Katherine C. Swaller
Senior Counsel

Southwestern Bell Telephone
One Bell Center, Room 3536
St. Louis, Missouri 63101
Phone 314 235-4099
Fax 314 331-2195

Southwestern Bell

February 16, 1999

The Honorable Dale Hardy Roberts
Secretary/Chief Regulatory Law Judge
Missouri Public Service Commission
301 West High Street, Floor 5A
Jefferson City, MO 65101

Re: Case No. TA-98-115

Dear Judge Roberts:

Enclosed for filing with the Commission in the above-referenced case are an original and fourteen (14) copies of Southwestern Bell Telephone Company's Reply Brief.

Also enclosed is an additional copy to be file stamped and returned to us in the enclosed self-addressed, stamped envelope.

Thank you for bringing this matter to the attention of the Commission.

Sincerely,

Katherine C. Swaller /TM

Enclosures

cc: Parties of Record

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of AT&T Communications of the Southwest, Inc.'s Petition for Second Compulsory Arbitration Pursuant to Section 252(b) of the Telecommunications Act of 1996 to Establish an Interconnection Agreement with Southwestern Bell Telephone Company.	))))))	Case No. TO-98-115

SOUTHWESTERN BELL TELEPHONE COMPANY'S
REPLY BRIEF

PAUL G. LANE
LEO J. BUB
ANTHONY K. CONROY
KATHERINE C. SWALLER
Attorneys for
Southwestern Bell Telephone Company
One Bell Center, Room 3536
St. Louis, Missouri 63101
(314) 235-4099 (Telephone)
(314) 331-2193 (Facsimile)

TABLE OF CONTENTS

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of AT&T Communications of the Southwest, Inc.'s Petition for Second Compulsory Arbitration Pursuant to Section 252(b) of the Telecommunications Act of 1996 to Establish an Interconnection Agreement with Southwestern Bell Telephone Company.	))))))	Case No. TO-98-115

SOUTHWESTERN BELL TELEPHONE COMPANY'S
REPLY BRIEF

The purpose of this docket is to set certain recurring and nonrecurring rates for elements or activities concerning which the Commission had insufficient information in Phase II of the AT&T arbitration. It was in that phase that the Commission, based upon the requirements of the Telecommunications Act of 1996, established the appropriate cost methodology and pricing for the vast majority of Southwestern Bell Telephone Company's (SWBT's) unbundled network elements and resold services. See Final Arbitration Order TO-97-40, July 31, 1997. In its Initial Brief, AT&T argues about cost methodology issues resolved in Phase II and that rates in this phase should be established as if SWBT had completely mechanized systems for ordering and provisioning all wholesale elements and services. AT&T Brief at pp. 7-30, 31-38. In so doing AT&T ignores both the facts in this case (there is not a single transcript reference in AT&T's entire brief) and the law. This Commission is obligated to follow the Courts' interpretation of the Act and to make a determination of cost-based rates relying upon the

record in this case and not AT&T's plea that the Commission set artificially low rates to facilitate competition. See AT&T Brief at p. 10, 14.

This Reply Brief will address the issues which are legitimately before the Commission, the applicable standard of law, the cost methodology properly used by SWBT and then respond to the specific allegations made by AT&T with certain rate proposals.

I. THE SCOPE OF THIS CASE IS LIMITED TO THE APPLICATION OF THE COSTING METHODOLOGY DETERMINED IN PHASE II APPLIED TO THE ELEMENTS AND SERVICES DEFERRED BY THE COMMISSION.

AT&T argues that the scope of this docket should include all issues regarding cost methodology, including those resolved by the Commission in the extensive hearing in Phase II, the cost phase of the AT&T arbitration. In that phase, rates for most unbundled network elements were established. Notwithstanding the Commission's clear directive in its December 23, 1997 Order that the AAS use "the same permanent costing approach adopted in TO-97-40" (AT&T Phase II), AT&T argues that the Commission's directive was only intended to apply to the AAS. See TO-97- 40, Report and Order at p. 52. In the ordering clause, the Commission specifically provided that "the scope of the evidentiary hearing shall be limited as described in this order." Id. at p. 53. In its Brief AT&T states that the Commission directive was "more of a procedural directive than a substantive one, although the Commission may have intended to restate its support for the TELRIC approach." Brief at p. 5. It makes no sense to SWBT that the Commission would have asked its Advisory Staff to use the same global modifications ordered in Phase II, and ordered that the same scope would apply to the Parties, but at the same time to have intended that the Parties would ignore those same modifications in their comments and

testimony and thus have completely different cases presented at the hearings. AT&T did not initiate a new arbitration with new issues and a new 160 (one hundred sixty) day clock under the Act. Clearly this case was opened to address unfinished business from Phase II because insufficient information was available to the Commission in that earlier phase regarding the elements and activities at issue here and thus they were deferred, but the Commission intended the same determinations on cost study inputs to apply here.

AT&T is already pursuing its concerns about the cost study inputs adopted in Phase II by appealing that decision to the federal district court. It is not proper or fair for AT&T to pursue its appellate issues here. If the Court, on appeal, determines that this Commission erred in its adoption of the cost study inputs in Phase II, the case will be remanded and that cost determination can be applied to this case as well.

AT&T also argues that SWBT has refused to raise issues addressed in other jurisdictions. AT&T states:

> The Commission itself has noted that it may use the best information available to it, from whatever source derived, and it appears that AT&T must bring this information to the Commission's attention since SWBT has not reasonably disclosed in Missouri what AT&T has discovered in other jurisdictions.

Brief at p. 7. That ridiculous statement should be recognized for what it is, a failure on AT&T's part to try this case in Missouri and instead to rely upon bits and pieces of the record in other jurisdictions. Although AT&T had an opportunity to review the actual cost studies at issue in this case and in fact signed a nondisclosure agreement to authorize such access, AT&T never conducted a review. AT&T chose instead to rely upon old testimony filed in other jurisdictions regarding other state cost studies. AT&T's recycled testimony carries no weight in this case. Recurring and nonrecurring rates must be

determined in a cohesive fashion since activities, which drive costs, must be divided among the recurring and nonrecurring studies to insure full recovery. See Tr. 248. It is not fair or accurate to argue that since certain adjustments to factors were made in Kansas such adjustments must be made in Missouri, when the costs removed from nonrecurring studies in Kansas were recognized in recurring studies and recovered in those rates. Id. at p. 276. AT&T's specific allegations are addressed in more detail in the final section of this Reply Brief.

II. THE COMMISSION MUST FOLLOW THE COURTS' INTERPRETATION OF THE TELECOMMUNICATIONS ACT WHEN ESTABLISHING PRICES IN THIS DOCKET.

Shortly before the initial briefs were due to be filed in this case, the Supreme Court issued its opinion in the Iowa Utilities Board case (appeal of the FCC's First Report and Order). AT&T Corp., et. al. v. Iowa Utilities Board, et. al, --S.Ct.---, 1999 WL24568 (U.S.), slip op. (January 25, 1999). Although the Supreme Court reversed the Eighth Circuit Court of Appeals decision on certain key issues, it did not disturb a key component of the Act and of this case: an incumbent local exchange carriers is not obligated to modify or improve its network to meet the demands of new entrants. Rather, an incumbent must unbundle its network "as is" and offer parity to new competitors in the manner in which unbundled network elements and wholesale services are delivered. The Eighth Circuit Court explained:

> Subsection 251(c)(3) implicitly requires access to an incumbent LEC's existing network – not a yet unbuilt superior one. [1]

[1] In that same Order, the Court found that Operational Support Systems are network elements which an incumbent must offer on an unbundled basis. *Id.* at 753.

Iowa Utilities Board, et. al. vs. FCC, 120 F.3d 753, 813 (8th Cir. 1997) (emphasis in original).

Without any discussion of the law, AT&T's Brief blatantly urges this Commission to ignore the Act and set prices based upon a completely mechanized, utopian OSS and thus set prices below cost in order to subsidize AT&T's entry into the local market. See AT&T Brief at pp. 10, 14. Both demands must be rejected and the Commission must set prices based upon the actual costs of SWBT's existing network — the same costs and the same network SWBT uses to serve its own customers.

III. SWBT'S PROPOSED PRICES PROPERLY REFLECT THE COMPANY'S EXISTING NETWORK.

AT&T urges the Commission to set nonrecurring prices for unbundled network elements based upon a fully mechanized network and to be generous offers to assume 1% or 2% fallout or that 1%-2% fall orders submitted by AT&T would not be successfully entered and provisioned on a mechanized basis. AT&T states:

> Since the use of electronic interfaces and forward looking processes are assumed, a 1% - 2% fall-out rate is more than an adequate rate of fall-out in a forward looking environment.

Brief at p. 12. AT&T completely ignores the manner in which the network actually operates and the reality that for a UNE or service to be provisioned, it must pass through numerous OSS stations and that each station has its unique fallout potential depending upon the complexity of the requested UNE or service requested. Additionally, AT&T ignores the fact that most complex services or task UNEs used to provision complex services involve manual activity even when they are processes in the most efficient manner possible. Tr.222-225 (Vest). Mr. Vest explained the multi-station nature of

SWBT's OSS, the variety of potential fallout rates and how efficient processes necessarily include manual activities. Tr. 225-229.

As Mr. Vest explained at the hearing, SWBT's OSS is composed of numerous systems which are like stations in an assembly line or factory and although it may be reasonable to assume a very low fallout rate for the ordering portion of a simple resold service, the same assumption would be incorrect for other "stations" for the same order . Additionally, the same would be true and for any station necessary for vastly more complicated unbundled network elements. What the decision really boils down to is whether this Commission believes Mr. Flappan, who has no OSS experience and who has never even attended a demonstration of SWBT's OSS systems, or the 13 (thirteen) SWBT employees with an average of 20 (twenty) years experience who perform on a daily basis, the tasks for which costs were calculated in the studies prepared by Ms. Smith and Mr. Moore. Unless the Commission accepts AT&T's allegation that SWBT employees padded the time records, AT&T's proposal cannot be accepted. See Tr. 202 - 203. Rather than assume improper conduct, with no record to support such inflammatory innuendo, the Commission should look closely at the evidence in this case. SWBT's time estimates are identical when used in a wholesale cost study or in a retail cost study for the equivalent service. Tr. 199-201. SWBT's time estimates are in most cases significantly less than AT&T time estimates used in its own retail cost studies. Id., Tr. 209-210. SWBT's time estimates are obtained from the real employees who perform the real tasks necessary to provision retail and wholesale services. Id.

At the hearing Mike Michalczyk, who supports installation and maintenance activities, explained why the Commission should have complete confidence in SWBT's time estimates:

> The time estimates we did,...we went through significant detail to identify the functions or subtasks involved with the whole service or product that we're providing for our customers.
>
> Within each subtask we defined the items that were completed within that subtask, ordering, order collection, logging, posting, actually performing the installation work....
>
> We verify that with people that have been on the job for a significant number of years. I myself have 23 years experience with installation and maintenance, and called upon people with similar experiences within installation and maintenance and verified the activity.
>
> We took the information, the segment information, formatted it into spread sheets that were again broken down into subtests and asked the people that were actually performing the work, this is real time at work that's being done today, with the people that support the field technicians, the first line managers in the field, to put down the times associated with each one of these subtasks.
>
> This time is not made up. This is time that's done by the technicians in the field. It's real and it's live. It's time that we estimated it would take for the work involved with resale and UNEs. It is also the exact same subtasks that are associated with retail, our own retail operations....
>
> In the accuracy part of it,...that AT&T actually performs similar tasks in their retail services, and it's my understanding that these tasks may have even taken longer for their employees than ours....

Tr. 199-201. Finally, the irony of AT&T's allegation that the time estimates are inflated is Mr. Flappan's statements at the hearing that AT&T is not challenging SWBT's time estimates. Mr. Flappan explained:

> Can I clarify that...We are accepting the time, to the extent that the function needs to be done on fall-out, we accept those times.

Tr. 212.

Accordingly, the only way the Commission can reduce the costs associated with manual activities in Southwestern Bell's studies is to accept AT&T argument that the actual work necessary to process UNE orders and provisions such UNEs should be ignored and that this Commission should simply assume a utopian network that does not require manual activity. Such an assumption would be in violation of the law. See Iowa Utilities Board, supra, at 813. The basis of Staff's recommendation is to simply split the difference between SWBT's and AT&T's proposed rates, rather than try to determine which estimate is accurate. See AAS Report. The Commission does not have the same luxury, the law requires that the Commission make a determination of fact based solely upon the record. State ex rel. Utility Consumers Council, et. al. v. Public Service Commission, 585 S.W.2nd 41, at 49 (Mo. 1979).

IV. SWBT'S PROPOSED PRICES REFLECT ACTUAL COSTS AS DISCLOSED BY COST STUDIES PERFORMED IN COMPLIANCE WITH THE ACT AND COMMISSION'S APPROVED METHODOLOGY.

If one believes Mr. Flappan that AT&T accepts SWBT's time estimates, the only argument AT&T puts forth to artificially reduce SWBT's costs is to ignore the time estimates all together in favor of a fantasy. AT&T argues that SWBT's cost studies are not in compliance with the Act because SWBT did not assume a brand new network with the most efficient facilities possible. Brief at p. 8, 14. The FCC has required forward looking cost methodology, but it does not require the assumption of a mythical, perfect

network, as AT&T advocates. Mr. Bailey explained SWBT's compliance with the law as follows:

> What our studies are are studies that conform with the FCC TELRIC methodology that was issued in 1996. They conform with the TELRIC methodology this Commission ordered in its first arbitration case and we've been using ever since that time.... The federal act doesn't require a competitive circumstance. It says forward-looking.... We're not proposing in this case an embedded methodology...

Tr. 214 - 215. Ms. Smith furthered explained:

> Our cost study methodologies for the nonrecurring has been the basis for all of our arbitrations in every state. And really the issue here is the inputs to our nonrecurring cost model, which Staff has suggested some specific input changes for fall-out and for some of the time estimates....

Tr. 220. The bottom line is that the Commission determined a methodology in Phase II of AT&T's perpetual arbitration and SWBT used that methodology to develop the cost studies underlying the rates at issue in this phase. It seems patently unfair that the bar would be raised in each phase, as AT&T is proposing here.

V. AT&T ALLEGATION REGARDING SPECIFIC RATE PROPOSALS.

(a) ICB Pricing

AT&T argues that ICB pricing is inherently anti-competitive. Brief at p. 19. ICB pricing is being proposed in this case in only seven (7) out of 136 (one hundred thirty-six) cases.[2] Staff supports SWBT's ICB pricing recommendation. See AAS Report, Section 2, Proposed Prices. The Commission has determined that ICB pricing can in some cases be a fair and reasonable pricing methodology. See T0-97-40, Arbitration Order at p. 36.

ICB pricing is appropriate for certain types of multiplexing and for large volume undedicated transport because it insures that the purchaser pays no more than the costs attributable to provisioning that item to that purchaser because these elements are not provisioned frequently and the arrangements are often unique and not subject to rate averaging. The AAS does not reject ICB pricing as inappropriate. In this case ICB pricing is necessary and the only fair approach. AT&T's concerns about competitive harm are baseless. See Brief at p. 20. The pricing methodology determined by this Commission assures that all ICB pricing arrangements will be based upon forward looking costs and therefore fair and reasonable.

(b) Cross Connects

AT&T argues that the prices should be reduced because the AAS Report includes costs for manual activity. Brief at p. 22. Cross connects are necessary to "migrate" SWBT facilities to AT&T when AT&T leases portions of SWBT's network. If the facilities are not transferred in some way to AT&T, AT&T cannot test nor take responsibility for their own customers. Mr. Moore, who sponsored the cross connect cost study in this case explained:

> SWBT must provide for the testing of unbundled network elements in order to maintain the same quality of service for wholesale (UNE) customers as it provides for [retail] customers. SWBT will require testing equipment on its facilities and the exclusion of such equipment will result in prices for such elements that are not compensatory.

Exhibit 9 (Moore Direct) p. 4.

[2] ICB pricing is proposed for certain forms of multiplexing other than DS-1 to voice grade and DS-3 to DS-1, unbundled dedicated transport at the OC 3 and OC 12 level and for OC 3, OC 12 and OC 48 cross connects.

(c) Local Switching FeaturesXAnalog and ISDN

AT&T disputes the proposed $5.00 service order charge and argues that SWBT's costs for service orders are $00.21 Brief at p. 24. AT&T's claim is without merit and has no basis in fact or the record. AT&T did not perform its own cost study and it did not even review the cost study underlying the rate proposal in this case. It is difficult to defend AT&T's proposed rate other than to state the simple truth: it was pulled out of thin air. If AT&T had reviewed the Transcript from the hearing they would recall that at the hearing Mr. Bailey explained that the $5.00 charge was substantially below SWBT's actual costs of service order activity on unbundled elements. He explained that

> [SWBT] did not propose a $5.00 [service order] rate in Missouri. We did not [identify] that as our cost, as I recall. The Commission dictated that [rate] and...that is what we have been using in this round....If [Mr. Flappan] is correct and we should adjust our cost to reflect something, it should not e reflected off the $5.00. It should be reflected off the cost that we submitted.

Tr. 253. TO-97-40 Arbitration Order (December 11, 1996) at p. 45.

AT&T also challenges the time estimates included in SWBT's cost study for local switching features and argues that "using forward looking OSS architecture, there should be no time required for SWBT technicians except for orders which fall-out of the system, which should be minimal." Brief at p. 23. First and most important. SWBT's OSS, which are the best among the incumbent local exchange providers, are what they are. See Exhibit 13 (Affidavit of Randall Vest) at p. 6. AT&T's contention that the Commission should set rates based upon a nonexistent, utopian OSS is contrary to the law and inconsistent with fair competition. The Act requires SWBT to provide parityXthat is that

AT&T gets the benefit of the same systems that SWBT has in place for its retail customers. Iowa Bd. of Utilities v. FCC, supra. To suggest, as AT&T does, that SWBT's rates should be set below cost to incent SWBT to reduce its costs is not only inconsistent with the law, but inconsistent with good business practice and common sense. The systems used to provide service to AT&T are the same systems SWBT uses for its own customers. Self interest provides incentive enough for SWBT to use the most efficient systems possible. Tr. 241. At the hearing Mr. Vest explained that SWBT upgrades its OSS's whenever it makes good business sense to do so.

> Every work station is an organization, and their objectives are to try and process with as little manual intervention as possible...so there is tremendous emphasis on achieving more and more efficiency...As [upgrades] are proposed...they are prioritized in a sequence of the most profitable ones, and then the very top projects each and every year are funded and advances made.

Tr. 241.

Setting below cost rate assumes that the incentive to provide low cost service does not already exist. As the witnesses explained, the time estimates that go into the wholesale cost studies are the same inputs into the retail cost studies where SWBT is attempting to derive low prices to meet the competition. Tr. 200. Finally, it is important to note that time estimates do include mechanization that is expected to occur in the near future and so some costs are actually understated based upon current business practices. Tr. 244. Accordingly, SWBT is already understating its current costs to AT&T's benefit.

(d) Unbundled Call Trace Per Activation and Other Unbundled Switching Features, Unbundled Dedicated Transport, LIDB

AT&T continues to argue for a mythical 1%-2% fallout rate. Brief at p. 25. The 1% AT&T supports is based upon taking a statement of SWBT OSS expert Liz Ham

made out of context and in another proceeding concerning the order processing (front office) activity on a simple resale order and attempting to misapply it to back office activity (provisioning) for an unbundled element. To make such an argument without discussing the context of the original statement borders on dishonesty. Ms. Smith explained the 1% fallout notion at the hearing,

> I need to clarify that the 99% flow-through that Mr. Flappan has been using in his testimony is from Liz Hamm's presentation to the Texas Commission of OSS. That was for a residential [retail] service rep, Southwestern Bell's service rep, who had processed an order, typing it in correctly and putting all the information in correctly. I must point out too, that that was for the EASE system, consumer EASE, which is only used for resale. It is not used for UNEs. So to use that 99% and apply it to UNEs, it's not proper to do that.

Tr. 255-256. Mr. Vest also explained how the 1% only applies to the front office, simple ordering, function and not the more complex provisioning activities and how unrealistic it is to apply that fallout rate to back office functions:

> Mr. Flappan...is attributing 1 to 2 percent to the front office systems and zero percent...to the back end in total. And I am going to tell you, that's just terribly unrealistic based upon our history and years of trying to go through these complex processes. No. 1, there's more processing at the back end, and perhaps I need to reemphasize what I said when I went through this. We're using the term fall-out and flow-through as if they were contrarian numbers. That's not true. Flow-through means no human intervention.
>
> Human intervention can include someone addressing something that did fall out, but it also can be that component where we have found it to be the most cost-efficient process, the best service to have that human operator do the process.

Tr. 258. To achieve the type of flow through advocated by AT&T would not produce better service or lower costs. Mr. Vest explained:

> If you gave me unlimited...funds to try and save two operators, it is true we may be able to derive some extremely costly computer to replace the two or three people doing the function, but that is just not practical. Humans still have a place in actually operating the processes....

Tr. 258. Accordingly, this Commission should ignore AT&T's request that the Commission ignore both the law and the facts and recognize the actual activity involved in provisioning unbundled call trace and other switching features and determine rates to cover the costs associated with those activities.

(e) Branding/Rating

AT&T argues that SWBT's proposed rates do not reflect a competitive market. Brief at p. 27. AT&T misses the point. SWBT's studies use the methodology determined by the Commission in Phase II of the AT&T arbitration and the studies are consistent with the Act. Mr. Bailey responded to this allegation at the hearing and explained:

> Our studies...conform with the FCC TELRIC methodology...the Act does not require a competitive circumstance. It says forward-looking....That is what we did here. We're not proposing in this case an embedded methodology.

Tr. 214

(f) Simple and Complex Service Conversions

AT&T argues that on simple conversions there should be no manual activity except for fallout and that computer time should be eliminated from the nonrecurring rates. Brief at p. 28. It is interesting that AT&T should argue for no manual simple

service orders when in fact that is the only way AT&T presently submits orders to SWBT. AT&T's reliance on manually submitted orders is in marked contrast to the significant number of CLECs in Missouri who are submitting orders on an electronic basis. See Tr. 232-233. Ms. Smith explained:

> Right now AT&T cannot submit a mechanized order. All the orders are coming in for UNEs are manual. So in this case it's being faxed to us. All the information is being typed by our service reps. In that case, the total front end and the back office is being done by Southwestern Bell.

Tr. 232. Additionally, the computer time is real time involved in nonrecurring activities and should be recognized.

AT&T's argument on complex orders is even harder to understand. Complex orders involve numerous back office or provisioning stations, which cannot be fully mechanized. Mr. Vest testified about the complexity of back office systems involved in complex orders:

> There is more volume of work in the back end, and I cannot think of hardly any instances where this is almost totally mechanized with zero percent manual input.
>
> In Mr. Flappan's testimony he refers to an industry standard document which attempts to describe this flow through....I was part of the team that helped put that [Bellcore document] together, and I went back and looked...that document describes this process in terms of 44 steps, and 5 of them appear on this side, 41 over here (back office). So to say that there is absolutely no work in those remaining 41 steps is just an almost impossible thing to say, that the computer is going to do it totally.

Tr. 236-237. AT&T also misunderstands the concept of the term negotiate and argues that SWBT will not be negotiating on AT&T's behalf. Brief at p. 29. AT&T is correct

that SWBT will not be negotiating with AT&T's customers, but that is not what the concept of negotiations is in the OSS environment.

> Negotiation in the UNE environment involves coordination activities associated with the validation process as well as coordinating frame due dates or dispatch required. The validation process includes activities such as receiving the order, reviewing the order for accuracy, possibly sending/calling back to the CLEC for correction. The validation process must be completed before orders can be typed into SORD.

Exhibit 12 (Smith) at pp. 13-14. Both simple and complex service orders involve varying amounts of manual activity and the costs associated with that labor must be recovered in the nonrecurring rate at issue in this case.

(g) Dark Fiber

Staff recognizes that there is manual activity that SWBT must perform to determine the availability of these facilities for AT&T's use. To that extent, although SWBT does not agree with the AAS recommendation, at a minimum it should be adopted over AT&T's proposal because it allows for, at least, some recovery of the resources that SWBT will expend. In addition, although SWBT is in the process of making preordering systems available to the wholesale customer, such systems are "front-end" systems and are certainly not similar in nature to the various system resources necessary to enable specific telephone plant research, those which are required for determining Dark Fiber availability.

(h) Plexar Custom

In passing, AT&T raises a new issue. Whether or not SWBT's Plexar Custom customers should be permitted to terminate term arrangements prior to the end of the term without paying the termination charges to which the customers have agreed. Brief

at p. 30. This issue of "fresh look," which AT&T did not raise in the first or second rounds of arbitration and which neither the AAS nor the Parties to the case addressed in testimony, has not been properly raised here and cannot be addressed for the first time in briefs.

(i) NXX Migration

AT&T argues that NXX migration is just like the normal network activity that occurs whenever a new NXX is activated in a switch. Brief at p. 31. AT&T is correct that the actual activity to migrate an NXX from SWBT to AT&T is the same activity that must be performed to introduce a new NXX, but that does not explain why the costs for such a migration should be borne by SWBT and its other customers instead of by AT&T who is the sole beneficiary of the migration. Barb Smith explained the issue in her Direct Testimony:

> When a CLEC request that SWBT move an entire NXX to their switch, SWBT incurs expenses and should be compensated. The migration requires network rerouting effort and equipment record changes. That effort is caused by the CLEC's activities but is not reflected, or compensated for, in any of the nonrecurring charges for individual UNEs. The efforts are in addition to whatever it takes to establish the UNE....Other CLECs and retail customers should not have to cover the cost being caused by one CLEC in a specific situation. There would be no reason for SWBT to incur that cost if not for the CLEC.

Exhibit 12 (Smith) pp. 15-16. This is another situation where AT&T is asking SWBT to subsidize its entry into the local market. That is neither appropriate nor required by the law.

VI. COST FACTORS/GLOBAL MODIFICATIONS

The primary problem with this issue is that the record is incomplete. The Commission approved SWBT's cost methodology in Phase II of the AT&T arbitration (cost phase) and ordered SWBT to use certain global modifications, like a specified cost of money and a particular treatment for inflation. SWBT complied with that directive and the AAS report adopts all of those modifications into the AAS recommendation. AT&T is now retrying issues from the second phase of the arbitration and seeking to raise the bar yet again. That was the essence of SWBT's Motion to Strike. More importantly it explains a dearth of testimony on these issues in this phase of the case. Southwestern Bell will do the best it can to respond based upon the record in this case.

AT&T maintains that SWBT includes the same support asset costs in both the investment-related support asset factors and in plant-related loaded labor rates. They further state that recurring rates are designed to "recover fully" all the proportionate support assets costs and that the labor rates are designed to recover "those same costs." There are some support assets costs that are included in both investment-related support assets used to establish recurring UNE prices, and in the support assets costs for labor rates used in nonrecurring costs studies. However, the investment-related recurring support assets in no way "recover fully" all the support assets included in the labor rates. A large portion of support assets expense is included only in the support assets loading for labor.

AT&T suggests that the support assets loading for labor should be eliminated because of this so-called "double counting". To completely eliminate the support assets loading from labor rates would under-recover the labor costs. These are legitimate costs

for motor vehicles, garage equipment, general-purpose computers and other support assets used by the workforce. One of the guiding rules of determining costs is that costs are to be associated with the cost causer. These support assets are "caused" by the workers doing the work and should, therefore, be assigned to labor rates. Id. If any adjustment is made, it should be to remove that portion of the support asset expenses that is also included in the development of the investment-related support assets factor.

AT&T also claims that 100% of SWBT's computer assets are included in the calculation of its support assets factors and that it should not be allowed to explicitly identify computer costs in its cost studies. The computer costs identified in the cost studies were for computers purchased specifically for CLECs in order to allow mechanized access to systems like TIRKS. These computer costs were not included in the support assets factor development. In fact, the purchases had not been made at the time the factors were developed. These systems are additions to existing systems, not replacements for existing systems. They are also directly caused by CLECs and therefore should be identified in the cost studies.

AT&T argues that the Transition Benefit Obligation (TBO) should not be included in SWBT's cost studies. Effective for SWBT in 1993, the rules regarding accounting for post retirement benefits for employees changed due to Statement of Financial Accounting Standards No. 106-Employers' Accounting for Post-retirement Benefits Other Than Pensions (SFAS No. 106). SFAS 106 requires all companies to report their post-retirement benefit liability on an accrual basis rather than on a pay-as-you-go basis. The Transition Benefit Obligation or TBO is the "catch-up" amount SWBT needs to record in post retirement benefits to restate its books as if it had been

utilizing SFAS 106 all along. For regulatory purposes, the FCC required SWBT to amortize the TBO over the average remaining service lives or working years of current employees. This does not imply the TBO is an historic expense. SFAS 106 recognizes that an employee earns post-retirement benefits over the employee's service life (16 (sixteen years for SWBT), and companies should recognize the cost of providing these benefits over that service life. SWBT provides post-retirement benefits in order to attract and retain competent employees. These benefits, including the TBO adjustment, are costs of the business, representing the company's obligation to pay future benefits to retirees. They are not an identification of amounts that have been paid in the past. Therefore, they cannot be considered historic. The TBO expense is expected to continue for what remains of the 16 (sixteen) years. The TBO continues to be a valid operating expense and should be included in the expense factor and labor rate calculations. UNE prices are to be based on SWBT's costs. This expense is part of SWBT's cost to attract and retain employees and will continue to be an expense for a great many years.

VII. CONCLUSION

The issue in this case is whether other not AT&T should pay its own way when (if?) it enters the local market or whether by arbitrarily reducing SWBT's costs that SWBT and its other customers should be required to subsidize that entry. See Tr. 283-284. Mr. Bailey addressed this issue at the hearings:

> The point is, what we're talking about here is we have a right to recover our costs... and the Commission should not be in a position where it is trying to incent competition by not allowing [SWBT] to recover its costs. We have a right to recover our costs when we do something for AT&T.

Tr. 280 – 281.

SWBT urges the Commission to adopt the rates proposed by SWBT. AT&T has the ability to enter the local market in the same way that Brooks, e'spire and others have successfully entered the local market. It is not necessary nor lawful for SWBT's cost to artificially reduced to subsidize a reluctant would-be competitor who prefers to delay SWBT's entry into its long distance market rather than enter the local market.

Respectfully submitted,

SOUTHWESTERN BELL TELEPHONE COMPANY

By Katherine C. Swaller /TM

PAUL G. LANE #27011
LEO J. BUB #34326
ANTHONY K. CONROY #35199
KATHERINE C. SWALLER #34271
Attorneys for
Southwestern Bell Telephone Company
One Bell Center, Room 3536
St. Louis, Missouri 63101
(314) 235-4099 (Telephone)
(314) 331-2193 (Fax)

CERTIFICATE OF SERVICE

I hereby certify that copies of the foregoing document were served on the following parties by first-class postage prepaid, U.S. Mail on February 16, 1999.

Katherine C. Swaller
Katherine C. Swaller

PENNY G. BAKER
MISSOURI PUBLIC SERVICE COMMISSION
301 W. HIGH STREET, SUITE 530
JEFFERSON CITY, MO 65101

MICHAEL F. DANDINO
SENIOR PUBLIC COUNSEL
OFFICE OF THE PUBLIC COUNSEL
301 W. HIGH STREET, SUITE 250
JEFFERSON CITY, MO 65101

PAUL S. DeFORD
LATHROP & GAGE
2345 GRAND BLVD., SUITE 2500
KANSAS CITY, MO 64108

CARL J. LUMLEY
LELAND B. CURTIS
130 S. BEMISTON, SUITE 200
CLAYTON, MO 63105

MARK WITCHER
AT&T COMMUNICAITONS
OF THE SOUTHWEST
919 CONGRESS, SUITE 1500
AUSTIN, TX 78701

EDWARD J. CADIEUX
MCI WORLDCOM
ONE BROOKS CENTER PARKWAY
4TH FLOOR
TOWN AND COUNTRY, MO 63017