CONFIDENTIAL PER PROTECTIVE ORDER
IN UTC DOCKET UT-100820

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the matter of, Joint Application of Qwest Communications International Inc. and CenturyTel, Inc. for Approval of Indirect Transfer of Control of Qwest Corporation, Qwest Communications Company LLC, and Qwest LD Corp.	Docket No. UT-100820

RESPONSIVE TESTIMONY

OF

JAMES A. APPLEBY

SPRINT NEXTEL CORPORATION

SEPTEMBER 27, 2010

REDACTED VERSION

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I. INTRODUCTION AND QUALIFICATIONS

Q. Please state your name and business address.

A. My name is James A. Appleby. My business address is 6450 Sprint Parkway, Overland Park, Kansas 66251.

Q. **What is your position and who are you representing in this proceeding?**

A. I am employed as a Regulatory Policy Manager for Sprint United Management Company, and I am testifying on behalf of Sprint Communications Company L.P., Sprint Spectrum, L.P., Nextel West Corp., and NPCR, Inc. (collectively, "Sprint Nextel" or "Sprint"). Sprint Nextel is a provider of wireline long distance service, wireless communications services, and wholesale services to cable providers in Washington.

Q. Please summarize your educational background and business experience.

A. I hold a Bachelor of Science degree in accounting from Shippensburg University in the state of Pennsylvania, and I became a Certified Public Accountant in Pennsylvania in 1989. I have been employed by Sprint since 1989. I began working with Sprint's Regulatory Policy Group in 1996, and in my current position as Regulatory Policy Manager I am responsible for the development of state and federal regulatory and legislative policy for all divisions of Sprint Nextel. I am also responsible for the coordination of regulatory policy across business units. The policy issues I oversee include, among others, intercarrier compensation, universal service support, service pricing, access charge reform, reciprocal compensation, and local competition.

Q. Have you previously testified before other state Commissions?

A. Yes. In my position as a manager of regulatory policy issues I have testified before the Public Service Commission of South Carolina, the Missouri Public Service Commission, the Indiana Utility Regulatory Commission, the Michigan Public Service Commission, the New Jersey Board of Public Utilities, the Virginia State Corporation Commission, the Nebraska Public Service Commission, the Kansas Corporation Commission, the Arizona Corporation Commission, the Illinois Commerce Commission, the Pennsylvania Public Utility Commission, and the Iowa Utilities Board. I have also testified before various state legislative committees on regulatory issues. Additionally, I routinely work with the Commission staffs in the states where Sprint Nextel provides services, as well as with the staff of the Federal Communications Commission ("FCC").

II. SUMMARY OF TESTIMONY

Q. Please summarize your testimony.

A. The proposed merger of CenturyLink and Qwest ("Petitioners") is a significant transaction that would nearly double the size of Qwest nationally, which is one of the Regional Bell Operating Companies ("RBOC") created by the AT&T divestiture. Within Washington, the combination of Qwest and CenturyLink (which I refer to in my testimony as the "Merged Firm") would increase the holding company's ILEC access line market share to approximately 74%. The Merged Firm will also increase its market concentration in the long distance, enterprise, and broadband markets. In short, the Merged Firm will have significantly increased market power nationally, as well as in Washington. The proposed merger therefore has the potential to cause substantial harm to the competitive balance within the telecommunications marketplace. This means the Washington Utilities and Transportation Commission ("Commission") should reject the merger absent appropriate conditions that not only mitigate potential harms to the public interest created by the merger, but also ensure that the benefits from the purported synergies created by combining the CenturyLink and Qwest companies are realized by Washington consumers and competitive carriers.

WAC 480-143-170 directs the Commission to determine if merger transactions are consistent with public interest. Further, the examination of public interest includes a list of factors one of which is "[t]he impact on competition at the wholesale and retail levels, including whether the transaction might distort or impair the development of competition."[1] In my testimony, I propose several conditions to mitigate the potential competitive harm posed by the proposed merger's concentration of market power in the Merged Firm. These include: (1) correcting the Merged Firm's discriminatory intrastate switched access rate structure; (2) requiring it to adopt cost-saving practices with respect to existing interconnection agreements; and (3) mandating its compliance with recognized best carrier-to-carrier business practices to avoid impairing competition. Petitioners object to the inclusion of the issue of its intrastate access charges in this merger proceeding but the ALJ has ruled that the access charge issues affect competition and are within the purview of the Commission's inquiry. The ALJ

[1] *See the Matter of the Joint Application of Verizon Communications Inc., and Frontier Communication Corporation For an Order Declining to Assert Jurisdiction Over, or, in Alternative, Approving the Indirect Transfer of Control of Verizon Northwest, Inc.*, Docket UT-090842,Order 06, Final Order Approving and Adopting, Subject to Conditions, Multiparty Settlement Agreements and Authorizing Transaction (April 16, 2010) at p. 53.

ruled in favor of Sprint on a motion to compel the production of access charge information from the Petitioners stating:

> Commission Staff pointed out, in its support for Sprint's late-filed petition, our examination of a merger's impact on the public interest includes several factors, one of which is "the impact on competition at the wholesale and retail level, including whether the transaction might distort or impair the development of competition." Staff suggested, and rightly so, that the mergers impact on access charges and competition is within the purview of our examination.[2]

Q. Do you sponsor any exhibits with your testimony?

A. Yes. I sponsor Exhibits JAA-1 through JAA-5, attached to my testimony, which illustrate the competitive advantage the Merged Firm will receive from access services, estimates of change Sprint's recommended condition will have on the Merged Firm's access charges and documents the financial strength of the two corporations that would become the Merged Firm if the merger is approved.

III. THE CONCENTRATED MARKET POWER OF THE MERGED FIRM WILL ADVERSELY IMPACT COMPETITION IN WASHINGTON

Q. Have Petitioners provided information about the increase in the magnitude of its operations if the merger is permitted?

A. Yes. CenturyLink states that the Merged Firm will serve a nationwide total of 17 million access lines, more than 5 million broadband customers,[3] over 1.4 million video subscribers, and 850,000 wireless customers.[4] The Merged Firm will have

[2] Docket UT-100820, Order 09, pp. 7-8.
[3] Jones Direct, p. 8, ll. 17-18.
[4] http://news.qwest.com/centurylinkqwestmerger (last viewed August 5, 2010).

access lines in 37 states, more than any other ILEC holding company and will be the largest ILEC in more states, 15, than all other ILECs except AT&T. This significantly larger company will have a greatly enhanced ability to wield market power to the detriment of both consumers and competitors, and the harm will be even greater in the markets for several telecommunications and broadband services.

Q. Does the merger concentrate the Merged Firm's market-share in Washington?

A. Yes. The Merged Firm will increase its market-share of Washington ILEC lines to 74%. Using Qwest's current 1.5 million lines as a base, the merger will result in an increase of approximately 13.3% to 1.7 million lines.[5]

Q. Will the Merged Firm have a facility-based long distance service provider?

A. Yes. It will have its own facility-based long distance service provider, Qwest Communications Company, LLC ("Qwest LD").

Q. What is the financial benefit for Merged Firm of adding a facility-based long distance provider?

A. The Merged Firm will enjoy an unwarranted advantage on terminating switched access and special access circuits over a broader swath of customers.[6]

Q. Please explain this financial benefit.

A. Qwest LD services can be provisioned to customers within the legacy CenturyLink service territories without incurring the inflated switched and special access charges CenturyLink imposed on Qwest when it was a competitor of CenturyLink. Thus,

[5] Reynolds Direct, p. 11, ll. 6-9.
[6] In the merger of Verizon and MCI, the MCI Board cited these "access economics" as one reason for its acceptance of the revised proposal from Verizon. MCI Press Release, *MCI Accepts Revised Proposal From Verizon* (March 29, 2005).

Qwest LD's offerings in the enterprise and mass markets will avoid these onerous input costs, unlike other service providers competing in the enterprise and mass markets who will continue to be burdened by the inflated access charges of the legacy CenturyLink ILECs.

Q. Please explain this reduction in input costs for Qwest LD.

A. Switched and special access service costs are a significant portion of the costs of providing mass market and enterprise services. Accounting rules will require the Merged Firm to eliminate an equal amount of access service costs and access service revenue on the consolidated corporation books to reflect intra-company access service transactions. As a result, the only real financial impact of the access services provided within the corporation will be the actual economic cost of those services. The Merged Firm can therefore price its services to cover only its true economic cost of the network functionality that the CenturyLink ILECs provide rather than that cost <u>plus</u> the inflated access service charges that all other long distance carriers must pay, and that Qwest's long distance arm had to pay before the merger. With the vast difference between the true cost of access services (both special and switched access) and the inflated cost resulting from CenturyLink's excessive access charges, the Merged Firm will possess a substantial input cost advantage over all other non-affiliated providers trying to serve the market.

The other carriers attempting to compete in the markets with Qwest LD will continue to face those excessive switched and special access charges, and will not be able to compete as vigorously on price as they would if the Merged Firm's access charges were set at economic cost. That is because Qwest LD will either price its retail long distance services below the level a competitive long distance carrier can, in which case Qwest can eliminate competition. Or Qwest LD will price its retail long distance service at a level that reflects the inflated access charges CenturyLink imposes on all the long distance competitors so Washington consumers will not get the lower price they could if competitors were provided non-discriminatory access service at cost-based rates. Either way, competition and consumers are harmed. Without correcting the discriminatory access rates that would result from the proposed merger, the merger will adversely affect competition in the enterprise and mass market long distance services markets to the detriment of Washington consumers.

Q. Will this reduction in input costs for Qwest LD also adversely affect long distance service competition within legacy Qwest ILEC service areas?

A. Absolutely. Legacy Qwest ILEC switched and special access rates are also greatly inflated. The vertical integration of an ILEC and long distance service provider gives a competitive advantage to the combined service provider.

Q. Will Qwest LD alone benefit from the discriminatory access rate structure that results from the proposed merger?

A. No. In addition to Qwest LD, the merger will vertically integrate non-facility based interexchange carriers (IXCs) CenturyTel Long Distance, LLC (CenturyTel LD) and Embarq Communications, Inc. (Embarq LD) with the Merged Firm. All of the Merged Firm's IXCs will thus enjoy discriminatorily favorable costs for interstate and intrastate switched and special access within their legacy local service territories, i.e., CenturyTel LD and Embarq LD in CenturyLink local service territory, and Qwest LD within Qwest local service territory.

Q. Have Qwest and CenturyLink disputed high access services will provide a competitive advantage to the Merged Firm?

A. Yes. CenturyLink and Qwest stated they believe as long as the individual legal entities within the Merged Firm continue to invoice each other from access services in accordance with tariffs underlying those charges, there can be no competitive advantage for any one of the Merged Firm's legal entities in the market.[7]

Q. Do you believe that view is accurate?

A. No. Each of the filing entities within the Merged Firm will be owned by a common set of shareholders. Each filing entity within the merged firm will have a fiduciary responsibility to that common group of shareholders to maximize the Merged Firm's profits. The goal of any one of the legal entities is not to maximize its own profits but instead to maximize the total profits of the Merged Firm. All business decisions will be made with this goal in mind. I know this to be true because Sprint also has many business interests. To the extent more than one of our businesses is impacted by a decision, the good of the full corporation is the most important factor the company considers in that decision.

Q. Can you provide an example of how this fiduciary responsibility would change the way the Merged Firm's filing entities operate in the market?

A. Yes. My example focuses on the telecommunications need of a hypothetical medium sized business located within a CenturyLink local service territory in Washington.

[7] Qwest and CenturyLink Response to Sprint DR 3; also see pages 2-3 of Qwest's and CenturyLink's Joint Answer to Sprint's Motion to Compel in this docket (filed August 20, 2010).

ABC Company has voice and data service needs. With 3 T-1 special access circuits, a carrier can connect ABC Company to the carrier's network for the provision of voice and data services. In addition to other self-provisioned network components, the carrier also would have to terminate ABC's voice traffic to other LECs including CenturyLink ILECs in Washington and across the nation. To serve this customer prior to the merger, Qwest LD and Sprint LD would each need to purchase the 3 T-1s from the CenturyLink ILEC and incur terminating access charges, both intrastate and interstate to complete ABC's voice calls. Each of these access services are priced far above the actual cost,[8] but the high switched and special access rates of the CenturyLink ILEC impact Qwest LD and Sprint LD equally. To collect a profit on the service provided to ABC and maximize the shareholders return, both Qwest LD and Sprint LD would be forced to price its retail service offering to ABC to recover the access costs imposed by the CenturyLink ILEC.

Let's now assume the merge is complete. Qwest LD and CenturyLink ILECs are part of the same Merged Firm. The merger has not changed Sprint or any other carrier's circumstances to serve ABC Company that are unaffiliated with the Merged Firm. To serve ABC Company telecommunications needs, Sprint and all unaffiliated carriers will still need to pay the same switched and special access charges to the CenturyLink ILEC. Qwest LD's financial view of serving ABC is changed. As discussed above, Qwest LD no longer views the business opportunity as its ability to generate a profit for itself but instead Qwest LD can now view ABC's business as an opportunity for

[8] See Exhibit JAA-2, infra, regarding the estimated amounts that the Merged Firm's switched and special access rates are above cost.

the Merged Firm to make a profit. It is true, Qwest LD will continue to be invoiced by the CenturyLink ILECs for access services; however, Qwest LD does not need to be concerned about the access transactions when setting an offer price to ABC Company. It can price its retail service offering to ABC Company without regard for the access costs that are internal to the Merged Firm. As long as the Qwest LD retail offering to ABC wins the bid and the price is above the actual cost of the services provided to ABC by all legal entities inside the Merged Firm, the Merged Firm has generated a profit on ABC's services. The Qwest LD pricing decision in its bid for ABC's service no longer needs to be concerned with the access costs it incurs internally within the Merged Firm. The pricing decision can be based on the much lower actual cost of the access functions. The merger transaction clearly provides Qwest LD with a competitive advantage over Sprint and all other non-affiliated carriers attempting to serve ABC Company's communications needs.

Q. Can you provide some financial context to the above example to demonstrate the competitive advantage the Merged Firm will possess in the market?

A. Yes. The Merged Firm will be both a wholesale and retail service provider within its local service territories after the merger. Let's assume one of its T-1s in the example cost $100 to produce and the price is $200. The unaffiliated IXC's retail bid must cover the price of the 3 T-1s or $600 to earn a profit for its corporation. The affiliated IXC's retail bid need only cover the cost of the 3 T-1s or $300 to earn a profit for its corporation.

Q. Why does the Merged Firm earn a profit at a lower price point?

A. Accounting Rules require the Merged Firm to eliminate the intra-company or internal financial transactions on its consolidated books. The $600 expense to the merged Firm IXC legal entity for the 3 T-1s and the $600 access revenue of the Merged Firm ILEC for the 3 T-1s are removed from the consolidated books. The financial transactions that remain in the consolidated corporation books are the retail revenue the Merged Firm collected from XYZ Company and the actual cost of the 3 T-1s incurred by the Merged Firm's ILEC.

Q. If the Merged Firm IXC sold retail service to XYZ for example at $550, would the Merged Firm earn a profit of $250? Would the unaffiliated IXCs be unable to match the retail offer?

A. The answer is yes to both. The Merged Firm would earn $250.[9] Unaffiliated IXCs because they pay the $200 price for each of the three T-1s could not match the $550 retail offer unless the unaffiliated IXC wished to sell service to ABC Company at a loss of $50.[10]

Q. Is this the competitive advantage Sprint is concerned about?

A. Yes. The Merged Firm can utilize its ability to sell wholesale services at far above cost based-rates, the T-1s in the example, to their advantage in the retail market. The only fix to this problem is to reduce the Merged Firm ILEC wholesale rates.

Q. In addition to the T-1 costs, the example above includes the cost the IXC will incur to complete ABC's voice calls. Since CenturyLink's switched access rates

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[9] The Merged Firm would generate a profit of $250 (retail price of $550 minus the 3 T-1s <u>cost</u> of $300).
[10] The Unaffiliated IXCs loss of $50 to match the Merged Firm IXC offer (Retail price of $550 minus the 3 T-1s <u>price</u> of $600).

are also above cost, does the Merged Firm also enjoy the same kind of competitive advantage on minute of use access charges?

A. Yes. For example, the intrastate access rate of Qwest is $.0228 and the cost is no higher than $.0007. The intrastate switched access service margin provides the Merged Firm the same type of competitive advantage in competing for the retail services of ABC Company as the T-1 wholesale services. In other words in this example the Merged Firm has a competitive advantage on both the originating and terminating sides of the retail service provided to ABC Company.[11]

Q. Do almost all voice service offerings in the market include non-local calling and accordingly the Merged Firm invoices access charges on all of those calls?

A. Yes. The Merged Firm ILECs invoices access charges to nearly all providers of voice service in today's market. Competitive carries rarely provide voice service without the ability to place non-local calls and the number of local customers where the Merged Firms ILECs provide only local voice is also quite small.[12] Accordingly, the competitive retail providers incur the inflated access charges and are competitively disadvantaged in comparison to the Merged Firm's voice service offerings in the market because of the above cost switched access charges of the Merged Firm.

Q. How significant is the intrastate switched access cost-per-minute advantage the IXCs in the Merged Firm will have over all other long distance service providers?

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[11] The Qwest interstate switched access service rates are far above cost and provide a competitive advantage to the Merged Firm; see Exhibit JAA-2.

[12] CenturyLink and Qwest supplemental responses to Sprint DR 6 **[Begin Confidential Data]** [redacted] **[End Confidential Data]** residential lines purchase only local voice service.

A. Exhibit JAA-1 shows the change in cost the Merged Firm will experience by internalizing the intrastate switched access costs. In the legacy CenturyTel of Washington service area for example, Qwest LD will no longer experience the $.0786 per minute intrastate access charges. Instead it will incur the incremental cost to terminate traffic, which several parties have demonstrated is likely far less than the current Internet Service Provider ("ISP") reciprocal compensation rate level of $.0007.[13] Using the rate of the FCC's ISP Remand Order, Qwest LD will also avoid at least $.0781 per minute or 99% of the CenturyTel of Inter Island tariffed intrastate switched access rate, and $.0265[14] per minute or 97% of the legacy Embarq/United telephone of Northwest tariffed rate. Finally, CenturyTel LD and Embarq LD will avoid 97%, or $.0221 of Qwest's inflated intrastate switched access tariff charges. Meanwhile, the competitors of the Merged Firm will not be able to avoid the expenses caused by its intrastate switched access rates.

Q. Is the magnitude of the intrastate switched access charges between the Merged Firm's long distance service providers that will be internalized as a result of this merger significant? [15]

A. Yes. CenturyLink ILECs in Washington billed Qwest LD nearly **[Begin Confidential Data]** [redacted] **[End Confidential Data]** in intrastate switched access charges in 2009. Qwest's ILEC billed CenturyLink **[Begin Confidential Data]** [redacted] **[End Confidential Data]** in intrastate switched access charges

[13] Order on Remand and Report and Order and Further Notice of Proposed Rulemaking, Docket No. 08-262 (rel. Nov. 5, 2008).
[14] Cost change reflects the changes Embarq/United Telephone of Northwest made on rates on March 12, 2010 and will make on 1-1-2011 and 1-1-2012 as documented in CTL response to Sprint DR 21
[15] See Exhibit JAA-2.

in 2009. This data does not include the access charges paid to Qwest by CenturyLink's wholesale long distance provider, Sprint. Sprint incurs intrastate switched access charges for CenturyLink retail customers. Unfortunately, Sprint is unable to separately identify the access cost it incurs for this wholesale business versus other Sprint traffic terminated to Qwest. But there certainly is an additional cost above the amount the Merged Firm identified. Therefore, in total at least **[Begin Confidential Data]** [redacted] **[End Confidential Data]** in intrastate switched access cost that once were costs incurred to unaffiliated companies will now be contained within the Merged Firm. It is clear that competitors would continue to be encumbered by Qwest's and CenturyLink's excessive access rates, while 97% to 99%, the service margins above actual cost, of this intrastate switched access cost disappears for the Merged Firm's affiliated long distance service providers post merger, thus giving them at least **[Begin Confidential Data]** [redacted] **[End Confidential Data]** cost advantage in the competitive market.

Q. Is the same true for interstate switched access costs?

A. Yes. Just like the intrastate switched access costs, interstate switched access costs between Qwest and CenturyLink will become internal transactions within the Merged Firm. The Merged Firms disclosed **[Begin Confidential Data]** [redacted] **[End Confidential Data]** in interstate switched access costs between the companies that results in a competitive advantage of approximately **[Begin Confidential Data]** [redacted] **[End Confidential Data].**[16] [17]

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[16] Id.

Q. Finally does the Merged Firm derive competitive advantage from the special access charges that will become internal transactions for the Merged Firm?

A. Yes. Like switched access services, special access services are priced far above the actual cost of those services, the magnitude of the overcharges varies by special access service. Sprint believes the special access prices are on average 50%-100% higher than comparable UNE service prices. These excessive margins create a competitive advantage for the Merged Firm on all services that require ILEC special access services as wholesale inputs. The Merged Firms disclosed approximately **[Begin Confidential Data]** [redacted] **[End Confidential Data]**[18] in interstate special access costs between the companies. The excess margin on those services would approximate **[Begin Confidential Data]** [redacted] **[End Confidential Data].**[19]

Q. What is the total amount of competitive advantage the access services will provide to the Merged Firm?

A. The excessive margins on The Merged Firm's intrastate and interstate switched access and special access services will generate more than **[Begin Confidential Data]** [redacted] **[End Confidential Data]**[20] in competitive advantage for the Merged Firm in Washington only. The Merged Firm will generate far more advantage nationally.

[17] Sprint also incurs interstate switched access costs in conjunction with the provision of wholesale long distance service to CenturyLink IXCs. Sprint is unable to quantify the additional amount of access expense it incurs beyond the amount disclosed by the Merged Firm.
[18] CenturyLink and Qwest responses to Sprint DR 14.
[19] See Exhibit JAA-2
[20] Id

Q. Will the access service cost differential between the Merged Firm's affiliated IXCs and competitive IXCs increase the magnitude of the traffic between the Merged Firm's ILECs and IXCs?

A. Yes. Driven by the access service cost advantage and the ability to bundle multiple services together, the Merged Firm will undoubtedly experience an increased amount of traffic between the ILECs and their affiliated IXCs going forward.

Q. What would the effects of that be on competition?

A. The Merged Firm will be in a position to create a product no other provider can match, namely, a service that permits the Merged Firm's customers to call any other Merged Firm customer for free or at a greatly reduced rate.

Q. Please explain why the Merged Firm would be able to do that while competitors would not.

A. The Merged Firm will be able to handle increased traffic volume on a geographically larger network at a much lower incremental costs than its competitors because it will wholly avoid the upward pricing pressures caused by the inflated access rates it imposes on all other carriers using its expanded network. An example of this is Sprint's own Any Mobile Any Time product offering, which permits the subscriber to talk to any other wireless provider's customer without the meter running. Sprint is able to provide this service because it is not required to pay its wireless competitors bloated access service rates. In fact, wireless carriers are precluded by law from requiring IXCs or any other carriers to pay access rates for call termination. So if the Merged Firm is allowed to significantly reduce its own access charge costs on its network while at the same time maintaining artificially high access charges for all competitors using its network, it will enjoy a cost advantage that will allow it to provide service offerings at prices its competitors cannot offer and still remain in business.

IV. THE CONCENTRATED MARKET POWER OF THE MERGED FIRM WILL ADVERSELY IMPACT COMPETITIVE CHOICES FOR WASHINGTONIANS

Q. Do Petitioners believe that competition for telecommunication services is impacting their business?

A. Yes. CenturyLink witness Jones explains, "Competition for voice, Internet, data and video is widespread with increasing competition from wireless companies, cable operators, VoIP providers and new, start-up entities."[21] Thus, "[t]he pressure on all of these companies to be responsive, invest and innovate is intense."[22]

Q. Do Petitioners believe that the merger will improve their ability to compete?

A. Yes. Mr. Jones states that the Merged Firm "will be better situated, both financially and operationally, with more flexibility to meet the challenges of a rapidly changing and intensely competitive communications environment."[23]

Q. Do the Petitioners acknowledge the value of competitive choice to customers?

A. Yes. Mr. Jones states "[h]ealthy competition is in large part driven by the existence of a variety of viable network platforms in a given market. Competition is most

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[21] Jones Direct, p. 7, ll. 14-16.
[22] Jones Direct, p. 7, ll. 17-18.
[23] Jones Direct, pp. 9-10, ll. 21, 1-2.

robust in markets where there is intermodal competition: that is, where services are being delivered over wireless, wireline and cable platforms."[24]

Q. Will CenturyLink no longer be a competitor in Qwest service areas and Qwest not a competitor in CenturyLink areas?

A. Yes. The merger will reduce the number of competitive alternatives in the market for Washington businesses. Qwest and CenturyLink provide actual competition to one another in their service territories in Washington. **[Begin Confidential Data]** [redacted] **[End Confidential Data]**[25] CenturyLink has acknowledged it provides Ethernet services in competition with Qwest in Qwest service areas.[26] CenturyLink continues to hide the magnitude of that business from parties in this case.[27] In addition, since they already provide service in each other's territory, there are the additional competitive benefits flowing from the threat of expansion of competitive efforts and potential competition. If the merger is completed, Qwest will no longer be an actual or potential competitor in CenturyLink territory and CenturyLink will not be an actual or potential competitor in Qwest territory. Any reduction in the number of actual or competitive alternative service providers will adversely impact competition.

Q. Even if one ignores the adverse impact on competition flowing from the loss of actual and potential competition, will the merger truly enhance competition if it

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[24] Jones Direct, p. 14, ll. 15-18.
[25] Qwest response to Sprint 41.
[26] CenturyLink response to Sprint 42.
[27] Despite being compelled to produce the data, CenturyLink initially labeled its response to Sprint DR 42 as highly confidential precluding me from reviewing the data. Sprint filed an objection to that designation. As of this writing, CenturyLink claimed it would redesignate the information as confidential but I still have not seen it.

generates a lop-sided competitive advantage for the Merged Firm over competing carriers?

A. No. If the Merged Firm is permitted to burden competing carriers so as to delay their introduction of new services or their entry into new markets, or is permitted to continue to impose inflated switched access rates- or simply artificially increase the costs competitors incur to interconnect to the Merged Firm's expanded network- telecommunications service choices and pricing for Washington customers will be adversely impacted.

Q. Does the Merged Firm have more potential to engage in anti-competitive behavior within its expanded footprint?

A. Yes. The synergies and economies of scale and scope created by this merger increase the Merged Firm's ability as the sole manager of the dominant ILECs in a much, much larger service territory to engage in anticompetitive behavior more than legacy Qwest or legacy CenturyLink could do absent the merger. Further, the increased number of competitors the Merged Firm will face within its much larger service area increases its incentive for such behavior. The FCC has acknowledged the harms associated with primarily horizontal ILEC mergers. Recently, the FCC stated in the CenturyTel/Embarq Order that "we find that the increase in size of CenturyTel's study area resulting from the merger may increase its incentive to engage in anticompetitive activity, although we think it is likely to have a lesser effect in the instant case than in the BOC mergers."[28] In contrast to the CenturyTel/Embarq

[28] *In the Matter of Applications Filed for the Transfer of Control of Embarq Corp. to CenturyTel, Inc.*, Memorandum Opinion and Order, WC Docket No. 08-238, FCC 09-54 (June 25, 2009) ("CenturyTel/Embarq Order"), ¶ 33.

merger, this merger between CenturyLink and Qwest does involve a Bell Operating Company (BOC). Therefore, the incentive to engage in anticompetitive behavior explained by the FCC is even more real and must be addressed.

Q. Are merger conditions necessary to maintain the current competitive balance and improve the competitive landscape going forward?

A. Yes, conditions are necessary. CenturyLink has testified to the value of intermodal competition to customers, and that the merger will improve the Merged Firm's competitive position in this regard. The conditions Sprint recommends are meant to ensure that customer choice among intermodal providers is not reduced or otherwise negatively impacted by the merger, but instead maintained so that it can be improved over time.

V. THE MERGER'S SYNERGY SAVINGS SHOULD BENEFIT ALL CUSTOMERS, INCLUDING WHOLESALE CUSTOMERS

Q. What synergy savings have Petitioners identified for the Merged Firm?

A. Petitioners announced they anticipate the Merged Firm will save $575 million annually in operating expenses in 3-5 years after the merger closes, and an additional $50 million annually in capital expenditure savings as a result of this transaction.[29]

Q. Have Petitioners produced a state-by-state merger synergy savings breakdown?

A. No.

Q. What portion of the merger synergies from the merger transaction should accrue to the operations in Washington?

[29] CenturyLink and Qwest Merger Conference Call of April 22, 2010, slide 6.

A. Merger synergies generally accrue to the overhead functions of the merging companies. Therefore, it is reasonable to allocate the savings to a specific state based on the relative size of the Merged Firm's anticipated state operations post-merger. Using the ratio of Washington access lines to total lines for the Merged Firm, approximately 10%[30] of the total synergies, which is $57.5 million of the $575 million in operating synergies and $5 million of the $50 million in capital synergies, should accrue to Washington operations. The magnitude of these savings suggests Washington wholesale customers should receive some benefits from the merger transaction.

Q. Do you have reason to believe the Merged Firm will achieve those levels of synergy savings?

A. Yes. CenturyLink provides guidance to its shareholders quarterly on the synergy results achieved in its last merger transaction, the purchase of the Embarq local telephone companies. The following is what was provided in its quarterly results press release for the second quarter of 2010:

> CenturyLink achieved approximately $75 million in operating cost synergies during second quarter 2010 and expects to achieve approximately $330 million in annual run rate synergies by year end 2010.[31]

CenturyLink will have achieved $30 million more than the originally forecasted $300 million in merger synergies within 18 months of the close of the Embarq merger

[30] Washington Lines from Reynolds Direct ,p. 11, ll. 6-9; Total Merged Firm lines nationally from Jones Direct, p. 8, ll. 17-18; 1,700,000/17,000,000 = 10%.

[31] CenturyLink Reports Second Quarter 2010 Earnings (rel. Aug. 4, 2010). CenturyLink's increased the anticipated synergy savings to $375 million after the close of the Embarq merger.

on July 1, 2009. CenturyLink originally estimated the synergies could be achieved within the first 3-5 years after the merger.[32]

Q. Are you aware that others have expressed concern about the financial strength of the Merged Firm and question its ability to generate the synergy savings Petitioners have claimed?

A. Yes, I am aware that some intervenors in Washington and other states are concerned that the claimed synergies may not be realized; they focus on how the merger may not be successful, and how competitors and customers should be protected from the fallout of that occurring. I assume, however, that the Merged Firm will make its projected synergy savings because investors will require it and historic results support it. Moreover, Petitioners rely on these savings to support its claim that the proposed merger is in the public interest, and they should therefore be held to those projections in considering what conditions are warranted to accept their public interest claims.

The question therefore is what are the means Petitioners have identified for achieving the projected synergy savings, and do competition and consumers benefit or not from those means? Put differently, does the Merged Firm achieve such large synergy savings by raising costs to competitors like Sprint by reducing wholesale staff, maintaining the existing bloated intrastate switched access rate structure, and cutting corners on OSS integration which makes customer choice more expensive? Or does the Merged Firm achieve savings by integrating best competition practices throughout its greatly enlarged service area so that wholesale and retail customers can benefit from the increased scale, scope, and efficiencies of the merged companies? Synergy

[32] http://www.centurytelembarqmerger.com/keyMaterials.cfm.

savings realized in Washington should not come at the expense of competitor viability and customer choice; merger benefits must be clearly shown to accrue not only to the Merged Firm's investors, but also to the various classes of customers in Washington, as well as the State's other telecommunications carriers.

Q. Do Petitioners indicate any portion of the synergy savings will be passed through to either retail or wholesale customers in the form of lower prices for service?

A. No. CenturyLink's testimony states prices will remain the same through the completion of the merger. Its testimony is then silent as to any future price changes, other than to say such changes will occur in accordance with applicable rules and laws.[33]

Q. Does the Petitioners' testimony detail how wholesale customers will benefit?

A. No. Qwest witness Reynolds does state generally that "customers will benefit from the efficiencies and synergies realized by the combined company,"[34] and then notes in passing that as a result of the merger it will have resources to continue to invest in the deploy fiber to cell sites.[35] But Qwest's ability to generate more revenues in the wireless backhaul market it already dominates within its ILEC service territory doesn't guarantee any benefits to wireless carriers or their customers. If the services provided to wireless carriers are priced like current special access services, far above the actual cost of the services, unaffiliated wireless service providers and consumers

[33] Jones Direct, p. 6, ll. 12-15.
[34] Reynolds Direct, p. 23, ll.13-14.
[35] Reynolds Direct, p. 25, ll. 9-11.

receive no benefit from the Merged Firm's investment in fiber to the cell sites.[36] This is true regardless of whether the services are provided via tariff or via contractual arrangements. And non-wireless wholesale providers receive no benefit whatsoever from fiber-to-cell site deployment.

Q. Does the Merged Firm plan to share any cost savings from the merger with its wholesale customers?

A. No. For instance, switched access service is a monopoly service and without regulatory intervention the Merged Firm has no incentive to reduce rates. In fact, CenturyLink has stated it has no plans to reduce intrastate switched access rates upon merger close.[37] Despite the fact that CenturyLink's regulated entities will benefit post-merger in the form of lower costs to the extent synergies savings are achieved, wholesale customers will not benefit from any of the savings realized absent conditions imposed by the Commission on its approval of the merger.

Q. Did CenturyLink make a commitment to share access savings when it merged with Embarq?

A. Yes. In the FCC's approval of the CenturyTel and Embarq merger, the FCC summarized that the applicants there claimed that the merger would be in the public interest because of its commitment to reduce its interstate access rates from $0.0095 per minute to the CALLS Order rate of $0.0065 per minute as a result of electing price cap status.[38] The FCC stated: "We also find that the merger should result in

[36] CenturyLink's second quarter 2010 revenue increases were primarily driven by growth in high-speed Internet customers and data transport demand from wireless providers. *See* http://ir.centurylink.com/phoenix.zhtml?c=112635&p=irol-newsArticle_Print&ID=1456278&highlight.
[37] CenturyLink response to Sprint DR 40.
[38] CenturyTel/Embarq Order, ¶ 43.

lower access rates because of the change in regulatory status for CenturyTel, which should benefit long-distance callers."[39] The Merged Firm has made no such commitment here to reduce its intrastate access rates, thereby eliminating a potential key public interest benefit from the merger of CenturyLink and Qwest.

Q. **Is there any other financial information that the Commission should consider in determining if the Merged Firm should be required to share merger synergies with its wholesale customers?**

A. Yes. CenturyLink is currently a profitable company, and explains in its testimony that it plans to be even more profitable after merging with Qwest. CenturyLink has indicated the dividend payout per share of the Merged Firm will remain at the same high level.[40] To illustrate the profitability of CenturyLink, the current distribution of profits to its shareholders via dividends is $10.79 for each access line per month.[41] Customers – including carrier customers – should also receive benefits from the synergy savings, rather than all of that being used to enrich the equity holders of the Merged Firm. I discuss below the benefits that the Commission should require the Merged Firm to share with its carrier customers as a condition for approval of the merger of CenturyLink and Qwest in Washington.

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[39] Id., ¶ 45.
[40] CenturyLink's pre-merger dividend is $2.90 per share and that policy will continue post-merger. *See* http://news.qwest.com/centurylinkqwestmerger (last viewed August 5, 2010).
[41] CenturyLink second quarter 2010 dividends paid June 21, 2010 were $219 million. *See* http://ir.centurylink.com/phoenix.zhtml?c=112635&p=irol-newsArticle_Print&ID=1456278&highlight. $219 million divided by 6,767,000 access lines = $32.36 per quarter, divided by 3 = $10.79 per line per month.

Q. Does CenturyLink witness Bailey attempt to justify the high dividend payout of CenturyLink by comparing his company's payout to other telecom companies?[42]

A. Yes. Mr. Bailey compares CenturyLink to four other large ILEC holding companies that also collect large amounts of revenues from other carriers in the form of bloated access charges. A comparison to the companies within the S&P 500 would be more meaningful.

Q. How does CenturyLink's dividend yield[43] compare to the average dividend yield within the S&P 500?[44]

A. First, it is important to note that only 372 of the S&P 500, 74.4%, pay dividends at all. Of the companies that do currently pay dividends, the average yield is just 2.46%. CenturyLink's yield is 7.95% or more than three times the S&P 500 average of the companies currently paying. The companies CenturyLink chose to compare itself to four other large ILEC holding companies. Each of these companies is in the top ten in dividend yield just like CenturyLink. Clearly, CenturyLink's dividend payout is not justified by a limited to comparison to 4 other telecom companies.

Q. Companies sometimes pay high dividend yields to reward equity shareholders when stock price appreciation is slow. Is this possibly the reason for the CenturyLink high dividend yield?

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[42] Bailey Direct, p. 24, ll. 1-8.
[43] Dividend Yield = Dividends paid per share divided by Share Price.
[44] Dividend Yield for Stocks in the S&P 500 updated Thursday, September 9, 2010; http://www.indexarb.com/dividendYieldSortedsp.html; See Exhibit JAA-4.

A. No. To analyze this possibility, I compared the stock appreciation for CenturyLink to the average stock appreciation for the S&P 500 companies over various timeframes.

Q. What did you find when you researched the stock appreciation of CenturyLink shareholders have experienced as compared to the S&P 500?

A. The CenturyLink stock has appreciated significantly more than the S&P 500 over the last 3 months, over the last 6 month period, over the last year, over the last 2 years and over the last 5 years. For example CenturyLink shares appreciated approximately 18% over the last year whiles the S&P average return was approximately 6%.[45]

Q. Does Qwest also pay a large dividend to its shareholders while the Qwest stock price also appreciates more than the average S&P 500 companies?

A. Yes. Qwest's dividend yield of 5.5% is <u>more than double</u> the average yield of S&P companies paying dividends of just 2.46%.[46] At the same time, Qwest share prices, just like CenturyLink's share prices, increased significantly more than the S&P 500 over the last 3 months, over the last 6 month period, over the last year, over the last 2 years and over the last 5 years. For example Qwest shares appreciated approximately 70% over the last year whiles the S&P average return was approximately 6%.[47]

Q. Is there another way equity shareholders are rewarded?

A. Yes. Stock buy-back programs reduce the number of outstanding shares which in turn increases the value of the remaining outstanding shares.

Q. Has CenturyLink had such programs recently?

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[45] See Exhibit JAA- 5.
[46] See Exhibit JAA-4.
[47] See Exhibit JAA-5.

A. Yes. CenturyLink has announced and completed $1.75 billion in stock repurchases since mid-2007.

Q. Given the magnitude of CenturyLink's stock appreciation of approximately 18% over the last year, can CenturyLink's high dividend yield be justified by low stock appreciation?

A. No. Although the theory that high dividends are used in some cases by companies to reward their equity shareholders when stock appreciation is slow, the data shows CenturyLink's equity shareholders are not only getting the high dividend but also stock appreciation significantly higher than the S&P 500.

Q. Why have you provided this analysis?

A. I have provided this analysis to demonstrate CenturyLink's financial strength and to show the merger conditions Sprint recommends will not adversely impact the Merged Firm's already strong financial position. If the conditions Sprint suggests are not imposed, competitive carriers will be competitively disadvantaged by CenturyLink's high access rates and the Merged Firm's already strong financial position will get stronger.

Q. Does Sprint believe CenturyLink's dividends should be reduced?

A. No. Sprint's concerns are not the level of dividends paid to Merger Firm shareholders but instead the high access charges that are competitively disadvantaging Sprint in the market and the substantial transaction costs incurred to interconnect with the various Merged Firm ILECs. Not only are the access rates anti-competitive, the excess revenues collected from above cost rates can be used for the Merged Firm's deployment of competitive products such as its IPTV offering.[48] Instead of paying high access rates to the Merged Firm so it can create new non-regulated services, Sprint would like to pay more reasonable rates for access services and invest the rate differential in its own business in direct competition to the Merged Firm. The lower access rates will facilitate competition which directly benefits consumers. Similarly, Sprint would rather use its scarce resources to develop new products and services consumers desire instead of negotiating and arbitrating interconnection agreements.

VI. MERGER APPROVAL SHOULD BE CONDITIONED UPON THE MERGED FIRM REDUCING INTRASTATE SWITCHED ACCESS RATES

Q. Why must CenturyLink's intrastate switched access rate be reduced as a result of this merger?

A. As I discussed above in Section III of my testimony, the vertical integration of CenturyTel LD, Embarq LD, and Qwest LD with the CenturyLink and Qwest ILECs results in a competitive advantage for these long distance service providers who no longer have to pay the inflated switched access rates the ILECs continue to charge all unaffiliated long distance service providers. To avoid negative impacts to the competitive market in Washington, the access rates of each of the pre-merger ILECs must be reduced.

Q. Has Qwest argued in the context of a merger proceeding that intrastate switched access rates should be reduced?

[48] Jones Direct, p. 8, ll. 5-7.

A. Yes. In the Iowa Telecom/Windstream merger proceeding before the Iowa Utilities Board, Qwest accurately explained how the expanded scope of an ILEC's business post-merger provides economies of scale that no longer justify inflated switched access rates:[49]

> Q. IS THERE ANY JUSTIFICATION FOR IOWA TELECOM HAVING ACCESS RATES NEARLY THREE TIMES HIGHER THAN THE RATE CHARGED BY QC?
>
> A. No. While, in the past, Iowa Telecom may have attempted to justify high switched access rates based on cost differences, with the proposed merger, arguments that the combined company does not have the size and scope of a company like Qwest no longer apply. As Sprint noted in its February 1, 2010 Statement In Lieu of Testimony, if the reorganization is approved the resulting combined company will have 3.3 million access line, roughly 13 times Iowa Telecom's present number of access lines. In light of the size of the new company, higher access costs cannot be justified by arguments that Iowa Telecom lacks the economies of scale available to large companies like Qwest.
>
> Q. CAN THIS SIGNIFICANT DISPARITY BETWEEN SWITCHED ACCESS RATES CAUSE MARKET DISTORTIONS?
>
> A. Yes. Unreasonably high access rates can lead to a distortion in local exchange rates. Companies who charge very high switched access rates (a monopoly service) can use these revenues to subsidize the cost of the local loop and can undercut the local rate of their competitors, or generate additional margin on their services. Unreasonably high access rates can also lead to arbitrage schemes. As the term is used here, "arbitrage" in the communications industry means routing traffic in such a manner to take advantage of discrepancies in rates. Wide disparities in rates between companies can provide opportunities for arbitrage and leads to abuses such as "Traffic Pumping," wherein IXC traffic is deliberately routed to rural carriers with high access charges by third parties.

Q. Has Qwest attempted to stop discriminatory switched access deals?

A. Yes. Qwest has pointed out the competitive advantage a carrier obtains if it has a contract with another provider to get access services at a cost less than the tariff rate.

[49] Direct Testimony of Lisa Hensley Eckert at 9-10 in Iowa Utilities Board Docket No. SPU-2009-0010.

Qwest has advocated that all providers should be able to get the same rates for access services to avoid competitive harm. For example, Qwest provided the following testimony before the Arizona Commission:[50]

> Q. STAFF RECOMMENDS IN THE TESTIMONY OF WILFRED SHAND THAT AGREEMENTS BETWEEN ILECS AND IXCS FOR SWITCHED ACCESS SERVICES, THOUGH THEY ARE NON- 251 INTERCONNECTION AGREEMENTS, SHOULD BE FILED. DOES QWEST AGREE?
>
> A. Qwest agrees that agreements between LECs and IXCs for services which are otherwise tariffed and involve intrastate switched access services should be made available to all IXCs on a non-discriminatory basis. Whether such agreements are filed with the Commission or otherwise made public is not a critical distinction. The important requirement is that such agreements must be promptly disclosed to the public and made available to all IXCs.

Q. Does the merger of Qwest and CenturyLink result in the same discriminatory advantage for its IXC affiliates over other providers that Qwest identified in its testimony to the Arizona Commission?

A. Yes. The Merged Firm's affiliates that pay access charges no longer need to worry about the tariffed access rates of the LECs in the Merged Firm. These affiliates have, in essence, just signed an agreement to get access services at cost-based rates instead of the bloated rates in the Merged Firm's tariffs. The Merged Firm's IXCs have received exclusive sweetheart access deals that Qwest has testified in other proceedings must be provided to <u>all</u> competitive carriers.

Q. What is Sprint's recommendation for the Merged Firm's intrastate switched access rates?

[50] Reply Testimony of Lisa Hensley Eckert at 11 in Arizona Corporation Commission Docket Nos. RT-00000H-97-0137 and T-00000D-00-0672.

A. The merger condition Sprint requests with respect to access rates is:

1) No later than 30 days after the closing date of the merger, all legacy CenturyLink ILECs in Washington (CenturyTel and Embarq ILECs) must reduce their intrastate switched access rates to mirror the intrastate access rates and rate structure of the Qwest ILEC in Washington; and

2) No later than 120 days after the closing date of the Merger, all CenturyLink ILECs in Washington (CenturyTel, Embarq and Qwest ILECs) must reduce their intrastate switched access rates to mirror the interstate switched access rates and rate structure of Qwest.

Q. Have you quantified the change in access revenues for the CenturyLink ILECs if this condition is adopted?

A. Yes. Sprint estimates the incremental reduction[51] in the Merged Firm's intrastate switched access revenues will be approximately **[Begin Confidential Data]** [redacted] **[End Confidential Data]** in the first step of the merger condition, and approximately **[Begin Confidential Data]** [redacted] **[End Confidential Data]** in the second step. The calculation is shown on Confidential Exhibit JAA-3 attached to my testimony.

Q. How does that amount compare to Washington's share of the estimated synergy savings of the Qwest merger?

A. The access revenue reduction of approximately **[Begin Confidential Data]** [redacted] **[End Confidential Data]** is less than the estimated $57.5 million

[51] The incremental reduction assumes the Embarq rate changes scheduled to occur on 1-1-11 and 1-1-12 have already occurred.; also see CenturyLink response to Sprint DR 21

Washington-specific operating expense synergies of the Qwest and CenturyLink merger.

Q. Using the formula you have proposed for estimating Washington's share of the synergy savings projected for this merger, how much of the synergy savings from CenturyLink's merger with Embarq should have been shared with customers in Washington?

A. Approximately $9.7 million of that merger's $375 million in operating cost synergies, based on the relative access line share of CenturyLink's Washington operations.[52]

Q. How does Sprint's recommended access rate reduction compare to Washington's share of the estimated synergy savings from both the Qwest and Embarq mergers with CenturyLink?

A. The access reduction of **[Begin Confidential Data]** [redacted][53] **[End Confidential Data]** of the Washington synergy savings generated by CenturyLink's last two mergers.

Q. If the Commission requires access rate reductions as a condition of merger approval, will retail customers realize any benefit?

A. Yes. The benefits derived from intrastate switched access rate reductions will accrue directly to retail customers in the form of lower prices for retail services. Customers will also benefit if the Merged Firm's competitors have more resources for innovation, to invest in their networks, or to develop better service offerings for the

[52] Embarq Washington and CenturyTel of Washington working loops (reported in the USAC 3d Qtr. 2008 HC05) divided by total access lines reported in the CenturyTel and Embarq 3d Qtr. 2008 report to shareholders: ((156,780+73,659) = 230,439 / ((2,041,000 + 5853,000) = 8,894,000) = 2.59%.

[53] **[Begin Confidential Data]** [redacted] **[End Confidential Data].**

customers. Finally, customers will see the benefit from lower access rates because the Merged Firm's inflated access rates will no longer slant the playing field in its favor. The competitive balance in the market will be more even for all providers. Consumers always receive better products and services at lower prices when the market is more competitive.

VII. MERGER APPROVAL SHOULD BE CONDITIONED UPON THE MERGED FIRM REDUCING INTERCONNECTION TRANSACTION COSTS

Q. What specific interconnection transaction costs are you asking the Commission to limit?

A. I am referring to the administrative and operational costs carriers incur to negotiate/arbitrate and implement interconnection agreements under sections 251 and 252 of the 1996 Telecommunications Act.

Q. What is the benefit of reducing these transaction costs in conjunction with this merger?

A. By reducing these transaction costs, the merger benefits the entire telecommunications market, providing a broader benefit to the public as a whole. Specifically, competition is enhanced by limiting these costs to the benefit of end users in Washington.

Q. How many interconnection agreements would the Merged Firm have post-merger?

A. In Washington, CenturyLink has 35 interconnection agreements with CLECs and 27 with wireless companies.[54] Qwest reported 135 interconnection agreements with CLECs and 17 with wireless companies.[55] In total the Merged Firm will have 214 interconnection contracts with competitors in Washington alone. CenturyLink reports it has more than a thousand agreements with CLECs nationally, and that does not include wireless interconnection agreements that surely number in the hundreds. Clearly, the magnitude of interconnection agreements must generate significant costs for the industry as a whole, and accordingly higher prices for the customers of all these service providers.

Q. Do Petitioners suggest interconnected carriers should receive some benefits of the merger?

A. Yes. CenturyLink states the merger transaction "[w]ill provide benefits to the customers and other stakeholders of the combined company."[56]

Q. Is CenturyLink clear what those benefits might be, when the benefits would be realized, or any other details surrounding its statement?

A. No, it provides no details. I suspect the interconnected carriers would realize the same portion of the merger savings from this merger as they have received from the CenturyTel and Embarq merger, i.e., nothing, unless the Commission imposes conditions on the merger.

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[54] CenturyLink response to Sprint DR 22.
[55] Qwest response to Sprint DR 22.
[56] Reynolds Direct, p. 3 ll. 20-21

Q. Is the Merged Firm likely to make interconnection easier or harder in the face of competitive pressures?

A. The larger scale and concentrated resources of the Merged Firm naturally enable it to obstruct competition more. And along with this increased power comes the increased inclination to exercise that power when faced with a competitor that is likely to have success in challenging the Merged Firm's retail or wholesale services.

Q. Have other commissions imposed interconnection contract conditions in the context of ILEC mergers?

A. Yes. The FCC set conditions in the AT&T and Bellsouth transfer of Control proceeding related to interconnection contracts.[57]

Q. What actions can the Commission take to limit local interconnection contract transaction costs and enable the continuing development of competition?

A. Transaction costs between the Merged Firm and all other interconnecting carriers could be greatly reduced if the Commission would impose merger conditions that 1) require the Merged Firm to extend the life of existing contracts; 2) allow requesting parties to port interconnection agreements to other Merged Firm affiliates and across state lines; and/or 3) require the adoption of standard agreements across the entire footprint of the merged ILECs. I discuss each of these conditions below.

1. <u>Extending Existing Contracts</u>

[57] In the Matter of AT&T Inc. and BellSouth Corporation Application of Transfer of Control, WC Docket 06-74 (released March 26, 2007), Appendix F .

Q. Why is it beneficial to the industry to extend the life of existing local interconnection contracts?

A. Competing carriers can avoid the burdensome cost of contract negotiations and potential arbitration if existing contracts are extended. As long as the current interconnection terms are satisfactory to the requesting carrier, the ability to extend its existing interconnection agreement for a substantial period of time provides the carrier with a real benefit from the merger. Instead of extended and costly negotiations with the CenturyLink and Qwest ILECs over interconnection terms and conditions, carriers can focus resources on providing the best service offerings for retail consumers.

Q. Would CenturyLink's interests be compromised if contracts are extended?

A. Typically, ILECs contend the rapid changes in the market mean changes are often needed to interconnection agreements. The history suggests otherwise. Sprint entities have eight interconnection agreements with the entities of the Merged Firm in Washington. All of the agreements expired long ago but the companies continue to operate under those agreements. No issues have arisen in those contracts during the years after each of the contract terms expired that warranted either party to notice the other. It is unlikely significant issues will arise in the future. There is no reason those agreements could not be officially extended as specified in this testimony below.

Q. If the interconnection contracts are extended, does CenturyLink have no recourse if an issue arises?

A. No. CenturyLink can always propose an amendment to the existing agreement. If the competing carrier agrees with the amendment, the change is incorporated into the agreement. Even if the carriers disagree about the need for the amendment, that one issue can be addressed through the dispute resolution or change of law provisions of the contract. Resolution of one issue in this manner is much less time consuming and drives much less expense than arbitration of an entirely new interconnection agreement.

Q. What is Sprint's specific recommendation for the extension of existing contracts?

A. Sprint recommends an existing interconnection agreement, whether in its initial term or otherwise currently effective, may be extended by a requesting carrier for 48 months from the date the merger closes or for three years after an extension request is granted, whichever is longer.

2. <u>Porting Existing Contracts</u>

Q. Why is it beneficial to the industry to port interconnection agreements to other affiliated ILECs of the Merged Firm?

A. Like contract extensions, the ability to port a contract from one ILEC to another in the Merged Firm avoids the burdensome incremental cost of contract negotiations and potential arbitration to establish a new contract. With more than 100 ILECs in the Merged Firm[58] and its stated plan to retain each legal entity, management of the

[58] Nationally, the Merged Firm will have approximately 75 legacy CenturyTel ILEC legal entities, approximately 25 legacy Embarq ILEC legal entities, and 13 legacy Qwest ILEC legal entities, according to CenturyLink and Qwest price cap filings at the FCC.

interconnection arrangements can be unnecessarily burdensome. A carrier wishing to interconnect with the Merged Firm in multiple locations would need to negotiate with the Merged Firm on a myriad of issues over and over again. It makes much more sense for the industry as a whole to permit the porting of existing agreements from one ILEC to another within the Merged Firm, even if the agreement originated in another state. The porting of existing agreements may also result in one nationwide interconnection agreement.

Q. Have Petitioners stated their opposition to porting an existing Qwest agreement into CenturyLink service territories within the same state or across states?

A. Yes. Both CenturyLink and Qwest explain it will not permit porting agreements in this manner and a carrier must instead "submit a request for negotiations pursuant to Section 252."[59]

Q. Did Petitioners disclose any technical reasons that would preclude agreement porting?

A. No, they did not.[60]

Q. Would the Commission be the first commission to require porting of interconnection contracts as a merger condition?

A. No. The Commission would not be the first commission to impose such a condition with a merger of two large ILECs. The FCC required porting of agreements between

[59] CenturyLink and Qwest responses to Sprint DR 33.
[60] CenturyLink and Qwest responses to Sprint DRs 32, 33, and 34.

states and legal entities for the 22 AT&T Corporation ILECs.[61] In this merger, we have over 100 ILEC legal entities.[62] At the state commission level, the Illinois Commerce Commission required porting of interconnection agreements in its approval of the both the SBC-Ameritech merger[63] and the Bell Atlantic-GTE merger.[64] The ability to port agreements between the Merged Firm ILECs will be even more important in this merger than it was in the AT&T-BellSouth merger due to the magnitude of the Merged Firm ILEC legal entities.

Q. What is Sprint's specific recommendation for porting existing agreements between ILECs of the Merged Firm?

A. The Merged Firm shall permit a carrier customer to port the entirety of an existing interconnection agreement (except for state-specific rates) entered into with any CenturyLink or Qwest ILEC in Washington, whether negotiated or arbitrated, to any other CenturyLink or Qwest ILEC within Washington. It shall also permit a carrier customer to port the entirety of an existing interconnection agreement from another state in the Merged Firm's territory where it is currently effective (except for state-specific rates), whether negotiated or arbitrated, to Washington. The Merged Firm shall apply the ported agreement (whether an in-state agreement or an agreement from another state) to all carrier customer affiliates, aggregating all carrier customer affiliate arrangements under the one ported agreement. For purposes of this condition, state-specific rates do not include billing arrangements such as bill-and-

[61] In the Matter of AT&T Inc. and BellSouth Corporation Application of Transfer of Control, WC Docket 06-74 released March 26, 2007, Appendix F
[62] See footnote 55 to this testimony
[63] ICC Docket No. 98-0555.
[64] ICC Docket No. 98-0866.

keep for the exchange of traffic, or contractual provisions to share the costs of interconnection facilities. This condition shall continue for 48 months after the closing date of the merger, and shall apply to any existing agreement, whether in its initial term or otherwise currently effective, and to any new agreements created during the 48 month period following the closing date of the merger. Any agreement ported more than 12 months after the merger shall be effective for 36 months after the porting request is granted. If an agreement is ported from a Merged Firm entity within a state or across state lines, any interconnection agreement that would otherwise apply is cancelled without penalty.

3. <u>One National Standard Interconnection Agreement</u>

Q. Why would it be beneficial to require the adoption of one standard agreement across the entire footprint of the Merged Firm?

A. As previously noted, the Merged Firm plans to continue to operate each of the existing ILEC legal entities post-merger, which would require carriers wishing to interconnect with more than one ILEC service territory to negotiate and potentially arbitrate a local interconnection agreement with each and every ILEC in the Merged Firm. Clearly this inflates the costs of entering the market, or of remaining in the market if entry has already occurred. Competitive offerings in the new market could be delayed or, at a minimum, the interconnecting company will incur more administrative/operational costs that must be recovered in some manner, such as through higher retail service rates. This condition is really just a matter of adopting a "best practice," which in this case is already used by Qwest. Qwest's SGAT, which is largely consistent except for local pricing, is an example of the movement toward a unified template across all of a company's service territories. The Merged Firm should be expected to do the same.

Q. What is Sprint's specific recommendation for one national standard interconnection agreement?

A. The Merged Firm shall recognize that porting existing agreements across state lines and applying them to affiliated carrier customers may result in a nationwide interconnection agreement. Any negotiations necessary to facilitate such porting to accommodate application of such agreements in multiple states or among requesting carrier customers shall occur in a timely fashion, and the results shall apply retroactively to the date that such porting was requested by a carrier customer. Negotiations concerning new or amended interconnection agreements shall be accomplished on a nationwide basis and include all ILECs of the Merged Firm in one contract.

VIII. THE MERGER SHOULD BE CONDITIONED UPON THE MERGED FIRM COMPLYING WITH BEST BUSINESS PRACTICES

Q. Sprint is aware of several business practices that are handled very differently by Qwest and CenturyLink pre-merger. What is the first practice that concerns Sprint?

A. Currently legacy CenturyLink has a limit of 10 circuit migrations a day for carrier customers, while Qwest has set its limit at 50. Sprint has found CenturyLink's limit to be restrictive, harming Sprint's ability to compete and offer services in an efficient manner. The Merged Firm should be required to adopt the best practices available to it rather than be allowed to harm competition by maintaining inferior practices. The

Merged Firm should be required to allow at least 50 circuit migrations a day to facilitate competition. When CenturyLink is currently paying investors nearly $11 in dividends per access line, there is no excuse for only having the capability of 10 migrations per day. The Merged Firm should be expected to invest some of its synergy savings in better meeting its obligations to facilitate fair competition.

Q. What is another practice that causes Sprint concern?

A. CenturyLink recently filed a request with the FCC to delay its implementation of the one-day local number portability standard.[65] Ironically, the reason CenturyLink gave was that it has not finished integrating the two OSS from its last merger, with Embarq. CenturyLink wants to finish adopting the Embarq porting system across its entire footprint rather than update two separate systems to one-day porting, and claims that it cannot satisfy both the timeline for merger conditions put in place by the FCC and the one-day porting requirement deadline. On the other hand, Qwest already provides one-day porting in Washington.[66] Failure to implement one-day porting delays customers who wish to switch carriers, causing some customers not to switch at all. The Merged Firm cannot be permitted to choose practices that inhibit competitive choice. As a condition of approval of the merger in Washington, the Commission should require that the Merged Firm not degrade existing Qwest capabilities in Washington, specifically ordering CenturyLink to implement one-day porting without any further delay, and in any event no later than February 2, 2011.

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[65] *See* Local Number Portability Porting Interval and Validation Requirements; Telephone Number Portability, WC Docket No. 07-244, *Century Link Petition for Waiver of Deadline* (filed June 7, 2010).
[66] Qwest Response to Sprint DR 39.

Q. Please illustrate the potential negative impact to customers in Washington if the Merged Firm were allowed to delay implementation of one-day porting in Qwest territory.

A. In all of 2009 CenturyLink processed only **[Begin Confidential]** [redacted] **[End Confidential Data]** LNP ports.[67] Since Qwest's operations in Washington are 7.5 times larger than the CenturyLink operations,[68] Qwest likely ported at least **[Begin Confidential Data]** [redacted] **[End Confidential Data]**[69] local numbers in 2009. If there were no one-day porting requirement in legacy Qwest territory in Washington, the number of customers negatively impacted would be much higher than the number of customers in legacy CenturyLink territory alone. The best practices of the two companies, in this case Qwest's current practice of one-day porting, must be adopted throughout the Merged Firm's service area for competition not to be harmed.

IX. THE COMMISSION SHOULD SPECIFY HOW MERGER CONDITIONS ARE ENFORCED

Q. How should merger commitments be enforced?

A. Based on its experience in attempting to implement intended competition-enhancing conditions imposed on other ILEC mergers, Sprint is concerned that the Merged Firm, whether intentionally or unintentionally, may not interpret a merger condition in the same manner that the beneficiaries of the merger condition do. Sprint also has encountered objections from ILECs as to what the appropriate forum is for bringing a

[67] CenturyLink response to Integra DR 2(i).
[68] Washington Lines from Reynolds Direct at p. 11 ll.6-9; Qwest lines divided by CenturyLink lines 1,500,000/200,000 = 7.5 times.
[69] Qwest did not provide a response to Integra 2(i) that Sprint could find. Qwest LNP ports estimate is based on CenturyLink LNP ports times 7.5, rounded. This number is conservative because Qwest has been losing access lines at a fasted rate than CenturyLink.

regulatory or legal action to enforce merger conditions. To erase doubt about merger condition enforcement, and to encourage the Merged Firm to implement in good faith all of the merger conditions approved by the Commission, Sprint proposes that the Commission specify how merger conditions are to be enforced.

Q. What is Sprint's specific recommendation for how merger conditions should be enforced?

A. The Washington Utilities and Transportation Commission, the courts, and to the extent appropriate, the FCC if it adopts a similar condition, shall each have jurisdiction to enforce these Merger Conditions and carrier customers shall be granted standing to complain to the foregoing bodies if the Merger Conditions are violated. The Merged Firm will be responsible for paying attorneys fees of complaining parties in any case where complaining parties seek to enforce Merger conditions and are successful in such enforcement. In addition, in any instance where a complaining party seeks to enforce a Merger condition through complaints to the Washington Utilities and Transportation Commission, the courts, or to the FCC to the extent appropriate if it adopts a similar condition, and is successful in such enforcement, the complaining party may also require, at its option, that the term of any Merger commitment so enforced be extended for an additional 48 months in addition to the initial term.

Q. Does this conclude your testimony?

A. Yes.