP tariffs. The ILECs' tariffs make plain that their actual incremental expenditures are only a fraction of the expenses that their average cost methodologies would permit them to claim. Given that Ameritech, SWBT and Pacific have no intention of reducing their existing recoveries of their signaling costs, the only possible conclusion is that the figures derived from their cost models create additional recoveries without corresponding expenses.

The ILECs also ignore in other respects the Commission's mandate that they may recover only their incremental costs via their LNP tariffs. Ameritech, SWBT and Pacific seek to double recover their costs relating to land, buildings and maintenance, while the SBC ILECs continue to seek to recover embedded costs via their proposed overhead charges. In addition, SWBT and Pacific inflate their recoveries for generic software upgrades by seeking to recover expenses without regard to the "for the provision of portability" prong of the Commission's test.

Pacific and SWBT do not even attempt to address the Designation Order's concern that their tariffs fail to document the costs that are purportedly recovered through their nonrecurring charges. It is plain that the intent of these charges is not to allow the SBC ILECs to recover their incremental costs associated with performing certain queries (indeed, they have not documented that any such costs exist), but rather to force carriers to prearrange for query service. The SBC ILECs also have failed to abide by their previous statements that they would update their tariffs to allow carriers that prearrange for query services to avoid paying monthly non-recurring charges.

The Designation Order also instructed Pacific and SWBT to explain why it is necessary for them to charge for queries on calls to NXXs in which no number has ported. The SBC ILECs attempt to argue that they cannot open an NXX for portability during the five-day period following receipt of a First Usage Notification ("FUN") message from the NPAC/SMS. SWBT and Pacific fail to provide any evidence to support this claim, however. Contrary to the SBC ILECs' dire predictions, other carriers have been performing the translations at issue during this five-day window for over a year without experiencing any of the problems the direct cases assert Pacific and SWBT will face. The SBC ILECs also contend that it would be wasteful for them now to remove the routing translations from their switches and then re-input them when they receive a FUN. This argument is nothing more than a claim that SWBT and Pacific must be permitted to gain the full benefit of their attempt to unlawfully bill other carriers for wholly unnecessary query services. Just as N-1 carriers cannot reasonably be forced to pay the SBC ILECs' for the patently useless "service" of launching a query before the first number ports in an NXX, they likewise cannot reasonably be required to bear SWBT's and Pacific's costs to undo the network modifications that made that misguided scheme possible. In any case, the Commission need not require SWBT and Pacific to cease querying calls before the first number ports in an NXX, but should instead simply rule that they may not lawfully charge other carriers for such queries if they elect to perform them.

Ameritech and the SBC ILECs admit that they have failed to remove LNP-related charges and associated revenues from their intrastate investments and expenses. Because future intrastate rate cases may make use of historical investments and expenses and these ILECs' intrastate figures currently are overstated by virtue of their inclusion of LNP-related costs,

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Ameritech, SWBT and Pacific should make the appropriate accounting adjustments in order to improve the accuracy of their reported intrastate results.

The direct cases also reveal other errors. Although GTE's direct case purports to correct the inflation factors it initially applied in its tariff, the new factors it proposes also overstate its costs. Finally, the Commission should prohibit Ameritech's attempts to bill LNP surcharges to CMRS providers that utilize Type 1 interconnection trunks are unlawful, and rule that ILECs may not seek to impose such charges.

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CC Docket No. 95-116
RM 8535

AT&T CORP. OPPOSITION TO DIRECT CASES

Pursuant to the February 26, 1999 Order Designating Issues For Investigation

("Designation Order"),¹ AT&T Corp. ("AT&T") hereby opposes the direct cases filed by Ameritech, GTE Service Corporation ("GTE"), Southwestern Bell ("SWBT"), and Pacific Bell

¹ Order Designating Issues For Investigation, Long-Term Number Portability Tariff Filings, CC Docket No. 99-35 (released February 26, 1999) ("Designation Order").

("Pacific")² concerning the lawfulness of their long-term local number portability ("LNP") query service and LNP end-user surcharge tariff filings.³

I. THE ILECS' COLLATERAL ATTACKS ON THE COMMISSION'S LNP COST RECOVERY STANDARDS ARE IRRELEVANT TO THIS PROCEEDING

Much of the direct cases consist of nothing more than improper collateral attacks on the Commission's LNP cost recovery standards, and are simply irrelevant to the ILECs' efforts to carry their burden of proof under 47 U.S.C. § 204(a)(1). For example, the ILECs devote the majority of their direct cases' discussion of their purported OSS-related LNP costs not to demonstrating that their tariffs comply with the LNP Cost Recovery Order⁴ and LNP Cost Classification Order,⁵ but to attacking the two-part test established in those rulings. It is both unavailing and patently improper for the ILECs to seek to attack the Commission's rulings in this proceeding. Moreover, even if their claims were cognizable in this tariff investigation (as they are not), the very arguments they seek to offer here have already been considered and rejected by the Commission.

Although the ILECs' have sought reconsideration of the Commission's cost recovery rulings, it is black-letter law that the filing of a petition for reconsideration in no way

² SWBT and Pacific filed virtually identical direct cases, and are under common ownership. Accordingly, this opposition will at times refer to them collectively as "SBC."

³ Unless otherwise indicated, all citations are to the direct cases of the ILEC's that filed the tariffs at issue.

⁴ Third Report and Order, Telephone Number Portability, CC Docket No. 95-116, FCC 98-82 (released May 12, 1998), ¶ 75 ("LNP Cost Recovery Order").

⁵ Memorandum Opinion And Order, Telephone Number Portability Cost Classification Proceeding, CC Docket No. 95-116, RM 8535 (released December 14, 1998) ("LNP Cost Classification Order").

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relieves the petitioner of its obligation to comply with the rules that it challenges. Section 405(a) of the Communications Act provides that:

A petition for reconsideration must be filed within thirty days from the date upon which public notice is given of the order, decision, report, or action complained of. No such application shall excuse any person from complying with or obeying any order, decision, report, or action of the Commission, or operate in any manner to stay or postpone the enforcement thereof, without the special order of the Commission.⁶

This is the third LNP tariff investigation, and the third time the ILECs have sought to establish rates that are based not on the Commission's rules, but on the rules as the ILECs argue they should be. In this proceeding, the Commission should not hesitate to disregard the ILECs' attacks on the incremental costing principles established in the orders that govern these tariffs -- indeed, as a matter of law it is required to do so. The sole issue presented by this investigation is the straightforward question whether the ILECs' LNP tariffs comply with the Commission's cost recovery requirements. The instant tariffs fail this test in significant respects. Accordingly, the Commission should prescribe LNP surcharge and query rates in accordance with AT&T's showing below, and should order that the unlawful charges imposed to date be refunded with interest.⁷

⁶ 47 U.S.C. § 405 (emphasis added). Even if Commission were, in another proceeding, to reconsider its rules in response to a petition for reconsideration or application for review, those rule changes would not have retroactive effect. See, e.g., Bowen v. Georgetown Hosp., 488 U.S. 204 (1988). Accordingly, SBC, Ameritech, and GTE would be required to refund any amounts collected under their LNP tariffs that was inconsistent with the Commission's rules as of the time the charges were incurred.

⁷ Interest should be "computed on the basis of daily compounded interest using interest rates specified by the United States Internal Revenue Service." See, e.g., Errata, 1997 Annual Access Tariff Filings, CC Docket No. 97-149 (released December 15, 1997), ¶ 3.

II. THE ILECS' CLAIMED OSS COSTS VIOLATE THE COMMISSION'S LNP COST RECOVERY REQUIREMENTS

A. **The ILECs' Attacks On The Commission's OSS Recovery Standards Are Meritless**

The direct cases alternately attack the LNP Cost Classification Order's standards for recovery of OSS costs in LNP tariffs, or attempt to twist that ruling in a manner that ignores its plain language. As shown in Section I, such collateral attacks are simply irrelevant to this proceeding. But even if they were properly before the Commission at all (which they are not), the ILECs' arguments are meritless.

Ameritech adverts to its pending application for review of the LNP Cost Classification Order, and tries to suggest that the Common Carrier Bureau somehow created uncertainty as to the OSS costs ILECs could recover via LNP tariffs.⁸ But this is a vain effort to find ambiguity where none exists, as AT&T showed in its opposition to Ameritech's application, which AT&T hereby incorporates into this pleading by reference.⁹ The plain language of the Designation Order shows that the Commission's requirements for recovery of OSS costs in LNP tariffs are unclear only in the minds of the ILECs. That order described the governing standards as follows:

In the Cost Classification Order, the Common Carrier Bureau ... defined incremental OSS costs as the difference between the costs of the OSS upgrades without the number portability functionality and the total cost of the upgrades with the number portability functionality. Only the difference in costs is an eligible number portability cost. The Cost Classification Order directed the incumbent LECs to distinguish costs that fall under the narrow definition of

⁸ Ameritech, p. 23.

⁹ AT&T Corp. Opposition To Applications For Review, filed January 28, 1999 in Telephone Number Portability Cost Classification Proceeding, CC Docket No. 95-115, RM 8535.

number portability with respect to OSS from costs incurred to adapt other systems to implement number portability, such as repair and maintenance, billing or order processing systems.¹⁰

As the above-quoted passage makes plain, there is simply no merit to the ILECs' claims that the Commission intended to permit them to recover in LNP tariffs their costs to modify billing, ordering or other systems that are affected by LNP, but are not used to provide that capability. The LNP Cost Classification Order established a two-part test to determine whether a cost purportedly incurred by an ILEC is "directly related to the implementation and provision of telephone number portability," and therefore recoverable in LNP tariffs.

Under this test, to demonstrate that costs are eligible for recovery through the federal charges recovery mechanism, a carrier must show that these costs: (1) would not have been incurred by the carrier "but for" the implementation of number portability; and (2) were incurred "for the provision of" number portability service.¹¹

The LNP Cost Classification Order made plain that the "for the provision of" prong of its test would not permit ILECs to recover their costs to modify pre-ordering, ordering, maintenance and other systems that, while potentially affected by LNP, are not used to provide that service.¹² Indeed, the order expressly rejected the very argument that the direct cases seek to make in this proceeding.

Several LECs argue that all costs that would not have been incurred but for portability should be included as eligible LNP costs. In effect, these LECs would define "for the provision of portability" as including all costs related to any

¹⁰ Designation Order, ¶ 3 (footnotes omitted, emphasis added).

¹¹ LNP Cost Classification Order, ¶ 10.

¹² Number portability breaks the link between the first three digits of a customer's seven-digit telephone number (the "NXX") and the carrier that provides his or her local service. Once LNP is in place, customers in the same NXX can be served by different LECs, and carriers must modify their internal systems to account for this fact.

changes made necessary as a consequence of LNP. We disagree. In our view, the Commission adopted a very narrow definition of this phrase in the Third Report and Order, stating that the only eligible LNP costs are "costs carriers incur specifically in the provision of number portability services, such as for the querying of calls and the porting of telephone numbers from one carrier to another." The Commission specifically rejected the proposition that eligible LNP costs include all costs that carriers incur as an "incidental consequence of number portability." For this reason, in submitting their tariffs, we require LECs to distinguish clearly costs incurred for narrowly defined portability functions from costs incurred to adapt other systems to implement LNP, such as repair and maintenance, billing, or order processing systems.¹³

The order went on to make even clearer the types of OSS costs that are recoverable in LNP tariffs, and to reject the very argument the ILECs attempt to offer here.

We also interpret the phrase "porting telephone numbers from one carrier to another" narrowly, as referring only to the systems for uploading and downloading LRN information to and from the regional Number Portability Administration Centers (NPACs) and for transmitting porting orders between carriers. Because some carriers may argue that this phrase encompasses a myriad of changes to OSS systems affected by the porting of a telephone number, we again advise LECs to distinguish costs that fall under the narrower definition of this phrase and costs that might be encompassed in a broader interpretation of it in filing their federal tariffs.¹⁴

Despite these unequivocal rulings, GTE nevertheless attempts to argue that the LNP Cost Classification Order authorizes the inclusion in LNP tariffs of costs for OSS for pre-ordering, ordering, billing and other functions not used for "porting telephone numbers from one carrier to another." GTE points to the LNP Cost Classification Order's statement that "'the costs of number portability' are the costs of enabling telecommunications users to keep their telephone numbers without degradation of service when they switch carriers"¹⁵ and argues that this

¹³ LNP Cost Classification Order, ¶ 12 (footnotes omitted, emphasis added).

¹⁴ LNP Cost Classification Order, ¶ 14 (footnotes omitted, emphasis added).

¹⁵ LNP Cost Recovery Order, ¶ 36.

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standard means that it can recover the costs of modifying any system affected by LNP, so long as that modification relates to quality of service. GTE's direct case states that it

has sought to recover only those expenses associated with those specific systems enhancements that enable telecommunications users to keep their telephone numbers when they switch carriers without degradation of service.¹⁶

Ameritech attempts to make the same claim, arguing that its OSS modifications were necessary to avoid impacting "LNP service quality."¹⁷ These arguments are baseless.

The LNP Cost Classification Order expressly considered -- and unequivocally rejected -- precisely the claim GTE and Ameritech offer in their direct cases.

Some LECs have asserted that all of the Operations Support Systems (OSS) and other systems costs they have incurred as a result of LNP are "for the provision of number portability." Their claims are based on the assertion that in the First Report and Order, the Commission stated that no degradation in the quality of any aspect of service received by any customer should result from the implementation of LNP. The statements relied on by these LECs occurred in the context of the discussion of particular database query methods. Specifically, degradation of the quality of service was one of several factors considered by the industry, the NANC, and the Commission in selecting a LRN-based method of number portability over a Query-on-Demand method. Thus, in that context, the Commission stated that, as a general matter, any long-term number portability must "not result in unreasonable degradation in service quality or network reliability when implemented." We note that while the Commission recognized that "[c]onsumers, both business and residential, rely on the public switched telephone network for their livelihood, health and safety," it also expressly stated that the implementation of any long-term method should not unreasonably degrade existing service quality or network reliability. We do not interpret this performance criterion as authority for the proposition that all costs incidental to achieving that performance level are costs incurred "for the provision of portability." As noted above, we find that such a reading would render meaningless the language of the Third Report and Order regarding the definition of eligible LNP costs.¹⁸

¹⁶ GTE, p. 8.

¹⁷ Ameritech, p. 22.

¹⁸ LNP Cost Classification Order, ¶ 13 (footnotes omitted, second emphasis added).

Ameritech also argues that it should be able to recover all of the OSS costs it seeks because the Commission identified functions such as pre-ordering, ordering, billing and maintenance as OSS capabilities subject to unbundling under § 251(c).¹⁹ However, the fact that certain types of OSS must be made available to competitors as part of ILECs' obligations to open their monopoly local markets to competition in no way implies that those systems are used "for the provision of portability," and Ameritech offers no substantive argument to the contrary.

SBC suggests that it should be permitted to recover in its LNP tariff OSS costs that its software vendors stated were related to LNP.

Pacific Bell/Southwestern Bell is proposing to recover only its direct costs for vendor development in connections with Operational Support Systems ("OSS") that meet the criteria established by the commission. In each case, the expenses for a specific software package which was included for recovery through LNP rate elements was specified by the vendor to attributable solely to LNP.²⁰

This claim finds no support in the Commission's orders -- OSS costs are recoverable only when they satisfy the two-part test promulgated in the LNP Cost Classification Order. Moreover, even if it were proper for SBC to apply any other test (which it is not), an ILEC's vendor cannot be presumed to have any special knowledge as to how an ILEC will actually employ a particular piece of hardware or software. Vendors also have no particular knowledge of the Commission's LNP cost recovery requirements, and no duty of candor or truthfulness to the Commission concerning their bills. Further, a vendor would be faced with an obvious moral hazard, as it would have a strong incentive to please its ILEC customer by acceding to requests to "certify" an expense as LNP-related.

¹⁹ Ameritech, p. 22 n.19.

²⁰ Pacific, p. 2; SWBT, p. 2.

B. The ILECs Significantly Overstate The OSS Expenses They Claim Are Recoverable In Their LNP Tariffs

The specific OSS costs that the ILECs seek to recover in the instant tariffs are significantly overstated. For example, GTE states that to identify the costs of OSS modifications that it included in its calculations it

evaluated whether an end user could port a telephone number without the modification at issue and whether an end user whose service wire center is not LNP-capable could benefit from the modification. Only if the responses to both questions were negative was the cost given modification considered for inclusion.²¹

This plainly is not the two-part test established in the LNP Cost Classification Order. Using this approach, GTE can -- and does -- claim any OSS costs that would not have been incurred "but for" its implementation of LNP, without regard to whether the system in question is used for "the provision of" portability.

Attachment 3 to GTE's direct case is a table that purports to justify the OSS costs GTE claims are recoverable in its LNP tariffs. The five columns in this table include "How modifications relate to performing queries" (column B); "How modifications relate to porting numbers between carriers" (column C); and "How modifications relate to other number portability functions" (column D). Columns B and C are, of course, the only two types of costs that the Commission permits ILECs to recover via LNP tariffs. GTE, however, seeks to recover a wide range of OSS costs for functions that it frankly admits do not relate to performing queries or to porting numbers between carriers -- that is, OSS that simply have the label "N/A" in columns B and C of GTE's Attachment 3. GTE's attempt to include costs of

²¹ GTE, p. 7.

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OSS modifications that merely "relate to other portability functions" is flatly foreclosed by the Commission's orders. Any GTE OSS for which column B or C of GTE Attachment 3 is not populated is, a fortiori, not recoverable in its LNP tariffs. Further, the fact that GTE Attachment 3 breaks out the OSS it lists into the categories "service fulfillment," "service assurance," and "billing and usage" simply underscores the fact that it seeks to recover costs that do not remotely satisfy the Commission's requirements.

GTE attempts to justify Attachment 3's extravagant claims by citing paragraph 50 of the LNP Cost Classification Order, which held that recoverable LNP costs include "OSS modifications supporting other functions that the LEC claims are 'for the provision of portability.'" This argument finds no support in the text of the order. First, as shown above, both that order and the LNP Cost Recovery Order make plain that only the costs of performing queries or porting numbers may be recovered via LNP tariffs. Second, the LNP Cost Classification Order expressly anticipates GTE's claim -- and expressly rejects it, observing that

the definition of "for the provision of number portability" is likely to be an issue during review of the LNP tariffs. Several LECs argue that all costs that would not have been incurred but for portability should be included as eligible LNP costs. In effect, these LECs would define "for the provision of portability" as including all costs related to any changes made necessary as a consequence of LNP. We disagree. In our view, the Commission adopted a very narrow definition of this phrase in the Third Report and Order, stating that the only eligible LNP costs are "costs carriers incur specifically in the provision of number portability services, such as for the querying of calls and the porting of telephone numbers from one carrier to another."²²

Exhibit 1 to this opposition lists the improper OSS modifications that GTE seeks to recover in its LNP tariff, and explains why each claimed expense is impermissible.

²² LNP Cost Classification Order, ¶ 12.

Pacific and SWBT also seek to recover OSS costs that do not comply with the Commission's requirements. Attachment B to the SBC ILECs' direct cases gives their rationales for including their claimed investments and expenses. SBC's own explanations make plain that many of these costs are actually attributable to modifying systems to operate in an LNP-enabled environment, not "for the provision of portability," and are therefore not eligible for LNP cost recovery. Exhibit 2 to this opposition lists the improper OSS modifications that the SBC ILECs seek to recover in their LNP tariffs, and explains why each claimed expense is impermissible.

Similarly, Ameritech's Appendix C purports to describe the OSS modifications it made "for the provision of portability." Exhibit 3 to this opposition lists the improper OSS modifications that the Ameritech seeks to recover, and explains why each is impermissible.

III. THE SBC ILECS' AND AMERITECH'S TARIFFS SEEK TO DOUBLE-RECOVER THEIR EMBEDDED COSTS

The Designation Order directed Ameritech, Pacific, and SWBT to include in their direct cases

actual expenditures, including expenditures to date and planned actual expenditures within the recovery period, for the number portability costs which have been developed utilizing CCSCIS or SCIS. The companies must explain the basis of each calculation of actual expenditures.

Where Ameritech, Pacific, and SWBT intend to continue to rely on the information produced by the cost models in support of their tariffs, we further direct the LECs to explain how the use of cost models would produce more accurate estimates of the incremental costs generated by number portability than would be produced by an analysis of actual and planned expenditures. These LECs also must demonstrate that the use of the models does not produce double recovery of embedded costs already being recovered through other cost recovery mechanisms. This demonstration must also include, at a minimum, a comparison of the model's calculation of average costs of number portability-type queries and the model's incremental costs of these queries. The LECs also must demonstrate

their total network switching and signaling costs with and without long-term number portability, or explain why their models cannot do so.²³

All three ILECs devote the bulk of their discussion of this subject to arguing that the Commission erred in adopting an "incremental" approach to LNP cost recovery, and contend that it should instead permit "average" costing, which Ameritech, Pacific, and SWBT used in their tariffs in lieu of the methodology prescribed by the Commission's orders. Once again, as shown in Section I, the ILECs' attacks on the LNP cost recovery principles are utterly irrelevant to their efforts to carry their burden of proving that their tariffs comply with those requirements. But in all events, the arguments presented by Ameritech and the SBC ILECs' ultimately serve only to prove that their LNP tariffs would permit them to double recover significant portions of their claimed expenses.

A. Ameritech's LNP Tariff Would Permit Double Recovery

Rather than demonstrating that its models produce accurate estimates of its incremental costs, Ameritech spends the majority of its response attacking the incremental costing methodology adopted by the Commission. Indeed, even when it purports to calculate its "actual expenditures," Ameritech simply ignores the Commission's instruction that it base that determination on its costs with LNP versus its costs without that capability. Ameritech's direct case describes the process it used to calculate its purported SS7 costs as follows:

Ameritech began its analysis by performing an inventory of its SS7 network equipment and facilities related to the components [Service Switching Points ("SSPs"), Signal Transfer Points ("STPs") and links] measured by the models. Once these components were inventoried, they were divided into two categories -- 1) shared equipment and facilities, and 2) equipment and facilities dedicated to LNP. All investment costs associated with dedicated equipment were assigned to LNP. Investment costs associated with shared equipment were

²³ Designation Order, ¶¶ 19-20 (emphasis added).

allocated based upon relative capacity utilization to each service sharing the equipment and facilities.

Once forward-looking investment amounts were determined for each piece of equipment and facility, those amounts were multiplied by their respective quantities to determine the aggregate SS7 forward-looking investment for each shared component. The aggregate forward-looking investment for each shared component was then allocated to each service, including LNP....²⁴

In simple terms, Ameritech calculated its total SS7 costs and then divided those costs by the total number of octets transmitted on that system to determine its purported investment per octet. This investment per octet was then multiplied the total number of octets Ameritech claims are required for LNP in order to calculate its claimed LNP investments.

If all investments and costs varied directly with the number of octets processed, Ameritech's approach could potentially provide an adequate estimate of the incremental impact of the additional SS7 messages generated by LNP. And because this methodology mimics the methodology used in the CCSCIS model, it is scarcely surprising that Ameritech's results "justify" those obtained by the model. However as Ameritech's own calculations show, many of its claimed costs do not vary with the level of octets processed. Therefore, these fixed/joint investments made prior to implementation of LNP are embedded costs, and if included as incremental LNP costs, would result in double recovery.

The Designation Order correctly isolated the problem inherent in using LNP cost assignment cost models such as Ameritech's when it required the ILECs to provide information concerning "the total network switching and signaling costs with and without long-term number

²⁴ Ameritech, pp. 19-20.

portability."²⁵ Ameritech's Appendix B reveals why that ILEC prefers to dispute the wisdom of the Commission's decision to require incremental cost calculations rather than addressing the Designation Order's core concern. Schedule 3 of Appendix B shows that by assigning existing network infrastructure to LNP, Ameritech was able to claim ██████████ in LNP-related investments. However, Schedule 4 of Appendix B shows that Ameritech's actual incremental investments necessitated by LNP totaled less than ██████████. As Ameritech's own calculations show, the actual incremental costs within the SS7 network to carry queries is minimal compared to the numbers that the SCIS and CCSCIS models estimate.

In defense of its methodology, Ameritech resorts to collateral attacks on the Commission's orders, arguing that marginal cost calculations are not appropriate for LNP cost recovery. Ameritech contends that its affiant "conclusively demonstrates that the 'average' calculation is more appropriate since it more fully identifies costs that incumbent LECs will in fact incur as a result of LNP in the long run."²⁶ The shortest answer to this claim is that the Commission has already considered and rejected this argument. The LNP Cost Classification Order recognized that average cost methodologies would potentially allow ILECs to double recover embedded costs. To guard against such double recovery the order held:

[W]e agree with AT&T that only new costs can be claimed as eligible LNP costs. AT&T maintains that investments made by an incumbent LEC prior to LNP implementation cannot be considered direct costs incurred to provide number portability. AT&T states that an incumbent LEC's use of embedded facilities cannot give rise to costs directly related to LNP unless the incumbent LEC can show that the use of the facilities for the provision of LNP gave rise to new costs. Otherwise, AT&T argues, allowing incumbent LECs to claim embedded investments as eligible LNP costs would grant them double recovery. We agree.

²⁵ Designation Order, ¶ 20.

²⁶ Ameritech, p. 18.

We find it reasonable to bar recovery of costs incurred by LECs prior to LNP implementation and concur that permitting embedded investments to be eligible LNP costs would amount to double recovery through standard mechanisms.

Because, as discussed above, existing cost recovery mechanisms already provide for the recovery of embedded costs, we conclude that LECs may recover through the federal LNP charges only those costs that are demonstrably incremental costs LECs incur in the provision of long-term portability.²⁷

Thus, the LNP Cost Classification Order expressly considered and rejected the very arguments Ameritech offers here, and ruled that LNP costs should be calculated based on the incremental costs that would not have been incurred "but for" LNP and were required "for the provision of" LNP.

Ameritech also attacks the Commission's rules regarding the recovery period for LNP surcharges, contending that:

The imposition of a five-year recovery period makes it all the more important that estimates of LNP traffic costs be made on a long-run basis, so incumbent LECs at least recover all the investment they will have to make as a result of LNP volumes received during that period. Otherwise, costs caused by LNP in the long-run, after the recovery period would never be accounted for in the federal recovery mechanism.²⁸

A few pages later, Ameritech states:

The cost of replacing capacity sooner is a real cost that results from additional traffic caused by LNP. While the expenditure may not be made until after the recovery period, it is nonetheless a real cost caused by LNP during the recovery period.²⁹

²⁷ LNP Cost Classification Order, ¶¶ 18, 21 (footnotes omitted, emphasis added).

²⁸ Ameritech, p. 11 (emphasis added).

²⁹ Ameritech, p. 18.

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Ameritech thus seeks to justify its use of an average cost methodology by arguing that it is necessary in order to permit it to recoup costs it may incur after the five-year recovery period.

The LNP Cost Recovery Order explicitly ruled, however, that ILECs could recover in LNP tariffs only the incremental costs they incurred during the five-year recovery period.

Another issue that may arise in review of the LNP tariffs is the use of "annuities" to capture ongoing costs of providing LNP beyond the five-year recovery period provided for in the Third Report and Order. For example, Ameritech states that it plans to include as a LNP cost the present value of expenses related to LNP during the recovery period and continuing perpetually. Our reading of the Third Report and Order would preclude this approach. In our view, the Commission concluded in the Third Report and Order that, after the five-year recovery period, LNP would have become a normal network function and, thus, LECs would not be entitled to any further special recovery for costs incurred in implementing number portability. In addition, we note that standard rate-making principles prohibit the charging of future costs to current rate payers.³⁰

Although Ameritech complains that the principles established in the LNP Cost Classification Order assume that its rates are set pursuant to a rate of return-type scheme,³¹ in making that argument it never comes to grip with one fundamental -- and fatal -- fact. Ameritech's rates were initially set at a level intended to permit it to recover the costs of its existing network, including the embedded costs associated with the SS7 and other functions it now seeks to recover from LNP charges.

Average cost approaches such as Ameritech's are a potentially reasonable approach when the prices of all the goods and services that utilize the inputs in question are taken into account. If Ameritech's average cost-per-octet-utilized before LNP is X, and its average cost-per-octet-utilized after LNP is Y (where Y is a number less than X, because costs

³⁰ LNP Cost Recovery Order, ¶ 15.

³¹ See, e.g., Ameritech, p. 12.

are now spread over a greater number of octets), then all of the services that utilize SS7 signaling should become proportionally less costly to Ameritech on a per-unit basis, reflecting the decreased average unit cost of signaling. What Ameritech and SBC propose, however, is to continue to charge X per octet for non-LNP services, an amount that fully recovers their embedded costs for SS7 -- while also charging Y per octet for LNP, an amount that includes embedded costs as well.

Ameritech's argument incorrectly presumes that its current rates only allow it to recover for some fraction of its fixed/joint SS7 costs because there are available octets in its signaling network that are not currently being utilized. To the contrary, Ameritech today charges rates that are sufficient to compensate it for its initial investment in its SS7 capacity. (Ameritech has, of course, not suggested that it will lower any of the rates that it currently charges in order to avoid double recovery of the embedded costs it seeks to load onto LNP surcharges and query charges.) Contrary to Ameritech's contentions, the Commission's rules do not require ILECs simply to absorb the costs of LNP implementation. Rather, ILECs are required to estimate the new incremental costs they incur to implement portability and are allowed to recover those costs (plus an 11.25% cost of capital - a rate that far exceeds the rates that these companies would actually pay for access to funds in current markets).³²

³² It is, moreover, plain that there is no merit to Ameritech's unsupported claim that the Commission's approach to LNP cost recovery is "confiscatory." Ameritech, p. 14. The Supreme Court has made clear that a regulated utility can show a taking only by demonstrating that its rates are so low that they in fact "jeopardize the [company's] financial integrity." See, e.g., Duquesne Light Co. v. Barasch, 488 U.S. 299, 312 (1989). "So long as a [carrier] is not caused by [the challenged order] to lose money on its overall business" there can be no Fifth Amendment violation. Baltimore & Ohio R. Co. v. United States, 345 U.S. 146, 148 (1953). Whatever the effect of the LNP Cost Classification Order, it plainly does not rise to this level.

B. The SBC ILECs' LNP Tariffs Would Permit Double Recovery

The SBC ILECs' tariffs present substantively identical arguments -- and therefore are invalid for the same reasons -- as Ameritech's, Pacific's and SWBT's direct cases appear to ignore the Commission's request that they provide their actual expenditures that would not have been made "but for," and were made "for the provision of" LNP, and instead attack the Commission's cost recovery standards. SWBT and Pacific offer the following reasons why their actual expenditures on LNP purportedly cannot be appropriately compared with CCSCIS:

--"Actual expenditures do not reflect the advancement costs to bring forward the next relief job of the equipment due to the increased demand on the network caused by LNP. The CCSCIS model recognizes advancement costs for Signal Transfer Point (STP) routing functions and the database at the STPs. Only a portion of links and the LNP database equipment are represented in the actual expenditures even though all of the equipment is being advanced."

--"The actual expenditures do not reflect the advancement costs associated with secondary investments. These secondary investments are associated with the advancement costs of central office equipment and are developed through the application of supplemental factors."

--"These investments also do not reflect the LNP portion of the shared 'waiting to serve' capacity in the SS7 network. This capacity usage is produced in the 'average' view of the models."³³

The SBC ILECs further state that:

CCSCIS and SCIS develops [sic] forward looking costs based on the fact that increasing capacity utilization today triggers an advancement in network expenses.... Because the models identify the unit costs of each fundamental unit by octet, each service using octets for that piece of equipment will recognize the same cost.³⁴

³³ Pacific, p. 4; SWBT, p. 4. SWBT also states that it "included as actual expenditures costs for equipment used for billing" and network security. SWBT, p. 4. For the reasons given above, such expenses do not satisfy the LNP Cost Recovery Order's requirement that claimed expenses be used "for the provision of" LNP.

³⁴ Pacific, pp. 4-5; SWBT, p. 5.

Thus SBC, like Ameritech, has employed a model that calculates an average cost per octet, and attributes that average cost to LNP based upon the number of octets that portability is projected to utilize.

Attachment F to Pacific's and SWBT's direct cases demonstrate why this issue is critical in determining incremental LNP costs. SBC's own calculations show that the actual incremental cost within its SS7 networks to carry queries is minimal compared to the costs estimated by the SCIS and CCSCIS models. According to SBC's own calculations, the marginal costs and investments calculated through the use of the CCSCIS models are [REDACTED] of the average costs.³⁵ Like Ameritech, SBC's approach assigns the joint costs of end office switching and the SS7 network to all services based on an average cost per octet, ignoring the fact that these costs already are being recovered through other services. These joint costs are the embedded investments that the Commission expressly, and correctly, sought to exclude from LNP tariffs in order to avoid double recovery. SBC effectively admits that its investments and expenses will not increase in direct proportion to the number of octets required for LNP when it states that "LNP queries will use a significant portion of capacity of STPs. None of these STP costs, however, have been tracked since no construction jobs have been triggered yet."³⁶ In response to the Commission's request to compare costs with and without LNP, SBC provides still further evidence of this fact by admitting that "[b]ecause no specific adjustments attributable to

³⁵ It is important to note, however, that this comparison actually understates the amount of that SBC improperly seeks to double-recover. Although SBC compares the models' marginal and average results, marginal runs of SCIS and CCSCIS include some embedded investment, such as equipment in an STP or end office switch that was purchased prior to LNP implementation.

³⁶ Pacific, p. 5; SWBT, p. 5.

LNP were made to the SCIS model calculations, there was no discernable difference which could be drawn under this model on the basis of LNP."³⁷

SBC argues that because its models divide its total investment by total demand to estimate unit costs, double recovery cannot occur.³⁸ To the contrary, the most that SBC can possibly claim is that for any given run of the model, its costs will not be double counted. Average costs, however, are not necessarily reflective of prices, and price information is necessary to determine cost recovery using an average cost approach such as that advocated by Pacific and SWBT. [REDACTED]

[REDACTED]³⁹

Since the models do not take into account cost recovery [REDACTED] issues, SBC simply cannot use the models' cost methodology to prove that double recovery will not occur. The inclusion of fixed costs in the models causes unit costs to vary inversely with demand. Even under a price cap scenario, SBC has already priced its services to fully recover the fixed and joint costs of its SS7 equipment prior to its implementation of LNP. As quoted above, SBC admits it has incurred little or no new incremental STP costs. Given that SWBT and Pacific have no intention of reducing their existing recoveries of their signaling costs, the only possible conclusion is that the fixed costs figure derived from the SBC ILECs' models and included in their LNP cost recovery calculation create additional recoveries without corresponding expenses.

³⁷ Pacific, p. 7; SWBT, p. 8.

³⁸ Pacific, p. 5; SWBT, p. 5.

³⁹ [REDACTED]

SBC also contends that it should be permitted to increase its recoveries to account for the fact that implementation of LNP will cause it to make some investments earlier than it otherwise might have. The LNP Cost Classification Order expressly addressed this issue, and expressly rejected this argument.

Several commenters suggest that all costs related to advancing the deployment date of switches and software should be included as eligible number portability costs, even though the advanced deployments also benefit other services. We disagree. As we found in considering what portion of generic upgrades should be eligible LNP costs recoverable through the federal LNP charges, we do not agree that the entire costs of an "advancement" should be recovered as number portability costs, especially where those costs were incurred for software generics switch hardware, OSS, SS7 or AIN. Although the costs of planned upgrades may have been advanced by LNP requirements and LECs would not have deployed the upgrades early "but for" the Commission's portability implementation schedule, the associated upgrades provide general enhancements to the LECs' networks. As such, we find that only the incremental portion of such costs directly related to the provision of number portability may be recoverable as eligible LNP costs. Thus, LECs may claim only the advancement costs associated with the difference between the costs of the upgrade with the LNP functionality and its costs without that functionality. In such cases, LECs should provide evidence clearly demonstrating that the replacement or "advancement" is actually due to number portability and would not have occurred otherwise.⁴⁰

IV. AMERITECH AND THE SBC ILECS SEEK TO DOUBLE RECOVER THE COSTS OF LAND, BUILDINGS AND MAINTENANCE

Paragraph 21 of the Designation Order requires the ILECs to provide further information concerning their actual expenditures "for all land, buildings, administration, and maintenance expenses that are claimed."

Pacific and SWBT respond this instruction as follows:

SWBT has identified costs for equipment maintenance, building maintenance, support assets (administration) and ad valorem taxes through the application of annual cost factors to the capitalized investment for each type of equipment....⁴¹

⁴⁰ LNP Cost Classification Order, ¶ 30 (footnotes omitted, emphasis added).

⁴¹ SWBT, p. 8; see also Pacific, p. 9.

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The SBC ILECs stated that their maintenance factors were derived by multiplying their equipment maintenance factors by an operating expense inflation factor, and applying that figure to their claimed investments. The SBC ILECs do not indicate how they determined their building or land expenses.

The Designation Order requires the ILECs to "identify costs that were derived either from model output or an allocation factor applied to actual costs on the basis that new investment has an impact on overall requirements."⁴² This instruction makes clear that Pacific and SWBT may not simply apply a maintenance factor to the number of octets attributable to LNP multiplied by their claimed average cost per octet, but instead should identify the incremental maintenance costs created by LNP. Given that, as shown above, SBC's own attachments show that LNP will not require significant new investments, there can be little doubt that the corresponding maintenance expenses and charges for land and buildings are also overstated. While the use of a factor may be the most practical method for determining these projected costs, that factor should be applied only to those incremental investments that would not have been made "but for" and "for the provision of" LNP. Moreover, the SBC ILECs' attempt to use an inflationary factor simply ignores the fact that, due to productivity enhancements, the LECs' costs are decreasing year over year, as the Commission's use of an "X" factor in access tariffs recognizes.⁴³ If anything, the SBC ILECs' inflation factor should be replaced by a net factor that includes adjusts for the impact of productivity enhancements.

⁴² Designation Order, ¶ 21 (emphasis added).

⁴³ See Section X, below.

In support of its claimed costs of land, buildings, administration and maintenance, Ameritech states that it determined its building and floor space investments based on a "percentage loading associated with central office and call center investments," and calculated its maintenance expenses "as a percentage of capital investment."⁴⁴ For the reasons described above, Ameritech's use of average cost models for these expenses overstates its incremental investments associated with LNP. For example, Ameritech has provided no evidence that it made any new investments in buildings in order to provide LNP. It is reasonable to assume that Ameritech will incur some incremental maintenance expenses associated with LNP, and the use of a factor may provide the simplest method for estimating what those costs will be. However, such a factor should be applied only to incremental investments.

V. THE SBC ILECS SIGNIFICANTLY OVERSTATE THEIR CLAIMED OVERHEAD

Paragraph 21 of the Designation Order provides that:

To determine whether the allocation factors used by Pacific and SWBT include only the incremental overheads attributable to number portability, we direct Pacific and SWBT to provide their actual incremental overheads using an approach similar to the approach employed by Ameritech as described in the Cost Classification Order.⁴⁵

Pacific states that in order to calculate their overhead costs, the SBC ILECs utilized a shared and common costs study performed for the purposes of identifying the forward looking shared and common cost allocator for TELRICs. Each work group was examined to determine whether the work group was affected by the implementation of LNP. If the work groups' costs were included in the direct cost portion of the LNP study, the work group was excluded from the LNP incremental cost pool. If a work group was affected by the implementation of LNP and the work group's costs were not included in the direct cost portions of

⁴⁴ Ameritech, p. 28.

⁴⁵ Designation Order, ¶ 28 (emphasis added).

the LNP cost study, the work group's shared and common costs as identified in the study were included in the LNP incremental cost pool.⁴⁶

Once again, the SBC ILECs ignore the unambiguous mandate of the Commission that they cannot simply seek to recover an average of their costs, but must instead limit their recoveries to only those incremental costs created by LNP.

Paragraph 33 of the LNP Cost Classification Order held that

only new overhead costs are eligible for recovery through the federal charges mechanism; no allocation of embedded overheads is permitted. LECs must, therefore, demonstrate that any incremental overheads claimed are actually new costs incremental to and resulting from the provision of LNP.⁴⁷

The Designation Order made this point clearer still, ordering Pacific and SWBT "to provide their actual incremental overheads using an approach similar to the approach employed by Ameritech as described in the [LNP Cost Classification Order]."⁴⁸ The January 15, 1999 Ameritech tariff filing referenced in that order included a [REDACTED] overhead factor, which Ameritech stated that it derived by limiting its claims to new overhead costs that were incremental to LNP implementation. In stark contrast, despite repeated instructions to the contrary, the SBC ILECs simply divided the sum of all shared and common costs for organizations such as sales, accounting and finance, human resources and other general and administrative work groups by their claimed total direct costs.⁴⁹ Not surprisingly, Pacific and SWBT each develop an overhead factor that is [REDACTED] than that used by Ameritech.

⁴⁶ Pacific, pp. 9-10.

⁴⁷ LNP Cost Classification Order, ¶ 33.

⁴⁸ Designation Order, ¶ 28.

⁴⁹ See Pacific, p. 10.

VI. THE SBC ILECS FAIL TO JUSTIFY THEIR PROPOSED NONRECURRING CHARGES

The Designation Order directed Pacific and SWBT to provide significant additional information to attempt to justify their proposed non-recurring charges.

Based on a preliminary investigation of the tariff filings, we find that Pacific and SWBT have not provided adequate explanations or documentation to support a nonrecurring charge for their query services. Moreover, Pacific and SWBT's supporting documentation does not identify additional costs created by billing for default queries on a monthly basis. The monthly "nonrecurring" charge for default queries appears to be a recurring charge that Pacific and SWBT will impose for the purpose of encouraging companies to request prearranged queries, and not for the purpose of covering costs that result from providing default query services. We find that Pacific and SWBT's inclusion of a monthly "nonrecurring" charge for their query services raises substantial issues of lawfulness that warrant an investigation. We designate for investigation whether SWBT and Pacific's monthly "nonrecurring" query service charges are reasonable.⁵⁰

Despite this clear instruction, Pacific and SWBT do not even attempt to carry their burden of proof -- their direct cases nowhere address the Designation Order's concern that they have failed to document that they actually incur their purported nonrecurring costs in each month. Instead, the SBC ILECs argue that unless they are "permitted to recover the additional non-recurring costs incurred by carriers making default queries, these carriers have little incentive to act in an efficient manner."⁵¹ Clearly, the intent of these charges is not to allow the SBC ILECs to recover their incremental costs associated with performing certain queries (indeed, they have not documented that any such costs exist), but rather to force carriers to prearrange for query service. The SBC ILECs also have failed to abide by their previous statements that they would update

⁵⁰ Designation Order, ¶ 43.

⁵¹ Pacific, p. 16; SWBT, p. 16.