

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In re Application of U S WEST, INC. and
QWEST COMMUNICATIONS
INTERNATIONAL INC.

Docket No. UT-991358

For an Order Disclaiming Jurisdiction, or in
the Alternative, Approving the U S WEST,

DIRECT TESTIMONY OF

TERRY MOYA

Senior Vice President of External Affairs

COVAD COMMUNICATIONS COMPANY

February 1, 2000

I.

WITNESS QUALIFICATIONS.

Q. PLEASE STATE YOUR NAME, POSITION, AND EMPLOYER FOR THE RECORD.

A. My name is Terry Moya. I am Senior Vice President of ILEC Relations and External Affairs of Covad Communications Company ("Covad").

Q. WHAT KIND OF COMPANY IS COVAD?

A. Covad is a facilities-based competitive local exchange carrier ("CLEC") focused on providing wholesale, high-speed broadband services using digital subscriber line ("DSL") technologies. Covad has been offering services in Washington since December of 1998.

Q. WHAT IS COVAD'S RELATIONSHIP WITH U S WEST IN WASHINGTON?

A. U S WEST is both Covad's number one vendor and number one competitor in Washington.¹ Covad must collocate its equipment in U S WEST central offices and lease unbundled network elements ("UNEs") from U S WEST to provide Covad's service. U S WEST is required by the Telecommunications Act of 1996 (the "Act") to open its network to Covad, and Covad's ability to offer services in areas where U S WEST is the incumbent local exchange carrier ("ILEC") depends entirely on U S WEST complying with the Act. Covad pays U S WEST for both the collocation and the UNEs. Covad's service, however, competes directly with U S WEST's MegaBit service, which is also a

¹ While I recognize that there may be a legal distinction between U S WEST, Inc. – the parent company – and U S WEST Communications, Inc. – the operating company in Washington – there is no real-world distinction between the two companies and I treat them here as the same entity.

DSL service. While U S WEST is required by law to open its network, therefore, it is not happy that it must do so.

Q. PLEASE DESCRIBE YOUR RESPONSIBILITIES ON BEHALF OF COVAD.

A. As you can imagine, the tension created by U S WEST being both Covad's primary vendor and primary competitor makes the vendor-customer relationship a rocky one. U S WEST does not really want to provide Covad the open network access that is required by law. My job is to manage Covad's business relationship with U S WEST (and other ILECs) to make sure that U S WEST is providing us with the open network access and UNEs that the law requires. Because of the importance of this relationship to our business, I report directly to Covad's CEO, Robert Knowling.

Q. PLEASE DESCRIBE BRIEFLY YOUR EDUCATION AND WORK BACKGROUND.

A. Before coming to Covad, I worked as the Vice President Operations & Technologies for U S WEST. In that position, I had primary responsibility for financing U S WEST's network build out. I worked for U S WEST for a total of seven years, holding a number of different positions including leading the outside plant construction contracting organization. For the first four and a half years I spent time in over a half dozen foreign countries helping establish and improving several different lines of business for U S WEST. These countries include Poland, Russia, Czech Republic, Hungary, Brazil and the United Kingdom. I graduated from the University of New Orleans in 1986 with a BS

degree in Accounting.

Q. PLEASE DESCRIBE HOW COVAD'S SERVICE WORKS, INCLUDING HOW COVAD INTERCONNECTS WITH U S WEST.

A. Covad is a facilities based provider. That means we collocate our DSL equipment – primarily digital subscriber line access multiplexers (“DSLAMs”) – in U S WEST’s central offices. Covad leases unbundled copper loops from U S WEST to reach the customer and then connects those loops to our DSLAMs. Covad then connects every DSLAM to regional hub equipment (usually also collocated in a central office) by high capacity circuits – or unbundled transport – that Covad also leases from U S WEST.

Covad’s DSLAMs allow it to transit data streams across copper telephone wires at speeds of up to 1.5 megabits per second. Compare this to a standard computer modem, which operates at 56 kilobits per second. Several network factors can affect our ability to transmit data at these speeds, including the length of the local loop. In addition, Covad cannot provision ADSL or SDSL, the two most popular “flavors” of DSL, across loops that have a digital line carrier (“DLC”) component. DLC is a technology that typically uses fiber to carry telephone signals from the central office to a remote terminal located in the outside plant. From the remote terminal (or “RT”), the telephone signals are separated and transmitted across copper wires to the customer’s home.

Covad can provision IDSL over loops with a DLC component. IDSL, however, is a much slower (144 kilobits per second) and more expensive flavor of DSL. Covad could also provision ADSL or SDSL across loops with a DLC component if it could place its DSLAM in the remote terminals. In fact, placing equipment in a remote terminal allows a carrier to provide VDSL (very high bit rate DSL), an ultra-high speed DSL service that is capable of supporting multiple video transmissions. I will discuss this issue in more detail later in my testimony.

II. PURPOSE OF TESTIMONY, COVAD'S INTEREST.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. I intend to show that the merger proposed by U S WEST and Qwest Communications International Inc. ("Qwest") (collectively "Applicants") is not in the public interest. The proposed merger will decrease existing telecommunications competition in Washington and, therefore, have a negative effect on the residents of Washington. Accordingly, I will recommend that Commission should either not approve the merger or, at a minimum, impose a set of conditions that will help ameliorate the competitive harm the merger will cause.

Q. BRIEFLY, WHAT IS COVAD'S INTEREST IN THE MERGER?

A. Covad has existing relationships with both U S WEST and Qwest. The merger will directly and adversely affect those relationships, resulting in less actual competition for

advanced telecommunications services in Washington and less incentive for U S WEST to open up its network to those competitors that remain. The merger, therefore, will damage Covad and other telecommunications competitors. By doing so, the merger will also damage Washington consumers.

Q. WHAT IS COVAD'S RELATIONSHIP WITH QWEST?

A. Qwest has an agreement to re-sell Covad DSL in many states, including Washington. In addition, Covad uses Qwest's frame relay network, which carries data across interLATA boundaries, to help manage Covad's DSL network in Washington.

Q. HOW WILL THE MERGER AFFECT THAT RELATIONSHIP?

A. Because Covad is a DSL wholesaler, it relies on its resellers to compete with U S WEST. Covad entered into its resale agreement with Qwest in reliance on Qwest's strong national presence and marketing skills to help Covad's DSL compete with ILEC DSL products, including U S WEST's MegaBit. If Qwest and U S WEST merge, then one of Covad's major DSL distribution channels will likely disappear in Washington as the merged entity obviously will sell MegaBit – not Covad DSL. There is also a danger that the merged entity will use Qwest's knowledge of Covad's network and customers to market directly to Qwest's Covad DSL customers. Finally, the merged entity will not be able to transport data across interLATA boundaries, Covad will therefore lose the use of Qwest's frame relay network in Washington. Covad will have to find a new system for managing its network, and the resulting delay and expense will hurt Covad.

Q. HOW WILL THE PROPOSED MERGER HARM COMPETITION IN WASHINGTON?

A. At least three ways that directly relate to Covad. First, the elimination of Qwest as a competitive reseller of Covad DSL will result in fewer DSL choices for Washington consumers. It will also result in less competitive choice for advanced services generally because Qwest will no longer be offering those services in competition with U S WEST. Second, the elimination of Qwest as a CLEC will result in fewer companies keeping vigilance over U S WEST's interconnection practices and compliance with Section 251 of the Act. Third, once U S WEST absorbs Qwest's assets, there will be fewer competitive providers of network facilities such as fiber transport. Reduced competition results in higher prices to companies like Covad – and those higher prices ultimately will be passed on to the consumer.

Q. ARE THERE ANY OTHER POTENTIAL HARMS RESULTING FROM THE MERGER?

A. Yes. The Applicants have announced plans to roll-out DSL and other advanced services nationwide as part of their merger. That effort is going to require funding, and raises important questions about how the merged entity will allocate resources. U S WEST has a well documented history of failing to fund network infrastructure so that it can divert money to its more lucrative advanced services, big business products.

Covad, and companies like it, depend on the availability of U S WEST's basic telephone network to provide services. One way to prevent companies like Covad from competing

with U S WEST, therefore, is to deny them facilities. The network here in Washington is already one of the poorest in the country, resulting in many held orders for Covad and other CLECs. Given U S WEST's history, there is a very real danger that the merged entity will divert money that could and should be used to increase the telecommunications infrastructure in Washington to fund the merged company's advanced services efforts in larger markets like New York, Chicago and Los Angeles. Therefore, by intentionally reducing the amount of available facilities to lease to competitors, U S WEST will be able to continue and strengthen its telecommunications monopoly in Washington.

Q. HOW WOULD A NEGATIVE IMPACT ON THE WHOLESALE MARKET BE RELEVANT TO THE PUBLIC INTEREST?

A. Very few consumers in Washington are currently being served by facilities not owned by U S WEST. For now and a long time to come most consumers will have no competitive alternative to U S WEST unless CLECs can obtain necessary facilities from the bottleneck supplier, U S WEST. Indeed, consumers may not even be able to obtain needed services from U S WEST's retail side if investment in bottleneck local facilities declines as a result of the merger. On the retail side, the merger is eliminating Qwest not only as an actual competitor, but also as a potential competitor. Elimination of competition is not in the public interest given that state and federal policy both seek to promote competition.

III. THE BREADTH OF U S WEST'S LOCAL SERVICE MONOPOLY IN THE STATE OF WASHINGTON AND THE RELATIVELY SLOW PACE OF DEVELOPMENT OF COMPETITION REQUIRES STRINGENT REVIEW OF THE MERGER TO PROTECT THE PUBLIC INTEREST.

Q. WHAT IS THE STATE OF TELECOMMUNICATIONS COMPETITION IN WASHINGTON?

A. U S WEST is the ILEC in most of the largest metropolitan areas of the state, including the I-5 corridor from Bellingham to Vancouver (except for the Everett/Marysville area); most of the Olympic Peninsula; Southeast King County including Bellevue, Renton, and Kent; and much of Eastern Washington, including Yakima, Pasco, and Spokane. Publicly available facts, however, make it clear that the development of a fully open and competitive market is far from being a reality in U S WEST's local service territories, including the state of Washington. The merger would be another step backward from that goal.

Several FCC reports indicate that U S WEST retains near-total control over the access lines in its service territories. Additionally, the extent of entry in U S WEST's states shows that the U S WEST region lags far behind entry into other RBOC regions. Table 1, below, compares the number of total service resale lines with switched lines of the five RBOCs.

Table 1. Lines Provided As Total Service Resale (TSR)

	TOTAL SWITCHED LINES (thousands)	TSR Lines (thousands)	PERCENT
Ameritech	21,054	450	2.1
Bell Atlantic	41,429	619	1.5
BellSouth	24,104	543	2.3
SBC	36,778	823	2.2
U S WEST	16,695	149	0.9

As of December 31, 1998 (latest data available)

Source: Industry Analysis Division, Common Carrier Bureau, FCC, *Local Competition: 1999*, Table 3.2 (Rev.)

As Table 1 shows, only nine tenths of one percent of the access lines in U S WEST's territory are resold lines. This percentage is less than all other RBOCs and is less than half the percentage of three of the other four RBOCs. Looking at Washington-specific data, the percentage is even less, just two tenths of a percent. *Id.*, Table 9.2.

Competitive entry in U S WEST's region looks even worse based on UNE resale. Table 2 compares the number of total UNE lines with switched lines of the five RBOCs.

Table 2. Lines Provided as UNEs

	TOTAL SWITCHED LINES (thousands)	UNE Lines (thousands)	PERCENT
Ameritech	21,054	100	.5
Bell Atlantic	41,429	91	.2
BellSouth	24,104	41	.2
SBC	36,778	67	.2
U S WEST	16,695	8	.00479

*As of December 31, 1998 (latest data available)

Source: Industry Analysis Division, Common Carrier Bureau, FCC, *Local Competition: 1999*, Table 3.3 (Rev.)

U S WEST is again far behind the rest of the pack, with less than five thousandths of a

percent of the lines in its territory being provisioned by UNE resale.² The RBOCs with the next worst record have over 40 times the percent of UNE lines in their territories that U S WEST has in its territory.

Q. WHAT DOES THIS DATA TELL US?

A. Competitive entry in U S WEST's region lags far behind that in other RBOCs' regions.

This indicates that there are greater barriers to entry in U S WEST's region than exist in other regions. A merger that has even a slight anticompetitive impact on a market that has greater entry barriers than other markets should not be approved unless the barriers are eliminated to the fullest extent possible before the merger is consummated.

The Commission may infer from the data in Tables 1 and 2 that U S WEST retains a monopoly in its service territories in Washington. The Commission should closely examine why development of competition in U S WEST's states lags so far behind other ILECs regions. Furthermore, because there is so little local competition to U S WEST the Commission should act aggressively to ensure that the merger carries **no** risk of reducing competition or allowing the combined entity to continue to maintain barriers to entry.

Q. DO YOU HAVE ANY REASON TO BELIEVE THAT THE MERGER WOULD REDUCE COMPETITION OR PERMIT THE MERGED COMPANY TO MAINTAIN BARRIERS TO ENTRY?

A. Yes, as to both. U S WEST's merger with an *actual* competitive entrant in these

² A precise figure for Washington is not available, but is substantially less than other RBOCs' territories. *See id.*, Table 9.4.

markets—Qwest—would have a clear impact upon competition. The loss of a significant, actual (or precluded) entrant of Qwest's stature and resources—in particular, an extensive sales force that would have been deployed to sell competitive xDSL service (Covad's) that now presumably will be selling ILEC xDSL service—is likely to have a significant adverse impact on the development of competition in the market for high-speed data services. Moreover, Covad's experience in entering seven geographic regions in U S WEST's territory (Washington, Oregon, Minnesota, Colorado, Arizona, Utah and New Mexico) demonstrates that while progress has been made on several fronts (particularly, in recent months, collocation), the keys to the development of broadband xDSL entry are far from in place. These anticompetitive impacts can only be remedied through aggressive and immediate market-opening steps.

IV. SUBSTANTIAL BARRIERS TO ENTRY REMAIN IN U S WEST'S TERRITORIES THAT SHOULD BE ADDRESSED AND CORRECTED IF THE MERGER IS TO BE APPROVED.

Q. WHY SHOULD THE COMMISSION LOOK AT BARRIERS TO COMPETITIVE ENTRY THAT MAY EXIST IN U S WEST'S TERRITORY IN WASHINGTON IF THE APPLICANTS HAVE COMMITTED TO FOLLOW THE LAW ON INTERCONNECTION, ACCESS TO UNEs, AND COLLOCATION AFTER THE MERGER?

- A. Eliminating a competitor in a market (which the merger clearly will) where entry is **difficult** has a much more serious anticompetitive effect than eliminating a competitor in a market where entry is relatively easy. A certain reduction of competition in a market that is vigorously competitive with low entry barriers may be acceptable. The same

absolute level of reduction in competition would be unacceptable in a market that is dominated by a monopolist, especially if the monopolist is able to (and does) maintain barriers to competitive entry.

Q. WHAT ARE THE ENTRY BARRIERS IN WASHINGTON THAT CONCERN COVAD THE MOST?

A. Three key barriers to entry exist: the collocation process, access to critical UNEs (including loops, line sharing, remote terminals, sub-loops, and OSS), and actual on-time loop provisioning performance. An examination of the facts reveals that U S WEST has not removed all of these barriers to entry. Indeed, entry into this market is difficult. Therefore, the elimination of an actual competitor (Qwest) is likely to have significant adverse competitive effects in this market.

Q. HOW IS COLLOCATION A BARRIER TO ENTRY?

A. Collocation of equipment in central offices is expensive and time consuming. Without collocation, however, a CLEC cannot provide service. Even if U S WEST performed at its very best, this barrier would be difficult or impossible to remove completely. That said, the Commission can lessen this barrier by requiring U S WEST to provide collocation in a timely fashion within intervals that allow a CLEC to build or add to its network as quickly as reasonably possible.

WHAT ABOUT ACCESS TO CRITICAL UNES?

- A. This barrier encompasses a lot. U S WEST's inability to deliver even basic UNE loops, for example, is a significant access barrier. In addition, U S WEST has refused until only very recently to share its existing voice lines with Covad, an issue I will address later in my testimony.

In addition, U S WEST currently does not provide CLECs with access to remote terminals and/or sub-loop elements. Earlier in my testimony I described remote terminals and their place in the network. Sub-loop elements include both the fiber serving the remote terminal and the copper extending from the remote terminal to the customer. Generally, a sub-loop element is any part of the transmission path between the central office or a terminal or feeder distribution interface and the next terminal or feeder distribution interface. Access to remote terminals and sub-loop elements is absolutely critical to ensuring that next-generation DSL technology over fiber-fed loops (such as VDSL) be available to consumers on a competitive basis. Remote terminal access has immediate competitive significance, because U S WEST has already begun to trial and deploy VDSL technology at fiber-fed remote terminals in Arizona.

Covad approached U S WEST many times before the FCC released its UNE remand

order³ to ask U S WEST to work with Covad to develop sub-loop unbundling and remote terminal access in a way that benefited both U S WEST and Covad. U S WEST refused even to discuss the subject. To date, U S WEST still has not proposed a plan for sub-loop unbundling that meets the requirements of the UNE remand order, and it appears that U S WEST will not work cooperatively with the CLECs to provide any more services than those that a strictly construed reading of the order requires.

Q. WHAT IS U S WEST'S RECORD ON LOOP DELIVERIES?

A. Perhaps the largest operational barrier Covad currently faces in its dealing with U S WEST today is ensuring that Covad's loop orders be completed on a nondiscriminatory and timely basis. No issue is more critical to a new company like Covad than customer service—which, in Covad's business, begins with the timely installation of a customer's xDSL line. U S WEST is Covad's only supplier of unbundled loops in U S WEST's region, and its performance on this key metric is the worst of any ILEC. Unfortunately, U S WEST's performance in Washington is worse than in any other state, meaning that Washington's residents are getting some of the worst telecommunications delivery in the country.

³ *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-98, Third Report and Order and Fourth Further Notice of Proposed Rulemaking, FCC 99-238 (rel. Nov. 5, 1999)("UNE Remand Order")

The main reason for the delays are what U S WEST refers to as "held orders." A "held order" is one which U S WEST removes from the normal provisioning cycle for one of any number of reasons. When an order goes "held," U S WEST refuses to tell Covad when the order might be filled. In other words, there is no interval within which U S WEST must resolve the problem that led to the order becoming held. U S WEST has held some Covad orders for 90 days or more before completing them.

As of January 3, 2000, 50.9% of Covad's UNE loop orders were in held order status in Washington. On a region-wide basis, 24% of Covad's orders are held for "local market" availability. In short, this means U S WEST does not have a facility available to the customer and is not planning on adding any facilities that will serve the customer within the next six months. In other words, U S WEST is telling Covad "you can't get a loop, so don't even try" in response to 24% of Covad's orders.

And U S WEST's performance is getting worse, not better. Between September 13, 1999 and January 3, 2000, the percentage of "local market" orders increased from 14% to 24% of Covad's total orders. U S WEST delivered a loop on time only 66% of the time in August 1999 and only 60% of the time in January 2000. On average, the commitment date we give our customers has to be changed 50% of the time because of U S WEST. In

fact, between August, 1999 and January, 2000, U S WEST's average interval for delivering a loop to Covad increased from 15 to 17 business days. (Because of limitations in Covad's ability to measure this data, this interval information is actually somewhat inaccurate in favor of U S WEST. Covad is updating its systems to capture actual loop delivery better and believes that the correctly measured interval will be something well over 20 business days on average.) U S WEST, in contrast, recently told the Minnesota Public Service Commission that it provides its retail MegaBit DSL customers service within 10 business days.⁴ Finally, Covad is finding an increasing number of problems with U S WEST's loops even after U S WEST has purportedly delivered them. The percentage of U S WEST delivered loops that required Covad to open a trouble ticket (an indication that the loop does not work) within seven days of delivery increased from 4% in August to 12% in December, 1999. During that same time period, the percentage of loops requiring Covad to open a trouble ticket within 30 days of delivery increased from 7% to 17%.

Q. WHAT CAN THE COMMISSION DO TO HELP LESSEN THESE BARRIERS TO COMPETITIVE ENTRY?

A. As I will discuss in more detail later in my testimony, there are several conditions the Commission could impose on the merger to help ameliorate these barriers to competitive

⁴ See U S WEST response to Minnesota Department of Commerce Data Request 10 in Minnesota Public Utilities Commission Docket No. P-999/CI-99-678 (Exhibit A).

entry if the Commission is inclined to grant the merger application at all. These conditions include: (1) order U S WEST to structurally separate its wholesale and retail operations; (2) require U S WEST to meet certain minimum performance standards or be subjected to fines; (3) require U S WEST to invest in the Washington outside plant so that facilities are available for CLEC and U S WEST's own use; and (4) require U S WEST to comply with the UNE remand order and make operational systems improvements that will increase its ability to meet wholesale demand. Attached to my testimony as Exhibit B is a full list of proposed conditions, including those discussed above, supported by Covad.

Q. WHY SHOULD THE COMMISSION CONSIDER THESE CONDITIONS HERE INSTEAD OF IN OTHER DOCKETS?

A. The key here, as I discussed earlier, is that the proposed merger will reduce competition in Washington, reduce the number of carriers pushing U S WEST to increase performance, and directly harm the ability of Covad and other CLECs to compete with U S WEST. The conditions that Covad proposes will address those harms by focusing on competitive issues.

Q. IS IT POSSIBLE THAT MERGED COMPANIES WOULD BE MORE INCLINED TO REDUCE ENTRY BARRIERS WITHOUT COMMISSION INTERVENTION?

A. Anything is possible, but I find it very unlikely. By far the greatest portion of the merged entity's revenues and profits will initially, and for the foreseeable future, be derived from

the local bottleneck monopoly. After the merger, the combined entity will continue to have the same economic motivations to protect its monopoly markets as U S WEST does today. That motivation is quite strong, and recent anticompetitive statements by U S WEST's senior executives belie the Applicants' claims that Section 271 incentives will drive them to open up the network.

According to a recent CNET News.com article, for example, Joe Zell, the President of U S WEST's !NTERPRISE division (which is responsible for U S WEST's advanced services products including MegaBit) stated that U S WEST "doesn't have to sell access to [fiber served] lines to competitors like Covad Communications, Rhythms NetConnections or other telephone companies, as it does with all of its other telephone services." The President of !NTERPRISE, went on to characterize this limitation as "a very positive thing." (See "US West looks to offer video over phone lines" (November 16, 1999) (<http://home.cnet.com/category/0-1004-200-1451286.html>)).

While Covad believes that Mr. Zell is legally wrong, the disturbing thing about this quote is that it indicates how hard U S WEST's senior executives are working to think of ways to close – not open – U S WEST's network. The Applicants have stated repeatedly that they intend to focus on DSL and other advanced services after the merger. Assuming Mr. Zell remains in charge of !NTERPRISE, the combined entity seems most likely to

maintain or even raise the existing barriers to competitive entry.

Q. BESIDES THE NEGATIVE IMPACT OF LOSING QWEST AS A RETAIL COMPETITOR TO U S WEST'S "MEGABIT" DSL SERVICE, IS THERE ANY OTHER REASON THE MERGER WOULD HINDER THE DEPLOYMENT OF DSL SERVICES?

A. Yes. As is discussed above, the biggest problem Covad faces in deploying its DSL services is the lack of loop facilities. The existence of competitors, or strong potential competitors, would give U S WEST an incentive to invest more into its loop plant, particularly now that the FCC has ordered sub-loop unbundling. The merger would eliminate one of U S WEST's strongest facilities-based competitors and therefore reduces U S WEST's incentives to invest in its already woefully inadequate loop facilities.

V. IN ORDER TO PREVENT THE PROBABLE AND POTENTIAL ANTICOMPETITIVE IMPACTS OF THE MERGER AND PROTECT THE PUBLIC INTEREST, THE COMMISSION SHOULD EITHER DENY THE MERGER OR IMPOSE APPROPRIATE CONDITIONS ON THE MERGER.

Q. WHAT OPTIONS SHOULD THE COMMISSION CONSIDER WITH REGARD TO THE APPLICATION?

A. The Commission should deny the merger application because of the direct competitive harm that the merger will cause in Washington. To put it simply, the merger is not in the public interest.

If, however, the Commission is inclined to grant the application it should do so only subject to the conditions proposed by Covad, Public Counsel, Commission staff and other CLECs to lessen the harm the merger will cause. Again, the list of conditions proposed

by Covad and other CLECs is attached to my testimony as Exhibit B. While we believe that all of these conditions are required to address the potential harm caused by the merger, I will briefly explain in the remainder of my testimony the conditions that are, in Covad's view, the most important.

Q. IN YOUR VIEW, WHAT ARE THE MOST IMPORTANT OF THE PROPOSED CONDITIONS?

A. From Covad's perspective, the most important conditions are the ones I proposed earlier in my testimony. More specifically, we believe that the Commission should (1) order U S WEST to structurally separate its wholesale and retail operations; (2) require U S WEST to meet certain minimum performance standards or be subjected to fines; (3) require U S WEST to invest in the Washington outside plant so that facilities are available for CLEC and U S WEST's own use; and (4) require U S WEST to comply with the UNE remand order and make operational systems improvements that will increase its ability to meet wholesale demand.

Q. WHAT KIND OF STRUCTURAL SEPARATION DOES COVAD PROPOSE?

A. Covad proposes that the Commission order complete separation of U S WEST's wholesale and retail operations. More precise details and requirements are spelled out in Exhibit B to my testimony.

Q. WHY IS STRUCTURAL SEPARATION REQUIRED, AND HOW DOES THAT RELATE TO THIS MERGER?

A. Structural separation is the only way to insure a completely level playing field in the

telecommunications services market. The idea is that a wholesale provider of network facilities will be incented to maintain the network at optimum capacity and condition to maximize potential profits generated by leasing network elements to multiple retail service providers. Structural separation therefore eliminates the incentive for the merged entity to divert money from infrastructure investment to out-of-region advanced services deployment. Structural separation will also mean that the merged entity's retail arm must deal with the wholesale arm in public, arms-length transactions that require the retail arm to stand in the same shoes as its CLEC competitors. Only under those circumstances can we be sure that parity exists.

In addition to the incentive issue I just raised, structural separation relates to the merger because it is the fastest, easiest way to address the competitive harm caused by the merger over the long term. If the Commission implements complete structural separation, properly done with all loopholes closed, then there should be less long-term need for the additional conditions Covad proposes.

Q. IS THERE ANYTHING LESS THAN A COMPLETE WHOLESALE/RETAIL SPLIT THAT MIGHT HELP ADDRESS THESE ISSUES?

A. Yes. SBC and Ameritech agreed to create a separate advanced services affiliate as part of their merger. Bell Atlantic recently agreed to something similar in New York as part of its effort to get Section 271 approval. These were important, if not complete, steps toward leveling the telecommunications playing field because they addressed the fastest

growing segment of the telecommunications market. The industry hope is that the creation of these separate advanced services affiliates will help open the nascent digital market to more competition before the ILECs completely leverage their existing network control to crush what little competition exists for advanced services.

Covad supports the separate data or advanced services affiliate idea but is concerned that the plans adopted by SBC and proposed by Bell Atlantic do not go far enough to ensure that the separate affiliates do not remain special beneficiaries of their too-close relationships with the ILEC. Accordingly, if the Commission is inclined to consider the separate affiliate idea, we suggest that the Applicants be required to create the affiliate under the same conditions (i.e. separate offices and officers, etc.) that we have proposed for a complete wholesale/retail split.

Q. IS THERE ANY EVIDENCE THAT STRUCTURAL SEPARATION OR THE CREATION OF A SEPARATE ADVANCED SERVICES AFFILIATE WILL HELP FOSTER COMPETITION?

- A. Yes. In announcing its commitment to a separate data affiliate, Bell Atlantic argued that "provision by Bell Atlantic of xDSL services through a separate affiliate would ensure that services and facilities are provided to competing xDSL providers on a nondiscriminatory basis." Thomas J. Tauke letter to the Honorable William E. Kennard, Chairman, Federal Communications Commission (December 10, 1999). When the FCC conditioned its approval of the SBC/Ameritech merger on the establishment of a separate

affiliate for data services, it did so to "ensure a level playing field between SBC/Ameritech and its advanced services competitors." Memorandum Opinion and Order In re Applications of Ameritech Corp. And SBC Communications Inc., CC Docket No. 98-141 (FCC October 6, 1999) ¶363. Further, the FCC noted that establishing a separate affiliate for advanced services "will provide a structural mechanism to ensure that competing providers of advanced services will receive effective, nondiscriminatory access to the facilities and services. . . that are necessary to provide advanced services." Id.

Q. CAN YOU GIVE SPECIFIC EXAMPLES FROM COVAD'S EXPERIENCE THAT DEMONSTRATE HOW THE CREATION OF A SEPARATE SUBSIDIARY MIGHT HELP LESSEN THE COMPETITIVE HARM YOU SAY WILL BE CAUSED BY THE MERGER?

A. Yes. The creation of either a wholesale/retail dichotomy or a separate advanced services affiliate will help ensure that U S WEST is not able to extend its existing monopoly over bottleneck local facilities to these new services. Time and time again, U S WEST has used its control over those bottleneck local facilities to try to give itself an advantage in competing with Covad and other CLECs.

Washington, for example, was one of the first states that Covad came to try to enter and provide DSL services. It took Covad the full nine months under the Act to obtain an acceptable interconnection agreement with U S WEST. One of the things that Covad had to fight hard for was cageless collocation, which was necessary to obtain collocation for

its DSLAMs at reasonable costs. While Covad was fighting with U S WEST for access to UNEs and cageless collocation on reasonable terms and conditions, U S WEST was developing its own DSL service, MegaBit. U S WEST's retail side did not have to go through any of the negotiation and arbitration proceedings as U S WEST. Moreover, at the outset U S WEST provided its Megabit service with the type of cageless collocation that Covad had to fight for for over the course of more than a year.

While U S WEST was within its rights under the Telecommunications Act to negotiate and arbitrate with Covad for nine months, the fact is that U S WEST was able to gain a competitive advantage for its own retail MegaBit DSL service. The nine month delay, coupled with Covad's need to build out its network after it reached agreement with U S WEST, enabled U S WEST to beat Covad to market in Washington with DSL service.

Another example is DSL line sharing. ADSL, one of the more popular flavor of DSL, can be provisioned over the same loop as existing voice service so that the customer can use one telephone line to transmit data and make voice calls at the same time.

U S WEST's retail DSL service has always been provided with line sharing – meaning that U S WEST has always provided voice and DSL services on the same loop.

U S WEST capitalized on this fact by advertising its ability to provide DSL over existing phone lines as a means of differentiating its products from Covad's. U S WEST also

relied on its use of line sharing to set its MegaBit pricing at levels intended to drive Covad and other DSL CLECs out of the market.

When Covad first approached U S WEST about line sharing with it, U S WEST rejected Covad's requests. Recently – as a result of Covad's legal and business efforts – U S WEST's attitude has changed, and Covad is currently negotiating an agreement with U S WEST to bring line sharing to Washington sometime later this year. U S WEST capitalized on the delay in providing Covad access to this network element, however, to strengthen its hold on Washington consumers.

If a separate subsidiary had been in place in either or both of these cases, then U S WEST would have been required as a matter of law to provide Covad with the same cageless collocation and line sharing that it was already providing to itself. From a business standpoint, the wholesale subsidiary would have provided cageless collocation and line sharing to Covad more quickly to maximize use of its network. Under those circumstances, neither issue would have delayed Covad's deployment.

Q. NOW THAT COVAD HAS CAGELESS COLLOCATION AND WILL HAVE ACCESS TO LINE SHARING IN THE FORESEEABLE FUTURE, IS THERE STILL A NEED TO REQUIRE A SEPARATE SUBSIDIARY?

A. Most definitely. As noted above, significant entry barriers still remain. Eventually Covad is likely to be able to obtain subloop unbundling and access to loops that are fed

by fiber. Once again, however, U S WEST, because its DSL service is integrated with its wholesale facilities provider, will be the first competitor to obtain access to DLC served loops. Indeed, if space is limited in remote terminals, U S WEST may be the only DSL provider that will be able to collocate its DSLAMs in those remote terminals. The regulatory environment will continue to evolve indefinitely and without a separate subsidiary requirement U S WEST is likely to always have access to more favorable terms and conditions before its competitors

Q. HOW WOULD A SEPARATE SUBSIDIARY AFFECT THIS PROBLEM?

A. A separate subsidiary would ensure that all DSL providers would have the same access to U S WEST's UNEs, collocation, and other services and facilities, under the same prices, terms, and conditions as U S WEST's retail advanced services subsidiary. Not only would a separate subsidiary ensure the same, nondiscriminatory access, it would ensure that all competitors would have access at the same time.

Q. WHY IS COVAD ALSO PROPOSING THAT THE COMMISSION MAKE PERFORMANCE MEASURES AND PENALTIES A CONDITION OF THE MERGER?

A. Again, the intent of Covad's proposals is to find ways to help lessen the competitive harm caused by the merger. One thing that would help is if U S WEST provisioned the most important UNEs in a timely fashion so that Covad and other CLECs can deliver service to its customers in something approximating the same time interval that U S WEST does. One important thing to remember is that U S WEST's retail intervals end when the

customer has service. On the wholesale side, Covad still has work to do to provision its services to its customer once it takes delivery of an unbundled loop. The question of U S WEST's performance on the wholesale side is therefore critical to Covad's ability to compete with U S WEST's retail side.

Q. WHAT PERFORMANCE MEASURES DOES COVAD PROPOSE?

A. The full detail is included on Exhibit B to my testimony. In general, Covad proposes UNE loop installation intervals of 3 business days when no conditioning is required, 7 business days when conditioning is required and 10 business days when U S WEST originally finds no facilities are available. Covad also proposes that U S WEST be required to return firm order confirmations ("FOCs") within 24 hours; provision DS1 and DS3 loops within 5 or 8 business days depending on the population density of the location for which the order is placed; and complete all collocation orders within 45 days. (Covad's interconnection agreement with U S WEST in Washington currently requires U S WEST to complete all cageless collocation orders in 45 days.)

Q. WHAT ABOUT FINES AND PENALTIES?

A. Covad endorses fines and penalties for non-performance as efficient tools for achieving two desired results. First, the fines and penalties will help prevent post-merger performance back-sliding and ensure that U S WEST complies with the conditions imposed by the Commission. Second, the existence of fines and penalties prevents U S WEST from deciding that it is less expensive to ignore the condition than it would be

to comply and face real competition. The fines and penalties, therefore, incent U S WEST to do whatever is necessary to comply with the network opening requirements of Section 251.

As one can see from Exhibit B, Covad proposes two kinds of fines and penalties. The first kind requires U S WEST to forfeit any non-recurring charges associated with a UNE when it does not provision the UNE on time. The basis for this fine is that the customer should not have to pay if U S WEST doesn't deliver. To make sure that the incentive to perform does not go away after U S WEST loses the nonrecurring charge, Covad proposes additional recurring charge reductions that vary depending on how long delivery of the final UNE takes.

The second kind of penalty is an aggregate penalty. The thought here is that U S WEST should pay substantially larger penalties if it fails to perform on a repeated basis over time. By imposing substantial fines and penalties for such repetitive behavior, the Commission can help guarantee that U S WEST does not simply write off the non-recurring charge penalties as a cost of helping to frustrate competition through lack of performance. If U S WEST knows it must perform or face penalties that could affect shareholder value, then U S WEST will do what it takes to perform.

Q. COVAD ALSO PROPOSES THAT U S WEST BE REQUIRED TO MAKE SPECIFIC INFRASTRUCTURE INVESTMENTS. CAN YOU PLEASE EXPLAIN COVAD'S PROPOSAL?

A. Covad's proposal, which the Commission can read at paragraph 2 of Exhibit B, is focused on requiring U S WEST to make infrastructure investments that benefit both its retail and wholesale customers. Some mechanism is needed to ensure that the merged entity will not neglect the investment that is needed in outside plant in Washington as a result of its desire to fund expansion into national markets.

Too often in proceedings like this, commissions will impose conditions that require ILECs to allocate funds for infrastructure investment without directing how those funds should be spent. When that happens, the ILEC is free to invest in business, advanced service, or other high-profit areas while it continues to ignore the outside plant infrastructure issues necessary to ensure that everyone receives quality telecommunications services and choice.

Covad's investment proposal mandates results without regard to costs. Covad's proposal would require U S WEST to maintain the outside plant so that a set percentage of loops are always available for retail and/or wholesale use. To do this, Covad focuses on the availability of transport facilities – meaning fiber or copper loops – at the feeder distribution interfaces (where the feeder cable meets the distribution cable) and the terminals (where the telephone cables end). Covad proposes that U S WEST be required

to maintain at least 15% unused capacity at each such point when averaged over a six month interval. By mandating results rather than dollar amounts, the Commission can encourage U S WEST to manage the plant efficiently while ensuring the availability of facilities for Washington consumers and CLEC competitors.

Q. WHAT OTHER CONDITIONS DOES COVAD PROPOSE?

A. Covad proposes two other conditions. First, Covad proposes that U S WEST be required to coordinate its planning and deployment of DLC systems to ensure that Covad and other CLECs have the opportunity to interconnect with those facilities. Given the Applicants' emphasis on deploying an advanced network, this provision is necessary to insure that competitors continue to have the ability to interconnect with that network. The Commission can find this proposed condition at paragraph 4 of Exhibit B.

Second, Covad proposes that U S WEST be required to make its network information databases – and in particular LFACs and TIRKS – available to all CLECs. LFACs and TIRKS are two databases that contain much of the network information regarding the outside plant and the central office. Access to this information is not only required by law, it is also needed by the CLECs for the planning and provisioning of competitive local exchange and advanced services. This condition, which the Commission can find at paragraph 3 of Exhibit B, will help CLECs create and manage the network necessary to compete with the merged entity.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes it does.

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