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May 3, 2004

Honorable Deborah Taylor Tate, Chairman
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, Tennessee 37238

Re Petition for Arbitration of ITC^DeltaCom Communications Inc , with BellSouth Telecommunications Inc , Pursuant to the Telecommunications Act of 1996
Docket 03-00119

Dear Chairman Tate·

On April 8, 2004, BellSouth filed a letter in this proceeding claiming to respond to ITC^DeltaCom's April 6, 2004 procedural request that the Authority rule on the remaining open issue in its arbitration, the "just and reasonable" rate for local switching that would apply to lines subject to the "4-line carve-out" adopted by the FCC in its UNE remand decision.[1] In large part, BellSouth's correspondence reiterates its continuing objection to the Authority's jurisdiction to resolve the pricing dispute between ITC^DeltaCom and BellSouth, even though the Telecommunication Act unambiguously assigns this role to state commissions[2] It is not our purpose here to further debate BellSouth's argument on this point In our view, the Authority has correctly interpreted its responsibility and appropriately directed each to file its best and final offer before issuing its ruling

There is one area discussed by BellSouth, however, that ITC^DeltaCom is compelled to address Although the Authority's procedural direction did not include a "rebuttal" opportunity with respect to each parties' "best and final offer," BellSouth has nevertheless used the guise of

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[1] The "3-line carve out" permits BellSouth to (potentially) charge different rates to CLECs using unbundled local switching to serve customers with more than 3 lines in certain end-offices in Nashville (which qualifies as one of the top 50 MSAs in the nation)

[2] BellSouth never disputes that it must offer unbundled local switching in order to remain in compliance with the competitive checklist of section 271 of the Act (and enjoy the opportunity to offer long distance services in Tennessee) Nor does BellSouth dispute that section 271 unambiguously requires that it must satisfy its competitive checklist obligations through interconnection agreements (§271(c)(2)(A)), that such agreements are required to have been *approved* under section 252 of the Act (see §271(c)(1)(A)), and that the Act makes clear (as the agency has ruled in a number of dockets, including this one) that states are to arbitrate all open issues in such agreements (such as the rate at issue here)

its procedural response to ITC^DeltaCom to try and introduce new "evidence" addressing ITC^DeltaCom's offer to pay a $5 08 rate per switch port. BellSouth goes so far as to call ITC^DeltaCom "disingenuous," characterizing its proposal as offering "free usage," and charging that ITC^DeltaCom is attempting to take "the market out of market rate "[3] In addition to its rhetorical excess, BellSouth makes one substantive claim – that ITC^DeltaCom's best and final offer is "materially indistinguishable" from TELRIC.

There are three ways to show that ITC^DeltaCom's offer is an honest "best and final offer" that is materially distinguishable from TELRIC First, we compare our proposed flat-rate switching rate to the other flat-rate TELRIC charges established throughout the country, including a rate recently established by the Federal Communications Commission for Verizon-Virginia. This comparison demonstrates that TELRIC-based flat-rate charges are within a relatively narrow range and well below the rate proposed by ITC^DeltaCom here. Second, we summarize the analysis that accompanied our offer that demonstrated that the proposed flat rate is above the average TELRIC rate imposed by BellSouth in Tennessee today. And finally, in a proprietary attachment to this letter, we demonstrate that the rate proposed by ITC^DeltaCom would materially increase the rates paid by ITC^DeltaCom for switching based on ITC^DeltaCom's specific usage in Tennessee

As indicated above, a number of states and, most recently, the Federal Communications Commission, have established TELRIC-based rates for local switching using an entirely fixed (or flat) rate per port, without a usage component Although BellSouth characterizes this rate structure as "free usage," a flat rate structure better reflects how costs are actually incurred.[4] These analyses – performed around the country by different regulators – produce a relatively narrow estimate of the TELRIC cost of unbundled switching As shown below, the rate proposed by ITC^DeltaCom is far above these TELRIC-based rates

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[3] Although we generally avoid responding to BellSouth's rhetoric, there are a number of points that must be made First, as we have repeatedly explained, the FCC never authorized BellSouth to charge "market rates," except in those unique circumstances where a market would be expected to produce just and reasonable rates (i e , where a competitive market exists) In this regard, we note that BellSouth's repeated claim that "market rates" should be unrelated to cost is an economic absurdity – one of the defining characteristics of a functioning market is that prices are forced towards cost The fact that BellSouth has successfully imposed its unjustified $14 rate on other CLECs proves only that it enjoys monopoly power, not that a market exists

[4] Attached are the relevant pages from the Federal Communications Commission's decision in the Virginia Arbitration explaining the superiority of a flat-rate structure for switching Memorandum Opinion and Order, CC Dockets 00-218 & 00-251, August 29, 2003

Comparing ITC^DeltaCom Offer to TELRIC[5]

State	TELRIC Rate	DeltaCom Proposal	Premium
Illinois	$2 18	$5 08	133%
Indiana	$2 98	$5 08	70%
Wisconsin	$2 83	$5.08	80%
Utah	$3.55	$5.08	43%
Minnesota	$3.12	$5.08	63%
FCC (Virginia)	$2.83	$5 08	80%
Average	$2.92	$5 08	74%

Second, attached to ITC^DeltaCom's best and final offer was a detailed analysis demonstrating that its proposed rate was above both BellSouth's embedded cost of switching and the current TELRIC rates established by the Authority. Because the existing TELRIC based rates include both a flat charge (per port) and a usage component, any comparison to ITC^DeltaCom's flat-rate proposal must incorporate a measure of average usage ITC^DeltaCom provided a clear a detailed explanation as to how it calculated average usage (3,622 minute per line) based on BellSouth's ARMIS filing with the FCC [6] Applying the TRA-approved TELRIC rates produces an average usage charge of $2.33 that,[7] when added to the existing port rate of $1.70,[8] yields a TELRIC-based charge of $4 03, substantially below ITC^DeltaCom's best and final offer (resulting in a premium of 26%).

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[5] Table includes only those jurisdictions that have adopted a flat rate structure such as included with the ITC^DeltaCom best and final offer

[6] As shown on Attachment 1 to ITC^DeltaCom's best and final offer, average usage was calculated by dividing BellSouth's reported Dial Equipment (Local Switching) Minutes from ARMIS 43-04 (Row 1216) by the BellSouth's reported Switched Access Lines (ARMIS 43-08, Row 530)

[7] Because calls that terminate on the same switch where they originate are billed only once for local switching, the analysis assumed that 40% of the calls remained "within" the switch The reasonableness of this assumption was generally confirmed by BellSouth testimony in South Carolina which indicated that 33 4% of its calls where intraswitch (Direct Testimony on Robert McKnight on behalf of BellSouth, Public Service Commission of South Carolina (McKnight Direct), Docket No 1977-239-C, filed December 31, 2003)

[8] BellSouth's August 8th letter incorrectly claims that the port rate for local switching in Tennessee in $1 89 when, in fact, the port rate for local switching as part of UNE-P is $1 70 as per BellSouth's Statement of Generally Available Terms and Conditions The relevant page from the SGAT is attached hereto The rate for "stand-alone" local switching (that is, local switching purchased independently of the loop) is commercially irrelevant – the reason that carriers lease local switching is to gain efficient access to BellSouth's monopoly loop network (i e , as part of

Third, ITC^DeltaCom has compared its proposed best and final offer to its own usage profile to confirm that its analysis was reasonable. This comparison (summarized in the confidential attachment) demonstrates that ITC^DeltaCom's actual usage is substantially below BellSouth's average usage and, as a result, its best and final flat-rate offer provides a higher premium above the TRA-set TELRIC rate than the premium based on BellSouth' average usage. As shown in the Confidential Attachment, ITC^DeltaCom's best and final offer would increase its charge for local switching by nearly 50% based on its actual usage profile. In addition, the Confidential Attachment summarizes for the Authority the premium estimated provided by the ITC^DeltaCom best and final offer from each of the three perspectives set forth above – comparing the best and final offer to (1) the TELRIC based flat rates established by Commission's around the country, (2) an estimate based on BellSouth's average usage in Tennessee, and (3) the rate paid by ITC^DeltaCom today based on it's actual usage No matter which perspective the Authority finds most reasonable, each clearly demonstrates that ITC^DeltaCom's best and final offer is a good faith proposal that is "materially distinguishable" from TELRIC [9]

In contrast to the powerful array of evidence above, BellSouth's bases its claim that the ITC^DeltaCom's offer is materially indistinguishable from TELRIC on the assertion – never supported by fact – that the average usage revenue for unbundled local switching is $3.23 per line.[10] The total "support" for this claim is the cryptic statement in its attachment:

> This figure is based on the TRA's usage rate per MOU and average usage characteristics consistent with FCC data Accordingly, we [BellSouth] think the $3.23 is a reliable number

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UNE-P) Consequently, any comparison between ITC^DeltaCom's proposal and the existing TELRIC rate should be based on the TELRIC rate for switching purchased as part of UNE-P

[9] We remind the Authority that ITC^DeltaCom believes that the existing TELRIC-based rates are just and reasonable and should remain in effect, even for network elements required under section 271 of the Act We respect. however, the Authority's decision to request best and final offers based on some other approach

[10] As noted earlier, BellSouth further distorts its analysis by basing the switching comparison to the *higher* port rate for switching purchased independently of usage (while comparing the ITC^DeltaCom total charge for UNE-P to the *lower* port rate purchased as part of a combination) The only comparisons that are relevant are comparisons that are premised on a loop-port combination, which means the lower loop and port charges associated with UNE-P BellSouth currently provides a lower port charge associated with UNE-P in its general offering to all CLECs The TRA approved BellSouth's SGAT and the lower port charge

This statement is hardly more credible than BellSouth's earlier support for its $14.00 rate Based on the TRA's usage rate of $0.0008041/minute, BellSouth's claim is equivalent to average usage in excess of 4,000 minutes per month, even assuming that no call ever terminates on the switch where it originates. If adjusted for the fact that local switching charges are applied only once on minutes that terminate within the switch, the average usage underlying BellSouth's revenue claim exceeds 5,600 minutes per month (roughly 4 7 hours per business day)

ITC^DeltaCom has fully complied with the Authority's request that it put forth a best and final offer for local switching provided in compliance with section 271 (but not necessarily section 251) of the Act. ITC^DeltaCom's proposal is clearly just and reasonable, as required by the FCC. BellSouth's criticisms of the proposal are both untimely and inaccurate

Very truly yours,

BOULT, CUMMINGS, CONNERS & BERRY, PLC

By: Henry Walker KG
Henry Walker

HW/pp

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing has been forwarded via U.S. Mail, postage prepaid, to:

Guy Hicks
333 Commerce Street
Suite 2101
Nashville, TN 37201-3300

on this the 3rd day of May, 2004.

Henry Walker KG

Henry Walker

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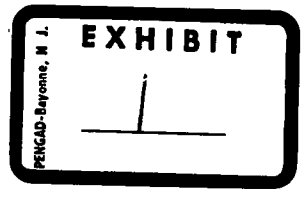
Before the
Federal Communications Commission
Washington, D.C. 20554



In the Matter of	)	
	)	
In the Matter of Petition of WorldCom, Inc.	)	
Pursuant to Section 252(e)(5) of the	)	CC Docket No. 00-218
Communications Act for Preemption of the	)	
Jurisdiction of the Virginia State Corporation	)	
Commission Regarding Interconnection	)	
Disputes with Verizon Virginia Inc., and for	)	
Expedited Arbitration	)	
	)	
In the Matter of Petition of AT&T	)	
Communications of Virginia Inc , Pursuant to	)	CC Docket No 00-251
Section 252(e)(5) of the Communications Act	)	
for Preemption of the Jurisdiction of the	)	
Virginia Corporation Commission Regarding	)	
Interconnection Disputes With Verizon	)	
Virginia Inc.	)	

MEMORANDUM OPINION AND ORDER

Adopted: August 28, 2003 **Released:** August 29, 2003

By the Chief, Wireline Competition Bureau

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461 AT&T/WorldCom assert that much of the total cost of a switch is associated with memory and processors and is incurred at the time a switch is placed in operation.[1173] According to AT&T/WorldCom, these "getting started" costs do not vary with usage [1174] They further assert that the majority of the costs of today's generation of digital switches is driven by ports, rather than usage, and only a very small percentage of the overall equipment in current digital switches is engineered based on peak-period usage.[1175] According to AT&T/WorldCom, based on actual Verizon total switch costs, most costs are non-usage sensitive and should be allocated to the port rather than MOU rate elements.

462 AT&T and WorldCom diverge slightly with regard to the precise allocation between usage and non-usage sensitive rate elements. AT&T recommends that Verizon continue to assess switching charges using the rate design currently in place, *i e.*, a separate fixed monthly port charge to recover the non-usage sensitive switch costs as well as a per MOU charge to recover the usage sensitive costs.[1176] Specifically, AT&T agrees with Verizon that shared, peak-period costs should be recovered on a usage sensitive basis [1177] WorldCom argues that all costs, even the shared, peak-period costs, should be recovered through a flat-rated port charge.[1178]

3. Discussion

a. "Getting Started" Costs

463 We conclude above, for purposes of determining the appropriate switch discount, that the "getting started" cost of the switch is a fixed cost, meaning that it does not vary with the number of ports or the level of usage on the switch [1179] We find here that the "getting started" costs of the switch should be recovered on a per line port basis. "Getting started" costs are incurred for capacity that is shared among subscribers. Verizon incurs these costs to be ready to provide service upon demand Given the record evidence that modern switches typically have large amounts of excess central processor and memory capacity,[1180] the usage by any one subscriber or group of subscribers is not expected to press so hard on processor or memory capacity at any one time as to cause call blockage, or a need for additional capacity to avoid such

[1173] AT&T/WorldCom Ex 4, at 7

[1174] *Id*

[1175] *Id*

[1176] AT&T Ex 4 (Kirchberger Direct), at 13-14

[1177] *Id*

[1178] WorldCom Ex 6, at 7

[1179] *See supra* section V(C)(1)(b)(i)

[1180] *See supra* para 391

blockage. Thus, no one subscriber or group of subscribers is any more or any less causally responsible for the processor or memory capacity costs. Principles of cost causation, therefore, support a per line port cost recovery approach because, more than any other approach, it spreads getting started costs to carriers in a manner that treats equally all subscribers served by a switch.

464. In addition, charging a per line port price for the central processor and memory recovers these costs from competitive LECs on a competitively neutral basis, thereby potentially extending to many different subscribers the benefits of competition The incumbent LEC incurs central processor and memory costs in order to provide service to all of the subscribers served by the switch's line ports. A competitive LEC may serve some of these subscribers and the incumbent LEC may serve some of these subscribers. The incumbent LEC's central processor and memory costs do not vary with respect to whether a subscriber connected to its switch is a high or low volume user, a residential or business user, or a peak-period or off-peak-period user A competitive LEC faces no advantage or disadvantage in competing against the incumbent LEC if it pays for use of the central processor and memory on a per line port basis. If the incumbent LEC chooses to recover relatively more or less of the central processor and memory cost from high volume business users or low volume residential users, for example, the competitive LEC is able to compete with the incumbent LEC (or another competitive LEC) by doing the same.

465. A per MOU price for the central processor and memory, in contrast to a per line port price, would not recover these costs on a competitively neutral basis. Again, the incumbent LEC's central processor and memory costs do not vary with respect to whether a subscriber connected to its switch is a high or low volume user, a residential or business user, or a peak-period or off-peak-period user A competitive LEC suffers a competitive disadvantage for high volume users relative to the incumbent LEC if the incumbent LEC recovers central processor and memory costs from the competitive LEC on a per MOU basis The competitive LEC would pay more to serve the high volume users, while the incumbent LEC could recover the central processor and memory costs, which do not vary with usage, on a per line basis from all of its subscribers, including high volume users Principles of cost causation do not, therefore, support a per MOU price, because it would recover proportionately more of the "getting started" costs from high usage subscribers than from low usage subscribers

466. We disagree with Verizon's argument that it "grows" or replaces virtually all of the components of a switch over its life and that, therefore, costs for the central processor are usage sensitive and should be recovered on a per MOU basis [1181] Verizon fails to show that it would expect to replace the central processor of a modern switch for the specific reason that usage increases over the life of the switch It identifies three reasons why the processor would be replaced. First, manufacturers continuously upgrade switch software to improve the operational and administrative efficiency of the switch [1182] These software upgrades at some point require an upgrade to the processor. Second, software is added frequently over time to add

[1181] Verizon Ex 123, at 6-12

[1182] Tr at 5435

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[1181] Verizon Ex 123, at 6-12

[1182] Tr at 5435

the capability to provide new vertical features as they are developed or to accommodate new regulatory mandates such as number portability.[1183] The software added to the switches over time for these reasons at some point requires a processor upgrade. Third, an increase in subscriber usage per line or the number of lines connected to the switch may increase to the point at which the processor must be augmented.[1184]

467 The first two reasons for replacing or upgrading the processor relate to obsolescence, not to the level of subscriber usage over time Switch obsolescence is accounted for in the useful life of the switch prescribed for estimating the depreciation expense recovered in the switch prices. Showing that the central processor may be replaced due to obsolescence does not demonstrate that processor capacity costs are usage sensitive or should be recovered on that basis. We note that for purposes of determining depreciation expense we have adopted an asset life at the low end of the Commission's safe harbor range: 12 years.[1185] We believe that this relatively short switch life is adequate to reflect the need to upgrade the processor for reasons of obsolescence [1186]

468 With respect to the frequency with which Verizon would expect to augment the central processor or memory of the switch as usage increases, the only evidence adduced is that processor switch blocking occurred in New Hampshire [1187] Verizon did not indicate, however, how many switches or subscribers connected to these switches experience blocking, or even whether these switches were modern digital switches. Instead, most of the written and oral testimony and evidence supplied by Verizon and AT&T/WorldCom, as discussed above, indicates that the central processor and memory of a modern switch installed today are unlikely to exhaust as a result of increased subscriber usage.[1188]

b. EPHC Costs

469 EPHC costs relate only to the Lucent 5ESS switch.[1189] The 5ESS switch is based

[1183] *Id*

[1184] *Id* at 5435-36

[1185] *See infra* section III(D)

[1186] The useful life for estimating depreciating expense reflects the average life of the various components of a switch There is no separate useful life for each separate component of the switch, such as the central processor

[1187] Tr at 5448

[1188] Verizon also provided in its surrebuttal testimony examples of various "getting started" components of the switch that it has grown or replaced Verizon Ex 122, at 176-78 Verizon explains that the majority of these components were upgrades developed by the switch manufacturer Again, the fact that Verizon upgrades the "getting started" equipment does not demonstrate that these costs are incurred as a result of increases in subscriber usage As we discuss above, moreover, Verizon does not provide empirical evidence to quantify the extent to which it has grown or replaced the "getting started" components of the switch *See supra* section V(C)(1)(b)(i)

[1189] Verizon Ex 123, at 10 EPHC stands for "equivalent POTS half call "

on a distributed processor architecture. The primary building block of the Lucent 5ESS distributed processor architecture is the switching module.[1190] The common equipment of the switching module consists of a processor complex and equipment designed to terminate line interface and trunk interface equipment.[1191] These common equipment costs are referred to as EPHC costs in the SCIS model output work papers.

470. The parties agree that in general port capacity is reached before processor capacity in the Lucent 5ESS switch modules.[1192] The SCIS model user guide indicates that the switch modules in the Lucent 5ESS switch by design have excess call capacity and that they therefore are expected to be port limited rather than terminal limited.[1193] AT&T/WorldCom argue that there is excess call capacity for every switch in the Verizon switch cost study [1194] When the number of ports on the switch module reaches capacity, a new switch module is purchased That is, according to AT&T/WorldCom, the port capacity exhausts before the call capacity of these modules. Verizon states that Lucent has evolved the processor capacities of these modules to stay one step ahead of call volume demand, thereby enabling the modules to avoid processor exhaust [1195] It did claim, however, that there are circumstances where the processor capacity is reached before the port capacity of the module.[1196]

471. We conclude that EPHC costs should be recovered on a per line port basis EPHC costs, like "getting started" costs, are incurred for capacity that is shared among subscribers. Verizon incurs these costs to be ready to provide service upon demand. The balance of the record evidence supports a finding that the Lucent 5ESS switch module costs do not vary with respect to usage. Verizon states that there are circumstances when the processor capacity of the module may be increased before its port capacity is reached, or when port demand is limited in order to avoid processor exhaust, thereby suggesting that the EPHC costs vary with usage.[1197] It did not quantify the frequency with which this occurs, however, nor did it provide any other details regarding these situations Absent such evidence, we cannot conclude that the EPHC costs vary with usage, given the other evidence and testimony in the record. Accordingly, consistent with our analysis of cost causation and competitive neutrality with respect to "getting started" costs, we require that EPHC costs be recovered on a per port basis

[1190] *Id*

[1191] *Id*

[1192] *Id* at 11, AT&T/WorldCom Ex 24, at 16-17

[1193] AT&T/WorldCom Ex 24, at 17, *see also* Verizon Ex 123, at 10

[1194] Tr at 5446-47

[1195] Verizon Ex 123, at 11

[1196] *Id* at 12-14

[1197] *Id*

c. RTU Fees

472. Verizon pays RTU fees to switch vendors for switch software Verizon states that it generally does not pay RTU fees on a per MOU or on a per line basis.[1198] Rather, Verizon most often pays the RTU fees on a per switch basis.[1199] Verizon also states that, in contracts for Lucent switches, which require software to be loaded into discrete service modules, payment might be made on the basis of the number of service modules.[1200] Accordingly, we find that RTU fees should be recovered on a per port basis for reasons similar to those set forth above with respect to "getting started" costs and EPHC costs.

d. Shared Peak-Period Costs

473. The parties agree that shared, peak-period costs – non-ISDN line CCS and ISDN CCS, D channel access PPS, PPB channel access PPS, inter-switch PPS, and SS7 link and trunk CCS – vary with usage.[1201] They are shared capacity costs AT&T/WorldCom emphasize, and Verizon does not dispute, that these costs are incurred for equipment that is engineered and purchased based on peak-period demand.[1202] The record supports a finding that the equipment for which these costs are incurred is a limiting resource and that congestion or blocking will occur as usage increases.[1203]

474. Peak-period users are causally responsible for shared capacity that is engineered to satisfy peak-period demand. The need to install additional capacity to avoid call blocking (or an unacceptably high rate of blocking) by installing more of this equipment results entirely from usage at its peak If off-peak usage were to decrease to zero, no costs would be saved whatsoever. Although the parties all agree that peak-period pricing is correct in principle,[1204] no party proposes a peak-period rate structure because such an approach is extremely difficult to

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[1198] Tr at 5492-93

[1199] *Id* In response to a record request, Verizon states that it generally pays for the right to use software on a "buyout basis" for base generic software Verizon Ex 231 (Verizon response to record request no 47 (requested Nov 29, 2001)) We understand the term "buyout basis" as used by Verizon to be equivalent to a per switch or per module basis Tr at 5494 Buyout basis may also refer to payment on the basis of all or a subset of a carrier's switches Tr at 5155

[1200] Tr at 5493

[1201] Verizon Ex 122, at 195, AT&T/WorldCom Ex 12, at 109

[1202] Verizon Ex 109, at 53, AT&T/WorldCom Ex 12, at 109

[1203] Verizon Ex 109, at 53, AT&T/WorldCom Ex 12, at 109

[1204] Tr at 5475, AT&T/WorldCom Switching Cost Brief at 26

implement in practice [1205] Instead, Verizon and AT&T propose recovery of these costs through a per MOU price that is developed by dividing total cost by total annual minutes of use, not peak-period minutes of use, and imposed on all minutes of use.[1206] In contrast, WorldCom proposes a flat per port price for recovery of these shared, peak-period driven costs [1207]

475. Although neither approach is ideal, we believe that the flat per port price advocated by WorldCom is the better approach A per MOU price for recovery of these shared, peak-period driven capacity costs, as proposed by Verizon and AT&T, would fail to signal to competitive LECs that these costs vary with subscribers' usage during the peak period in particular. Competitive LECs paying for subscribers' off-peak usage based on a price developed by spreading costs over all minutes of use would pay too much relative to the costs for which they bear causal responsibility. Competitive LECs paying this same price for subscribers' peak-period usage would pay too little. A per MOU rate therefore could result in under-utilization of Verizon's switches during non-peak periods and over-utilization during peak periods.

476 A per MOU price for recovery of shared, peak-period costs also may place the competitive LEC at a competitive disadvantage, as WorldCom points out.[1208] Because Verizon's costs vary with peak-period usage, Verizon may be able to recover shared, peak-period costs from its subscribers by offering a per MOU price for peak-period minutes of use and a zero price for unlimited off-peak minutes of use A competitive LEC may not be able to recover its costs by offering the same peak/off-peak prices that Verizon offers, however, because the competitive LEC's costs would reflect how Verizon bills the competitive LEC and not how Verizon actually incurs the cost

477. A flat per port price for recovery of these shared, peak-period driven costs, as proposed by WorldCom, avoids the competitive concerns that arise with a per MOU charge A flat per port price for recovery of shared, peak-period costs also avoids problems in Verizon's switch cost study associated with estimating the minutes of use over which to spread its switching costs. The Verizon study uses a ratio of busy hour minutes of use to annual minutes of minutes of use (BHAR ratio) to convert its estimate of switch costs per busy hour to switch costs per annual minutes of use As explained above, the BHAR ratio that Verizon proposes is flawed because it significantly underestimates the annual minutes of use over which the switching costs are spread.[1209] By spreading switching costs over line ports, rather than annual minutes of use,

[1205] For example, different switches would have different peak periods Peak-period pricing would require either different prices for different switches based on the probabilities of peak-period usage for each switch, or developing some meaningful way to reflect peak-period usage probabilities in statewide or UNE zone average rates

[1206] AT&T Ex 4, at 14, Verizon Ex 115, at 2-3

[1207] WorldCom Ex 6, at 5

[1208] *Id* at 5-6

[1209] *See supra* section V(C)(8), *see also New Jersey 271 Order*, 17 FCC Rcd at 12295, para 48 (noting "serious questions" regarding Verizon's assumptions underlying its busy hour determinations)

this problem is avoided.

478. Verizon argues that flat-rated recovery of costs that vary with usage would result in low volume subscribers subsidizing high volume subscribers.[1210] We have no basis on the record to conclude that Verizon is correct We do not know the extent to which low or high volume subscribers' usage occurs during the peak period or non-peak periods, and, therefore, we do not know whether a flat per port price or a per MOU price imposed on all subscriber minutes is more likely to recover these shared, peak-period driven costs from subscribers in proportion to their peak-period usage. Thus we cannot assess the extent to which low volume users would be subsidizing high volume users, or vice versa, under either rate structure. We acknowledge that the approach we adopt is imperfect in the sense that it would fail to signal to competitive LECs the costs that Verizon would incur if subscriber usage were to increase, which could result in over-utilization of Verizon's switches, and blocked calls, during peak periods. Given that Verizon already offers flat-rated calling to its own end-users,[1211] however, we do not believe that offering similar pricing to competitive LECs would increase the likelihood of blocked calls due to increased calling by competitive LEC customers.

479. AT&T/WorldCom suggest that we adopt different results for the two different agreements before us.[1212] AT&T and Verizon agree that shared, peak-period costs should be recovered through a per MOU charge on all usage As noted above, however, WorldCom argues, and we agree, that these costs should be recovered on a flat, per port basis. Thus, consistent with "baseball arbitration," we could adopt a per MOU charge for the AT&T-Verizon agreement and a flat, per port charge for the WorldCom-Verizon agreement.

480 Verizon argues, however, that prescribing two different rate structures raises the possibility that a competitive LEC paying the flat, per port rate would target high volume users, while a competitive LEC paying the combined flat, per port and per MOU rates would target low volume users,[1213] which might preclude Verizon from recovering all of its shared costs [1214] Verizon is correct in theory. The per port price is an average price and the per MOU price is an average price A carrier serving low volume subscribers would pay Verizon an amount that is less than the overall cost per subscriber, if it pays for the shared peak-period driven capacity costs on a per MOU basis; a carrier serving high volume subscribers would pay Verizon an amount equal to the overall cost per subscriber, if it pays for the shared peak-period driven capacity costs on a per port basis. Verizon would not recover all of its shared costs under this scenario if it were to lose enough high volume and low volume subscribers to these competitive

[1210] Verizon Switching Cost Brief at 23

[1211] AT&T/WorldCom Switching Cost Brief at 26

[1212] *See* AT&T/WorldCom Switching Cost Brief at 27

[1213] Tr at 5474-75

[1214] *Id*

LECs and is unable to recover a disproportionate share of these costs from its own subscribers.

481. AT&T/WorldCom respond that the risk of under-recovery that Verizon would face if it offers two different rate structures is no different from the risk it currently faces by offering its residential subscribers a choice between flat-rated or message unit pricing plans.[1215] They also note that a competitive LEC paying the per MOU price for unbundled switching bears the risk of paying peak-period driven capacity costs for off-peak usage , while Verizon does not incur these costs in off-peak periods or face that risk [1216]

482 We agree with Verizon that a requirement to offer unbundled switching on both a flat-rated, per port basis and a combined flat-rated, per port and per MOU basis creates the potential for under-recovery of switching costs AT&T/WorldCom's analogy to retail rates is not convincing The Commonwealth of Virginia has jurisdiction over the risk of under-recovery that Verizon faces by offering its own residential subscribers flat-rated and message unit pricing options The matter before the Bureau is the risk of under-recovery that Verizon would face if required to offer unbundled switching on both a flat-rated, per port basis and a combined flat-rated, per port and per MOU basis to wholesale customers AT&T/WorldCom allege that the relative risk faced by Verizon due to its retail flat-rated and message unit pricing options is similar to the risk associated with offering competitive LECs both flat-rated, per port and per MOU pricing options, but they did not quantify this risk Nor could we know, based on the record, whether this is an acceptable level of risk for Verizon to bear when selling unbundled switching to competitors. We therefore reject AT&T/WorldCom's arguments that in this proceeding we should require Verizon to offer unbundled switching on both a flat-rated, per port basis and a combined flat-rated, per port and per MOU basis.[1217]

483. Based on the potential for under-recovery that might exist if we require two different rate structures, we find that the shared, peak-period costs should be recovered on a flat, per port basis in both agreements. As explained above, this approach avoids the competitive disadvantages associated with use of a per MOU price imposed on all usage and it avoids the problems involved with estimating the minutes of use over which to spread an estimate of switching costs.

[1215] *Id* at 5478

[1216] *Id* at 5479

[1217] We recognize that the rates we establish in this arbitration proceeding reflect a different mix of port charges and usage charges than the rates contained in Verizon's agreements with other competitive LECs in Virginia Because this would be true even if we allowed Verizon to recover the shared, peak period costs on a per MOU basis, we do not believe the existence of these other agreements is reason not to permit consistency between the two agreements at issue here

BellSouth/CLEC-1 Tennessee Rates
Network Elements and Other Services

BellSouthTelecommunications, Inc.
SGAT Attachment 2, Exhibit B
Rates
August 30, 2002

Cost Element	Network Elements	Unit	Recurring Rate	Nonrecurring First	Nonrecurring Additional	Source of Rate (Docket No.)(P=Permanent; I=Interim)
P.4	DAILY USAGE FILES					
P.4.1	Enhanced Optional Daily Usage File					
P.4.1.1	Enhanced Optional Daily Usage File, Message Recording, Per Message	Message	0.228978			BellSouth Reduction
P.6	UNBUNDLED LOOP COMBINATIONS					
	Note: Pursuant to the Authority decision in Docket No. 97-01262, decided September 25, 2001, the non-recurring rates for all "new" combinations are interim rates that are subject to true-up. Permanent rates shall be established in the Generic Docket to C					
P.1	2-Wire Voice Grade Loop with 2-Wire Line Port	Combination				
	Zone 1		$12.81			97-01262 (P)
	Zone 2		$16.35			97-01262 (P)
	Zone 3		$28.08			97-01262 (P)
P.1.1	2-Wire Voice Grade Loop	$14.12				
	Zone 1		$11.11			
	Zone 2		$14.65			
	Zone 3		$27.89			
P.1.2	Exchange Port - 2-Wire Line Port	$1.70				
P.1.3	2-Wire Voice Grade Loop/Line Port Combo - Switch-as-is	Combination		$1.63	$0.28	97-01262 (P)
	2-Wire Voice Grade Loop/Line Port Combo - NEW	Combination		$22.14	$15.25	97-01262 (P)
P.1.4	2-Wire Voice Grade Loop/Line Port Combo - Incremental Cost Manual Svc. Order vs Electronic	Combination		$30.89	$7.03	97-01262 (P)
P.1.5	2-Wire Voice Grade Loop/Line Port Combo - Subsequent Database Update	Combination		$0.76		97-01262 (P)
P.1.6	2-Wire Voice Grade Loop/Line Port Combo -Subsequent Database Update - Incremental Manual Svc Order vs. Electronic	Combination		$7.97		97-01262 (P)
P.3	2-Wire Voice Grade Loop with 2-Wire DID Trunk Port	Combination				
	Zone 1		$17.32			97-01262 (P)
	Zone 2		$21.56			97-01262 (P)
	Zone 3		$30.16			97-01262 (P)
P.3.1	2-Wire Voice Grade Loop	$10.86				
	Zone 1		$8.55			
	Zone 2		$12.80			
	Zone 3		$21.38			
P.3.2	Exchange Port - 2-Wire DID Trunk Port	$6.78				
P.3.3	2-Wire Voice Grade Loop with 2-Wire DID Trunk Port Combo - Switch-as-is	Combination		$8.76	$5.75	97-01262 (P)
	2-Wire Voice Grade Loop with 2-Wire DID Trunk Port Combo - NEW	Combination		$45.44	$28.94	97-01262 (P)