

Opinion."<sup>47</sup> He nevertheless recommended that certain NRCs be disallowed, and he proposed, as well, a tightening of the regime instituted in Phase 2 to preclude double recovery of NRCs. The latter issue is discussed first.

### Double Recovery

In an effort to ensure that the costs underlying the NRCs were not doubly recovered, New York Telephone, in its Phase 1 cost study, credited \$15 million of non-recurring revenues against the directly attributable joint expense portion of its carrying charge factors (CCFs). In its Phase 2 NRC presentation, it recognized that NRC revenues would likely exceed \$15 million, and it proposed to track those revenues and use the excess to reduce CCFs and the network element charges based on them. We found that remedy inadequate and directed New York Telephone to propose, in any future filing, a better method for avoiding double recovery. As an interim method, we applied \$10.9 million of forecast NRC revenues as a total offset to the ongoing OSS costs that would otherwise have been recoverable in Phase 2 and directed New York Telephone to apply any remaining revenues to mitigate, in a manner we would determine, future rate increases for network elements.<sup>48</sup>

In Phase 3, New York Telephone continued to favor its initial proposal to use NRC revenues in excess of \$15 million a year to recompute CCFs. Should we adhere to our Phase 2 decision, however, New York Telephone would agree that NRC revenues exceeding the \$15 million recognized in Phase 1 and the \$10.9 million already applied in Phase 2 should be used to mitigate future network element rate increases.<sup>49</sup> AT&T objected

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<sup>47</sup> R.D., pp. 49-50.

<sup>48</sup> Phase 2 Opinion, mimeo pp. 40-43.

<sup>49</sup> It regards this proposal as fulfilling its obligation to propose a better method for avoiding double recovery. (New

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to both solutions, contending that each would permit at least interim double recovery subject to later adjustment.

The Judge found that New York Telephone had failed to fulfill its obligation to propose a better method for avoiding double recovery. He therefore recommended that the decision in Phase 2 be reaffirmed and that, to protect against interim double recovery that might prejudice the CLECs, New York Telephone be permitted henceforth to hold less than 100% of the revenues being tracked. The remainder would be applied immediately as a temporary reduction to network element rates. All overpayments and underpayments by CLECs would be reconciled when we reached our final decision on double recovery, a matter that could be considered as part of the forthcoming plenary reexamination of element rates. The recommended decision assumed that New York Telephone would be permitted to hold 50% of the revenues at issue, but it suggested that the precise figure be determined only after New York Telephone had submitted, in its brief on exceptions, a report on the revenues tracked to date and forecast through 2001.

In its brief on exceptions, New York Telephone has submitted the required report on and forecast of revenues, noting that it is subject to change in the near future and that it omits information on collocation NRCs in view of the issues still to be resolved there. It agrees with the suggestion that the double recovery issue be finally resolved in the new proceeding and it does not appear to object in principle to the interim sharing proposal, presenting, instead, only a requested clarification and a suggestion for implementation.

Specifically, New York Telephone urges that the recommended decision be read to call for application of 50% of the non-recurring revenues on a year-by-year basis, rather than immediate use for rate reductions of 50% of projected NRC

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York Telephone's Brief on Exceptions, p. 26 n. 69.)

revenues through 2001. It suggests the latter reading would be unfair in view of the uncertainty of forecasts and the possibility that New York Telephone would be required to remit immediately revenues that it would not receive until later. It adds that any offset must take account of the amounts already applied in Phase 1 and Phase 2 as well as the possibility that projected NRC revenues may reflect a level of activity greater than the 1995 levels implicit in the CCFs, and it notes that annual NRC revenues are not expected to exceed the \$25.9 million a year already applied. Finally, it suggests that any rate reductions associated with the proposed remedy be applied to the local switching network element inasmuch as that rate remains temporary. In addition, a reduction to that rate would flow through to reciprocal compensation rates, thereby benefiting both network element purchasers and interconnectors.

AT&T responds that New York Telephone's objection to the recommended decision's method should be summarily rejected in view of its failure to respond to the directive to propose a better method for dealing with the double recovery issue.

The caption to this section of New York Telephone's brief on exceptions suggests a more forceful opposition to the suggestion than New York Telephone in fact mounts, and AT&T's response seems directed more at that caption than at what New York Telephone in fact says in the text of its brief. Be that as it may, New York Telephone does not seem to object to the sharing proposal, and it is adopted, along with New York Telephone's requested clarification, which properly applies the revenues year-by-year and does so only with respect to revenues in excess of those already applied.<sup>50</sup>

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<sup>50</sup> As a practical matter, this may vitiate the effect of the remedy, for annual forecast revenues are less than those already applied. But to construe the remedy contrary to New York Telephone's requested clarification would unfairly double count the revenues in favor of the CLECs.

Worktime Estimates

In Phase 2, we criticized New York Telephone's methods for estimating worktimes associated with NRCs and, in general, adjusted them downward by approximately 57%. That adjustment represented the average effect of applying, in each work function for which New York Telephone had conducted a task oriented costing (TOC) analysis, the minimum rather than the mean TOC data point. We applied this adjustment to the non-TOC studies as well.

In the current phase, New York Telephone did not use TOC studies and claims to have addressed our other criticisms of its Phase 2 method. Among other things, it submitted a statistical validation of its analyses performed by its consultant National Economic Research Associates (NERA). The Judge found that while the NERA analysis validated, as a matter of statistical theory, the worktime estimates to which it applied, it did not affect other worktime estimates, which continued to be based on only a small number of data points. Because of those deficiencies, similar to the ones that afflicted the Phase 2 worktime studies, the Judge recommended disallowance of the NRCs for line-port traffic study, OS/DA branding and unbranding, and network design request.<sup>51</sup> New York Telephone objects with regard to each of these items.

The network design request (NDR) process is required to establish a CLEC ODP in a New York Telephone switch; it includes worktimes needed for service delivery engineers to support the provisioning and development of the ODP. The concerns with respect to this item were centered on the uniformity of the

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<sup>51</sup> New York Telephone accurately notes that the NRC for LDC 45 was inadvertently included in both the allowed and disallowed lists at page 53 of the recommended decision. As made clear at page 61 of the recommended decision, the intention was to recommend its approval.

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responses provided by the five individuals who estimated worktimes for the service delivery engineer activity and the fact that there was only one individual who responded with regard to the worktime for the Market Area Center (MAC) activity.

On exceptions, New York Telephone renews its argument that only one individual performs the MAC activity within the company and that his actual experience provides, in effect, many observations or data points. As for the service delivery engineering function, it sees no cause for concern over the uniformity of the responses, noting that NDRs almost always require a type of work activity involving little or no variation and that it therefore makes sense that there be little or no variation in the estimated worktimes. It requests as well that if we adopt the recommendation to reject the worktime estimates, we allow a return to the time-and-materials based rate for NDR that New York Telephone had proposed before Phase 3. (In its post-hearing brief, New York Telephone attributed its abandonment of the time-and-materials based charge to the tendency of such charges to provoke billing disputes.)

Turning to the line port traffic study, New York Telephone asserts that the recommended decision does not specifically explain its concerns. It notes that it provided supporting data in an interrogatory response and that the five individuals who provided estimates had a total work experience of 93 years and total current job experience of 35 years.

Finally, with respect to branding/unbranding, New York Telephone asserts that the respondents for this item included five account managers, each of the three employees who handled translations for branding/unbranding, and one central office equipment installation manager.

With respect to all three items, AT&T's sole response is that New York Telephone's exceptions should be denied summarily, inasmuch as New York Telephone has done no more than restate its earlier arguments, contrary to the admonition in our

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rules of procedure regarding the proper content of exceptions.<sup>52</sup>

AT&T is correct; New York Telephone has shown no basis for rejecting the recommended decision's results on these items, and its exceptions are denied. Its alternative proposal to allow a time-and-materials based charge for NDR also is rejected, for New York Telephone is correct that a fixed charge for this item is preferable, and its own failure to present a suitably calculated fixed charge does not make a time-and-materials charge more acceptable.

#### OTHER SERVICES

##### SS7 Transport

New York Telephone's Phase 3 SS7 Transport cost study encompasses the cost of transporting an SS7 message required for the normal operation of other unbundled services purchased by the CLEC.<sup>53</sup> According to New York Telephone, the investment used in the study had been derived from the Bellcore common channel signalling cost information system (CCSCIS); on cross-examination by AT&T, however, it became apparent that the version of CCSCIS that had been provided to AT&T in discovery differed from the version New York Telephone claimed to have used in preparing its Phase 3 presentation.<sup>54</sup> AT&T therefore urged that the study be rejected entirely, inasmuch as it lacked evidentiary support on the record; New York Telephone responded that its error did not compromise AT&T's ability to understand CCSCIS and that, in any event, it could have been corrected in discovery had AT&T raised the issue earlier. The Judge recommended the following resolution of the issue:

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<sup>52</sup> 16 NYCRR §4.10(c)(2)(iv).

<sup>53</sup> SS7 refers to signalling system 7, a common-channel signalling system that is prerequisite to establishment of an integrated services digital network (ISDN).

<sup>54</sup> Tr. 5,987.

Cutting through the rhetoric on both sides, New York Telephone's view of this error's significance seems more on the mark than AT&T's, for the error did not really hamper one's ability to analyze the basis for New York Telephone's cost claims. No specific adjustment is warranted on this account. Still, errors such as these are disquieting, and parties should strive to avoid them.<sup>55</sup>

On exceptions, AT&T renews its claim that there is no record support whatsoever for New York Telephone's claimed SS7 costs, inasmuch as the record shows that New York Telephone relied solely on the electronic version of CCSCIS provided to AT&T in discovery and that that version of CCSCIS did not support New York Telephone's cost claims and did not correspond to the explanation of those costs in New York Telephone's work papers. It asserts that the recommendation understated the significance of New York Telephone's error and reflects "plain error of fact and law," for "AT&T successfully demonstrated on cross-examination that [New York Telephone's] sole claimed support for its Phase 3 claimed SS7 costs was bogus, [and] as a matter of law, that factual showing requires a finding that New York Telephone failed to sustain its burden of proof."<sup>56</sup> It suggests that allowing these costs "would effectively reward [New York Telephone's] incompetence, sloppiness, and arrogance" and that New York Telephone should be required to bear the full consequences of its evidentiary failures.<sup>57</sup>

New York Telephone responds by reiterating its earlier argument on the subject. It adds that the record, which shows no flaws in the CCSCIS method on which the SS7 cost studies were based, in fact supports its cost estimates, and it objects to

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<sup>55</sup> R.D., p. 64.

<sup>56</sup> AT&T's Brief on Exceptions, p. 8 (emphasis in original).

<sup>57</sup> Id.

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AT&T's effort "to turn a discovery error into a failure of proof."<sup>58</sup>

New York Telephone's arguments are well taken, and AT&T's exception is denied. AT&T's ability to analyze New York Telephone's cost claims was not impaired by the latter's slip-up.

#### AIN-Based Services

New York Telephone describes the advanced intelligent network (AIN) as "a service platform that utilizes the SS7 signalling network. It consists of a database that can intelligently route calls or provide other intelligent functionalities."<sup>59</sup> New York Telephone presented studies for several AIN related services: AIN trigger (i.e., the mechanism for querying the database), AIN message, AIN record storage, and AIN service creation.

As discussed above, the recommended decision called for disallowance of AIN service creation costs as cost onsets. On exceptions, AT&T maintains that AIN trigger costs should be similarly disallowed on the grounds that New York Telephone had never shown why they should not be classified in the same manner.

In addition, AT&T contends that the AIN message and record storage costs were based solely upon CCSCIS and therefore should be disallowed for the reasons described under the preceding heading. In sum, therefore, AT&T would disallow all AIN costs.

New York Telephone responds that no development costs are included in the AIN Trigger cost study and that AT&T has shown no basis for its proposed disallowances.

New York Telephone is correct on this point as well, and AT&T's exception is denied.

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<sup>58</sup> New York Telephone's Reply Brief on Exceptions, p. 4.

<sup>59</sup> New York Telephone's Initial Brief, p. 42.

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Operator Services and  
Directory Information Services

Among the various items considered in this category, the only one raised specifically on exceptions pertains to automated telephone listing address system (ATLAS) display of listings. New York Telephone there proposed a computer maintenance factor equal to 15% of computer system development costs. We used a 10% factor for analogous costs in Phase 2, finding New York Telephone's 15% proposal to be unsubstantiated, and New York Telephone here cited various studies that, in its view, supported the higher factor.

The Judge recommended retention of the 10% factor, agreeing with AT&T that New York Telephone had not established the pertinence and significance of the studies on which it was relying.

On exceptions, New York Telephone reiterates, without further explanation, its position that the documentation it submitted fully supports use of the 15% factor. AT&T responds that New York Telephone's statement is conclusory and unsupported.

AT&T is correct. There is no good basis for granting New York Telephone's exception, and it is denied.

MULTIPLEXING

As authorized by the Phase 2 Opinion, RCN raised various issues in Phase 3 regarding New York Telephone's rates for DS1 to DS0 demultiplexing (1/0 Muxing).<sup>60</sup> With regard to

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<sup>60</sup> Multiplexing is "the combining of two or more information channels onto a common transmission medium." (Federal Standard 1037C, Glossary of Telecommunication Terms, 1996.) Demultiplexing is the reversal of that process; that is, the separation of two or more channels previously multiplexed. DS0, DS1, and DS3 describe increasingly higher transmission rates for digital signals, requiring equipment of increasingly greater capacity. Movement to a higher rate is achieved by multiplexing; movement to a lower rate requires demultiplexing. "Muxing" can refer, depending on context, to

costing issues, the Judge recommended adjusting New York Telephone's proposed rates to reflect vendor discounts. New York Telephone does not except,<sup>61</sup> but the reply briefs on exceptions disclose a new costing issue related to loading factors. The other issues raised on exceptions relate to rate structure; they are discussed first.

#### Rate Structure

New York Telephone proposed to charge a CLEC requesting 1/0 Muxing for certain common equipment, such as a multiplexing shelf and common plug-ins, as well as for the cost of 24 channel units that terminate individual low-speed lines. RCN proposed an alternative, under which CLECs taking 1/0 Muxing service would pay a base monthly rate for the channel bank and separate monthly rates for each voice and data channel unit requested. In that way, RCN contended, a CLEC would pay only for the functionality it actually used.

New York Telephone did not object in principle to a rate structure based on the provision of channel unit functionalities on demand, but it contended that RCN's specific proposal failed to insure recovery of certain costs, among them, inventory management. It therefore proposed a monthly inventory management charge, intended to cover the costs and risks associated with matching capacity with demand and maintaining an inventory of channel units sufficient to meet CLECs' orders.<sup>62</sup> At the exceptions stage, the principal issue is how the inventory management risk should be shared between New York Telephone and the CLEC.

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either multiplexing or demultiplexing.

<sup>61</sup> New York Telephone's Brief on Exceptions, p. 28.

<sup>62</sup> New York Telephone also questioned whether RCN's proposal permitted it to recover nonrecurring service order and central office wiring costs. While RCN initially opposed the associated charges as redundant, neither party excepts to the

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RCN objected to the inventory management charge on the grounds that New York Telephone already had in place an inventory management control system (the plug-in inventory control system or "PICS") used to provide multiplexing to itself on demand, and that it recovers the costs of PICS either through TELRIC-based multiplexing rates or via the CCF for directly attributable joint costs. In New York Telephone's view, however, the costs, even if included in the CCFs, would not be fully recovered if the CCFs were applied only to a portion of the investment in a fully equipped multiplexer, and a CLEC that ordered only 12 channel banks (instead of the full complement of 24) would pay only a portion of the expense. RCN rejoined that CCFs are set to recover expenses associated with each unit of investment to which they are applied and that New York Telephone would recover the proper amount of PICS costs associated with each channel unit whenever it applied the CCF to the price paid for the unit.

The Judge was persuaded by New York Telephone's assessment of RCN's pricing proposal and found that:

under RCN's method, the cost of an incremental channel bank would be determined by dividing a fixed cost (including PICS) by the estimated number of channel banks to be sold. If that estimate proved too high, New York Telephone would not recover all of its costs; and the pertinent question thus becomes whether that risk is one that New York Telephone, in fairness, should bear.<sup>63</sup>

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recommended decision's conclusion, on the basis of further argument, that New York Telephone had reasonably supported the need for wiring and service order charges in the multi-connection collocation context posited in its presentation but that such charges should not be imposed in the direct connection, noncollocation context that RCN was interested in. (That context is referred to as the Enhanced Extended Link, or EEL.)

<sup>63</sup> R.D., pp. 82-83.

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The Judge went on to suggest that the risk should be shared between the parties, given that the forecast was New York Telephone's but that the novelty of the situation limited New York Telephone's ability to forecast accurately, and he requested the parties to consider possible risk sharing methods in their briefs on exceptions. Each has done so.

As a threshold matter, RCN notes that although its proposal focuses on Muxing in the EEL context, the same rate structure arguments apply elsewhere as well, in that CLECs should pay only for the number of channels they actually use. New York Telephone, meanwhile, states that issues related to the EEL context, including the costing issues referred to earlier and this rate design issue, should be considered, as the recommended decision suggested, not in this proceeding but in the review of New York Telephone's July 23, 1998 EEL tariff filing. It therefore responds to RCN's rate design proposal only to the extent it would be applied in the non-EEL context as well.<sup>64</sup>

With respect to this issue, RCN proposes that whenever a CLEC purchases an EEL that requires a new multiplexing channel bank to be set up, it pay at the outset 50% of the total PICS costs associated with applying the CCFs to a multiplexer fully equipped with voice grade channel units. As CLECs purchase individual channel units, New York Telephone would collect PICS costs through the CCF, subject to a cap equal to 100% of the PICS costs associated with the fully equipped channel bank. RCN asserts that its risk sharing method guarantees that New York Telephone would recover more than half of its PICS costs at the outset (since the CLEC would pay 50% of the cost plus the cost associated with at least one channel bank) and recover the remainder of its costs rapidly, reaching the total by the time the CLEC purchases approximately half of the channel units.

New York Telephone responds that the proposal deals

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<sup>64</sup> New York Telephone's Reply Brief on Exceptions, p. 5.

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only with the expense of inventory management, ignoring the investment in additional channel banks that would have to be maintained; and it questions RCN's premise that all channel units would be voice rather than data grade. In addition, it says RCN's proposal would require it to develop a new tracking system to determine how many channel units are deployed in each multiplexer.

New York Telephone's own proposal starts from the premise that the average channel unit utilization for a 1/0 multiplexer is 60% and that the inventory level maintained for the relevant equipment is 2%. It therefore proposes an inventory charge of 2% of 40% of the total cost of 24 channel units (in the most frequently encountered array of 18 analog and 6 digital), resulting in monthly charges of \$151.97 (common), \$10.42 per analog channel unit, and \$15.14 per digital channel unit. New York Telephone notes that its 60% utilization figure is based on current retail utilization and that it bears the risk that wholesale utilization would be lower. It adds as well that while it accepts these arrangements as a pricing concept, it is not certain how soon they could be made operationally available.

RCN responds that New York Telephone, by proposing a separate charge for inventory management functions, would recover a second time the PICS costs already recovered through the CCF. It charges New York Telephone with ignoring the recommended decision's determination that the CCF recovers the cost of the PICS that performs the inventory management functions at issue here.

Each party has raised fair criticisms of the other's proposal. RCN's plan, it appears, could leave unrecovered some needed inventory investment and appears administratively burdensome. New York Telephone's plan, meanwhile, fails to preclude double recovery of PICS expense. To resolve this issue as promptly and efficiently as possible, Staff should immediately convene a technical conference of the parties to further examine

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and compare the two proposals, with an eye to resolving the matter in the context of New York Telephone's Phase 3 compliance filing. Until then, the rates for 1/0 Muxing, already considerably lower than those proposed by New York Telephone (in view of the recommendation on vendor discounts, next discussed) will be kept temporary.

### Costing

New York Telephone included in its brief on exceptions a detailed presentation of its inventory risk sharing proposal. In its reply brief on exceptions, it reports that counsel for RCN had observed to it that various loading factors in that presentation differed from those that had been used in the original, Phase 2, 1/0 Muxing study. It explains that it had applied the loading factors used in its other Phase 3 studies, derived as set forth in the Phase 3 workpapers. In particular, it explains that the new circuit engineering and installation factor, which is higher than that used in the original study, reflects actual 1995 data rather than the estimates used in Phase 1.<sup>65</sup>

In its own reply brief on exceptions, RCN excepts strenuously to the revised loading factors, noting that their effect is to substantially attenuate the reduction in the 1/0 Muxing charge that otherwise would have resulted from New York Telephone's recalculation of the charge, consistent with the recommended decision, to impute vendor discounts. RCN goes on to recount the genesis of the Phase 3 consideration of multiplexing, recalling its concern that the Phase 2 multiplexing study had produced a charge for 1/0 Muxing, in which most CLECs were interested, far in excess of the rate for DS3 to DS1 (3/1) Muxing

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<sup>65</sup> New York Telephone suggests in this regard that the substitution of actual for estimated data for a given year should not be regarded as an update. (New York Telephone's Reply Brief on Exceptions, p. 7, n. 16.)

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that had been set in Phase 1, even though historically the relationship between those rates had been the opposite. In response to an inquiry in the Phase 2 recommended decision, New York Telephone attributed the difference to vendor material prices, over which it had no control--which led to the consideration of vendor prices in Phase 3--and suggested the loading factors for 3/1 and 1/0 Muxing were the same. RCN accordingly objects to substitution of the Phase 3 loading factors with respect to 1/0 Muxing, seeing no reason to now use different loading factors for the two forms. It adds that New York Telephone, which has the burden of proof, made no effort to justify the different loading factors; did not disclose its intention to use the new loading factors until it filed its brief on exceptions; and raised no objection to the use of the original loading factors in the cost calculations set forth in RCN's direct testimony.

New York Telephone's proposal to change the loading factors at this stage of the game is procedurally improper for all the reasons RCN suggests and may be substantively improper as well if done selectively, as New York Telephone appears to advocate.<sup>66</sup> The multiplexing costs should be recalculated on the basis of the original loading factors.

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<sup>66</sup> Whether the change is technically an "update" is of little consequence; but to change the loading factor to rely on actual rather than estimated data seems no different for these purposes.

COLLOCATION

Introduction

Collocation refers generally to the placement of a CLEC's equipment in an ILEC's central office building for the purpose of interconnection and access to unbundled network elements. In "physical collocation," the ILEC makes space available in its central office building to a CLEC for placement of the necessary equipment and provides CLEC personnel access to the equipment. An alternative is "virtual collocation," which permits a CLEC

"to place transmission equipment in relay racks in the same area as similar equipment as owned by [the ILEC] for the purpose of accessing unbundled network elements and for interconnection. . . . The Virtual Collocation equipment is purchased by the CLEC and installed in a relay rack located among [the ILEC's] own digital circuit (toll type) equipment. The collocator transfers ownership of the equipment to [the ILEC] for \$1. [The ILEC] maintains the equipment at the direction of the collocator."<sup>67</sup>

Section 251(c)(6) of the Telecommunications Act of 1996 requires an ILEC to make both physical and virtual collocation arrangements available to requesting telecommunications carriers on rates, terms, and conditions that are just, reasonable, and non-discriminatory.<sup>68</sup>

Collocation costs were the subject of initial presentations by both New York Telephone and AT&T/MCI. The presentations in some ways echoed those submitted with regard to

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<sup>67</sup> Tr. 6,209.

<sup>68</sup> More precisely, the statutory provision requires that physical collocation be made available but permits the provision of virtual collocation instead "if the local exchange carrier demonstrates to the State commission that physical collocation is not practical for technical reasons or because of space limitations."

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network elements generally in Phase 1; once again, New York Telephone submitted a company-specific study that was attacked for its excessive reliance on historical, allegedly embedded costs, while AT&T/MCI submitted a generalized Model that was attacked, like their Phase 1 Hatfield Model, for its allegedly tenuous connection to reality.

In general, the Judge recommended using the AT&T/MCI Model as the starting point for determining collocation costs, but he recommended various adjustments to that Model's inputs, having found New York Telephone's position with regard to those inputs more persuasive. He recommended as well that we revisit our decision, in orders issued with respect to non-pricing collocation matters,<sup>69</sup> that New York Telephone in general be allowed to recover actual collocation room conditioning costs on an individual case basis (ICB); he proposed, instead, that such costs, like others, be estimated on a TELRIC basis and recovered through fixed-per-square-foot rates. New York Telephone regards that recommendation as "the most significant error in the [recommended decision]"<sup>70</sup> and devotes much of its brief on exceptions to that issue and to others involving the premise that costs should be determined on the basis of a hypothetical central office. The principal (but not the sole) issue raised by AT&T/MCI is the recommendation to adopt certain power costs proposed by New York Telephone.

The recommended decision included an overview of the parties' presentations; we need not reiterate it here. There

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<sup>69</sup> We decided the non-rate issues, following the submission of written comments and a collaborative process, in orders issued last year. (Cases 95-C-0657 et al., Order Directing Tariff Changes for Non-Price Terms and Conditions for Collocation (issued March 2, 1998) (the March 2 Order); Order Adopting the March 2, 1998 Order as a Permanent Rule and Denying Petitions for Rehearing (issued May 29, 1998) (together referred to as the Non-Price Collocation Orders).)

<sup>70</sup> New York Telephone's Brief on Exceptions, p. 1.

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followed a description of the parties' general criticisms of each other's presentations and defenses of their own, along with a discussion of these general issues and the basis for the recommendation to adopt the AT&T/MCI Model as the point of departure. These general issues remain important and will be referred to to the extent necessary in the context of the parties' specific exceptions. We note at the outset, however, that New York Telephone continues to object in general terms to an approach for recovering collocation costs that is based, in its words,

on the costs of building a brand new, imaginary central office. Within that imaginary central office is a perfectly sized and conditioned collocation room, which is magically placed close to [New York Telephone's] frames and in an ideal location so that collocators are not permitted unfettered access to [New York Telephone's] central offices. The Model then determines how much it would cost to create such an imaginary central office on a per square foot basis. Under the Model, [New York Telephone] only recovers the costs from the collocators associated with the square footage of central office space used by their collocation cages, not all of the costs of building this brand new office. Thus, instead of recovering the costs to build a collocation room dedicated to the collocators using [New York Telephone's] existing central offices, [New York Telephone] only recovers the collocators' portion of the hypothetical costs associated with building this imaginary central office.<sup>71</sup>

AT&T/MCI, of course, take a very different view of their approach; the matter is considered further in the following section.

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<sup>71</sup> Ibid., p. 2.

Room Construction Costs

1. Background

The special construction costs at issue here are those incurred to condition or otherwise prepare for collocation use central office space that is not already suitable for that use. They are to be distinguished from the costs of constructing collocation cages themselves, treated separately, as well as from the per-square-foot charges proposed by New York Telephone with respect to ongoing building-related costs.

In the Non-Price Collocation Orders, we determined that New York Telephone would be required to pay all special construction costs except for the initial collocators' proportionate share. The balance of the construction costs would be amortized by New York Telephone over a period to be determined in cooperation with Staff and would be recovered, with interest, from all physical collocators within a defined geographic area. In the event New York Telephone later found it had to use some of the conditioned space for its own purposes, it would be required to pay its proportionate share of the cost, as if it were itself a collocator. In explaining that decision, we noted that "the need for special construction is likely to become more prevalent.

Special construction will be a significant, routine cost for all [collocators] and should thus be part of the basic floor-space rate."<sup>72</sup> In New York Telephone's view, that decision authorizes it to recover actual room construction costs and to measure those costs on an individual case basis, inasmuch as each central office requires unique preparation.

In proposing that we revisit this decision, the recommended decision suggested that it be seen as the logical outgrowth of the Commission's long-standing effort, predating the 1996 Act, to encourage New York Telephone to make collocation available; consistent with that effort, our policies insured New

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<sup>72</sup> March 2 Order, p. 11.

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York Telephone recovery of its construction costs, measured on an individual case basis. But the Judge suggested further that more recent law and practice--including the requirement that collocation be offered; the availability of entry into the long-distance market for Bell ILECs that meet the applicable requirements; the use in these proceedings of forward-looking TELRIC-based pricing for elements and interconnection; and the inconsistency, in general, of ICB pricing with a forward-looking construct--might make it reasonable to modify that decision and, instead, estimate room construction costs, like all other network element and collocation costs, on a TELRIC basis and reflect them in standard collocation fees.

2. Arguments

New York Telephone objects to that recommendation on a variety of grounds.<sup>73</sup> Citing not only the Non-Price Collocation Orders but also our earlier statement that collocation conditioning costs should be studied case-by-case,<sup>74</sup> New York Telephone contends that the second of the Non-Price Collocation Orders rejected the argument, there raised by CLECs and now referred to in the recommended decision, that allowing it to recover all room construction costs was inconsistent with a forward-looking costing method. In its view, the recommended decision simply disagrees with our previous determination. New York Telephone notes as well that the approved cost recovery method is incorporated in its April 6, 1998 prefiling statement in Case 97-C-0271, and it points to a determination by the Florida Commission that costs should be determined on a case-by-case basis. Disputing AT&T/MCI's effort to analogize its proposal to a landlord charging both a market rental rate and a property renovation charge, New York Telephone observes that the collocation rate does not reflect the market value of the property; that many tenants do in fact pay for renovations; and that it lacks the option, available to landlords, of declining to renovate the property if rental rates cannot recover the costs.

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<sup>73</sup> The immediate question here is whether to allow actual costs on an individual case basis (ICB) or to require use of a uniform price set on the basis of estimates; in principle, that issue is distinct from whether those estimates should be based on TELRIC hypotheticals or on some other costing method, perhaps one based on the network New York Telephone actually has in place. Nevertheless, the parties' disagreement over costing method is played out in large part on the stage set by this issue (perhaps because the recommended decision also linked the issues, noting that ICB pass-throughs of actual costs compromised TELRIC principles), and their arguments regarding costing method, though having implications going beyond this issue, are presented and discussed here as well.

<sup>74</sup> Cases 29469 et al., Order Regarding OTIS II Compliance Filing (issued May 8, 1991).

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Turning to forward-looking costing principles, New York Telephone contends they are fully served by allowing the construction costs it will actually incur on a going-forward basis to provide collocation. The costs adopted in the recommended decision, in contrast, reflecting those of a hypothetical central office, "are not forward looking; they are based on science fiction."<sup>75</sup> New York Telephone notes in this regard the provisions of our costing manuals that warn against speculative or hypothetical scenarios as well as our statement in Phase 1 that a TELRIC analysis, though assuming that a least-cost, most-efficient network is dropped into place, "does not mean that the method requires consideration of 'fantasy networks' or 'speculative future innovations'; it requires primarily that the hypothetical network design assume full deployment of the most efficient technology currently (or very soon to be) available."<sup>76</sup> The imaginary central office configuration contemplated in the recommended decision will never be deployed, it says, and it will continue to provide collocation using its existing central offices. Even the FCC's pricing rules, it adds, contemplated that "costs ... be based on the incumbent LEC's existing wire center locations and most efficient technology available,"<sup>77</sup> and it argues that reliance instead on a hypothetical wire center in a fantasy network contradicts the FCC's reference to existing wire centers. It cites as well various FCC decisions that, it says, consistently rule that ILECs are entitled to recover all collocation construction costs.

New York Telephone further maintains that the

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<sup>75</sup> New York Telephone's Brief on Exceptions, p. 5.

<sup>76</sup> Phase 1 Rehearing Opinion, mimeo pp. 4-5, cited at New York Telephone's Brief on Exceptions, pp. 5-6 (emphasis added by New York Telephone).

<sup>77</sup> First Report and Order, ¶690 (emphasis added by New York Telephone).

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recommended decision would deny it recovery of costs it is obliged to incur, while, at the same time, permitting collocators to avoid the ordinary business costs associated with their voluntary decisions to become facilities-based competitors rather than resellers and to use physical rather than virtual collocation or other alternatives. Such pricing arrangements, it argues, contradict the requirements of the Public Service Law and the 1996 Act that collocation rates be just and reasonable. It warns of providing CLECs an incentive to over-collocate and then simply vacate a central office that proved unprofitable to serve.

Citing the Eighth Circuit's recognition that carriers electing facilities-based competition rather than resale face the risk of having to make a substantial upfront investment, large enough to pay the cost of acquiring access to unbundled elements, it asserts that collocation room conditioning costs are part of that upfront investment. Further, New York Telephone maintains that requiring it to permit collocation on its premises while denying it the ability to recover the costs it thereby incurs would constitute an unconstitutional taking of property. It suggests that the provision of the 1996 Act requiring that physical collocation be provided on rates, terms, and conditions that are "just, reasonable, and non-discriminatory" was inserted in response to a court decision warning that requiring ILECs to provide physical collocation might constitute an unlawful taking in violation of the Fifth Amendment.<sup>78</sup>

Finally, New York Telephone requests that it be authorized, in the event we do reverse the earlier decisions regarding room construction costs, to present evidence regarding the appropriate rate to be adopted. It asks, for example, to be allowed to present evidence that the analysis should be based on a collocation room, not on an entire central office, and that the

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<sup>78</sup> New York Telephone's Brief on Exceptions, p. 9, citing Bell Atlantic Telephone Company v FCC, 24 F.3rd 1441 (D.C. Cir. 1994).

cost of preparing the room should be borne entirely by collocators. It would also question the building costs used in the AT&T/MCI Model; it explains that in the hearings thus far conducted, it did not present its own evidence on building costs because it believed the issue had already been resolved in the Non-Price Collocation Orders.<sup>79</sup>

AT&T/MCI respond that New York Telephone, ignoring the record evidence that its existing central offices are not configured on a forward-looking best-practices basis to accommodate collocation, is simply calling on us to reject a TELRIC-based best practices analysis in favor of a monopoly regime "under which [New York Telephone] gets paid no matter what its costs are and no matter how inefficiently [it] provides collocation to its competitors."<sup>80</sup> According to AT&T/MCI, a hypothetical network, far from being improper because of any failure to reflect contemporary reality, must be relied on because New York Telephone's existing central offices are not designed to accommodate multi-carrier interconnections. AT&T/MCI go on to explain their view that by adopting their approach, the recommended decision properly simulated the costs that would be incurred for collocation in an efficient competitive market. They cite in this regard their Model's assumption that collocation occurs in pockets of existing available space; its reliance on average connectivity lengths, which minimizes the potential for costly collocation areas to be created in remote locations and insures that New York Telephone applies the same space planning strategies to collocation as it does to placement of its own equipment; its expectation that all central office resources will be shared on a non-discriminatory basis by all

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<sup>79</sup> New York Telephone states that the evidence and responsive evidence could be dealt with in writing alone and that no evidentiary hearing would be warranted.

<sup>80</sup> AT&T/MCI's Reply Brief on Exceptions, p. 4.

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users; and its allowance for each cost element that a CLEC may incur for collocation, with no hidden charges.

AT&T/MCI disparage as well New York Telephone's claims that the recommended pricing construct is unlawful, regarding them as mere reiterations of claims made earlier, before the Phase 3 evidentiary record was compiled. They stress the FCC's endorsement of a TELRIC-based forward-looking costing method and its statement that such a method satisfies constitutional requirements. The FCC's reference to existing wire center locations, emphasized by New York Telephone and relied on in our Phase 1 network construct, is irrelevant to collocation, in their view, inasmuch as central office location is not the issue, and the Phase 3 evidence shows that New York Telephone's central office configurations do not reflect forward-looking best-practices for collocation.

In response to New York Telephone's claim that we already have decided the issue, AT&T/MCI stress the fact that the earlier determinations were rendered before the creation of the Phase 3 evidentiary record on collocation costs and were reached, as suggested in the recommended decision, as an outgrowth of our pre-1996 Act effort to make collocation available. AT&T/MCI point out that our present consideration of the issue is our first opportunity to do so on the basis of the Phase 3 evidentiary record developed pursuant to the 1996 Act.

Finally, AT&T/MCI characterize as "patently absurd"<sup>81</sup> New York Telephone's request that it be permitted to present new evidence on collocation costs. They note that New York Telephone had a full opportunity to present evidence and argument in Phase 3 and urge that it be required to "bear the consequences of its failed litigation strategies" and be denied any opportunity to put on an entirely new case now.<sup>82</sup>

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<sup>81</sup> Ibid., p. 11.

<sup>82</sup> Ibid., p. 12. AT&T/MCI vigorously dispute New York

In their own exceptions, AT&T/MCI focus on the recommended decision's observation that instead of being recovered on an individual case basis, construction costs should be estimated on a TELRIC basis and reflected in standard collocation fees. Apparently taking that as an implication that construction costs are not now adequately reflected in the AT&T/MCI Model, they contend that because the Model contemplates an entirely new central office building, it already incorporates all necessary forward-looking room construction costs. The costs are now included as part of the cage preparation charges developed by the Model; AT&T/MCI express their willingness to reorganize the Model so that they could be separately identified or to incorporate any costs that might be identified in future cases as having been inadvertently omitted.

### 3. Discussion

As already suggested, New York Telephone excepts to the recommended decision's treatment of this issue on two distinct, conceptually unrelated, grounds: it opposes any effort to estimate room construction costs for purposes of computing a uniform charge, favoring, instead, ICB pass through of actual room construction costs; and it objects in particular to use of the TELRIC method to estimate those costs (if they are to be estimated at all).

Turning first to costing method, the Judge explained in some detail why he favored reliance on the AT&T/MCI Model as the starting point for analysis and why the success of a TELRIC analysis did not depend on its ability to insure full recovery of actual costs, something New York Telephone seems to continue to regard as essential. He noted, among other things, that "the purposes of a TELRIC analysis include overcoming the need to rely

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Telephone's suggestion that any such new evidence could be adequately considered without hearings.

on any one company's processes and associated costs--unless that company has persuasively shown them to be forward-looking best practices, something New York Telephone has not done."<sup>83</sup> On exceptions, New York Telephone presses its argument that the hypothetical central offices posited by the AT&T/MCI Model reflect "science fiction" rather than reality. But in doing so, it fails to distinguish between technologies and methods that are not generally available and those that are available as best practices but, for historical or other reasons, are not in fact deployed. To rely on the former would indeed be to posit a fantasy world, caricaturing TELRIC principles. To rely on the latter, in contrast, is merely to fulfill TELRIC's best-practices mandate and would be proper in principle even if it meant that some actual costs were not recovered. Those actual costs reflect the historical configuration of the ILEC's system, pre-dating any expectation that central offices would be designed for multiple occupancy, and one should not presume that the actual added costs of retrofitting central offices for multiple occupancy should necessarily be borne entirely by the CLECs.

The question then becomes whether room construction costs should constitute an exception to the effort to estimate uniform costs and should be priced on the ICB pass-through basis proposed by New York Telephone. The Judge noted that ICB pricing was "superficially fair" but that its "use compromises TELRIC principles and, as a practical matter, introduces a degree of unpredictability that enhances the ILEC's competitive position by making it harder for CLECs to enter the market."<sup>84</sup> He recognized that denying ICB pricing would require reversing our earlier determinations, but he found a distinction between the circumstances out of which those determinations grew and those that exist now.

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<sup>83</sup> R.D., p. 108.

<sup>84</sup> Ibid., pp. 108-109.

In assessing this issue, we start by noting it is far from clear that the Judge's recommendation would disadvantage New York Telephone. AT&T/MCI's proposed recurring charge for space used by a collocator is \$7.53/sq. ft./month, while New York Telephone's price, lower in expectation of ICB recovery of special construction costs, is only \$2.21/sq. ft./month, the amount now being charged on a temporary basis. The recommended decision's adjustments to the AT&T/MCI model, however, produce a figure of \$8.98/sq. ft./month. (The recommended decision also includes a non-recurring charge of \$8,436 per application, in comparison to New York Telephone's requested \$7,508 and AT&T/MCI's proposed \$3,464.) According to information provided by New York Telephone, approximately 22,000 square feet of collocation space were being provided in July 1998; increasing the monthly rate for that space from the present temporary level to that proposed by the recommended decision would produce additional annual revenues of about \$1.8 million. Those figures do not include requests, known to Staff, for about 30,000 additional square feet, the revenue from which would be about \$2.5 million a year. These revenues total \$4.3 million, a figure that may be compared to estimated room construction costs of about \$3.6 million, based on construction in each of the 12 central office buildings now out of collocation space and typical costs per project of \$300,000. It thus appears possible, if not likely, that the pricing proposed by the recommended decision would make New York Telephone whole for its room construction costs.<sup>85</sup>

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<sup>85</sup> The costs described reflect additional collocation in buildings in which collocation already exists. Given that central offices in which there is no collocation at present are smaller, more simply constructed, and less likely in any event to be of interest to collocators, New York Telephone's exposure to unrecovered collocation construction costs in those buildings may be even less. Overall, it is difficult to predict which side would gain more under each pricing method,

New York Telephone, of course, prefers the certainty of recovery that ICB pricing provides. But ICB pricing simply shifts the burden of unpredictability to the CLECs and departs as well from our approach to TELRIC pricing, steps that would not be warranted merely to provide New York Telephone the certainty it craves. Still, these waters are largely uncharted, and a case can reasonably be made for greater price uniformity and predictability, within a framework that reasonably shares the risk of uncertainty.

Taking account of all these considerations, we adopt the recommended decision's proposed treatment of these costs on a TELRIC basis but direct as well that New York Telephone propose, in its compliance filing, a carefully defined and suitably limited mechanism for dealing with significant over- or underrecovery of room construction costs in comparison with those that would have been recovered under New York Telephone's method.

The mechanism should include provisions for ensuring that only reasonable construction costs were recovered; should include a substantial "dead band," that is, a range within which no adjustment would be made; and should not take it for granted that amounts beyond the "dead band" would be subject to 100% adjustment. Comment on the mechanism will be invited and the matter considered either in the 1999 reexamination of network element rates or separately, depending on the timing and nature of the issues posed.<sup>86</sup>

Finally, it is necessary to consider the situation of existing collocators who have already paid ICB room construction costs; to subject them to the higher per-square-foot charges here

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and it appears, as discussed below, that both sides are motivated in large part by the interest in certainty.

<sup>86</sup> We believe a mechanism of this sort can be consistent with the FCC's pricing rules reinstated by the Supreme Court. Parties will be free, of course, to address themselves to that issue in their comments on New York Telephone's proposal.

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adopted would be to recover those costs twice. In each such instance, New York Telephone and the collocator should attempt to arrive at an equitable means for moving the collocator to the new rates at some point, recognizing the possibility that doing so would entail a refund of some portion of the construction costs already paid. Staff is directed to make itself available to assist in those negotiations.

#### Power Costs

A collocation installation requires delivery of negative<sup>87</sup> 48-volt direct current power, and the parties differed on how and at what cost that power would be provided in a forward-looking system. The Judge found that New York Telephone had shown the AT&T/MCI power cost estimate to be understated in several respects and that AT&T/MCI's criticisms of New York Telephone's claimed power costs were largely unpersuasive. He therefore proposed that New York Telephone's per-amp power costs be adopted as the inputs to be used in the AT&T/MCI Model, except insofar as New York Telephone's power investment figures had to be modified in light of the effects on central office and collocation cage configuration of the overall recommendation to use the AT&T/MCI Model as the starting point.<sup>88</sup> AT&T/MCI except to several aspects of this recommendation.

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<sup>87</sup> The "negative" designation refers to the polarity of the power feed.

<sup>88</sup> R.D., pp. 122-123.