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BEFORE THE ARIZONA CORPORATION COMMISSION

WILLIAM A. MUNDELL
CHAIRMAN
JIM IRVIN
COMMISSIONER
MARC SPITZER
COMMISSIONER

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AZ CORP COMMISSION
DOCUMENT CONTROL

IN THE MATTER OF THE INVESTIGATION OF
THE COST OF TELECOMMUNICATIONS
ACCESS

Docket No. T-00000D-00-0672

NOTICE OF FILING
DIRECT TESTIMONY

Cox Arizona Telcom, L.L.C. hereby gives notice that it files the attached direct
testimony of Douglas Garrett.

RESPECTFULLY SUBMITTED June 28, 2002.

COX ARIZONA TELCOM, L.L.C.

By

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Arizona Corporation Commission

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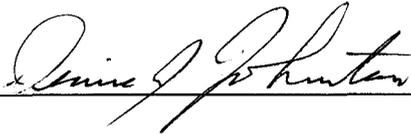
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BEFORE THE ARIZONA CORPORATION COMMISSION

WILLIAM A. MUNDELL
CHAIRMAN
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IN THE MATTER OF THE INVESTIGATION OF
THE COST OF TELECOMMUNICATIONS
ACCESS

Docket No. T-00000D-00-0672

DIRECT TESTIMONY
OF
DOUGLAS GARRETT
ON BEHALF OF
COX ARIZONA TELCOM, L.L.C.

JUNE 28, 2002

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Testimony of Douglas Garrett

Q. WHAT IS YOUR NAME AND WHAT IS YOUR BUSINESS ADDRESS?

A. My name is Douglas Garrett, 2200 Powell Street, Suite 1035, Emeryville, CA 94608.

Q. BY WHO ARE YOU EMPLOYED AND IN WHAT POSITION?

A. I am employed by Cox Communications, Inc. as Vice President of Regulatory Affairs for the Western Region of Cox's telephony operations. I am responsible for regulatory issues that affect Cox Arizona Telcom, LLC ("Cox").

Q. WHAT IS YOUR BACKGROUND AND EXPERIENCE?

A. I have been employed in my current capacity by Cox since August 2001. Prior to that I was employed by NorthPoint Communications as Vice President Service Provisioning and Vice President Local Exchange Carrier Relations. My responsibilities included managing all operational and customer service issues related to the company's broadband provisioning. I was also responsible for managing interconnection agreements with incumbent telephone companies, including the provisioning of central office collocation and unbundled network element. Previous to North Point, I served as Vice President, State Regulatory Affairs for ICG Communications, a facilities-based CLEC based in Denver, Colorado. From 1973 to 1998, I was employed by Pacific Bell and SBC Communications in a variety of capacities, including network operations, marketing, and financial management. I was Executive Director, Local Interconnection for Pacific Bell at the time the company negotiated and implemented its first round of interconnection agreements under the Telecommunications Act of 1996. I have a Bachelor's degree in Management from St. Mary's College of California.

1 **Q. MR. GARRETT, WOULD YOU SUMMARIZE YOUR TESTIMONY?**

2 A. Cox is not proposing a specific intrastate access charge reform plan. Cox has
3 some concern that such a plan may be premature. First, the Commission may want
4 to consider access charge reform in conjunction with any reform of the Arizona
5 Universal Service Fund. The Commission also should consider maintaining
6 existing access charges or deferring any decision until the FCC conducts a
7 significant restructuring of access charges. If the Commission pushes forward
8 with intrastate access charge reform at this time, Cox presents several policy issues
9 that the Commission should incorporate in deciding on the appropriate reforms.

10 **Q. SHOULD THE COMMISSION PUSH FORWARD WITH ACCESS**
11 **CHARGE REFORM NOW?**

12 A. It may make sense to delay intrastate access charge reform until the FCC conducts
13 a significant reform of access charges. If one of the goals is to parallel the federal
14 scheme, then we should wait to see what that scheme is. Regardless, Arizona
15 should not implement access charge reform if there is a risk such reform may
16 conflict with the ultimate federal scheme. Such conflict will require us to revisit
17 the issue of intrastate reform and is not a beneficial use of resources at this time.
18 Moreover, Cox expects that some of the access charge reform proposals will be
19 tied to AUSF issues. It may be appropriate for the Commission to combine this
20 docket with the AUSF docket to ensure consistency, to avoid access charge reform
21 from dictating what can and cannot be done in the AUSF docket or to avoid having
22 to revisit access charge reform in light of issues subsequently raised in the AUSF
23 docket.

24 **Q. WHAT ARE OVERARCHING CONCERNS ABOUT ACCESS REFORM?**

25 A. There are a variety of creative approaches to access charge reform, but none are
26 without drawbacks. The theoretical benefits of these approaches must be weighed

1 against the potential for shifting the access burden too much to consumers in fixed
2 costs or destabilizing telecommunications revenue flows, particularly for new and
3 recent market entrants or for rural carriers. Much of the analysis of access charge
4 reform boils down to acceptable types and levels of explicit and implicit subsidies.
5 Moving too quickly to a pure cost recovery from those who cause the costs may be
6 too disruptive. Moreover, determining the appropriate methods of calculating
7 access charge costs and allocating those costs is a difficult task that may not have a
8 single answer that can be applied to different segments of the market.

9 **Q. ARE THERE PARTICULAR ISSUES CONCERNING SUBSIDIES THAT**
10 **NEED TO BE ADDRESSED IN ACCESS CHARGE REFORM?**

11 A. Presently, switched access charges, and the CCL charge in particular, do contain
12 subsidies. This is true not because switched access is priced too high overall, or
13 because access is billed to carriers rather than end users, but because of the
14 structural dissimilarity between how costs are incurred and how these costs are
15 recovered. In effect, these are not true subsidies but rather are mismatched costs.
16 The CCL charge, for example, contains subsidies because it recovers, by defini-
17 tion, nontraffic-sensitive costs with traffic-sensitive rates. Other usage sensitive
18 switched access rate elements also contain substantial nontraffic-sensitive costs.
19 Such a structure creates a subsidy that ultimately flows from high volume toll users
20 to low volume toll users. This mechanism has historically kept monthly recurring
21 line rates low. Historically switched access rates have been set above long run
22 incremental costs, and as a result, they have contributed to the recovery of joint
23 and common costs.

24 Although implicit subsidies can be quantified by determining the long run
25 incremental costs of each service that shares any joint and common costs, the
26 rooting out of implicit subsidies should not be the only objective here. The
27 Commission has other policy objectives (such as providing affordable basic

1 service at averaged rates or nondiscriminatory service). For example, basic
2 exchange service is priced at a single rate even though the cost of service through
3 shorter loops subsidizes service through longer loops. A theoretical case can be
4 made that interexchange carrier switched access charges – at least as presently
5 structured – should not exist, and that actual access costs should be borne directly
6 by end users. However, since IXC access charges have existed in some form or
7 another for decades, and since all market participants – end users, IXCs and LECs
8 – have had their behavior and expectations influenced by them, their elimination
9 carries high potential for destructive market disruption. In the absence of an
10 interstate shift to eliminate IXC switched access charges, such a plan would be
11 highly impractical and disruptive to implement on a state-by-state basis.

12 If the Commission is determined to “cost match” for intrastate access and
13 eliminate implicit subsidies, it will need to adopt an appropriate cost standard for
14 such analysis. Some variation of long run incremental costs (TELRIC) could be
15 used to determine whether any single service is receiving a subsidy. But the
16 Commission cannot stop there, because it must then address how it will recover the
17 joint and common costs. It is not unreasonable that every service that uses the
18 local loop provides some contribution to the recovery of the costs of the loop –
19 however the structure of such cost recovery should more closely match the nature
20 of the cost. Where a large part of the cost of a set of services is a joint cost (one
21 that cannot be avoided if any one of the services is offered), it is difficult to make
22 an allocation of that joint cost that is absolutely right. In such a case, a price
23 exceeding the range between the stand-alone cost for any one product, and its long
24 run incremental cost (with some contribution toward the joint cost) would be an
25 appropriate measure of whether a subsidy exists. It is important to understand the
26 degree of structural dissimilarity between how costs are incurred and how these
27 costs are recovered. Such a study should not be limited to the access market,

1 however, since switched access services and local services are inextricably linked,
2 and since the joint cost of the loop (which is used for both) must be recovered
3 somehow. If incremental costs alone were the determinant, the Commission would
4 find that a variety of additional "subsidies" exist – business customers subsidize
5 residential customers, feature users subsidize non-feature users, low-usage local
6 customers subsidize high usage local customer, etc.

7 Cox would note that interstate access charge rates are the product of historic
8 fully allocated costing, as well as some incremental costing. Price Cap ILECs no
9 longer cost-justify their rates through detailed new cost studies, but rather change
10 rates based on the Price Cap Model.

11 Finally, Cox does not believe that access charges should be set at the same
12 rates as unbundled network elements for the same network elements and
13 functionalities, at least not at the outset of any access charge reform. In isolation it
14 would be reasonable to assume that like functions should all be priced the same –
15 and in the long run they probably will be. However, potentially dramatic shifts of
16 prices in one category of telecommunications service would certainly impact rates
17 in other categories. Since switched access, particularly on a terminating basis, is
18 relatively insensitive to competition, rate reductions in switched access services
19 would likely have to be shifted to other services similarly insensitive to
20 competition. This would likely place most of the burden on residential ratepayers;
21 not business or toll users. Again, the potential for market disruption is high if this
22 transition is too quick or unpredictable.

23 **Q. WHAT CONSIDERATIONS MAKE ACCESS CHARGE REFORM IN THE**
24 **PUBLIC INTEREST?**

25 **A.** The Commission should identify the shortcomings, if any, of the existing access
26 charge structure to achieve its public policy objectives. Any restructuring must
27 identify how the existing problems will be reduced or eliminated, and how other

1 policy objectives, such as reasonable local service rates at average prices and the
2 development of meaningful local competition and increased consumer choice will
3 not be compromised.

4 Additionally, there may be benefits to keeping access charges structurally
5 consistent with interstate access until such time as the FCC undertakes significant
6 access reform. Substantial interstate/intrastate access rate disparity is one of many
7 issues the Commission should consider in this proceeding. However, complete
8 access rate parity would drive out any other policy matters the Commission may
9 want to consider. Complete parity abandons access charges as a policy tool for the
10 Arizona Commission.

11 Any access charge reform also must be competitively neutral. For example,
12 Qwest's withdrawn tariff filing in Docket No. T-01051B-01-0391 (*In the Matter of*
13 *Qwest Corporation's Tariff Filing to Introduce a New Rate Structure for an Access*
14 *Service Used by Interexchange Carriers*), presented a situation that was arguably
15 revenue-neutral for Qwest but that created significant anti-competitive impacts
16 because it created "subsidies" for one class of interconnectors (IXCs) at the
17 expense of another class of interconnectors (facilities-based LECs such as Cox).

18 Finally, the Commission should address proper imputation under A.A.C.
19 R14-2-1310 before (or if) it decides to set new access charges. The Commission
20 recognized potential problems with that regulation during the recent Qwest Rate
21 Case that adopted Qwest's Price Cap Plan.

22 **Q. WHAT SHOULD THE COMMISSION DO WITH SPECIAL ACCESS**
23 **RATES?**

24 A. The Commission should focus on switched access in this docket, not special
25 access. Although the services are somewhat cross-elastic, it is unlikely that an
26 intrastate special access restructuring could significantly influence the overall rate
27 relationship between intrastate switched and special access. First, special access is

1 most often jurisdictionally interstate due to the *de-minimus* rule of jurisdictional
2 classification of dedicated services. Second, pricing for special access services
3 approximates a true competitive outcome to a much greater degree than switched
4 access pricing. With switched access, only the carrier who provides the local loop
5 to the customer can terminate calls (and collect access charges) to that customer.
6 Consequently, the Commission's ability to revise special access rates in concert
7 with a switched access restructure without distorting special access rates and
8 competition appears limited.

9 **Q. DOES THAT CONCLUDE YOUR TESTIMONY, MR. GARRETT?**

10 **A.** Yes, it does.