

PUBLIC UTILITIES COMMISSION505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

August 12, 2002

Agenda ID #985
8/22/2002

TO: PARTIES OF RECORD IN APPLICATION 01-02-024 ET AL.

This is the draft decision of Administrative Law Judge (ALJ) Duda. It will be on the Commission's agenda at the meeting on August 22, 2002. The Commission may act then, or it may postpone action until later.

When the Commission acts on the draft decision, it may adopt all or part of it as written, amend or modify it, or set it aside and prepare its own decision. Only when the Commission acts does the decision become binding on the parties.

Pursuant to Rule 77.7(f) of the Commission's Rules of Practice and Procedure, the Commission may reduce or waive comments in an unforeseen emergency situation. The remand order of the U.S. District Court in AT&T Communications of California v. Pacific Bell Telephone Co. (No. C01-02517) (N.D. Cal. August 6, 2002) constitutes an unforeseen emergency. Parties shall have seven days to comment on this order. Comments are due on August 19, 2002. No reply comments will be permitted.

Consistent with the service procedures in this proceeding, parties should send comments in electronic form to those appearances and the state service list that provided an electronic mail address to the Commission, including ALJ Duda at dot@cpuc.ca.gov. Comments should be sent to the service list for A.01-02-024 et al. and R.93-04-003/I.93-04-002 (OANAD proceeding). Service by U.S. mail is optional, except that hard copies of comments should be served separately on ALJ Duda and the Assigned Commissioner, and for that purpose I suggest hand delivery, overnight mail, or other expeditious methods of service. In addition, if there is no electronic mail address available, the electronic mail is returned to the sender, or the recipient informs the sender of an inability to open the document, the sender shall immediately arrange for alternate service (regular U.S. mail shall be the default, unless another means—such as overnight delivery—is mutually agreed upon). The current service lists for these proceedings are available on the Commission's web page, www.cpuc.ca.gov.

/s/ CAROL A. BROWN by PSW
Carol A. Brown, Interim Chief
Administrative Law Judge

CAB:sid

Attachments

Decision **DRAFT DECISION OF ALJ DUDA (Mailed 8/12/2002)****BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

Joint Application of AT&T Communications of California, Inc. (U 5002 C) and WorldCom, Inc. for the Commission to Reexamine the Recurring Costs and Prices of Unbundled Switching in Its First Annual Review of Unbundled Network Element Costs Pursuant to Ordering Paragraph 11 of D.99-11-050.

Application 01-02-024
(Filed February 21, 2001)

Application of AT&T Communications of California, Inc. (U 5002 C) and WorldCom, Inc. for the Commission to Reexamine the Recurring Costs and Prices of Unbundled Loops in Its First Annual Review of Unbundled Network Element Costs Pursuant to Ordering Paragraph 11 of D.99-11-050.

Application 01-02-035
(Filed February 28, 2001)

Application of The Telephone Connection Local Services, LLC (U 5522 C) for the Commission to Reexamine the Recurring Costs and Prices of the DS-3 Entrance Facility Without Equipment in Its Second Annual Review of Unbundled Network Element Costs Pursuant to Ordering Paragraph 11 of D.99-11-050.

Application 02-02-031
(Filed February 28, 2002)

Application of AT&T Communications of California, Inc. (U 5002 C) and WorldCom, Inc. for the Commission to Reexamine the Recurring Costs and Prices of Unbundled Interoffice Transmission Facilities and Signaling Networks and Call-Related Databases in Its Second Annual Review of Unbundled Network Element Costs Pursuant to Ordering Paragraph 11 of D.99-11-050.

Application 02-02-032
(Filed February 28, 2002)

Application of Pacific Bell Telephone Company (U 1001 C) for the Commission to Reexamine the Costs and Prices of the Expanded Interconnection Service Cross-Connect Network Element in the Second Annual Review of Unbundled Network Element Costs Pursuant to Ordering Paragraph 11 of D.99-11-050.

Application 02-02-034
(Filed February 28, 2002)

Application of XO California, Inc. (U 5553 C) for the Commission to Reexamine the Recurring Costs of DS1 and DS3 Unbundled Network Element Loops in Its Second Annual Review of Unbundled Network Element Costs Pursuant to Ordering Paragraph 11 of D.99-11-050.

Application 02-03-002
(Filed March 1, 2002)

**OPINION MODIFYING DECISION 99-11-050 TO REMOVE RESTRICTION
ON REVIEW OF THE SHARED AND COMMON COST MARK-UP**

I. Summary

This decision modifies Decision (D.) 99-11-050 to remove a restriction contained in that order on review of the shared and common cost mark-up of

19%. This modification is made in response to a remand of the Commission's calculation of the total direct cost of providing unbundled network elements (UNEs) by the U.S. District Court for the Northern District of California. (*AT&T Communications of California Inc. et al., v. Pacific Bell Telephone Company, et al.* Order on Cross-Motions for Summary Judgment No. C01-02517 (CW) (N.D. Cal. August 6, 2002). The total direct cost of UNEs is a component of the mark-up calculation. The Court found that the Commission made a double-counting error when it calculated this number. The assigned Administrative Law Judge (ALJ) will issue a further ruling in this docket allowing parties to comment on how the Commission should correct the double-counting error found by the U.S. District Court.

II. Background

In D. 99-11-050,¹ the Commission adopted prices for the UNEs that Pacific Bell Telephone Company (Pacific) sells to competitors who use portions of its network. One component of the prices adopted in that order was a percentage mark-up over the forward-looking cost of UNEs to recover Pacific's "shared and common costs."² The Commission adopted a mark-up percentage of 19% based on a calculation of Pacific's shared and common costs divided by the total direct

¹ D.99-11-050 was issued in the Commission's Rulemaking and Investigation to Govern Open Access to Bottleneck Services and Establish a Framework for Network Architecture and Development of Dominant Carrier Networks (Rulemaking 93-04-003/ Investigation 93-04-002) ("OANAD proceeding").

² Shared and Common costs are defined in Appendix C of D.95-12-016. According to page 6 of Appendix C, shared costs are defined as "costs that are attributable to a group of outputs but not specific to any one within the group, which are avoidable only if all outputs within the group are not provided." Common costs are defined as "costs that are common to all outputs offered by the firm."

costs of UNEs and total non-recurring costs adopted in D.98-12-079.

(D.99-11-050, mimeo. at 72, and 257.) Essentially, for each of the UNEs that Pacific sells to competitors, the UNE cost is increased by 19% to establish a UNE price.

At the same time the Commission adopted UNE prices in 1999, it noted the need to address the future status of the prices it was setting. Therefore, D.99-11-050 established a process for an annual reexamination of the costs of no more than two UNEs. (*Id.*, at 168-169.) The order specified, however, that the Commission would not entertain requests to reconsider the 19% markup for shared and common costs in any annual cost reexamination proceeding. (*Id.*, at 169, footnote 155, and 272.) The Commission is currently reviewing the costs of several UNEs in the above-captioned proceeding (also referred to as the “2001/2002 UNE Reexamination”).³

AT&T Communications of California, Inc., MCI Worldcom Network Services, Inc. and MCImetro Access Transmission Services LLC (jointly “Plaintiffs”) filed a suit in U.S. District Court seeking to overturn aspects of D.99-11-050 related to the shared and common cost mark-up. Plaintiffs argued that the Commission improperly determined Pacific’s firm-wide shared and common costs and unreasonably allocated these costs only to UNEs. In a cross-motion, Pacific argued that the Commission’s OANAD decisions contained other

³ Indeed, in the 2001/2002 UNE Reexamination, AT&T Communications of California, Inc. and WorldCom, Inc. (“Joint Applicants”) have made repeated requests for review of the 19% mark-up. In light of the language contained in D.99-11-050 restricting review of the mark-up, this request was first denied by the Assigned Commissioner and ALJ in a ruling of 6/14/01, and subsequently denied in rulings of 7/11/01 and 6/12/02.

errors because they rejected Pacific's proposed risk adder, double-counted non-recurring costs, failed to set a recurring rate for OSS costs and erroneously ordered Pacific to provide CLCs with combination of UNEs at cost-based prices.

On August 6, 2002, the U.S. District Court issued its order in *AT&T v. Pacific Bell*. The court denied all of Plaintiff's claims and denied all but one of Pacific's claims. The court agreed with Pacific that the Commission had double-counted non-recurring costs when it calculated Pacific's total direct costs of UNEs. The order states, "The [Commission's] determination of Pacific's direct cost of providing UNEs (the denominator of the common cost mark-up), and any decision which relies on this determination, must be vacated and remanded, so that the double-counting can be remedied." (*AT&T v. Pacific Bell*, slip op. at 38.)

III. Discussion

Based on the remand contained in the order of the U.S. District Court in *AT&T v. Pacific Bell*, the Commission is obligated to review the shared and common cost mark-up adopted in D.99-11-050. The logical place for the Commission to undertake this review is within the currently open 2001/2002 UNE Reexamination, where we are already reviewing UNE prices. Therefore, we should modify the restriction the Commission initially placed on this review and allow it to proceed within the scope of the currently open 2001/2002 UNE Reexamination Proceeding.

The assigned ALJ should issue a subsequent ruling in this docket to initiate the adjustment directed by the Court's remand order. That ruling should allow parties an opportunity to comment on how the Commission should proceed and what Commission orders might be impacted. The ruling should ask parties to comment on the correct methodology to be used to adjust the calculation of the total direct costs of UNEs. For example, should the Commission correct any

double-counting by subtracting \$583 million from the denominator of the mark-up calculation adopted in D.99-11-050? The ruling should also ask for comment on whether any changes to the mark-up calculation should apply retroactively to the effective date of D.99-11-050 or prospectively only.

IV. Comments on Draft Decision

Pursuant to Rule 77.7(f) of the Commission's Rules of Practice and Procedure, the Commission may reduce or waive comments in an unforeseen emergency situation. Rule 81(g) states that a deadline for Commission action imposed by a court is an example of an unforeseen emergency. The remand order contained in *AT&T v. Pacific Bell* constitutes an unforeseen emergency because the court has placed a level of uncertainty over the UNE prices contained in D.99-11-050, D.02-05-042, and interconnection agreements between Pacific and competitive local carriers. Therefore, we will reduce the standard time frame for comments on this order so that the review of the remanded matter can be initiated as soon as possible. Parties shall have seven days to comment on this order. No reply comments will be permitted.

The Commission mailed the draft decision of the ALJ in this matter to the service list for the OANAD proceeding and the parties in the 2001/2002 UNE Reexamination. Comments were filed by _____.

Findings of Fact

1. D.99-11-050 states that the Commission shall not consider any requests to change the 19% mark-up for shared and common costs within the scope of the annual UNE cost reexamination proceeding.

2. On August 6, 2002, the U.S. District Court issued an order in *AT&T v. Pacific Bell* that remanded to the Commission its calculation of the shared and common cost mark-up contained in D.99-11-050.

Conclusions of Law

1. In light of the remand order of the U.S. District Court, Ordering Paragraph 12 of D.99-11-050 should be modified to remove the restriction on consideration of the shared and common cost mark-up within the annual cost reexamination proceeding.
2. The remand of the calculation of Pacific's direct costs of UNEs should occur within the scope of the 2001/2002 UNE Reexamination proceeding.
3. The U.S. District Court remand order constitutes an unforeseen emergency.

O R D E R

IT IS ORDERED that:

1. Decision 99-11-050 is modified to remove Ordering Paragraph 12 and footnote 155 on page 169.
2. The assigned Administrative Law Judge shall issue a ruling allowing parties an opportunity to comment on how the Commission should correct the double-counting error found by the U.S. District Court.
3. This decision should be mailed to the service list for Rulemaking 93-04-003/Investigation 93-04-002 (OANAD proceeding).

This order is effective today.

Dated _____, at San Francisco, California.