Exhibit ____ (TJG-4T)

BEFORE THE WASHINGTON STATE
UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Petition for Arbitration of an Interconnection Agreement Between COMCAST PHONE OF WASHINGTON, LLC, with UNITED TELEPHONE COMPANY OF THE NORTHWEST, INC. d/b/a EMBARQ Pursuant to 47 U.S.C. Section 252(b).	)	DOCKET UT-083025

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REPLY TESTIMONY

OF

TIMOTHY J GATES

ON BEHALF OF COMCAST PHONE OF WASHINGTON, LLC

August 1, 2008

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EXHIBITS

I. INTRODUCTION & PURPOSE OF TESTIMONY

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Timothy J Gates. My business address is QSI Consulting, 819 Huntington Drive, Highlands Ranch, Colorado 80126.

Q. ARE YOU THE SAME TIMOTHY GATES WHO FILED DIRECT TESTIMONY IN THIS PROCEEDING ON JULY 2, 2008?

A. Yes.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. I will respond to the direct testimony of Alan L. Lubeck on behalf of United Telephone Company of the Northwest d/b/a Embarq ("Embarq"), filed on July 2, 2008.[1]

Q. PLEASE SUMMARIZE YOUR REACTIONS TO MR. LUBECK'S DIRECT TESTIMONY?

A. I have three main reactions to Mr. Lubeck's testimony. ***First***, I am surprised that he did not offer a serious rebuttal to the main point in Comcast's Petition for Arbitration. Comcast's Petition claims that Embarq's proposed Directory Listing Storage and Maintenance charge ("DLSM") violates Embarq's Section 251(b)(3) duty to provide Comcast with "nondiscriminatory access to Directory Listing[s]." The facts are undisputed: Embarq does not impose a similar charge on its own

[1] Direct Testimony of Alan L. Lubeck on behalf of Embarq, Docket No. UT-083025, Embarq Exhibit No. (ALL-1T), July 2, 2008 ("Lubeck Direct" or "Exhibit ALL-1T").

customers or on CLECs that purchase UNE-loops or that resell Embarq's service, and Embarq has not offered a cost justification for the disparate treatment. The DLSM charge is, therefore, impermissible under the FCC's long-standing interpretation of Section 251(b)(3).

In response, Mr. Lubeck claims that Section 251(b)(3) no longer applies because Embarq has sold its directory publishing business to a third party (Donnelley a/k/a DEX).[2] To support this position, Mr. Lubeck offers only his own policy views and no legal authority, which is not surprising, as no such authority exists. The only way that Section 251(b)(3) could not control the outcome of this proceeding is if the Federal Communications Commission ("FCC") issued an order authorizing states to forebear from enforcing that legal requirement. It has not done so.

Second, I was surprised by Mr. Lubeck's contention that Comcast wants access to Embarq's DL service for free.[3] It is hard to understand how Mr. Lubeck could make that claim. It is undisputed that Comcast has agreed to pay the non-recurring charge ("NRC") that Embarq proposed for the DL service order entry processing charge. And it is clear that many of the activities associated with the NRC are the same as those that Embarq claims are associated with the DLSM charge and which the parties have agreed during the course of their negotiations would be recovered by the NRC. It is also undisputed that Embarq is paid by

[2] Comcast has sought additional documents from Embarq to evaluate these Embarq contentions, which Embarq has not yet provided.

[3] *See* Lubeck Direct, ALL-1T, at 3:7-9, 3:17-20.

directory publishers ("DPs")[4] at the FCC-authorized rates for the listings that Comcast provides. So I do not see how Mr. Lubeck can say that Comcast wants anything for free.

Third, I am struck by the lack of analytical rigor in Mr. Lubeck's economic and market analysis. Despite Mr. Lubeck's speculation about what might be possible, there is no existing "market" for directory listings. Moreover, Mr. Lubeck's claim that prices are unbounded by cost in competitive markets is at odds with more than a century of micro-economic theory. Indeed, the point of price constraints in regulated industries like telecommunications is to reproduce the cost-based pricing found in competitive markets.

II. EMBARQ'S PROPOSED DLSM CHARGE IS DISCRIMINATORY

Q. MR. LUBECK CLAIMS THAT EMBARQ IS CHARGING ITSELF THE SAME CHARGE THAT IT IS IMPOSING ON COMCAST. IS THAT CORRECT?[5]

A. No. The undisputed fact is that Embarq ***does not*** impose a separate charge on its customers (or UNE-L and resale CLECs) to have their numbers listed in the local Embarq-branded directories. Embarq's claim that some unspecified directory listing charge is "implicit" in local rates is unsupported and, therefore, beside the

[4] Although Mr. Lubeck contends that Comcast "benefits in other ways" from the storage and maintenance of its listings by Embarq, such as the provision of directory listings to directory assistance ("DA") services (Lubeck Direct, p. 6, lines 9-19), the primary concern in this proceeding involves the storage and maintenance of Comcast's subscriber listings for publication in Embarq's branded directories.

[5] *See, e.g.,* Lubeck Direct, ALL-1T, p. 14, lines 4-6 and p. 24, lines 5-7.

point. Embarq has the burden of proof in this proceeding. By failing to present evidence to prove that it imposes a similar charge on its own customers, it has failed to meet that burden.

Q. WOULD CHARGING FACILITIES-BASED AND UNE-L/RESALE CLECs DIFFERENT RATES, AS EMBARQ PROPOSES, BE INCONSISTENT WITH THE PURPOSE OF SECTION 251(B)(3)?

A. Yes. Permitting Embarq to charge its competitors different rates for the same service would confound the purpose underlying the enactment of Section 251(b)(3) which, as the FCC has explained, was intended "to provide competitors with access to the incumbent LECs' networks sufficient to create a competitively neutral playing field for new entrants ...."[6] It would violate this competitive neutrality principle if Embarq could unilaterally raise the exogenous costs of some of its competitors, but not others.

Q. AT PAGES 11 AND 12 OF HIS DIRECT TESTIMONY MR. LUBECK SUGGESTS THAT THE "NONDISCRIMINATION" REQUIREMENT OF SECTION 251(B)(3) DOES NOT APPLY WHEN "...THE CLEC CAN DEAL DIRECTLY WITH THE DIRECTORY PUBLISHER...."[7] IS THIS CORRECT?

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[6] *Implementation of the Telecommunications Act of 1996: Telecommunications Carriers' Use of Customer Proprietary Network Information and Other Customer Information, Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, Provision of Directory Listing Information under the Telecommunications Act of 1934 [sic], As Amended*, CC Docket Nos. 96-115, 96-98, 99-273, Third Report and Order, Second Order on Reconsideration, and Notice of Proposed Rulemaking, 14 FCC Rcd 15550, ¶ 6 (1999) ("*SLI/DA Order*").

[7] Lubeck Direct, ALL-1T, p. 12, lines 14-15.

A. No. The FCC has explained that, "the term 'nondiscriminatory,' *as used throughout section 251*, applies to the terms and conditions an incumbent LEC imposes on third parties as well as on itself."[8] Simply put, because Embarq does not impose the DLSM charge on itself (*i.e.,* on its own customers) or other carriers that utilize different business models, it may not impose it on Comcast. There is nothing in the text of the statute or the FCC's regulations that suggests that Section 251(b)(3) should not apply when a CLEC "can deal directly with a directory publisher." To the extent that Embarq believes that changed circumstances should lead the FCC to change its rules and forbear from enforcing Section 251(b)(3), it should petition the FCC for relief. This bilateral arbitration proceeding, however, is not the appropriate forum for Embarq to seek this change.

Q. HAVE LECS EVER PREVIOUSLY ARGUED THAT THE DIVESTITURE OF THEIR DIRECTORY PUBLISHING BUSINESSES ELIMINATED THEIR SECTION 251(B)(3) OBLIGATIONS?

A. Yes, and those arguments were squarely rejected. In the late 1990s, not long after it became clear that the then-newly enacted Section 222(e) was going to be successful in creating a competitive DP market, ILECs began selling off those lines of business. US WEST (now Qwest) and Ameritech (now AT&T) were among the first ILECs to do so, and they almost immediately began claiming that Section 251(b)(3) no longer obligated them to forward competitors' DL information to their newly independent DP operations. The Courts rejected that

[8] *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996,* First Report and Order, 11 FCC Rcd. 15499, (1996) ("*Local Competition Order*"), ¶ 218 (emphasis added).

theory as "specious."[9] The relevant consideration under the FCC's regulations, these courts found, is whether the LEC "causes" its listings to be published in the at-issue directory.[10] The confidential agreement between Embarq and Donnelley makes it very clear that Embarq "causes" its listings to be published in the Embarq-branded Donnelley directories.

Q. WHAT DOES THE AGREEMENT BETWEEN EMBARQ AND DONNELLEY SAY?

A. The "Subscriber Listings Agreement" between Donnelley and Embarq (attached as Confidential Exhibit ___ (TJG-5C)) states that the Agreement was entered into, "in order to provide for the continued production, publication and distribution of the Embarq Directories by [Donnelley]." Recital ¶ A. It is, thus, clear that Embarq "causes" the publication of the Embarq Directories.

Q. WHAT'S HAPPENED SINCE THE *MCI* AND *HIX* DECISIONS?

A. Not much. To the best of my knowledge, no LEC – until Embarq – has attempted to argue that it could divest itself of its Section 251(b)(3) obligations while at the same time continuing to issue LEC-branded directories. None of the laws or basic facts has changed either. It is still the case that no CLEC that I know of anywhere in the country by-passes the ILECs' DL function and no other LEC imposes a

[9] *See MCI Telecomm. Corp. v. Michigan Bell Tel. Co.*, 79 F. Supp. 2d 768, 801 (E.D. Mich. 1999); *see also U.S. West Comm., Inc. v. Hix* , 93 F. Supp. 2d 1115, 1132 (D. Colo. 2000) (*citing MCI Telecomm.*).

[10] *See MCI*, 79 F. Supp.2d at 802 (citing 47 C.F.R. § 51.5 definition of "directory listings"); *Hix*, 93 F. Supp.2d at 1131.

DLSM charge.[11] These facts completely undermine Mr. Lubeck's suggestion that there is a competitive market for the DL function. (I discuss Embarq's flawed economic analysis later in this testimony.)

Q. MR. LUBECK CLAIMS THAT COMCAST AND UNE-L/RESALE CLECS ARE NOT "SIMILARLY SITUATED" AND THAT SECTION 251(B)(3) IS NOT VIOLATED.[12] IS THAT TRUE?

A. No. While Comcast and other CLECs may utilize different business models, for purposes of Embarq's Section 251(b)(3) obligations, they are *identically* situated. The FCC has explained that, "*price difference based not on cost differences*, but on such considerations as competitive relationships, the technology used by the requesting carrier, the nature of the service the requesting carrier provides, or other factors not reflecting costs, the requirements of the Act, or applicable rules, *would be discriminatory and not permissible* ...."[13] Examples of impermissible discrimination, the FCC found, would "include the imposition of different rates, terms and conditions based on the fact that the competing provider does or does not compete with the incumbent LEC, or offers service via wireless rather than wireline facilities."[14] To summarize, the FCC has explained the discrimination standard established by Section 251 as follows:

> We find that it would be unlawfully discriminatory, in violation of sections 251 and 252, if an incumbent LEC were to charge one

[11] When asked to identify another ILEC in the United States that imposes a DLSM charge in discovery (DR #1-17), Embarq was unable to do so.

[12] Lubeck Direct, ALL-1T, p. 22, line 17.

[13] *Local Competition Order*, ¶ 861 (emphasis added).

[14] *Id.*

> class of interconnecting carriers ... higher rates for interconnection than it charges other carriers, unless the different rates could be justified by differences in the costs incurred by the incumbent LEC.[15]

Thus, Embarq may not treat facility-based carriers like Comcast differently from UNE-L or resale-based CLECs absent a showing that the ***cost*** of serving Comcast differs. But Embarq does not even attempt to make this showing. It does not claim that it is more expensive to load or maintain Comcast's subscriber list information into its databases than for UNE-L or resale CLECs, as it could not.[16] Both types of companies use the same Operations Support Systems ("OSS") interfaces to submit subscriber list information to Embarq, and once loaded, to the extent that there are any expense-generating activities at all, the DLSM function is the same. Instead, Embarq simply ***asserts*** a difference between Comcast and other CLECs and claims that this unidentified difference justifies its discriminatory treatment of Comcast.

Q. IS IT REASONABLE FOR EMBARQ TO BASE THE DLSM CHARGE ON THE FOREIGN LISTING CHARGE?

A. No. The Foreign Listing Charge is assessed on out-of-region retail customers that wish to have their listings placed in a directory that is not their local directory. But it is not correct to suggest that a charge that Embarq imposes on non-local end-user customers is comparable to an assessment on a local telecommunications service provider like Comcast. Instead, the comparison should be to what Embarq

[15] *Id.*
[16] In Response to Comcast DR 1-8, Embarq admitted that "There is no difference in the way Embarq stores and maintains its own and CLECs' directory listings."

charges its own in-region (*i.e.*, local) customers to have their listing information published in the local, Embarq-branded directory. Embarq does not charge its customers a monthly recurring charge to have their phone numbers listed in the local directory; it may not, therefore, charge Comcast.

Moreover, the comparison is completely inapt. ***End-users*** – whether they are Embarq customers or not – pay a Foreign Listing charge when they want their information published in an additional or a non-local directory. The interest that out-of-territory customers have in placing their listings in non-local directories bears little relation to the ***need*** that CLEC customers have to make sure that their listings are published in the local telephone book. Congress recognized that nondiscriminatory access to directory listing was an imperative if telephony competition was to take root. The Foreign Listing service, obviously, is not such an imperative. Likewise, the comparison of Comcast – a state certified local exchange carrier with full statutory rights under Sections 251 and 252 of the Communications Act – to wireless and VoIP providers is inappropriate.

Finally, at least one state Commission – in the only analogous case that Comcast has discovered – agrees that it is inappropriate to charge competitors the equivalent of the foreign listing charge to have CLEC customers listed in the local directory. Thus, in an arbitration between Sprint and several ILECs in Illinois, the Illinois Commerce Commission rejected the ILECs' attempt, "to charge Sprint the

tariff rate for foreign listings in connection with" maintaining and publishing Sprint's DLs.[17] The Illinois Commission explained its reasoning as follows:

> The RLECs' tariffs are clear that the Foreign Exchange Directory Listing charge applies to a listing that is included in the directory of another exchange and not the exchange in which the end-user is provided local service. To charge Sprint for primary listings when the Sprint/MCC customer is located within one of the RLECs' exchanges would be contradictory to the RLECs' own tariffs and the Federal Act.[18]

The same is true here,[19] and the result should be the same, as well.

III. THE DLSM CHARGE IS PRECLUDED BY OTHER CONSIDERATIONS, AS WELL

Q. WHAT DO YOU MEAN THAT THE CHARGE IS PRECLUDED BY OTHER CONSIDERATIONS?

A. It may help to provide some context. During the process of negotiating and arbitrating this issue with Embarq around the country, I have been struck by the way that Embarq's position has "evolved." For example, it is undisputed that the current industry standard practice is for ILECs to sell the subscriber list information that they collect from CLECs third party DPs that request it. Indeed, I know of no case in which a CLEC bypasses the ILEC DL function and provides listing information to DPs directly, and no DP has ever asked Comcast for its

[17] Arbitration Decision, *Sprint Communications L.P. d/b/a Sprint Communications Co. L.P.* Dkt. No. 05-0402 (Illinois Commerce Commission Nov. 8, 2005) (available at 2005 WL 3710228 (Ill.C.C.)).

[18] *Id.* at Westlaw printout page 17.

[19] *See* Embarq General Exchange Tariff, Docket No. UT-070955, at Schedule AE-3, Original Sheet 2 (eff. May 16, 2007).

customers' subscriber list information. (For that reason, I am not concerned by Mr. Lubeck's taking Comcast to task (at page 7 of his Direct Testimony) for not establishing the capability to fulfill requests from directory publishers. Since no DP has ever requested such information, it would be a waste of resources for Comcast to attempt to develop such a capability.)

It is also undisputed that Embarq currently sells Comcast's customers' subscriber list information to DPs that request it at the FCC approved "Section 222(e) rate" of $0.04 per listing / $0.06 per update.

At no point during the parties' negotiations did Embarq seek interconnection language to alter this arrangement. To the contrary, when negotiations began, Embarq proposed only to delete the language in the parties' current interconnection agreement which provides that, "[Embarq] shall not charge for storage of CLEC subscriber information in the DL systems,"[20] and to replace it with the following:

> The charge for storage of CLEC subscriber information in the DL systems is included in the rates where CLEC is buying UNE Loops or resold services with respect to specific addresses. CLECs that are not buying UNE Loops or resold services shall pay for such storage services at the rate reflected on Table One [*i.e.,* $0.50 per listing per month]."[21]

[20] Master Interconnection and Collocation Agreement for the State of Washington between Comcast Phone of Washington, LLC and United Telephone Company of the Northwest, § 70.2.5 (emphasis added), approved by the Washington Utilities and Transportation Commission in Docket No. UT-053035.

[21] Embarq Response to Petition, Exhibit 1 (proposed § 71.2.5).

Comcast, of course, questioned the appropriateness of the proposed rate. How could Embarq seek $0.50 per month per listing to "store" directory listing ("DL") information when the cost of such computer storage is essentially zero, especially given that Comcast had agreed to the DL service order entry charge of $9.41 that Embarq proposed. The clearly discriminatory, unjust and unreasonable nature of the DLSM charge led Comcast to initiate this proceeding.

It was not until Embarq responded to Comcast's discovery requests that Embarq explained that this so-called "storage charge" was really for activities associated with directory publishing, not "storing" information in Embarq's databases. Comcast was still not persuaded, however, because (1) the FCC has ruled that carriers are to recover such costs from the DPs to whom listings are sold, (2) the FCC has established a mechanism for carriers to pursue if they believe those rates to be confiscatory, (3) most of the activities that Embarq identified as associated with the proposed charge are clearly not appropriately charged-back to Comcast under ***any*** circumstance, as I explained in my direct testimony (at 18-20), and (4) contract terms the parties have already agreed to preclude these additional charges.

Q. HOW DOES EMBARQ JUSTIFY THE PROPOSED DLSM CHARGE TODAY?

A. It appears to me that Embarq has modified its position yet again, claiming that its ***real*** objective is to stop serving as a "clearinghouse" for Comcast subscriber list

information.[22] When Embarq refers to the "clearinghouse" function, it means that it does not want to sell Comcast's subscriber list information to third party DPs that request it – unless, of course, Comcast pays the DLSM charge. Embarq claims that it serves as a clearinghouse ***whenever*** it sells Comcast listing information to a DP – including Donnelley, the company that publishes Embarq-branded directories on Embarq's behalf.

In other words, Embarq claims that when it sold its publishing business to Donnelley, it divested itself of its Section 251(b)(3) obligation to "plac[e] … [Comcast's] listing information in a directory assistance database or in a directory compilation for external use (such as a white pages)," which is what the FCC has said Section 251(b)(3) requires LECs to do.[23]

Q. WHAT ELSE STRIKES YOU ABOUT MR. LUBECK'S CLEARINGHOUSE ARGUMENTS?

A. I just do not see how they are relevant to this case. Comcast's request in this proceeding is based on its right as a LEC, under Section 251(b)(3), to have "nondiscriminatory access" to Embarq's DL function, which includes the right to have its subscriber listing information placed into Embarq's databases and published in Embarq-branded directories on the same rates, terms and conditions as it and other CLECs enjoy.

[22] *See, e.g.*, Lubeck Direct, ALL-1T, p. 10 and pp. 11-12.

[23] Direct Testimony of Timothy J Gates, on behalf of Comcast, Docket No. UT-083025, July 2, 2008 ("Gates Direct"), p. 10.

Embarq's "clearinghouse" arguments, on the other hand, are related to its obligation under a different statute, Section 222(e), to sell subscriber list information to third party DPs that request it. As I explained at length in my Direct Testimony, it is established industry practice for ILECs to serve as the central repository for all listing information in a given service territory. ILECs profit from performing this role both because CLECs pay a handsome sum ($9.41 per listing) to place that information in ILEC databases, which orders they are required to accept pursuant to Section 251(b)(3). There would be no economically rational ground for an ILEC to stop performing this function, and I believe that Comcast – not to mention the third-party DPs that rely on this information – would be quite concerned if, at some point in the future Embarq took the position that it was not willing to sell Comcast listing information unless Comcast paid an additional charge. That said, however, Comcast's request in this proceeding is under Section 251(b)(3) – not Section 222(e) – so all these clearinghouse arguments Embarq has raised are simply irrelevant.

Q. HOW DOES SECTION 222(e) BEAR ON THE QUESTION OF PRICING UNDER SECTION 251(B)(3)?

A. In my direct testimony (at 9-11 and 34-35), I noted the connection between Section 251(b)(3) and Section 222(e). Both sections are aimed at ameliorating the anticompetitive bottleneck that LEC control of DL information poses to the development of competition. Section 251(b)(3) requires that all LECs provide one another with non-discriminatory access to DLs, while Section 222(e) "requires carriers that provide telephone exchange service to provide subscriber

list information to requesting directory publishers 'on a timely and unbundled basis, under nondiscriminatory and reasonable rates, terms, and conditions."[24]

While, as I have noted, Comcast's claims here are not based on Section 222(e), a consideration of how the FCC chose to set rates under Section 222(e) is, thus, relevant for several different reasons. One of the early questions the FCC faced was how to implement the "reasonable rate" requirement of Section 222(e). As I recount in my direct testimony (at 34-35), some LECs argued that they should be allowed to charge DPs "value-based" rates for the DL information stored in their DL databases, which is exactly Embarq's proposal here.

The FCC, however, found that LECs should only be allowed to charge for the actual cost of providing the service, which the FCC estimated was $0.04 per listing and $0.06 for updates to a listing. As the FCC explained, "basing rates on costs should promote the development of a competitive directory publishing market, while fairly compensating carriers for the subscriber list information they provide directory publishers."[25]

This history explains why rates under Section 251(b)(3) must be cost-based, as well. It would be anomalous to allow a LEC to charge a so-called "value based" rate of $0.50 per month per listing to have their customers' DL information stored in the same database that DPs only pay $0.04 per listing to access. It also

[24] *SLI/DA Order*, ¶1.

[25] *SLI/DA Order*, ¶ 87, n.207. I would note that because telecommunications is a decreasing cost industry, if the $0.04 and $0.06 rates were compensatory in 1999, they are providing even more profit nine years later.

provides a definitive rebuttal to Embarq's claim that cost-based rates are the same as TELRIC-based rates, and to its claim that Congress' decision not to require that a LEC's DL function be priced at TELRIC means that DL rates can be set without respect to cost considerations.

Q. IS IT RELEVANT THAT THE DIRECTORY LISTING FUNCTION IS NOT AN UNBUNDLED NETWORK ELEMENT THAT ILECS MUST SELL AT TELRIC?

A. No. The TELRIC pricing standard applies to UNEs that ILECs must "unbundle" pursuant to Section 251(c)(3). The FCC never ordered the "unbundling" of the ILEC DL function and, therefore, could not have subjected it to TELRIC pricing. But that does not mean that ILECs can charge whatever they want to for DLSM. Note that Section 251(b) obligations apply to ***all*** LECs, while Section 251(c) obligations only to ILECs. It was unnecessary for the FCC to order the unbundling of ILECs' DLSM function because Section 251(b)(3) already explicitly mandates that ILECs provide CLECs with "nondiscriminatory access." Since it would be absurd to think that ILECs would charge themselves or their retail customers for this function, the FCC reasonably took the view that no specific pricing rules were necessary.

Moreover, TELRIC is not the only cost-based pricing methodology found in the telecommunications regulatory arena. One need look no further than the rate the FCC set for implementing Section 222(e), which is based on the actual costs

ILECs incur.[26] Thus, to the extent that Embarq did attempt to impose a non-discriminatory charge for its DLSM function – which, by definition would have to be imposed on ***all*** of its customers, end-users and CLECs alike – it would be bound to base that charge on its costs, not the perceived "value" of the service.[27]

IV. EMBARQ'S "MARKET" FACTS AND ARGUMENTS ARE WRONG

Q. WHAT IS THE BASIS FOR EMBARQ'S POSITION THAT IT MAY CHARGE NON-COST-BASED RATES?

A. As noted above, Mr. Lubeck states that the DLSM charge is justified because Embarq sold off its directory publishing business and no longer "controls access" to third-party publishers.[28] As a consequence of this divestiture, Mr. Lubeck claims that Embarq is no longer bound by Section 251(b)(3); is, therefore, not required to provide a directory listing service; and should, therefore, be permitted to charge a "non cost-based rate" if it chooses to do so.[29] Embarq's proposal is based on a policy argument that has no basis in fact or even sound business practice. (It is also prohibited by law – but that is a separate consideration.)

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[26] TELRIC, on the other hand, is based on the hypothetical, forward-looking costs that a new entrant would incur if it re-built the ILEC network from scratch using the most efficient technologies currently available.

[27] In addition to being non-discriminatory, Embarq would still have to prove that its proposed charge was "just and reasonable." Given that Embarq almost certainly already recovers its costs many times over (see my direct testimony at 15-17), it is highly unlikely that it would be permitted to impose any DLSM charge.

[28] Lubeck Direct, ALL-1T, p. 9, line 19; p. 13, lines 20-21; p. 14, line 10; p. 17, line 18; and p. 21, line 15.

[29] *See, e.g.,* Lubeck Direct, ALL-1T, p. 13, lines 19-20.

Q. MR. LUBECK CLAIMS THAT CLECS LIKE COMCAST *COULD* DEAL WITH DPs DIRECTLY. IS THAT CLAIM ENOUGH?

A. No. At pages 16-17 of his direct testimony, Mr. Lubeck claims that he has confirmed that Comcast could deal with Donnelley directly. It remains undisputed that there is no evidence in the record of this proceeding that any CLEC anywhere in the country actually bypasses the local ILEC's DL database and provides subscriber list information directly to third-party DPs. As I explained in my direct testimony (at 11-12), ILECs remain the sole repository for this information, and, thus, retain the "total control" over subscriber list information. In fact, Mr. Lubeck's repeated assertion that Embarq does not "control" access to directory publishers, including Donnelley, is entirely irrelevant. Rather, the question of "control" as it pertains to 251(b)(3) is whether Embarq maintains "control" over the subscriber listing information contained in its database. Allowing Embarq to impose a discriminatory charge on Comcast subscribers, but not on its own subscribers, would, in turn, grant Embarq "control" over the manner in which Comcast subscribers are published in Embarq's directory. This is exactly the type of bottleneck function that has not and will not go away even though there is entry and competition in the local exchange market, and even though some of the competitors, such as Comcast, are completely facilities-based. Indeed, this is exactly why Congress enacted Sections 222(e) and 251(b)(3) in the first place – to remove the ability of an ILEC, as the sole repository of subscriber listing information, to "control" those

listings by dictating the terms and conditions by which a particular subscriber is published in Embarq's directory.

Moreover, even if it was possible for Comcast to one day do what Embarq suggests, that would still not satisfy Embarq's burden of proof in ***this*** proceeding. Embarq must support its proposed rates,[30] and its DLSM rate proposal is predicated on the supposed existence of a "market alternative" to its own DLSM function. Absent concrete evidence of such a market, Embarq fails to satisfy its burden of proof.

Q CAN YOU GIVE AN EXAMPLE OF WHERE THE FCC HAS MADE AN ANALOGOUS RULING?

A. Yes. The FCC's recent ruling denying Verizon's request for forbearance from various dominant carrier and unbundling obligations in six northeast markets is similar.[31] In that proceeding, Verizon petitioned the FCC to "forbear" from enforcing regulations that, among other things, impose a variety of wholesale service obligations on Verizon. Verizon argued that forbearance was appropriate based on the contention that the presence of retail-level competition justified easing the extent of its wholesale obligations.[32]

[30] Including compliance with Section 251(b)(3) and other legal requirements.

[31] *See Petitions of the Verizon Telephone Companies for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Boston, New York, Philadelphia, Pittsburgh, Providence and Virginia Beach Metropolitan Statistical Areas,* Memorandum Opinion and Order, WC Docket No. 06-172 (Dec. 5, 2007) ("Verizon 6-Market Forbearance Order").

[32] *Id.* ¶ 27.

The FCC found that the competitors' market share was nowhere near sufficient to justify the withdrawal of the competition-promoting, wholesale service requirements that Verizon sought.[33] And the FCC expressly refused to forbear based on the ***potential*** that competition might emerge in the future.[34] Just this week, the FCC made a substantively identical ruling with respect to a forbearance request filed by Qwest.[35] As these rulings make clear, the FCC will not grant a forbearance request without evidence of ***actual*** competition. Thus, even if the Commission could forebear from applying Section 251(b)(3) in this case – which it can't – it would not have sufficient grounds to do so.

Embarq's request here is very similar, and the result should be the same. For all intents and purposes, Embarq is asking this Commission to forebear from enforcing Section 251(b)(3) because, it claims, the ***possibility*** of competition is such that the Commission can rely on market forces rather than regulation to maximize public welfare. Embarq has not presented any evidence of competitive alternatives for its DLSM services, and the speculative possibility that market alternatives might emerge is simply not enough.[36]

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[33] *Id.* ¶ 36.

[34] *Id.* (discounting the significance of Verizon's showing that cable competitors had deployed facilities to 75% of end-user customers in some market territories, and thus ***could*** compete with Verizon for those customers' business, although they had not yet succeeded in winning the business).

[35] *See In the Matter of Petitions of Qwest Corporation for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Denver, Minneapolis-St. Paul, Phoenix, and Seattle Metropolitan Statistical Areas*, Memorandum Opinion and Order, FCC 08-174 (rel. July 25, 2008).

[36] The FCC's promulgation of rates under Section 222(e) is another good example which is obviously directly related to the issues in this proceeding. The FCC rejected there, "the idea that incumbent LECs be allowed to charge either whatever they want or value-based prices for

Finally, Embarq's citation to situations in which state commissions have relaxed ILEC retail rate regulation is simply inapt. While Mr. Lubeck's testimony does not include much in the way of discussion as to why those cases are applicable here, the state commissions in those cases presumably relied on the presence of actual competition in reaching their respective decisions. Such competition is simply not present here. More importantly, the Commission's state law authority to relax regulation of local, purely intrastate retail services, does not extend to its wholesale local competition rights and responsibilities arising under the federal Communications Act.

V. EMBARQ'S ECONOMIC ANALYSIS IS FLAWED

Q. DO YOU AGREE WITH MR. LUBECK'S ECONOMIC ANALYSIS?

A. No. The main problem with Mr. Lubeck's economic testimony is that it assumes the presence of competitive market which is unsupported by the record facts. Embarq cannot point to a single CLEC that bypasses an ILECs' DL function anywhere in the country. There is, thus, no proof that there is a market for the DL listing function for which Embarq proposes to charge Comcast in this proceeding.

Q. BUT MR. LUBECK SAYS THAT COMCAST HAS THE OPTION OF DEALING DIRECTLY WITH R.H. DONNELLEY. IS THAT PROOF OF AN ALTERNATIVE?

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subscriber list information. Congress enacted section 222(e) to correct a perceived failure in the market for subscriber list information. All directory publishers require timely and complete access to accurate subscriber list information in order to compete effectively." *SLI/DA Order* ¶ 84. The "perceived failure" that the FCC was discussing was the ILEC's "total control" over subscriber list information and the potential for unfair LEC practices that Congress identified. *Id.*

A. No. In economics when one speaks of alternatives in the market it is in terms of buyers and sellers. But there is no evidence that Donnelley would be interested in purchasing subscriber list information from Comcast, and every reason to believe it would not be interested in doing so. Donnelley publishes white pages directories as an adjunct to its yellow pages business. Businesses pay to publish advertisements in yellow pages, but there is no similar revenue stream from white pages publications. Thus, Donnelley has no real incentive to pursue Comcast's (or other CLECs') listing information. It publishes CLECs' listings today because Embarq provides the information and there is no additional expense involved.

Moreover, Mr. Lubeck has not identified another provider (other than Embarq) that can store and maintain Comcast's listings for use in publishing directories for Embarq's service territories. Suggesting that Comcast can do it completely disregards the logistical problems that I discussed in my direct testimony.[37] This is similar to suggesting that the power company can price power to me at any price because I have the option of generating and transmitting my own power. While this may be true from a theoretical perspective, the proposal fails when reality and resources are considered.[38]

Q. PLEASE CONTINUE YOUR REVIEW OF MR. LUBECK'S ECONOMIC "ANALYSIS".

[37] *See* Gates Direct at 28-30.

[38] Unlike Embarq, Comcast has not had decades of monopoly heritage under which it could purchase, engineer and deploy the systems necessary to receive and manage the subscriber list information.

A. Mr. Lubeck begins his analysis (at 18) by explaining that individual producers in a market do not always set prices for goods and services based on the cost of production. While it is certainly true that individual producers will seek to set prices in excess of costs, competition typically constrains them from doing so for long, if at all. Microeconomics teaches that the individual firm operating in a competitive market is a "price taker" who is simply confronted with a market price for the firm's product. If the firm can produce the product at less than the market price, it will do so, and will profit accordingly. If not, then it won't. And even if the firm has some unique asset (*e.g.*, a farmer with better land) and can produce some quantity of output at lower cost, its pricing will still be constrained by pressure from potential competitors.

But it is important not to confuse an ***individual*** firm's supply or demand curve with that of the ***market*** as a whole. This is precisely the mistake that Mr. Lubeck makes with his hypothetical. In a competitive market, prices will converge to cost, and Mr. Lubeck is simply wrong to suggest otherwise.[39] In a competitive market, high cost, less efficient producers are weeded out as lower-cost, more efficient producers win market share. The whole point of regulation is to step in when effective competition is not present in a given market and to attempt to reproduce the efficiency-enhancing effect of competition. This explains why regulators almost always attempt to set rates based on some measure of cost,

[39] *See, e.g.,* United States Department of Justice and Federal Trade Commission, *Horizontal Merger Guidelines*, 1992, Revised 1997, Section 0.1 ("The unifying theme of the Guidelines is that mergers should not be permitted to create or enhance market power or to facilitate its exercise. Market power to a seller is the ability profitably to maintain prices above competitive levels for a significant period of time").

because that is where prices trend to in a competitive market. The examples in the communications regulatory arena are many and varied. I cite a few illustrative examples in the footnote below.[40]

Microeconomics also teaches that only in markets where competition is limited and entry is not possible or very costly will a producer/supplier be able to sustain above-cost prices in the long-run as in the case presented by Mr. Lubeck (on pages 18-19 of his testimony). Vendor Y, which Mr. Lubeck posits can produce product at $0.60 per unit and whose only competition's $1.00 per unit cost structure is much higher will, indeed, win the entire market if it sets its price at $0.99.

But in a competitive market that would only be true in the short run, because Vendor Y would soon be subject to competition from Vendor Z, which can produce at comparable cost and will put price pressure on Vendor Y. In a

[40] *See Local Competition Order*, 11 FCC Rcd 15499, ¶ 8 (1996) ("It is widely recognized that, ***because a competitive market drives prices to cost***, a system of charges which includes non-cost based components is inherently unstable and unsustainable") (emphasis added); *INFOXX, Inc. v. New York Telephone Co.*, Memorandum Opinion and Order, File No. E-96-26 (released October 10, 1997) at ¶ 15 ("[C]osts are traditionally and naturally a benchmark for evaluating the reasonableness of rates under Section 201(b) of the Act"); In the Matter of International Settlements, Policy Reform International Settlement Rates, IB Docket Nos. 02-324 and 96-261, *First Report and Order* (released March 30, 2004) at ¶ 74 ("The Commission determined that above-cost settlement rates paid by U.S. carriers to terminate international traffic are neither just nor reasonable, and it acted pursuant to its statutory authority in Section 201(b) of the Communications Act to prohibit U.S. carriers from continuing to pay such charges"); *In the Matter of Access Charge Reform, Price Cap Performance Review of Local Exchange Carriers, Transport Rate Structure*, CC Docket Nos. 96-262, 94-1 and 91-213, Second Order on Reconsideration and Memorandum Opinion and Order (released October 9, 1997) at ¶ 44 ("In reviewing the Commission's interim transport rate structure, the United States Court of Appeals for the District of Columbia Circuit (D.C. Circuit) found that the just and reasonable rates required by Sections 201 and 202 of the Communications Act must ordinarily be cost-based, absent a clear explanation of the Commission's reasons for a departure from cost based ratemaking").

competitive market, that is what inevitably occurs. Only in structurally non-competitive markets, where economies of scale or scope, network effects, exclusive rights, or other factors, prevent efficient competitors from entering the market and driving price toward cost, can suppliers charge above-cost prices in the long-run. This market monopoly is exactly what Mr. Lubeck presents in his depiction of Vendor Y's long-run success, which is an obviously poor choice in light of his claims that Embarq does not have monopoly power with regard to directory listing rates.

Monopoly market power is also presented in the charts on page 18 of Mr. Lubeck's direct testimony. Only a firm with significant market power will be able to maintain prices far in excess of marginal cost. The following chart, which is taken from a recent presentation given by the Assistant Attorney General for the Antitrust Division of the U.S. Department of Justice, provides a graphic illustration of the difference between pricing and production in monopoly versus competitive markets:

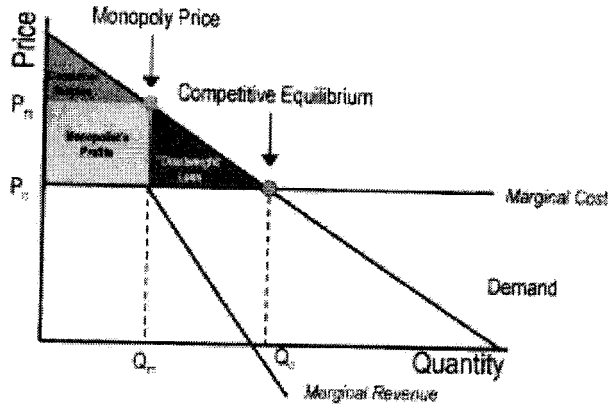

Illustration:
Monopoly Pricing Superimposed Over The Economic Demand Curve[41]

Note that this chart is essentially the same as Mr. Lubeck's, and shows that, in monopoly market conditions, the monopolist sets the "Monopoly Price" at the point where its cost curve intersects with its marginal revenue curve. Assistant Attorney General Barnett describes it this way: "This graph demonstrates that such monopoly pricing, as opposed to competitive pricing, can result in a higher price and a smaller area of consumer surplus. A portion of consumer surplus is transferred to the monopolist, and another portion is simply lost – this lost portion is labeled 'deadweight loss.'"[42] This "dead weight loss" is why public policy often calls for the regulation of monopoly markets, and explains why Congress enacted Sections 251(b)(3) and 222(e). While I know he did not mean to, Mr. Lubeck proves this very point in his testimony.

Q. SO WHAT DOES ALL THIS MEAN FOR THIS CASE?

[41] Thomas O. Barnett, *Maximizing Welfare Through Technological Innovation* (Presentation to the George Mason University Law Review 11th Annual Symposium on Antitrust Oct. 31, 2007) (available at: http://www.usdoj.gov/atr/public/speeches/227291.htm#img2).

[42] *Id.* (hyperlink note: http://www.usdoj.gov/atr/public/speeches/227291/2.htm).

A. The economic analysis that Mr. Lubeck provides is incorrect and the Commission should ignore the flawed conclusions that result from it. Perhaps more importantly, Embarq has failed to show that a competitive market exists for the DLSM offering.

Q. IS MR. LUBECK'S DISCUSSION OF THE COX/YELLOW BOOK CO-MARKETING AND DISTRIBUTION AGREEMENT RELEVANT TO THIS ISSUE?

A. No. Mr. Lubeck's reference (at 16) to a recent announcement that Cox and Yellow Book plan to co-market and distribute commercial directories has no bearing on this case. As the press release explains, Cox and Yellow Book plan to "promote each other's products and services through a variety of sales and marketing channels" and "publication of Yellow Book directories that will include Cox branding and product information…" As the press release indicates: this is a "co-marketing and distribution agreement." It does not involve residential subscriber listings,[43] has nothing to do with access to directory listings, and as such, would not involve any of the issues I've identified in my testimony.

Q. DOES THIS CONCLUDE YOUR REPLY TESTIMONY?

A. Yes.

[43] Yellow Book publishes only commercial directories. *See* http://corporate.yellowbook.com/faqs/.