Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Cost Review Proceeding for Residential and	)	CC Docket Nos. 96-262, 94-1
Single-Line Business Subscriber Line Charge	)	
(SLC) Caps	)	

REPLY COMMENTS OF QWEST CORPORATION

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Qwest Corporation ("Qwest") hereby respectfully submits its reply comments regarding proposed increases to the subscriber line charge ("SLC") caps for residential and single-line business lines pursuant to the *CALLS Order*.[1]

I. INTRODUCTION AND SUMMARY

In its initial submission, Qwest supplied forward-looking cost information supporting proposed increases of its residential and single-line business SLC caps to $6.50 on July 1, 2003.[2] In response, the National Association of State Utility Consumer Advocates ("NASUCA") and other commenters raise various issues, many of which are beyond the scope of this proceeding.

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[1] *In the Matter of Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Low-Volume Long-Distance Users; Federal-State Joint Board on Universal Service*, *Sixth Report and Order* in CC Docket Nos. 96-262 and 94-1, *Report and Order* in CC Docket No. 99-249, *Eleventh Report and Order* in CC Docket No. 96-45, 15 FCC Rcd 12962, 12994 ¶ 83 (2000) ("*CALLS Order*"), *aff'd in part and remanded in part on other grounds sub nom. Texas Office of Pub. Util. Counsel v. FCC*, 265 F.3d 313 (5th Cir. 2001) ("*TOPUC II*"). *See Initiation of Cost Review Proceeding for Residential and Single-Line Business Subscriber Line Charge (SLC) Caps; Pleading Cycle Established*, *Public Notice*, CC Docket Nos. 96-262, 94-1, DA 01-2163, 16 FCC Rcd 16705 (rel. Sept. 17, 2001) ("*September 17 Public Notice*"). *See also, Limited Extension of Time to File Comments and Reply Comments in the Cost Review Proceeding for Residential and Single-Line Business Subscriber Line Charge (SLC) Caps, Public Notice*, CC Docket Nos. 96-262, 94-1, DA 01-2547, 16 FCC Rcd 19365 (rel. Nov. 1, 2001).

[2] Letter from John Kure, Qwest, to Magalie Roman Salas, FCC (Nov. 16, 2001) ("Qwest Initial Submission").

Despite the length of its comments, however, NASUCA's challenge reduces to one primary argument – that the forward-looking cost information submitted by Qwest should be rejected because it is not identical to the forward-looking analysis adopted by the Federal Communications Commission ("Commission") for determining the allocation of universal service high cost support for non-rural LECs. NASUCA's position is without merit. As the Commission made clear in the very orders upon which NASUCA relies, the determinations in the universal service proceeding cannot be relied upon to question forward-looking cost studies submitted in other proceedings. Specifically, in adopting the Synthesis Model and nationwide input values for determining high cost support, the Commission emphasized that the Synthesis Model was developed for the purpose of determining federal universal service support, and that it may not be appropriate to use the model or the nationwide input values for other purposes. The Commission specifically cautioned parties from doing exactly what NASUCA is attempting here – making claims in other proceedings based upon the model and input values adopted in the universal service proceeding.[3]

Given the nature of this proceeding, the forward-looking cost information submitted by Qwest provides a more appropriate basis for examining the application of the SLC caps in Qwest's study areas than the analysis advocated by NASUCA. The purpose of this cost review proceeding is to determine whether an increase of the SLC caps for residential and single-line business lines is appropriate, given the forward-looking costs faced by the price cap LEC providing voice grade service in a particular study area. The Commission's objective here is

[3] *In the Matter of Federal-State Joint Board on Universal Service*, *Ninth Report and Order and Eighteenth Order on Reconsideration*, 14 FCC Rcd 20432, 20455 ¶ 41 (1999), *aff'd in part, rev'd in part*, *Qwest Corp. v. FCC*, 258 F.3d 1191 (10th Cir. 2001); *In the Matter of Federal-State Joint Board on Universal Service; Forward-Looking Mechanism for High Cost Support for*

very different from the Commission's goal in the universal service proceeding of allocating cost support among the states, ignoring considerations such as service quality standards and other important factors. Accordingly, allegations of mere inconsistency with the Synthesis Model or *Inputs Order* provide no basis to question the validity of the cost analysis submitted by Qwest in this proceeding. A *fortiori*, they do not establish the invalidity of Qwest's cost analysis, or place any further burden on Qwest to prove its reasonableness.[4]

Likewise meritless are claims by NASUCA and the Ad Hoc Committee that Qwest has failed to provide sufficient information and detail regarding its forward-looking analysis. In its initial submission, Qwest provided a description of the nonproprietary cost models and methodology used to derive its forward-looking loop and switch port costs, as well as an explanation of the marketing costs used in its analysis. For each study area, Qwest submitted a detailed breakdown by expense type of its loop and switch port costs. The level of detail provided by Qwest is fully consistent with that submitted in other proceedings examining the reasonableness of an incumbent LEC's retail rates. Notably, neither NASUCA nor any other party requested a copy of the cost models or inputs used by Qwest in its forward-looking analysis. Qwest remains willing to provide such information to any interested party upon request.

Finally, it would be inappropriate for the Commission to consider in this proceeding NASUCA's request to amend the Commission's cost allocation rules. In the *CALLS Order*, the Commission specifically rejected NASUCA's claim that the CALLS plan is inconsistent with

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Non-Rural LECs, *Tenth Report and Order*, 14 FCC Rcd 20156, 20172 ¶ 32 (1999) ("*Inputs Order*"), *aff'd*, *Qwest Corp. v. FCC*, 258 F.3d 1191 (10th Cir. 2001).

[4] For the sake of a complete record, Qwest below refutes NASUCA's specific criticisms of the assumptions and inputs used in Qwest's forward-looking cost analysis.

Section 254(k) of the Act,[5] and the Court of Appeals for the Fifth Circuit subsequently agreed. Moreover, such a challenge to the Commission's cost allocation rules – which NASUCA acknowledges has been raised in the jurisdictional separations proceeding by the State Members of the Joint Board – is clearly beyond the scope of this cost review proceeding. Given the focus of this proceeding, the Commission also need not address the issues raised by the Ad Hoc Committee regarding the multi-line business SLC and primary interexchange carrier charge ("PICC").

II. THE FORWARD-LOOKING COST INFORMATION SUPPLIED BY QWEST FULLY JUSTIFIES INCREASES IN THE RESIDENTIAL AND SINGLE-LINE BUSINESS SLC CAPS TO $6.50

As required by the *CALLS Order*, Qwest has submitted forward-looking cost information associated with its provision of retail voice grade access to the public switched telephone network ("PSTN").[6] This information fully justifies the scheduled increases of the residential and single-line business SLCs to $6.50. As discussed below, NASUCA's reliance on the universal service proceeding is misguided and fails to undermine the reasonableness of Qwest's analysis.

A. Qwest's Forward-Looking Cost Analysis Is Sufficiently Detailed And Open

In the *CALLS Order*, the Commission committed to initiate and complete a cost review proceeding prior to any scheduled increases above a $5.00 cap on residential and single-line business SLCs. In that proceeding, the price cap LECs would provide, and the Commission would examine, forward-looking cost information associated with the provision of retail voice grade access to the PSTN.[7] The Commission declined to define the scope of the cost review

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[5] 47 U.S.C. § 254(k).

[6] *See CALLS Order*, 15 FCC Rcd at 12994 ¶ 83.

[7] *See id.*

study or the specific information to be examined, stating its preference to address those issues when initiating the cost study.[8] On September 17, 2001, the Commission issued a *Public Notice* initiating the cost review proceeding and requiring the price cap LECs to provide forward-looking cost information associated with the provision of retail voice grade access to the PSTN. The *Public Notice* provided no additional information regarding the type of forward-looking information required.[9] It did not direct the use of a particular forward-looking model or inputs, nor did it require the submission of the models and inputs used by the price cap LECs.

On November 16, 2001, Qwest submitted forward-looking cost information regarding the provision of retail voice grade access to the PSTN. Qwest provided several pages of analysis for each study area with a detailed breakdown of the forward-looking cost for the loop and the port. Qwest explained that it had used its LoopMod cost model, Switch Cost Model, and Retail Cost Program to compute the forward-looking cost information submitted in this proceeding. Each of these models are nonproprietary and have been used in numerous state cost proceedings.

With regard to inputs, Qwest used input values from its public filings in state cost proceedings. In its initial submission, Qwest identified the values of some of the most important input variables used in the model. In these Reply Comments, Qwest provides further information with regard to the assumptions and inputs questioned by NASUCA and the Ad Hoc Committee, and shows that these assumptions and input values used by Qwest are reasonable.

The Commission should reject NASUCA's suggestion that Qwest was required to, but did not, comply with procedures regarding the disclosure of its cost models and inputs. The purpose of this proceeding is to determine whether an increase in the SLC cap for a particular study area served by a price cap LEC is justified, similar to the Commission's review of the

[8] *Id.* at 12994-95 ¶ 84.

reasonableness of a LEC's retail rates for new services.[10] The procedures identified by NASUCA have never been required for these purposes. Indeed, the Commission did not establish such standards in the *CALLS Order* or *Public Notice* initiating this proceeding.[11] Thus, contrary to NASUCA's arguments, acceptance of the forward-looking cost information submitted by Qwest would not be a deviation from the Commission's past policies in analogous contexts.

B. The Assumptions And Input Values Used In Qwest's Cost Analysis Are Reasonable

NASUCA appears to challenge any perceived deviation in the LECs' cost analyses from the Commission's approach in the universal service proceeding – notwithstanding the Commission's warning against this very practice. With regard to Qwest's analysis, all of NASUCA's claims are misplaced. In many cases, NASUCA's assumptions about Qwest's analysis or input values are factually inaccurate. While most of NASUCA's questions and criticisms are directed at the submissions of other companies, Qwest nevertheless responds to these issues. Qwest also provides additional information regarding the five inputs that the Ad Hoc Committee identified as particularly important in a cost model. As explained below, the assumptions and input values used in Qwest's forward-looking cost analysis are reasonable and provide a sound basis for the proposed increases to the residential and single-line business SLC.

Forward-Looking Model. Contrary to NASUCA's suggestions, Qwest's model is a

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[9] *September 17 Public Notice* at 1.

[10] *See* 47 C.F.R. § 61.38.

[11] Contrary to NASUCA's claim, the Commission's adoption of such procedures in the universal service proceeding does not support their application here. The Commission's actions in the universal service proceeding demonstrate that when the Commission wants to mandate such procedures, it knows how to do so. The Commission did not, however, mandate such procedures here. Further, as discussed *infra*, the universal service proceedings were conducted for a different purpose than the purpose here, which essentially is ratemaking.

forward-looking model and is a "replacement," not a "reproduction" model. LoopMod develops the network components required to provide voice grade telephone service by incorporating data on customer locations and demand quantities with forward-looking network designs and technologies.

State-Specific Input Values. The Commission also should reject NASUCA's suggestion that the use of state-specific input values in this proceeding is inappropriate. Once again, NASUCA's sole support for its proposition is the Commission's approach in the universal service proceeding.[12] However, the concerns that led to that approach are inapplicable here. In the universal service proceeding, the Commission concluded that "using company-specific data *for federal universal service support purposes* would be administratively unmanageable and inappropriate,"[13] though it might be appropriate in other contexts.[14] The Commission noted that adopting state-specific values in the universal service proceeding would require the Commission to adopt different values for each input value for each of the fifty states, the District of Columbia, and Puerto Rico, or for the 94 non-rural study areas.[15] The Commission may have also been concerned that the adoption of state-specific input values would complicate the task of running the model and updating the model in future years. Those administrative concerns do not exist in this proceeding where the Commission is engaged in a one-time comparison of the price cap LECs' costs to the current residential and single-line business SLC caps. As discussed below with regard to specific inputs, the state-specific inputs used by Qwest more accurately reflect the forward-looking costs that Qwest faces in providing service in particular study areas than the

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[12] NASUCA Comments at 20-21.

[13] *Inputs Order*, 14 FCC Rcd at 20198 ¶ 90 (emphasis supplied).

[14] *Id.* at 20199 ¶ 92. For example, it may not be appropriate to use nationwide values for determining prices for unbundled network elements. *Id.* at 20172 ¶ 32.

nationwide inputs used in the Synthesis Model and thereby reflected in NASUCA's analysis.

In the universal service context, the Commission also noted that it was not attempting to identify any particular company's cost of providing the supported services,[16] but rather trying to establish a national benchmark for purposes of allocating support amounts. The Commission noted that it was not taking into account such unique, but real, circumstances as differing service quality standards. The Synthesis Model assumes, for example, that all customers will receive a certain quality of service whether or not carriers actually are providing that or a higher quality of service.[17] The Commission noted that if it were determining the rates a carrier could charge for a particular "service," as is the case here, the quality of service the carrier actually was providing could be a relevant factor.[18] The models in this proceeding are being used to compare the absolute forward-looking cost for the price cap LEC to provide service in a particular study area versus the current $5.00 SLC cap. Thus, the use of nationwide input values is neither required, nor appropriate.

Cost of Money. As noted in Qwest's initial filing, Qwest used a cost of money (*i.e.*, cost of capital) factor of 11.7 percent. This factor is a composite cost of debt and equity weighted by the debt-to-equity ratio of a company, in Qwest's case approximately 0.39. Qwest computed the cost of money factor based on an analysis of the forward-looking rate that an efficient carrier of Qwest's size would face in seeking to raise new capital. The cost of debt component of the factor reflects such a carrier's cost of new debt financing. The cost of equity is estimated using financial models and market data for LECs and other companies with risk comparable to

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[15] *Id.* at 20199 ¶ 92.

[16] *Id.* at 20198 ¶ 90.

[17] *Id.* at 20310-11 ¶ 360.

[18] *Id.* at 20311 n.793.

Qwest's.[19] Economically efficient companies in all industries routinely alter their debt-to-equity ratio to maximize efficiency. Additionally, real world economic conditions routinely change the cost of debt and the expected return on equity. The cost of money factor used in Qwest's analysis therefore more closely reflects Qwest's forward-looking cost of money than the 11.25 percent cost of capital rate prescribed in the universal service proceeding.

Depreciation. In response to the questions raised by NASUCA and the Ad Hoc Committee,[20] Qwest clarifies that its forward-looking analysis used the depreciation lives and net salvage percentages that the Commission prescribed for each study area's interstate depreciation lives and salvage values.

Shared and Common Costs. NASUCA incorrectly assumes that Qwest's forward-looking analysis assigns all shared and common costs to the loop.[21] In fact, much like the HAI Model, the Qwest Retail Cost Program computes common costs for each network element by applying common cost factors to the direct costs for each element, including the loop and the port. In addition, the Qwest SLC cost study applies separate Commission-defined separations factors to the total loop and port costs, including shared and common costs. The SLC costs developed in Qwest's forward-looking analysis therefore include appropriate common and shared costs.

Qwest did not include any call completion or numbering services costs in its forward-looking analysis, but appropriately assigned expenses for uncollectible revenues using the same cost factor for all services. Qwest's assignment of these and all other expenses were reflected in Qwest's initial submission. Attachments 2 and 3 of Qwest's submission display the expense and

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[19] Qwest Initial Submission at 4 n.5.

[20] NASUCA Comments at 27-28; Ad Hoc Committee Comments at 7.

[21] NASUCA Comments at 29, 33.

the expense factor for each major account by study area. Thus, NASUCA's criticisms in this regard do not apply to the forward-looking information supplied by Qwest.

Digital Loop Carrier Assumptions. NASUCA also wrongly asserts that the price cap LECs' cost analysis should assume 100 percent use of integrated digital loop carrier ("IDLC") equipment, and no use of universal digital loop carrier ("UDLC").[22] This assertion is based on the faulty assumption that an IDLC configuration will always be less expensive than a UDLC configuration. In point of fact, Qwest has found that a UDLC configuration is cheaper than an IDLC configuration for small distribution areas. Therefore, LoopMod employs IDLCs for large (*i.e.*, 672-line or 1344-line) and medium (*i.e.,* 96-line or 192-line) remote terminals, but UDLCs for small (*i.e.*, 32-line) remote terminals. In any case, LoopMod's use of UDLCs is unlikely to have a significant impact on its cost estimates.

Fill Factors. In response to questions by NASUCA and the Ad Hoc Committee,[23] Qwest clarifies that it did not use "embedded" fill factors, but rather fill factors that reflect forward-looking assumptions, given the real-world requirements of providing service in Qwest's service territory. Those factors are as follows:

Distribution

Density Group	**Fill**
DG1	50%
DG2	50%
DG3	33%
DG4	33%
DG5	50%

Feeder

Density Group	**Copper**	**Fiber**
All	80%	100%

LoopMod Distribution Designs:

[22] *Id.* at 31. *See also* Ad Hoc Committee Comments at 7-8 (asserting that the type of DLC investment used in a cost model is an important cost driver).

[23] NASUCA Comments at 31-32; Ad Hoc Committee Comments at 7.

- Density Group 1 (DG1) - high-rise buildings
- Density Group 2 (DG2) - multi-building / multi-tenant distribution areas
- Density Group 3 (DG3) - single family with standard lot sizes (approximately 600 to 2500 homes per square mile)
- Density Group 4 (DG4) - single family with larger lots (approximately 50 to 600 homes per square mile)
- Density Group 5 (DG5) - rural serving areas (less than 50 homes per square mile)

Qwest's approach also is consistent with the methodology outlined by the Commission in the *Local Competition First Report and Order* for developing forward-looking costs for unbundled network elements: "Per-unit costs shall be derived from total costs using reasonably accurate 'fill factors' (estimates of the proportion of a facility that will be 'filled' with network usage); that is, the per-unit costs associated with a particular element must be derived by dividing the total cost associated with the element by a reasonable projection of the actual total usage of the element."[24] Furthermore, the fill factors used by Qwest are similar, but not identical, to the factors adopted in the *Inputs Order* for use in the universal service model.

Loop Length. The Commission also should disregard NASUCA's complaints regarding the computation of loop length and customer locations. Qwest's LoopMod model determines customer locations and designs plant using a combination of census block information and actual distribution area data. This data allows LoopMod to build efficient forward-looking feeder designs that recognize real-world obstacles to placing outside plant. Since the existing

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[24] *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers*, *First Report and Order*, 11 FCC Rcd 15499, 15847-48 ¶ 682, *aff'd in part and vacated in part sub nom.*, *Competitive Telecommunications Ass'n v. FCC*, 117 F.3d 1068 (8th Cir. 1997) and *Iowa Utils. Bd. v. FCC*, 120 F.3d 753 (8th Cir. 1997), *aff'd in part and remanded*, *AT&T v. Iowa Utils. Bd.*, 525 U.S. 366 (1999), *on remand*, *Iowa Utils Bd. v. FCC*, 219 F.3d 744 (8th Cir. 2000), *pets. for writ of cert. granted*, *Verizon Communications Inc. v. FCC*, 121 S. Ct. 877, 878 (2001); *Order on Recon.*, 11 FCC Rcd 13042 (1996), *Second Order on Recon.*, 11 FCC Rcd 19738 (1996), *Third Order on Recon. and Further Notice of Proposed Rulemaking*, 12 FCC Rcd 12460 (1997), further recons. pending.

distribution areas are built in recognition of the current man-made and natural obstacles in the outside plant environment, these areas are used as the starting point to develop the forward-looking design.

Structure Sharing. NASUCA's concerns about structure sharing in Qwest's model are similarly unfounded. Qwest's LoopMod model does not assign 100 percent of structure costs to local telephone plant, as suggested by NASUCA.[25] The LoopMod assigns 50 percent of aerial structure, 80% of buried structure, and 95% of underground structure to Qwest. These sharing percentages are within range of the percentages used in the Synthesis Model,[26] particularly given the Commission's recognition that there is room for reasonable analysts to differ on the precise values for these inputs.[27]

OSS Transition Costs. Contrary to NASUCA's suggestion, Qwest did not include any "OSS [Operational Support System] transition costs" in its forward-looking cost estimates.

Marketing. The Commission should reject NASUCA's attempt to eliminate or reduce the marketing expenses that are assigned to the common line basket by the Commission's rules. In essence, NASUCA argues that the Commission should modify its rules that currently allocate marketing expenses to the common line rate elements.[28] Clearly, such rule changes are beyond the scope of this proceeding. Moreover, NASUCA recognizes that such modifications would result in an expense for which there is no explicit recovery mechanism.[29] As Qwest stated in its

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[25] NASUCA Comments at 33.

[26] In the universal service proceeding, the Commission assigned 35 to 50 percent of the costs of aerial structure to the LEC, and 55 to 100 percent of the costs of buried and underground structure to the LEC, depending on the density zone. *Inputs Order*, 14 FCC Rcd at 20260-61 ¶ 243.

[27] *Id.* at 20261 ¶ 244.

[28] NASUCA Comments at 34-35.

[29] *Id.* at 35.

initial submission, the marketing expenses currently in the Price Cap Common Line, Marketing, and Certain Residual Interconnection Charge ("CMT") were not, and are not, associated with any particular rate elements, so it would be inappropriate to compute a SLC cap using a forward-looking estimate of marketing expenses associated with local exchange services. Qwest instead used the marketing expenses from its annual filing, which do not include special access and interchange marketing expenses.[30]

III. THE COMMISSION SHOULD REJECT NASUCA'S COST ANALYSIS

In addition to its broad brush attack on the forward-looking cost information submitted by Qwest and the other price cap LECs, NASUCA asserts that the Commission should analyze the LECs' SLCs using the Synthesis Model, which was specifically developed for determining universal service high-cost support for non-rural LECs. NASUCA ignores the Commission's repeated warnings that the Synthesis Model and its nationwide inputs may not be appropriate for purposes other than determining universal service support.[31] In light of these prior statements by the Commission, it would be unreasonable for the Commission to rely on the Synthesis Model in this proceeding.[32]

Although the Synthesis Model is a forward-looking cost model, it is designed for an entirely different purpose than the forward-looking cost information provided in this proceeding. In the universal service proceeding, the Commission sought to determine the relative (not

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[30] *See id.* at 35-36 (questioning whether price cap LECs have included special access and interexchange marketing expenses in their analysis).

[31] *Ninth Report and Order*, 14 FCC Rcd at 20455-56 ¶ 41; *Inputs Order*, 14 FCC Rcd at 20172 ¶ 32.

[32] On numerous previous occasions, Qwest has argued that the Synthesis Model should not be used even in determining universal service high-cost support, because it understates the cost of providing service in Qwest's territory. These same arguments apply in this context, but will not be repeated here.

absolute) cost of providing service in each state. Given the nature of this exercise, and in the interest of simplicity and administrative efficiency, the Commission intentionally ignored real-life differences among study areas. For example, the Commission recognized that the model did not account for service quality differences among states, and that such differences might be important if the Commission were determining the rates a carrier could charge for a particular service.[33] While the Commission justified this approach based on its goal of establishing a national benchmark to compare the relative costs of providing service in the states, that justification does not apply here. In this proceeding, the Commission is evaluating whether the absolute (as opposed to relative) forward-looking cost of providing service in a particular study area exceeds the current $5.00 SLC cap for residential and single-line business lines and therefore justifies an increase of the cap for the study area. Higher service quality standards in particular states impose real forward-looking costs on a price cap LEC that provides service in that area. Such service quality standards may include installation and repair intervals and restrictions on held orders, which require the incumbent to deploy and maintain sufficient plant to meet both expected and unexpected demand and to avoid outages. Qwest's models are designed to meet these standards. The Synthesis Model, however, fails to account for such costs and therefore is not appropriate for this proceeding.

Equally important, the Synthesis Model also disregards cost differences faced by particular incumbent LECs,[34] as the Commission has acknowledged. In the universal service proceeding, the Commission justified this approach based on its objective of estimating the costs

[33] *Inputs Order*, 14 FCC Rcd at 20310-11 ¶ 360 n.793. Because differences in service quality can cause different maintenance expense levels, by assuming a consistent nationwide quality of service, the Commission controlled for variations in company-specific maintenance expenses due to variations in quality of service. *Id.* at 20310-11 ¶ 360.

an efficient provider would incur in providing the supported services. Because universal service "high-cost support is portable, a competitive eligible telecommunications carrier, rather than the incumbent LEC, may be the recipient of the support."[35] In contrast, the objective of this proceeding is to determine the forward-looking cost of the price cap LEC providing service in a particular study area. The Commission has acknowledged that particular carriers may face different costs based on their size, regional variations, and other factors, as well as their relative efficiency.[36] While the Commission suggested that the Synthesis Model accounted for some of these differences, many were ignored. For example, smaller price cap LECs may face higher costs of capital and may enjoy fewer economies of scale. It would be unreasonable to ignore such variations in this context through reliance on the Synthesis Model.

The Synthesis Model also departs from reality in estimating the number of customer locations within a geographic area and the demand for service at each customer location. As adopted in the universal service proceeding, the Synthesis Model estimates forward-looking cost based upon the number of <u>occupied</u> living units within a geographic area and thereby ignores the three-to-six percent of living units that are unoccupied at any given point in time.[37] Obviously, a living unit that is unoccupied today may be occupied tomorrow and therefore must continue to be served by the incumbent LEC. However, the cost of network capacity to serve both occupied and unoccupied living units can only be recovered from the existing customer base. Thus, particularly in computing forward-looking costs in this context, it is appropriate to include the costs of connecting all living units in the numerator of the cost equation and to divide by a

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[34] *Id.* ("Clearly, we are not attempting to identify any particular company's cost of providing the supported services.").

[35] *Id.*

[36] *Id.* at 20308-09 ¶ 355.

denominator reflecting the lines currently providing service (*i.e.*, occupied living units).[38] Thus, the Synthesis Model's estimate of costs based on serving occupied living units is inconsistent with a price cap LEC's carrier-of-last-resort obligations and is not appropriate for the computation of its rates.

Based upon its use of the Synthesis Model, NASUCA asserts that residential and single-line business customers are subsidizing other customers. NASCUA has it backwards. It is well accepted that rates have been designed historically to provide subsidies from business to residential customers. For example, the Commission acknowledged in the *CALLS Order* that the rates for residential customers are subsidized by large business customers through multi-line business SLCs and PICCs.[39] The whole point of the *CALLS Order* was to begin to eliminate these subsidies through means such as the proper sizing of the residential and single-line business SLCs. In sum, NASUCA's observation that the Synthesis Model indicates that subsidies are running from residential customers to business customers confirms, as the Commission warned in its *Inputs Order*, that the Synthesis Model should not be used for any purpose other than the one for which it was designed.

In addition to its improper reliance on the Synthesis Model, NASUCA also makes basic errors in its characterization of Qwest's cost analysis. For example, in a chart comparing Qwest's and NASUCA's cost analysis,[40] NASUCA incorrectly identifies Qwest's computation of

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[37] *Id.* at 20180 ¶ 48.

[38] *Compare id.* at 20183-84 ¶ 56 (concluding that such an "inconsistency" in the numerator and denominator is not appropriate for purposes of computing universal service high-cost support).

[39] *See, e.g., CALLS Order*, 15 FCC Rcd at 12971-72 ¶ 23, 13004 ¶ 106.

[40] NASUCA Comments at 26 (Table 1).

its forward-looking cost per line (plus marketing) as the "Price Cap CMT Per Line."[41] In addition, in the next column of this table, "SLC from Carrier Cost Studies," NASUCA inappropriately omits Qwest's marketing expenses.

The Commission should also ignore NASUCA's argument that allowing the SLC caps to rise will increase implicit subsidy payments.[42] As long as a price cap LEC charges SLC rates that are averaged across a study area, the SLC rate will be higher than the cost of some loops and lower than others. Moreover, increasing SLC rates will in many cases decrease these "subsidies" by allowing price cap LECs to deaverage their SLC rates within a study area.[43] It should be noted that, even if the Commission increases the SLC caps, a price cap LEC's SLC rates may be constrained by its CMT per line.

NASUCA also wrongly suggests that the price cap LECs can easily forgo revenue from SLC increases given their current intestate rates of return. In evaluating such information, however, the Commission must consider the revenue for the common line basket at issue in this proceeding. Qwest's interstate rate of return in that context is less than 11 percent.[44]

In sum, NASUCA's cost analysis fails to undermine the validity of the forward-looking cost information submitted by Qwest and the conclusion that the proposed increases to the residential and single-line business SLC caps are justified.

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[41] It appears that this column of Table 1 reflects the "Total CMT Interstate Cost with Marketing" in Qwest's initial submission, which is the forward-looking cost computed by Qwest, plus the marketing expenses from Qwest's last annual filing.

[42] NASUCA Comments at 42.

[43] *CALLS Order*, 15 FCC Rcd at 12975 ¶ 31. Under the *CALLS Order*, a price cap LEC is not permitted to deaverage its SLCs in a study area until it has eliminated its PICCs and carrier common line charge, which is more likely to occur with an increase in SLC rates.

[44] ARMIS 43-01 "Cost and Revenue Table" Rows 1910 and 1915 Columns H (Interstate) and M (Common Line).

IV. THE REMAINING ISSUES RAISED BY NASUCA AND THE AD HOC COMMITTEE ARE BEYOND THE SCOPE OF THIS PROCEEDING

Both NASUCA and the Ad Hoc Committee raise issues that clearly fall outside the scope of this proceeding. As the Commission indicated in the *Public Notice* initiating this proceeding, the sole focus of this proceeding is the review of the forward-looking cost information provided by the price cap LECs to determine whether an increase in the SLC cap above $5.00 is warranted for residential and single-line business lines.[45]

A. The Commission Should Reject NASUCA's Request To Amend The Commission's Cost Allocation Rules In This Proceeding

NASUCA devotes the last 50 pages of its comments to a challenge of the Commission's cost allocation rules, claiming that those rules do not properly assign costs between services included and excluded from the definition of universal service.[46] This proceeding obviously is not the proper place for the Commission to consider a change to its cost allocation rules. Moreover, such a change is not warranted in this context, as the Commission already considered and rejected NASUCA's Section 254(k) challenge in the *CALLS Order*.[47] NASUCA may have reformulated its argument to try to avoid the import of two court of appeals decisions, but the outcome should be the same.

In adopting the CALLS proposal, the Commission rejected NASUCA's claim that the proposal violated Section 254(k) of the Act, including the contention that it causes services included in the definition of universal service to bear more than a reasonable share of the joint

[45] *September 17 Public Notice* at 1.

[46] *See* NASUCA Comments at 9 ("It is time for the FCC to revise its rules such that they are in accordance with a modern, multi-service platform"); *id.* at 60 ("It is clear . . . that [the Commission's] rules are now antiquated . . . .).

[47] NASUCA appears to acknowledge that this issue was considered in the *CALLS Order*. *See id.* at 69 ("The issue of shared costs discussed in the prior section was raised with the Commission in the CALLS proceeding.").

and common costs of facilities used to provide those services.[48] "Because the SLC is a method of recovering properly allocated loop costs, not an allocation of those costs between supported and unsupported services, section 254(k) is not implicated."[49] On appeal, the Fifth Circuit agreed with the Commission and the Eighth Circuit, finding that Section 254(k) does not implicate the SLC.[50]

Even if the Commission wished to revisit this issue, this proceeding is not the appropriate context for such review. If NASUCA believes that the Commission's cost allocation rules should be changed, it is free to file a petition for rulemaking. Moreover, as NASUCA acknowledges, the state members of the Federal-State Joint Board have raised similar issues in the jurisdictional separations proceeding.[51] Before considering any change to its rules, the Commission must provide notice and opportunity for all interested parties to comment, consistent with the requirements of the Administrative Procedure Act.

B. This Proceeding Is Also The Wrong Place To Consider The Multi-Line Business SLC and PICC Issues Raised By The Ad Hoc Committee

The Ad Hoc Committee also raises issues that are beyond the scope of this proceeding. As outlined in the *September 17 Public Notice*, the Commission's consideration in this proceeding is limited to the cost justification for proposed increases to the residential and single-line business SLCs and does not include questions regarding the multi-line business SLC and PICC.

[48] *CALLS Order*, 15 FCC Rcd at 12998-99 ¶¶ 90-93.

[49] *Id.* at 13000-01 ¶ 96 (citing *Southwestern Bell Telephone v. FCC*, 153 F.3d 523, 559 (8th Cir. 1998).

[50] *TOPUC II*, 265 F.3d at 324.

[51] NASUCA Comments at 68.

V. CONCLUSION

As discussed above and in its initial submission, the forward-looking cost information provided by Qwest adequately justifies increases of the residential and single-line business SLCs to the $6.50 caps currently in the Commission's rules.

Respectfully submitted,

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February 14, 2002

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CERTIFICATE OF SERVICE

I, Richard Grozier, do hereby certify that I have caused the foregoing **REPLY COMMENTS OF QWEST CORPORATION** to be filed with the FCC via its Electronic Comment Filing System, and a copy of the **REPLY COMMENTS** to be served, via email, on all parties listed below.*

Richard Grozier
Richard Grozier

February 14, 2002

*Parties wishing to receive a hard copy may contact Kelseau Powe in our Washington, DC office at 202-429-3114.

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