STATE OF IOWA

DEPARTMENT OF COMMERCE

UTILITIES BOARD

IN RE: U S WEST COMMUNICATIONS, INC., n/k/a QWEST CORPORATION	DOCKET NOS. INU-00-2 SPU-00-11

CONDITIONAL STATEMENT REGARDING PUBLIC INTEREST AND TRACK A

(Issued January 25, 2002)

On February 10, 2000, the Utilities Board (Board) issued an order initiating an investigation relating to the possible future entry of U S WEST Communications, Inc., n/k/a Qwest Corporation (Qwest), into the interLATA market. The investigation was identified as Docket No. INU-00-2.

In a filing dated May 4, 2000, Qwest encouraged the Board to consider a multi-state process for purposes of its review of Track A (competition issues)[1], various aspects of each item on the 14-point competitive checklist, § 272 (separate subsidiary) issues and public interest considerations. The Board considered the concept of a multi-state process for purposes of its review of a Qwest § 271 application, sought comment, and subsequently issued an order dated August 10, 2000, indicating that its initial review of Qwest's compliance with the requirements of 47 U.S.C. § 271 would be through participation in the multi-state workshop process with the Idaho Public Utilities Commission, North Dakota Public Service Commission, Montana Public Service Commission, Wyoming Public Service Commission, and the

[1] See 47 U.S.C. § 271(c)(1)(A).

Utah Public Service Commission. Since the time of that order, the New Mexico Public Regulation Commission has also joined in the workshop process.

A report was filed with the Board on September 24, 2001, addressing issues related to Track A § 272, and general terms and conditions. On October 22, 2001, Liberty Consulting Group (Liberty) filed a report addressing issues raised by workshop participants related to the public interest of Qwest's future entry into the in-region interLATA market.[2] Only the Track A issues of the September 24, 2001, report and the public interest issues filed in the October 22, 2001, report are considered in this conditional statement.

TRACK A

There are four Track A requirements of 47 U.S.C. § 271(c)(1)(A). The requirements pertain to the degree of local-exchange market entry by Qwest's competitors. They are summarized as follows:

(1) Whether Qwest has signed one or more binding interconnection agreements that have been approved under section 252;

(2) Whether Qwest is providing access and interconnection to unaffiliated competing providers of telephone exchange service;

(3) Whether there are unaffiliated competing providers of telephone exchange service to residential and business customers; and

(4) Whether the unaffiliated competing providers offer telephone exchange service exclusively over their own telephone exchange service facilities or predominantly over their own telephone exchange service facilities in combination with the resale of the telecommunications services of another carrier.

[2] These reports were prepared by the "outside consultant," The Liberty Consulting Group (Liberty), which has been retained to assist the state commissions collectively by making recommendations for resolution of impasse issues.

Whether Qwest Corporation (Qwest) met the first, second, and fourth Track A requirements was generally uncontested. The only controversy was over the third requirement.

For those issues where agreement has been reached, the Board is prepared to indicate at this time its conclusion that Qwest has conditionally satisfied the Track A requirements in the areas identified by the September 24, 2001, report. To the extent that an issue requires performance of some duty or activity on Qwest's part, Qwest will need to demonstrate that it adequately performs as expected in order for the Board to make a positive recommendation to the FCC following an application filed by Qwest.

After reviewing the September 24, 2001, report relating to the issue of Track A, the testimony, pre-report briefs, and post-report comments filed by those interested participants, the Board finds that no further proceedings are necessary to reach a conditional determination on those issues that remain subject to disagreement.

The Board will address each of the Track A requirements in turn in this conditional statement.

1. Existence of Binding, Approved, Interconnection Agreements

Qwest presented evidence that, in Iowa, as of April 30, 2001, it had entered into 94 binding and approved interconnection agreements.[3] No party contested this aspect of Track A compliance.

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[3] Exhibit S8-QWE-DLT-9.

Liberty noted the FCC held that, for agreements to be binding, it is sufficient that they "specify the rates, terms, and conditions under which [the Bell Operating Company (BOC)] will provide access and interconnection to its network facilities." [4] Liberty concluded that Qwest has met the first Track A requirement because it has signed at least one binding interconnection agreement that has been approved under section 252.

The Board agrees with Liberty's conclusion that Qwest has met the first Track A requirement.

2. Provision of Access and Interconnection to Unaffiliated Competitors

Qwest offered evidence that, as of April 30, 2001, it was providing access and interconnection to 14 Iowa CLECs. As of the same date, it had leased 138,192 unbundled loops to competitors.[5] No party contested this aspect of Track A compliance.

Liberty noted that satisfaction of the second Track A requirement does not require CLECs to have achieved any given geographic service range in a state.[6] Additionally, satisfaction does not require CLECs to have placed "a substantial commercial volume" of orders or achieved a minimum market share.[7] Liberty concluded that Qwest's unrebutted evidence addressing unbundled loop leases demonstrates that it meets the requirement that it provides access and interconnection to unaffiliated competing providers of telephone exchange service.

4 Memorandum Opinion and Order, *Application of Ameritech Michigan Pursuant to Section 271 of the communications Act of 1934, as amended, To Provide In-Region, InterLATA Services in Michigan*, 12 FCC Rcd 20543, (released August 19, 1997) ¶¶ 72-73. (Ameritech Michigan Order)
5 Exhibit S8-QWE-DLT-9.
6 Ameritech Michigan Order at ¶ 76.
7 Ameritech Michigan Order at ¶ 77.

The Board agrees with Liberty's conclusion that Qwest has met the second Track A requirement.

3. Existence of Competing Residential and Business Service Suppliers

Qwest is required to show that CLECs are providing telephone exchange service to residential and business subscribers.[8] Of the four Track A requirements, this was the most contested. Testimony from AT&T and the Office of Consumer Advocate Division of the Department of Justice (OCA) challenged the competitive access line estimates Qwest submitted to show that it had met the requirement. Qwest argued the use of estimates was appropriate because it had limited data on the number of customers actually served by CLECs. The following aspects of this Track A requirement were identified in Liberty's report:

A. Market share of competing providers
B. Estimates of bypass lines
C. The number of CLECs serving end users

A. Market Share of Competing Providers

Qwest quoted that as long as CLECs are "serving more than a de minimis number of end-users for a fee in their respective service areas," the FCC will "find that each of these carriers is an actual commercial alternative to the BOC."[9] Qwest estimated that, as of April 30, 2001, Iowa CLECs were serving between 163,392 and 216,675 total access lines. Qwest noted that the lower estimate was determined by its preferred methodology. The higher estimate was determined using the methodology approved by the FCC for Kansas and Oklahoma.

[8] Ameritech Michigan 271 Order at paragraph 82.
[9] Ameritech Michigan Order at ¶ 78.

Qwest estimated that Iowa CLECs have captured a 14.2 percent market share.[10] This is a higher competitive market share than in either Kansas or Oklahoma, each of which received 271 approval. Qwest stated that it did not know the exact split between competitive residential and business lines, because only CLECs have the information, thus estimates were used.

There was specific access line information provided by one CLEC that gave a breakdown of its access lines between business and residential customers.[11] Additionally, information was provided that further delineated between access lines served over facilities owned by the CLEC, via UNEs, and via resale.[12]

OCA noted that the FCC has begun reporting on the development of local competition on a semi-annual basis. According to the FCC's most recent report, as of December 31, 2000, the national competitive market share was 8.5 percent, while Iowa’s competitive market share stood at 10 percent.[13]

AT&T stated the Ameritech Michigan Order, at paragraphs 75 and 77, adopted the requirement that there be "an actual commercial alternative to the BOC" and it recognized that "there may be situations where a new entrant may have a commercial presence that is so small that a new entrant cannot be said to be an actual commercial alternative to the BOC and, therefore, not a 'competing provider.'" AT&T estimated that CLECs are serving a miniscule number of residential customers, over their own facilities, in the seven states-about 30,000 combined.

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[10] Confidential Exhibit DLT-2.
[11] Confidential S8 QWE DLT-25
[12] Confidential S8 QWE DLT-26
[13] "Local Telephone Competition: Status as of December 31, 2000," Federal Communications Commission, May 2001, Table 1 and Table 6. This report can be found at http://www.fcc.gov/Bureaus/Common_Carrier/Reports/FCC-State_Link/IAD/lcom0501.pdf

Liberty concluded that the decision on this aspect of Track A is not illuminated by arguments that the number of residential customers being served by CLECs is small, or even "minimal." The FCC has already decided that it will not impose a market share test, and it has deemed Track A to be satisfied at very low CLEC levels of penetration into the residential market. Therefore, in the event that Qwest can demonstrate that it is providing service at the levels shown in its testimony, it should be considered to have met this aspect of Track A.

The Board notes that Liberty's conclusion for this aspect of Track A was addressed to the seven states as a group. Liberty's conclusion relates to the FCC's determination that "one or more" CLECs providing service to residential and business subscribers will satisfy this aspect of Track A.[14] Compared with the earlier, more strict, interpretation of section 271 this is a relaxed standard. The earlier interpretation indicated there must be at least one CLEC providing more than a "de minimis" amount of service to both residential and business subscribers.

For some of the other seven states, there appeared to be no single CLEC that could meet the requirement. Iowa is able to rely on the actual numbers provided by one CLEC to meet the requirement. The confidential record indicates that McLeodUSA is providing service to both residential and business customers at more than "de minimis" levels. Alternatively, even without the specific actual numbers found in the confidential record, customer counts of multiple CLECs would be sufficient to meet this requirement in Iowa.

[14] Ameritech Michigan Order at ¶ 82.

The Board concludes that CLECs in Iowa are serving more than a "de minimis" number of residential and business end users and that Qwest has satisfied this aspect of the third Track A requirement.

B. Estimates of Bypass Lines

Bypass lines are access lines provisioned independently by CLECs rather than leased UNE loops. Qwest estimated that, as of April 30, 2001, Iowa end-users were being served by 15,428 competitive bypass lines. Qwest further estimated that 90% of those bypass lines serve business customers with the remaining 10% serving residential customers. Qwest was unable to provide any evidence other than estimates because it does not have access to confidential CLEC network information. Additionally, it could not secure the information, through discovery, from CLECs who did not participate in the workshops.[15] Qwest noted that the FCC has relied upon estimates in every section 271 application it has granted.

Qwest made the estimate by dividing ported numbers in half, on the assumption that CLECs might not still be serving the customers whose numbers were ported. Qwest argued that two factors serve to make its method conservative: (1) the division of ported numbers, and (2) the decision not to consider in its estimate the fact that CLECs were serving customers through non-ported numbers. Qwest also argued its estimation method was much more conservative than the method on which the FCC relied in the Kansas/Oklahoma proceeding. According to Qwests testimony, employing the estimation method relied upon by the FCC in the

[15] The Board notes that very few CLECs who have been granted a certificate of public convenience and necessity to provide local telephone service pursuant to Iowa Code § 476.101 (2001) requested authority to participate in this docket.

Kansas/Oklahoma 271 proceeding would produce bypass line estimates from 200 to 800 percent higher than Qwest's ported number method.[16]

AT&T argued that there is no statistical basis for accepting the linkage between number porting and bypass lines. AT&T noted that the method Qwest used in Washington was the same arithmetically, but that Qwest explained differently the steps involved in applying it. According to AT&T, the differences in the explanations produced an "air of mystery and obfuscation to an already questionable methodology."[17] AT&T also argued that the SBC method fails to pass what it termed a "straight-face test, otherwise Qwest would have relied upon it to the exclusion of its own methodology." AT&T suggests that the inference to be drawn is that competition in the seven states is "pathetically low" when compared to Kansas or Oklahoma.[18]

The OCA also criticized Qwest's use of estimates. OCA argued that when two estimation methodologies produce results that differ by as much as eight hundred percent, there is reason to question both methods.[19]

Liberty stated that Qwest's use of ported numbers to derive estimates of bypass lines was logical. Qwest's method produced results that were substantially less than what it could have claimed had it chosen to use the Kansas/Oklahoma method. Liberty acknowledged that while the method may not be perfect, it is reasonable, and the challenges were unpersuasive. Liberty noted that if Qwest's method had produced inaccurate results, it is likely that CLECs would have

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[16] Qwest Track A Brief at pages 30 through 33. *See* S8 QWE DLT-9.
[17] AT&T Track A Brief at page 4.
[18] AT&T Track A Reply Brief at page 20.
[19] OCA Track A Reply Brief at page 6.

presented evidence of their own to challenge the numbers. Liberty concluded that Qwest made a credible showing with a foundation in prior FCC decisions.

In comments to Liberty's report, both AT&T and OCA reiterated their objections to the estimation method used to derive the line counts. However, the Board notes that no specific information was presented by any participant that would provide a substantive challenge to Qwest's estimates. The argument was over the method Qwest used to derive the number, and it is likely that no estimates would have escaped criticism. Qwest noted that an alternative to estimates would be for the Board to serve data requests on all Iowa CLECs.[20]

This is not a necessary endeavor for the Board to undertake, because information provided pursuant to Qwest's data requests (and made a part of the confidential record in this proceeding) corroborate the presence of competitive bypass lines in Iowa.[21]

The Board concludes that sufficient business and residential bypass lines are being served by competitors in Iowa for Qwest to have satisfied this aspect of the third Track A requirement.

C. The Number of CLECs Serving End Users

Qwest described five Iowa CLECs providing competition: McLeodUSA, Cox Cable, Hickory Tech, Goldfield Access Network, ald AT6T Broadband.[22] Qwest indicated that each of the first four CLECs is providing both business and residential service. Qwest noted that AT&T Broadband was expected to provide telephone service in 2001.

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[20] Qwest Track A Brief at 28.

AT&T argued that none of the CLECs should be considered a "commercial alternative" to Qwest until they can handle order volumes at commercial levels or until they can provide service at the same level as Qwest.[23] The OCA raised concerns with Qwest's list of CLECs, noting that AT&T Broadband had sold its Iowa assets and left the state.[24] OCA opines the loss of AT&T Broadband is symptomatic of the difficulties of bringing competition to the local market.[25]

Liberty concluded the record supports a determination that CLECs are providing service to business and residential customers and this aspect of the third Track A requirement has been satisfied in Iowa.

Achieving compliance for this aspect of Track A appears to be the same as achieving compliance for the "market share" section above. The FCC stated that compliance can be "met if multiple carriers collectively serve residential and business customers."[26] No participant disputed Qwest's basic contention that multiple CLECs are serving residential and business customers either individually or collectively.

AT&T's "commercial alternative" argument appears to be misplaced in the context of Track A, but it will be addressed in the context of OSS Testing. OCA's complaint that AT&T Broadband has left the state is irrelevant, because there are still multiple Iowa CLECs serving business and residential customers.

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[21] Confidential S8 QWE DLT-25 at 1-2 and Confidential S8 QWE DLT-26 at 2.
[22] Qwest Track A Brief pp. 12-15. *See* S7 QWE DLT-1 and S7 QWE DLT-2
[23] AT&T Track A Brief at page 25.
[24] *See* S7 IOCA DSH-4.
[25] OCA Track A Brief at 10.
[26] Ameritech Michigan Order at ¶ 82.

The Board concludes there are multiple CLECs serving business and residential customers in Iowa, and Qwest has satisfied this aspect of the third Track A requirement.

4. Existence of Facilities-Based Competitors

As noted above, for the third Track A requirement, Qwest provided actual counts for UNE-loops leased to competitors and estimates of full facilities bypass lines placed in service by competitors.

Liberty noted that the FCC has ruled that a CLEC's "own" facilities include UNE-loops leased from the incumbent carrier.[27] Liberty also pointed out that opposing testimony only challenged Qwest's bypass line estimates and the allocation of the bypass lines between residential and business customers. The testimony did not challenge the existence of facilities-based competitors. Therefore, Liberty concluded that, because of the lack of a specific challenge to the fourth Track A requirement, its conclusions regarding the third Track A requirement apply here.

In its comments to Liberty's Report, AT&T did not specifically address facilities-based competition in Iowa. AT&T instead focused on the general estimation methodology for CLEC bypass lines. Its comments overlooked FCC recognition that leased UNE-loops qualify as facilities-based competition and that Qwest provided actual numbers for the UNE-loops.

OCA did not specifically challenge Liberty's conclusion in its comments on the report. However, it maintained its general argument that Track A approval is not in the public interest.

[27] Ameritech Michigan Order at ¶ 99.

The Board agrees with Liberty's conclusion that there are facilities-based competitors in Iowa and that Qwest has met the fourth Track A requirement.

PUBLIC INTEREST

The Telecommunications Act requires an applicant to show that "the requested authorization is consistent with the public interest, convenience, and necessity."[28] The FCC has emphasized that public interest is a separate inquiry from the competitive checklist, and the FCC addresses public interest separately in its decisions.[29] Nevertheless, the FCC has also indicated that compliance with the competitive checklist, itself, provides a strong indication that long distance entry is consistent with the public interest.[30]

Based on the FCC's stated position, Liberty ruled that the burden of proof for public interest issues would lie with the party raising them, not Qwest.[31] Liberty also ruled that any public interest issue that restated an issue from a checklist item in a manner that attempted to merely increase Qwest's burden of proof would be disregarded. Without this limitation, the intent of Congress in adopting the checklist, while also allowing a separate consideration of public interest matters, would be compromised.

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[28] 47 U.S.C. § 271(d)(3)(C).

[29] Memorandum Opinion and Order, *Joint Application by SBC Communications, Inc., Southwestern Bell Telephone Company, and Southwestern Bell Communications Services, Inc. d/b/a Southwestern Bell Long Distance for provision of In-Region, InterLATA Services in Kansas and Oklahoma,* 16 FCC Rcd 6237 (2001) at ¶ 267. (SBC Kansas/Oklahoma Order)

[30] Memorandum Opinion and Order, *Application of Bell Atlantic New York for Authorization Under Section 271 of the Communications Act To Provide In-Region, InterLATA Service in the State of New York,* 15 FCC Rcd 3953 (1999) at ¶ 422 (Bell Atlantic New York Order), *aff'd sub nom. AT&T Corp. v. FCC*, 220 F.3d 607 (D.C. Cir. 2000)

[31] For non-public interest issues i.e., checklist compliance and post assurance plans, the burden of proof lies with Qwest.

Eleven issues were raised by workshop participants as an attempt to show 271 approval for Qwest is not in the public interest. The Board will address each of the eleven issues.

1. UNE Prices

AT&T testified that recurring and non-recurring Unbundled Network Element (UNE) prices exceed Qwest's retail rates, arguing these prices are a primary cause of the failure of Qwest retail markets to be open to competition. AT&T compared 1FR and UNE-P prices to show that local entry is unprofitable because of the higher UNE prices.[32] Both Sprint and ASCENT made similar arguments.

Qwest argued that the FCC has previously ruled that the ability of CLECs to make a profit after leasing UNEs is irrelevant. The only consideration is whether UNE prices are cost-based.[33]

Liberty articulated that checklist compliance requires UNE pricing to meet the standards of the Act. However, Liberty concluded that AT&T's comparison was simplistic because it did not consider vertical features, intrastate toll revenues, or the existence of resale as an option for classes that do not lend themselves to economical use of UNEs. Additionally, AT&T's comparison did not include business rates, nor address the economics of residential competition using full facilities-based competition.

Liberty concluded that whether or not Qwest's UNE rates meet the checklist is a question that it was unable to answer. Instead, Liberty quoted the FCC as follows:

[32] AT&T Public Interest Brief, p. 6. *See* S7 ATT MJR-4.
[33] SBC Kansas/Oklahoma Order at ¶ 92.

> The Act requires that we review whether the rates are cost-based, not whether a competitor can make a profit by entering the market. Were we to focus on profitability, we would have to consider the level of a state's retail rates, something which is within the state's jurisdictional authority, not the Commission's.[34]

In its post-report comments, AT&T objected that Liberty had not addressed the basic problem that, under current UNE prices, a new entrant must compete with a well-funded incumbent, while losing money on each new customer, while at the same time attempting to raise capital. According to AT&T, as long as the pricing disparity exists, the introduction and development of competition will be hindered.

Qwest responded to Liberty's report by reiterating that incumbent LECs are not required, pursuant to section 271, to guarantee competitors a profit margin.[35] Qwest commented that the FCC has twice reaffirmed this position since the *SBC Kansas/Oklahoma Order,*[36] and it has specifically refused to consider this argument as part of its Public Interest Inquiry.[37] Given that the FCC has rejected AT&T's UNE pricing argument three times, Liberty concluded that the argument was "of questionable relevance."

The Board agrees with Liberty's conclusion that according to previous FCC orders, the issue of whether UNE prices are too high for CLECs to make a profit is

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[34] *Id.* at ¶ 92.
[35] SBC Kansas/Oklahoma Order at ¶ 65.
[36] *See,* Memorandum Opinion and Order, *Application of Verizon Pennsylvania Inc., Verizon Long Distance, Verizon Enterprise Solutions, Verizon Global Networks Inc., and Verizon Select Services Inc., for Authorization to Provide In-Region, InterLATA Services in Pennsylvania,* CC Docket No. 01-138, FCC 01-269 (rel. Sept. 19, 2001), ¶ 70 (Verizon Pennsylvania Order); and Memorandum Opinion and Order, *Application of Verizon New England Inc., Bell Atlantic Communications, Inc. (d/b/a Verizon Long Distance), NYNEX Long Distance Company (d/b/a Verizon Enterprise Solutions) and Verizon Global Networks Inc., for Authorization to Provide In-Region, InterLATA Services in Massachusetts,* 16 FCC Rcd 8988, ¶ 41 (Verizon Massachusetts Order).
[37] SBC Kansas/Oklahoma Order at ¶ 281.

not relevant to the public interest inquiry. Therefore, the Board makes no determination on this issue.

2. Intrastate Access Charges

AT&T argued that Qwest's intrastate access charges are significantly above cost and would provide it an unfair price advantage if allowed to serve the combined interLATA and local markets. AT&T listed Qwest's intrastate access charges in the seven participating states and estimated that they range from 227 to 894 percent in excess of Qwest's costs. The listing indicated that intrastate access charges in Iowa are 362 percent above Qwest's costs.[38] AT&T compared Qwest's intrastate access charges to the federal interstate BOC surrogate charge to estimate the amount that Qwest's rates exceed costs.

Assuming the access charges are above cost, AT&T maintained that Qwest would make excess profits whether it or a competitor processes a customer's long distance calls. AT&T suggests that Qwest's ability to bundle local and long distance service will squeeze competitors out of the long distance market. AT&T maintained that Qwest's high access charges are not in the public interest because they will result in substantial harm to the development of telecommunications competition.

AT&T further argued that the imputation requirements of section 272 would not resolve this problem. Although it precludes Qwest from charging its long distance affiliate lower access rates than a competitor, it does not address the problem that the above-cost portion of the access charge flows right back to Qwest. AT&T urged

[38] S7 ATT MJR-4, pp. 11-12.

state commissions to address access charge reform prior to the approval of a 271 application. Sprint also requested access charge reform.

In briefing the issue, Qwest relied on two arguments. First, the FCC has never conditioned 271 approval on reforming access charges. Second, section 272 requires Qwest's long distance affiliate to pay the same interstate access charges as any competing carrier. Therefore, there is no need to stretch the Public Interest Inquiry to include this issue.

Liberty focused on whether the imputation requirement of section 272 provides an adequate resolution of the issue. Liberty acknowledged that access charges paid by the Qwest affiliate ultimately flow to another Qwest entity, while CLECs do not pay access charges to an entity with whom it shares a bottom line interest. Liberty noted, however, that a proper inquiry into this issue must go beyond equality of payment. It must also address the uses to which the access charges paid by a Qwest affiliate are put, such as, to a universal service fund or to offset facilities costs. Depending upon how the money is used would indicate whether competitors could be "squeezed out" of the local market.

Liberty noted that there was not sufficient evidence to examine this issue "as it absolutely must be examined." Liberty also stated that an examination of how access costs are recovered and how margins are distributed is "critical to assuring that undesirable barriers to competition are avoided." Liberty indicated that it could not resolve the issue. However, it recommended that the individual commissions determine whether the "competitive playing field" has been leveled "consistent with public policy in their jurisdictions."

In its post-report comments, AT&T was critical of Liberty for not proposing a resolution after stating the significance of the problem. AT&T stated that Liberty had improperly shifted the burden of proof from Qwest to the intervening parties, arguing that Qwest has the evidence necessary to examine the issue, not the new entrants. Although the issue and its ramifications were brought to light, Qwest was not required to answer based on the Liberty report. Thus, AT&T recommends postponing a finding of public interest compliance until state-specific proceedings can address the issue.

Qwest responded to Liberty's report by buttressing the arguments from its briefs with quotes from the FCC's specific ruling on this issue. Relevant sections of that ruling are as follows:

> Incumbent LECs seeking to provide interLATA services through an affiliate must adhere to certain structural separation and nondiscrimination requirements. For example, Congress anticipated that some Bell Operating Companies ("BOCs") would obtain authorization under 47 U.S.C. § 271 to originate in-region long distance services before the completion of access charge reform . . . . Congress therefore enacted Section 272, which requires a BOC competing in the in-region long distance market to create a separate long distance affiliate and to recover access charges from that affiliate on the same basis on which it recovers such charges from unaffiliated carriers. As we have consistently determined, those structural and non-discrimination requirements provide adequate safeguards against any effort by an incumbent to obtain an unfair competitive advantage in the long-distance market . . . . Indeed, those "separation requirements have been in place for over ten years, and independent (non-BOC) incumbent LECs have been providing in-region interexchange services on a separated basis with no substantiated complaints of a price squeeze."[39]

[39] Supplemental Order Clarification, *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, 15 FCC Rcd 9587, ¶19 .

Qwest, therefore, maintains that access reform is not an appropriate issue for a Public Interest Inquiry.

Qwest did not submit the FCC ruling cited above in its workshop testimony or its pre-report briefs. Prior to Liberty's report, Qwest simply maintained that the section 272, imputation requirement was sufficient and that the FCC had never conditioned approval of a 271 application on access reform.

Liberty apparently, not satisfied with the basis of Qwest's position, concluded that the individual states should investigate further. The implication is that 271 approval may need to be delayed until the completion of access charge reform.

The FCC quotes provided in Qwest's post-report comments, however, seem to overwhelmingly support Qwest's position. It appears that Congress, itself, contemplated this issue and reasoned that the imputation requirements of section 272 provide an adequate safeguard.

The Board does not agree that a delay in implementing access charge reform precludes a finding that Qwest's 271 approval is in the public interest. Clearly the FCC has indicated otherwise.

3. Performance Assurance Plan

AT&T, Sprint, and ASCENT identified the need for a performance assurance plan as relevant to the Public Interest Inquiry. Liberty noted that Qwest's performance assurance plan (QPAP) would be fully addressed in Liberty's QPAP Report. Only Qwest filed post-report comments, agreeing it would be duplicative to address the issue as part of the Public Interest Inquiry.

The Board agrees that a post assurance plan is not an issue for the Public Interest Inquiry. The Board will address Qwest's performance assurance plan in a separate statement.

4. Lack of Competition

The OCA argued that Qwest remains dominant, and serves 85.8 percent of the lines in Iowa. This yields a Herfindahl-Hirshmann Index (HHI) between 7,367 and 7,563. These numbers are midway between a complete monopoly (HHI - 10,000) and a fifty-fifty duopoly (HHI - 5,000).

OCA notes a failure of other BOCs to cross into Qwest's service territory to compete. Moreover, Qwest has not ventured beyond its 14-state region to compete elsewhere. In 2000, Qwest's return on equity was 20.78 percent according to OCA testimony.

As for the competition, OCA points to an FCC report showing that there are no competitive carriers in 64 percent of Iowa's postal zip code zones. OCA notes the financial difficulties of CLECs and that AT&T has sold its Iowa cable network. OCA questions the long-term viability of McLeodUSA.

OCA also criticizes the 271 approvals granted by the FCC in other states. OCA asserts that the FCC should more seriously consider the evidence that actual competition is slight. OCA argues that checklist compliance is not synonymous with public interest. It is the actual level of competition that acts to cancel a monopolist's power and determines whether consumer benefits will flow.

OCA contends that public interest was at the heart of Congress' design of the Telecommunications Act. In the past, too much reliance has been placed on the checklist and not enough on developments in the marketplace. In order to maximize consumer welfare, OCA contends the FCC should recognize the continued resilience of the local monopolies and deny 271 approval in Iowa.

Similar arguments calling for market share tests and noting the financial difficulties of CLECs, were put forth by AT&T, ASCENT, and Sprint.

Qwest states that that the interveners' attempts to reintroduce market share tests into the Public Interest Inquiry ignore previous FCC orders. In the SBC Kansas/Oklahoma Order, the FCC noted that "Congress specifically declined to adopt a market share or other similar test for BOC entry into long distance, and we have no intention of establishing one here."[40] The order also states, "Given an affirmative showing that a market is open and the competitive checklist has been satisfied, low customer volumes in and of themselves do not undermine that showing."[41]

Regarding the financial problems CLECs are facing, Qwest says these are matters over which it has no control such as: CLEC business plans, the overall economic slowdown; inexperienced CLEC management; too many competitors with the same business plans; and unmanaged growth. The financial health of the capital markets, or of the CLECs in general, should not be considered in the Public Interest Inquiry.

Liberty noted that Congress clearly intended that section 271 can be met in an empty room, provided there is certainty that the door to the room has been unlocked.

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[40] SBC Kansas/Oklahoma Order, at ¶ 268.
[41] *Id.*

As noted previously in the discussion of the Track A requirements, there is no explicit or implied minimum market penetration test required for 271 approval.

Liberty also noted that OCA's evidence shows that local exchange competition in Iowa significantly exceeds what existed in other states where 271 authority has been granted. Liberty questioned the merits of placing Qwest under a stricter standard than applied to other BOCs. Liberty concluded that whether a standard is to a participant's liking is not material. What is material is whether Qwest meets the law and the precedent established by the FCC.

In its post-report comments, OCA urged the Board to request that the FCC review its position on how it determines whether the public interest has been met. OCA recommends the FCC adopt a revised standard making meaningful competition an essential element of the Public Interest Inquiry. OCA argues the overriding goal of the Act, as set forth by Congress, is to serve the public interest through healthy, unfettered competition. It is not enough to merely determine that the door is now open for the CLECs to compete. For the goal to be met, there must also be a finding that CLECs can provide meaningful competition. According to OCA, the market power issue, central to any antitrust inquiry, should be central to the Public Interest Inquiry, thus OCA argues the FCC needs to find the existence of meaningful competition before granting Qwest 271 approval.

What OCA is asking the Board to support is a quest to change the rules of the 271 approval process in mid-stream. OCA's premise seems to be that the FCC has misconstrued the intent of Congress by not adopting a market share/power test before granting 271 approval. This concern has been raised in other jurisdictions, and the FCC continues to address it in its 271 orders. Most recently the FCC reiterated, "[t]hat Congress had considered and rejected language that would have imposed a 'market share' requirement in section 271(c)(1)(A)."[42]

The Board agrees with Liberty's conclusion that the level of CLEC market penetration is not relevant to the Public Interest Inquiry.

5. Prior Qwest Conduct

AT&T cited the FCC's public interest discussion, regarding anti-competitive behavior, from the Ameritech Michigan 271 Order:

> Furthermore, we would be interested in evidence that a BOC applicant has engaged in discriminatory or other anti-competitive conduct, or failed to comply with state and federal telecommunications regulations. Because the success of the market opening provisions of the 1996 Act depend, to a large extent, on the cooperation of incumbent LECs, including the BOCs, with new entrants and good faith compliance by such LECs with their statutory obligations, evidence that a BOC has engaged in a pattern of discriminatory conduct or disobeying federal and state telecommunications regulations would tend to undermine our confidence that the BOC's local market is, or will remain, open to competition once the BOC has received interLATA authority.[43]

AT&T asserted that Qwest has disobeyed federal or state telecommunications regulations and engaged in a pattern of anti-competitive conduct. AT&T cited the following examples of Qwest's behavior since the passage of the Telecom Act:

- Qwest entered the interLATA market by providing (1-800-4USWEST) calling card services.

- Qwest entered the interLATA market through its provision of nonlocal directory assistance.

[42] Verizon Pennsylvania 271 Order, at C-6, footnote 27.
[43] Ameritech Michigan 271 Order, at ¶ 397.

- Qwest provided their local customers with "one-stop shopping" that included interLATA services.
- Private line services (interLATA transport) for 266 large businesses were billed and branded as "Qwest services."
- Qwest sought to remove a LATA boundary in Arizona so it could provide long distance service throughout the state.
- In Minnesota, Qwest refused to cooperate with various OSS testing procedures.
- In Washington, Qwest refused to provide NID (network interface device) access at multi-tenant dwellings.
- In Colorado, Qwest refused to convert Sun West Communications' customers from resale to UNEs. It also failed to provide interconnection to Sun West's customers, depriving them of telephone service.
- In Washington, Qwest deliberately delayed providing interconnection to MCI Metro.
- In Colorado, Qwest refused to provide Rhythms with ADSL and IDSN capable loops.

AT&T maintains that these violations should cause state commissions to conclude that Qwest has refused to open its local markets in compliance with section 271.

Regarding the cases involving interLATA services, cited by AT&T, Qwest responded by explaining these were pre-merger U S WEST good-faith interpretations of the requirements of section 271. In the case involving private lines, the services were provisioned by Touch America, but they were erroneously billed in the name of Qwest. This matter is currently under review by the FCC. Qwest did not respond to the cases, cited by AT&T that occurred in Arizona, Minnesota, Washington, and Colorado.

Liberty separated the cases cited by AT&T into two categories: (1) those relating to pre-271 approval limits on in-region, interLATA service and (2) those relating to Qwest's obligations to provide wholesale services to CLECs. Liberty also stated its view that the Public Interest Inquiry is not meant to be "punitive."

Regarding the first category, Liberty noted that it previously addressed the same issue in its Group Five Report under Section 272 requirements.[44] In that report, Liberty noted that Qwest had already been held accountable for failing to correctly interpret what constitutes in-region, interLATA service. For the Public Interest Report, Liberty stated that those violations are not predictive of Qwest conduct after 271 approval may be granted. Consequently, Liberty concluded that Qwest's past infractions were not of the nature to support a finding that Qwest's entry into the in-region, interLATA market would contravene the public interest.

Considering the second category of cases cited by AT&T, Liberty noted that several of them represented good faith disputes that Liberty addressed in previous reports. Several of the other cases involved allegations of a complaint by a third party in a non-participating workshop state. Liberty saw these examples as insufficient to demonstrate a pattern of past abuse significant enough to question the public interest of permitting Qwest to enter the in-region, interLATA market.

In its post-report comments, AT&T disagreed that Qwest's "prior bad acts" are not predictive of future behavior. AT&T also criticized Liberty's comment that the Public Interest Inquiry is not meant to be punitive. AT&T suggested that Liberty thinks the Act itself is punitive, such that every minute Qwest is denied the ability to provide interLATA service is another minute the company is being punished for something.

According to AT&T, the question is not whether Qwest should be denied 271 authority in order to punish it for its prior bad acts, but whether granting 271 approval is consistent with the public interest, in light of those prior bad acts. AT&T maintains that it provided sufficient evidence of Qwest's prior actions, but that Liberty dismissed the evidence by setting a new standard-that the proof would have to be "predictive" of future actions, that would be necessary to show that Qwest has failed the public interest standard of section 271.

The foundation of AT&T's argument is the Ameritech Michigan 271 Order. That order was issued in August 1997. The FCC denied Ameritech 271 authority in Michigan. The order contains a lengthy discussion about issues to be considered in a Public Interest Inquiry. Paragraph 397 references a BOC's past failure "to comply with state and federal telecommunications regulations" as subject to a Public Interest Inquiry.

At the time of that order, however, there was no good means, to deal with a BOC's future infractions of telecom regulations after winning 271 approval. The Ameritech Michigan 271 Order was only the second of the 271 applications that resulted in an FCC order. Since that order, all BOC's that have gained 271 approval voluntarily proposed performance assurance plans, with financial penalties, to assure future compliance. Qwest has also proposed a performance assurance plan (QPAP),

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[44] General Terms and Conditions, Section 272, & Track A Report, issued September 24, 2001, pp. 49-50.

which is the subject of a Liberty report that will be addressed by the Board in the future.

AT&T's position allows no middle ground for dealing with past infractions. It assumes that if some infraction occurred in the past, it will absolutely occur in the future. Following this logic, 271 approval can never be in the public interest. AT&Ts position provides no means for Qwest to move forward.

The QPAP provides the means to move forward by creating a middle ground in which Qwest could receive 271 approval while at the same time being subject to backsliding penalties. In this light, Liberty's burden of proof standard, that past behavior must be predictive of future behavior, appears entirely appropriate.

Regarding the actual infractions, AT&T's position seems to make no allowance for the possibility that Qwest's actions were done in good faith. It is noteworthy that the Board has conditionally ruled against AT&T, and taken Qwest's position, in several of these disputes while deciding other section 271 issues.[45]

The Board agrees with Liberty's ruling that none of Qwest's past actions, as noted in this record, should be considered predictive of future behavior or contrary to the public interest.

6. Structural Separation

Both AT&T and Sprint argued that a structural separation of Qwest is in the public interest. Both companies want to see Qwest's retail and wholesale operations separated at least to the extent of the Verizon separation ordered by the

[45] *See*, Conditional Statement Regarding August 20, 2001, Report, OSS Testing (pp. 11-18) and "NID" Definition and Access to Terminals Where Qwest Owns Facilities (pp. 46-49).

Pennsylvania Commission. AT&T sees structural separation as being a state specific condition for 271 approval.

AT&T notes that regulation is a substitute for competition. If there is to be less regulation, structural separation would provide a more appropriate level of consumer protection. Structural separation would put the retail operations of Qwest on an equal footing with other CLECs. The result would be Qwest's wholesale operations being prohibited from delivering retail services or discriminating between retail carriers. The local exchange market would become as competitive as the long distance market.

AT&T also argues that structural separation is a tried and true method of forcing monopoly markets to be competitive. First implemented with the divestiture of AT&T, structural separation has created a vibrantly competitive market for long distance service. Although not required by the 1996 Act or FCC rules, federal law does not prohibit a state from conditioning its recommendation of 271 approval upon structural separation.

Qwest notes that AT&T cannot point to a single FCC 271 order indicating that structural separation is part of a Public Interest Inquiry. Whether Qwest has sufficiently opened its markets to warrant long distance entry is primarily determined by compliance with the competitive checklist. Qwest posits that AT&T's suggestion that regulators can also require a corporate restructuring as part of the process, just for good measure, is a gross distortion of Congress' instructions and intent.

From Qwest's perspective, AT&T's proposal is about dividing Qwest's network and network systems into halves, thus duplicating resources, increasing Qwest's costs, and impairing Qwest's ability to be an effective competitor.

Liberty, noted that the divestiture of AT&T was not a structural separation but a spin-off of various divisions to different corporate ownerships. The structural separation discussed in the briefs would make Qwest's wholesale and retail operations separate departments within the same corporation. Liberty believed such a change would have little effect since both departments would ultimately be under the same ownership. It would also have little effect on the efforts necessary to deter, detect, and sanction inappropriate interactions. Thus, even with structural separation, numerous procedures would need to be set in place to achieve the competitive environment that AT&T seeks.

Liberty stated that structural separation would only accomplish an increase in Qwest's transaction costs. Liberty stated that it is not the role of states to increase Qwest's costs of doing business in order to improve the competitiveness of CLECs. The proper role is to deter, detect, and sanction failures to conform to rules about self-dealing. Liberty concluded that structural separation would have no bearing on that role.

In its post-report comments, AT&T stated, that under Qwest's present corporate structure, there is a fundamental conflict of interest. Qwest remains the wholesale operator of the local telephone network that virtually all CLECs rely upon to provide their own local telephone service. At the same time, Qwest remains the principal competitor of the same CLECs in the same retail markets.

AT&T clarified that structural separation means that Qwest would establish a separate retail affiliate, which would provide finished services to consumers just like any other CLEC. It would also establish a separate wholesale affiliate, which would continue to own and operate the network facilities necessary to provide local telephone services. Thus, in order to provide finished retail services, Qwest's retail affiliate would have to negotiate an interconnection agreement with the wholesale affiliate, pay cost-based UNE rates, and access the affiliate's OSS just like every other CLEC.

Structural separation, properly done, would insure that each entity had separately traded stock. There would be different management, directors, employees, books, records, accounts, and facilities. AT&T is promoting structural separation as an intermediate step, arguing that regulators at a later date may deem full divestiture to be necessary or appropriate.

AT&T's pre-workshop testimony makes the following statement about structural separation.

> [I]f Qwest were structurally separate, the retail arm would have to pay the same price for UNEs as CLECs. Because structural separation includes the mandate that the retail arm of Qwest would not be permitted to sell services below its costs, Qwest would now, for the first time, have at least some incentive to moderate its UNE rates so that its retail arm could effectively compete. [46]

Although not addressed by Liberty, it would seem that structural separation could provide CLECs a means of resolving the UNE pricing issue. UNE pricing remains a point of contention for CLECs who argue that UNE prices remain too high

[46] S7 ATT MJR-4, p. 42, footnote deleted.

for them to compete. Structural separation, as envisioned by AT&T, would subject a structurally separated Qwest retail arm to state-approved UNE prices. AT&T states that Qwest would then have an incentive to moderate UNE prices.

Although this could prove to be true under a specific blueprint for structural separation, it is important to note that structural separation was not Congress' blueprint for achieving local exchange competition. The Congressional blueprint was the Competitive Checklist, Track A, the Affiliate Requirements of Section 272, and the Public Interest Inquiry.

Congress could have passed legislation for achieving local exchange competition based on some form of BOC structural separation, but it did not. Liberty phrased the question at hand as, "whether in the absence of structural separation, Qwest's 271 approval would meet the public interest." The FCC has answered this question by not once requiring structural separation as a prerequisite for a 271 approval.

The Board agrees with Liberty's conclusion that the public interest can be met without a structural separation of Qwest's retail and wholesale operations.

7. Sustained Checklist Compliance

ASCENT argued that there are only speculative assurances that markets will remain open after Qwest receives 271 approval. Therefore, until a record of sustained compliance has been demonstrated, it cannot be found that the public interest, nor compliance with the competitive checklist, has been met.

Liberty ruled that there is no FCC precedent for setting a minimum period of time during which the BOC must demonstrate checklist compliance before being granted 271 approval. Liberty noted that ASCENT's concerns would best be addressed through a sound performance assurance plan.

ASCENT did not file post-report comments on this issue, therefore, the issue should be considered closed.

The Board will adopt Liberty's resolution and consider this issue closed.

8. Inducing Competition

Qwest argued that local competition could increase once it receives 271 approval. This is what happened in New York after Verizon received 271 approval. The following year CLEC access lines increased by 130 percent. Qwest maintained that once BOCs enter the long distance market, other IXCs, facing the prospect of lower long distance revenues, will accelerate their local entry plans in a bid to retain customers through bundled service offerings.

The OCA argued that New York is not Iowa, and Qwest made no effort to test this theory in any other state where 271 authority was granted. Allowing Qwest to enter the interLATA market before sustainable entry has occurred will raise, rather than lower, entry barriers. In order to overcome entry barriers, CLECs should be able to offer something Qwest cannot. Currently, only CLECs may offer bundled local and long distance services. The power of this bundle gives CLECs the means to establish a sustainable foothold in the local exchange market. Allowing Qwest to bundle local and long distance would eliminate this CLEC advantage, and it is not in the public interest.

Liberty noted that Qwest cannot be precluded from bundling just because bundling might deter CLEC local market entry. The Act itself anticipates bundling when applicable conditions are met. Liberty pointed out that the role of those participating in implementing the Act is to decide whether those conditions have been met. Any arguments about the merits of the Act itself are irrelevant to this proceeding.

The Board notes that OCA did not file post-report comments specifically addressing this issue. The Board agrees with Liberty's comments and considers the issue closed.

9. Advanced Services Resale

ASCENT asserted that Qwest had failed to make a showing that that it provides advanced services on a resale basis as affirmed by a January 2001, United States Court of Appeals (D.C. Circuit) decision – also know as the ASCENT Decision.[47]

The Board does not consider this to be a public interest issue. It is a Checklist Item 14, resale issue. ASCENT made the same claims in a November 7, 2001, Letter in Lieu of Exceptions, to the Board's October 12, 2001, Conditional Statement Regarding May 15, 2001, Report (statement). That statement addressed resale issues among others. The Board will address ASCENT's claim in a supplemental statement to the October 12, 2001, Conditional Statement Regarding May 15, 2001, Report.

This is not an issue for the Public Interest Inquiry.

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[47] *Ass'n of Communications Enterprises v. FCC*, 235 F3d 662 (D.C.Cir. 2001) *aff'd* – F3d –-, No. 00-1144 (D.C.Cir. June 26, 2001).

10. OSS Testing

ASCENT argued that since the ROC OSS testing procedures have not been completed, and final test and audit results have not been released, it is premature conclude that Qwest has met the public interest standard.

Liberty recognized that the results of the OSS test are to be released in the future. OSS testing is a component of the overall competitive checklist. The purpose of this Inquiry is to explore considerations, beyond the competitive checklist, that may indicate 271 approval is not in the public interest.

The Board does not find OSS testing to be an issue for the Public Interest Inquiry. The Board will consider OSS testing in a separate review.

11. Change Management

Sprint stated that there are unresolved issues surrounding Qwest's Change Management processes (CMP), arguing that a public interest finding in favor of Qwest cannot be made until these issues have been resolved.

Liberty pointed out that it addressed Change Management in its previous report.[48] The Board notes that Change Management is an issue relating to General Terms and Conditions, which relates to a broad range of checklist items. Therefore, it is not an issue for the Public Interest Inquiry. The Board will address Change Management in a separate statement with other General Terms and Conditions issues.

[48] General Terms and Conditions, Section 272, & Track A Report, issued September 24, 2001, p. 41.

SUMMARY

Assuming Qwest incorporates each of the recommendations as set forth above, verbatim, the Board is prepared to indicate at this time its conclusion that Qwest has conditionally satisfied the Track A issues discussed in the September 24, 2001, report and the public interest issues addressed in the October 22, 2001, report from Liberty Consulting Group. This conditional statement indicating these requirements are satisfied is subject to the same limitations noted earlier in this statement related to other proceedings and processes.

UTILITIES BOARD

/s/ Diane Munns

/s/ Mark O. Lambert

ATTEST:

/s/ Judi K. Cooper
Executive Secretary

Dated at Des Moines, Iowa, this 25th day of January, 2002.