

**STATE OF ILLINOIS  
ILLINOIS COMMERCE COMMISSION**

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Petition of Hamilton County Telephone Co-Op.	)	
<i>et al.</i> , for Arbitration under the Telecommunications	)	05-0644 -- 05-0649
Act to Establish Terms and Conditions for	)	and 05-0657
(Consol.)	)	
Reciprocal Compensation with Verizon	)	
Wireless and its Constituent Companies.	)	

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**REPLY BRIEF ON EXCEPTIONS OF THE ADMINISTRATIVE  
LAW JUDGE'S PROPOSED ARBITRATION DECISION  
OF THE STAFF OF THE ILLINOIS COMMERCE COMMISSION**

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Now comes the Staff of the Illinois Commerce Commission ("Staff"), by its undersigned attorneys, and pursuant to Sections 200.830 and 761.430 of the Commission's Rules of Practice (83 Ill. Adm. Code 200.830 and 83 Ill. Adm. Code 761.430) respectfully submits this Brief on Exceptions of the Administrative Law Judge’s (“ALJ”) Proposed Arbitration Decision (“PAD”) issued on January 3, 2006.

**I. Introduction**

Both the Petitioners and Verizon Wireless (the “parties”) repeat in their BOEs many of the points previously made in their Initial Briefs. In an effort at avoiding rehashing what has already been argued, Staff has not addressed in detail each and every assertion made by the parties in their respective BOEs. Instead, Staff reasserts and reincorporates all of the arguments in its Initial Brief and its Brief On Exceptions (“BOE”) in this proceeding as though fully set forth herein. Accordingly, where Staff does not respond specifically to an assertion made by another party in its BOE, this should not be deemed a waiver of any

argument in support of Staff's position, but rather a decision to stand on arguments that Staff has raised in its prior Briefs.

The parties' respective BOEs suffer from similar logical inconsistencies regarding the usage of the HAI model. For example, Verizon Wireless does not object to the use of the HAI model to set final rates if the Commission adopts Verizon Wireless approved input values but simultaneously maintains the Petitioners have not met their burden of proof in this case because the HAI model overstates costs. Verizon Wireless BOE at 1. According to Verizon Wireless, if the Commission uses Verizon Wireless' input values the HAI model is acceptable but if the Commission uses other input values then the HAI model is fatally flawed. Likewise, albeit to a lesser degree, the Petitioners argue that the HAI model produces reasonable forward looking cost estimates when Petitioner recommended inputs are adopted but does not produce reasonable approximations of the forward looking cost estimates when Commission approved input values are used. Petitioners' BOE at 1.

This logical inconsistency has, like a virus, infected the reasoning of both parties throughout this proceeding. In Staff's view, the well documented shortcomings of the HAI model cannot be overcome by merely changing a few input values selectively. In other words, changing a few inputs does not transform a bad model into a good model. Because of the severe reservations expressed by all parties in this proceeding concerning the ability of the HAI model to generate reciprocal compensation rates for small Illinois RLECs, Staff took the position that, under the facts of record in this proceeding, a proxy rate

for reciprocal compensation best approximates the additional costs of terminating the traffic at issue in this proceeding.

For the reasons explained in Staff's briefs, Staff continues to recommend that the Commission adopt Dr. Staranczak's proxy recommendation and also continues to offer the alternative recommendations for specific HAI model inputs, as expressed in its Initial Brief, *if* the HAI is adopted.

## **II. Staff Reply to the Petitioners' Exceptions**

The Petitioners contend that the Commission correctly determined that the HAI model can provide a reasonable approximation of forward looking costs. Petitioners' BOE at 1. The Petitioners, however, take exception to the exclusion of switching costs. *Id.* In addition, the Petitioners' maintain that the Commission unfairly singles out the HAI results for LaHarpe as an "outlier" when there are good reasons for LaHarpe's HAI estimated costs. *Id.* The Petitioners further argue that if the Commission treats HAI results for LaHarpe as an outlier it should similarly treat HAI results for Marseilles and Metamora as outliers as well since HAI estimated costs for these companies is, according to the Petitioners, unreasonably low. *Id.* at 2. They argue that the unreasonably low HAI model results for Marseilles and Metamora could be corrected if switching costs are added back to HAI. *Id.* at 3. These arguments are addressed later in this BOE.

The Petitioners also claim that once it has made a prima facie showing that its proposed rates are reasonable and forward-looking then the burden shifts to any party that does not agree with the Petitioners' proposals. Petitioners' BOE at 13, *citing* City of Chicago v. ICC, 133 Ill. App. 3d 435 (Ill. App. Ct. 1st Dist

1985). Staff disagrees. The FCC, not Illinois state courts, provide for the burden of proof in this proceeding. In *City of Chicago*, the court was addressing a traditional rate-of-return case brought entirely under state law. This proceeding, however, is brought under the federal Act. For arbitrations brought under Sections 251/252 of the federal Act, the FCC pointed out that only the ILEC has free access to the necessary information so it must bear the burden of proof.

We note that incumbent LECs have greater access to the cost information necessary to calculate the incremental cost of the unbundled elements of the network. Given this asymmetric access to cost data, we find that incumbent LECs must prove to the state commission the nature and magnitude of any forward-looking cost that it seeks to recover in the prices of interconnection and unbundled network elements.

First Report and Order; ¶ 680; *see also* 47 CFR § 51.505(e); *see also* 47 USC § 252(d)(1)(A)(i) (“determined without reference to a rate-of-return or other rate-based proceeding”).

**A. *End Office Non Line Port Fraction***

The Petitioners took exception to the PAD’s finding regarding input change number 13- end office non line port fraction. This input change ultimately determines the percentage of end office switching costs that appear in the Petitioners reciprocal compensation rates. If the Commission is intent upon using the HAI model, Staff agrees with the Petitioners that end office switching costs should be added to HAI model estimated transport and ISUP costs to estimate total forward looking reciprocal compensation costs. Staff, however, recommends that only 25% of the HAI model’s default switching costs be added back to HAI rather than the 70% advocated by the Petitioners. The FCC, moreover, clearly intended that reciprocal compensation rates include a

switching component, since the FCC set the proxy rate for switching between \$0.002 and \$0.004 per minute. Staff's recommended 25% allocation for switching would add approximately \$0.004 cents to the Commission's approved reciprocal compensation rates – a figure within the FCC's proxy range.

Petitioners devote a significant portion of their BOE in this proceeding on this very issue. While Staff is not persuaded by the entirety of their arguments, especially those supporting the 70% default fraction for this input, Staff does agree with the Petitioners that the PAD errantly relies upon Docket 00-0700 and the December 29, 2005 ruling in the Ace Telephone case. As such, Staff finds the first paragraph of exceptions language on this issue, found on page 25 of the Petitioners BOE, to be acceptable but not the remaining three proposed paragraphs.

***B. Treatment of LaHarpe as an Outlier***

The Petitioners also take exception with the PAD's finding that the HAI results for LaHarpe should be treated as an outlier, and that its reciprocal compensation rate be figured as the average of the other six carriers in this proceeding. The Petitioners reason that if LaHarpe is to be considered an outlier, so should Marseilles and Metamora – the HAI estimated reciprocal compensation rates for Marseilles are less than reciprocal compensation rates for AT&T Illinois even though AT&T Illinois has millions of access lines and Marseilles has some 3700. Staff finds this logic to be convoluted, as it presupposes that HAI is both reasonable while also producing results for 3 out of 7 carriers that are not reliable. Staff views the questionable HAI reciprocal

compensation rates for Marseilles and Metamora as further proof that the HAI model should not be used to estimate forward looking transport costs for small companies in this proceeding.

However, if the Commission is intent upon using the HAI model results to set reciprocal compensation rates, the HAI results for LaHarpe must then be treated as an outlier. The Petitioners completely ignore the underlying reason why LaHarpe's HAI results are significantly higher than those of the other carriers. Verizon Wireless witness Wood explained very clearly why the methodology in HAI will consistently produce an overbuilt network for carriers with a single host-remote design. The Petitioners do not provide any evidence to suggest that this finding by Mr. Wood is not accurate, choosing instead to try to impeach his qualifications for making such a finding. Consequently, if the Commission chooses to use the HAI results, then the HAI estimates for LaHarpe are inconsistent with the HAI estimates for the other companies. LaHarpe's reciprocal compensation rates are therefore best set by proxy, which the PAD has correctly decided.

### **III. Staff Reply to Verizon Wireless' Exceptions**

Verizon Wireless maintains that the PAD should be modified to be made consistent with the 1996 Telecom Act and the Rules and Orders of the FCC. Verizon Wireless BOE at 1. In particular, Verizon Wireless is concerned that the PAD resolves certain inputs in a manner that assumes embedded costs are equivalent to forward-looking costs. Verizon BOE at 13. In addition, Verizon Wireless argues that the Petitioners have not met their burden of proof in this

case because the HAI model overstates costs. *Id.* Finally, Verizon Wireless asserts that the PAD incorrectly concludes that proxy rates need not be forward looking. *Id.*

#### **A. The Use of HAI**

Verizon Wireless does not object to the use of the HAI model to set final rates if the Commission adopts Verizon Wireless approved input values but maintains the Petitioners have not met their burden of proof in this case because the HAI model overstates costs. Verizon Wireless BOE at 1. Staff disagrees. The main problem with the use of HAI is not with the inputs used to populate HAI but with the model itself. Simply put, the HAI model is not an appropriate tool for estimating transport and termination costs for small companies because it was primarily designed to estimate loop costs for large ILECs.

#### **B. Proxy Rates**

Verizon Wireless also maintains that proxy rates must be based on forward looking costs. Verizon Wireless BOE at 14. This logic is faulty. If there are no reliable forward looking cost estimates, then it would be impossible to implement proxy rates (according to Verizon Wireless' reasoning). On the other hand if there are reliable forward looking cost estimates then there would be no need to implement proxy rates at all. Verizon Wireless' arguments against proxy rates are circular, lack logical consistency, and must be rejected on common sense grounds.

The PAD properly concludes that the Commission can adopt proxy rates. PAD at 6-7, 55-56. Verizon Wireless, however, continues to insist that the Eighth Circuit removed the proxy option and that endorsing a proxy that was not based upon forward-looking costs would set a dangerous precedent. Verizon Wireless BOE at 13-14. Beyond the logical inconsistencies pointed out above (*i.e.*, there are no reliable forward-looking costs in the record), Verizon Wireless is simply wrong – there is no prohibition against adopting a proxy that is not based on forward-looking costs.

Verizon Wireless, moreover, has utterly failed to specifically identify this prohibition. Verizon Wireless, however, does cite to two United States Supreme Court cases to support the *general* proposition that the “FCC’s decision to establish a mandatory pricing methodology for states to apply in arbitrations under the act.” See Verizon Wireless BOE, at 13-14 *citing to AT&T Corp v. Iowa Utils. Bd.*, 525 U.S. 366, 384-385 (1999)(“AT&T”) and *Verizon Comms. Inc. v. FCC*, 535 U.S. 467 (2002)(“Verizon”). Staff agrees with this general proposition, as far as it goes. Verizon Wireless, however, reads these two Supreme Court cases much too broadly as neither decision prohibits the Commission from adopting a proxy not based on forward-looking costs.

Both the AT&T case and the Verizon case are inapposite to the facts that the Commission must address in this proceeding. First, in both cases the Supreme Court was *not* addressing a proxy rate in the context of setting reciprocal compensation rates as an alternative to bill and keep (which clearly has no forward-looking cost requirement) or the use of a cost study (which would

require forward-looking costs). The Court, moreover, was not addressing the issue in a proceeding where all parties, albeit to differing degrees, agree that the HAI model is problematic. Petitioners Ex. 1 (Hendricks), at 5-6; Verizon Wireless Ex. 2 (Wood), at 6-7; Staff Ex. 1.0 (Staranczak), at 5-8; and Staff Ex. 2 (Koch), at 26.

The issue the Supreme Court decided in *AT&T* was whether the FCC had the authority to set intrastate rates. *AT&T Corp v. Iowa Utils. Bd.*, at 525 U.S. at 385 (“We hold, therefore, that the [FCC] has jurisdiction to design a pricing methodology.”). In *Verizon*, on the other hand, the Court addressed the issue of whether the FCC’s choice of the TELRIC methodology was appropriate. *Verizon Comms. Inc. v. FCC*, 535 US at 523 (“We cannot say whether the passage of time will show competition prompted by TELRIC to be an illusion, but TELRIC appears to a reasonable policy for now, and that is all that counts.”). In sum, neither of these Supreme Court opinions contains a prohibition against the Commission adopting a proxy for reciprocal compensation rates that is not forward-looking. Verizon Wireless’s prohibition is a phantom, it simply does not exist. The Commission, therefore, should summarily reject Verizon Wireless arguments that a proxy rate must be based on forward-looking costs.

#### **IV. Conclusion**

WHEREFORE, the Staff of the Illinois Commerce Commission respectfully requests that its exceptions and recommendations be adopted in their entirety consistent with the arguments set forth herein.

Respectfully submitted,

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