IN THE MATTER OF INVESTIGATION
INTO U S WEST COMMUNICATIONS, INC.'S COMPLIANCE WITH CERTAIN WHOLESALE PRICING REQUIREMENTS FOR UNBUNDLED NETWORK ELEMENTS AND RESALE DISCOUNTS

DOCKET NO. T-0000A-00-0194

NEXTLINK ARIZONA INC.'S POST-HEARING BRIEF

I. INTRODUCTION

This Commission long ago recognized the need for competition in the provision of telecommunication services in Arizona. See, e.g., A.A.C. R14-2-1108. Nevertheless, progress in providing true competitive choice to Arizona consumers has been slow. Today, competition using unbundled loops provided by U S WEST totals less than one-third of one percent of the lines U S WEST provides in this state.

One of the reasons that so little competition has developed thus far is the Commission’s adoption of a state-wide averaged loop rate of $21.98. As U S WEST admits, competitors are likely to purchase loops only if the cost of those loops is less than U S WEST’s retail rate for providing basic services. Tr. 62 (Million Cross). New entrants like NEXTLINK cannot profitably provide residential service using unbundled loops where the cost of each loop alone exceeds U S WEST’s residential retail rate. Moreover, the high loop rate combined with the network and marketing expenses a new entrant must incur also discourages competition for business customers. Knowles Direct, p. 6.

This proceeding gives the Commission another opportunity to permit competition to develop in at least some areas of Arizona. Seeking to avoid this result, U S WEST has proposed
only token deaveraging, with a loop rate in its least expensive proposed zone that is only marginally less than the statewide averaged rate. In contrast, AT&T’s proposal would allow competition using unbundled network elements ("UNEs") to develop in areas of the state where such competition makes economic sense. While severely limited by the statewide average prices the Commission has previously determined, AT&T has proposed cost-based deaveraged unbundled loop rates that reflect underlying cost differences and meet the requirements of the FCC. The Commission should adopt AT&T’s proposal.

II. ARGUMENT

A. FCC Requirements.

Congress and the FCC have recognized the vital importance of UNEs as a means for new entrants to provide local exchange service to a broad range of potential customers without having to duplicate an incumbent local exchange carrier’s entire network. See, e.g., In re Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98, FCC 96-325, First Report and Order ¶¶ 10-14 (August 8, 1996) ("Local Competition Order"). A new entrant’s ability to take advantage of the ILEC’s scope and scale, however, depends in large measure on the price the new entrant must pay to use ILEC facilities. For this reason, Congress required that UNE rates must be “based on cost.” 47 U.S.C. § 252(d)(1)(A)(i). "Deaveraged rates more closely reflect the actual costs of providing interconnection and unbundled elements.” Local Competition Order, ¶ 764. Accordingly, the FCC has required that each state create “a minimum of three cost-related rate zones to implement deaveraged rates.” Id. ¶ 765. In addition, each state may “establish more than three zones where cost differences in geographic regions are such that it finds additional zones are needed to adequately reflect the costs of interconnection and access to unbundled elements.” Id.
B. Application In Arizona.

In Arizona today, the statewide average unbundled loop rate alone exceeds the retail price of residential service provided by U S WEST. As competitive local exchange carriers ("CLECs") predicted when this rate was adopted, the effect of this high rate has been to prevent any significant competition within Arizona using UNEs. U S WEST provides slightly more than 8,000 unbundled loops to competitors throughout Arizona. Knowles Direct, page 6. As even U S WEST admits, this is the natural result of an unbundled loop rate that alone exceeds U S WEST's retail residential rate. Million Direct, page 9. New entrants simply cannot economically use unbundled loops to provide local exchange service in Arizona at the statewide averaged rate adopted by the Commission.

Geographic deaveraging of unbundled loop rates to reflect the underlying cost of those facilities more accurately provides the Commission with an opportunity to allow competition to develop in at least some parts of Arizona. Recognizing this, U S WEST has presented a proposal that provides for almost no deaveraging, allowing U S WEST to continue to avoid UNE competition. In contrast, AT&T's proposal would permit competition to begin to develop. For this reason, NEXTLINK and other competitive carriers believe that the AT&T proposal should be adopted on an interim basis in this docket.

C. AT&T's Proposal.

AT&T's proposal establishes interim geographically deaveraged loop prices in five zones by grouping together wire centers based on loop costs within the wire center. Loop costs within each wire center are calculated using the HAI model, a successor to the model adopted by the Commission in the Consolidated Cost Docket. This proposal meets the FCC's requirement to establish different rates for elements reflecting geographic cost differences in a minimum of three zones. See 47 C.F.R. § 51.507(f). Moreover, the AT&T proposal is relatively easy to implement and will allow competition to develop in at least some parts of Arizona. Denney Direct, p. 9.
A review of AT&T’s proposal makes it clear that loop costs do vary significantly among wire centers.\(^1\) Based on the statewide average rate of $21.98, loop costs calculated by the HAI model range from $11.26 to $336.34. Denney Direct, Att. A. Given the broad range in loop costs that exist in this state, it makes sense to establish more than the FCC’s minimum of three zones so that deaveraged loop prices will more closely approximate the actual cost of providing loops. As Mr. Denney explained, rates set close to the actual cost of provisioning a loop give competitors and others in the market appropriate signals regarding whether purchasing an unbundled loop to provide service is economically rational. Denney Direct, pp. 3-4. AT&T’s proposal of five zones increases the areas in which new entrants may economically use unbundled loops to provide local exchange service without creating difficult implementation issues that would delay the availability of geographically deaveraged rates.

NEXTLINK remains concerned that even five wire center-based zones severely limit the areas in which the use of unbundled loops is economically viable in Arizona. Even under Mr. Denney’s proposal, it will be uneconomical for new entrants to purchase unbundled loops in more than half of the wire centers in the state. See Denney Direct, Att. A. In other jurisdictions, NEXTLINK has proposed further deaveraging prices at a sub-wire center level based on distance from the wire center as a way to increase competition and encourage customer choice. Knowles Direct, p. 8. Distance-sensitive prices on a sub-wire center level would make more wire centers potential candidates for initial competitive entry and would encourage expansion of the initial base in each wire center as the new entrant seeks to maximize its initial investment. Presently, however, it appears that the costs of implementing distance sensitive prices on an interim basis are prohibitive. Although NEXTLINK continues to take the position that distance sensitive pricing on a sub-wire center level makes sense for permanent unbundled loop deaveraging, AT&T’s proposal is the most sensible compromise on an interim basis.

\(^1\) The Staff’s proposal also demonstrates the wide variability in wire center costs.
D. **Staff Proposal.**

Staff’s proposal in many respects mirrors that made by AT&T. Nevertheless, there are problems with Staff’s proposal that have compelled NEXTLINK to endorse the AT&T proposal instead.

From a policy perspective, the most serious concern with Staff’s proposal is the failure of that proposal to sufficiently deaverage costs. Staff has proposed only three zones, with a loop rate of $16.95 in zone one, $19.97 in zone two, and $32.41 in zone three. All of these loop rates substantially exceed U S WEST’s rate for residential retail service. As U S WEST admits, rates for unbundled loops exceeding U S WEST’s residential rate will prevent the use of unbundled loops in providing service to residential customers, stifling competition in Arizona. Tr. 62 (Million Cross). The more substantial deaveraging proposed by AT&T, in contrast, will allow at least some residential competition to develop in the state.

There are also technical concerns with staff’s proposal. As Mr. Rowell admitted, there is a question concerning the line counts used in performing the wire center cost analysis. Staff’s line count substantially undercuts that of both U S WEST and AT&T. Tr. 87, 124. In addition, the Hybrid Cost Proxy Model used by staff in calculating loop costs by wire center was designed to determine cost for services, not costs for individual unbundled elements. Tr. 88 (Denney Direct). Moreover, this is not a model that has been reviewed and accepted by the Commission. For these reasons, the loop costs generated by the model are suspect.

E. **U S WEST Proposal.**

In contrast to the AT&T and staff proposals, U S WEST’s proposal is “geographic deaveraging” in name only. U S WEST has proposed prices for three “zones,” but two of the three zones each contain less than three percent of U S WEST’s lines in the state. Almost 95% of the lines are in one zone, with an unbundled loop price that varies only slightly from the current statewide averaged rate of $21.98. These zones were not developed by determining the cost of providing service, but rather by first defining the geographic zone and then determining
the cost within that zone. Tr. 30-31, 33 (Million Cross). In fact, U S WEST admits that costs vary significantly within the zones it has proposed. Tr. 66 (Million Cross). U S WEST’s proposal thus does not comply with the concept of geographic deaveraging, much less with the FCC’s requirements with respect to developing appropriate geographically deaveraged rates.

Moreover, the cost model U S WEST used in developing loop costs within its predefined zones is a successor to the RLCAP model rejected by the Commission during the cost proceeding in this state. Tr. 52, 74 (Million Cross). The results of the cost model bear no relationship to actual geographies or wire centers within the state of Arizona. Instead, the model produces generic results that could as easily apply in North Dakota as Arizona. Tr. 52; 54-56 (Million Cross). For these reasons, the Commission cannot rely upon U S WEST’s proposal to establish deaveraged rates.

U S WEST attempts to support its proposal by arguing that it mirrors the retail structure proposed in U S WEST’s pending rate case. According to U S WEST, deaveraging in accordance with the AT&T or Staff proposals raises a threat of substantial increases in some retail rates. This threat of retail rate deaveraging, however, should carry little, if any, weight in determining whether and how unbundled loops should be geographically deaveraged. Despite the prospect of geographically deaveraged loop rates in Utah, U S WEST did not seek to deaverage its retail prices in that state. Tr. 117-118 (Denney Redirect); see Utah Code Ann. § 54-8b-2.4(3)(b) (permitting rate rebalancing prior to initiation of price cap regulation). U S WEST has also failed to seek rate deaveraging in four other states that have deaveraged loop rates. Tr. 91 (Denney Direct). Moreover, even if retail rate deaveraging became necessary in the future, retail rates need not necessarily mirror unbundled loop rates. Denney Direct, p. 7. In light of this history and the minimal levels of unbundled loops U S WEST is currently providing, the remote possibility that a future need for retail geographic deaveraging may arise is an insignificant consideration.
U S WEST also expresses concern that retail customers would be confused by a retail
deaveraging scheme based on a wire center grouping used to establish geographically
deaveraged unbundled loop rates. As discussed above, however, retail rate deaveraging
historically has not accompanied unbundled loop rate deaveraging, and there is no requirement
that any deaveraged retail prices mirror the deaveraging methodology employed to establish
unbundled loop rates. More fundamentally, U S WEST’s purported concerns directly conflict
with one of the important benefits of effective local exchange competition – downward pressure
on retail rates. The Commission should expect that as competition drives prices closer to cost,
competition-induced price reductions, at least initially, will occur in lower cost areas. Rather
than stifle competition, as U S WEST proposes, by preventing some customers from obtaining
competitive benefits unless and until all customers within a broad “community of interest” can
obtain the same benefit, the Commission should encourage the natural, incremental development
of competition, which will eventually benefit all consumers.

U S WEST also complains that geographic deaveraging of loop prices without also
deaveraging retail rates will threaten universal service. U. S WEST, however, has produced no
evidence that geographic deaveraging of loop rates has threatened the availability of universal
service in any other state. Moreover, in Arizona, U S WEST has admitted that even its rural high
cost exchanges are profitable. Tr. 115 (Denney Cross). Universal service cannot, therefore,
suffer any adverse impacts from geographic deaveraging of unbundled loop rates.

III. CONCLUSION

Geographic deaveraging allows this Commission an opportunity to permit the
development of competition in Arizona. The proposal made by AT&T for geographic
deaveraging of unbundled loop rates will permit competition to occur in at least some parts of the
state. For this reason, AT&T’s proposal should be adopted.
DATED this 26th day of May, 2000.

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CERTIFICATE OF SERVICE

I hereby certify that the original and 10 copies of the NEXTLINK ARIZONA INC.'s Post Hearing Brief regarding Docket No. T-00000A-00-0194, were hand delivered on this 26th day of May, 2000, to:

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