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Arizona Corporation Commission

BEFORE THE ARIZONA CORPORATION COMMISSION

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DEC 13 1996

1 RENZ JENNINGS
2 CHAIRMAN
3 MARCIA WEEKS
4 COMMISSIONER
5 CARL J. KUNASEK
6 COMMISSIONER

DOCKETED BY

6 IN THE MATTER OF THE
7 PETITION OF MCIMETRO ACCESS
8 TRANSMISSION SERVICES,
9 INC., FOR ARBITRATION OF
10 INTERCONNECTION RATES,
11 TERMS, AND CONDITIONS
12 PURSUANT TO 47 U.S.C.
13 § 252(b) OF THE
14 TELECOMMUNICATIONS ACT OF
15 1996.

DOCKET NO. U-3175-96-479
DOCKET NO. E-1051-96-479

U S WEST COMMUNICATIONS,
INC.'S EXCEPTIONS TO
RECOMMENDED OPINION AND
ORDER

12 I. INTRODUCTION

13 U S WEST Communications, Inc. ("USWC") files these exceptions
14 to the recommendations of the Arbitrators issued on December 4, 1996
15 (the "Recommended Order"). Sections 252(b)(4)(c) and 252(c) of the
16 Telecommunications Act of 1996 (the "Act") require the Arizona
17 Corporation Commission (the "Commission") as the arbitrator to
18 resolve open issues, including the establishment of rates and
19 charges for interconnection and unbundled elements.

20 The Commission must address the following issues in its final
21 order. First, the Commission should establish the levels of
22 reciprocal compensation paid by USWC and MCI for call termination
23 and reject the use of bill and keep as an interim solution.
24 Alternatively, the Commission should require that any use of bill
25 and keep be subject to a true-up at the end of the bill and keep
26 period if traffic was out-of-balance during that period. The FCC

1 Rules provide for adoption of a true-up mechanism where bill and
2 keep is adopted. See FCC First Order ¶ 1114. Second, the
3 Commission should determine that the interim rate for unbundled
4 loops and other unbundled elements should be set at the USWC-
5 proposed TELRIC-based prices. Since the Eighth Circuit Court of
6 Appeals has stayed the FCC pricing provisions, the Commission may
7 not apply the FCC proxy rate for interconnection and unbundled
8 elements. Because Section 252(d) of the Act requires the Commission
9 to determine just and reasonable rates for interconnection and
10 unbundled elements based on the cost of their provision, the
11 Commission should adopt USWC's cost-based pricing proposals, the
12 only cost-based proposals supported by credible evidence in the
13 record. Second, the Commission should determine what services may
14 be purchased from USWC at wholesale prices and resold by MCI Metro
15 Access Transmission Services, Inc. ("MCI"). The Commission must
16 also determine the appropriate interim wholesale discount for resold
17 services. Because Section 252(d)(3) of the Act requires the
18 Commission to determine wholesale rates based on "costs that will be
19 avoided by the local exchange carrier" and the only credible
20 evidence in the record of the avoided costs is contained in the USWC
21 cost studies and the testimony of Ms. Santos-Rach, the Commission
22 must adopt USWC's proposed wholesale discounts. Third, the
23 Commission should not permit sham unbundling which will signifi-
24 cantly erode the development of facilities-based competition and
25 undercut the role of legitimate resale in Arizona. Fourth, the
26 Commission should permit USWC to charge MCI cash in advance for

1 special construction of any facilities by USWC specifically to serve
2 MCI.

3 As will be more fully described hereafter, USWC takes exception
4 to several of the findings and rulings in the Recommended Order. If
5 adopted, these rulings will cause substantial prejudice and harm to
6 USWC in the following ways:

7 1. The rates proposed by the Arbitrators will not allow USWC
8 to recover the cost of providing the services. Therefore, the
9 Recommended Order, if adopted by the Commission, will consti-
10 tute a confiscatory taking under the 5th and 14th Amendments to
11 the United States Constitution and Article II, Section 4 of the
12 Arizona Constitution.

13 2. By not allowing USWC to recover the cost of providing the
14 services or in not providing a mechanism for the recovery of
15 certain costs, the Recommended Order is inconsistent with the
16 provisions of the Act. Therefore, the Recommended Order, if
17 adopted, would directly violate the statutes governing the
18 Commission's actions in this matter and would be in excess of
19 the Commission's authority. As such, the Commission's actions
20 would be contrary to law.

21 3. In several instances, the findings in the Recommended
22 Order are not based on substantial evidence in the whole record
23 before the Arbitrators and the Commission. To the contrary,
24 the substantial evidence in the record would mandate that the
25 Commission find that proposals made by USWC must be adopted as
26 fair and reasonable.

4. The scope of the Commission's authority to arbitrate
issues is limited by Section 252(c) to those open issues to (i)
ensure compliance with Section 251 and the FCC regulations, and
(ii) establish rates pursuant to Section 252(d) and to provide
a schedule for implementation. No other authority is granted
to the Arbitrators by the Act. Thus, where the parties have
not agreed on contract provisions, such as those involving
indemnity or limitation of liability, the Commission may not
impose these provisions in its final order because to do so
would exceed the scope of the Commission's authority under the
Act.

5. If adopted, the provisions of the Recommended Order
challenged hereafter, would be arbitrary, capricious, an abuse
of discretion and in violation of the Act.

1 II. EXCEPTIONS

2 A. RECIPROCAL COMPENSATION

3 The Act requires that, in order for rates to be just and
4 reasonable, reciprocal compensation must "provide for the mutual and
5 reciprocal recovery by each carrier of costs associated with
6 transport and termination." Act § 252(d)(2)(A)(i). The FCC has
7 determined that for shared transmission facilities between tandem
8 switches and end offices, states may establish usage-sensitive or
9 flat-rate charges to recover those costs. The states may further
10 use, as a default proxy, the rate derived from the incumbent LEC's
11 interstate direct-trunked transport rates in the same manner that
12 the FCC derives presumptive price caps for tandem switched transport
13 under the interstate price cap rules. (FCC First Order ¶ 822). The
14 FCC has also determined that a bill and keep arrangement is
15 appropriate only when rates are symmetrical and traffic is in
16 balance, a situation not likely to occur in Arizona. (FCC First
17 Order ¶ 1111; see also, A.A.C. Rule R14-2-1304). Nonetheless, the
18 Recommended Order adopts bill and keep for two years from the date
19 an agreement is approved.

20 Until MCI can directly trunk to each end office over its
21 facilities, MCI's exchange of traffic with USWC will necessarily
22 impose additional costs on USWC. The existing USWC network routes
23 traffic directly from end office to end office through the use of
24 direct trunks. Traffic during unusual calling patterns or peak
25 usage periods may overflow to the local tandem switches. MCI would
26 use trunks to the tandem not as overflow routers, but rather as

1 primary call routers, causing USWC to add capacity to its tandem
2 switches and tandem transport facilities to accommodate the
3 increased traffic. This will result in USWC's cost of terminating
4 MCI's traffic exceeding MCI's cost of terminating USWC's traffic,
5 even if the volume were the same. Further, traffic that has
6 historically been intraoffice in nature (e.g., calls between
7 neighbors served by the same USWC central office) will be converted
8 to interoffice (e.g., calls between a USWC end office and an
9 interconnector's end office), representing an increased traffic load
10 on the USWC interoffice transport network. Under the Act, USWC must
11 be allowed to recover the costs of this transport. Bill and keep
12 does not allow USWC to recover these costs. Even if the minutes of
13 use balance, the cost of each minute will differ and thus the costs
14 will not balance.

15 1. Bill and Keep

16 Bill and keep is also inappropriate because it does not permit
17 USWC to recover the cost of terminating MCI's traffic. Any
18 assumption that USWC's terminating traffic and MCI's terminating
19 traffic would be in balance or that USWC's cost of terminating calls
20 is the same as MCI's, which are key assumptions under any bill and
21 keep system, is patently unreasonable. Because MCI can choose to
22 target particular types of customers (such as businesses), and
23 because different customers have different patterns of originating
24 and terminating traffic, traffic is not likely to be in balance
25 between USWC and MCI. Given the different network architectures,
26 the cost of termination for each of the carriers will not be the

1 same.

2 Further, MCI is not required to and cannot provide ubiquitous
3 service on its network. The difference in size of networks and
4 number of customers served by the networks will create an imbalance
5 in both traffic and the cost of termination. Because bill and keep
6 will prevent USWC from recovering its real cost of terminating MCI's
7 traffic, it will inevitably result in under-recovery by USWC and is,
8 therefore, confiscatory.

9 Other commissions have rejected bill and keep for a number of
10 compelling reasons in addition to its unwarranted assumption that
11 traffic will inevitably balance. First, these commissions have
12 recognized that bill and keep does not reflect the different costs
13 of the respective networks of the LECs and the new entrants.
14 Second, bill and keep creates the opportunity for new entrants to
15 shift costs to the LECs through selection of meet points. Third,
16 bill and keep assumes that costs will be equal and does not
17 recognize the additional cost incurred by LECs in providing
18 transport. The Recommend Order's adoption of bill and keep should
19 be rejected, and USWC's rates for call transit, transport and
20 termination should be adopted instead.

21 At a minimum, the Recommended Order should be amended to
22 provide that bill and keep is subject to a true-up at the end of the
23 interim period during which it is in effect. Otherwise, the interim
24 implementation of bill and keep will result in USWC not recovering
25 its costs of terminating traffic for the period bill and keep is in
26 effect and will result in the illegal confiscation of USWC's

1 property. The FCC First Order also interprets the Act to allow
2 commissions to adopt true-ups in connection with bill and keep. The
3 Commission, therefore, cannot simply rely on the absence of a true-
4 up mechanism in its Rules, but not consider whether such a true-up
5 is appropriate under the evidence in the record.

6 USWC recommends that page 10, line 12 through line 16 of the
7 Recommended Order be deleted and replaced with the following
8 language:

9 The Commission adopts reciprocal compensation.

10 **2. Interconnection**

11 The Recommended Order permits MCI to select a single point of
12 interconnection in each LATA. Establishing a single POI per LATA
13 will lead to inefficient engineering of the network and will impose
14 significant additional costs on USWC, who will have to back haul
15 traffic from the single point of interconnection if and when MCI
16 chooses to offer facilities-based local service outside the Phoenix
17 calling area. To discourage the establishment of inefficient POIs,
18 USWC should be permitted to charge construction costs to MCI if MCI
19 chooses a point of interconnection that requires USWC to construct
20 additional facilities to carry MCI's traffic.

21 Because the Recommended Order has adopted bill and keep, USWC
22 cannot recover the additional costs of hauling this traffic.
23 Further, the Recommended Order permits MCI to interconnect at USWC's
24 access tandem. This will further increase the costs that USWC
25 cannot recover. The Recommended Order should be amended to require
26 MCI to establish one point of interconnection per local calling area

1 at a place agreed upon by the parties. Alternatively, MCI should,
2 at a minimum, establish its local point of interconnection at Points
3 of Presence in Arizona for the provision of long distance service.

4 Additionally, MCI's switch should be treated as an end office
5 switch rather than a tandem switch for call termination rates for
6 reciprocal compensation. MCI's switch will serve only a very small
7 portion of the Tucson LATA and Tucson calling area -- only 75-100
8 square miles out of a much larger area serviced by USWC's local
9 tandem, let alone its toll tandem. Tr. 175-79 (Mason), Tr. 148
10 (Wiseman). MCI will be connected to only six or seven of the 18 end
11 offices that serve USWC customers. Tr. 148-49 (Wiseman); Tr. 68,
12 203-04 (Johnson). MCI will depend heavily upon USWC's tandem to
13 complete calls to customers in the offices to which it is not
14 directly connected. Tr. 148-49 (Wiseman). It will serve only a
15 small percentage of the 420,000 access lines served by USWC in the
16 Tucson metro area. Tr. 148 (Wiseman); Tr. 184 (Mason).

17 MCI's switch does not serve the same geographic area and
18 provide the same tandem switching functions as USWC's tandem. MCI's
19 switch is much more equivalent to MFS's switch, which the Commission
20 treated as an end office switch, then TCG's switch, which it treated
21 as a tandem switch. Compare MFS Order at 6-7 to TCG Order at 9-10.
22 Accordingly, MCI's switch ought to be treated as an end office
23 switch rather than a tandem switch, see FCC First Order ¶ 1090, and
24 USWC should not pay tandem rates for its use. USWC Ex. 1 at 85-86
25 (Mason); USWC Ex. 2 at 68-70 (Harris). Using USWC's facilities to
26 reach customers simply does not meet the coverage and function test

1 established by the FCC. If the Commission rules that MCI's switch
2 is a tandem, it should also rule that MCI is a facilities-based
3 carrier under § 271 of the Act and USWC will submit this agreement
4 in conjunction with its application for entry into the interLATA
5 market.

6 In the event that the Commission adopts bill and keep on an
7 interim basis, USWC suggests that the Commission treat MCI's switch
8 as an end office switch, also on an interim basis. Such interim
9 treatment is particularly appropriate here because MCI is seeking to
10 have its switch treated as a tandem switch not on the basis of its
11 facilities as they exist now but rather as it hopes to build them.
12 The Commission should wait until MCI actually builds these
13 facilities and the Commission implements a compensation system other
14 than bill and keep before making a final determination concerning
15 MCI's switch.

16 USWC opposes bill and keep for any reciprocal compensation.
17 USWC Ex. 1 at 68-86 (Mason). As Dr. Harris explained, bill and keep
18 encourages economic inefficiencies, even cherry-picking, and is not
19 used in any other industries. USWC Ex. 2 at 65-68 (Harris). At the
20 very least, if traffic is out of balance, as it plainly will be, Tr.
21 173 (Mason), there should be a true up and, as the Commission
22 ordered in the TCG arbitration, either party should be permitted to
23 seek termination of the bill-and-keep mechanism. TCG Order, at 9.

24 USWC recommends that page 5, line 21 through page 6, line 4 of
25 the Recommended Order be deleted and replaced with the following
26 language:

1 Evidence was presented that the MCI switch does not function
2 as, nor cost the same as, a tandem switch. The network and
3 switch have the scope of an end office. U S WEST would not
4 receive the service equivalent of tandem functionality when it
5 would hook up with MCI's network. The network provides no
6 extra trunking or efficient service of an area. U S WEST does
7 not save use of its tandem switch or reduce its capacity needs
8 by use of MCI's switch. We therefore agree with U S WEST that
9 for the purposes of call termination, the initial MCI switch
10 should be treated as an end office switch.

11 **B. DARK FIBER**

12 The Recommended Decision's resolution of the Dark Fiber issue
13 does not adopt either the position of USWC or MCI. While USWC
14 believes that the evidence presented at the hearing compels the
15 conclusion that USWC need not and should not be required to unbundle
16 dark fiber, with one significant exception, the resolution achieved
17 in the Recommended Order is a reasonable balancing of the interests
18 of the parties so long as the requirement contained in the
19 Recommended Order that access to dark fiber be reciprocal is
20 continued.

21 In addition, the reciprocity requirement in the Recommended
22 Order is not effective until "such time as all CLECS in U S WEST's
23 service territory reach a combined total of 200,000 access lines."
24 Recommended Order at 8. By imposing the 200,000 line minimum, the
25 Recommended Order misapplies A.A.C. R14-2-1307. The rule was
26 designed to require that small LECs with less than 200,000 access
lines be exempt from the unbundling requirements in the rules which
did not anticipate unbundling of dark fiber. It was intended to
create an exemption for small carriers who would never reach such a
capacity, and not to create a cushion for large carriers like MCI.

1 Indeed, based on the evidence at the hearing, MCI may well have more
2 dark fiber than USWC. (Tr. 620) (Powers).

3 If MCI challenges the reciprocity requirement either before the
4 Commission or in court and that requirement is eliminated, the
5 Commission should eliminate any requirement that USWC make dark
6 fiber available to MCI or other CLECs.

7 USWC recommends that page 8, line 13 through page 9, line 8 of
8 the Recommended Order be deleted and replaced with the following
9 language:

10 In Para. 450, the FCC ruled that a sufficient record did not
11 exist upon which to determine whether dark fiber qualified as
12 a network element under Sections 251(c)(3) and 251(d)(2) of the
13 Act. The FCC did not leave the dark fiber issue open to state
14 commissions. In addition, the evidence presented in this
Docket establishes that dark fiber is not a network element
subject to the terms of the Act. Therefore, we will not
require U S WEST to offer dark fiber as an unbundled element.

15 Alternatively, USWC recommends that the sentence appearing on page
16 8, line 25 through line 27 of the Recommended Order be replaced with
17 the following language:

18 If MCI requests dark fiber, it must be willing to make a
19 comparable amount of its dark fiber available on a reciprocal
basis.

20 **C. UNBUNDLED LOOP AND OTHER ELEMENT PRICES**

21 The Recommended Order proposes an interim unbundled loop price
22 of \$21.76 by averaging USWC's proposed unbundled loop price of
23 \$30.67 and the FCC proxy price of \$12.85. It also determines the
24 rate for other unbundled elements not on the basis of cost but on
25 the rates established in the MFS and TCG orders. Section 252(d) of
26 the Act requires the Commission acting as arbitrator to determine

1 just and reasonable rates for interconnection and unbundled elements
2 -- "based on the cost" of their provision. The recommended rates
3 are not cost-based because they simply average USWC's proposed rates
4 and the FCC proxies. Averaging of proposed prices violates the
5 "cost-based" requirement in Section 252(d).¹ The Commission should
6 reject the Recommended Order's unbundled loop price of \$21.76 and
7 adopt USWC's proposed price for the unbundled loop and other
8 elements. Because the Eighth Circuit has stayed the FCC's pricing
9 rules, including the FCC's establishment of so-called "proxy
10 prices", the Commission may not use the proxy prices to set rates or
11 to average against USWC's cost-based prices. To the extent that the
12 Recommended Order leaves these pricing issues for resolution
13 following a later generic proceeding, it is inconsistent with the
14 Act and should not be accepted by the Commission. Therefore, the
15 Commission should reject the Recommended Order and adopt an
16 unbundled loop price of \$30.67 based on USWC's cost studies. The
17 adoption of a rate less than the proposed USWC rate would be
18 inconsistent with the mandate of the Act and constitute an illegal
19 taking of USWC's property.

20 USWC's proposed unbundled loop price and prices for other
21 unbundled elements are based on a Total Element Long Run Incremental
22 Cost ("TELRIC") study as testified to by Ms. Santos-Rach. USWC's
23 studies and prices are specifically tailored to Arizona and provide
24 a realistic estimate of the forward-looking costs of building a
25

26 ¹ Moreover, the rates are not based on substantial evidence in
the record.

1 network in this state. AT&T has been reviewing and verifying this
2 publicly available model in Utah since mid-1996. In sharp contrast,
3 the cost studies submitted by MCI rely almost exclusively on
4 national, unverifiable data and fail to take into account conditions
5 unique to Arizona.

6 Dr. Harris explained that USWC's cost model uses its actual
7 experiences in building a network in Arizona and elsewhere to
8 project forward-looking costs. Dr. Harris worked closely with USWC
9 employees over the past year to ensure that the assumptions and
10 values in the model follow actual experience and the field
11 conditions that would exist if a new entrant were to build a
12 network.

13 USWC issued requests for proposals ("RFPs") to construct out-
14 side plants that would provide complete telephone service. USWC
15 issued these RFPs to compare the bids that USWC received against the
16 cost results of USWC's model. Responsive bids almost equaled the
17 same cost per line calculations produced by the USWC model,
18 confirming the model's reliability.

19 The painstaking process USWC followed to construct and verify
20 its cost study resulted in a model that estimates forward-looking
21 costs realistically and reliably. The model uses fill factors that
22 follow USWC's actual experience in Arizona and that take into
23 account its legal obligations to provide service upon demand and to
24 serve as the carrier of last resort. Similarly, the model reflects
25 USWC's actual experience in Arizona relating to sharing with other
26 utility companies the cost of installing cable and building

1 structures.

2 MCI's proffered evidence based on the Hatfield model does not
3 constitute substantial evidence to support the interim rates in the
4 Recommended Order. The Hatfield model stands in sharp contrast to
5 the USWC cost model; it uses a myriad of insupportable, unrealistic
6 assumptions that artificially depress the costs of building a new
7 network. There is no evidence substantiating the engineering
8 assumptions and inputs within the Hatfield model. Despite MCI's
9 claims, the model is not publicly available and cannot be verified
10 because the inputs remain secret or rest on the judgment of Hatfield
11 employees and consultants.

12 First, the model assumes that a carrier building a new network
13 would share the costs of building and installing much of the network
14 -- cables, conduits, and poles -- with other utilities, so that the
15 carrier would only have to bear one-third of these costs. This
16 assumption reduces the results produced by the Hatfield model,
17 because the costs of building facilities and structures are a
18 substantial percentage of the overall costs of building a new
19 network. USWC's actual experience in Arizona demonstrates that
20 cost-sharing among utilities typically occurs only when cable and
21 other structures are installed in new housing developments.

22 Second, the Hatfield model uses unrealistic fill factors do not
23 account for the immediate ready-to-serve obligations that Arizona
24 law imposes on USWC, and are not achievable by any local exchange
25 carrier. In practice, efficient carriers routinely lay excess cable
26 in anticipation of future growth because it is significantly less

1 costly to do so than to retrench and add additional cable to
2 accommodate increased demand. Even MCI recognizes this practice as
3 cost-efficient and reasonable.

4 Third, the Hatfield model uses unrealistic assumptions about
5 the existing field conditions under which a carrier would have to
6 build a new network. The Hatfield model fails to account for the
7 higher costs required to install conduits and cables in populated
8 areas, in order to dig up and repair roads, lawns, and gardens.

9 Additional flaws in the Hatfield model include the following:

10 Capital costs -- estimated at 10.24% -- are not forward-
11 looking, are not based upon actual conditions prevailing in
12 debt and equity markets, and do not account for the increased
13 risks USWC faces in a competitive environment;

14 The model assumes a uniform depth for trenches of one foot,
15 failing to recognize that deeper trenching -- and higher
16 trenching costs -- often is called for by soil conditions and
17 local regulation; and

18 The model fails to use forward-looking economic depreciation
19 lives, using, for example, a life of 15 years for digital and
20 office switching, even though MCI itself uses a 9.7 year life
21 for digital switching.

22 In sum, as these fundamental flaws demonstrate, the Hatfield
23 model does not provide a realistic estimate of the costs of building
24 a network. USWC's TELRIC estimates are far more realistic and
25 reliable. Accordingly, the Commission should adopt USWC's proposed
26 price of \$30.67 for an unbundled loop as the interim rate, subject
27 to true-up. USWC recommends that page 27, line 12 through line 19
28 of the Recommended Order be deleted and replaced with the following
29 language:

30 The Commission adopts the proposed TELRIC price of \$30.67 for
31 an unbundled loop, subject to true-up.

1 D. COMBINATION OF UNBUNDLED ELEMENTS ("SHAM UNBUNDLING")

2 The Recommended Order would allow carriers, such as MCI, to
3 purchase unbundled elements and combine them into a service to be
4 offered for resale. The ability to combine unbundled elements and
5 offer the service for resale in this fashion is known as "sham
6 unbundling." Sham unbundling will lead to severe rate arbitrage
7 between resale prices and unbundled element prices. To prevent rate
8 arbitrage, sham unbundling should not be permitted until USWC has
9 been allowed to re-balance its retail rates.

10 Under the Recommended Order, MCI could purchase the equivalent
11 of a "finished" service solely through the purchase of unbundled
12 network elements at "cost-based" rates. Thus, MCI can order USWC to
13 provide a finished retail service at a cheaper price than the Act's
14 resale price (retail less cost avoided) by utilizing the fiction
15 that MCI is buying unbundled network elements -- when in reality
16 there is no unbundling involved. In this manner, MCI can completely
17 circumvent the resale provisions of the Act - engaging in "sham"
18 unbundling.

19 In effect, sham unbundling upsets the balance between resale
20 and unbundling that was established in the Act. Congress realized
21 that both unbundling and resale are critical to the development of
22 meaningful competition. It therefore crafted a carefully balanced
23 mechanism to allow new entrants to enter local markets rapidly,
24 through resale, while developing their facilities-based networks
25 with the purchase of unbundled network elements from incumbent LECs.
26 The Recommended Order misapplies the Act and is inconsistent with

1 it.

2 Congress also realized that the state commissions have set
3 prices for some retail services to include large contributions to
4 help support residence basic exchange service. Therefore, Congress
5 defined "margin neutral" resale rules in §§251(c) and 252(d)(3) of
6 the Act to allow the purchase of retail services by resellers at
7 wholesale rates, based on the retail price less avoided costs.
8 Thus, the margins that existed for these retail services and the
9 contributions to other services would be preserved.

10 In summary, sham unbundling allows new entrants to arbitrage
11 the resale of local exchange service and violates the objectives of
12 the Act. The overwhelming weight of the evidence mandates that the
13 Commission modify the Recommended Order to prohibit sham unbundling
14 and there is no substantial evidence to support the adoption of sham
15 unbundling. USWC recommends that page 11, line 6 through line 13 of
16 the Recommended Order be deleted and replaced with the following
17 language:

18 The Commission will allow carriers to purchase unbundled
19 elements from U S WEST for use in conjunction with their own
20 facilities or facilities leased from a third party; however,
21 these carriers are prohibited from recombining any unbundled
22 elements purchased from U S WEST into a "finished" service or
23 product which MCI could obtain from U S WEST on a resale basis.

24 Alternatively, USWC recommends that page 11, line 6 through
25 line 13 of the Recommended Order be deleted and replaced with the
26 following language:

27 At the present time, the Commission will allow carriers to
28 purchase unbundled elements from U S WEST for use in
29 conjunction with their own facilities or facilities leased
30 from a third party; however, these carriers are prohibited

1 from recombining any unbundled elements purchased from
2 U S WEST into a "finished" service or product which MCI
3 could obtain from USWC on a resale basis until U S WEST's
4 retail rates are rebalanced by this Commission.

4 **E. RESALE**

5 **1. Resale Wholesale Rates.**

6 The Recommended Order adopts a discount rate of 17%, the low
7 end of the FCC proxy price range. The Eighth Circuit stay precludes
8 the Commission's reliance on the proxy discounts. Section 252(d)(3)
9 of the Act requires the Commission as arbitrator to determine
10 wholesale rates "on the basis of retail rates ... excluding the
11 portion thereof attributable to ... costs that will be avoided by
12 the local exchange carrier." (Emphasis added). Thus, the discount
13 price for resale services should be set at USWC's retail rate for
14 the relevant service less USWC's avoided cost.

15 Again, the only credible evidence of avoided costs introduced
16 by either party was USWC's avoided cost study and Ms. Santos-Rach's
17 testimony concerning that study. USWC's study sets proposed
18 wholesale rates that accurately reflect the costs USWC will
19 eventually avoid in a wholesale setting. To calculate these rates,
20 USWC formulated six product categories, identified all retail
21 elements included in offering each product, and determined the
22 TELRIC for each element that will be avoided when USWC offers the
23 service for resale. USWC also identified the portion of shared
24 costs that would be avoided for the wholesale products in each
25 category. USWC's calculation of "avoidable" costs also includes a
26 prorated share of common costs. Through this methodology, USWC has

1 calculated discount rates that realistically reflect avoidable
2 costs, which range from 0-9% depending on the service. Rather than
3 adopting a point in the FCC proxy range, the Commission should adopt
4 cost-based rates.

5 MCI's "simplified" avoided cost study does not provide
6 substantial evidence to support the Recommended Order. MCI's
7 so-called "simplified" avoided cost study proposes a wholesale
8 discount of 22% for all services. The study dramatically overstates
9 the costs USWC would avoid in providing service to a reseller
10 instead of an end customer.

11 First, under the Act, avoided costs are "marketing, billing,
12 collection, and other costs that will be avoided by the local
13 exchange carrier" if it provides service on a wholesale, rather than
14 retail basis. The avoided costs must be calculated on a net basis,
15 adding back the additional marketing costs of serving resellers.
16 The FCC has endorsed this "net" approach, acknowledging that some
17 new expenses may be incurred in addressing the needs of resellers as
18 customers. FCC First Order at ¶ 911. Hence, in calculating avoided
19 costs, these additional costs should be considered.

20 However, MCI's study subtracts avoided retail costs from the
21 retail price, but it does not add in the wholesaling costs USWC will
22 incur. This approach conflicts directly with the Act and ensures
23 that any discount rate MCI proposes will be grossly inflated. The
24 MCI study also provides no basis to support its discount for repair
25 and maintenance and uses an improper denominator that excludes
26 intrastate access, thus overstating the discount.

1 Second, MCI's study improperly assumes that USWC will have no
2 marketing or billing expenses in providing services to resellers.
3 Although USWC may eliminate some marketing expenses, significant
4 marketing and other expenses will remain: USWC employees still must
5 interact with resellers, provide customer service, process service
6 orders, and maintain customer service needs. MCI also assumes that
7 USWC will completely avoid product management expenses, but ignores
8 that the product management services USWC provides are required
9 regardless of whether the service is provided on a retail or
10 wholesale basis. With respect to billing expenses, how could MCI
11 assume that USWC will avoid these expenses when selling wholesale?
12 USWC will bill for the exact same facilities it provides, whether on
13 a retail or wholesale basis, and it will continue to incur real
14 costs in doing so.

15 USWC recommends that page 26, line 26 through page 27, line 4
16 of the Recommended Order be deleted and replaced with the following
17 language:

18 The FCC Order, permitting state commissions to establish
19 interim resale discounts of 17 to 25 percent has been stayed.
20 Based on all the evidence presented, we find wholesale
21 discounts ranging from 1.01 to 8.17 percent as requested by
22 U S WEST to be just and reasonable as interim resale discounts,
23 depending on the service provided, and subject to true-up upon
24 the establishment of permanent rates.

25 **2. Resale Restrictions.**

26 The Recommended Order requires that the following services be
made available for resale at a discount: (1) private line transport
(special access and private line) services, (2) services subject to

1 volume discounts, and (3) basic residential services.² The
2 Recommended Order misapplies the standards of the Act, reaches
3 conclusions unsupported by any substantial evidence, and will result
4 in confiscatory rates.

5 USWC should not be required to provide private line services to
6 resellers at a discount because these services are already sold at
7 wholesale prices. In Arizona, private line services are sold to
8 carriers and end users from the special access tariff. Further,
9 private line services are already discounted in Arizona as wholesale
10 services and require no further discounts to set a wholesale price.
11 The FCC First Order provides that exchange access services are not
12 subject to resale requirements even though these services are
13 offered to and taken by end users as well as carriers. (FCC First
14 Order ¶¶ 873-874). The FCC also recognizes that LECs do not avoid
15 any retail costs if access services are offered at wholesale to
16 competitors. Id. Because private line and special access are the
17 same service, provided out of the same tariff, they should not be
18 available to resellers at a discount.

19 The Recommended Order should also not require USWC to offer
20 further discounts on resellers services that are already offered at
21 a volume discount.³ Services that are provided to large customers,

22
23 ²The parties agree that enhanced services, deregulated
24 services, and promotions of less than 90 days, need not be provided
to MCI for resale.

25 ³ The FCC Order is unclear in its treatment of volume discount
26 services. The FCC requires that discounted services be provided to
resellers at the discount rate less the avoided cost. However, to a
large extent, the FCC has left the determination of "the substance
and specificity of rules concerning such discount and promotion

1 such as Motorola, are already priced to reflect the fact that USWC
2 avoids many of the usual costs of selling at retail. Further,
3 discounts are based primarily on commitments to receive specified
4 quantities of service for defined terms. The discounts therefore
5 reflect costs avoided because of the quantities and the term of the
6 contract. For example, marketing expenses such as advertising are
7 avoided when selling a large volume of service to a customer for an
8 extended period. It makes no sense to apply the same discount to
9 these services on the basis that USWC has avoided significant costs.
10 If a new entrant is allowed to compete with USWC, both by selling
11 its own services and by reselling USWC's service at a discount in
12 excess of the avoided cost, USWC cannot unable to effectively
13 compete. At the very least, the Commission in the generic pricing
14 proceeding should establish separate discount rates for these
15 services.

16 USWC should not be required to offer basic residential service
17 for resale at a wholesale discount. The only evidence in the record
18 confirms that USWC's current 1FR rate of \$13.18 does not cover its
19 cost. Requiring USWC to discount a below-cost service will force
20 USWC to subsidize competitors, such as MCI, with revenues from
21 USWC's retail customers. Basic residential service is priced below
22 cost in order to ensure universal service. Therefore, it is not
23 appropriate for resellers to obtain this below-cost service at a
24 discount. Further, if USWC is required to provide residential
25 _____
26 restrictions may be applied to resellers in marketing their services
to end users" to state commissions. (FCC First Order ¶¶ 951-952).

1 service to resellers at a price below cost, it will retard the
2 development of facilities-based competition. New entrants in the
3 market will have no incentive to build facilities if they can
4 purchase USWC services for less than their cost to construct new
5 facilities.

6 USWC recommends that page 12, line 19 through page 13, line 2
7 of the Recommended Order be deleted and replaced with the following
8 language:

9 U S WEST is not required to make private line transport
10 (special access and private line) services, services subject to
11 volume discounts, and basic residential services available for
12 resale at a wholesale discount.

12 **F. BRANDING**

13 The Recommended Order requires USWC to take certain steps to
14 rebrand repair and maintenance service. It is important that the
15 Recommended Order be amended to be clear that these steps need to be
16 taken where technically feasible and that rebranding occur when it
17 is technically possible to do so. Rebranding as contemplated in the
18 Recommended Order will require systems development and
19 implementation. Some time will be required for that implementation
20 and USWC will need to determine whether its systems can be altered
21 in a manner that meets the provisions of the Recommended Decisions.
22 Further, on some repair and maintenance situations, such as oral
23 rather than computer dispatches, rebranding may still not be
24 possible in the manner contemplated by the Recommended Order.

25 USWC recommends that the following sentence be added to the end
26 of page 14, line 4 of the Recommended Order:

1 The foregoing steps to rebrand repair and maintenance service
2 need only be taken by U S WEST where technically feasible.

3 **G. INTERCONNECTION**

4 The Recommended Order permits MCI to select a single point of
5 interconnection in each LATA. Establishing a single POI per LATA
6 will lead to inefficient engineering of the network and will impose
7 significant additional costs on USWC, who will have to back haul
8 traffic from the single point of interconnection if and when MCI
9 chooses to offer facilities-based local service outside the Phoenix
10 calling area. To discourage the establishment of inefficient POIs,
11 USWC should be permitted to charge construction costs to MCI if
12 MCI's meet point is more than a mile from a USWC end office.

13 Because the Recommended Order has adopted bill and keep, USWC
14 cannot recover the additional costs of hauling this traffic.
15 Further, the Recommended Order permits MCI to interconnect at USWC's
16 access tandem. This will further increase the costs that USWC
17 cannot recover. The Recommended Order should be amended to require
18 MCI to establish one point of interconnection per local calling area
19 at a place agreed upon by the parties. Alternatively, MCI should,
20 at a minimum, establish its local point of interconnection at points
21 of presence in Arizona for the provision of long distance service.

22 USWC recommends that page 6, line 5 through line 8 of the
23 Recommended Order be deleted and replaced with the following
24 language:

25 MCI shall be required to select at least one point of
26 interconnection per local calling area at a place agreed upon
by the parties.

1 Alternatively, USWC recommends that page 6, line 5 through line
2 8 of the Recommended Order be deleted and replaced with the
3 following language:

4 If MCI chooses not to select at least one point of
5 interconnection per local calling area, it will be
6 required to compensate U S WEST for additional switching
and transport of traffic resulting from that choice at the
switching and transport rates established herein or in the
generic pricing docket.

7
8 **H. COLLOCATION**

9 **1. Collocation of Remote Switching Units.**

10 USWC opposes the collocation of remote switching units ("RSUs")
11 in its end offices. The Commission should refuse to order
12 collocation of RSUs because: (1) the FCC First Order excludes
13 switching equipment; (2) it is not necessary for interconnection or
14 access to unbundled elements; (3) it creates a significant threat of
15 bypass of switched access services; (4) it will exacerbate space
16 limitation problems in USWC central offices; and (5) alternatively,
17 MCI can locate its RSU where its point of presence ("POP") is
18 located or at some other location and connect to USWC's central
19 office without collocating the RSU.

20 The FCC specifically required ILECs to permit collocation of
21 transmission equipment, including any type of equipment used to
22 terminate basic transmission facilities. FCC First Order at ¶ 580.
23 Despite the specific requests of the CLECs, the FCC declined to
24 order that the ILECs permit collocation of switching equipment
25 "since it does not appear that [switching equipment] is used for the
26 actual interconnection or access to unbundled elements." Id. at

1 ¶ 581. An RSU is switching equipment and not transmission
2 equipment; it is not primarily used for interconnection or access to
3 unbundled elements but, as configured by MCI with trunking capacity,
4 for other purposes.

5 Further, placing a trunking-capable RSU in USWC's central
6 office raises a significant prospect of access by-pass. Collocating
7 an RSU, which is trunked directly to other MCI switches or to other
8 CLEC's switches, creates a significant possibility of by-pass. Id.
9 at 500. USWC cannot effectively monitor MCI's use of its RSU to
10 ensure that by-pass was not occurring, and there is no method to
11 program or otherwise disable the RSU so that it could not be used
12 for by-pass. MCI promised not to use RSU's for by-pass; however,
13 because USWC collected \$238,000,000 from interstate and intrastate
14 switched access charges in Arizona, and MCI has substantial market
15 penetration in Arizona, MCI would have a powerful incentive to by-
16 pass whenever the opportunity arises.

17 Collocating RSUs in USWC central offices also will exacerbate
18 serious space limitations in those offices. When RSUs with trunking
19 functionalities are deployed in a USWC central office, additional
20 transmission equipment must also be installed, placing further
21 demands on scarce space.

22 Finally, MCI can often place its RSU within the space currently
23 leased or owned for its POP used to deliver interstate and interLATA
24 traffic to USWC or in other space located near USWC's central
25 offices and avoid collocating those facilities in USWC central
26 offices. It is technically feasible for MCI to collocate RSUs in

1 MCI space near USWC's central offices and connect to USWC through
2 MCI or USWC facilities. Indeed, in their Proposed Order in the
3 Brooks Fiber arbitration, the arbitrators require exactly this
4 arrangement for location of RSUs by Brooks. For these reasons, the
5 Commission should at a minimum order MCI to locate its RSUs in its
6 own premises or in premises obtained by MCI where technically
7 feasible and economically reasonable as Brooks Fiber agreed.

8 USWC recommends that page 21, line 3 through line 19 of the
9 Recommended Order be deleted and replaced with the following
10 language:

11 Under the Act, equipment requested to be collocated by a CLEC
12 must be collocated if it is "necessary" for interconnection or
13 access to unbundled elements. U S WEST has satisfied its
14 burden to establish that RSUs are not necessary for
interconnection or access to unbundled elements. Therefore,
U S WEST will not be required to permit MCI to collocate RSUs.

15 **2. Other Collocation Issues.**

16 The Recommended Order permits MCI to collocate at any
17 technically feasible point and rejects USWC's proposal that the
18 space available to any single new entrant for collocation in a given
19 central office be limited so as to make space available for other
20 new entrants. This portion of the Recommended Order is not
21 supported by substantial evidence and is contrary to sound public
22 policy.

23 In order to protect the rights of all potential competitors,
24 USWC argued that the agreement must contain some limitation on the
25 amount of floor space in a central office, made available to MCI for
26 physical collocation. USWC will have to provide physical

1 collocation to a number of new entrants, and there will be limits on
2 the available amount of floor space, particularly in light of the
3 space limitation problems USWC already faces in some of its Arizona
4 central offices. USWC has proposed that MCI and each other new
5 entrant be limited to 400 feet in any single central office. MCI
6 offered no reasonable alternative suggestion, and the Recommended
7 Order simply fails to address this issue.

8 An even more significant issue with respect to collocation is
9 the premises at which collocation should be offered. The
10 Recommended Order simply adopts the FCC's broad definition of
11 "premises" without considering the significant evidence of problems
12 created by a general rule that new entrants can collocate at
13 manholes, vaults and other locations outside the central office.
14 Although the FCC First Order states that USWC should offer
15 collocation at its "premises", USWC proposed that the presumptive
16 point of collocation be in USWC's central offices, with other
17 arrangements to be made on an as-needed basis. Because the most
18 efficient form of interconnection would be for MCI to interconnect
19 at USWC's end office or tandem switches, and because collocation at
20 other points raises serious issues concerning adverse service
21 impacts, it makes sense for collocation to occur in the central
22 offices. MCI has not requested collocation at any "premise" other
23 than a USWC central office, nor has it given an example about what
24 such a request might possibly be. The Recommended Order
25 specifically applies the BFR process to collocation. The Commission
26 should resolve these issues by requiring use of the BFR process here

1 as well.

2 Finally, the Recommended Order adopts MCI's request that no
3 restriction be placed on the types of cable used for entry into
4 collocated space. Where entry into the collocated space is through
5 USWC's conduit or ducts, the use of copper facilities will lead to
6 a quicker exhaust of that conduit and duct and it may well be
7 impossible to build more. The use of fiber facilities for
8 connection of the RSUs would require significantly less duct or
9 conduit. This will preserve the space for use by MCI and other
10 CLECs as well as USWC. The Recommended Order should be amended to
11 provide that the parties should mutually agree on the type of
12 facilities used to enter collocated space and that where technical
13 feasibility requires the use of fiber, USWC may require MCI to _____
14 on fiber facilities.

15 USWC recommends that page 19, lines 15 through 19 of the
16 Recommended Order be deleted and replaced with the following
17 language:

18 MCI may collocate at any U S WEST central office. If MCI
19 wishes to collocate at a location other than a central office,
20 MCI may do so if collocation is technically feasible and
21 subject to the BFR process. In addition, entry into a central
22 office for collocation must occur on fiber facilities, unless
23 otherwise agreed by the parties.

24 Alternatively, USWC recommends that page 19, lines 15 through
25 19 of the Recommended Order be deleted and replaced with the
26 following language:

27 MFS may collocate at any U S WEST central office. If MCI
28 wishes to collocate at a location other than a central
29 office, MCI may do so if collocation is technically
30 feasible and subject to the BFR process. If space

1 limitations exist at any central office making entry on
2 copper or coaxial cable infeasible, U S WEST may require
3 MCI to enter a central office for collocation or fiber
4 facilities.

4 I. MISCELLANEOUS CONTRACTUAL TERMS

- 5 1. The Commission should endorse USWC's proposed bona fide
6 request process.

7 USWC's best and final offer to MCI contains a proposed bona
8 fide request process that CLECs can use to request interconnection
9 or additional unbundled network elements on a case-by-case basis.
10 The time frames within this process are reasonable and comply with
11 the applicable rules of the FCC and the Commission. USWC Ex. 8 at
12 11-13 (Mason).

13 The proposed response time, Tr. 144 (Laub); MCI Ex. 4 at 36
14 (Laub), is unreasonable and unnecessary. Initial requests often
15 lack complete information on the scope of the request, Tr. 552
16 (Mason), and MCI plainly will not be able to deploy a service within
17 this short time in any event. See Tr. 148-49 (Laub).

18 USWC recommends that page 9, lines 23 through 27 of the
19 Recommended Order be deleted and replaced with the following
20 language:

21 The parties are directed to negotiate expedited and coordinated
22 installations provided such installation is technically and
23 reasonably feasible. With regard to any expedited installation
24 requested by MCI, U S WEST may recover not only the cost of
25 installation reflected in its TELRIC studies but also
26 additional costs incurred in expediting the installations. If
meeting a request for expedited installations would adversely
affect or detract from the level of service U S WEST provides
to its other customers, U S WEST may decline the request.

1 2. MCI should pay for the full construction costs incurred
2 by USWC to provide additional unbundled elements and
3 facilities for resale.

4 New entrants, such as MCI, who request additional unbundled
5 elements, require the construction of additional facilities for
6 resale. Other special construction is often desired in connection
7 with collocation. New entrants should pay for the construction
8 costs incurred by USWC -- they should not shift these costs to USWC
9 and its retail customers.

10 Requiring that any carrier requesting an additional network
11 element pay the cost that USWC incurs to unbundle and provide that
12 element, such as special construction charges, follows the FCC First
13 Order, which permits incumbent LECs to recover the costs of
14 unbundling network elements from requesting carriers. In addition,
15 the only way to insure that the benefits of unbundling will exceed
16 the costs is to have the requesting party pay.

17 The Recommended Order provides that USWC may collect up-front
18 construction charges from a new entrant only if USWC end users would
19 pay these charges pursuant to USWC's tariffs. This is both
20 inconsistent with the Act -- because it does not require new
21 entrants to pay the true cost of providing the service -- and
22 confiscatory. The Recommended Order should be modified to require
23 that USWC be compensated up-front by MCI for construction costs if
24 USWC has to construct new facilities to enable it to provide
25 services at resale or on an unbundled basis to MCI, and should not
26 be limited only to situations in which an end-user tariff is
involved. If USWC is required to build facilities, then MCI should

1 also pay a construction charge whether an end-user tariff is
2 involved or not.

3 Further, the Recommended Order, in discussing several issues,
4 provides that USWC should recover specific costs of providing
5 service to new entrants but fails to provide for a recovery
6 mechanism. Under the Act, USWC is entitled to recover its cost of
7 providing service to the new entrants. The Commission should amend
8 the Recommended Order to grant USWC a means to recover the costs due
9 from MCI.

10 USWC recommends that page 23, line 20 through line 26 of the
11 Recommended Order be deleted and replaced with the following
12 language:

13 To the extent U S WEST is required to build facilities to
14 provider interconnection, resale or unbundled services to MCI,
15 MCI must pay for those costs up-front. If the tariff for a
16 specific service or a proposed tariff for that service would
17 pass construction costs up-front to an end user, or if a
18 customer has agreed contractually to pay such costs, it is also
19 appropriate to charge MCI up-front for the construction as
20 well.

21 In addition, the word "however" should be omitted from page 23, line
22 27 of the Recommended Order.

23 3. The Commission should require MCI to compensate USWC to
24 reserve space on poles, in ducts and in conduits and to
25 permit USWC to impose reasonable minimum purchase
26 requirements.

27 MCI wants to be able to reserve space for as long as 90 days on
28 USWC poles and in ducts and conduits and then take as long as six
29 months to begin attaching or installing its facilities, yet pay
30 nothing to USWC to compensate it for the loss of revenue that USWC

1 could realize by leasing the facility to someone else. MCI Ex. 4 at
2 35 (Laub); Tr. 153-54 (Laub). Without the requirement of some
3 reservation fee, MCI could reserve facilities to block new entrants.
4 Tr. 576-77 (Mason).

5 Also, the Commission should not permit MCI and other requesting
6 carriers to use pole and conduit space in an inefficient or
7 disruptive manner. The Commission should permit USWC to impose
8 reasonable minimum purchase requirements so that MCI or another CLEC
9 cannot tie up long lengths of conduit or pole runs by selecting
10 individual poles or very short spans of conduit. USWC Ex. 8 at 105
11 (Mason).

12 USWC recommends that the two sentences appearing on page 22,
13 line 16 through line 19 be deleted and replaced with the following
14 language:

15 U S WEST may impose reasonable minimum purchase requirements at
16 this time.

17 III. LEGAL ISSUES

18 A. APPLICATION OF STATE AND FEDERAL LAW

19 In deciding the various issues before them, the Commission
20 should look to and rely on the Act and then state law and policy
21 where there is no inconsistency with federal law. Preemption should
22 not be presumed. Congress can preempt state law only if it
23 evidences an intent to occupy a given field. If Congress has not
24 entirely displaced state regulation, state law is preempted only to
25 the extent it actually conflicts with, or stands as an obstacle to,
26 federal law. California Coastal Comm'n v. Granite Rock Co., 480

1 U.S. 572, 580, 107 S. Ct. 1419, 1425 (1987).

2 The Act clearly does not evidence an intent by Congress to
3 preempt the entire field of telecommunications regulation. The Act
4 explicitly recognizes the importance of the state commissions' role
5 in implementing congressional intent underlying the Act; it
6 expressly preserves the right of the Commission to apply state law
7 where not inconsistent with the Act. See, e.g.,
8 §§ 252(e)(2)(A)(ii); 252(e)(3); 252(f)(2); 253(b); 253(c). The
9 Eighth Circuit stay in Iowa Utilities Board reaffirms the states'
10 rights to make final decisions in these arbitrations. See also
11 O'Melveny & Myers v. Federal Deposit Ins. Corp., 512 U.S. 79, 114 S.
12 Ct. 2048, 2054 (1994) (matters left unaddressed in a comprehensive
13 federal regulatory scheme are presumptively subject to disposition
14 by state law). Therefore, absent a conflict with state law, the Act
15 does not preempt state law regarding telecommunications regulation.

16 If the Commission determines that the FCC Order conflicts with
17 the Act, they must decline to follow the Order and instead comply
18 with the Act. A federal agency must promulgate rules consistent
19 with Congress' intent in enacting the enabling legislation from
20 which authority to promulgate the rules is derived. Federal
21 Election Comm'n v. Democratic Senatorial Campaign Committee, 454
22 U.S. 27, 31, 102 S. Ct. 38, 42 (1981). Put simply, regulations
23 inconsistent or in conflict with provisions of the Act cannot stand.
24 NLRB Union v. Federal Labor Relations Authority, 834 F.2d 191, 195
25 (D.C. Cir. 1987); McNabb v. Bowen, 829 F.2d 787, 791 (9th Cir.
26 1987); Rakes v. Housing Authority of Dunbar, 765 F. Supp. 318, 320

1 (S.D.W.Va. 1991). Ultimately, federal courts must resolve any such
2 conflicts pursuant to § 252(e)(6) of the Act. Nonetheless, in
3 issuing their decision in this arbitration, the Commission must, if
4 it cannot reconcile provisions of the FCC order with the Act, reject
5 the offending portions of the order and comply with the Act.

6 Courts and quasi-judicial bodies are not required to adhere to
7 unlawful statutes or regulations. Accordingly, if the Commission
8 concludes that provisions of the FCC orders are inconsistent with
9 the Act or exceed the FCC's authority, it should exercise its
10 regulatory authority by not enforcing the unlawful provisions. In
11 determining whether provisions of the FCC orders are unlawful, the
12 Commission should analyze whether any of the provisions improperly
13 interfere with the Commission's authority over intrastate matters.
14 See Louisiana Public Service Comm'n v. Federal Communications
15 Comm'n, 476 U.S. 355, 374 (1986) (FCC regulations preempting state
16 depreciation regulations are ultra vires).

17 Section 252(e)(6) of the Act, which grants federal district
18 courts jurisdiction to review the decisions of state arbitrators,
19 confirms the Commission's obligation to resolve issues in a manner
20 consistent with the Act -- as opposed to the FCC order. That
21 section provides that a party aggrieved by the arbitration process
22 may bring an action in federal court "to determine whether the
23 agreement or statement meets the requirements of section 251 and
24 this section." (Emphasis added.) This language establishes that
25 federal courts must review arbitration decisions for compliance with
26 the Act, not for compliance with the FCC's orders. It follows,

1 therefore, that the ultimate obligation of these and other state
2 arbitrators is to ensure compliance with the Act. Moreover,
3 Congress directed that state arbitrators must interpret the Act in
4 a manner that will "protect the public safety and welfare, ensure
5 the continued quality of telecommunication services, and safeguard
6 the rights of consumers." 47 U.S.C. § 253(b). This provision
7 further supports the Commission's obligation and authority to
8 resolve issues consistently with the Act and in furtherance of the
9 public interest.

10 Finally, the Tenth Amendment prohibits the federal government
11 from improperly stripping states of control over state policies. As
12 one court recently stated, the "Tenth Amendment confirms that the
13 power of the Federal Government is subject to limits that may, in a
14 given instance, reserve power to the States." Koog v. United
15 States, 79 F.3d 452, 455 (5th Cir. 1996). The federal government
16 lacks the "power to compel the states to require or prohibit
17 [certain] acts." Id. at 456, citing New York v. United States, 505
18 U.S. 144 (1992).. The federal government "may not compel the states
19 to enact or administer a federal regulatory program." Id.

20 In sum, even though the Commission acts under congressional
21 mandate, principles of state law, including the broad constitutional
22 and statutory authority vested in the Commission concerning the
23 regulation of telecommunications providers, should guide its
24 decisions.

25 **B. UNCONSTITUTIONAL CONFISCATORY TAKINGS**

26 Under the Takings Clause of the United States Constitution,

1 public utilities are entitled to just and reasonable utility rates.
2 Federal Power Comm'n v. Hope Natural Gas Co., 320 U.S. 591, 603
3 (1944). "If the rate does not afford sufficient compensation, the
4 State has taken the use of utility property without paying just
5 compensation. . . ." Duquesne Light Co. v. Barasch, 488 U.S. 299,
6 308 (1989). Indeed, utilities are entitled to a reasonable
7 opportunity to recover not only their costs but a reasonable profit
8 as well. Hope, 320 U.S. at 603; Duquesne, 488 U.S. at 310. The
9 Takings Clause of the Arizona Constitution, art. 2, § 17, bars
10 confiscatory takings as well. Thus, under both the United States
11 and Arizona Constitutions, the Commission must set rates that permit
12 USWC at least to recover all of the actual costs incurred for
13 unbundled network elements and resale. It may not set below-cost
14 rates.

15 **C. SUBSTANTIAL EVIDENCE STANDARD**

16 Submitting a proposed interconnection agreement does not put
17 all issues or language in that proposed agreement before the
18 Commission. The Act provides, "The State Commission shall limit its
19 consideration of any petition under paragraph (1) (and any response
20 thereto) to the issues set forth in the petition and in the
21 response." 47 U.S.C. § 252 (b)(4)(A). In this proceeding MCI
22 introduced testimony that highlighted key issues in dispute with
23 USWC, but did not identify with specificity all of the disputed
24 terms and conditions of the proposed interconnection agreements or
25 provide testimony in support of all these terms and conditions.

26 Under Arizona law a court will examine the decision of the

1 Commission to determine if it is supported by substantial evidence.
2 U S WEST Communications, Inc. v. Arizona Corp. Comm'n, 185 Ariz.
3 277, 281-82, 915 P.2d 1232, 1236-37 (App. 1996); Tucson Elec. Power
4 Co. v. Arizona Corp. Comm'n, 132 Ariz. 240, 241, 645 P.2d 231, 232
5 (1982); Simms v. Round Valley Light & Power Co., 80 Ariz. 145, 154-
6 55, 294 P.2d 378, 384 (1956). Furthermore, a Commission order may
7 be unlawful even though supported by substantial evidence if the
8 evidence was improper or illegal. Arizona Corp. Comm'n v. Citizens
9 Utility Co., 120 Ariz. 184, 187-88, 584 P.2d 1175, 1178-79 (App.
10 1978). Accordingly, those issues without substantial evidentiary
11 support are not properly before the Commission.

12 Moreover, section 252 of the Act limits the matters at issue in
13 an arbitration to section 251, section 252 (d) and the establishment
14 of an implementation schedule. 47 U.S.C. § 252(c). If a party
15 requests the Commission to adopt other terms and conditions of a
16 proposed interconnection agreement, the Commission need not resolve
17 issues concerning those other matters.

18 IV. CONCLUSION

19 The Commission should amend the Recommended Order as set forth
20 in these exceptions and thereby adopt a resolution to the disputed
21 issues that fairly balances the interests of USWC and its ratepayers
22 with the interests of MCI and the other new entrants. The
23 Recommended Order, with its use of uneconomic and unrealistic proxy
24 prices and its authorization of price arbitrage through sham
25 unbundling, unfairly disadvantages USWC and its customers. USWC has
26 offered evidence of its costs of service that form a just,

1 reasonable and fair basis on which to establish interim prices and
2 interim wholesale discounts. Because any interim rates are subject
3 to true-up following the permanent pricing proceeding, MCI and the
4 other new entrants will not be prejudiced by the use of interim
5 rates based on USWC's cost studies.

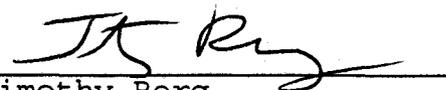
6 Therefore, based on the reasons set forth herein, USWC asks
7 that the Commission modify the Recommended Order as requested.

8 DATED this 13th day of December, 1996.

9 Respectfully submitted,

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16 AND
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27 ORIGINAL and 10 copies of
28 the foregoing delivered for
29 filing this 13th day of
30 December, 1996 to:

31 Docket Control
32 Arizona Corporation Commission
33 1200 WEST Washington Street
34 Phoenix, AZ 85007

1 COPY of the foregoing delivered
this 13th day of December, 1996 to:

2 Jerry L. Rudibaugh
3 Chief Hearing Officer
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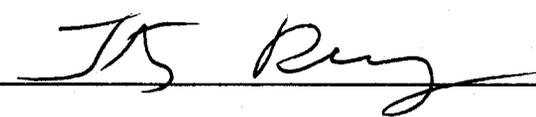
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23 this 13th day of December, 1996 to:

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