

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION
COMMISSION

In the Matter of the Petition of

QWEST CORPORATION

For Competitive Classification of
Basic Business Exchange
Telecommunications Services.

Docket No. UT-030614

THE UNITED STATES DEPARTMENT
OF DEFENSE AND ALL OTHER
FEDERAL EXECUTIVE AGENCIES'

INITIAL BRIEF

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OF

THE UNITED STATES DEPARTMENT OF DEFENSE AND
ALL OTHER FEDERAL EXECUTIVE AGENCIES

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TABLE OF CONTENTS

	Page
I. INTRODUCTION	1
II. APPLICABLE LAW	6
III. DEFINITION OF RELEVANT MARKET	9
A. Definition of Product Market	9
B. Definition of Geographic Market	15
IV. REVIEW OF STATUTORY FACTORS FOR EVALUATING EFFECTIVE COMPETITION	18
A. Number and Size of Alternative Providers of Service	18
B. Extent to Which Services are Available from Alternative Providers in the Relevant Market	21
C. The Ability of Alternative Providers to Make Functionally Equivalent or Substitute Services Readily Available	24
1. Wholesale-based Services (resale; UNE-P; UNE-L)	24
2. CLEC-owned Loops	25
3. Intermodal (wireless, VOIP, Wi Fi, cable, etc.)	26
D. Other Indicators of Market Power	30
1. Market Share Analysis	30
2. Market Concentration Analysis	34
3. Ease of Entry	36
4. Affiliation of Providers of Service	38
5. Other – Relevance of Section 271 Approval	39
E. Significant Captive Customer Base	42
V. OTHER ISSUES	44
A. Impact of Other Dockets	44
B. Cost Floor	47
C. Access Charges	49
D. Proposed Conditions on Approval	49
VI. CONCLUSION	50
VII. CONFIDENTIAL ATTACHMENT	

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I. INTRODUCTION

The Secretary of Defense, through duly authorized counsel, on behalf of the customer interests of the United States Department of Defense and All Other Federal Executive Agencies (collectively referred to herein as "DoD/FEA"), hereby submits its Initial Brief in the above-captioned proceeding.¹ For the reasons set forth herein, DoD/FEA recommends that the Washington Utilities and Transportation Commission ("the Commission") deny the petition filed by Qwest Corporation ("Qwest") on May 1, 2003 ("the Petition"), in which it seeks reclassification of its analog basic business exchange telecommunications services throughout the state as competitive, pursuant to RCW 80.36.330 and WAC 480-121-062.

DoD/FEA's interest in this matter is based on its purchase of large quantities of telecommunications services provided by Qwest throughout the state of Washington.

¹ In this Initial Brief, DoD/FEA will focus on major issues. Our failure to address an issue or position does not necessarily indicate agreement with any party's position thereon. We wish to avoid burdening the already voluminous record with information that is more fully developed by other parties, and thus limit this Initial Brief to salient points as to which our perspective and expertise can be of meaningful assistance.

DoD/FEA, with more than 60,000 civilian and 30,000 military employees in Washington, is probably the largest user of Qwest's telecommunications services in the state.

DoD/FEA installations, facilities and offices, ranging widely in size, are located throughout Washington, and the business telecommunications services purchased range from large complex systems to small office services.² To obtain the best available services at the lowest possible costs, DoD/FEA obtains services through competitive bidding procedures whenever possible. The Commission's decision in this proceeding may affect both the cost of services provided by Qwest to DoD/FEA and the extent to which competitive services will be available. Thus, the decision will affect the ability of DoD/FEA (and all other users) to obtain telecommunications services service at competitive rates from a variety of suppliers. Accordingly, DoD/FEA will be directly and significantly affected by the Commission's decision as to Qwest's proposed reclassification of all its analog basic business exchange services as competitive.

As we describe below, Qwest may have been able to justify, under prevailing statutes, rules and precedent, a more limited reclassification of certain of its business exchange services. As a general principle, it is DoD/FEA's guiding position that where the record demonstrates that effective competition exists, we would support reclassification. The existing record here, however, is not sufficient for DoD/FEA -- or the Commission, in our view -- to even determine the scope of an appropriate reclassification. Thus, we have recommended that the Commission deny the request in its entirety, with sufficient direction, reiterated again, to Qwest that would allow it to file a more focused petition if desired.

² DoD/FEA obtains a broad variety of services; has a wide range of sizes of customer serving sites and number and kind of urban/rural locations throughout the state; and uses a variety of providers (CLEC,

Qwest filed its petition on May 1, 2003, seeking Commission reclassification of its analog basic business exchange telecommunications services, excluding digital services, throughout the state as competitive. Qwest stated that the services for which reclassification is sought fall into two categories: services that provide access to the network and "discretionary business features" that are available as access line or trunk options.³ Qwest addressed each of the statutory factors, and stated that it met those criteria because:

- There are 161 registered competitive local exchange carriers ("CLECs") in Washington, and Qwest had 152 Commission-approved interconnection agreements;
- Business customers have reasonably available alternative basic exchange services throughout the state, as evidenced by the number of CLECs, their price lists and the fact that those lists offer service throughout the state;
- Alternative providers can offer service through resale and unbundled network element platforms ("UNE-P") throughout the state, and Qwest has implemented processes that ensure that competitive services using Qwest facilities are readily available and provided in a nondiscriminatory manner;
- The minimum CLEC share of business access lines in Washington is 17%, with a range of 7% to 22%, not counting lines provisioned over CLEC-provided facilities;
- CLEC market share increased by 32% in 2002; and CLECs enjoy ease of entry into the market; and
- Qwest does not have a significant captive customer base, in light of the foregoing facts as to the CLEC presence and Qwest's provision of cost-based UNEs in a nondiscriminatory manner.⁴

Parties requested that the Commission set the Petition for a public hearing.

DoD/FEA supported the commencement of a public hearing, as did others, noting that the Petition "raises significant issues and concerns that are not fully addressed in the material

ILEC) and mechanisms of acquiring service (regulated tariff, ICB and competitive offerings).

³ Petition, pp. 1-2.

⁴ *Id.*, pp. 3-13. The Petition also considered CLEC presence based on E-911 records, and the affiliation of the providers of service.

presently before the Commission."⁵ At its May 28, 2003, meeting, the Commission suspended the effective date of the proposed reclassification and designated the Petition for hearing.⁶ The Commission appointed Administrative Law Judge Theodora M. Mace as the Presiding Officer and scheduled a prehearing conference for June 6, 2003. Subsequent to the prehearing conference, the Presiding Officer ordered "all CLECs providing business service in the state of Washington" to file certain information about the number of lines provided to business customers and the number of business customer locations.⁷

In accordance with the procedural schedule established at the prehearing conference, Qwest filed its direct testimony on July 1, 2003. The Staff and other parties filed responsive testimony on August 13, 2003, and Qwest and parties filed rebuttal testimony on August 29, 2003. The Staff's witnesses supported the Petition and recommended reclassification of all business exchange services, as defined in the Petition, throughout the state. The Commission's Staff also provided to parties a summary version of the data that CLECs were required to file with the Commission pursuant to *Order No. 6*. No other party supported reclassification. DoD/FEA will address the relevant testimony in the following portions of this brief. Hearings were held in September and October, and concluded on October 22, 2003.

In the *DoD/FEA May 2003 Letter*, DoD/FEA urged the Commission to consider whether market forces, rather than Commission regulation, are sufficiently strong at this time so as to ensure that rates, services and practices throughout the state will be just,

⁵ Letter from Stephen S. Melnikoff, Counsel for DoD/FEA to the Commission's Secretary, May 27, 2003, p. 1 (footnote omitted) (hereafter, "*DoD/FEA May 2003 Letter*").

⁶ Order No. 1, Docket No. UT-030614, served May 30, 2003.

⁷ Order No. 6, Docket No. UT-030614, served June 30, 2003 ("*Order No. 6*").

reasonable and nondiscriminatory. It is important that the Commission address the reclassification issue with caution -- as it did in Docket No. UT-000883 -- and proceed with balanced and fair incremental steps to remove the regulatory oversight that has served the public so well in the past, but now exists in a changing competitive environment. The Federal Communications Commission ("FCC") described well the dangers inherent in removing regulation in a market where competition is emerging:

While there are clear benefits from pricing flexibility, there are also competitive concerns raised by their introduction. Thus, if introduced too soon, pricing flexibility might be used to erect a barrier to competitive entry. For example, a rate-of-return carrier could deaverage its rates so that the attractive customers received very low rates, or it could lock up customers before entry began through the use of lengthy term contracts. In addition, in offering deaveraged rates or volume and term discounts, a carrier could, absent some restrictions, increase rates excessively for remote customers or for low-volume customers to offset reductions resulting from the introduction of deaveraged rates or volume discounts for higher-volume customers. Such practices could inhibit competitive entry and deny customers in rate-of-return carrier service areas the benefits of competition.⁸

Thus, hasty action can produce adverse consequences for both existing competitors and consumers: competitors are driven from the market and small and/or remote (and even large business) customers bear undue costs that result from the lack of a truly competitive environment, as well as from subsidization of other customers.⁹

⁸ Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers, *Second Report and Order and Further Notice of Proposed Rulemaking*, FCC 01-304 (released November 8, 2001), para. 250 (footnote omitted).

⁹ DoD/FEA recognizes that RCW 80.36.330(3) provides that rates charged for competitive telecommunications service must cover their costs, and RCW 80.36.330(6) prohibits the recovery of losses in the provision of competitive services from being recovered from noncompetitive services. These provisions do not adequately protect competitors and customers from the practices that the FCC described. The danger is not that the revenues from all deregulated business services will not cover their costs in the aggregate. It is that the incumbent can selectively price services according to the level of competition in a given market. Moreover, it appears that the Commission would have to institute a proceeding, no doubt subject to strong opposition from the incumbent, to undo the effects of such selective pricing. While in the short run large business customers might gain some relief from elimination of overly burdensome/restrictive regulatory policies, in the long run the growth of a strong and vibrant competitive environment would be threatened.

Premature reclassification of a service as competitive also affects the interest and ability of carriers to enter the market for local service. This is especially true as to carriers considering the investments required to provide facilities-based competitive services. DoD/FEA considers it to be important that Commission adopt regulatory programs that encourage facilities-based competition, as that is the type of competition that will truly allow marketplace forces to ensure just, reasonable and nondiscriminatory prices, and to encourage innovative offerings. Companies, however -- and especially those companies with limited funds and existing commitments in other markets -- will hesitate to enter and invest the money and other resources if it appears that the Commission is taking premature steps to free the incumbent from regulation. Accordingly, the Commission should take a cautious and incremental approach to reclassification of any local service.

II. APPLICABLE LAW

Qwest filed the Petition pursuant to the terms of RCW 80-36.330. That statute provides that the Commission "may classify a telecommunications service provided by a telecommunications company as a competitive telecommunications service if the service is subject to effective competition." "Effective competition" is defined to mean that "customers of the service have reasonably available alternatives and that the service is not provided to a significant captive customer base." To determine whether "effective competition" exists, the Commission is required to consider certain criteria, but its review is not limited to those factors. The mandatory criteria are:

- (a) The number and size of alternative providers of services;
- (b) The extent to which services are available from alternative providers in the relevant market;
- (c) The ability of alternative providers to make functionally equivalent or substitute services readily available at competitive rates, terms, and conditions; and

- (d) Other indicators of market power, which may include market share, growth in market share, ease of entry, and the affiliation of providers of services.

The classification of a service as competitive allows the carrier to provide the service pursuant to a price list, rather than by tariff. Rates for competitive services must cover the costs of providing service, and the Commission may investigate the prices for reclassified competitive services. Moreover, losses incurred in providing competitive services may not be recovered through rates for noncompetitive services. The Commission has authority to waive certain statutory provisions for competitive services, namely the provisions prohibiting undue preference (RCW 80.36.170) and rate discrimination (RCW 80.36.180).¹⁰

The Commission's rules provide guidance as to filing a petition for reclassification of a telecommunications service as competitive, and state that the Commission will consider the four statutory criteria quoted above in determining whether the carrier has met the statutory definition of "effective competition." Those rules also provide for the mandatory filing of information with a petition for reclassification, including the following:

- A description of all functionally equivalent or substitute services in the relevant market;
- The names and addresses of all providers of the services known or reasonably knowable to the petitioner;
- The prices, terms, and conditions under which the services are offered by competitors to the extent known or reasonably knowable to the petitioner;
- A geographical description of the relevant market;
- An estimate of the petitioner's market share;
- A description of ease of entry into the market; and
- A statement of whether the petitioner has a significant captive customer base and the basis for any contention that it does not.¹¹

¹⁰ See, generally, RCW 80.36.330. Counsel for Qwest has indicated that it is not requesting such a waiver. Tr. 276-7.

¹¹ WAC 480-121-062(5)(a)-(g).

The Commission has considered one previous petition for reclassification of Qwest's basic exchange telecommunications service as competitive pursuant to the statutory provisions summarized above. In June 2000, Qwest petitioned to reclassify all business exchange service in 31 wire centers. The Commission considered that petition in Docket No. UT-000883. In its decision in that case, the Commission granted the petition as to 23 of the 31 wire centers, located in four exchanges, and only for business customers served on DS-1 or larger capacity circuits.¹² In the *2000 Reclassification Order*, the Commission stated that the statutory criteria cited above are not exclusive, and that it had the authority to consider other factors such as its own "institutional knowledge."¹³ The Commission's findings in that case provide considerable guidance for a carrier seeking competitive classification of a service. Among the salient points that the Commission enunciated, the following are particularly relevant to the current proceeding:

- For "effective competition" to exist, the Commission must have confidence that competitors "*are offering and will offer*" viable alternatives to the services provided by the incumbent; evidence that there are competitors who are capable of providing alternative service is unacceptable.¹⁴
- As to reclassification of a local exchange service, it is not adequate to rely only on the number of lines served by competitors; rather the carrier's showing must show the number of customers served by competitors to ensure that the market share does not simply represent the purchase by a small number of end-user customers.¹⁵
- The statute does not permit the Commission "to impose future conditions to eliminate the significance of what currently is a significant captive customer base."¹⁶

¹² Petition of Qwest Corporation for Competitive Classification of Business Service in Specified Wire Centers, *Seventh Supplemental Order Denying Petition and Accepting Staff's Proposal*, Docket No. UT-000883 (released December 21, 2000) (hereafter cited as the "*2000 Reclassification Order*").

¹³ *Id.* at para. 10.

¹⁴ *Id.* at para. 66; italics in original.

¹⁵ *Id.* at para. 68.

¹⁶ *Id.* at para. 71.

- The volume of service provided to end-user customers is more relevant to the issue of "reasonably available alternatives" than is the size of the business.¹⁷
- The analysis of market concentration should not include resold lines, because "resale does not constrain prices."¹⁸

Based on the statutory criteria and the above considerations, and looking at the number of customers that had switched to an alternative provider, the Commission concluded that market concentration and structure were adequate to warrant reclassification in only the 23 wire centers.¹⁹

III. DEFINITION OF RELEVANT MARKET

A key factor in assessing a petition for reclassification is the identity of the "relevant market." The statute requires a petitioner to show that alternative services are available in the relevant market. Indeed, one must understand the market characteristics before the other statutory criteria can be addressed. Market considerations look to both the product and the geographic area. Defining these markets too narrowly or broadly can cause "spurious conclusions."²⁰

A. Definition of Product Market

Parties' Positions

Qwest defined the relevant product market as all business exchange services, excluding digital switched services, not distinguishing between, for example, a single-line business and a large business served by high capacity facilities. The Petition does not provide any explanation for this assumption, and the Qwest witnesses likewise simply aggregate all business lines, excluding digital lines, for purposes of displaying

¹⁷ *Id.* at para. 72.

¹⁸ *Id.* at para. 75.

¹⁹ *Id.* at para. 76.

²⁰ Ex. 401T, p. 38.

competitive activity throughout the state. The only explanation in the Direct Testimony for aggregating all business lines is Mr. Reynolds' assertion that "...there is significant competitive activity in this market...."²¹ As to the exclusion of digital lines, Mr. Reynolds simply states that competitors are not using unbundled loops and UNE-P to provision their digital switched services, and the Petition is focused on Qwest wholesale services.²²

Staff witness Wilson likewise considered the relevant product market to be all business exchange lines other than digital lines, stating simply:

[The relevant market] is the market for small, medium, and large-sized basic business exchange telecommunications services, including private branch exchange (PBX) and certain centrex-type services. It is the so-called market for "last mile" services to small, medium, and large-sized business customers, providing basic connectivity to the public network for switched, voice-grade communications.²³

During cross-examination, he stated that he simply adopted the Qwest definition of the product market because Qwest made that distinction in the Petition.²⁴ Mr. Wilson did, however, provide information as to the CLECs' share of the Basic Business, PBX and Centrex services.²⁵

Public Counsel witness Baldwin criticized the level of aggregation in this regard, stating that: "A CLEC's efforts to attract large businesses do not represent effective competition for small businesses."²⁶ She further noted that small customers are not likely

²¹ Ex. 1T, p. 5. In his Rebuttal Testimony, he stated that Qwest did not separate Centrex, PBX and individual line service because Qwest did not know what service a CLEC is provisioning from the wholesale service obtained from Qwest, and because these services provide functionally equivalent exchange access. Ex. 7RT, p. 13.

²² Ex. 1T, p. 5.

²³ Ex. 201T, p. 15.

²⁴ Tr. 1311.

²⁵ Ex. 201T, p. 14.

²⁶ Ex. 401T, p. 13.

to be "at the top of CLECs' strategic plans."²⁷ Further, she stated that FCC data reflect that only 46% of CLECs' lines serve mass-market customers, and that Qwest disproportionately serves that market.²⁸ Witness Baldwin also quotes extensively from the FCC's recent *Triennial Review Order*²⁹ as to how different markets exist for differing size customers.³⁰

Discussion

Small and Large Business Segments

DoD/FEA believes that Qwest has improperly defined the product market, and that such failure of proof in this critical area warrants denial of the Petition. There is no single market for all business exchange services when considering the presence and growth of competition. We will not repeat here the FCC's extensive discussion, as it is set forth in Ex. 422RT, but simply point out its belief that there are three product markets for local service: mass market, small and medium enterprise, and large enterprise. The first category includes residential customers as well as very small businesses that purchase few vertical features, generate tight profit margins that are sensitive to marketing, administrative, advertising and customer costs, and usually do not sign long term contracts.³¹ We believe that the Commission should keep these distinctions in mind when resolving the issues in this proceeding. Clearly, as we show herein, there is no support for the Qwest and Staff position that one can overlook these differences.

²⁷ *Id.*, p. 16.

²⁸ *Id.*, p. 36. The FCC's report summarizing competitive activity on a statewide basis defines "mass market" customers as those customers with three or fewer lines. *Id.*, fn. 59.

²⁹ Review of the Section 251 Unbundling Obligations of Local Exchange Carriers, *Report and Order on Remand and further Notice of Proposed Rulemaking*, FCC 03-36 (released Aug. 21, 2003) ("*Triennial Review Order*").

³⁰ Ex. 422RT, pp. 4-5.

³¹ *Id.*, citing *Triennial Review Order*, para. 127.

First, we note that neither Qwest nor the Staff has adequately explained the reason for aggregation of all business services into one product market. We do not believe that "business exchange service" is or should be considered a service for analysis in a competitive inquiry. Indeed, Qwest cites to no regulatory commission that has aggregated all business exchanges into a single service with respect to assigning a competitive classification for local exchange service. In the *2000 Reclassification Order*, the Commission references the Staff's position that reclassification should not encompass all business customers in the geographic markets where it recommended reclassification, but that if the Commission did reclassify all business service in those areas, the Commission should impose certain conditions to protect small business customers.³²

The aggregation of all business exchange services into a single "market" also is inconsistent with the FCC's local competition reporting requirements. Rather than distinguish between business and residence customers, the FCC has looked at the quantity or type of local service that the customer is provided. In its long-standing program for the collection of data to assess the status of competitive entry on a state-by-state basis, the FCC has consistently broken out of the total line data the number of lines provided to "residential and small business" service, with the threshold for that category being three or fewer lines connected to a customer location. The FCC stated, with regard to its local competition reporting efforts, that "Access to this information will materially improve our ability to develop, evaluate, and revise policy in these rapidly changing areas and will provide valuable benchmarks for Congress, this Commission, other policy

³² *2000 Reclassification Order*, paras. 23, 71. As noted above, the Commission declined to reclassify small business exchange service subject to conditions, and rather reclassified only business service for customers served on DS-1 or larger circuits.

makers, and consumers."³³ Clearly, that agency has not found that there is a single market for all business services in the context of assessing the status of competition.

The need for identification of and distinction between "mass market" and larger business customers in this proceeding is highlighted by the large number of "mass market" Qwest customers. Those data are found in Ex. 412C. If the reclassification were approved, **[See Confidential Attachment]** Qwest mass-market and small/medium customers respectively would be affected. Clearly, our concerns in this regard are not academic. Many customers, often with limited if any competitive alternatives, would find themselves no longer subject to regulatory oversight as to the provision of services for their small systems.

Moreover, even assuming that Qwest had separated the product into at least small and large business, it is clear that competitive presence in the large market is varied. Staff witness Wilson's estimate of the market shows that Qwest provides **[See Confidential Attachment]**% of the Centrex lines, compared to its apparent provision of **[See Confidential Attachment]**% of the general business lines.³⁴

Finally, we note that even Qwest appears to recognize that there is not a single business market. It distinguishes the business market for purposes of tracking service quality with "large business" customers having five or more access lines.³⁵ The Qwest home page has separate links on the opening page for small business and large business, and each of those pages has a separate "quick links" section.³⁶

³³ Local Competition and Broadband Reporting, *Report and Order*, 15 FCC Rcd 7717 (2000), para. 1.

³⁴ Ex. 201T, p. 14 (revised).

³⁵ Ex. 401T, p. 36, fn. 59.

³⁶ www.qwest.com, visited October 6, 2003.

Analog

As to Qwest's assertion that there exists a market for analog business exchange service, rather than a market for analog and digital service, DoD/FEA submits that there does not exist in this record any basis for that distinction. Qwest's references in the Petition to the exclusion of digital services were not even contained in the text thereof, and witness Reynolds' testimony was similarly unenlightening. Staff witness Wilson appears to have looked at the analog market only because Qwest took that approach, not because he believed it to be a product market.³⁷ In fact, Mr. Wilson acknowledged on re-cross examination that under the Longstaff approach³⁸ (which he cited favorably), it would be appropriate to consider CLEC digital and Qwest digital services, but that data and analysis are not in the record and thus he could not give a directional estimate of its impact upon the analyses' results.³⁹ In the recently concluded Idaho reclassification proceeding, Qwest did not make such a distinction.⁴⁰ In view of our overall recommendation that the Commission deny the Petition as filed because of other failings, however, we do not believe that the Commission need make definitive findings in this regard, beyond reiterating instructive guidelines for future use.

In summary, a general distinction between "residence" and "business" services may have existed at one time (or still exist) in the context of telecommunications carrier tariffing practices. That distinction, however, is neither relevant to nor sufficiently detailed for assessing the state of competition in an area or to removing regulatory

³⁷ Tr. 1311. However, he stated in his testimony that competitors offer both digital and analog services in competition with Qwest analog services. Ex. 201T, p. 15.

³⁸ Ex. 201T, fn. 20.

³⁹ Tr. 1531-2. Furthermore, Mr. Wilson candidly acknowledged that the Commission "cannot put blinders on" and ignore services (*e.g.*, digital) that affect the business services (analog) for which Qwest has requested reclassification. Tr. 1325-6.

⁴⁰ Tr. 437-8.

safeguards as local competition is emerging in an area. The Commission, accordingly, should reject the Qwest's assertion of a single local analog business market for purposes of this proceeding. Clearly, the lack of data in this proceeding should not allow glossing over or omitting material, relevant and decisionally important, necessary analyses.

B. Definition of Geographic Market

Parties' Positions

Qwest states in the Petition that "the market for business services should be appropriately defined as statewide."⁴¹ Qwest witness Reynolds testified in support of the proposition that the entire state is the relevant market. He stated that CLECs' price lists state that service is available "where facilities exist."⁴² Because such facilities are available anywhere that Qwest offers service, he argues, CLEC services therefore are available everywhere that Qwest operates. Qwest witness Teitzel also addressed the relevant market. He stated that "for ease of reference" Qwest divided the state into nine geographic zones to assess the level of competition for business exchange service.⁴³ The maximum Qwest share, excluding lines provided by CLECs on their own facilities, varied from 78% to 93%.⁴⁴ He also displayed the competitive presence by exchange.⁴⁵

The Commission's Staff also apparently believes that the relevant market for consideration of all business exchange service is the entire state. Staff witness Wilson testified that the relevant market is "Qwest's statewide service territory, defined at the exchange level."⁴⁶ Mr. Wilson clarified on cross-examination that his definition meant

⁴¹ Petition, p. 4.

⁴² Ex. 1T, pp. 8-9.

⁴³ Ex. 51T, p. 6

⁴⁴ *Id.*, p. 8.

⁴⁵ Ex. 54C.

⁴⁶ Ex. 201T, p. 15.

"the Qwest service territory in its entirety," but he also stated that he had looked at the application criteria at the wire center or exchange level.⁴⁷ He also divided the state into five zones to summarize market concentration data.⁴⁸ These zones do not appear to have any significance as markets, however.

Other witnesses disagreed with the Qwest and Staff definitions of the relevant geographic market. Public Counsel witness Baldwin stated that Qwest's assertion that the entire state is a single geographic market is incorrect, and that the nine areas for which Mr. Teitzel summarized data are overly broad for this purpose.⁴⁹ She stated that Qwest has ignored the "disparate stages of competition that are emerging throughout the state."⁵⁰ In contrast, she summarized competitive data at the exchange level, and found that Qwest's market share varies "significantly" among those exchanges.⁵¹ Other witnesses also disagreed with the use of the entire state as the relevant market.⁵²

Discussion

The data of record show, without question, great variations in CLEC activity among exchanges in Washington. This is not unusual to find in a period of emerging competition -- competitors will first seek to serve larger, more lucrative markets where economies of scale exist. And, as DoD/FEA noted in the *DoD/FEA May 2000 Letter*, competition is emerging in Washington less rapidly than on a nationwide basis.⁵³ Given those variations, the Commission should continue to approach reclassification cautiously,

⁴⁷ Tr. 1317-8.

⁴⁸ Ex. 201T, p. 25.

⁴⁹ Ex. 401T, p. 10.

⁵⁰ *Id.*, p. 13.

⁵¹ *Id.*, pp. 39-40; Ex. 414C and 415C.

⁵² *See, e.g.*, Ex. 701, pp. 6-8;

⁵³ *DoD/FEA May 2000 Letter*, p. 2, *citing* Federal Communications Commission, Local Competition: Status as of June 30, 2002 (Ex 429), Table 6. A more recent survey, using data as of December 31, 2002, shows a CLEC market share in Washington of 9.74%, compared with a nationwide share of 13%.

as it did in Docket No. UT-000883, and assess the need for reclassification on a basis no greater than each exchange.

DoD/FEA also notes that in the FCC's *Triennial Review Order*, that agency established rules applicable to the provision of UNEs to CLECs. States were given authority as to certain UNEs to determine whether competitive conditions in their states warranted continued provision of UNEs, based upon market analysis under the rules adopted by the FCC. The FCC mandated, however, that for purposes of the competitive analysis the state commissions may not define the market as encompassing the entire state.⁵⁴ Rather, state commissions must define the market on a granular level, taking into consideration factors such as the locations of customers served, variations in competitors' ability to serve customers and ability to serve specific markets economically and efficiently.⁵⁵ The FCC's action in this regard is understandable. Consumers in areas where competition is limited should not have data applicable to them subsumed in a much larger state-wide analysis, which will presumably be heavily weighted by the presence of competition in urban areas. Competitors actively seeking customers in Seattle may have little interest in serving towns in the eastern part of the state. That such variations exist in Washington is evident from data in the record. Staff witness Wilson, for example, referred to the existence of 27 competitors in the Seattle area, and also to numerous exchanges where only one to three competitors exist.⁵⁶ Even Qwest witness Teitzel acknowledges that the level of competition will be greater in more densely populated urban areas compared with more rural areas, although his comments in that

⁵⁴ *Triennial Review Order*, para. 495.

⁵⁵ Ex. 422RT, p. 4, quoting *Triennial Review Order* at para. 495.

⁵⁶ Compare Ex. 201T, p. 4 and the numerous cities listed in Ex. 203C, p. 1.

regard are directed to urban states versus states with rural areas served by independent companies.⁵⁷ Accordingly, the Commission should reclassify, if at all, on no greater than an exchange basis.

IV. REVIEW OF STATUTORY FACTORS FOR EVALUATING EFFECTIVE COMPETITION

A. Number and Size of Alternative Providers of Services

Parties' Positions

The statute requires that the Commission consider the number and size of alternative providers of service in a reclassification proceeding. In this case, the relevant group to be assessed is those carriers providing exchange service to business customers in Qwest's Washington service area. The parties have cited a wide variety of numbers. In the Petition, Qwest states that there are 161 CLECs registered with the Commission, and that it had 152 interconnection agreements in 2002.⁵⁸ Qwest witness Reynolds stated that "over 35" companies purchase wholesale services from Qwest and provide competing services to those sought to be reclassified.⁵⁹ Qwest witness Teitzel stated that as of April 30, 2003, 78 carriers were purchasing wholesale services from Qwest to serve their Washington customers.⁶⁰ He also stated that the companies purchasing wholesale services from Qwest are active in all but five of the Qwest wire centers.⁶¹

Staff witness Wilson testified that the Staff conducted a survey of registered CLECs in Washington, and sent the inquiry to more than 200 companies. The staff, however, received just 24 responses, of which only 17 apparently were usable, and

⁵⁷ Ex. 60RT, p. 12.

⁵⁸ Petition, pp. 3-4.

⁵⁹ Ex. 1T, p. 20; Ex. 3. Exhibit 3 lists 37 companies.

⁶⁰ Ex. 51T, p. 6

⁶¹ *Id.* at p. 9.

several others verified the Qwest data.⁶² In his Rebuttal Testimony, Mr. Wilson stated that 27 CLECs responded to the staff's inquiry.⁶³ He also stated that, based on the Staff's inquiry, only one exchange in Qwest's territory is not served by a competitive carrier.⁶⁴ In his study, Mr. Wilson did not disclose the identity of the reporting carriers or show their sizes. He stated that some of the reporting carriers provided only residential service.⁶⁵

Other witnesses addressed the number and size of providers of competitive services. Public Counsel witness Baldwin testified that, as to the CLECs actually providing services competitive to the services for which reclassification is sought, "the market shares of the vast majority" are negligible.⁶⁶ AT&T witness Cowen stated that, based on his partial survey of the registered CLECs, many are no longer in business at all, or did not provide a competitive service.⁶⁷ Finally, DoD/GSA notes that the FCC's semi-annual report assessing the extent of local competition on a state-by-state basis shows that, as of December 31, 2002, only 11 competitive carriers reported that they had more than 10,000 total access lines -- business and residential -- in Washington.⁶⁸

Discussion

The Commission's assessment of the record as to the first statutory criterion must conclude that Qwest has overstated the number of carriers providing a competitive alternative to its business exchange services. In assessing the number of alternative

⁶² Ex. 201T, p. 12.

⁶³ Ex. 210TC, p. 6.

⁶⁴ *Id.* at p. 6.

⁶⁵ Tr. 1532. On separate cross-examination, Mr. Wilson stated that he believed that there were about 40 CLEC alternative providers for Qwest's business services at issue, but that those not "captured in the data" were not significant. Tr. 1431-2.

⁶⁶ Ex. 401T, p. 14.

⁶⁷ Ex. 701, p. 9.

⁶⁸ Ex. 429, Table 12.

providers, the Commission should ignore the number of CLECs that are certificated or have interconnection agreements, because those data fail to address the critical issue, as the Commission noted in the *2000 Reclassification Order*, as to the companies actually providing a competitive service. Certification may indicate an interest in entering the market, but clearly that interest is not relevant to the statutory criteria.

A better view of the number of competitors, in DoD/FEA's view, is those CLECs that responded to *Order No. 6* and provide local business service. A CLEC that failed to respond to a Commission order is not properly viewed as an "alternative provider," in our opinion. We note also that less than half of the 27 responding CLECs in the subject study are large enough to meet the FCC's reporting threshold of 10,000 or more lines, as discussed above. Moreover, Staff witness Wilson stated that for companies that own several different CLECs in the state, he treated each CLEC as a separate reporting entity.⁶⁹ Eleven CLECs providing more than 10,000 total access lines in Washington -- which would include non-Qwest territory -- is not, in our view, an insignificant competitive presence. That fact, however, has little bearing on the relevant issues herein in light of the other findings detailed below.

Because the record data do not disclose the size of the reporting CLECs, it is not possible to make solid findings that the alternative providers are sufficiently large and financially positioned to exercise pricing restraints on Qwest. Several witnesses discussed the financial problems that exist in the CLEC industry, and the sharp declines in market capitalization since December 31, 1999.⁷⁰ Moreover, although the carriers are not identified, Public Counsel witness Baldwin looked at those CLECs reporting lines in

⁶⁹ Tr. 1465. He estimated the number of such instances to be less than five.

⁷⁰ See, e.g., Ex. 501T, pp. 48-51.

the Spokane market -- not a rural market. The largest CLEC share of the 20 reporting CLECs was [See Confidential Attachment]%, but after that the shares are relatively minimal.⁷¹ Carriers that have such minimal presence in a major state market are not providing such constraints or effective competition. In summary, the evidence in this area is so lacking in specifics that the Commission cannot determine to what extent large competitors who might have the ability to constrain prices are actually serving customer "segments" (small and large) -- specifically in each Qwest exchange throughout the state.

B. Extent to Which Services are Available From Alternative Providers in the Relevant Market

Parties' Positions

In support of his testimony that Qwest has met this statutory criterion, Mr. Reynolds referred to a matrix showing prices and services "in the relevant market" for 32 CLECs.⁷² He noted language in each price list to the effect that the CLEC's service is available where facilities exist. If this is the case, he stated, and such facilities are available anywhere Qwest currently offers service, "...then CLEC services are available everywhere Qwest services are available."⁷³ Consistent with Qwest's position that the relevant market is the entire state, the witness makes no attempt to show the particular geographic area where each of those 32 companies currently operates. Qwest witness Teitzel, as noted above, looked at wholesale lines in nine geographic areas, and found competitive activity throughout those areas. Only five wire centers in Qwest's service area were not currently served by CLECs, taking wholesale service from Qwest, to some extent.

⁷¹ Ex. 402C.

⁷² Ex. 1T, p. 8; Ex. 4.

⁷³ *Id.*, p. 9.

Staff witness Wilson stated that, based on the study of CLEC-supplied data and Qwest wholesale data, services are available "...at competitive rates from one to three alternative providers in every exchange except Elk."⁷⁴ He stated that the dispersion of alternative business services is very broad everywhere but this one exchange, and that Qwest provides wholesale services at parity with the service quality level that it provides to its own customers.⁷⁵ Public Counsel witness Baldwin testified that the theoretical availability of service in a market is not adequate in the determination of effective competition; rather, the Commission must examine the extent to which CLECs are actually serving customers.⁷⁶ She also noted that Qwest's showing under this criterion fails to demonstrate the extent to which small business customers are being served by alternative providers.⁷⁷ MCI witness Gates also addressed this criterion and also found Qwest's showing lacking; he disagreed with the proposition that the criterion can be met if there are only a few competitive lines in an exchange or if the services are not functionally equivalent.⁷⁸

Discussion

DoD/FEA believes that Qwest has not made the showing required under this consideration that would permit the Commission to find that "effective competition" exists in the relevant market. Initially, we point out that Qwest and the Staff have, in our view, failed to identify the relevant product and geographic markets. A review of the service descriptions for the carriers listed in Exhibit 4 discloses that some of the services

⁷⁴ Ex. 201T, p. 20.

⁷⁵ *Id.*

⁷⁶ Ex. 401T, p. 14.

⁷⁷ *Id.* at 17-8.

⁷⁸ Ex. 501T, p. 13.

provided by those carriers would only be provided to large business customers, and not available to small businesses. Thus, there is no record evidence that supports their view that alternative providers provide service to all "market segments" throughout the state. Moreover, as we have discussed, the statute requires an assessment of whether services are available -- not whether, as is the basis of Mr. Reynolds' testimony, a competitive carrier could provide service in the market.

Viewing, hypothetically, the exchange as the relevant market, it is clear that services are not available from alternative providers in the Elk exchange. In other exchanges, some of which are served by only one CLEC (who may not be serving the mass market customers), the extent to which services are available is so small that the alternative providers are incapable of providing an alternative that could restrain Qwest's ability to set prices above or below costs. The high degree of aggregation in the Staff's study makes it impossible to assess the extent to which competitive services exist in specific exchanges, but that study provides little assurance that facilities-based competition -- the type of competition that would constrain Qwest pricing -- exists at all. In summary, the evidence as to this criterion is too inconclusive to allow for a Commission finding that the competitive services are available to all "market segments" throughout the state.⁷⁹

⁷⁹ Staff witness Wilson testified that Qwest exercises no market power in **any** exchange. Tr. 1373-4. DoD/FEA finds this assertion to be completely inconsistent with the data on currently available alternatives that is available to us (Ex. 205C), and no doubt inconsistent with the raw data concerning CLEC presence in rural exchanges.

C. The Ability of Alternative Providers to Make Functionally Equivalent or Substitute Services Readily Available

1. Wholesale-based Services (resale; UNE-P; UNE-L)

Parties' Positions

Qwest witness Reynolds stated generally that Qwest's competitors have the ability to provide equivalent or substitute services by means of resale and the purchase of wholesale services.⁸⁰ He cited in this respect also the matrix contained in Ex. 4, showing certain competitive prices for business offerings. Staff witness Wilson also noted the ability of alternative providers to make functionally equivalent or substitute services available, and calculated the CLECs' distribution of the alternative services as 9.16% resale, 38.58% UNE-L, 24.34% UNE-P, and 17.93% Facilities-based.⁸¹ He later revised these percentages.⁸²

Discussion

DoD/FEA will generally agree that a carrier has the ability to "readily" provide service in Qwest's service area through resale, but resale is not, in our view, a "functionally equivalent" or "substitute" service. Moreover, such service cannot be provided at competitive rates and conditions. Rather, resale is simply a Qwest service provided by another entity, whose ability to provide service features and change rates is constrained by Qwest. Resale is not a long-term solution to the efforts to encourage competition for the ILECs' wireline services and, in any event, the parties here agree with the Commission's conclusion in the *2000 Reclassification Order* that resale does not

⁸⁰ Ex. 1T, pp. 9-11.

⁸¹ Ex. 201T, p. 22. This distribution does not reflect the changes to CLEC market shares resulting from the submission of updated data by certain CLECs in connection with the filing of a petition on October 7, 2003 for a new survey of CLECs' business lines.

⁸² Ex. 205C; Ex. 232.

constrain prices.⁸³ In assessing the evidence in this proceeding on a variety of factors reviewed, the Commission should essentially ignore resold Qwest service (which in any event is becoming a relative minor CLEC activity).⁸⁴

Likewise, UNE-P is limited by Qwest's prices and features and, as we describe below, may be subject to regulatory action that diminishes CLECs' ability to provide competitive services in this manner. The deployment of UNE-L services is more relevant to this consideration because the CLEC is using in part its owned facilities, and can add features and have more control over its prices. Thus, the Commission may consider under this area that UNE-L services are, to a lesser degree than facilities-based services, evidence of a functionally equivalent or substitute service.

2. CLEC-owned Loops

Parties' Positions

Because data on CLEC-owned loops were not available to Qwest, evidence applicable to this factor was not addressed in the Petition or its Direct Testimony. The Staff's study disclosed that alternative providers are making facilities-based competitive offerings available in certain locations in Washington.⁸⁵ The Staff study calculated that **[See Confidential Attachment]**% of the CLECs' lines are provided on their own loops.⁸⁶

Discussion

The ability of alternative providers to offer business customers competitive services by means of their own switches and loops certainly is an important consideration for the Commission's analysis under the statute. The facts are, however, that the Staff's

⁸³ See, e.g., Tr. 306-7.

⁸⁴ Ex. 1T, p. 13.

⁸⁵ See generally, Ex. 205C.

⁸⁶ Ex. 232.

study shows that relatively few competitive lines are provided in this manner, and a review of Ex. 205C discloses numerous exchanges where no such lines are provided at all. There is no data in the record as to growth in facilities-based competitive business lines. Using as the relevant market the exchanges, if not the wire centers, regardless of whether one is considering small or large business "markets," these CLEC-provided functionally equivalent or substitute services are often not available at all -- at any price. In DoD/FEA's view, the record evidence in this regard mandates that the Commission's consideration result in a finding that Qwest and the Staff have not shown that facilities-based service is sufficiently available so as to support reclassification.

3. Intermodal (wireless, VoIP, Wi-Fi, cable, etc.)

Parties' Positions

Qwest witness Teitzel addressed intermodal services available in Washington and concluded that existence of these services demonstrates that its compilation of competitive data is "very conservative" and that such services provide the Commission with a "level of comfort that effective competition exists in the business local exchange market."⁸⁷ He stated the obvious -- that wireless phones are "widely accepted" as providing voice telephony -- and cited studies showing that the total number of wireless units is approximately 75% of the total Washington wireline access lines.⁸⁸ Mr. Teitzel acknowledged that wireless is not a substitute for large systems such as Centrex and PBX, but he believed wireless to be a substitute for certain small businesses. In support of that belief, he cited to Qwest research in Idaho and Iowa to determine the extent to which business customers perceive wireless service to be a "reasonable substitute" for

⁸⁷ Ex. 51T, p. 28.

⁸⁸ *Id.*, pp. 15-16.

wireline service. He reported that slightly more than 30% of the respondents stated that they could rely solely on wireless service for their incoming and outgoing calls.⁸⁹ Mr. Teitzel also stated that Voice over Internet Protocol (VoIP) service exists in Washington, that it is a price-competitive service for business customers with broadband Internet connections, and that VoIP calls are indistinguishable in quality from wireline calls.⁹⁰

Staff witness Wilson also testified in this regard as to the presence of VoIP in Washington, stating that there were a number of reasons for businesses to "begin the convergence to VoIP."⁹¹ Staff witness Williamson stated that digital services could be used as substitutes for basic business exchange service.⁹² He also addressed the purported substitutability of VoIP for traditional wireline business service.⁹³

Other witnesses challenged the Qwest and Staff testimony in this area. MCI witness Gates disputed that wireless services are substitutes for wireline services. He cited factors such as ability to access the Internet, call quality, inability to send or receive fax transmissions, inability to provide PBX services, absence of multiple line service, absence of white pages listing, security and dependability of service.⁹⁴ He also disputed that VoIP is a substitute for wireline service.⁹⁵ In his Rebuttal Testimony, Qwest witness Teitzel disputed certain of the Gates' attributes of wireless service, asserting that some are incorrect.⁹⁶

⁸⁹ *Id.*, pp. 19-21.

⁹⁰ *Id.*, pp. 22-26.

⁹¹ Ex. 201T, p. 29.

⁹² Ex. 301T, p. 5.

⁹³ *Id.*, pp. 5-7.

⁹⁴ Ex. 501T, pp. 19-36.

⁹⁵ *Id.*, pp. 38-9.

⁹⁶ Ex. 60RT, pp. 20-29.

Discussion

We find compelling that Staff witness Wilson stated on cross-examination that there were insufficient data in the record to evaluate the impact of either wireless or VoIP as substitutes for wireline service.⁹⁷ In addition, Staff witness Williamson acknowledged on cross-examination that both wireless and VoIP services introduce problems and issues for some customers, such as DoD/FEA, that preclude them from being substitutes. Such issues involve security, interoperability, survivorability and quality/accuracy of transmission.⁹⁸ Furthermore, DoD/FEA believes that wireless service is properly characterized as a service that augments the communications services provided by carriers' wireline service, and as such it is neither functionally equivalent nor a substitute as those terms are used in the applicable statute. In other parts of this brief, we have stressed that to be relevant as an alternative to the service to be reclassified, the statute looks to present circumstances such as market share, not theoretical substitutability. The record here does not contain evidence as to the extent to which VoIP or wireless service has replaced wireline service in Washington. Qwest cites a study, taken **in other states**, purporting to show that over 30% of business respondents stated that they **could** completely replace their wireline service with wireless. The deficiencies in this approach are obvious -- we are concerned with what Washington consumers have already done, not what they tell a survey taker that they could do. And the Commission's concern is with respect to Washington, not two other states. Interestingly, Qwest witness Shooshan stated that he **has** made state-specific studies as to the substitutability of wireless for

⁹⁷ Tr. 1418-9.

⁹⁸ Tr. 933-8.

wireline service, but he presented no data relevant to Washington in this case.⁹⁹ We also note that the Idaho Public Utilities Commission recently denied Qwest's petition for reclassification of basic local exchange service in certain exchanges, concluding, *inter alia*, that "... the record is practically devoid of information to show that cellular service competes effectively with Qwest's basic local service in the seven exchanges named in Qwest's Application."¹⁰⁰ In this regard, the Idaho Commission stated that the FCC, in the *Triennial Review Order*, found that "... neither wireless nor cable has blossomed into a full substitute for wireline telephony."¹⁰¹

As to VoIP as a substitute, DoD/FEA additionally points out that the uncertainty as to the regulatory status of VoIP service makes any finding of substitutability for wireline service premature, even if the record contained sufficient evidence on VoIP actual substitutability, which it does not. The Commission recently set for hearing, pursuant to a court remand, an adjudication involving a VoIP provider's obligation to pay access charges.¹⁰² Proceedings that will address the regulatory status and obligations of VoIP providers also are expected to be held by the FCC. A finding that VoIP is a telecommunications service, and that VoIP providers must pay access charges, could negatively impact the growth and characteristics that the Qwest and Staff witnesses have

⁹⁹ Ex. 101T, pp. 12-13, n. 9. His description of the New Jersey and Illinois studies indicates, however, that he was looking at the number of **calls** made on wireless phones, not the actual substitution of wireline **service**.

¹⁰⁰ In the Matter of the Application of Qwest Corporation for Deregulation of Basic Local Exchange Rates in its Boise, Nampa, Caldwell, Meridian, Twin Falls, Idaho Falls, and Pocatello Exchanges, Case No. QWE-T-02-25, Order No. 29360 (served October 20, 2003), p. 11.

¹⁰¹ *Id.* at p. 20, citing *Triennial Review Order*, para. 245.

¹⁰² Washington Exchange Carrier Association, et al. v. LocalDial Corp, Docket No. UT-031472, served September 29, 2003.

described.¹⁰³ Given these circumstances, the Commission would be ill advised to consider VoIP a substitute service at this time.

D. Other Indicators of Market Power

1. Market Share Analysis

Parties' Positions

A considerable effort has been made to present data as to the CLECs' share of the market for aggregated business exchange service (in the absence of market share for a more refined category such as large business). Qwest's Direct Testimony presented market share data on a statewide and wire center basis, with the CLECs' overall market share of 17%. That compilation did not include lines provided by CLECs on their own facilities. In response to *Order No. 6*, the CLECs provided data to the Staff as to all of their business lines, and the Staff compiled an exhibit showing market shares on a statewide basis and as to certain geographic areas in which certain smaller exchanges were combined to protect against the display of confidential information. Because DoD/FEA believes that the inclusion of CLEC-owned lines must be taken into account, our discussion here does not address the Qwest presentation that does not include that information.¹⁰⁴

Staff Witness Wilson compiled the data provided by Qwest and the CLECs to obtain the results displayed in Ex. 205C. On a statewide basis, he computed the CLECs'

¹⁰³ An attorney for one VoIP provider was quoted in USA TODAY that a requirement that VoIP providers pay access charges would mean that "many of these (VOIP) providers will have to go out of business." USA TODAY, October 9, 2003, p. B1.

¹⁰⁴ We note, however, that the Staff computed the CLEC market share by wire center, using only wholesale data. Ex. 208C. The CLEC market shares for those wire centers, if the CLEC-owned lines were included, would presumably be greater in each instance. Thus, Ex. 208C gives some indication of CLEC market share in the relevant geographic markets -- but still the product market has been improperly defined.

share of the business exchange market to be 30.74%.¹⁰⁵ He aggregated the data obtained from Qwest and the CLECs into 39 areas, with total CLEC lines of 231,030.¹⁰⁶ No market share data were provided to parties as to many individual exchanges, however, because of the Staff's need to aggregate certain data for confidentiality reasons.

The manner in which the survey of CLEC lines was conducted led parties to request that the Commission re-survey the CLECs to obtain more accurate information than was first provided. The initial CLEC responses included in some instances digital services.¹⁰⁷ The Commission denied the request that a new survey be conducted, and instead certain CLEC parties filed new line counts. The new data were included in the statewide counts, but not in the 39-area breakdown in the Staff's summary.

Although Qwest generally affirmed the study that included the CLEC-owned lines (subject to the correction of an error in that study), other parties questioned the validity of the Staff's work in this regard. Public Counsel witness Baldwin noted the discrepancies between the data in Exhibits 204C and 205C, and the absence in the Staff's testimony as to the reason for such discrepancies.¹⁰⁸ MCI witness Stacy testified that the market share analysis should exclude resold and UNE-P lines, because Qwest is the underlying carrier for those lines.¹⁰⁹ He then computed the CLEC market share without these lines, and found CLECs to have a 16% statewide share of the business lines, and less than 5% of the lines in 52 of the 66 exchanges in Washington.¹¹⁰ Mr. Stacy also noted that the CLEC share is divided among many smaller carriers, and the aggregated CLEC share should not

¹⁰⁵ Ex. 201T, p. 14 (revised).

¹⁰⁶ *Id.*

¹⁰⁷ See Joint Motion to Require Staff to Re-Survey and Recompile CLEC Data, or to Disregard Results of Previous CLEC Survey and Data Compilation, filed October 7, 2003.

¹⁰⁸ Ex. 422RT, pp. 8-10.

¹⁰⁹ Ex. 603T, p. 3.

¹¹⁰ *Id.*, p. 5.

be thought of as one might consider one competitor with that share.¹¹¹ MCI witness Gates concurred in these concerns.¹¹²

Parties also addressed the growth in CLECs' market share, which, under the statute, the Commission may take into account as an indicator of market power. Qwest witness Teitzel stated that total CLEC lines in Washington experienced a 20% growth in the year ending December 31, 2002, while Qwest experienced a line loss of 13%.¹¹³ Qwest witness Reynolds stated that CLECs' business lines provided with Qwest wholesale services overall grew 32% in the year ended December 31, 2002. The growth was 45% in UNE-P, minus 41% in resale, and 46% for UNE-L.¹¹⁴ Data regarding growth in CLEC usage was also provided in Ex. 5C.

Staff witness Wilson, who included CLEC-owned lines in his estimates, found an overall CLEC market share of 30.74%¹¹⁵ as of December 31, 2002 but did not address growth in market share, a subject that was not contemplated in *Order No. 6*.¹¹⁶ Other witnesses discounted the growth in CLEC lines, noting that relatively minor CLEC growth can cause a large increase in market share.¹¹⁷ Public Counsel witness Baldwin also noted that, based on the FCC's semi-annual reports on the status of local competition, the CLECs' share of the overall Washington market lags behind the national average and that the gap is growing.¹¹⁸

¹¹¹ *Id.*, pp. 9-11.

¹¹² *See, e.g.*, Ex. 504T, pp. 11-14.

¹¹³ Ex. 51T, p. 4.

¹¹⁴ Ex. 1T, p. 13.

¹¹⁵ Mr. Wilson acknowledged that the Qwest market share without UNE-P was 74%. Also, without non-price constraining resale, that share would be 76%. Finally, the Qwest market share without UNE-P and resale would be 76.8%. Tr. 633.

¹¹⁶ Ex. 201T, p. 14 (revised). His original estimate of 24.5% was revised to correct an error.

¹¹⁷ Ex. 401T, p. 26.

¹¹⁸ *Id.*

Discussion

DoD/FEA believes that it is difficult for the Commission to make any inferences as to market share, as that term is used in the statute, in this proceeding. Statewide data, in our view, are inadequate to support a request for reclassification of all Qwest business services because the Commission must look at the more granular market of at least an exchange. The results by exchange show great variation, as Ex. 54C shows, with a CLEC-owned market share of 0% in some exchanges. Moreover, the data that exist do not properly reflect the relevant product markets. As to growth in CLEC market share, the statewide data cited by Qwest are of little relevance absent identification of the exchanges where the growth took place. Growth in the exchanges where reclassification was previously granted, four large urban/business geographic areas which continue to be competitively contested markets, could significantly be responsible for any growth.

Because Staff witness Wilson considered market share to be an imperfect indicator of market power, he indicated that one must look beyond numbers and consider the structure of the market.¹¹⁹ He conceded, however, on cross-examination that ease of entry and other market structure factors are already reflected in the market shares.¹²⁰

In addition, we note that *Order No. 6* required CLECs to report the number of locations within an exchange where they provided service, which is necessary to perform an appropriate analysis of market share (and to identify whether a captive customer base exists). Public Counsel, after being given access to the raw data by the Commission, was able to establish with Mr. Wilson's assistance that seven of the reporting CLECs (somewhere between about 25% to 40+% of the usable reporting entities) failed to

¹¹⁹ Ex. 210, p. 8.

¹²⁰ Tr. 1438-9.

provide such data.¹²¹ Such a failure in the location data casts serious doubt upon the validity of the market share (and captive customer base) analyses.

Finally, we point out that evidence as to market share of customers served, rather than lines provided, was not submitted in this record. In the *2000 Reclassification Order*, the Commission noted that such information was important because a small number of customers may purchase a majority of the lines.¹²² It is possible -- if not probable -- that the "skewing effect" that concerned the Commission previously also is present in this proceeding, but Staff witness Wilson confirmed that he did not perform any analysis of the skewing effect potential because, as in Docket No. UT-000883, the necessary data was not present in this proceeding.¹²³

2. Market Concentration Analysis

Parties' Positions

Qwest witness Shooshan stated that the Commission should not rely on concentration ratios *per se* because, in his view, they are not sufficient to demonstrate market power.¹²⁴ Rather, market power should involve an examination of "The actual and potential supply capabilities of competing firms; that is, their capacity."¹²⁵ Staff witness Wilson addressed market concentration by analysis of the Hirschman-Herfindahl Index ("HHI") on the Qwest wholesale data. He calculated the HHI for each wire center, and summarized the analysis by grouping the data into five zones.¹²⁶ He stated that the data indicate high market concentration, but in his view the analysis is not the best

¹²¹ Tr. 1381.

¹²² *2000 Reclassification Order*, para. 68.

¹²³ Tr. 1410.

¹²⁴ Ex. 101T, p. 8.

¹²⁵ *Id.*, p. 9.

¹²⁶ Ex. 201T, pp. 19-20; Ex. 208C.

representation of the market. His basis for this assertion is the fact that the analysis only included wholesale CLEC lines, and HHI is a "static measure of the market" that quickly becomes stale.¹²⁷

Public Counsel witness Baldwin also conducted an HHI analysis, both as to CLEC wholesale lines and as to data that included CLEC-provided lines. She explained that a market with an HHI below 1000 is considered to be unconcentrated, those with an HHI between 1000 and 1800 are considered to be moderately concentrated, and markets with an HHI above 1800 are considered to be highly concentrated.¹²⁸ She noted that the absence of information about small firms does not significantly affect the HHI. Ms. Baldwin included CLEC-owned lines in an analysis of the business line market by exchange, and found that throughout the state the HHI still shows a high degree of concentration.¹²⁹

Discussion

In the *2000 Reclassification Order*, the Commission noted that the Staff analysis, which considered the relevant market to be the exchange, included a market concentration study using the HHI. The staff chose a threshold of 5000 for the market structure under consideration in that proceeding. In the markets where the HHI exceeded 5000, the staff recommended that competitive classification not be granted.¹³⁰ The Commission granted reclassification in the areas in which the staff analysis showed an HHI below 5000, and stated that it had considered in its decision the "line-based market concentration." The Commission also noted, though, that if the structure of a market is

¹²⁷ *Id.*, p. 19.

¹²⁸ Ex. 401T, pp. 19-20, *citing* the Department of Justice Horizontal Merger Guidelines.

¹²⁹ *Id.*, p. 25; Ex. 405C.

¹³⁰ *2000 Reclassification Order*, paras. 25-6.

sufficiently "pro-competitive," a high market concentration would not prevent a reclassification.¹³¹

DoD/FEA believes that the market concentration analyses contained in the record provide further evidence that the Petition must be denied. The Commission properly decided in the *2000 Reclassification Order* that it would take this factor into account -- and the HHI calculations in that case were far more favorable to the Qwest request than they are in this proceeding. In this case, no wire center had an HHI less than 5000 -- clearly an indicator of very high market concentration -- and Staff Witness Wilson stated that he doubted that inclusion of the CLEC-owned lines would "change things much."¹³² No matter how the data are viewed -- whether including CLEC-owned lines or at the exchange or statewide level -- the concentration data consistently exceed the threshold that the Staff used just three years ago, and that threshold was very generous.

3. Ease of Entry

Parties' Positions

Qwest witness Reynolds stated that CLECs can, using Qwest facilities, enter the market "with ease."¹³³ He asserted that the Commission has approved the procedures for such entry, converting customers from Qwest to a CLEC is "inexpensive and fast," and CLEC service could be provided to customers in areas where there is no CLEC presence "virtually instantaneously."¹³⁴ Staff witness Wilson likewise concluded that CLECs enjoyed ease of entry into the market: "The requirements can be as little as having satisfied regulatory registration requirements and adoption of an interconnection and

¹³¹ *Id.*, para. 73.

¹³² Ex. 208C; Tr. 1429.

¹³³ Ex. 1T, p. 14.

¹³⁴ *Id.*, pp. 14-16.

resale agreement. For a small fee, a CLEC can switch a customer from Qwest to its service almost automatically."¹³⁵ MCI witness Gates stated, however, that entry into the local market is "anything but easy," citing, among other things, the decrease in CLECs' market capitalization and their reliance on Qwest to provide essential facilities.¹³⁶

Discussion

There is no question that entry into the provision of local exchange service has eased since passage of the Telecommunications Act of 1996, and the market-opening activities that incumbent carriers have implemented pursuant to law. There is no regulatory barrier to entry. That does not mean, however, that an entity can quickly enter the business or stay in it profitably. DoD/FEA urges the Commission to reject the Qwest and Staff testimony regarding the ease of entry into providing local business service. They have oversimplified a very complex area. Mr. Wilson's cross-examination reflects a great understatement of the staff and facilities that are required to provide a competitive local service.¹³⁷ Moreover, Qwest and the Staff appear to base their conclusions on the ability of potential competitors to enter the market using Qwest facilities -- either resale or UNE-P. Clearly, providing facilities-based competition is costly, capital intensive and possibly not available to a company without access to capital. In the *Triennial Review Order*, the FCC discussed barriers to entry into the local market, noting that "the telecommunications industry is replete with the kinds of barriers [to entry] described in the economics discussion above."¹³⁸ The FCC discussed in detail the problems

¹³⁵ Ex. 201, p. 23.

¹³⁶ Ex. 501T, pp. 47-51.

¹³⁷ Tr. 1331-5.

¹³⁸ *Triennial Review Order*, para. 86. The FCC's discussion included barriers such as sunk costs, scale economies, and first-mover advantages.

associated with "hot cuts" to CLEC service, and cited record evidence as to specific failures in this regard.¹³⁹ It concluded that "the operational and economic barriers arising from the hot cut process create an insurmountable disadvantage to carriers seeking to serve the mass market...."¹⁴⁰ Accordingly, the Commission should give no weight to the oversimplified Qwest and Staff testimony on this issue.

4. Affiliation of Providers of Service

Parties' Positions

Qwest stated in the Petition that providers of basic business service in Washington include affiliates or subsidiaries of large telecommunications companies such as AT&T, MCI, Verizon and SBC. It also noted independent companies, and provided a list of its own affiliates to show that its competitors do not include its affiliates.¹⁴¹ Qwest's testimony did not directly address this statutory factor. The Commission's Staff noted simply that Qwest does not have affiliates in adjacent or input markets that would give it "any unique advantage over competitors."¹⁴²

Public Counsel witness Baldwin testified that CLECs' affiliation with larger companies may give them access to resources and expertise, but that ability does not translate into effective competition.¹⁴³ She agreed that affiliates of larger companies are buying Qwest's wholesale service, and described the entry of two large LECs, Verizon and SBC.¹⁴⁴ She urged the Commission, however, to consider their market share, as

¹³⁹ *Id.*, para. 468 (AT&T unable to serve low-volume business locations using UNE-L that relied on hot cuts, leading to cancellation of orders; other ILECs limit hot cuts for a given day).

¹⁴⁰ *Id.*, para. 475. Staff witness Wilson apparently did not take this issue into account in his study of the ease of entry factor because he stated that he had not reviewed any part of the *Triennial Review Order* for this docket and was not aware that it addressed, for example, market definition. Tr. 1380-1

¹⁴¹ Petition, p. 12.

¹⁴² Ex. 201T, p. 23.

¹⁴³ Ex. 401T, p. 49.

¹⁴⁴ *Id.*, pp. 50-56.

described in Ex. 419C, in assessing the importance of the presence of Verizon and SBC.¹⁴⁵ No other witnesses specifically addressed this factor.

Discussion

In the *2000 Reclassification Order*, the Commission partially granted Qwest's petition, but did not specifically address the providers' affiliation specifically. In this proceeding, it is clear that some of the competitive providers of business exchange service are affiliated with large, national telecommunications companies. Because the Staff's data as to CLEC lines did not provide line counts by carrier, it is not possible to determine whether these companies are serving a significant number of customers or where they are operating. (There is no record data, as discussed above in Section IV.D1, which is informative of the type of number of customers of these "affiliated CLECs.") Merely reciting the names of carriers is of little value. Accordingly, DoD/FEA is unable to state the extent, if any, to which the Commission should consider this factor in its decision.

5. Other -- Relevance of Section 271 Approval

Parties' Positions

In its testimony supporting the Petition, Qwest argued that the Commission's and FCC's approvals of its application to provide in-region long distance service in Washington, pursuant to Section 271 of the Communications Act, are relevant to and support the grant of reclassification of business exchange service. References to the approvals permeate the testimony. Qwest witness Reynolds, for example, referred to the findings that its operations support systems were non-discriminatory and that its Performance Assurance Plan ensures that the market in Washington will remain open to

¹⁴⁵ *Id.*, p. 56.

competition.¹⁴⁶ Qwest witness Teitzel also referenced the Section 271 approval as support for a grant of the Petition, and quoted extensively from the FCC's order finding that the market in Washington was "fully open to competition."¹⁴⁷ In his rebuttal testimony, Mr. Teitzel responded to parties' assertions to the contrary, and again stated that the Section 271 findings "are germane to this proceeding."¹⁴⁸ He acknowledged that such approval is not tantamount to a finding that effective competition exists statewide, but argued that the open market has enabled competitive activity.¹⁴⁹ Staff witness Wilson, supporting Qwest's Petition, also found the FCC's Section 271 approval to be relevant to this proceeding, stating that the structural framework of the Section 271 safeguards is "critical to Staff's analysis and conclusions."¹⁵⁰

Other witnesses disagreed as to the relevance of the Section 271 approval to this proceeding. Public Counsel witness Baldwin distinguished between the two proceedings, and stated that the FCC's determination did not address whether the level of competition in Washington represents effective competition.¹⁵¹ In fact, she testified, the ability of Qwest to bundle local and long distance service may allow it to lock customers into an exclusive arrangement.¹⁵² MCI witness Stacy and AT&T witness Cowan also disagreed with Qwest's and Staff's reliance on the Section 271 approval in this proceeding.¹⁵³

¹⁴⁶ Ex. 1T, p. 11.

¹⁴⁷ Ex 51T, p. 13; 14-5.

¹⁴⁸ Ex. 60RT, p. 4.

¹⁴⁹ *Id.*

¹⁵⁰ Ex. 201T, p. 7.

¹⁵¹ Ex. 401T, pp. 46-8.

¹⁵² *Id.*, p. 48.

¹⁵³ *See* Ex. 601T, pp. 12-14; Ex. 702, pp. 4-8.

Discussion

DoD/FEA believes that the Commission's and FCC's approvals of Qwest's Section 271 application are not relevant to this proceeding except to the limited extent discussed in the "ease of entry" indicator discussed above. Accordingly, the Commission's decisional process should not be influenced by that consideration. Initially, we note that the Commission, in the *2000 Reclassification Order*, gave no indication of a link between Section 271 approval and reclassification, such that it would have made different findings had Qwest at that time been found to have satisfied the federal statutory "checklist." Rather, the Commission's focus was on the state statutory requirement regarding reclassification that customers must currently have viable alternatives to the incumbent's service and that there must be no significant captive customer base.¹⁵⁴ Section 271 approval does not speak at all to the competitors' ability to provide an effective alternative to the incumbent. Rather, that approval confirms that competitors exist and the market is open to those competitors and others who may wish to enter. Whether competitors decide to enter in such numbers and impact that they become an effective presence is subject to many factors, such as commitments elsewhere, the regulatory climate for new entrants, the size of population centers, etc. Moreover, approval of a Section 271 application does not address the question that DoD/FEA finds to be essential to a grant of a reclassification petition -- is the competition that currently exists so strong that market forces can be assured of creating just, reasonable and nondiscriminatory rates and practices? Unless that question is answered in the positive, customers should not bear the absence of regulatory oversight of a service.

¹⁵⁴ *2000 Reclassification Order*, para. 65. The Commission rejected Qwest's position that effective competition exists if competitors are capable of providing alternative services. *Id.* at para. 66.

E. Significant Captive Customer Base

Parties' Positions

Qwest witness Reynolds stated that there is no significant captive customer base for business exchange service, based upon, apparently, the totality of Qwest's testimony, exhibits and the Petition.¹⁵⁵ In his Rebuttal Testimony, Qwest witness Shooshan stated that there is no captive customer base because customers have a "range of choices," and such choices preclude the finding of a significant -- in fact any -- captive base.¹⁵⁶ Staff witness Wilson also stated that there are no captive customers -- even in the one exchange where there is no CLEC presence (because a CLEC "could relatively easily enter" that exchange).¹⁵⁷

Other witnesses concluded that there does exist a significant captive customer base. Public Counsel witness Baldwin stated that the small business customers are particularly vulnerable to premature relaxation of regulatory oversight.¹⁵⁸ Her exhibits showed differences in percentages of small businesses in the different Qwest geographic markets, and concluded that customers in areas where small businesses predominate are more captive to Qwest than those in areas with relatively fewer small businesses.¹⁵⁹ She provided an exhibit showing that there are [See Confidential Attachment] Qwest mass market customers (those with fewer than 4 lines per location) and [See Confidential Attachment] small/medium customers (those with four or more lines per location).¹⁶⁰ In her view, these small customers are not likely to be served by CLECs.¹⁶¹

¹⁵⁵ Ex. 1T, pp. 20-1.

¹⁵⁶ Ex. 103T, pp. 15-16.

¹⁵⁷ Ex. 201T, p. 26.

¹⁵⁸ Ex. 401T, p. 36.

¹⁵⁹ *Id.*, citing Ex. 411C.

¹⁶⁰ Ex. 412C.

¹⁶¹ Ex. 401T, p. 37.

Discussion

The Commission may not reclassify a service unless it concludes that the service is subject to effective competition, which requires that the carrier's customers have reasonably available alternatives and the carrier does not have a significant captive customer base. In assessing the existence of these statutory criteria for effective competition, the Commission looks to the four factors discussed in this section.¹⁶² When the Commission last addressed this criterion in the context of local service reclassification, it found that Qwest did have a significant captive customer base for business exchange services in all but a few exchanges.¹⁶³ Likewise, the Staff argued that, without the imposition of conditions, there would be a significant captive base of small business customers.¹⁶⁴ Given these considerations, DoD/FEA would have expected that Qwest -- and the Staff -- would pay particular attention to the issue of whether the captive base for small business customers still exists. Instead, with their definition of the product market being all business customers, no such showing was made.

DoD/FEA believes that the data contained in the confidential exhibits of Public Counsel witness Baldwin cited above, along with her explanation of their significance, support the conclusion that a captive base exists for small business customers in most if not all of the Qwest service area. The record is simply lacking in evidence and reasoned analysis to show that the Commission's prior conclusions in this regard are no longer valid.¹⁶⁵ Moreover, it is clear that a significant captive base exists in at least one

¹⁶² WAC 480-121-061(5).

¹⁶³ *2000 Reclassification Order*, para. 68.

¹⁶⁴ *Id.*, para. 71. The Commission determined that it could not impose future conditions to eliminate the significance of existing captive base. *Id.*

¹⁶⁵ On cross-examination, Staff witness Wilson pointed out that there were data and analyses on different segments (basic business, PBX, and Centrex) of that broad "relevant" market. Tr. 1275-6; 1411;1507-8. However, not only does Mr. Wilson utilize a flawed proxy for the small business market, but he also

exchange where there is no CLEC presence at all, and the captive base no doubt exists in the five exchanges where only one CLEC operates.¹⁶⁶ As to Mr. Shooshan's belief that there can be no captive base if "customers have choices," we note that there is no evidence in the record that small businesses have any choice of providers in exchanges served by few (or no) CLECs, because no evidence was presented to show that such CLECs actually offer small business service. Nor are there any data in the record to show the number or types of customers served by CLECs, as discussed above.

A captive customer base may exist for other than small business service. The data compiled by the Staff, and that provided by Qwest, show a remarkable lack of competition for Centrex services, and that in some exchanges CLECs provide no Centres and PBX services at all.¹⁶⁷ Although these customers are large users of telecommunications services, they remain reliant on Qwest.

V. OTHER ISSUES

A. Impact of Other Dockets (TRO, Cost Docket, etc.)

The Commission initiated Docket UT-033025 by its August 22, 2003, "Notice Inviting Comments Concerning Process for Implementing FCC Triennial Review Order." The Notice invited interested parties to file comments on certain procedural issues associated with the Commission's implementation of the *Triennial Review Order*, which required state commissions to conduct proceedings involving the continued availability of UNEs within specified time periods. Pursuant to the filing deadlines established in

combines it with the medium-size segment, thereby masking the presence of captive market evidence for this vulnerable segment. Tr. 1411-4. His rudimentary breakdown, assumptions (Tr. 1412-3), and anecdotal experiences (Tr. 1275-6) are just inadequate to support a finding of no captive customer base.

¹⁶⁶ Tr. 1433-4.

¹⁶⁷ Ex. 201T, p. 14; Ex. 204C, p. 4; Tr. 1388-9.

Docket No. UT-033025, Qwest filed, on October 10, 2003, the "Petition of Qwest Corporation to Initiate a Nine-Month Case Under the Triennial Review Order." In that Petition, Qwest requests the Commission to initiate a proceeding to review the FCC's findings as to impairment for its provision of mass-market switching and dedicated transport as UNEs. The Commission initiated such a proceeding under Docket No. UT-033044, and by Order No. 1 in that Docket established a procedural schedule. The first round of testimony and exhibits is scheduled for December 19, 2003.

Parties' Positions

Qwest witness Shooshan, anticipating the filing of a Qwest petition, testified that such a proceeding need not affect the Commission's decision in this proceeding. As he stated it:

... if the Commission were to find that removing unbundled switching from the list of required UNEs in Washington would not impair competition, it will be because the Commission itself has determined that there are competitively supplied alternatives readily available.¹⁶⁸

Staff witness Wilson briefly addressed the FCC's decision and anticipated Commission implementation thereof, noting that UNE-P based competition represents only about 25% of the CLEC loops in the relevant market.¹⁶⁹ He testified on cross-examination that he had not considered in his testimony and recommendations the impact of the elimination of UNE-P or any increase in loop costs.¹⁷⁰

Other witnesses disagreed with the Qwest position that a proceeding considering the removal of mass-market switching from the list of required UNEs is not relevant to

¹⁶⁸ Ex. 101T, p. 16.

¹⁶⁹ Ex. 201T, p. 10.

¹⁷⁰ Tr. 1400. He also testified on cross-examination that he did not consider in his analysis the impact on the telecommunications market of the grant of Section 271 authority to Qwest. Tr. 1404.

the subject Petition. Public Counsel witness Baldwin stated that the FCC's decision may provide useful ways to analyze market structure, and if the Commission decides this case before completing an impairment proceeding, the Commission may arrive at contradictory conclusions regarding the extent of competition.¹⁷¹ She also found relevant the Commission's proceeding in Docket Nos. UT-023003 and 033034 as to the local loop costs.¹⁷² MCI witness Gates stated that if UNE-P were eliminated -- that is, if the Commission should find that there is no impairment if Qwest is not required to provide mass-market switching as a UNE -- the ability of CLECs to compete would be significantly impaired. He noted that UNE-P is a primary market entry strategy for new carriers, allowing carriers without facilities in an area to accumulate customers, and stated that the Staff approach to this matter seems to downplay the importance of UNE-P.¹⁷³

Discussion

DoD/FEA believes that Qwest's approach to this issue is greatly oversimplified. It is clear that the removal of the mass-market switching UNE would affect the manner in which competitive local service is provided, and a transition would not lessen that impact. Qwest's data show that the lines that CLECs provide to business customers by means of UNE-P grew by 45% in the year ended December 31, 2002.¹⁷⁴ If the preferred method of entry by carriers lacking their own facilities is eliminated, the growth in CLEC lines will doubtless be slowed until new assessments of entry and service strategy can be accomplished. Moreover, such a finding in Washington might encourage CLECs to enter

¹⁷¹ Ex. 401T, p. 62.

¹⁷² *Id.*, p. 63

¹⁷³ Ex. 501T, pp. 59-60; Ex. 504T, p. 31.

¹⁷⁴ Ex. 1T, p. 13.

or expand in other states where UNE-P is available. As the Commission stated in the *2000 Reclassification Order*, "... we must also have confidence that competitors *are* offering and *will* offer competitive services."¹⁷⁵

While Staff witness Wilson, as noted previously, calculated the Qwest market share to be 76.8% (without UNE-P and resale), there are no data in the record as to the number and types of customers served by CLECs, as discussed in Section IV.D1 above. Thus, the impact of the elimination of UNE-P on the individual "market segments" in total or by geographic area is unknown. Similarly unknown is the impact of an UNE-P elimination upon any captive customer base analysis.

Accordingly, the Commission should afford the possibility of the elimination of UNE-P due consideration in its decision herein by taking, as we suggested in the introduction, a measured and incremental approach to reclassification.

B. Cost Floor

MCI witness Stacy testified that if the Commission grants some degree of reclassification, it should at a minimum impose a price floor below which Qwest would not be allowed to set retail rates.¹⁷⁶ He recommended that as cost components the Commission use the imputed costs of the UNEs used to provide the service and a measure of minimum retail related costs.¹⁷⁷ Qwest witness Reynolds stated in rebuttal that the Commission does not need to establish a price floor, as it has the authority that it needs to ensure that rates are just and nondiscriminatory.¹⁷⁸ Staff witness Wilson disagreed that the Commission concern itself herein with below-cost pricing because the

¹⁷⁵ *2000 Reclassification Order*, para. 66. Italics in original.

¹⁷⁶ Ex. 601T, p. 8.

¹⁷⁷ *Id.*

¹⁷⁸ Ex. 7RT, p. 10.

price floor applicable to Qwest's offerings is well known and established in other dockets.

In his view, prices reflecting TELRIC would suffice as price floors for services provided following reclassification.¹⁷⁹ However, Mr. Wilson on cross-examination conceded that he was not recommending a price floor mechanism in this proceeding.¹⁸⁰ On cross-examination from the Bench, he emphatically stated "... it hasn't been analyzed, discussed, there hasn't been cost study analysis done in this case, and it isn't necessary to do that."¹⁸¹

Discussion

DoD/FEA acknowledged in the Introduction its concerns about the anti-competitive and anti-consumer practices that can occur if a carrier is freed from regulation before competitive markets can constrain prices and practices. However, we do not see a need for the Commission to establish pricing principles on the form of a specific floor in this proceeding, should it grant reclassification in whole or in part. Parties requested that the Commission establish a price floor in Docket No. UT-000883, but the Commission declined to do so.¹⁸² The Commission noted that the existing rates had been approved by the Commission, having been shown to be above the costs of providing the service.¹⁸³ No need exists to anticipate and resolve an issue that is not required by statute at this time.

¹⁷⁹ Ex. 210TC, pp. 2-3.

¹⁸⁰ Tr. 1419-20.

¹⁸¹ Tr. 1491.

¹⁸² *2000 Reclassification Order*, para. 77.

¹⁸³ *Id.*

C. Access Charges

MCI witness Gates testified that access charges must be reduced to cost—based levels. He stated that alternative toll providers must pay Qwest for access, and the access rates are not priced at TELRIC levels. In his view, access charge reform -- accomplished in a separate proceeding -- is required before Qwest's business service is reclassified as competitive.¹⁸⁴ No other party supported the view that access charge reform is a necessary antecedent to reclassification. Qwest witness Reynolds disagreed, citing the statute prohibiting subsidization of local service through access charge revenues.¹⁸⁵

DoD/FEA disagrees with the proposition that access charge reform is required before business service can be reclassified as competitive. The issues appear to be distinct enough to warrant independent consideration. Moreover, the Commission made no such finding in the *2000 Reclassification Order*, in which it reclassified certain Qwest business services in four exchanges.

D. Proposed Conditions on Approval

Because DoD/FEA believes that the Commission must deny the Petition in its entirety, we have no recommendations as to proposed conditions that might be applicable upon approval. We note again that the Commission has previously held that it is without authority to grant reclassification with conditions if it concludes that there exists a significant captive customer base.¹⁸⁶

¹⁸⁴ Ex. 501T, pp. 52-59.

¹⁸⁵ Ex. 7RT, pp. 12-3.

¹⁸⁶ *2000 Reclassification Order*, para. 71.

VI. CONCLUSION

DoD/FEA's review of the extensive record in this proceeding leads to the conclusion that the Commission must deny the Petition. As we have shown above, Qwest improperly defined both the product market and the geographic market. Although other carriers offer competitive services in some areas, the record does not disclose sufficient activity throughout the state such that the competitive market could constrain Qwest's prices and practices. Indeed, several exchanges are served either by no CLEC or only one competitor. All exchanges show a high degree of concentration -- not one has an HHI below the threshold that the staff and Commission used in the *2000 Reclassification Order* and inclusion of the CLEC-owned lines would not change that fact. Facilities-based competition, the type of competition that **could** replace regulatory oversight, comprises only about one-fifth of the CLEC lines. However, crucial data concerning the number of customers served and their relative sizes are not part of the record of this proceeding. Small business customers would doubtless be left with few alternatives in areas, and thus Qwest retains a significant captive customer base.

Respectfully Submitted,

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For
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And
All Other Federal Executive Agencies

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