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BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Joint Petition of VERIZON COMMUNICATIONS, INC. and MCI, INC. For a Declaratory Order Disclaiming Jurisdiction Over or, in the Alternative, a Joint Application for Approval of Agreement and Plan of Merger	DOCKET NO. UT-050814 NARRATIVE SUPPORTING MULTIPARTY SETTLEMENT AGREEMENT

I. Preliminary Matters

This Narrative Supporting Settlement Agreement ("Narrative") is filed pursuant to WAC 480-07-740(2)(a), on behalf of the signatories to the Multiparty Settlement Agreement ("Agreement") filed in this docket. A portion of this Narrative is contained in Confidential Appendix A, which sets forth the cost and revenue effect of certain terms described below and in the Agreement.

This Narrative summarizes many aspects of the Agreement. It is not intended to modify any terms of the Agreement.

The Agreement is supported by this Narrative, the Joint Petition filed on May 27, 2005, and the proposed testimony and exhibits on file in this docket.[1]

[1] The specific testimony supporting the Agreement is (1) the direct testimony of Carl Danner, Michael Beach, and Dr. William Taylor, filed on behalf of Verizon and MCI, (2) the response testimony of Jing Roth, Kathy Folsom, and Thomas Wilson, filed on behalf of Staff, (3) the response testimony of Jason Koenders, filed on behalf of Integra, and (4) the rebuttal testimony of Danner, Beach, Taylor, Steven Smith, and Julie Canny, on behalf of Verizon and MCI.

A. Signatories

The signatories to the Agreement are Verizon Communications Inc. ("Verizon"); MCI, Inc. ("MCI"), Integra Telecom of Washington, Inc. ("Integra"); and the Staff of the Washington Utilities and Transportation Commission ("Staff") (collectively, the "Settling Parties").

B. Non-Signatories

The parties of record in Docket No. UT-050814 that are non-signatories are: the Public Counsel Section of the Attorney General of Washington ("Public Counsel"); XO Communications Services, Inc. ("XO"); and Covad Communications Company ("Covad") (collectively, the "Non-settling Parties").[2]

II. Scope of the Underlying Dispute

The underlying dispute concerns the acquisition of MCI by Verizon (collectively, "Joint Petitioners"). During the course of this proceeding, Joint Petitioners filed pleadings and testimony arguing that (1) the Commission does not have jurisdiction over the transaction because the transaction is occurring only at the parent company level and neither corporate parent operates as a public service company in Washington; and (2) if the Commission exercises jurisdiction, it should approve the transaction without conditions because the transaction causes no harm and is in the public interest. See, e.g., Joint Petition at ¶¶ 16-17; Direct Testimony of

[2] The Citizens Utility Alliance of Washington initially intervened in this case but, in an e-mail to all parties dated September 13, 2005, stated that it will not participate further in this docket.

Dr. William E. Taylor, Carl R. Danner, and Michael A. Beach, filed June 28, 2005 on behalf of Joint Petitioners.

Commission Staff, Public Counsel, Integra, XO, and Covad filed testimony disagreeing with the Joint Petitioners, presenting their own analysis of the effects of the merger, and proposing several conditions for the commission to impose upon approval of the merger to ensure that the transaction is in the public interest. Staff proposed a number of conditions designed to mitigate the potential harms to competition and to consumers that Staff believes would otherwise result from the merger. Staff also proposed conditions to ensure that merger benefits and savings are passed on to Washington consumers. See, e.g., Testimony of Jing Y. Roth at 2-4. Similarly, Public Counsel proposed conditions to make the merger consistent with the public interest under its analysis of the merger's effects on competition and to ensure that savings and other purported benefits of the merger will be passed on to customers. See, e.g., Testimony of Trevor R. Roycroft at 4-5. Intervenors Covad and XO proposed conditions intended to increase competitive carrier's access to unbundled network elements (UNEs) at prices favorable to competitive carriers following the merger. Testimony of Joseph Gillan at 3-4, Testimony of Don J. Wood at 83-87. Covad also proposed conditions to address negative effects it alleged the merger would have for Internet Protocol-based competition. Testimony of Joseph Gillan at 45-46. Intervenor Integra proposed that Verizon be required to comply

with wholesale performance standards for its UNE ordering and provisioning processes in Washington following the merger. Testimony of Jason Koenders at 20-21.

In response, Joint Petitioners filed the rebuttal testimony of five witnesses that responds to the other parties' arguments and explains why, under the Joint Petitioners' analysis, none of the proposed conditions is warranted. See Rebuttal Testimony Dr. Taylor, Mr. Danner, Mr. Beach, Mr. Steven Smith, and Ms. Julie Canny, filed October 6, 2005 on behalf of Joint Petitioners.

In general, the parties' testimony and arguments can be distilled to three major issues:

> First, does the Commission have jurisdiction over this parent-company transaction?
>
> Second, assuming the Commission has jurisdiction, is the transaction in the "public interest?" In deciding this issue, is the appropriate standard "the transaction must cause no harm," or must Joint Petitioners also show that the transaction produces public benefits?
>
> Third, if the transaction, standing alone, is not in the public interest, what conditions should the Commission impose to ensure the transaction meets the public interest standard?

As discussed below, the Settling Parties have reached an agreement that resolves (or renders moot) all of these issues. The settlement, of course, does not adopt all the conditions proposed by every party. For example, Covad, a non-settling party, asks the Commission to establish new unbundled network element

(UNE) rates for Verizon NW and to regulate these rates via a price cap plan. Covad also asks the Commission to impose §271 obligations[3] upon Verizon NW. Verizon did not agree to these conditions because, in addition to being unnecessary, they are inconsistent with federal law.[4] The settlement agreement does include conditions that, in Joint Petitioners' view, do not relate directly to the proposed merger, but Joint Petitioners nevertheless have agreed to such terms in the spirit of compromise and to facilitate a prompt resolution of this proceeding.

In short, not all parties got what they asked for, but the settlement is a fair and reasonable resolution of all the issues in this docket, including the issues raised by the Non-settling Parties. Accordingly, the Settling Parties ask the Commission to approve the settlement agreement without material change.

III. Overview of the Proposed Settlement Agreement

A. Substance of the Settlement Agreement

The settlement agreement is between Verizon, MCI, Integra and Staff ("the Settling Parties"). The Settling Parties agree that the settlement's terms are in the public interest, and that the settlement agreement should be accepted as a

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[3] This section is part of the federal Telecommunications Act of 1996 ("the Act") (47 U.S.C. § 271).

[4] More specifically, § 252 of the Act governs the manner in which UNE rates are to be set, and this Commission recently established new UNE rates for Verizon NW in Docket No. UT-033034. Also, § 271 of the Act expressly applies only to Regional Bell Operating Companies ("RBOCs"). In Washington, Verizon NW is not the RBOC; Qwest is. Covad admits this fact in its testimony. It states, "Verizon's Washington property is not legally bound by § 271 which applies only to Regional Bell Operating Companies," but it nevertheless argues that the Commission "should ignore" this point. Testimony of Joseph Gillan at 17. Joint Petitioners disagree.

resolution of all issues in this docket, not just those issues in dispute among the Settling Parties.[5]

Pursuant to the settlement agreement, the Commission would approve the Verizon-MCI merger as being in the public interest subject to eight conditions:

> 1. Verizon Northwest Inc. ("Verizon") will extend service to the petitioners in docket UT-050778 and will recover only those costs permitted by its tariff. Verizon will not attempt to recover these particular line extension costs through its line extension tariff as otherwise would be allowed by WAC 480-120-071(3), or through its interim terminating access tariff as otherwise would be allowed by WAC 480-120-071(4). Staff agrees that the settlement of docket UT-050778 will not serve as precedent for future line extension cases. In fulfilling this term, Verizon shall undertake all reasonable efforts to provide service and to obtain approvals and permits from every necessary governmental agency. Verizon is not required to spend more than $325,000 in fulfilling this term, which is the cost Verizon estimated based on the representations made in petitioners' complaint in UT-050778. In the event that, despite all reasonable efforts, Verizon is unable to extend service within the $325,000 limit, Verizon or Staff will propose and the Commission may approve expenditure of a comparable amount for a similar public benefit.
>
> 2. Verizon will consolidate the three Skagit County rate centers – Anacortes, Mount Vernon, and SedroWoolley – into a single rate center, resulting in county-wide local calling for customers in Skagit County. Verizon will also consolidate the Arlington, Darrington, Granite Falls, and Marysville rate centers into a single rate center. Verizon will eliminate the flat and measured Premium Plus Adders that currently apply to customers in Fairfield, Farmington, Latah, Oakesdale, Rockford, Rosalia, and Tekoa and will maintain the existing unlimited usage service area for each exchange.

[5] As noted in the Settlement Agreement, Integra agrees that the agreement resolves the sole issue raised by Integra in this proceeding – Verizon's wholesale service quality – and therefore is in the public interest and should be approved in its entirety. Since Integra was not involved in the other issues raised by the non-signing parties, it does not take a position on them.

3. Verizon will not raise its basic residential or business service rates above the levels set by the rate case settlement in docket UT-040788 until June 30, 2009. During this period, Verizon may propose to reduce its local service rates and make other rate changes on a revenue-neutral basis. This term does not otherwise affect or supersede any provision of the rate case settlement including paragraphs 41-46 of the settlement agreement. Also, this term does not affect the rights of Verizon to make the Second Tariff Filing described at paragraph 25 of the rate case settlement agreement.

4. Verizon will continue to report under the now expired Bell Atlantic-GTE FCC merger conditions performance metrics (as such metrics have been or are modified from time-to-time) until it implements for Washington the revised California JPSA Verizon metrics (as such metrics have been or are modified from time-to-time) (see California Docket R. 97-10-016/I.97-10-017). Verizon will implement the California JPSA Verizon metrics for Washington when the California PUC approves revisions pending before the California PUC and revisions to reflect the withdrawal of the UNE Platform service and Line Sharing. (Verizon's implementation of the California JPSA Verizon metrics also will depend on the availability of Verizon Information Technology resources needed to implement the California JPSA Verizon metrics and on Verizon's need to schedule the implementation work so as not to adversely affect the performance of other CLEC affecting work by Verizon's Information Technology Organization.) Verizon expects it will be able to implement the revised California JPSA Verizon metrics in Washington by December 2006. Verizon will continue to provide metrics reports electronically. Verizon shall have the right to modify the metrics from time-to-time, e.g., to remove from the metrics measurements for "delisted" UNEs such as UNE Platform and Line Sharing. Also, Verizon will send a letter to all CLECs indicating that Verizon will continue to provide service quality measurements, initially under the Bell Atlantic-GTE FCC merger conditions service quality plan metrics (as such metrics have been or are modified from time-to-time) and then under the California JPSA Verizon metrics (as such metrics have been or are modified from time-to-time). Verizon will report these measures until December 31, 2008, although any party can attempt to initiate a proceeding after July 1, 2008 to extend the reporting date

beyond December 31, 2008. In providing UNEs, Verizon shall follow all effective FCC regulations prohibiting discrimination in the provision of, and access to, unbundled network elements, e.g., 47 C.F.R. 51.311(a) and (b) ("Nondiscriminatory access to unbundled network elements"). Finally, Verizon will provide WUTC Staff with access to all reports.

5. Verizon and MCImetro Access Transmission Services, LLC ("MCImetro") agree to continue to meet the Commission's retail service quality standards. Once the merger is approved, MCImetro will be required to file service reports applicable to Class A, competitively classified companies under WAC 480-120-439, and shall be subject to the standards applicable to such companies. This term does not prohibit MCImetro from seeking alternative measurement or reporting formats under WAC 480-120-439(12) or exemptions under WAC 480-120-015.

6. Verizon NW agrees to file a promotional intrastate tariff under which Verizon NW will issue a credit equal to the applicable local PIC ("LPIC") change charge in its intrastate tariff for those current residential customers who have Verizon NW local service and local toll service provided by an MCI subsidiary and who choose a non-MCI local toll provider during a promotional period, which will be 60 days in length. The credit will be available only to such customers who change their LPIC during the specified promotional period. Customers who change their long distance provider at the same time they change their LPIC also are eligible for the credit. Verizon NW will, upon request of the customer, provide a bill adjustment to any Verizon NW customer who changes his or her long distance provider from an MCI subsidiary during the promotional period but does not qualify for the automatic credit (this bill adjustment shall not exceed Verizon NW's LPIC charge). Verizon NW will give readily understandable notice of this term to its residential customers via bill inserts or bill message.

7. Verizon Northwest, Inc. and MCImetro are parties to a Wholesale Advantage Services Agreement for Washington. Upon request of any competing carrier, Verizon will make this Agreement, or any new commercial agreement between Verizon Northwest, Inc. and any former MCI Inc. subsidiary or between Verizon Northwest,

Inc. and any other telecommunications carrier affiliate of Verizon, available to the competing carrier subject to similar rates, terms and conditions, including volume and term commitments (i.e., Verizon will make these agreements available to similarly situated CLECs.) Verizon will make these agreements available for inspection and review to competing carriers. This term will apply for a period of two years following the completion of the merger.

8. If the FCC requires Verizon to reduce interstate special access rates as part of the FCC's merger review in Docket WC-0575, Verizon will support a review by this Commission to determine whether any changes to Verizon's intrastate special access rates should be made.

As discussed in greater detail in Section IV below, these conditions address Staff's concerns regarding any possible anti-competitive effects of the merger and also ensure public benefits.

B. Procedure

The Settling Parties understand the Commission has discretion, consistent with applicable law, to determine the appropriate procedures for determining whether it will approve the agreement. The Settling Parties, however, urge the Commission to retain the existing procedural schedule and use the presently scheduled hearing dates to review the proposed settlement and – if necessary – to address all contested issues. At the conclusion of the hearing and after submission of briefs, the Commission should accept the settlement as the resolution of all issues in the case and thus avoid having to rule on the jurisdiction issue. If the Commission does not accept the settlement, then it should make findings on all issues, including jurisdiction. Pursuant to WAC 480-07-740(1), the Settling Parties

urge the Commission to approve the settlement agreement no later than December 21, 2005.

More specifically, the Settling Parties propose the following:

November 1. The Settling Parties present witnesses to support the settlement. Parties opposed to the settlement may cross-examine these witnesses. The specific testimony supporting the Agreement that the parties will submit into the record is (1) the direct testimony of Carl Danner, Michael Beach, and Dr. William Taylor, filed on behalf of Verizon and MCI, (2) the response testimony of Jing Roth, Kathy Folsom, and Thomas Wilson, filed on behalf of Staff, (3) the response testimony of Jason Koenders, filed on behalf of Integra; and (4) the rebuttal testimony of Danner, Beach, Taylor, Steven Smith, and Ms. Julie Canny, on behalf of Verizon and MCI.

November 1-November 3. Parties that oppose the settlement may present evidence in support of their preferred position(s). Public Counsel, for example, can present the testimony of Messrs. King and Roycroft. Thereafter, Verizon and MCI may present the testimony of their rebuttal witnesses, and parties opposing the settlement may cross-examine these witnesses.

November 14. Simultaneous opening briefs due.

November 21. Simultaneous answering briefs due.

December 21. Commission issues an order that either accepts the settlement without material change or addresses all the contested issues, including the jurisdictional issue.

IV. Statement of Parties' Views

WAC 480-07-740(a) requires this Narrative to include a "statement of parties' views about why the proposal satisfies both their interests and the public interest." Each Settling Party has contributed the following separate statements:

A. Commission Staff

Commission Staff believes the settlement fully satisfies the public interest. In fact, the settlement adopts almost every condition Staff proposes in its testimony, as well as a certain condition recommended by one of the CLEC intervenors.

As explained above, Staff conducted a careful and through analysis of the proposed transaction and its effects upon consumers, competitors, and the Washington telecommunications market in general, and concluded that the transaction would be in the public interest if Staff's proposed conditions were adopted. Roth at 12. The settlement adopts all of Staff's proposals with one exception or modification: instead of reducing Verizon NW's intrastate access charges to UNE-based levels, as proposed on page 27 of Jing Roth's testimony, the settlement requires Verizon NW to support a review by this Commission of its intrastate special access rates if the FCC requires Verizon NW to reduce interstate special access rates as part of the FCC's separate review of the proposed merger. In this way, the Commission will have an immediate opportunity to determine if Verizon NW's intrastate special access rates should be reduced.

Staff proposed to reduce Verizon's intrastate special access rates in large part because the FCC recently eliminated high capacity and dark fiber transport and loops as required UNEs. As Ms. Roth stated,

> [I]t is vital to reduce the retail rates for special access services today because CLECs rely on this type of service to compete with Verizon,

> and the FCC has eliminated high capacity and dark fiber transport and loops as required UNEs that are served out of ILECs' central offices that serve more than 24,000 business access lines or have three fiber-based collocators. Reducing Verizon's special access rates will mitigate the potential competitive harm of the merger when the high capacity loops will no longer be available as UNEs.

Roth at 28.

This concern is mitigated because in Verizon NW's entire footprint in Washington, only one route between two Verizon NW central offices qualifies under the FCC's "delisting" rule. In other words, even under the new FCC rules, Verizon NW is still required to provide high-capacity UNE transport and loops almost everywhere.

In sum, the settlement agreement satisfies Staff's interests by preventing anticompetitive behavior, protecting consumers, and providing direct benefits and savings to Washington consumers. It also is in the public interest and therefore should be approved without change.

B. Verizon

Verizon's position is that (1) the Commission does not have jurisdiction over this parent company transaction, and (2) even if it did, the transaction does no harm and is in the public interest, and therefore should be approved without any condition. Nevertheless, the settlement agreement satisfies Verizon's interest because it resolves this matter without further delay and avoids a decision (and perhaps protracted litigation) over the threshold jurisdictional issue.

Also, the settlement agreement clearly is in the public interest. First, absent any conditions, the transaction will produce the significant benefits discussed in Joint Petitioners' testimony. Second, by addressing Staff's and Integra's concerns and agreeing to certain conditions, Verizon has sought to eliminate certain controversies and thereby more quickly conclude this proceeding.

C. MCI

MCI agrees with Verizon's statement. Also, MCI states that the settlement is in its interests as well as the public interest because the transaction will benefit customers by enabling the combined entity to operate more efficiently, develop high-quality innovative services, and deploy those services more rapidly than either company could on its own. Also, because MCI's and Verizon's facilities and businesses in the state generally do not overlap, the transaction will not result in a lessening of competition in the enterprise market or in the provision of special access services. Finally, because MCI's mass market business is in a state of irreversible decline for the reasons set forth in Mr. Beach's testimony, the transaction will not result in harm to the mass market.

D. Integra

Integra believes the settlement - particularly term 4 - satisfies its interests and is in the public interest. Under this term, Verizon will report the Bell Atlantic-GTE FCC merger condition metrics until it implements for Washington the California

JPSA Verizon metrics. These metrics measure Verizon's performance in its wholesale transactions with competitive LECs like Integra. Under the Agreement, Verizon will report on wholesale metrics at least until the end of 2008. Integra requested this condition in its testimony, and Verizon's commitment satisfies Integra's interest and the public interest because it provides certainty and accountability in wholesale transactions, which ultimately strengthens the provision of service to end user customers.

V. Legal Points that Bear on the Proposed Settlement Agreement

The Settling Parties do not believe there are any legal points that require discussion under WAC 480-07-740(2)(a). By adopting this settlement agreement, however, the Commission avoids the need to address the threshold legal issue – i.e., whether the Commission has jurisdiction over this transaction between parent companies. In its "Notice of Pre-hearing Conference" dated June 3, 2005, the Commission stated it would address this jurisdictional issue "in the context of the adjudication." Approving the settlement agreement will render this issue moot.

Also, by adopting the settlement agreement, the Commission need not address the appropriate standard for merger review under state law and under WAC 480-143-170. Verizon and MCI argue that the standard is "no harm;" Staff argues that the standard should be "no harm" plus some affirmative public benefit.

Roth at 11-12. The settlement agreement easily satisfies both standards, and therefore by adopting it, the Commission need not resolve this legal issue.

Furthermore, Public Counsel, Covad and XO have proposed conditions that Verizon and MCI believe are outside the Commission's jurisdiction. For example, Public Counsel asks the Commission to regulate DSL deployment, but DSL service is an interstate service, and Joint Petitioners do not believe the Commission has jurisdiction to impose this condition. In a similar vein, Covad and XO ask the Commission to regulate UNE prices and interconnection agreements in a manner Verizon believes is inconsistent with, and preempted by, federal law. These legal issues, too, are avoided if the Commission adopts the settlement.

VI. Conclusion

The Parties respectfully request the Commission approve the Settlement Agreement filed in this docket.

DATED this 20th day of October, 2005.

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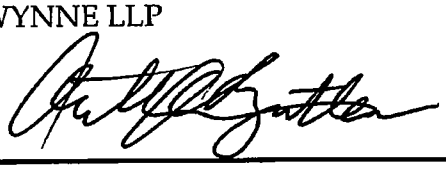

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