Exhibit No. ___ (RB-6)
Docket UT-100820
Witness: Rebecca Beaton

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the 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 UT-100820**

EXHIBIT TO TESTIMONY OF

REBECCA BEATON

STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

"Evaluating the Proposed Merger of CenturyLink and Qwest Communications"
Sherry Lichtenberg, Ph.D., July 9, 2010

September 27, 2010

National Regulatory
Research Institute

Evaluating the Proposed Merger of CenturyLink and Qwest Communications

Sherry Lichtenberg, Ph.D.

July 9, 2010

Introduction

Telecommunications mergers require analysis and supervision both before and after approval to ensure that they proceed smoothly and do not harm the very consumers they are meant to benefit. While Company applications uniformly proclaim that bigger is better, promise new products and services, and state that the integration of ordering, billing, installation, and maintenance systems will be easily accomplished, the legacy of recent mergers has been delayed customer orders, a decline in service quality (including installation and repair times), and even, as in the case of the Carlyle Group's acquisition of Verizon Hawaii and FairPoint's acquisition of Verizon's New England properties, bankruptcy. In these cases, (and even in the better managed transition of BellSouth's systems to those of its new owner AT&T) the rush to achieve the promised financial "synergies" from the integration of disparate IT systems and processes for ordering, installing, billing, and trouble handling have had unanticipated negative consequences.

Commissions can minimize these problems by clearly understanding and evaluating the details of the merger plan, both in the short and the long term, crafting conditions that will ensure that systems changes and other "synergies" are well thought out and tested, and monitoring progress on an on-going basis, including assessing penalties for non-performance.

This brief paper provides a framework for that evaluation in the specific case of the merger of CenturyLink and Qwest.

Overview of the Transaction

CenturyLink and Qwest have filed applications for approval of their proposed merger in the 14-state Qwest region and with the FCC, citing the "national breadth and local depth [of the combined company that will allow it] to provide a compelling array of products and services to its customers."[1] The transaction is a stock-for-stock swap that, according to the petitioners, will not require new financing, will not add new debt, and will "generate some $625M in annual run-rate operating and capital synergies."[2] The companies will merge at the holding company level, so changes to Qwest's operating certificates are not required. Finally, the petitioners state that the new company will continue to operate as Qwest did in the past and "any subsequent service or price changes will be made, just as they are now, in accordance with all applicable rules and laws."[3]

[1] Joint Notice and Application for Expedited Approval of Proposed Merger, Arizona Docket T-01051B-10-0194, et al, filed 5/13/10

[2] Ibid, pg. 2

[3] Ibid pg 5

Qwest is the Incumbent Local Exchange Carrier (ILEC) in Arizona, Colorado, Idaho, Iowa, Minnesota, Montana, Nebraska, New Mexico, North Dakota, Oregon, South Dakota, Utah, Washington, and Wyoming, with approximately 10M access lines in its 14-state region.[4] It was formed by the merger of US West with Qwest in 2000.[5] Qwest provides bundled local and long distance service, data services, wholesale services, and resold wireless and TV services throughout its 14-state region, and is the carrier of last resort in its region. Qwest also provides national local, long distance, and business services to a variety of mid-sized and large businesses throughout the country. It is the expansion of this "national footprint" on which the petitioners appear to be focusing.[6]

CenturyLink is based in Monroe, Louisiana and was formed through mergers with a number of rural and large companies in the 33 states it serves, most notably Embarq Corporation (formerly Sprint). The Embarq merger was completed in July 2009, although integration activities, including combining many of its operational support systems is still on-going. CenturyLink has approximately 7M access lines nationwide.[7]

CenturyLink resells long distance service to customers through its Embarq subsidiary. We assume that these lines will be converted to Qwest/CenturyLink once the transaction is completed.

<u>Commissions Should Focus Their Review on 5 Key Issues</u>

While each state has a different legal framework for evaluating utility mergers, all have a duty to ensure that customers are not disadvantaged by reduced quality of service or increased costs associated with these mergers. Based on its experience with telecommunications mergers in Hawaii (Hawaii Telcom), New England (FairPoint Communications), BellSouth, and energy company mergers across the county, the National Regulatory Research Institute (NRRI) recommends that state commissions review the CenturyLink application in detail before making a determination on the merits of the merger. The Commissions' reviews should focus on 5 specific areas: (1) Financial review, (2) quality of service/customer support, (3) systems integration, (4) competition, and (5) broadband deployment/support.

---

[4] Ibid pg 7

[5] The merger petitions stated that approval of the transaction would "create a next generation telecommunications company dedicated to bringing advanced voice, data, and broadband Internet services to customers in [its 14 states], across the United States , and around the world." The applicants opined that "the strategic merger of Qwest and US West will serve the public interest by producing significant pro-competitive effects that will lead to substantial benefits for customers." Arizona Application

[6] "The combination will position post-merger CenturyLink to offer more vigorous competition to larger players in multichannel video and bundled services. . ." and '. . . will allow it to expand Qwest's enterprise and government business to compete more effectively against . . . AT&T and Verizon." FCC Application for Consent to Transfer Control, p.2

[7] Joint Notice and Application, AZ Docket T-01051B-10-0194, pg 5

The following paragraphs review these issues.

1. Financial Review. CenturyLink's application states that there will be no additional costs associated with the merger and promises synergies that will provide $625M in yearly operational and run-rate savings over the next 3-5 years. The application also projects significant growth in large business sales revenues, as well as potential new revenues from next generation TV services and other new products. Commissions should examine the proposed savings carefully to determine their impact on the Company's operations and personnel. In addition they should review the revenue growth projections in detail, including running sensitivity analyses, to judge for themselves the likelihood of success and to ensure that a failure to meet projections does not jeopardize the combined company's overall financials. The review should pay particular attention to revenues for the regulated company, including examining the assumptions driving line loss estimates, new product sales projections, and the costs associated with the development/integration of ordering, installation, billing, and repair systems.

   Operational support systems (OSS) changes and integration efforts in other telecommunications mergers have resulted in unanticipated costs. For example, the failure of the new OSS in both Hawaii and the New England states depleted the companies' reserves and forced both entities into bankruptcy. And the "simple" integration of the former BellSouth ordering and billing systems into AT&T's OSS platform delayed customer installations, forced wholesale customers to develop costly new interfaces, and resulted in the company's failure to meet service quality standards, installation timeliness.

2. Quality of Service/Customer Support. Retail and wholesale service quality are key drivers of success, since unhappy customers may "vote with their feet" and move their business to competitors. Commissions should develop a process for continuous monitoring of the results of the transaction after close to ensure that the quality of service provided to both retail and wholesale customers does not decline. There should be clear consequences for shortcomings Customer service metrics (particularly installation times, repair times, and order and billing accuracy) may be impacted by systems and staffing changes. Commissions should review the applicants' plans to determine if customer service centers will be relocated or combined, if new or modified support systems will be deployed, and how other changed circumstances may impact the service provided to retail customers. In order to ensure that competition continues at its current level in the Qwest states, Commissions should also review any changes planned to Qwest's current wholesale support centers to

ensure that staffing levels and familiarity with the products purchased by wholesale customers is not diminished by transitioning work to create "synergy savings."[8]

3. Systems conversion/integration. The CenturyLink/Qwest merger will include a number of significant systems integration/conversions projects that will impact financial and human resource systems, retail customer service systems, and retail billing systems, as well as wholesale ordering, installation, trouble handling and billing systems. For example, CenturyLink's Arizona application stresses the Company's "ability to successfully integrate acquisitions and its foresight in anticipating growth as it makes operational or systems decisions," [9] but it does not define the conversion efforts it will undertake or provide the detail necessary to evaluate the risk associated with them. Both the Hawaii Telcom and the FairPoint acquisitions failed at least in part due to problems associated with the development and cutover to new systems. The Commission should require a detailed listing of and timeline for these projects so that it may assess risk and develop the monitoring plans necessary to ensure that these changes do not negatively impact either retail or wholesale customers.

4. Impact on competitive providers. Qwest has a robust wholesale business, using systems and processes that were developed, tested, and refined as part of obtaining approval to offer long distance services as required under Section 271 of the Telecommunications Act of 1996. CenturyLink has a smaller wholesale presence, in part due to its history as a rural provider, which was not under an obligation to provide unbundled network elements to its competitors. Commissions should review the merged company's plans for continuing to provide systems access, performance metrics, and a change management process that will allow it to fulfill its wholesale requirements and ensure that wholesale revenues continue. This review should include an analysis of any operational changes required to achieve the "synergies" forecast in the merger financials.

   The failure to maintain the existing wholesale systems or seamlessly transition to new systems could drive even the largest competitors from the market. For example, the failure of the Hawaii and FairPoint operational support systems and the merged BellSouth/AT&T systems (albeit for a shorter time) resulted in thousands of orders that did not complete (including orders to transfer customers to cable companies), dissatisfied customers, and incorrect bills. Each of these problems significantly impacted the ability of competitors to retain and support their customers and resulted in financial loss.

---

[8] Qwest currently provides unbundled network elements to CLECs under Interconnection Agreements and a commercial UNE-P replacement product under contract, as well as real-time operational support systems for ordering, installation, billing, and trouble handling.

[9] Direct testimony of Todd Schafer, Arizona, pg 7

5. Broadband deployment/support. The merger applications stress the strength of a combined CenturyLink/Qwest in increasing fiber penetration throughout its network and providing "next generation services" (including high speed internet and enhanced video services, commonly referred to as "next generation TV") to its customers. With the increasing requirement for broadband connectivity for all consumers, Commissions should focus on this aspect of the merger plan to ensure that all customers are able to take advantage of these services. The Commissions should request a detailed plan for broadband implementation, including time tables, and should establish a process for assessing progress and establishing consequences for failure.

Summary

The Qwest region public utility commissions are obligated to ensure that customers of the combined company continue to receive quality telecommunications services at reasonable rates. By reviewing this merger in depth, the commissions will be able to avoid many of the problems that have plagued similar mergers in Hawaii, New England, and Bell South.

NRRI understands these issues in detail and looks forward to working with the states to assist in its review of this application.