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REHEARING 3-11-98



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February 19, 1998

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COMMUNICATIONS

Arizona Corporation Commission
1200 West Washington Street
Phoenix, AZ 85007

RE: Docket Nos. T-03021A-96-0448, et al.

To The Commission:

Attached is AT&T Communications of the Mountain States, Inc.'s Application for Reconsideration of Decision No. 60635.

Sincerely,

Mary B. Tribby DP

Mary B. Tribby

Attachment

cc: Certificate of Service

~~Arizona Corporation Commission~~
DOCKETTED

FEB 19 1998

DOCKETED BY *[Signature]*

BEFORE THE ARIZONA CORPORATION COMMISSION

IN THE MATTER OF THE PETITIONS OF:

**AMERICAN COMMUNICATIONS SERVICES,
INC. AND AMERICAN COMMUNICATIONS
SERVICES OF PIMA COUNTY, INC.;**

**AT&T COMMUNICATIONS OF THE
MOUNTAIN STATES, INC.;**

MFS COMMUNICATIONS COMPANY, INC.;

TCG PHOENIX;

**MCIMETRO ACCESS TRANSMISSION
SERVICES, INC.;**

**BROOKS FIBER COMMUNICATIONS OF
TUCSON, INC.;**

**SPRINT COMMUNICATIONS COMPANY,
L.P.;**

GST TUCSON LIGHTWAVE, INC.; and

COX ARIZONA TELECOM, INC.

**FOR ARBITRATION OF THE RATES,
TERMS, AND CONDITIONS OF
INTERCONNECTION WITH U S WEST
COMMUNICATIONS, INC. PURSUANT TO
§ 252(b) OF THE TELECOMMUNICATIONS
ACT OF 1996.**

**DOCKET NO. U-3021-96-448
DOCKET NO. U-3245-96-448
DOCKET NO. E-1051-96-448**

**DOCKET NO. U-2428-96-417
DOCKET NO. E-1051-96-417**

**DOCKET NO. U-2572-96-362
DOCKET NO. E-1051-96-362**

**DOCKET NO. U-3016-96-402
DOCKET NO. E-1051-96-402**

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

**DOCKET NO. U-3009-96-478
DOCKET NO. E-1051-96-478**

**DOCKET NO. U-2432-96-505
DOCKET NO. E-1051-96-505**

**DOCKET NO. U-3155-96-527
DOCKET NO. E-1051-96-527**

**DOCKET NO. U-3242-97-017
DOCKET NO. E-1051-97-017**

(Consolidated)

DOCKETED

FEB 19 1998

APPLICATION FOR RECONSIDERATION

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AT&T Communications of the Mountain States, Inc. ("AT&T"), by and through its undersigned counsel and pursuant to A.A.C. §R14-3-11, submits this Application for Reconsideration of the Arizona Corporation Commission's ("Commission") Opinion and Order ("Order"), Decision No. 60635, dated January 30, 1998. Certain of the decisions made by the

1 Commission are inconsistent with the Telecommunications Act of 1996 ("Act") and are not
2 supported by record evidence. The overall impact of the decision is that the price for an
3 unbundled loop, a primary cost component for local service, is \$21.98. When this loop price is
4 compared to U S WEST's IFR rate of \$13.18, it is obvious that no competitor could offer
5 economically attractive local service in Arizona. Even the prices ordered by the Arbitrators in
6 their Recommended Opinion and Order ("Arbitrators' Decision") (which included an unbundled
7 loop price of \$14.15) posed competitive concerns. Moreover, several of the decisions made by
8 the Commission will have deleterious and unavoidable consequences on the rates for all
9 telecommunications consumers in Arizona. For these reasons, AT&T seeks reconsideration of
10 the Order on the issues set forth below.

11

12 **A. Depreciation**

13 The Arbitrators' Decision accepted, with limited modifications, the depreciation lives
14 proposed by U S WEST. In its Exceptions, AT&T objected to these lives on the basis that the
15 proposed depreciation lives had not been subjected to appropriate review and were inconsistent
16 with cost-based pricing principles. In its Order, while acknowledging that its own rules require
17 consideration of depreciation adjustments in a rate case, the Commission modified the
18 Arbitrators' Decision by adopting the lives set forth in a depreciation study by Technology
19 Futures, Inc. ("TFI"), and adopted a 15 year depreciation life for underground copper cable.¹
20 There is no evidence in the record to support the adoption of 15 year depreciation life for
21 underground cable or the remainder of the depreciation lives recommended in the TFI study.² In

22 ¹ The Commission's Order is internally inconsistent because in deciding the issue of capital
23 structure the Commission relied on its last decision addressing that issue (Decision No. 58927)
24 on the basis that it reflected both actual capital structure and the impact of increased competition.
25 The same logic should apply to depreciation lives. The Commission should defer to Decision
26 No. 58927 for depreciation lives, since that decision took into account the impact of competition
on depreciation lives.

² While U S WEST sponsored the TFI study, it did not support the depreciation lives proposed
in the TFI study which have the greatest impact on local service costs. For example, for

1 addition the depreciation lives adopted by the Commission result in Unbundled Network
2 Element ("UNE") prices that are not cost-based as required by Section 252(d) of the Act.

3 The arbitrary nature of the Commission's Order is highlighted by the Commission's
4 deliberations over whether to use a 15 or 16 year life for underground copper cable.
5 Commissioner Kunasek stated to Chairman Irvin:

6 "So you're at 16 and I'm at 15. I'm comfortable with 16. If you're
7 comfortable with 15, go flip a coin, and Mr. Jennings will call it."

8 Transcript of Deliberation, dated January 8, 1998 ("Delib.Tr."), p. 218.

9
10 Depreciation lives play a critical role in the quantification of the cost of facilities used in
11 the provision of telecommunications service. Shortening the depreciation lives, as recommended
12 in the TFI study, results in significant increases in the cost of the UNEs, particularly shortening
13 the depreciation life for underground cable – the predominant cost associated with the local loop.
14 Increasing the UNE costs that must be paid by Competitive Local Exchange Carriers ("CLECs")
15 will materially increase the rates the CLECs must charge their Arizona customers. Similarly, the
16 Commission has increased the costs purportedly incurred by U S WEST for the use of these loop
17 facilities, thereby increasing the costs that must be recovered by U S WEST in its retail rates.
18 For example, these same loop facilities are used by U S WEST to provision local service to its
19 Arizona retail customers. There is no basis for these loops to bear one depreciation life when
20 offered to CLECs and a different life for U S WEST's end users – the situation which the
21 Commission has created by this decision since the life for underground copper cable for end
22 users in Arizona is 30 years and is now 15 for CLECs. The Commission's Order must be applied
23 in the pricing of U S WEST's retail services as well. To do otherwise would be patently
24 discriminatory, giving U S WEST an unfair competitive advantage in the marketplace and would
25

underground copper cable, U S WEST supported an 11.3 year life, not the 14 year life supported
26 by TFI.

1 deter entry by CLECs because CLECs could not compete against U S WEST if they were forced
2 to incur, and thus charge their customers for, higher costs than U S WEST for the same facilities.

3 As the Commission acknowledged, its Rules generally preclude public service
4 corporations like U S WEST from changing depreciation rates except in a rate case where the
5 depreciation issue can be fully explored and litigated. A.A.C. §R14-2-102. The Commission
6 waived this rule on its own motion, concluding that the above rule may not apply to this kind of
7 case but, even if it did, a waiver of the rule was appropriate under these circumstances. There is
8 no legal basis for concluding that Rule 102 does not apply to this proceeding. Moreover, Rule
9 102 should not have been waived. This rule ensures that, before the Commission changes
10 depreciation lives, it has adequate information regarding the impact of changes in depreciation
11 lives on the Company and ratepayers. As evidenced in the transcript of the Commission's
12 deliberations, that information is clearly not available here. Given the myriad issues under
13 consideration in this cost proceeding, depreciation was the subject of only limited testimony and
14 analysis.

15 Moreover, even the present limited record on depreciation shows that the use of the TFI
16 study is questionable. First, the study's sponsor, U S WEST, did not support a number of the
17 lives recommended by TFI, in particular the depreciation life for underground copper cable.
18 Second, the TFI study relies upon flawed assumptions and is an insufficient and inappropriate
19 tool for setting depreciation lives for U S WEST facilities.

20 The TFI study, published in 1995, assumes that competition, technology, and consumer
21 demands will force incumbent local exchange carriers ("ILECs") to retire their existing
22 narrowband networks and to replace those networks with broadband integrated networks.
23 Santos-Rach Direct Test. at Ex. 9. This assumption drives the study's conclusion that central
24 office equipment and outside plant investments will all be replaced very rapidly. *Id.*

25 However, the assumption that broadband services will replace existing narrowband
26 networks is an invalid assumption to rely on for purposes of determining depreciation lives for a

1 telecommunications network and is contradicted by what is actually occurring with respect to
2 facility placement in telecommunications networks.

3 First, the term "telecommunications" as used in the FCC's First Report and Order refers
4 to services regulated under Title II of the Communications Act, as amended. Those services
5 include switched telephone voice and data services, not broadband video cable services. See
6 Allocation of Costs Associated with Local Exchange Carrier Provision of Video Programming
7 Services, CC Docket No. 96-112, Notice of Proposed Rulemaking, FCC No. 96-214, (May 10,
8 1996), paragraph 2. Thus, the plant lives appropriate for calculating cost-based UNE prices
9 should not be based upon the assumption that efficient telecommunications facilities will be
10 retired prematurely in order to provide broadband video services. In fact, the FCC has
11 specifically ruled that the cost of premature retirements will not be charged to regulated
12 telephone services. The FCC states:

13
14 Facilities upgrades and accelerated replacement of older facilities might also be
15 undertaken primarily for the benefit of unregulated service offerings. The
16 principles adopted in the Order dictate that such costs be excluded from the
17 regulated accounts.

18 See Separations of Costs of Regulated Telephone Service from Costs of Nonregulated Activities,

19 CC Docket No. 86-111, Report and Order, FCC 86-564, (February 6, 1987), at para. 115.

20 Improper reliance on an assumption that the telecommunications network will be replaced by an
21 integrated telecommunications/video network will effectively cause Title II telephone services to
22 pay the costs of premature retirements driven by anticipated unregulated broadband or video
23 services. This is not a proper pricing assumption and should not be the basis for UNE pricing in
24 this proceeding.

25 Second, evidence was presented during the hearing that U S WEST continues to place
26 underground copper cable, despite TFI's assumption that copper is a dying technology.

Moreover, evidence was presented that the life of copper is being extended (or given new

1 longevity) through the use of new technology such as Asymmetrical Digital Subscriber Line
2 ("ADSL") service. In addition, evidence was presented that U S WEST's plant replacement
3 program does not contemplate replacement of distribution cable, where the lion share of copper
4 underground cable is used, for some time. Most importantly, U S WEST admitted that copper
5 cable presently has a field life of approximately 20 years. Therefore, it is premature to shorten
6 the life of underground copper cable at this time.

7 If the Commission is concerned that the existing prescribed lives do not adequately
8 reflect the emergence of competition in telecommunications markets, the solution is not to adopt
9 the flawed TFI study. Rather, the Commission should conduct a more thorough depreciation
10 analysis and use either the depreciation lives adopted in Decision No 58927, or the prescribed
11 lives adopted by the FCC on an interim basis until the more thorough analysis is completed. The
12 FCC has conducted a careful and thorough analysis of each RBOC's network, including
13 U S WEST's. As a result of this analysis, the FCC has adopted prescribed depreciation lives for
14 U S WEST's facilities that are designed to be forward-looking, and to pay "close attention to
15 company plans, technological developments and other future-oriented analyses." Report on
16 Telephone Industry Depreciation, Tax and Capital-Expense Policy, Accounting and Audits
17 Division, Federal Communications Commission, April 15, 1987 (AAD Report), p.3.

18 Recently, the FCC reaffirmed its forward-looking orientation in connection with the
19 simplification of its depreciation represcription practices. The FCC has prescribed a range of
20 depreciation lives which can be selected by carriers for prescription on a streamlined basis.
21 These ranges were based upon:

22
23 "statistical studies of the most recently prescribed factors. These statistical
24 studies required detailed analysis of each carrier's most recent retirement
25 patterns, the carriers' plans, and the current technological developments and
26 trends."

1 See Simplification of the Depreciation Process, CC Docket No. 92-296 Third Report and Order,
2 FCC 95-181, (May 4, 1995) at p.6. This streamlined represcription practice assures the
3 development of depreciation lives that allow forward-looking capital recovery.

4 Attachment 1 to AT&T's Exceptions filed on July 21, 1997 identifies the prescribed
5 depreciation lives adopted by the FCC that are relevant to this proceeding. Unlike the lives
6 adopted by the Commission, the FCC lives comply with the requirements of the Act and the
7 FCC's First Report and Order. If any changes are made to U S WEST's prescribed lives in
8 Arizona, the Commission should go no further than to adopt the FCC prescribed lives on an
9 interim basis until further review is made of U S WEST's Arizona-specific data.

10

11 **B. Distribution Design**

12 The Arbitrators adopted the distribution design reflected in the Hatfield Model 2.2.2
13 ("HM2.2.2"). In its Order, the Commission adjusted the cable sheath mileage used in HM2.2.2
14 from 15,600 miles to 26,092 miles, nearly doubling the number of sheath miles without any
15 explanation to support this adjustment and without record support.

16 The adjustment made by the Commission is based exclusively on extra record evidence
17 and is, therefore, improper. In post-hearing briefs filed well after the record closed in this case,
18 U S WEST asserted that certain selective modifications reflected in a subsequent version of the
19 Hatfield Model HM3.1 ("HM3.1") should be made to HM2.2.2 in this case. Of course,
20 U S WEST only recommended those HM3.1 modifications that increased costs.³ There is no
21 evidence in the record to support the use of any HM3.1 results in this case. Indeed, during
22 deliberations when the Commission was confronted with the absence of any record evidence on
23 HM3.1, Chairman Irvin concluded that this problem could be cured by simply striking any

24

25 ³ In fact, as pointed out by the CLECS in their response filed on October 23, 1997, there are
26 numerous other changes in HM3.1 that must be taken into account when looking at the change in
distribution miles. Indeed, if all revisions from HM3.1 were made to HM2.2.2, the loop cost
would decrease from \$16.28 (the loop cost from HM2.2.2) to \$14.95.

1 reference to HM3.1 in the proposed Amendment and subsequent Order. (Delib.Tr., pp. 176-77.)
2 This action does not cure the absence of record evidence to support the Commission's Order. To
3 the contrary, there is no record support for the Commission's sheath mile adjustment.
4 U S WEST studies used a sheath miles figure of 34,000. U S WEST identified actual
5 distribution miles at 43,504. HM2.2.2 used 15,600 sheath miles. The only reference to the
6 26,092 mile modification made by the Commission is the HM3.1 reference from the U S WEST
7 brief. The source of the figure cannot be disguised by omitting the reference to HM3.1. Simply
8 stated, the sheath mile adjustment made by the Commission cannot be made on the basis of the
9 record before it and is, therefore, improper.

10 The Commission also, responding to issues regarding the impact that the sheath mile
11 adjustment could have on local loop prices, established an arbitrary cap of \$4.00, i.e., the
12 resultant increase in the loop price associated with this change would be no more than an
13 additional \$4.00. Again, there is no support for the underlying adjustment and the use of the
14 \$4.00 cap to make the adjustment more palatable demonstrates just how arbitrary this
15 amendment is.

16
17 **C. Structure Sharing**

18 After hearing substantial evidence regarding present and future sharing opportunities
19 available to U S WEST, the Arbitrators found the structure sharing assumptions of 33% in
20 HM2.2.2 were appropriate. The Commission altered the Arbitrators' Decision, establishing a
21 structure sharing assumption of 50%. Again, there is no record support for the sharing
22 assumption adopted by the Commission and the prices adopted employing this sharing
23 assumption are not cost based. Indeed, as evidenced by the Commission's deliberations, the
24 source of the 50% figure is a compromise between the Arbitrators' Decision of 33% and the
25 initial amendment of 66% proposed by Chairman Irvin. Specifically, Commissioner Kunasek
26

1 stated "Well, I guess my preference would be to split the difference and go 50 percent for the 66
2 to the 33, strike a balance." Delib.Tr., p. 302.

3 The record demonstrates that as competition increases, the potential and incentive for
4 sharing increases. Because the cost of placement is such a significant cost of doing business,
5 efficient providers will seek every opportunity to reduce costs by sharing those costs with other
6 parties. Indeed, with the advent of competition in the telecommunications, cable and electric
7 industries, the number of parties that will be seeking sharing opportunities has expanded
8 exponentially.

9 In addition, the record establishes that in new developments, developers are required to
10 pay the entire cost of trenching, with no costs being borne by U S WEST. Moreover,
11 municipalities are beginning to require the sharing of trenches to minimize disruption to the
12 public. The Arbitrators relied on this evidence to support their adoption of the 33% sharing
13 assumption from the Hatfield Model. On the other hand, there is no record basis for the
14 Commission's modification and adoption of a 50% sharing assumption. The Arbitrators'
15 Decision should not have been altered.

16
17 **D. Resale Discount**

18 The Arbitrators adopted the avoided cost methodology proposed by MCI, with the
19 exception that they superimposed disaggregated service discounts proposed by U S WEST.
20 AT&T took exception to this juxtaposition of models on the basis that the MCI model was
21 designed to produce a single composite discount, not service-specific discounts and it made no
22 sense to superimpose U S WEST model's disaggregated discount weighted percentages that had
23 been rejected by the Arbitrators in calculating service-specific discounts. The Arbitrator's
24 Decision concurred in the MCI methodology, but then made arbitrary, unsupported adjustments
25 that reduced the aggregated discount to 20.22%. Then, the Arbitrators arbitrarily weighted the
26 20.22% discount among different services coming up with service-specific discounts ranging

1 from 10 to 63%. The Commission, during the Open Meeting, arbitrarily changed the discount
2 set by the Arbitrators and adopted a 12% discount for residential services and an 18% discount
3 for all other services.

4 Once again, there is absolutely no record evidence to support the discounts adopted by
5 the Commission. Indeed, both discounts are below the 20.22% aggregated discount chosen by
6 the Arbitrators. The arbitrary nature of the Commission's Order is again evidenced in the
7 deliberations where the following exchange occurred:

8 COM. KUNASEK: I would start out the negotiations
9 at 18 percent.

10 COM. JENNINGS: Take that in a flash. I must say I
11 prefer the targeted approach, but 18 percent doesn't
 sound bad to me.

12 COM. KUNASEK: The overall Staff proposal was 20
13 percent.

14 ARBITRATOR BEHUN: 20.22.

15 COM. KUNASEK: You're functioning now on 17
16 percent.

17 ARBITRATOR RUDIBAUGH: That's correct.

18 COM. KUNASEK: Any reaction to that?

19 CHMN. IRVIN: Do I hear 15.50?
20

21 Simply stated, the resale discounts adopted by the Commission reflect the results of an
22 arbitrary bidding process. The Order should be revised and MCI's avoided cost discount of
23 22.5% in the aggregate should be adopted, since the Arbitrators found MCI's methodology to be
24 the most reliable after hearing all the evidence.
25
26

1 There are other reasons that a single discount should be adopted. Accurately calculating
2 service-specific discounts would require meticulous, expensive, and time-consuming activities-
3 based cost studies. U S WEST does not now record its costs in this fashion. For this reason,
4 there is no accurate way to determine appropriate groupings of services for disaggregated
5 discounts. U S WEST simply cannot meet its burden to show that disaggregated discounts
6 reflect cost-based pricing. Moreover, the adoption of multiple, service-specific discounts would
7 require the Commission to determine new discount rates whenever U S WEST introduces new
8 products or combines existing products. These problems can be avoided by applying one
9 discount to all products.

10

11 **E. Geographic Deaveraging**

12 In its Order, the Commission directed the Hearing Division to set a proceeding to
13 determine whether geographically deaveraged rates should be established and, if so, how that
14 should be done and when such rates should become effective. Until such a proceeding is
15 resolved, there will be one state-wide price established for unbundled network elements. The
16 decision not to deaverage rates now is contrary to the Act and inconsistent with the record.
17 Moreover, this decision will delay the development of cost-based rates and, thus, hamper the
18 development of competition in Arizona.

19 While the Commission stated that there was insufficient evidence in the record to support
20 deaveraging, in fact, the record fully supports deaveraging of loop costs, the highest cost
21 component for local service. First, it is undisputed that U S WEST's costs of providing
22 unbundled network elements vary across the state. ACSI Ex.2; Tr. 405 (Harris Testimony).

23 Second, the proponents of the Hatfield Model provided cost support for nine zones for
24 Arizona. In addition, evidence was presented that such deaveraging was critical to successful
25 implementation of competition in Arizona.

26

1 The Commission seemed to be swayed by U S WEST's argument that geographic
2 deaveraging should not occur until U S WEST deaverages its retail rates. U S WEST clearly has
3 control over the pricing of its retail services. To date, U S WEST has not sought such
4 deaveraging of its retail rates. Instead, it has used this argument to delay proper, cost-based
5 pricing of UNEs. U S WEST's motives are obvious – delay meaningful competition for as long
6 as possible. This Commission should require deaveraging of UNEs and that decision will
7 provide the impetus for U S WEST to realign its retail rates. U S WEST testified in this
8 proceeding that it would file a rate case "in the near future." Tr. 675. The Commission should
9 not wait for U S WEST to decide if and when it will file such a case. U S WEST's failure to
10 seek deaveraged retail rates provides no basis for the Commission to ignore the Act's
11 requirement of cost-based pricing for unbundled network elements.

12

13 **F. Non-Recurring Charges**

14 The Arbitrators established two different pricing structures for non-recurring rate
15 elements. Where there is a retail tariff corresponding to a non-recurring charge proposed by
16 U S WEST in this docket, the Arbitrators required that the charge to new entrants equal the retail
17 tariff less an avoided cost discount. Where there is no corresponding retail tariff, the charge to
18 new entrants is set at the Hatfield Model's recommended charge, which incorporates the non-
19 recurring costs within its recurring rate calculations for each unbundled element. In its Order, the
20 Commission adopted the approach employed by the Arbitrators. The use of the Hatfield Model
21 to price non-tariffed nonrecurring charges is proper. However, use of tariff-based nonrecurring
22 charges is inconsistent with the requirement in the Act that UNE prices be cost-based. Further,
23 because the Hatfield Model includes nonrecurring charges in its recurring rate calculations,
24 additional non-recurring charges would result in double recovery.

25 Section 252(d)(1)(A) of the Telecommunications Act of 1996 ("the Act") requires that
26 the rate for an unbundled network element be based upon the cost of providing the element. The

1 Commission's Order that certain non-recurring charges be based on tariffed retail rates does not
2 comply with this requirement. The Commission's 1995 decision which established these retail
3 non-recurring rates clearly set those rates not just on the basis of embedded costs, but also
4 applying other factors such as "rate continuity, as well as simplicity and stability of rates". In the
5 Matter of Application of U S WEST, Decision No. 58927 (Arizona Corp. Comm'n) (Jan. 3,
6 1995) at p. 69. U S WEST's interstate tariff rates, which provide the basis for non-recurring rate
7 elements such as the Expanded Interconnection Channel Termination, also are not based on
8 U S WEST's forward-looking costs. In fact, the FCC has recently determined that U S WEST's
9 collocation prices are not cost-based. In the Matter of Local Exchange Carriers' Rates, Terms,
10 and Conditions for Expanded Interconnection Through Physical Collocation, CC Docket No. 93-
11 162, Second Report and Order, (June 13, 1997) FCC 97-208.

12 Moreover, even if retail non-recurring charges were based on forward-looking costs, the
13 retail rate elements listed in U S WEST's tariff are not identical to the unbundled network
14 elements being priced in this docket. The price of nonrecurring charges for unbundled network
15 elements that are based upon a different retail element, by definition, cannot be cost-based. For
16 these reasons, the Commission's Order should require that all non-recurring charges be set based
17 on the Hatfield Model's unbundled network element prices.

18
19 **G. Overhead Factor**

20 The Commission adopted the common cost factor recommended by the Arbitrators of
21 15%, far in excess of the presumptive 10% factor prescribed by the Commission's Rules. See
22 A.A.C. R14-2-1310. There is no basis in the record for this determination.

23 The Arbitrators determined that U S WEST's evidence of its common costs should be
24 rejected. In its Order, the Commission rejected U S WEST's 22% overhead factor on the basis
25 that it was derived using embedded costs and therefore included costs which do not relate to the
26 use of network elements. However, the Commission then ignored the only forward-looking

1 evidence presented in this proceeding, the 10% factor developed by the Hatfield Model and,
2 instead, selected a factor of 15%, which appears to be a factor proposed by BellSouth for use in
3 its service territory. Adoption of a 15% overhead factor in Arizona is simply not supported by
4 record evidence.

5 Moreover, the Commission's Rules limit the overhead factor that U S WEST may
6 recover to 10% above TSLRIC. Id. Under A.A.C. §14-2-1310, recovery in excess of 10% is
7 allowed only with verifiable proof that common costs will, in fact, exceed 10% on a forward-
8 looking basis. The Commission alludes that there is record support that the 10% factor is
9 insufficient to cover U S WEST's overhead expenses. The Commission cited no record evidence
10 for this conclusion because there is none to be cited. Indeed, the only evidence that 10% was
11 insufficient was presented by U S WEST and the Commission properly rejected that evidence
12 because it was based upon embedded costs. The only forward-looking cost-based evidence was
13 presented by the proponents of the Hatfield Model and that evidence fully supported application
14 of the Commission rule. This evidence was not rebutted by any valid forward-looking evidence.

15 In addition, the developers of the Hatfield Model conducted a study of overhead expense
16 experienced in similar service industries operating in more competitive environments. Siwek
17 Dir. at Ex. SES - 1 at p. 38. This study demonstrates that the Commission's 10% factor and the
18 factor used in HM2.2.2 is conservative in a competitive environment. Id. Based on this
19 evidence, the Commission's presumptive overhead factor of 10% should be adopted for use in
20 calculating the price of unbundled network elements.

21
22 **H. Network Maintenance Costs**

23 U S WEST contended during the arbitration that it will experience no reduction in
24 network maintenance expenses on a forward-looking basis. The Hatfield Model 2.2.2 adopted a
25 30% reduction, based on the reality that technological advances in equipment will result in lower
26 maintenance costs. The Commission adopted the same percentage recommended by the

1 Arbitrators, which falls between these two recommendations, adopting a compromise reduction
2 of 15% for U S WEST's network maintenance expenses. Again, there is no record support for
3 the 15% figure and it will result in UNE prices that are not cost-based, contrary to the
4 requirements of Section 252(d) of the Act.

5 The 30% reduction used in Hatfield Model 2.2.2 is, if anything, a conservative estimate
6 of the cost savings that would result from forward-looking network technology. In fact, after
7 substantial review and analysis, later versions of the Hatfield Model have adopted a 50%
8 network maintenance cost reduction. This 50% reduction has been substantiated by estimates of
9 maintenance cost savings provided by other ILECs. See Attachment 2 to AT&T's Exceptions
10 filed July 21, 1997, pp. 74-75. Based upon the evidence presented, the Commission should
11 adopt the 30% network maintenance factor reduction recommended by AT&T and other parties.
12 There is no record evidence to support shaving 50% off the Hatfield Model results.

13

14 **I. Cost of Capital**

15 The Arbitrators' Decision applied the capital structure and cost of capital from Decision
16 No. 58927, with minor modifications to the cost of debt and equity based on U S WEST's actual
17 experience. The resulting composite cost of capital was 10.06%. The Commission, however,
18 again based on no record evidence whatsoever, increased the cost of capital from 10.06% to
19 10.37%. This change is not supported by the record, is not reflective of what U S WEST's
20 experience will be in the emerging competitive environment and should be rejected as non cost-
21 based in violation of the Federal Act.
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1
2
3 **CONCLUSION**

4 The portions of the Commission Order cited above are not based on record evidence, are
5 inconsistent with the requirements of Section 252 of the Act because they are not cost-based and,
6 as a result, will severely deter the development of local service competition in Arizona. For
7 these reasons and those stated above, AT&T requests reconsideration of the above decisions by
8 the Commission.

9
10 **DATED this 19th day of February, 1998.**

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the Mountain States, Inc.**

CERTIFICATE OF SERVICE

I hereby certify that the original and ten copies of the Application for Reconsideration of AT&T Communications of the Mountain States, Inc. regarding Docket Nos. T-03021A-96-448 ET AL., were hand delivered on this 19th day of February, 1998, to:

Arizona Corporation Commission
Docket Control - Utilities Division
1200 West Washington Street
Phoenix, AZ 85007

and a true and correct copy was hand delivered on this 19th day of February, 1998, to:

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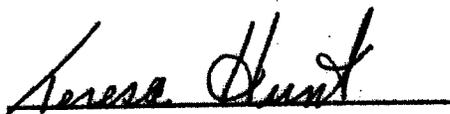
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