Ex. T- _____ (GB-T)
Docket No. UT-981367
Witness: Glenn Blackmon

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In re Application of GTE CORPORATION and BELL ATLANTIC CORPORATION for an Order Disclaiming Jurisdiction, or in the Alternative, Approving the GTE CORPORATION -- BELL ATLANTIC CORPORATION Merger	)	DOCKET NO. UT-981367

TESTIMONY OF

GLENN BLACKMON

STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

AUGUST 2, 1999

Q. PLEASE STATE YOUR NAME AND QUALIFICATIONS TO PROVIDE TESTIMONY IN THESE PROCEEDINGS.

A. I am the Assistant Director for Telecommunications for the Washington Utilities and Transportation Commission (Commission). I hold Ph.D. and master's degrees in public policy from Harvard University and a bachelor's degree in economics from Louisiana State University. I have been employed at the Commission since August 1995 and assumed my current position in April 1996. I previously served as the Commission's economics advisor in the interconnection case, UT-941464, and the U S WEST general rate case, UT-950200. Prior to working at the Commission, I was a consultant in private practice, where my clients included both regulated companies and consumer advocates, and an analyst for the Washington State Senate Energy and Utilities Committee. I have presented testimony as an expert witness before this Commission, as well as the Illinois and Idaho commissions. I am the author of a book, *Incentive Regulation and the Regulation of Incentives* (Boston: Kluwer Academic Publishers, 1994). I have authored or co-authored articles on utility regulation and economic theory published in *American Economic Review*, *Journal of Regulatory Economics*, *Yale Journal on Regulation*, *Journal of Risk and Uncertainty*, and *Public Utilities Fortnightly*.

Need for Conditions to Mitigate Competitive and Consumer Harms

Q. IS THE MERGER OF GTE AND BELL ATLANTIC, ON THE TERMS PROPOSED IN THE APPLICATION, EITHER IN THE PUBLIC INTEREST OR RESULTING IN NO HARM TO THE PUBLIC?

A. No. In the absence of conditions or requirements on the applicants, the merger itself would be harmful to the public interest. It would be harmful to competition and to consumers.

Q. PLEASE EXPLAIN HOW THE MERGER HARMS THE PUBLIC INTEREST.

A. Bell Atlantic and GTE are both incumbent local exchange companies that each have, within their respective service areas, substantial market power. State and federal policy makers have adopted a pro-competitive policy toward the telecommunications industry, and this merger generally runs counter to the public policy direction of increasing competition. The merger of Bell Atlantic and GTE reduces the expected level of competition that would obtain in the areas served by GTE-NW. Had the two companies not merged, they might well have competed for the customers currently being served by GTE-NW. That competition would have brought benefits to customers in the form of lower prices, new products, and better service.

In addition, the merger could adversely affect the pace of competition in the areas of Washington where U S WEST is the incumbent local exchange company. The rivalry between General Telephone and the Bell Operating Companies long predates the Telecommunications Act of 1996, and in the absence of this merger, it is reasonable to expect that GTE would compete against U S WEST. Washington state has already seen some effects of this, such as GTE-NW's provision of local service to the University of Washington's Seattle campus and the entry of GTE Communications Corporation as a competitive local exchange company. It is not a given that Bell Atlantic's control will reduce that rivalry with U S WEST, but it is certainly a concern to Staff that Bell Atlantic and U S WEST may cooperate rather than compete.

In summary, without the conditions recommended by Staff, the merger would cause customers to be harmed. In other words, they would be worse off with the merger than they would have been without the merger.

Q. YOU ASSERT THAT THE MERGER REDUCES THE NUMBER OF POTENTIAL COMPETITORS, BUT COULDN'T THE MERGER ALSO MAKE BELL ATLANTIC INTO A STRONGER COMPETITOR AGAINST OTHER INCUMBENTS SUCH AS U S WEST?

A. There are probably some mergers that increase competition by creating a more financially or technically viable firm, particularly where neither of the merging firms had significant market power. However, that is far from the case here. Measured by market capitalization, GTE is already more than twice the size of U S WEST, and Bell Atlantic is more than three times the size of U S WEST. Each is already more than capable of obtaining the resources necessary to compete against U S WEST and every other incumbent local exchange company.

Q. IS THE HARM TO COMPETITION AND THE PUBLIC INTEREST CAPTURED IN THE APPLICANTS' ESTIMATES OF MERGER SAVINGS AND EFFICIENCIES?

A. No. The applicants have merely estimated the benefits that they will enjoy if their merger is approved, though as Ms. Folsom notes, they appear to have omitted the substantial "revenue synergies" that the larger company acknowledges it would realize. The lost benefits, i.e, the benefits that consumers would have enjoyed with greater competition, are not accounted for at all.

Q. HOW DOES STAFF PROPOSE THAT THE COMMISSION MITIGATE THE HARM TO THE PUBLIC INTEREST OF THIS MERGER?

A. Staff recommends that the harm be mitigated by establishing a offsetting benefits to competition and to consumers. The offset for competition is to require a more open competitive access to GTE-NW's incumbent local exchange network than GTE would likely have provided without the merger. The offset for consumers is a "consumer dividend," i.e., to require that the full Washington intrastate share of estimated merger benefits be flowed through to Washington intrastate customers.

Access to Competitive Services

Q. PLEASE EXPLAIN STAFF'S RECOMMENDED CONDITION ON PROVISION OF WHOLESALE SERVICES.

A. Staff recommends that GTE-NW provide "operations support system" (OSS) functions, including pre-ordering, ordering, provisioning, maintenance and repair, and billing, to its local exchange competitors that are comparable in quality to those provided by Bell Atlantic in other jurisdictions.

Q. WHY IS THERE A CONCERN THAT GTE COULD END UP WITH INFERIOR ACCESS TO COMPETITIVE SERVICES?

A. The concern arises because of the difference in Bell Atlantic's status as a "regional Bell operating company" under federal law and the more favorable treatment afforded GTE under federal law. GTE and Bell Atlantic are both incumbent local exchange companies as defined in Sec. 251 of the Telecommunications Act of 1996, and both are subject to the duties imposed on incumbent local exchange companies by that law and Sec. 252. However, Bell Atlantic is subject to the "competitive checklist" requirements of Sec. 271 while GTE arguably is not.[1] Bell Atlantic must demonstrate to state commissions, the U.S. Department of Justice, and the FCC that it complies with the competitive checklist requirements before it is permitted to provide in-region interLATA long distance service. While GTE ostensibly must comply with the same market-opening requirements under Sec. 251, it does not have to demonstrate compliance to regulators before it can provide interLATA service. Indeed, GTE has been providing in-region interLATA long distance service since shortly after the passage of the 1996 Telecommunications Act without meeting the requirements of Sec. 271.

[1]Whether the merger causes GTE to become subject to Sec. 271 will likely be decided by the Federal Communications Commission and ultimately by the courts. For the purposes of this proceeding, Staff assumes that GTE will not be subject to Sec. 271 in Washington state.

The concern, therefore, is that after the merger Bell Atlantic would take the steps necessary to secure 271 approval but would do so only for legacy Bell Atlantic areas. It would provide better competitive access in legacy Bell Atlantic areas, where it faces Sec. 271 requirements, than it does in legacy GTE areas such as Washington, where only Secs. 251 and 252 apply. Staff believes that Bell Atlantic's Washington state customers should not have second-class access to competitive services. To prevent that possibility, Staff recommends that the merged entity be required to provide competitive access in Washington state that is comparable to the competitive access provided in legacy Bell Atlantic states.

Q. WHY WOULD GTE-NW CUSTOMERS BE HARMED IF AN INADEQUATE OSS IS PROVIDED TO LOCAL COMPETITORS IN WASHINGTON STATE?

A. For a competitive telecommunications environment to succeed, it is essential that competitors receive non-discriminatory access to incumbents' networks. A competitive carrier does not really have that access if it cannot use pre-ordering functions to check the availability of facilities, cannot place orders and confirm due dates, cannot check the status of pending orders, cannot respond to trouble reports and repair requests, or cannot collect the information necessary to render bills on the same time intervals and with the same level of accuracy as the incumbents themselves.

Q. WHY SHOULD OSS ISSUES BE ADDRESSED IN THIS MERGER CASE, RATHER THAN IN A RULEMAKING SUCH AS IS CURRENTLY UNDERWAY IN DOCKET NO. UT-990261?

A. It is not yet clear whether general industry rules on carrier-to-carrier service quality will be pursued by the Commission. If they are, they almost certainly would address parity between wholesale and retail services and parity among competitive local exchange companies. In other words, the rules would require that (1) Bell Atlantic provide service to its competitors that was at least as good as service provided to itself and (2) Bell Atlantic provide comparable service to each competitor. Those rules would probably not address the issue of concern here, which is that Bell Atlantic might provide inferior service to all Washington customers – both retail and wholesale – than it provides to customers in legacy Bell Atlantic areas.

Moreover, OSS should be addressed in the merger because it can help mitigate the overall negative effect that this merger has on competition. In general, consumers would be better off to have GTE and Bell Atlantic as separate entities competing for their telecommunications business. That harm can be mitigated somewhat if GTE-NW's customers end up with better competitive access than they would have had in the absence of this merger.

Q. IS STAFF RECOMMENDING THAT GTE-NW BE SUBJECT TO SEC. 271 OR A SIMILAR "COMPETITIVE CHECKLIST" REQUIREMENT?

A. No. That issue should be decided at the federal level. Staff's recommendation is that, as a condition of approval of the merger, Bell Atlantic be required to provide comparable competitive access. The company would not be required to demonstrate compliance before the fact. Instead, this would establish a standard against which GTE-NW's performance could be measured in the future. This standard would not entail any particular level of service but would merely require that Washington customers be treated comparably to those in legacy Bell Atlantic areas. Bell Atlantic can readily comply with this condition if it uses whatever OSS platform it develops to meet Sec. 271 requirements in legacy Bell Atlantic areas to provide the same services to competitors in Washington state. An alternative approach would be for Bell Atlantic to continue using the GTE OSS platform but make the same improvements to it that are currently being made to the Bell Atlantic platform.

Flow-through of Merger Cost Savings and Revenue Increases

Q. DOES THE LEVEL OF MERGER SAVINGS, INCLUDING ESTIMATED EXPENSE REDUCTIONS, CAPITAL SYNERGIES, AND REVENUE SYNERGIES, EXACTLY MATCH THE LEVEL OF BENEFITS THAT GTE-NW CUSTOMERS COULD HAVE EXPECTED FROM COMPETITION IN THE ABSENCE OF THE MERGER?

A. Probably not. It is not possible to measure the impact of competition -- or the prospect of competition -- from Bell Atlantic on the benefits that GTE-NW customers may have enjoyed. The competitive benefits arguably could have been greater or less than the merger savings amount identified by the companies.

Moreover, the merger savings amount itself is at best an estimate. The merged company may well experience greater revenue growth or efficiency gains than they have identified in this proceeding. The merged entity will be a very large incumbent local exchange company with a substantial national presence. The opportunities to exert market power will likely produce financial benefits that extend well beyond the modest three-year period for which the applicants have provided estimates.

Q. GIVEN THIS UNCERTAINTY ABOUT BOTH THE FINANCIAL GAINS OF THE MERGING COMPANIES AND THE FOREGONE COMPETITION BENEFITS TO CONSUMERS, HOW SHOULD THE COMMISSION PROCEED TO ESTABLISH A CONSUMER DIVIDEND AMOUNT?

A. While neither the competitive benefits without a merger nor the merger savings amount can be calculated exactly, it is clear that the merger cannot meet the "no harm" standard unless savings are flowed through to customers. Staff recommends that the Commission recognize the general negative public interest effects of this merger by requiring that the merged company flow through the full amount of merger savings -- including the revenue synergies not yet quantified by the applicants -- in the form of a consumer dividend.[2]

Conclusion

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes, it does.

[2]As Ms. Folsom notes, the applicants have not yet provided a complete estimate of the merger savings and synergies. A rough estimate by Staff is $12.6 million when revenue synergies are included. This amount is about 3% of GTE-NW's intrastate operating revenue. It represents only the merger benefits that result from regulated operations within the State of Washington. It does not include any extra revenues or expense savings from the applicants' unregulated lines of business.