BEFORE THE WASHINGTON UTILITIES & TRANSPORTATION COMMISSION

In the Matter of the Petition of QWEST CORPORATION

To be Regulated Under An Alternative Form of Regulation Pursuant to RCW 80.36.135.

DOCKET NO. UT-061625

DIRECT TESTIMONY OF MARY M. KIMBALL (MMK-1TC)

ON BEHALF OF

PUBLIC COUNSEL

JANUARY 29, 2007

REDACTED VERSION

NON-CONFIDENTIAL

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I. INTRODUCTION / SUMMARY

Q. Please state your name, employer, and present position and role in the case?

A. My name is Mary M. Kimball and my business address is 800 Fifth Avenue, Suite 2000, Seattle, Washington, 98104. I am employed as a Regulatory Analyst with the Public Counsel Section of the Attorney General's Office.

Q. Please briefly outline your education and employment background.

A. I received a B.A. in Political Science from Williams College in Williamstown, Massachusetts in 1992. In 1997 I received a Masters in Public Policy from the University of California, Berkeley. Since joining the Public Counsel section in July 2000, I have worked on a wide range of issues in the telecommunications and energy sectors. I monitored Qwest's implementation of the US West-Qwest merger settlement agreement, which included numerous service quality and network investment provisions. I developed Public Counsel's recommendations regarding the mechanics and terms of Qwest's Performance Assurance Plan (QPAP) in the Company's Section 271 proceeding before this Commission. I also helped negotiate the settlement agreement between Public Counsel, Qwest, and other consumer groups in the sale of the company's Yellow Pages Directory business, which was approved and adopted by the Commission. With respect to energy-related issues, my work has included service quality, energy efficiency, decoupling mechanisms, power costs, and affiliate interest issues.

Q. Have you previously testified before this Commission?

A. Yes. I testified before the Commission in two service quality proceedings in the US West-Qwest merger settlement docket (UT-991358). The first proceeding concerned Qwest's petition for mitigation of service quality credits and modification of the Service Quality Performance Plan

(SQPP). The second proceeding concerned Qwest's petition for termination of the SQPP, or in the alternative, modification of the program. I also provided testimony in support of the service quality settlement in Puget Sound Energy's 2001 general rate case. Finally, I have testified before the Commission as part of settlement panels, including the recent proceeding considering the spin-off of Sprint-United's local telephone business, now known as Embarq.

Q. What is the focus of your testimony in this case?

A. My testimony focuses on service quality issues related to Qwest's proposed Alternative Form of Regulation (AFOR). I recommend that the Commission reject Qwest's request for a waiver of the Commission's service quality reporting requirements, and that the Commission direct the Company to modify its Customer Service Guarantee program reports to include information about out-of-service credits. In addition, I recommend the Commission condition the acceptance of any AFOR for Qwest on implementation of a service quality incentive program as an anti-backsliding mechanism, to help ensure that the Company's retail service quality does not experience any degradation as a result of the AFOR. I recommend a Service Quality Incentive Plan (SQIP) which places $16 million at risk annually in automatic, self-actuating credits to customers should retail service quality fall significantly below certain benchmarks. This program includes eight performance measures, and is an update to the Service Quality Performance Program (SQPP) instituted as part of the US West-Qwest merger settlement, approved and then later modified by the Commission in UT-991358. I also recommend that Qwest continue to offer its Customer Service Guarantee Programs, set forth in the Company's tariff WN U-40, Section 2.2.2B, for the duration of any AFOR.

Q. Why is it important to consider service quality in evaluating a potential AFOR?

A. The AFOR statute states that among the factors which the Commission shall consider in determining the appropriateness of any AFOR, is whether it will "Preserve or enhance service quality and protect against the degradation of the quality or availability of efficient telecommunications services."[1] The Commission has cited protecting against any degradation of service quality, as "one of the most important conditions for approving an AFOR."[2]

II. QWEST'S PROPOSAL WOULD NOT ENHANCE OR PROTECT SERVICE QUALITY

Q. Does Qwest's AFOR petition include any proposals related to service quality?

A. Yes. Qwest's AFOR petition includes a proposal that the Company would be granted a waiver from the Commission's service quality reporting requirements of WAC 480-120-439(1) for Class A companies. However, Qwest would continue to provide monthly service quality reports, comparable to those of other Class A telephone companies, during the four year "transition period" of the AFOR. This aspect of the Company's AFOR petition is discussed in the testimony of Mr. Mark Reynolds.[3]

Q. Do the Commission's service quality reporting requirements apply only to incumbent local exchange carriers, and not competitive carriers?

A. No. The Commission's service quality reporting requirements in WAC 480-120-439(1) apply to all Class A companies – local exchange carriers with more than 2% of the access lines in

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[1] RCW 80.36.135 (2)(d).
[2] *Washington Utilities and Transportation Commission v. US West Communications, Inc.*, Docket No. UT-950200, Fifteenth Supplemental Order, Commission Decision and Order Rejecting Tariff Revisions; Requiring Refiling, April 11, 1996, p. 11. (hereafter, "1995 Rate Case Order").
[3] Exhibit No. ___ (MSR-1T) at p. 9, ll. 14-21, and p. 12, l. 22 – p. 13, l. 3.

Washington. The Class A designation is made without respect to a company's classification as a competitive carrier under RCW 80.36.320.[4] Qwest seeks a waiver from these reporting requirements, partly on the grounds that they should have parity with competitors.[5] Actually, the requirements apply to all local exchange carriers with more than 2% of access lines, including competitive carriers. The testimony of Dr. Loube on behalf of Public Counsel discusses the extent of competition faced by Qwest, including intramodal competition, and concludes that Qwest remains the dominant telecommunications provider in Washington.

Q. Do you believe Qwest's proposal related to service quality would help "preserve or enhance service quality and protect against the degradation of the quality or availability of efficient telecommunications services," as the AFOR statute directs?

A. No, absolutely not. It does nothing to preserve or enhance service quality. It defies common sense to say that impeding the ability of the Commission and other stakeholders to monitor the Company's service quality and detect any problems, preserves or enhances service quality. I am not aware that *any* of the companies that are required to abide by the Commission's service quality rules and to file monthly service quality reports with the Commission have been granted a complete waiver of the reporting requirements of WAC 480-120-439(1).

Q. But doesn't Qwest offer to continue service quality reporting for four years?

A. Yes, Qwest's petition includes a proposal that the Company would file monthly service quality reports, similar to those provided by other Class A companies, during a four year "transition"

[4] See also, WAC 480-120-034.
[5] Exhibit No. ___ (MSR-1T), p. 14, ll. 13-14.

period. Qwest's monthly reports have already been scaled back, beginning October, 2006.[6] We are still determining exactly what their proposed monthly reports would look like, according to their AFOR proposal. We have asked for clarification from the Company in discovery and have not yet received a response.

Qwest's proposal to provide some level of service quality reporting for a four year period, at the end of which the Company would be granted an automatic waiver of the reporting requirements, creates an extremely awkward structure. We do not know what the Company's service quality will look like four years from now, or what the telecommunications landscape will be in four years. It would be premature to grant Qwest a waiver of the Commission's service quality reporting rule four years from when any AFOR becomes effective. Granting Qwest a waiver of the Commission's service quality reporting rule as part of this AFOR is not in the public interest. I recommend the Commission reject this aspect of Qwest's proposal.

Q. Qwest also requests a waiver of the requirement that they file reports with the Commission regarding their Customer Service Guarantee Programs. Do you support this aspect of the Company's proposal?

A. No. I do not believe that it is in the public interest to relieve Qwest from this requirement as part of an AFOR. Qwest is the largest local exchange carrier in the state, and the Commission has expressly ordered the Company to file reports containing information about the credits provided to customers under the Customer Service Guarantee Programs.[7] The Customer Service

[6] Qwest's monthly service quality reports no longer include dial tone and answer time reports, if the company meets the Commission's standards. If Public Counsel's recommended SQIP is included as part of an AFOR, we recommend that these reports be provided, at least on a quarterly basis, to verify and monitor performance.

[7] In its Sixteenth Supplemental Order in the merger docket, the Commission directed Staff to draft an order directing Qwest to "report current and historical information in reports that continue for the duration of the [Customer Service Guarantee] program unless terminated earlier by order of the Commission Executive Secretary, pursuant to authority

Guarantee is an important element of service quality because it provides some compensation to consumers for service failures. While it is currently in Qwest's tariff, Qwest has made no commitment to continue it during the AFOR. Public Counsel recommends that Qwest should continue to provide the customer service guarantee programs for the duration of any AFOR and to continue providing reports to the Commission.

Q. Do you believe Qwest's current reports on the Customer Guarantee Programs are sufficient?

A. No, I do not. I believe that in fact Qwest's reports need to be updated. Subsequent to the Commission's Seventeenth Supplemental Order in UT-991358, which was entered on October 22, 2004, the Company made significant modifications to the customer guarantee programs. (These modifications, which took effect in October 2005, are described below, at footnote 21). Public Counsel recommends that the Commission direct Staff, Public Counsel, and Qwest to develop an appropriate reporting format suitable to the new program. In particular, since the Company modified the out-of-service program in October 2005, they have not included information about credits paid under the out-of-service guarantee, which is offered under tariff WN U-40, Section 2.2.2.B.3 Previously, the Company offered a $5 credit for out-of-service conditions not repaired in two working days, and a credit of one month's recurring charge plus associated regulated features if the service was not repaired in seven calendar days. The current

granted in RCW 80.04.080." (Docket No. UT-991358, Sixteenth Supplemental Order, f. 7 at p. 12). In its Seventeenth Supplemental Order in the merger docket, the Commission established the specific elements that should be included in the Qwest's reporting of the customer guarantee programs.

program provides pro-rata credits that will generally be smaller than the credits provided under the previous program.[8]

III. QWEST/US WEST'S HISTORY OF SERVICE QUALITY PERFORMANCE IN WASHINGTON

A. *US West Service Quality Issues in the 1990s*

Q. Did the Commission make any findings concerning the Company's service quality performance in the 1990s?

A. Yes. In 1996, the Commission found there were serious problems with the Company's service quality (then known as US West Communications). After reviewing extensive evidence as part of the Company's 1995 rate case, the Commission determined that the Company's service quality had become substantially worse, particularly in the areas of installing service and restoring service outages in a timely fashion. The Commission determined that these service failures were "caused in part by lack of facilities and in part by restructuring and downsizing."[9] These findings were later upheld by the Washington State Supreme Court.

Q. Did the Company operate under an AFOR in Washington in the 1990s?

A. Yes. Qwest's predecessor, US West, Inc., operated under an AFOR in Washington from January 16, 1990 to December 31, 1994. That AFOR settlement was approved by the Commission in Docket No. 89—3245-P.[10] The Company was relieved of some regulatory constraints and

[8] For example, a customer with an outage lasting eight days would have received a credit of the basic monthly local exchange rate and associated regulated features under the previous program, but would only qualify for a credit equal to 8 * 1/30th of their monthly recurring charges under the existing program. Customers subscribing to certain bundled packages, with larger monthly recurring charges, may receive a pro-rata credit that is larger than the $5 credit offered under the previous program, depending on the length of their outage and their monthly recurring charges.
[9] 1995 Rate Case Order, p. 16.
[10] *In the Matter of the Petition of Pacific Northwest Bell Telephone Company, d/b/a US West Communications For an Alternative Form of Regulation,* Docket No. U-89-3245-P, Fourth Supplemental Order Accepting Settlement with Modifications, Resolving Complaint and Authorizing An Alternative Form of Regulation, January 16, 1990.

allowed to earn and retain earnings in excess of its authorized return in exchange for sharing excess earnings with customers as directed by the Commission. That AFOR did contain reporting requirements related to service quality.

Q. Did this Commission determine that there were major problems with US West's service quality during the period that the Company operated under an AFOR?

A. Yes. In its Fifteenth Supplemental Order in Docket No. UT-950200, the Commission made the following findings related to the Company's service quality:

> The Commission finds that USWC is providing service that is substantially worse than that which the Company provided only a few years earlier, at the beginning of its AFOR. The Commission's frequent and consistent attempts to achieve improvement in service quality have been unsuccessful. We find major problems with the Company's ability to install service when needed and its ability to provide repair service when needed, caused in part by lack of facilities and in part by restructuring and downsizing.
>
> The Company's inability to meet its basic service obligations hurts individual ratepayers and it hurts the state economy as a whole. This Commission has not micro-managed USWC's re-engineering and restructuring efforts and does not intend to do so. We are concerned with results. To that end, we are ordering the Company to provide customer service guarantee programs and reducing the Company's return on equity by 0.5% to the low end of the reasonable range, to reflect the level of service it is providing and provide incentive for improvement. We also are ordering improved service quality statistics reporting, and disallowing management team and merit awards that are not clearly and directly linked to meeting service quality targets. When the Company can demonstrate that it is providing adequate service, it may petition to lift any or all of these requirements.
>
> The Company has argued that it cannot invest in Washington state because of uncertainty about its future ability to recover its capital investment. The record in the case demonstrates this to be unfounded. Under the AFOR (January 16, 1990 to December 31, 1994), the Company was authorized to earn an attractive 11% rate of return, and it retained excess profits of $77 million. At the same time, it was cutting investment and reducing staffing levels in the state. Instead of re-investing its

> earnings in Washington State, the Company is generating funds by dis-investing in the state and failing to provide minimum levels of service to the harm of its citizens and economy. In this Order we authorize the Company to recover its proper costs of operating and to earn a market-based rate of return on its investment.[11]

In addition to reducing the Company's return on equity, ordering improved service quality reporting, and disallowing management and team awards, the Commission also ordered the Company to offer a held order/wireless loaner guarantee.[12]

The Commission also noted that the Company's service failures occurred after the Company was granted regulatory flexibility as part of an AFOR. The Commission stated:

> It is unfortunate that the Commission's attempts to reduce the regulatory burdens on USWC appeared to result in the violation of one of the most important conditions for approving an AFOR, that it "[w]ill not result in a degradation of the quality or availability of efficient telecommunications services[.]" RCW 80.36.135(3)(e).[13]

US West appealed the Commission's Final Order in the 1995 rate case, and in December 1997 the Washington Supreme Court upheld the Commission's decision, finding:

> We conclude there was substantial evidence to support the Commission's finding that US West was providing inadequate service to its customers and its competitors, and that the Commission has authority to consider service quality in setting the rate of return within the range of reasonable rates. [14]

The WA Supreme Court also upheld the Commission's decision to order US West to implement a held order/wireless loaner customer service guarantee program.[15]

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[11] 1995 Rate Case Order, pp. 11-12; footnotes and citations omitted.
[12] 1995 Rate Case Order, p. 23.
[13] 1995 Rate Case Order, f. 6.
[14] 134 Wn.2d 74, 949 P.2d 1337, at 123-124.
[15] *Id.*

Q. Did the Commission later expand upon the customer guarantee program?

A. Yes. The program was continued and expanded as part of the 1997 "make whole" US West rate case, in which the Commission directed the Company to institute a $50 missed appointment/commitment program.[16]

B. *US West – Qwest Merger, 2000 to the Present*

Q. Did the US West – Qwest Merger Settlement include any provisions related to service quality?

A. Yes. US West Inc. and Qwest Communications International Inc. sought Commission approval for their merger in a petition filed August 31, 1999. The Commission approved the merger in its Ninth Supplemental Order in docket UT-991358, and adopted two settlement agreements – a "Retail Settlement Agreement" and a "Competitive Settlement Agreement."[17] The Retail Settlement Agreement included a set of conditions designed to ensure the merger did not harm customers. These included a rate freeze, a Service Quality Performance Program, and a Qwest commitment to maintain historic investment levels in Washington following the merger. The Company also agreed to further expand the customer service guarantee programs, adding new programs for no dial tone and trouble report credits, and agreed continue these programs for a

[16] *Washington Utilities and Transportation Commission v. US West Communications, Inc.*, Docket No. UT-990766, Tenth Supplemental Order, Commission Decision and Order Rejecting Tariff Revisions; Requiring Refiling, January 15, 1998, p. 27. *See also* Docket No. UT-970766, Twelfth Supplemental Order, Commission Order on Clarification (Service Guarantee and Missed Appointment Issues).

[17] *In re Application of US WEST, INC. and QWEST COMMUNICATIONS INTERNATIONAL INC. For an Order Disclaiming Jurisdiction or, in the Alternative, Approving the US WEST, INC. - QWEST COMMUNICATIONS INTERNATIONAL INC. Merger*, Docket No. UT-991358, Ninth Supplemental Order Approving and Adopting Settlement Agreement and Granting Application ("Merger Order"). The "Retail Settlement Agreement" is included as Attachment A to the Ninth Supplemental Order, and the "Competitive Settlement Agreement" is included as Attachment B to the Order.

minimum of three years.[18] The Competitive Settlement Agreement addressed carrier-to-carrier service quality issues.

Perhaps the most significant commitment in the Retail Settlement Agreement was the Service Quality Performance Program (SQPP), which established performance benchmarks and placed $20 million at risk per year should the Company not meet the benchmarks. The program established eight performance baselines designed to provide an incentive to Qwest to provide adequate service quality. If the Company failed to meet those eight baseline performance levels, the Company provided bill credits to customers to compensate them for shortcomings.

At the time of the merger, therefore, Qwest agreed to both customer-specific guarantees and the Service Quality Performance Program (SQPP), which placed $20 million at risk annually for failure to meet eight different performance benchmarks.

Q. What was Qwest's performance under the SQPP?

A. Qwest paid credits to customers every year that the SQPP was in effect, as shown in Table 1 below.

Table 1. Qwest's Performance Under the SQPP

Year	Total Credits Paid under SQPP
2001	$3,173,803
2002	$1,895,242
2003	$1,926,473
2004	$1,345,587*
2005	$916,667*

* Pursuant to the Commission's Sixteenth Supplemental Order in Docket No. UT-991358, certain performance standards and penalty calculations for the SQPP were modified. *See infra*.
Source for Credit amounts: Qwest's Annual Service Quality Report to Customers (bill inserts) and Qwest's Supplemental Response to Public Counsel Data Request No. PC-14.

[18] Docket No. UT-991358, Retail Settlement Agreement, Section II.A.

For the first three years that the program was in effect, from 2001 to 2003, Qwest failed to meet five of the eight performance measures in the SQPP. Those five performance measures were held orders (both 5 day and 90 day standards), repairing out-of-service conditions, telephone answer time in calls to the business office, and complaint response to the Commission's Consumer Affairs section. During the final 18 months that the SQPP was in effect, from July 2004 through December 2005, Qwest failed to meet four of the eight performance measures. Those four measures were held orders (both five day and 90 day standards), trouble report, and repairing out-of-service conditions. Several modifications to the SQPP were in effect for the final 18 months of the program, as described briefly below.

Under the terms of the Retail Settlement Agreement approved by the Commission, the program began January 1, 2001, and remained in effect through 2005. Qwest was permitted to petition to terminate the Service Quality Performance Program after calendar year 2003.[19] On January 30, 2004, Qwest Corporation (Qwest) filed a petition to terminate the SQPP. In its Sixteenth Supplemental Order in Docket No. UT-991358, the Commission rejected Qwest's petition for early termination of the SQPP. However, the Commission did grant Qwest's request to modify the SQPP.

Qwest's petition to modify certain performance standards and credit calculations was granted by the Commission in the Sixteenth Supplemental Order in the merger docket (UT-991358). Six of the eight performance standards were modified to match the Commission's revised service quality rules, which took effect in July 2003. In some instances the performance standard became stricter (e.g. no dial tone, trouble report, out-of-service repair), whereas in other

[19] Merger Order, ¶ 30.

instances the rule was more lenient than the SQPP standard. Qwest also sought to modify the payment calculation for two measures (out-of-service repair and complaint response), to create a graduated, sliding scale payment structure. Those proposals were also adopted by the Commission in the Sixteenth Supplemental Order.

C. *Customer-Specific Service Guarantees*

Q. Does Qwest presently offer the Customer Guarantee Programs discussed earlier in your testimony?

A. Yes, although these programs have been modified and scaled back from the five programs offered subsequent to the US West-Qwest merger settlement. The Company currently offers three programs, set forth in Qwest's tariff WN U-40, Section 2.2.2.B.[20] The Company modified the Customer Service Guarantee programs in October 2005, primarily to reduce the amount of customer-specific credits provided under the various programs, and also to eliminate two of the guarantee programs.[21]

Q. Should Qwest continue to offer these Customer Guarantee Programs as part of an AFOR?

A. Yes. I believe it is important that the Company continue to offer these programs, which provide direct compensation to those customers who experience inferior service from the Company, for the duration of an AFOR.

[20] This section of the tariff is attached as Exhibit No. ____ (MMK-2).
[21] In Docket No. UT-051498, the Commission allowed tariff modifications to the customer service guarantee programs to take effect. The no dial tone and trouble report credit programs were eliminated, and the credit amount for missed appointments or commitments for *residential* installation or repair was reduced from $50 to $25. In the delayed primary basic exchange guarantee, the service alternatives were modified, and potential credit amounts reduced. Finally, the out-of-service repair guarantee credits were modified to a pro-rata credit.

Q. Do you believe Qwest's Customer Service Guarantee Programs provide sufficient protection against any potential degradation to service quality, as set forth in the AFOR statute?

A. No. The customer service guarantees are designed to provide credits to specific customers who experience inferior, inadequate service. While these credits provide compensation to those individual customers, in the aggregate, the dollar amount the Company pays to customers is not necessarily large enough to provide an effective incentive to encourage high quality service. While the pro-rata credit is important in that it provides some compensation to the individual customer, the amount Qwest pays in customer credits is most likely small enough that it is recognized by the Company as merely a cost of doing business.

IV. PUBLIC COUNSEL RECOMMENDS AN INCENTIVE-BASED, SELF-EXECUTING SERVICE QUALITY PERFORMANCE PLAN

A. *The Rationale For Serivce Quality Incentives*

Q. Why should the Commission adopt a service quality incentive plan as part of an AFOR?

A. Public Counsel's proposed Service Quality Incentive Plan is designed as an anti-backsliding measure, consistent with the statutory requirement that the Commission should consider whether an AFOR will preserve or enhance service quality. The Company's service quality has improved in many areas in recent years, and we applaud those improvements. The incentive plan we recommend is not intended as either a reward or punishment for the company's recent service performance. Rather, it is designed as an anti-backsliding plan, to help ensure that the Company's service quality does not deteriorate. To the extent there is room for improvement in some areas, the SQIP provides an incentive to achieve improved performance.

The purpose of a service quality incentive program with self-actuating penalties is to place enough dollars at risk in potential financial payments to function as an effective incentive for the Company to make the necessary investments in Washington in order to provide satisfactory service. During the Commission's March 14, 2000, hearing considering the Retail Settlement Agreement in the US West-Qwest merger proceeding, US West witness Ms. Theresa Jensen indicated that the service quality conditions in the settlement agreement, and particularly the SQPP, would provide such an incentive. In response to a question from Chairwoman Showalter, Ms. Jensen stated:

> "We would much rather take the potential 20 million dollars and invest it in the network to provide services to the customers than to pay it as a credit to customers, so the reality of this agreement is it insents [sic] the company to look at not only it's [sic] investment but its practices, its forecasts, its planning, to attempt to minimize what it pays in the form of service programs or credits and provide better service to the customer in the end, and everyone will benefit from that, not just consumers." [22]

While US West operated under an AFOR in the early 1990s, serious service quality degradation occurred. Certainly, we want to avoid that happening again. The Commission has found that service quality performance plans, with self-executing payments, provide a better incentive for performance than the enforcement mechanisms under the Commission's rules. In its Sixteenth Supplemental Order in the merger docket, rejecting Qwest's petition for early

[22] Docket No. UT-991358, Tr. 403.

termination of the SQPP, the Commission concluded:

> …while the rules and the SQPP address similar behaviors they also are designed for different purposes and they have substantially different remedies.
>
> Enforcement mechanisms for the SQPP and the rules are different. This record does make it clear that the enforcement mechanism associated with the SQPP provides a better incentive for performance than that of the rules.
>
> The SQPP is self-executing, in that Qwest knows the standards, keeps track of performance, and provides the credit based on its performance and the scale for providing credits. Enforcement of the rules, however, requires a Commission (or private) complaint or a penalty assessment, and the existence of penalties for rule violation is somewhat academic until penalties are assessed and paid. Litigating a complaint can be more expensive than the value of the penalties that may result. A private complaining party enjoys no financial benefit from the payment of penalties to the public service revolving fund and so may have little incentive to make a necessary investment in a complaint. While the SQPP continues, it provides a constant incentive for the Company to meet SQPP standards. We find that a purpose of the SQPP is to maintain an incentive for the Company to provide satisfactory service. We find that Qwest's service quality has improved, but believe that the SQPP credit requirements have provided, and should continue to provide, important incentives in fostering good service quality.[23]

Q. Earlier you discussed the relationship between investment and service quality. Do you have any recent data available regarding Qwest's investment in Washington?

A. Yes. Exhibit No. ___ (MMK-3C) shows Qwest's capital investment in Washington from 2001 through 2005. As part of the merger settlement agreement, the Company was required to

[23] Docket No. UT-991358, Sixteenth Supplemental Order, at ¶¶36-38.

maintain historic investment levels of $133 per access line for a period of three years following the merger.[24] The Company filed investment reports with the Commission pursuant to this commitment, and those reports serve as the source for data for 2001 through 2003 in Exhibit No. ___ (MMK-3C). In response to a data request from Public Counsel, Qwest provided similar information for 2004 and 2005.

This exhibit shows that there is a very clear **[Begin Confidential] ************** [End Confidential]** beginning in 2002. We cannot know with certainty whether any **[Begin Confidential] ******* [End Confidential]** investment will ultimately result in service quality **[Begin Confidential] *********** [End Confidential]**. This is why an anti-backsliding plan such as the SQIP is the most appropriate means of protecting against potential degradations to service quality. It provides an incentive to the Company to make the necessary investments needed to continue to offer satisfactory service, and to provide better service in areas where there may be room for improvement. As the Commission stated in the 1995 Rate Case Order, "[w]e are concerned with results."[25] Instead of attempting to micromanage the Company's capital investment decisions, the SQIP is appropriately focused on how those decisions translate into service quality performance.

Q. Does an incentive-based service quality program, with self-actuating "penalties" or customer credits, serve a different purpose than customer-specific service quality remedies?

A. Yes. The Customer Service Guarantees are designed as a compensation mechanism, while the

[24] Docket No. UT-991358, Merger Order at ¶31, and Retail Settlement Agreement, Section III.D; see also Tr. 391-395.
[25] 1995 Rate Case Order, p. 11.

SQIP is designed as an incentive mechanism, as described above. While the customer service guarantees provide at least a nominal remedy to those consumers that have already been harmed by inferior service, an incentive-based program with self actuating payments, such as the SQIP, is designed to provide Qwest with incentives to provide satisfactory service quality to all of its customers.

Another way in which the customer guarantees and the SQPP complement rather than duplicate one another is that some of the performance measurements in the SQPP are not captured at all by the customer guarantee programs. This is due in part to the fact that in some circumstances it is impossible or impractical to identify and thereby compensate the affected customers. For example, with respect to the two performance standards measuring answer time in Qwest's customer service (business) centers and repair centers, it may be impossible and cumbersome to locate those customers who experience long hold times, some of whom may decide to hang up in frustration. Additional areas not covered by the customer guarantees are Qwest's response to WUTC Consumer Affairs complaint staff, and the dial tone and trouble report standards.

Q. Has Qwest operated under retail service quality plans in other states, with self-executing payments for sub-standard performance?

A. Yes. Qwest has operated under such plans in several of the states in the Company's 14-state local service territory. These retail service quality programs are often established as part of an AFOR or price-cap plan.[26] In Arizona, for example, Qwest has operated under a retail service

[26] Public Counsel has asked Qwest for information about AFORs and price cap plans that the Company has operated under in other states in its service territory, but we have not yet received a complete response from the Company.

quality plan for several years, with self-actuating penalties, as part of a price cap regulation plan. Qwest has faced potential penalties for the following areas of performance:[27]

- Held Orders
- Out-of-Service Repair
- Telephone Answer Time – Residence Calls to Business Office
- Telephone Answer Time – Business Calls to Business Office
- Telephone Answer Time – Repair Center Access

The current Arizona price cap plan, approved by the Arizona Corporation Commission in March 2006, also includes a provision that in any year in which Qwest becomes subject to penalties under two or more of the five categories above, an additional credit of $2.00 for each residential and business access line shall be imposed.[28]

In New Mexico, the Public Regulation Commission recently issued a Final Order on Pricing and Quality of Service, Case No. 05-00466-UT, in November 2006, as part of a proceeding to establish an AFOR (AFOR II) that would apply after the expiration of the Company's current AFOR (AFOR I). This Order establishes pricing and service quality standards and requirements to be incorporated in Qwest's subsequent AFOR. The service quality provisions include standards with self-executing penalties, as well as provisions for direct customer remedies in certain areas.[29]

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[27] Qwest's Supplemental Response to Public Counsel Data Request PC-14 and Qwest's Response to Staff Data Request No. 4.
[28] *In the Matter of Qwest Corporation's Filing of Renewed Price Regulation Plan*, Docket No. T-01051B-03-0454 et. al., Decision No. 68604 Opinion and Order, March 23, 2006, at pp. 9-10.
[29] *In the Matter of the Development of An Alternative Form of Regulation Plan for Qwest Corporation*, Case No. 05-00466-UT, Final Order on Pricing and Quality of Service, November 2006.

Qwest has operated under retail service quality performance plans, with self-executing penalties, in other states as well. These include Colorado, Minnesota, Oregon, and Iowa, in addition to those of Arizona, New Mexico, and Washington which have been discussed.[30]

Q. You have indicated that Qwest's service quality has improved in many areas, please describe some of those improvements.

A. An area where Qwest has shown significant improvement is the Company's response to WUTC Consumer Affairs complaint staff. The merger's SQPP included a measure that placed $1 million at risk annually if Qwest did not provide a complete and detailed response to complaint staff within two business days. During the first year of the SQPP, in 2001, Qwest's performance fell below this standard in every month. In February 2001, for example, Qwest had 300 violations assessed by WUTC Consumer Affairs staff.[31] By 2003, the Company's performance was below the standard in only 2 months of the year, and in each of those months they were assessed only one violation.[32] During the final two years of the SQPP, Qwest met the standard each month and thus did not face any credit liability. The SQPP thus provided an incentive for Qwest to take the steps necessary, in terms of staffing, resources, and procedures, in order to meet this performance standard.

Another area where the Company's performance has improved is in the installation of orders. The Company's credit liability for the two held order measures (5 day and 90 day) declined significantly from 2001 to 2005. The Company's best performance for these measures was in 2004.

[30] Qwest's Supplemental Response to Public Counsel Data Request No. PC-14.
[31] Qwest's 2001 Annual Service Quality Report to Consumers.
[32] Qwest's 2003 Annual Service Quality Report to Consumers.

Q. Given these improvements, why is there a need for a Service Quality Incentive Plan?

A. While Qwest's service quality did improve in many areas, resulting in fewer total customer credits in the later years of the SQPP, I believe this indicates that the SQPP served its intended purpose in providing an incentive to improve service quality. As noted above, the Commission concluded in June 2004 that the SQPP was indeed providing such an incentive: "[w]e find that Qwest's service quality has improved, but believe that the SQPP credit requirements have provided, and should continue to provide, important incentives in fostering good service quality.[33]

As I discussed above, the SQIP Public Counsel recommends is designed as an anti-backsliding plan, to help ensure that service quality does not deteriorate during the term of an AFOR. I believe this is consistent with the statutory requirement that the Commission should consider whether an AFOR will enhance or preserve service quality. Qwest has operated under service quality mechanisms similar to the SQIP in other Qwest states, as part of AFORs or other schemes of relaxed regulation. In addition, as I discuss below, there are areas where it appears that Qwest has room for improved service quality, in restoring out-of-service conditions, and in meeting the Commission's trunk blocking standards.

Finally, a retail service quality incentive plan would complement Qwest's wholesale service quality plan, the Performance Assurance Plan, or QPAP. The QPAP is composed of numerous performance measures, and is self-executing. If Qwest's performance falls below certain levels, it must make payments to competitive local exchange carriers (Tier 1 payments), and/or the State of Washington (Tier 2 payments). Many of the QPAP performance measures

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[33] Docket No. UT-991358, Sixteenth Supplemental Order, at ¶38.

are 'parity' measures, in which Qwest's service to its wholesale customers is compared to its retail customers. To the extent Qwest's retail service quality declines, their service to wholesale customers may also decline, and if there are no financial incentives on the retail side, then Qwest arguably has an incentive to provide inferior service to retail customers because doing so would make it easier for them to meet certain QPAP performance standards. An anti-backsliding plan for retail service quality would therefore function as a natural counterpart to the QPAP, and would provide some mitigation against such a perverse incentive.

Q. Given that some of the standards were modified in July, 2004, does that affect our ability to analyze the Company's performance in some areas?

A. Yes. One area where it is difficult to determine whether Qwest's performance has improved is the telephone answer time in calls to the Company's repair centers and business offices. At the inception of the SQPP, the standard for these two measures was that 80% of calls be answered within thirty seconds. In 2001 Qwest failed the business office standard for 9 of 12 months. In 2002 the Company's performance improved, resulting in only 3 months below the standard, but in 2003 performance worsened and Qwest failed this standard 8 months during the year.[34] Effective July 2004, the standard changed to an average wait time on all calls of not more than 60 seconds. Once this new standard took effect, the Company's performance did not fall below the standard for the remaining 18 months of the SQPP. We do not know if that change is due to improved performance, or due to the new standard.

Another area where the standard changed is the measure for repair of out-of-service conditions. At the inception of the SQPP, the standard was repair within two working days, but

[34] Qwest's Annual Service Quality Reports to Consumers for 2001, 2002, and 2003, respectively.

was then later modified to 48 hours, consistent with the Commission's standard in WAC 480-120-440. Qwest's performance in restoring out-of-service conditions from July 2000 to the present is provided in Exhibit No. ___ (MMK-8C).

B. *Public Counsel's Service Quality Incentive Plan*

Q. Please describe the specific performance measures included in Public Counsel's proposed Service Quality Incentive Plan?

A. Public Counsel's proposed SQIP is composed of nine performance measures and places $16 million at risk annually to provide an incentive for Qwest to provide satisfactory service quality to its retail customers. The plan is set forth in detail in Exhibit No. ___ (MMK-4). The first eight measures are identical to those in the merger program, the SQPP. Those eight measures are held orders (5 day and 90 day standards), trouble reports, dial tone speed, out-of-service repair, telephone answer time (repair center and business office), and complaint response to WUTC Consumer Affairs. The performance standards for these measures, which are also shown in Exhibit No. ___ (MMK-4), are identical to those in the SQPP, as modified by the Commission in the Sixteenth Supplemental Order in the merger proceeding.

The ninth performance measure, which was not included in the merger's SQPP, is for trunk blockage of interoffice facilities. The performance standard we have incorporated into the SQIP is identical to that in Commission's rules, as set forth in WAC 480-120-401(3). That rule establishes trunk blocking standards during the average busy hour for intertoll and intertandem facilities, local and EAS facilities, and E911 facilities. The performance of Class A carriers is provided on the telecommunications service quality page of the Commission's Internet website, which shows that from January to November of 2006, Qwest failed to meet the standard in several months for two of the three trunk blocking standards – E911, and intertoll and intertandem trunk blocking. Based on the information provided on the Commission's website, it appears that during this same time frame, the other carriers consistently met the Commission's trunk blocking standards. In this regard, it appears that there may be room for improvement in Qwest's performance in this area.

Q. Please explain why the SQIP places $16 Million at risk annually in potential customer credits, which is lower than the $20 Million under the merger's SQPP?

A. Public Counsel's proposed SQIP would place a total of $16 million at risk in potential customer credits. This amount is comparable to the $20 million at risk annually as part of the merger settlement's SQPP, based on an analysis of the company's adjusted intrastate revenues, as shown in Exhibit No.___ (MMK-6C). This exhibit shows that the $20 million in maximum annual bill credits to customers under the SQPP reflects **[Begin Confidential]***** [End Confidential]** of the company's 1999 intrastate adjusted revenues.[35] This same percentage, when applied to Qwest's 2005 intrastate adjusted revenues, yields approximately $16 million.

As a point of comparison, Qwest's wholesale service quality program, the Performance Assurance Plan, or QPAP, places a maximum of 36% of the company's net return at risk, calculated using certain ARMIS data reported on the Form 43-01. As shown in Exhibit No. ___ (MMK-7), the current annual cap on penalty payments under the QPAP is $62 million.

In summary, I believe that a maximum of $16 million for a retail service quality incentive program is reasonable.

Q. Please explain the payment calculations in the SQIP.

[35] Qwest's Response to Staff Data Request No. 25, US West's 1999 A61, fourth quarter report to the WUTC.

A. The payment calculations for the SQIP are performed in the same manner as those of the SQPP, subsequent to the modifications to the SQPP that were made at Qwest's request. The primary difference is that since the total dollar amount at risk is reduced – from $20M to $16M – the total amount at risk annually for four measures – order completion (5 day and 90 day standards), trouble report, and dial tone – is lower under the SQIP than it was under the merger settlement's SQPP. The SQPP had placed $4 million at risk annually for each of those four measures, and $1 million at risk annually for the remaining four measures in the program. Public Counsel's proposed SQIP places $3 million at risk annually for the order completion and trouble report measures, and $2 million for the dial tone speed measure. A complete comparison of the SQPP to Public Counsel's proposed SQIP is provided in Exhibit No. ___ (MMK-5).

Q. Please explain why the amount at risk for the dial tone measure is further reduced, compared to the other measures you just discussed?

A. The dial tone speed measure is based on the Commission's rule establishing network performance standard, WAC 480-120-401. As discussed earlier in my testimony, the SQIP includes an additional network performance measure, for trunk blocking. This standard is also established in WAC 480-120-401. Because both measures address network performance, it seemed most appropriate to place a generally comparable amount at risk under the SQIP for network performance, as had been at risk under the SQPP.

Q. If Public Counsel's proposed SQIP had been in effect in 2006, what would Qwest have paid in bill credits to customers?

A. Exhibit No. ___ (MMK-9C) provides a simulation of the credit obligation Qwest would have faced during the first nine months of 2006, based on the Company's service quality performance in the nine measures of the SQIP. This exhibit shows that Qwest would have faced a total credit obligation of **[Begin Confidential] ********** [End Confidential]** under the SQIP, from January to September 2006. As the exhibit further shows, the majority of the simulated credit obligation results from Qwest's level of performance in restoring out-of-service conditions and trunk blocking.

Q. What do you recommend as the duration of the SQIP?

A. I recommend that a service quality incentive plan such as the SQIP remain in place for the duration of an AFOR.

Q. Are there any other provisions of Public Counsel's recommended SQIP, aside from the performance standards and potential credit obligation?

A. Yes. Exhibit No. ___ (MMK-4) outlines the SQIP, and includes provisions that were included in the merger settlement agreement. These include a mitigation provision, whereby the Company may file a petition seeking mitigation of customer credits, as well as an annual report to customers, outlining annual performance under the SQIP.

Q. Does this conclude your testimony?

A. Yes.