BEFORE THE TENNESSEE REGULATORY AUTHORITY
Nashville, Tennessee

IN RE: Contested Cost Proceeding to Establish Final Cost Based Rates for Interconnection and Unbundled Network Elements

Docket No. 97-01262

Response of ACSI to BellSouth's Petition to Reconsider

The Tennessee Regulatory Authority's "Interim Order on Phase I," issued January 29, 1999, in the above-captioned proceeding adopts many of the recommendations of American Communications Systems, Inc.("ACSI"[1]) regarding the cost study filed by BellSouth Telecommunications, Inc. ("BellSouth" or "Bell"). BellSouth has now filed a "Petition for Reconsideration and Clarification" asking the TRA to reverse its findings on some of those recommendations. ACSI files this answer in response to BellSouth's arguments.

A. Fill Factors

BellSouth's Petition asserts that "there is simply nothing in the record" to support the fill (*i.e.* utilization) factors recommended by ACSI witness Dr. Marvin Kahn and adopted by the TRA. Petition, at 2. Bell also disputes the TRA's conclusion that the company's utilization rates will increase in the future. *Id.* According to BellSouth, such a conclusion necessarily "assumes that BellSouth imprudently over built in the past." *Id.*

There is, in fact, amply evidence "in the record" to support the TRA's findings. In his pre-filed testimony, at pp. 48-53, Dr. Kahn explains in detail how he developed the fill factors adopted by the TRA. (Contrary to BellSouth's argument that Dr. Kahn's factors allow

[1] ACSI is now doing business under the name e.spire.

"practically no spare capacity" in Bell's network, Dr. Kahn allowed spare capacity of 30% for distribution plant ((pre-filed testimony at 48-49) and 15% for feeder plant. *Id.*, at 51.)

BellSouth's cost study is based on the company's current, actual fill factors. But as the TRA and Dr. Kahn both point out, Bell's methodology is inconsistent with the purpose of developing a forward looking cost study. As competition develops, utilization factors will inevitably increase in comparison to Bell's embedded utilization rates. That does not imply that Bell's current network is "over built," only that competitive pressures will force BellSouth to make more efficient use of its network on a forward looking basis. Rebuttal testimony of Kahn, at 17. As Dr. Kahn also noted, Bell's existing network has been deployed, not merely to offer voice grade service, but "to meet future . . . strategic requirements" such as broadband services. Pre-filed testimony, at 46 and 52. Such excess capacity should not be considered when projecting the costs of offering basic, local exchange service. *Id.*, at 52.

Finally, it should be noted that, although BellSouth now attacks Dr. Kahn's fill factors in the "Petition to Reconsider," the company did not cross-examine Dr. Kahn about this issue except to note that Dr. Kahn's analysis is more conservative (*ie.*, more consistent with BellSouth's position) than the fill factors used in the Hatfield Model. Transcript of February 23, 1998, at pp. 305-306.

B. <u>Depreciation Expense</u>

BellSouth argues that state law requires the TRA to adopt whatever depreciation expense the company proposes in its cost study. Petition at 4-5.

The statute to which Bell refers, T.C.A. § 65-5-209(i), states only that Bell is not required to seek TRA "approval of [BellSouth's] depreciation rates." For example, BellSouth's financial reports filed with the TRA presumably no longer reflect the depreciation rates last approved by the TRA. In this proceeding, however, the TRA is required by federal law to fix "cost-based" rates and, therefore, the agency must independently calculate BellSouth's depreciation costs in order to arrive at cost-based rates. Nothing in T.C.A. § 65-5-70(i) prohibits the TRA from making its own determination of BellSouth's actual depreciation expenses. Even if it did, any such limitation on the TRA's power to fix rates in accordance with the FCC's rules would now be preempted by federal law. *See AT&T Corp. v. Iowa Utilities Board*, 1999 WL 23568 (U.S. January 25, 1999).

C. Network Maintenance Expense

Although the TRA relied upon the testimony of AT&T witness Art Leema on this issue, the TRA's conclusions are also supported by Dr. Kahn's testimony, at pp. 60-64.

D. Operational Support System Costs

As Dr. Kahn testified (pre-filed testimony at pp. 72-74), BellSouth should not be permitted to charge CLECs more than BellSouth charges its own customers for establishing new service. Bell's proposal to extract an up-front, OSS charge every time a CLEC places a service order is precisely the kind of anticompetitive charge that Dr. Kahn described.

BellSouth contends that "the OSS costs at issue pertain only to . . . electronic interfaces that were developed solely for and used solely by CLECs." Petition, at 13. Since the new systems will only benefit Bell's competitors, BellSouth argues that CLECs should pay all of the costs associated with developing and building these systems.

Federal law, however, does not require Bell to build duplicative, electronic interfaces for the use of Bell's competitors. Instead, Bell could have allowed CLECs to use Bell's existing OSS systems. Now, to add insult to injury, Bell argues that the CLECs must reimburse Bell for building these redundant systems that still don't work as well as Bell's own.

As Dr. Kahn testified, a properly executed TELRIC cost study must allocate demand among all anticipated users, both CLECs and ILECs. That's what the "T" in TELRIC means. He explained (pre-filed testimony at 16):

> The relevant increment of demand to estimate network element costs is the *total demand by all users*, including the incumbent. Hence, the "total service" (or total element) designation. ILECs realize economies of scale. Focusing on any volume of output smaller than the total volume realized may result in higher per unit costs than actually realized.

For these reasons, Bell's attempt to allocate all OSS costs to CLECs is inappropriate and inconsistent with TELRIC. The TRA properly allocated those costs among all carriers.

Respectfully submitted,

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