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George Ripley
Manager - Regulatory Matters

April 24, 2000

Jerry L. Rudibaugh
Chief Hearing Officer
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

Dear Mr. Rudibaugh:

Re: Docket No. T-00000A-00-0194

Pursuant to the procedural order in the above referenced docket, enclosed please find one original and ten copies of U S WEST's direct testimony for Teresa K. Million to be presented at the hearing on May 11, 2000.

Please let me know if you have any questions.

Sincerely,



Enclosures



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Arizona Corporation Commission
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ARIZONA CORPORATION COMMISSION
REGULATORY MATTERS

BEFORE THE ARIZONA CORPORATION COMMISSION

**CARL J. KUNASEK
CHAIRMAN
JIM IRVIN
COMMISSIONER
WILLIAM A. MUNDELL
COMMISSIONER**

**IN THE MATTER OF INVESTIGATION INTO] DOCKET NO. T-00000A-00-0194
U S WEST COMMUNICATIONS, INC.'S]
COMPLIANCE WITH CERTAIN WHOLESAL]
PRICING REQUIREMENTS FOR UNBUNDLED]
NETWORK ELEMENTS AND RESALE]
DISCOUNTS.]**

TESTIMONY OF

TERESA K. MILLION

ON BEHALF OF

U S WEST COMMUNICATIONS

APRIL 24, 2000

TESTIMONY INDEX

	<u>Page</u>
I. IDENTIFICATION OF WITNESS.....	1
II. SUMMARY OF TESTIMONY	2
III. DEAVERAGING OF UNBUNDLED NETWORK ELEMENTS	4
IV. CONSISTENCY BETWEEN RETAIL AND WHOLESALE RATES	6
V. DEAVERAGED COST INFORMATION.....	10
VI. CONCLUSION.....	20

1

I. IDENTIFICATION OF WITNESS

2 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

3 A. My name is Teresa K. (Terri) Million. My business address is 1801 California
4 Street, Room 4450, Denver, Colorado 80202.

5 **Q. PLEASE IDENTIFY YOUR EMPLOYER AND EXPLAIN YOUR POSITION AND**
6 **RESPONSIBILITIES.**

7 A. I am employed by U S WEST Communications, Inc. (U S WEST) as a Director,
8 Cost Advocacy in the Retail Markets Organization. In this position, I am
9 responsible for preparing testimony and testifying about U S WEST's cost studies
10 in a variety of regulatory proceedings.

11 **Q. WHAT IS YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL**
12 **EXPERIENCE?**

13 A. I received a Juris Doctor from the University of Denver, College of Law and am
14 licensed to practice law in the state of Colorado. I also have a Master of
15 Business Administration from Creighton University and a degree in Animal
16 Science from the University of Arizona.

17 I have more than 16 years experience in the telecommunications industry with an
18 emphasis in tax and regulatory compliance. I began my career with
19 Northwestern Bell Telephone Company, now U S WEST Communications, in

1 1983, where I administered Shared Network Facilities Agreements with AT&T
2 that emanated from divestiture. I held a variety of positions within the
3 U S WEST, Inc. Tax Department over a period of ten years, including tax
4 accounting, audit, and state and federal tax research and planning
5 responsibilities. In 1997, I assumed a position that had responsibility for affiliate
6 transactions compliance, specifically compliance with Section 272 of the
7 Telecommunications Act of 1996 (the "Act"). In September 1999, I began my
8 current assignment as a Cost Witness.

9 **Q. HAVE YOU PREVIOUSLY TESTIFIED IN ARIZONA?**

10 **A.** Yes. I have provided testimony in Arizona regarding U S WEST's compliance
11 with Section 272 of the Telecommunications Act of 1996 in Docket No. T-
12 00000B-97-0238. I also provided Section 272 testimony in Colorado and
13 Nebraska. In addition, I have provided testimony in cost proceedings related to
14 operational support systems (OSS) in New Mexico and Washington, and
15 unbundled network element deaveraging in South Dakota.

16 **II. SUMMARY OF TESTIMONY**

17 **Q. PLEASE SUMMARIZE YOUR TESTIMONY.**

18 **A.** My testimony proposes a method of deaveraging for unbundled network
19 elements (UNEs) that provides for the geographic deaveraging of wholesale

1 rates into three cost-related, distance-based geographic zones. This proposal is
2 designed to comply with the Federal Communications Commission's (FCC's)
3 interconnection rules, 47 CFR § 51.507(f). Because of the strong connection of
4 wholesale rates to retail rates, this geographic proposal deaverages the
5 unbundled loop UNE in a manner consistent with the way retail basic exchange
6 prices are currently structured in Arizona.¹ It can be implemented within existing
7 service provisioning, customer billing and network management systems in
8 Arizona. Since the FCC requires deaveraging only to the extent that such a
9 deaveraging reflects *geographic cost differences*, U S WEST is not proposing to
10 deaverage the prices for any other UNEs.

¹ I have assumed the base rate areas with the expanded boundaries as recommended by David Teitzel in Docket No. T-1051B-99-105, see Teitzel Direct Testimony, filed January 8, 1999, page 42.

1 **III. DEAVERAGING OF UNBUNDLED NETWORK ELEMENTS**

2 **Q. PLEASE SUMMARIZE U S WEST'S PROPOSAL IN THIS PROCEEDING.**

3 A. U S WEST proposes to deaverage the price of the unbundled loop UNE into
4 three geographic zones, as I will describe below. This proposal deaverages the
5 unbundled loop in a manner that is consistent with the three-zone structure of
6 retail basic exchange prices in Arizona. U S WEST is not proposing to
7 deaverage the price for any other UNEs.

8 **Q. WHY IS U S WEST PROPOSING A PLAN FOR THE GEOGRAPHIC**
9 **DEAVERAGING OF THE UNBUNDLED LOOP AT THIS TIME?**

10 A. U S WEST is filing a plan for the geographic deaveraging of the unbundled loop
11 UNE in order to comply with the FCC's interconnection rules. This filing will also
12 meet the requirements outlined in the Arizona Corporation Commission's
13 procedural order in this docket dated March 30, 2000.

14 **Q. PLEASE BRIEFLY DESCRIBE THE FCC'S DEAVERAGING REQUIREMENT.**

15 A. In 1996, the FCC promulgated rules implementing and interpreting Section 251
16 of the Telecommunications Act of 1996. Rule 51.507(f) required each state
17 public utilities commission to establish different rates for unbundled network
18 elements in at least three geographic areas within the state to reflect geographic
19 cost differences. The Court of Appeals for the Eighth Circuit stayed and then

1 vacated the deaveraging rule. In January 1999, the United States Supreme
2 Court reversed that aspect of the Eighth Circuit's decision and reinstated Rule
3 51.507(f). On May 7, 1999, the FCC stayed the effectiveness of Rule 51.507(f)
4 in order to allow it to act on the issue of universal service. In its Universal
5 Service Order released November 2, 1999, the FCC lifted its stay of the rule and
6 stated that, by May 1, 2000, "states are required to establish different rates for
7 interconnection and UNEs in at least three geographic areas pursuant to section
8 51.507(f) of the Commission's rules."²

9 **Q. SHOULD THE COMMISSION CONSIDER THE GEOGRAPHIC**
10 **DEAVERAGING OF ANY OTHER UNES AT THIS TIME?**

11 A. No. Consistent with the FCC's rules, the Commission should consider
12 deaveraging of UNEs only to the extent that such deaveraging reflects
13 *geographic* cost differences. Therefore, the unbundled loop is the only UNE that
14 should be deaveraged because its costs vary between geographic areas based
15 on loop distances (i.e., between customer and central office) and the density of
16 the serving area. In contrast, the costs for many other unbundled network
17 elements, such as unbundled switching, do not vary significantly in a cost-
18 causative manner between geographical areas. If geography is not a cost driver,
19 there is no meaningful basis for geographic deaveraging. In addition, the costs
20 for other elements, such as unbundled transport, that vary due to distance are

² *In the Matter of the Federal-State Joint Board on Universal Service*, CC Docket 96-45, Ninth Report and Order and Eighteenth Order on Reconsideration, FCC 99-306, ¶ 120 (released Nov. 2, 1999).

1 already inherently geographically deaveraged with distance based rates. Thus, I
2 recommend that geographic deaveraging be limited to the unbundled loop UNE.

3 **IV. CONSISTENCY BETWEEN RETAIL AND WHOLESALE RATES**

4 **Q. DOES U S WEST BELIEVE THAT THE DEAVERAGING OF UNE RATES IS**
5 **INEXTRICABLY LINKED WITH THE DEAVERAGING OF RETAIL RATES?**

6 **A.** Yes. U S WEST believes that, ultimately, the deaveraging of wholesale rates
7 *drives* the deaveraging of retail rates. In a competitive environment retail rates
8 will necessarily be drawn toward the level of wholesale deaveraging. In other
9 words, where lower wholesale rates prevail, lower retail rates will prevail.
10 Conversely, where higher wholesale rates prevail, higher retail rates must follow.

11 Discrepancies between the retail and wholesale price structures undermine
12 competition and competitive neutrality. Otherwise, competitors could obtain
13 unbundled loops for low-cost urban business consumers at a deaveraged price,
14 and purchase high-cost longer loops at a non-deaveraged retail price less the
15 avoided cost discount. This presents an arbitrage opportunity for Competitive
16 Local Exchange Carriers (CLECs) that choose the economically more attractive
17 option of providing service to high-cost customers through resale. As the
18 Incumbent Local Exchange Carrier (ILEC), U S WEST would then be left with the
19 obligation of maintaining the more expensive loops without receiving offsetting
20 revenues of either higher averaged UNE loop prices or higher deaveraged retail

1 prices. Therefore, deaveraging of wholesale rates without the deaveraging of
2 retail rates is not consistent with the intent of Congress when it drafted the
3 Telecommunications Act. The intent of the Act is to encourage competition, and
4 the purpose of deaveraging is to facilitate retail competition that is based on the
5 underlying cost to provide service, *not* to encourage CLECs to engage in rate
6 arbitrage against ILECs.

7 **Q. IS IT NECESSARY TO DEAVERAGE RETAIL RATES ALONG WITH**
8 **WHOLESALE RATES IN ORDER TO MAINTAIN THE COMPETITIVE**
9 **NEUTRALITY OF UNE DEAVERAGING?**

10 **A.** Yes. Today, the majority of competition for basic exchange services in Arizona is
11 in the low-cost urban business areas, such as Phoenix and Tucson, not the high-
12 cost outlying areas of the state. This is not surprising because of the economic
13 opportunity that the current averaged rate retail structure provides. While retail
14 rates vary by exchange zones, U S WEST's retail rates are still averaged on a
15 statewide basis (e.g., the residence and business "base rate area" prices are the
16 same in Phoenix and Flagstaff). Despite the zone increment rate structure, high-
17 cost consumers still enjoy prices that are below the cost of providing service in
18 those areas. Thus, high-cost retail customers with longer loops receive a
19 subsidy from low-cost areas, and low-cost urban business customers in the base
20 rate area pay prices that are above their costs, helping to recover costs for high-
21 cost areas. This creates margin opportunities for the CLECs in low-cost urban
22 business areas because U S WEST's retail rates are higher than the costs to

1 provide the service. The result is that competitors flock to urban business areas,
2 where UNE rates are low and retail rates are high, while ignoring the remainder
3 of Arizona's consumers whose retail rates are low compared to their UNE rates.

4 For a deaveraging plan to work in a competitively neutral manner, competitors
5 would need to purchase unbundled network elements in all deaveraged areas.
6 That way, aggregate revenues derived from the sale of deaveraged UNEs would
7 be the same as the aggregate revenues derived based on the state-wide
8 average price. As noted above, if UNE rates increase in high-cost areas, but
9 U S WEST's retail rates remain the same, UNE based competition will be
10 discouraged in the high-cost areas of Arizona. This scenario is not deaveraging;
11 it is simply a UNE price decrease in low-cost urban business areas since only
12 deaveraged UNEs priced below U S WEST's retail rates are likely to be
13 purchased. When retail and wholesale prices are synchronized, UNE based
14 competition has a chance of happening because competitors will see opportunity
15 in urban business areas as well as higher-cost outlying areas. However, if retail
16 rates are not adjusted to reflect UNE rates U S WEST will, ultimately, be unable
17 to recover its costs as provided under the Telecommunications Act. In order to
18 avoid this competitively non-neutral outcome, retail and UNE rates must be
19 deaveraged on a consistent basis.

1 **Q. HAS THIS COMMISSION PREVIOUSLY CONCLUDED THAT THE**
2 **DEAVERAGING OF UNE AND RETAIL RATES SHOULD BE CARRIED OUT**
3 **TOGETHER?**

4 A. Yes. This Commission has previously recognized that UNE rates and retail
5 prices should be deaveraged in concert. Specifically, in Docket No. U-3021-96-
6 448 ET AL., at pp. 21-22 (January 30, 1998), the Commission concluded "we
7 share U S WEST's concerns that geographic deaveraging would need to occur
8 for U S WEST retail customers *at the same time* it occurs at the wholesale level."
9 (Emphasis added).

10 **Q. IS U S WEST LIKELY TO SEEK DEAVERAGING OF ITS RETAIL RATES?**

11 A. Yes. Because of the reasons explained above, U S WEST will be forced to seek
12 deaveraging of its retail rates in order to recover its cost of providing service in
13 high-cost areas. In addition, since those retail rates will necessarily reflect the
14 Commission's decision on UNE deaveraging, I would encourage the Commission
15 to consider the impact to consumers. This will avoid further compounding the
16 unequal balance of competitive choices for Arizona consumers and allow
17 deaveraging to be implemented on a competitively neutral basis.

V. DEAVERAGED COST INFORMATION

1
2
3

4 **Q. WHAT TYPE OF GEOGRAPHIC DEAVERAGING PLAN SHOULD BE**
5 **ADOPTED BY THE COMMISSION?**

6 **A.** As discussed above, U S WEST recommends that the Commission maintain a
7 consistent deaveraged rate structure for both wholesale and retail rates. In
8 Arizona, such a structure would result in three distance-based cost-related zones
9 as follows:

- 10 • Inside the Base Rate Area
- 11 • Outside the Base Rate Area – Zone 1
- 12 • Outside the Base Rate Area – Zone 2

13 This deaveraging structure – based on the base rate area and zone increments –
14 is consistent with the way retail services are currently provided in Arizona, and
15 includes the expanded base rate areas proposed by U S WEST in Docket No. T-
16 1051B-99-105. This structure is also similar to the way retail service prices and
17 unbundled loop UNE prices are deaveraged in other U S WEST states. For
18 example, both Colorado and Wyoming have retail rate structures that are based
19 on a base rate area and zone increments, although these states have three zone
20 increments as opposed to Arizona's two. As the following table shows, the
21 deaveraged UNE rates that have been approved in these states are similar to the
22 proposal in Arizona:

	<u>Zone</u>	<u>Arizona</u>	<u>Colorado</u>	<u>Wyoming</u>
1				
2	Base Rate Area	\$ 20.12	\$ 19.65	\$ 19.05
3	Zone 1	\$ 40.65	\$ 26.65	\$ 31.83
4	Zone 2 & 3	\$ 63.70	\$ 38.65 – \$ 84.65	\$ 40.11 – \$ 58.43

5 Since the U S WEST deaveraging plan is based on the currently proposed retail
6 rate structure it would be relatively simple to administer and could be
7 accomplished fairly quickly in Arizona. A UNE rate structure that is consistent
8 with the retail rate structure is easy for consumers to understand and can be
9 effectively communicated. In addition, the three-zone structure is compatible
10 with the current systems that U S WEST uses to provision service, bill
11 customers, and manage the network.

12 **Q. HOW WOULD UNBUNDLED LOOPS BE ASSIGNED TO THE THREE ZONES**
13 **UNDER U S WEST'S PROPOSAL?**

14 **A.** Unbundled loops would be assigned to the base rate area and the incremental
15 zones based on information derived from actual customer locations. In other
16 words, retail customers are assigned to zones based on actual locations and
17 unbundled loop UNEs would be assigned consistent with retail.

18

19

1 **Q. IS THE U S WEST DEAVERAGING PLAN COST-BASED?**

2 A. Yes. The U S WEST plan establishes three distance-based cost-related zones
3 that are structured consistently with the manner in which the costs of providing
4 the loop are incurred. Costs in three geographically similar areas have been
5 grouped together, and an average cost for each area developed (i.e., loop rates
6 for shorter loops inside the base rate area are based on lower costs, and longer
7 loops outside the base rate area are based on higher costs). FCC Rule 51.507(f)
8 does not require UNE wholesale rates to be set at a level exactly equal to cost,
9 but requires "cost-related" zones. Rule 51.507 states:

10 (f) State commissions shall establish different rates for elements in at
11 least three defined geographic areas within the state to reflect
12 geographic cost differences.

13 (1) To establish geographically-deaveraged rates, state commissions
14 may use existing density-related zone pricing plans described in §
15 69.123 of this chapter, **or other such cost-related zone plans**
16 **established pursuant to state law.** (Emphasis added).

17 (2) In states not using such existing plans, state commissions must
18 create a minimum of three cost-related rate zones.

19 Since, it would be impossible to set the price for each loop at its "true" or exact
20 cost (i.e., on an individual customer basis) any deaveraging plan will include
21 some averaging of prices at some level. The U S WEST proposal offers
22 unbundled loops at lower prices in the low-cost base rate areas, and higher
23 prices in the higher-cost zone increments. Thus, U S WEST's deaveraging plan

1 contains cost-related zones, consistent with the requirements of FCC Rule
2 51.507(f).

3 **Q. HOW WERE THE COSTS FOR THE THREE ZONES DETERMINED?**

4 A. Three distance-based zones were established that correlate to the retail zones
5 currently proposed in the Arizona rate case. The statewide average data was
6 segregated into separate files according to the three zones. Three separate runs
7 of the loop model were made, one for each zone. I have attached summaries of
8 this cost information in a confidential exhibit to this testimony (Exhibit TKM-1).
9 The investment components for the unbundled loop were determined for each
10 zone separately by the loop model. The loop (feeder, distribution, and drop)
11 investment was summed to achieve three levels of total investment, one for each
12 zone. Each zone investment was then compared to the statewide investment
13 data. A percentage was determined by dividing each zone investment by the
14 statewide average investment. These percentages were multiplied by the
15 statewide average unbundled loop price of \$21.98, as established in Docket No.
16 U-3021-96-448, ET AL., to determine the deaveraged price for each zone.

1 **Q. WHAT WERE THE RESULTS OF THESE CALCULATIONS?**

2 A. The investments and percentages of the statewide average for the three zones
3 are:

4	Base Rate Area	\$ 890.01	91.5%
5			
6	Zone 1	\$1,798.48	185.0%
7			
8	Zone 2	\$2,818.05	289.8%
9			
10	Statewide Average	\$972.34	
11			

12 **Q. WHAT ARE THE RATES DETERMINED BY THIS INFORMATION?**

13 A. The deaveraged unbundled loop cost/rates are:

14	Base Rate Area	\$20.12
15	Zone 1	\$40.65
16	Zone 2	\$63.70
17	Statewide Average	\$21.98

18

19 **Q. DOES THIS CALCULATION OF THE UNBUNDLED LOOP UNE RATE**
20 **INCLUDE WIRE CENTERS THAT U S WEST IS PROPOSING TO SELL IN**
21 **ARIZONA?**

22 A. Yes. I have included in the cost calculation of the unbundled loop UNE the wire
23 centers that U S WEST is proposing to sell in Arizona. The reason for this is that
24 the original calculation of the statewide average rate (i.e., \$21.98), that is the

1 basis for the proposed deaveraged rates, included those wire centers. In
2 addition, it is difficult to exclude wire centers from the calculation with certainty
3 until the sales of those wire centers have closed. As the Commission knows,
4 from a legal and regulatory perspective, U S WEST continues its responsibility
5 for those wire centers up until the time that legal ownership transfers to the
6 purchasing entity. Therefore, I believe that it is appropriate to include the wire
7 centers that are "for sale" in the calculation of the UNE loop rates.

8 Nevertheless, recognizing that under a TELRIC methodology one could argue
9 that wire centers that have been contracted for sale should be excluded from
10 forward-looking costs, I have also calculated the unbundled loop UNE with the
11 wire centers that are identified in the contract excluded. The impact on the UNE
12 loop rates was a slight increase in the base rate area, a slight decrease in Zone 1
13 and about a 5% decrease in Zone 2.

14 **Q. GIVEN THE EARLIER DISCUSSION REGARDING THE INEVITABLE**
15 **CONVERGENCE OF RETAIL AND WHOLESALE RATES, DOES U S WEST**
16 **HAVE ANY CONCERNS ABOUT ITS PROPOSED DEAVERAGED RATES?**

17 **A.** Yes. U S WEST has two related concerns that arise in the context of UNE
18 deaveraging. The first concern has to do with the erosion of implicit subsidies.
19 The second, related concern, has to do with the retail customer "rate shock" that
20 could result from the shift in the UNE loop rates from a statewide average to
21 deaveraged zones.

1 As implicit subsidies erode due to competition, they are replaced by rate
2 increases in high-cost areas and explicit subsidies such as universal service.
3 This is inevitable, and a result that was intended by the Telecom Act. Basic
4 exchange retail rates in Arizona currently range from \$32.78 in the base rate
5 area to \$35.78 in Zone 2 for business customers, and from \$13.18 to \$16.18 for
6 residential customers in those zones. In order for U S WEST to cover costs in a
7 competitive environment it is clear that, with the exception of the business rate in
8 the base rate area, retail prices are likely to increase for customers in the other
9 zones. This is especially true if, through convergence, the retail rates for
10 business customers inside the base rate area decrease.

11 U S WEST is currently involved in a rate case in Arizona and, as a result, has an
12 opportunity to seek increased retail rates that would reflect the deaveraged UNE
13 rates established in this proceeding. However, as stated above, U S WEST is
14 concerned with the "rate shock" to Arizona consumers that could result from
15 seeking significant rate increases in a short period of time in the high-cost zones.
16 Therefore, in order to avoid an outcome that would be unpleasant for consumers,
17 U S WEST will likely propose to increase retail basic exchange rates in steps or
18 phases over time. Fortunately, under the retail structure in Arizona, a little more
19 than 5% of consumers fall into Zones 1 and 2, while almost 95% of consumers
20 are located inside the base rate area. This is due primarily to the fact that the
21 vast majority of lines in Arizona are concentrated in dense metropolitan areas.

1 Therefore, only the small percentage of truly high-cost consumers with longer
2 loops could possibly, ultimately, be subject to higher retail rates under the
3 U S WEST proposal, depending on future universal service funding.

4 **Q. WHY IS U S WEST CONCERNED WITH THE EROSION OF IMPLICIT**
5 **SUBSIDIES?**

6 A. As described earlier in my testimony, UNE deaveraging that does not also take
7 into effect deaveraging of retail rates will necessarily result in a competitively
8 non-neutral outcome. Assuming wholesale rates are set at cost, any discrepancy
9 between wholesale rates and their retail counterparts represents an arbitrage
10 opportunity that undermines the current subsidy flow to high-cost areas. This is
11 because customers paying rates that are higher than the cost to serve them,
12 especially businesses, provide implicit subsidies that support services in high-
13 cost areas. (U S WEST currently charges only a maximum of \$16.18 per month
14 for residential service in areas where its deaveraged UNE rate would be \$63.70
15 based on cost to provide service). The revenue shortfalls that would result from
16 this upside-down rate structure are made up through implicit subsidies contained
17 in other rates, including the 1FB in the base rate area.

18 Competitors taking advantage of deaveraged unbundled network loop rates
19 could quite easily undercut U S WEST's basic business rate of \$32.78 in the
20 base rate area. U S WEST is then left with two choices: (1) reduce its retail rates
21 in order to provide a viable economic alternative to business customers, and thus

1 lose the implicit subsidy, or (2) do nothing and lose the customers providing the
2 implicit support through the business rate. In either case, the source of the
3 implicit subsidy disappears. Remember, competitors will not likely be serving
4 customers in high-cost areas, unless they do so at significantly below-cost rates
5 through a resale discount.

6 Implicit subsidies will erode away over time due to competition. Thus, as the
7 current implicit subsidies disappear, they must be replaced with rate increases or
8 explicit subsidies in high-cost areas. In order to remain financially viable in the
9 long run, a company must be able to cover its cost of providing service.

10 Therefore, any attempt to deaverage wholesale rates should contemplate similar
11 long-term revisions to the retail rate structure (i.e., increases in rates in higher
12 cost areas) in order to replace the implicit subsidies that will be lost.

13 **Q. ARE THERE OTHER METHODS OF UNE DEAVERAGING THAT COULD BE**
14 **SELECTED IN ARIZONA?**

15 **A.** Yes. Although, there are several alternative methods of deaveraging, none of
16 those methods fit the unique circumstances in Arizona as well as the zone
17 increments I am proposing here. For example, U S WEST has proposed a
18 different base rate area and zone increment approach in Montana and Nebraska.
19 That approach recommends deaveraging of the UNE loop in the same
20 increments as exist in the retail rates. However, by virtue of the rate case,

1 U S WEST's retail rates are unsettled in Arizona. Therefore, that option was
2 foreclosed.

3 In addition, there are methods of deaveraging UNE loops by the aggregation of
4 wire centers. Under those methods, U S WEST typically proposes a
5 Metropolitan Statistical Area (MSA) approach. This method groups wire center
6 costs based on "communities-of-interest." It has been proposed to establish
7 cost-related UNE rates in states such as North Dakota and South Dakota. This
8 method is consistent with the way retail rates are structured in these states and
9 makes sense in states whose retail rates are consistent with a wire center
10 approach.

11 Alternatively, wire centers can be aggregated strictly on the basis of relative
12 costs. This is the least practical method of determining rates, particularly in
13 Arizona. It is a method that results in a hodge-podge of wire centers being
14 grouped together with no relationship between wholesale rates and the retail
15 consumers being served. Remember, there is a potential for arbitrage and a
16 competitively non-neutral outcome where discrepancies exist between wholesale
17 and retail rates. Further, if averaged wire center costs are used to determine
18 deaveraged zones many consumers who reside in the base rate area under
19 Arizona's retail structure will find themselves in a high-cost zone from a
20 wholesale perspective. When retail and wholesale rates converge, this will result
21 in far more than 5% of consumers being impacted by significantly higher rates.

1 **VI. CONCLUSION**

2 **Q. WHAT IS YOUR RECOMMENDATION?**

3 A. I recommend that the unbundled loop UNE be deaveraged using U S WEST's
4 proposal. The deaveraging proposal I have submitted is consistent with the
5 manner in which retail rates are structured and can be easily implemented. The
6 structure of the deaveraged rates is similar to permanent decisions made by two
7 other states in U S WEST's territory, Colorado and Wyoming. It meets the FCC's
8 requirement of three cost-related geographic areas and is based on the
9 statewide average loop rate determined by the Commission. I urge the
10 Commission to adopt this proposal.

11 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

12 A. Yes, it does.

BEFORE THE ARIZONA CORPORATION COMMISSION

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CONFIDENTIAL EXHIBITS OF

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ON BEHALF OF

U S WEST COMMUNICATIONS

APRIL 24, 2000

EXHIBITS INDEX

DESCRIPTION

EXHIBIT

Deaveraged Unbundled Loop Calculations

Confidential TKM-1

U S WEST Communications

Arizona

Deaveraged Unbundled Loop Calculations

REDACTED

BEFORE THE ARIZONA CORPORATION COMMISSION

CARL J. KUNASEK
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STATE OF COLORADO

COUNTY OF DENVER

DOCKET NO. T-00000A-00-0194

AFFIDAVIT OF
TERESA K. MILLION

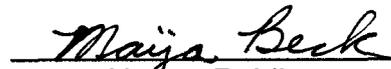
SS

Teresa K. Million, of lawful age being first duly sworn, deposes and states:

1. My name is Teresa K. Million. I am Director-Cost Advocacy in the Retail Markets Organization of U S WEST Communications in Denver, Colorado.
2. I hereby swear and affirm that my answers contained in the attached testimony to the questions therein propounded are true and correct to the best of my knowledge and belief.


Teresa K. Million

SUBSCRIBED AND SWORN to before me this 19 day of, April 2000.


Notary Public

My Commission Expires:

May 8, 2000