BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF SOUTH DAKOTA

IN THE MATTER OF THE PETITIONS OF ALLIANCE COMMUNICATIONS COOPERATIVE, INC., MCCOOK COOPERATIVE TELEPHONE COMPANY, BERESFORD MUNICIPAL TELEPHONE COMPANY, KENNEBEC TELEPHONE COMPANY, SANTEL COMMUNICATIONS COOPERATIVE, INC., WEST RIVER COOPERATIVE TELEPHONE COMPANY, INC. (COLLECTIVELY THE "RLECS") FOR ARBITRATION PURSUANT TO THE TELECOMMUNICATIONS ACT OF 1996 TO RESOLVE ISSUES RELATING TO AGREEMENTS WITH ALLTEL COMMUNICATIONS, INC.	Docket Nos. TC07-111 TC07-112 TC07-113 TC07-114 TC07-115 TC07-116

REBUTTAL TESTIMONY OF SUE VANICEK
ON BEHALF OF THE SOUTH DAKOTA RLECS

Q. **Please State your Name, Employer, Business Address and Telephone Number.**

A. My name is Sue Vanicek. I am employed with Consortia Consulting ("Consortia"), formerly known as TELEC Consulting Resources Inc. My business address is 233 South 13th Street, Suite 1225, Lincoln, Nebraska, 68508.

Q. On whose behalf are you testifying?

A. I am testifying on behalf of Alliance Communications Cooperative, Inc., McCook Cooperative Telephone Company, Beresford Municipal Telephone Company, Kennebec Telephone Company, Santel Communications Cooperative, Inc., and West River Cooperative Telephone Company, Inc., which collectively I'll refer to as the RLECs. Each RLEC provides local telephone exchange service and exchange access services predominantly in the more rural parts of South Dakota.

Q. What is your current position?

A. I am a Senior Consultant at Consortia Consulting, Inc. ("Consortia") which assists local exchange telephone companies in regulatory analysis and representation, as well as evaluation of financial and operational decisions.

Q. What are your duties and responsibilities at Consortia?

A. I monitor and analyze state and federal regulatory proposals that could affect our client's operations, and advise them of potential impacts. I work with our clients to develop responses to regulatory proposals, including comments and testimony. The most common issues I work with are universal service and a host of regulations that have resulted as the Telecommunications Act of 1996 has been implemented. I have provided expert testimony on universal service issues in both Nebraska and South Dakota. I also testified in a wireline-wireless arbitration proceeding in Nebraska, and have filed written testimony in a wireline-wireless arbitration proceeding in South Dakota that reached a negotiated settlement prior to hearing.

Q. What was your experience prior to your current position?

A. I have worked in the telecommunications industry for 23 years. Prior to my position at Consortia, I was employed by Lincoln Telephone/Aliant Communications. I held a variety of positions specializing in regulatory and legislative analysis and strategic planning. My most recent position at Aliant Communications was Economic Costs and Analysis Manager. In that position I was responsible for managing the development of cost information, both forward-looking and historical, and for analyzing and developing responses to state and federal regulatory proposals on issues such as universal service.

Q. What is your educational background?

A. I have a Master of Arts degree in Economics and a Bachelor of Science degree in Business Administration, both from the University of Nebraska-Lincoln.

Q. Have you read the direct testimony of Mr. W. Craig Conwell filed on behalf of Alltel Communications, LLC ("Alltel") in this proceeding?

A. Yes, I have.

Q. What is the purpose of your rebuttal testimony?

A. The purpose of my rebuttal testimony is to respond to the direct testimony of Mr. Conwell in regard to policy issues regarding the pricing of transport and termination that he discussed in his direct testimony in connection with the determination of reciprocal compensation rates pursuant to 47 U.S.C. § 251(b)(5).

Q. What is the statutory requirement for transport and termination rates contained in 47 U.S.C. § 252(d)(2)?

A. 47 U.S.C. § 252(d)(2) reads as follows:

(2) CHARGES FOR TRANSPORT AND TERMINATION OF TRAFFIC.—
(A) IN GENERAL. – For the purpose of compliance by an incumbent local exchange carrier with section 251(b)(5), a State commission shall not consider the terms and conditions for reciprocal compensation to be just and reasonable unless –
"(i) such terms and conditions provide for the mutual and reciprocal recovery by each carrier of costs associated with the transport and termination on each carrier's network facilities of call that originate on the network facilities of the other carrier; and

"(ii) such terms and conditions determine such costs on the basis of a reasonable approximation of the additional costs of terminating such calls.

(B) RULES OF CONSTRUCTION. – This paragraph shall not be construed –

"(i) to preclude arrangements that afford the mutual recovery of costs through the offsetting of reciprocal obligations, including arrangements that waive mutual recovery (such as bill-and-keep arrangements); or

"(ii) to authorize the Commission or any State commission to engage in any rate regulation proceeding to establish with particularity *the additional costs of transporting or terminating calls*, or to require carriers to maintain records with respect to the additional costs of such calls. (emphasis added)

Q. How did the Federal Communications Commission ("FCC") interpret the "additional cost" standard for the pricing of transport and termination?

A. The FCC found that the pricing of transport and termination under the "additional cost" standard should use the same economic cost-based pricing standard that it established for the pricing of unbundled elements.[1]

Q. How did the FCC codify this finding into rules for pricing transport and termination.

A. The FCC established rules for pricing transport and termination in 47 C.F.R. §51.505 and 47 C.F.R. §51.511. 47 C.F.R. §51.505(a) specifies that the forward-looking economic cost of an element (in the present case transport and termination) equals the sum of: (1) the total element long-run incremental cost of an element; and (2) a reasonable allocation of forward-looking common costs. 47 C.F.R. §51.511(a) specifies that the forward-looking economic cost per unit of an element equals the forward-looking economic cost of the element, as defined in § 51.505 of this part, divided by a reasonable projection of the sum of the total number of units of the element that the incumbent LEC is likely to provide to requesting telecommunications carriers and the total number of units of the

[1] *See Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98, and *Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers*, CC Docket No. 95-185, First Report and Order , FCC 96-325 (*"Local Competition Order"*) (rel. Aug. 8, 1996) at ¶ 1054.

element that the incumbent LEC is likely to use in offering its own services, during a reasonable measuring period.

Q. Please explain the economic theory underlying the FCC's choice of the forward-looking economic cost standard for pricing contained in 47 C.F.R. § 51.505 and 47 C.F.R. § 51.511.

A. The FCC chose a pricing standard that it felt would most closely mirror entry decisions and utilization of telecommunications infrastructure in a competitive market.[2] This standard, forward-looking economic cost, includes the total element long-run incremental cost of an element ("TELRIC"), plus a reasonable allocation of forward-looking common costs.[3]

Q. Please describe the TELRIC costing methodology as adopted by the FCC in § 51.505(b).

A. TELRIC can be simply explained by elaborating on each word in this term. The word "total" refers to the increment of the network element or service over which the cost is to be computed. In other words, as stated by the FCC, "the increment that forms the basis for a TELRIC study shall be the *entire quantity* of the network element provided."[4] (emphasis added) The word "element" refers to the good/service for which a cost is being developed. In this case, the elements for which costs need to be developed are transport and termination (switching). The words "long-run" refer to a period long enough so that all of a firm's costs become variable or avoidable.[5] Finally, the words "incremental cost" refer to the

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[2] *See Local Competition Order* at ¶¶ 630 and 679.

[3] *See* 47 C.F.R. § 51.505(a).

[4] *See Local Competition Order* at ¶ 690.

[5] Id. at ¶ 677.

additional costs a firm will incur as a result of expanding the output of a good or service by producing an additional quantity of the good or service.[6]

Q. Are there any other FCC rules that are pertinent to the pricing of transport and termination?

A. Yes. § 51.507 contains general rate structure standards for elements including transport and termination. The text of **§** 51.507(c) states in part "[t]he costs of shared facilities shall be recovered in a manner that efficiently apportions costs among users."

Q. Based upon your review of the FCC's pricing rules, in your opinion, is Mr. Conwell correct in his assertion that usage-sensitive costs refer to the costs of components of plant (e.g., a switch) whose capacity is exhausted by the volume of traffic handled by the plant component?[7]

A. No, not in my opinion. Usage-sensitive costs are not determined by whether or not a component of plant, e.g., a switch, are exhausted by the traffic volume placed upon a component. Rather, usage-sensitive costs are costs that vary with usage or the volume of traffic.

Q. Based upon your review of the FCC's pricing rules, in your opinion, is Mr. Conwell correct in his assertion that the "additional cost" standard requires that transport and termination rates recover only an RLEC's costs that are caused by handling land-to-mobile traffic?[8]

A. No, not in my opinion. As I mentioned previously, the FCC determined that transport and termination rates should be based upon TELRIC, plus a reasonable allocation of forward-looking common costs. Furthermore, TELRIC requires that the cost, or rate, be computed over the *total*, or *entire quantity* of the network

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[6] Id. at ¶ 675.

[7] *See* Conwell Direct Testimony at p. 17, footnote 8.

[8] Ibid.

element provided. Therefore, the TELRIC rates should be determined over the total quantity of transport and termination (switching) provided by an RLEC. The rates should not be determined based upon costs and quantities of demand associated with any particular carrier or group of carriers (for example, mobile carriers). This would be a violation of FCC rules.

Q. Based upon your review of the FCC's pricing rules, in your opinion, is Mr. Conwell correct in his assertion that the RLECs must produce evidence to prove that the capacities of the equipment components included in the switch common category are exhaustible by expected usage demand in order to be treated as usage-sensitive switch investments that are recoverable through termination rates?[9]

A. No, not in my opinion. Mr. Conwell states that it does not appear that usage exhausts the capacity of the RLEC's switch processors, therefore, he asserts that there are no additional costs caused by usage.[10] The dictionary defines capacity as "the ability to contain, receive, or accommodate," and "the maximum amount or number that can be contained." If switching costs were not sensitive to usage, then a discussion of switch capacity would be unnecessary and irrelevant. As I mentioned above, usage-sensitivity is based upon whether costs vary with usage, not whether foreseeable usage would exhaust the capacity of a given network component. As Mr. Conwell mentions in his testimony, Beresford stated in its response to Alltel's interrogatory that the capacity of the switch processor components is volume-sensitive, and that multiple volume-sensitive variables may be limiting factors that can exhaust the capacity of the switch processor function. The fact that a new switch has been engineered with sufficient capacity

[9] *See* Conwell Direct Testimony at 45:6-14.

[10] *See* Conwell Direct Testimony at 44:7-10.

and currently possesses unused capacity does not mean that the switch is not usage sensitive. In fact, in order to meet the standards for TELRIC that the FCC has established, the costs must be based on an efficient network configuration. It may be the most cost efficient to base termination (switching) rates upon a switch that has a processor that is sufficiently large so that it does not need to be augmented or replaced during its useful life.

Q. What are the ramifications of Mr. Conwell's assertion that the switch processor is not usage-sensitive and that the cost of the processor should not be included in termination (switching) rates?

A. If the switch processor was found not to be usage-sensitive and the costs of the processor were not included in the termination (switching) rates, this would result in Alltel not paying for the use of *shared* components in the switch. As I mentioned earlier, the FCC rules require that the costs of shared facilities shall be recovered in a manner that efficiently apportions costs among users. Mr. Conwell is suggesting that others, for example consumers subscribing to basic local exchange service and interexchange carriers that provide long-distance service, should be required to pay for the use of the switch processor, while wireless carriers such as Alltel should not. Such a pricing regime, that is, requiring consumers and long-distance carriers to pay for the switch processor while not requiring Alltel to do so, would not efficiently apportion costs among users. If Alltel was not required to pay for the use of the switch processor, it would encourage Alltel to maximize its termination to the RLECs, as Alltel would likely receive revenues from its end users for doing so, while not incurring termination costs for the use of such switch components.

Q. Have any regulatory agencies ruled that the cost of a switch processor are usage-sensitive and should be included in termination (switching) rates?

A. Yes. The Nebraska Public Service Commission ("NPSC") has found in an arbitration regarding an interconnection agreement between a wireless carrier and an incumbent local exchange carrier that the switch processor is usage-sensitive and therefore the costs of the processor should be included in usage-sensitive rates for termination (switching). The NPSC indicated in an order reviewing an arbitrated interconnection agreement and approving traffic-sensitive rates for the switch processor "[t]he Commission is of the opinion that switch costs should be shared by users of switching resources."[11]

Q. What argument had the wireless carrier in the Nebraska arbitration case made as to why the cost of the switch processor should not be included in termination (switching) rates?

A. The wireless carrier in the Nebraska arbitration case, WWC License L.L.C., had made an argument similar to Alltel's argument in the instant proceeding, that is, "that the current and reasonably anticipated volume of traffic on the networks is so small, and that the smallest available switches are so powerful, that it is not appropriate to characterize the switches as having any cost that varies with use or that contributed additional cost to the termination of calls."[12]

Q. Are you the economist who testified on behalf of the incumbent local exchange carrier in the Nebraska arbitration case?

A. Yes, I am.

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[11] *See The Petition of Great Plains Communications, Inc., for Arbitration to Resolve Issues Relating to an Interconnection Agreement with WWC License L.L.C.*, Application No. C-2872, Interconnection Agreement Approved as Modified (entered Sept. 23, 2003) at ¶ 40.

[12] WWC License, L.L.C., v. Boyle, 459 F.3d 880, 895 (8th Cir. 2006).

Q. Was your argument regarding the reasons as to why the cost of the switching processor should be included in termination (switching) rates the same in the Nebraska arbitration case as presented in the instant proceeding?

A. Yes, it was.

Q. Was the finding of the NPSC that the cost of the switch processor should be included in per-minute compensation rates for termination reviewed and upheld by any courts?

A. Yes. The finding of the NPSC that the switch processor costs should be included in a per-minute compensation rate was reviewed and upheld by the United States District Court for the District of Nebraska[13] and the United States Court of Appeals for the Eighth Circuit.[14]

Q. What is your reaction to Mr. Conwell's assertion that transport cable costs should be computed specifically for routes that are used to transport Alltel's mobile-to-land traffic?[15]

A. Mr. Conwell is not properly applying the TELRIC pricing rule in asserting that transport cable costs should be computed specifically for mobile-to-land traffic. As I indicated previously, the "T" in TELRIC stands for the *total* costs attributable to an element, in this case transport. If the transport distances for mobile-to-land traffic are shorter than transport distances for the network in general, as asserted by Mr. Conwell, developing rates based on a subset of the total costs associated with transport could result in insufficient cost recovery, as I will explain later in my testimony. Furthermore, it could result in inefficient resource allocation, as artificially-low rates for transport may stimulate the

[13] WWC License L.L.C. v. Boyle, 2005 WL 3676515 (D. NE 2005).

[14] WWC License, L.L.C., v. Boyle, 459 F.3d 880 (8th Cir. 2006)

[15] *See* Conwell Direct Testimony at 77:10-19.

demand for transport by sending incorrect pricing signals regarding the total cost of providing such an element.

Q. What is your reaction to Mr. Conwell's assertion that transport cable costs should be computed specifically for routes used by Alltel for mobile-to-land traffic, unless the RLECs can prove that longer cable mileages are more efficient?[16]

A. As I just discussed, Mr. Conwell is not properly applying the TELRIC pricing rule. The "T" in TELRIC stands for the *total* costs attributable to an element, in this case transport. Therefore, to comply with the TELRIC pricing standard, the transport network should be designed to minimize costs as a whole over the *entire* network. There are no requirements that element costs should be computed to minimize the costs for the benefit of a specific carrier using the network. In fact, designing a network to minimize the costs for a particular carrier could violate the TELRIC requirements if it increased the total cost of the network.

Q. What potential consequences could occur if transport costs were computed as being specific to land-to-mobile traffic, instead of being computed for the entire network?

A. The Telecommunications Act of 1996 (the "Act") contains § 252(i), a provision which allows *any* requesting telecommunications carrier to "opt-in" or adopt an agreement upon the same terms and conditions as approved by a state commission for another carrier. Therefore, if the transport rates specified in this proceeding were approved by the South Dakota Public Utilities Commission, any telecommunications carrier, not just mobile carriers such as Alltel, could seek to receive transport for the same rate from the RLECs. This would clearly be inappropriate, as the rates as suggested by Mr. Conwell would include only the

[16] *See* Conwell Direct at 77:21-78-4.

costs associated with Alltel's mobile-to land traffic, and would not be appropriate for other carriers. As I mentioned previously, setting a transport rate in this manner could result in under-recovery of transport costs for the RLECs. For example, if the South Dakota Public Utilities Commission approved a transport rate that applied only to transport routes of shorter distances than average, other telecommunications carriers, even those that would utilize transport routes of greater distances than those utilized by mobile-to-land traffic, could "opt-in" to an agreement between any of the RLECs and Alltel. Such carriers would receive transport services at a rate less than the cost of the RLECs to provide transport. Therefore, the RLECs could ultimately receive less compensation than the TELRIC, plus a reasonable allocation of common costs, which they are entitled to receive under the Act.

Q. What is your reaction to Mr. Conwell's assertion that CALEA and Centrex license fees should not be included in termination, since these costs are not attributable to terminating mobile-to-land traffic[17]

A. Mr. Conwell is not properly applying the TELRIC pricing rule. The "T" in TELRIC stands for the *total* costs attributable to an element, in this case termination. As I just explained with regard to transport, TELRIC rates are not specific to a given carrier's use of a specific network element. TELRIC rates must include all costs associated with a network element.

Q. What is your reaction to Mr. Conwell's assertion that investments associated with Web Self-Care should not be included in termination, since these costs are attributable to retail services, rather than to terminating mobile-to-land traffic?[18]

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[17] *See* Conwell Supplemental Direct at 10:3-5.

[18] *See* Conwell Supplemental Direct at 10:16-11:6.

A. Mr. Conwell is not properly applying the TELRIC pricing rule. The "T" in TELRIC stands for the *total* costs attributable to an element, in this case termination. As I just explained with regard to transport, TELRIC rates are not specific to a given carrier's use of a specific network element. TELRIC rates must include all costs associated with a network element. Custom calling features, such as caller ID, call waiting, etc., are not separate network elements, rather, they are included in the switching (termination) element.[19] If a landline CLEC were to request the use of an unbundled switching network element from the RLECs, it would be necessary for the landline CLEC to have access to the Web Self-Care System in order to provide custom calling features to the landline CLEC's customers in the same manner as provided by the RLEC. The rules for unbundled network elements ("UNEs") require that an incumbent LEC offer UNEs at a level of quality that is equal to that which the incumbent LEC provides itself.[20] The rules further specify that "[t]his obligation is not limited to a consideration of service quality as perceived by end users, and includes, but is not limited to, service quality as perceived by the requesting carrier."[21] Therefore, the Web Self-Care System should be included in the termination rate, as it is part of the total cost of providing termination (switching).

With regard to Mr. Conwell's assertion that the investment associated with Web Self-Care should not be included in termination since FCC Rule § 51.505(d)(2)

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[19] *See* 47 C.F.R. § 51.319(c)(1)(i)(C)(2).

[20] *See* 47 C.F.R. § 51.305(a)(3).

[21] Ibid.

does not permit “retail service costs” to be included in the FLEC costs of termination, I do not believe that Mr. Conwell has correctly cited and interpreted that rule. FCC Rule § 51.505(d)(2) is entitled “Retail costs” not “Retail service costs.” Examples of retail costs that the FCC states should not be included in UNEs are the costs of billing, marketing, and collection.[22] Retail costs are costs associated with offering a retail service to subscribers that are not telecommunications carriers, but are not, as Mr. Conwell suggests, investments to provide a retail service. Therefore, I believe that investments associated with the Web Self-Care System are appropriately included in the termination (switching) rate.

Q. Does this conclude your testimony?

A. Yes, it does.

[22] See 47 C.F.R. § 51.505(d)(2).