

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

NON-CONFIDENTIAL

REPLY BRIEF OF PUBLIC COUNSEL

WASHINGTON STATE ATTORNEY GENERAL'S OFFICE

NOVEMBER 7, 2003

I. INTRODUCTION

1. Qwest has placed the Washington Utilities and Transportation Commission in a very difficult position by filing and prosecuting this petition, as to the substance, as to timing, and as to policy. The petition asks the Commission to depart from its careful approach to competitive classification of business services in cases since 1999, and, on an “all or nothing” basis, authorize statewide geographic retail rate deaveraging by the company. Ironically, the company asks the Commission to grant it this power on the strength of statewide averaged and aggregated data which disregards the “deaveraged” realities of different regions of the state.
2. Qwest, with Staff’s support, seems determined to force this petition through at a time when the Washington telecommunications market faces real uncertainty. Neither Qwest nor Staff has explained why there is such urgency to move so far and so fast, with so much risk to business customers and to the emergence of a healthy competitive telecommunications market in Washington.
3. Qwest calls the questions raised by Public Counsel and others a “shotgun” approach. What has really occurred in this case is that parties have identified an extraordinarily large number of serious shortcomings with the petition, implicating nearly every element of the statute and raising serious public interest questions as well. The list is indeed a long one, and Qwest would no doubt prefer it were shorter. Qwest has created its own difficulties, however. If Qwest had not selected the artificial analog product market, if it had followed the path of its earlier business competitive classification cases and focused the case on its more competitive exchanges, if it had acknowledged the distinction between the small and large business market segments, and if it had filed the petition after the competitive market analysis under the Triennial Review Order was completed, this case would have been far more straightforward. Having chosen this course at this time, Qwest should not be surprised that serious questions arise.

II. APPLICABLE LAW

4. In its discussion of applicable law, Staff provides the Commission with an inaccurate paraphrase of RCW 80.36.330 (1) , stating:

In fact, market share is listed as merely one of the “other indicators” of effective competition that the Commission may consider under the statute.

Staff Opening Brief, ¶14. The statute, of course, refers expressly to “other indicators of market power.” This is not an insignificant point. The words omitted from Staff’s paraphrase, and their place in the statute, make clear that the focus of the statute is on market power generally. Public Counsel does agree with Staff that market share is important because the “proof is in the pudding.” Staff Opening Brief, ¶16. Unfortunately, Staff does not appear to have lived by this maxim in its analysis of this case, but instead seeks to explain away the importance of Qwest’s remaining market share, which continues to be very high in many areas of the state.

III. QWEST HAS NOT PROPERLY DEFINED THE RELEVANT MARKET

A. The Product Market

5. Perhaps the most striking aspect of the product market discussion in Qwest’s brief is its failure to point to any standard or test which the Commission can use to arrive at a relevant product market definition based on sound and accepted economic principles. Staff, however, does acknowledge the basic precept that if consumers consider one service to be a substitute for another they are in the same relevant market. Staff Opening Brief, ¶ 19. This is consistent with the demand oriented approach reflected in the Horizontal Merger Guidelines. Ex. 224, §1.0, pp. 4-5. Qwest witness Shooshan also concurred, on the stand, that “the market is defined by the demand side,” Tr. 529, and that substitution is part of the analysis. Tr. 531. The substitution and functional equivalence analysis which are at the core the demand approach cast serious doubt on the Qwest exclusion of digital services from the relevant product market.

1. Analog v. Digital Markets.

a. By themselves, different CPE requirements for analog vs. digital service are not an adequate basis for a product market.

6. Qwest appears to base its analog/digital market distinction primarily upon the type of customer premises equipment (CPE) used by the consumer. Qwest’s Opening Brief, ¶12. This is a weak reed upon which to build a case. This may be the classic case of a distinction without a difference. Except for this distinction, there appears to be no dispute on this record that the analog and digital business services at issue are functionally equivalent and could be substituted for each other by a customer. Qwest’s witness Mr. Shooshan testified digital services were “easily substituted” for those in the purported analog market. Tr. 531. Mr. Wilson observed at the hearing: “to the customer, oftentimes, whether it came to them over an analog or a digital medium, wireless, wire, you name it, they don’t care. They just want to talk to the other party... [question omitted] You know if the functional equivalency is there, that’s the main thing to them. They’re like me. They’re not interested in the technical stuff too much maybe.” Tr. 643. *See also* Reynolds Tr. 299-300

7. While conceding that digital services “can represent substitutes for Qwest’s analog services,” Staff’s Opening Brief, ¶ 22, Staff argues they are not as close substitutes as CLEC analog services because CPE would have to be replaced. *Id.* Staff and Qwest at the same time repeatedly ask the Commission to take notice of wireless and VOIP competition as substitute services, both of which require replacing analog equipment. This is an arbitrary distinction. Staff and Qwest cannot have it both ways.¹

8. Qwest also suggest that Public Counsel’s challenge that grouping basic business, PBX, Centres, and features into one “product” as too broad is somehow inconsistent with arguing the analog market is too narrow. These are two different issues. It is perfectly consistent to argue

¹ Public Counsel does not concede that wireless and VOIP are functionally equivalent substitute services for services in this petition. There are other significant distinctions between the services beyond the CPE employed. Public Counsel’s argument here is that if CPE is to be a basis for distinguishing between relevant product markets, it must be consistently applied, both as to intermodal competition, and as to the intramodal basic/PBX/Centrex market.

that basic business is not the same product as Centrex, and at the same time suggest that, within the basic business market market, defining the market to exclude functionally equivalent and substitutable digital services is improperly narrow. Public Counsel understands that the basic business/PBX/Centrex product market was accepted as the relevant market in UT-000883. Public Counsel would simply note that CPE based distinctions could be made between these services also. A customer who wishes to change from basic business to PBX service must invest in CPE equipment. It is patently arbitrary to overlook this distinction here, while treating it as significant in the analog/digital context.²

b. Qwest fails to show that CLECs only use wholesale services to provide analog services.

9. Another basis stated by Staff and Qwest for excluding digital services is the assertion that Qwest competitors are not generally using UNE-L and UNE-P to provision their digital services. Staff's Opening Brief ¶ 21. This is far from clear on the record of this case. In fact, both Staff and Qwest have reported the difficulty with which they had sorting reported lines using wholesale Qwest products between those providing analog and digital services. This difficulty has been one of the reasons for the changing calculations of CLEC line counts, which have shrunk from **[Begin Confidential]** ***** **[End Confidential]** during the pendency of the case (business line counts have been reduced from **[Begin Confidential]** ***** **[End Confidential]** Ex. 201T, p. 14, lines 12-16. Ex. 225. It is important to recall that the early numbers in response to Order No. 6 came from CLECs who were asked to simply report their resale, UNE-L and UNE-P used to provide these services without any analog/digital distinction. If wholesale services were by definition used only for analog services, there would have been nothing for CLECs to correct when they were later asked to distinguish.

² Compare, for example, Staff's Opening Brief at ¶ 34, where the need for different CPE and network connections to obtain VOIP is described to show how easy it is to substitute VOIP, with Staff's Opening Brief ¶ 22, where the fact that "a customer who wishes to switch from Qwest analog services to a comparable digital service would have to replace analog customer premises equipment" is presented as a rationale for why analog is not "as close a substitute" and therefore should not be included in the market definition.

c. The Commission’s order in Docket No. UT-000883 did not distinguish between analog and digital services.

10. Staff damns Qwest’s analog market definition with faint praise by saying that the analog market is “not inappropriate.” Staff makes the argument on brief that the analog/digital distinction is not new and that it was used in UT-000883. Notwithstanding Staff’s arguments, a review of the testimony and the order in that case reveal no reference to this distinction. Qwest’s understanding of the services it petitioned for in UT-000883 apparently differs from Staff’s. In Qwest’s Opening Brief, the company highlights the fact that the “*only difference* between the list of services in the instant case and the list of services in UT-000883 is that the list in the current list [sic] *explicitly states exclusions (including an exclusion of digital services)*[.]” Qwest’s Opening Brief; ¶13, note 6 (emphasis added). Since the list of services in UT-000883 did not contain an exclusion for digital services, by definition it included both analog and digital, according to Qwest’s own argument.

d. Relevant market analysis is not determined by impact on market share.

11. Staff makes the unexpected point that the “only way” the analog/digital distinction might be problematic would be “if it were clear that Qwest had a proportionally higher market share in the market for comparable digital services in comparison to its competitors.” Staff’s Opening Brief ¶ 23. This is a remarkably outcome-oriented rationale that improperly blurs the question of market definition with that of market share. As Mr. Shooshan observed, correct market definition is a distinct first step in analyzing market power. Tr. 528-529. Determining market definition based on whether the incumbent has bigger or smaller market share is facially invalid under any reasonable economic theory.

12. Public Counsel’s position is that the market should be defined correctly, and then let the chips fall where they may. Here, Staff suggests that we know from the record what the outcome would be if digital services were included. We know nothing of the kind. Neither Qwest nor Staff provided an empirical analysis of market shares in the combined analog/digital market in

direct or rebuttal testimony. While Mr. Reynolds was asked to make rough and ready calculations on the witness about relative line counts, cited in Staff's Opening Brief, ¶23, he also was careful to state that Qwest does not know and has not done any study of what market shares would be in the combined market. Tr. 225, 292-293, 323-326.

e. Creating a distinct “analog business market” is likely to be confusing and unworkable on a practical level.

13. There is a real question about whether this distinction is even practical to implement or comprehensible for the customer. Visualize two small business customers in neighboring premises in a strip mall in the city of Woodburg. Both use identical services and features from the list in this case. Both are provisioned identically (digitally) over the network. The only difference is their CPE. Ajax Plumbing has analog equipment so his signals are translated from analog to digital for transmission over digital facilities. Next door, Customer Bob's Boutique has digital equipment, and which uses the same digital transmission facilities. Both customers use the same services for the same purposes in the same volumes.
14. If this petition is granted and Qwest decides to deaverage by increasing rates in Woodburg, Ajax could see a rate increase, while Bob's continues to pay the previous regulated rate for what appears to both customers to be the same service. When he learns of the increase, Ajax may be upset to learn that his neighbor at the Boutique isn't paying more, and may find it difficult to comprehend that the reason is solely that the equipment sitting in Bob's office is electronically different than his. Ajax will also be interested to learn that the increase will not be subject to a rate case hearing by the Commission, whereas any increase for Bob's equivalent service will be. If Ajax's rate goes down, conversely, Bob's Boutique may be baffled to learn that it is not entitled to the decrease because his equipment is different and he is in entirely different market.
15. It is also unclear how Qwest would market differently to these similarly situated customers. Exhibit 26, which contains excerpts from Qwest's Large Business and Small

Business web pages, make no reference to analog or digital in the service descriptions. The prospects for customer confusion seem numerous.

16. Qwest's inappropriate product market definition here seems to pose a high likelihood that the classification will again be shelved by the company for practical reasons, as they did with the UT 000883 grant. Such an outcome is not in the public interest, placing Qwest's business customers in regulatory limbo until the company decides to "dust off" the classification at some indeterminate future point. The far better approach here is for the Commission to suggest that Qwest refile this petition after the mass market impairment issues are resolved, with more defensible product and geographic markets. Qwest has indicated that it intends to request classification of the same services on a digital basis in the near future. There appears to be every reason, based on this record, why a decision should be postponed until they do so, and the Commission can look at both aspects of the market. Qwest has offered no compelling reason why the Commission should be forced to go forward with this arbitrary and unworkable sub-classification of the business market at this time.³

2. "Mass market" small business is a clearly identifiable market segment.

17. Staff's Opening Brief, ¶¶ 28-29 states "there is no basis to conclude that small businesses that purchase three lines or fewer constitute a separate market for purposes of this case." Staff's brief makes no mention of the fact that the mass market business customer, defined as three business lines or less, is a standard FCC definition, or that the Triennial Review Order expressly identifies this market segment as having its own economic characteristics. Ex. 229. Nor does Staff acknowledge that the Commission, concurrently with this docket, is beginning to implement the Triennial Review Order, and will be evaluating the very mass market which Staff here dismisses to determine the competitive conditions in that market.⁴ Staff, in effect, asks the

³ Qwest is currently subject to a form of "rate freeze" under the terms of the US West/Qwest Merger Settlement. UT-991358, Ninth Supplemental Order, App. A., p. 9. The rate stability period ends on January 1, 2004.

⁴ UT-033044, Order No. 03, Order Requiring Disclosure of Information, CLEC Question No 14, asks for reporting of voice grade equivalent lines serving four market segments: (a) residential customers; (b) business

Commission to issue an order here finding that no such separate market segment exists, while simultaneously issuing orders in another docket which recognize the market segment.

B. The Geographic Market

18. Qwest catalogs the Commission's past competitive classification cases for a wide variety of services to support the assertion that statewide geographic market definitions are permissible and should, therefore, be used here. This argument is unpersuasive. Public Counsel does not argue that statewide markets can never be employed. For toll services, and other statewide services such as directory assistance, there is a reasonable rationale for a statewide geographic market. What matters is that the market analysis should be appropriate for the individual case at issue. It is significant that the two exceptions by Qwest are the two preceding dockets in which competitive classification for Qwest business services was considered.⁵ In both cases, Qwest framed the petition, and the Commission found it proper, to analyze the development of competition on an exchange by exchange basis. This makes sense. Different parts of the state have different market conditions, a fact amply demonstrated by exhibits such as Qwest Ex. 55C and Staff Exs. 209C and 232C. The exchange level analysis of the prior dockets is consistent with the market definition in the Horizontal Merger Guidelines, which states that the market should be no larger than necessary. Ex. 224, §1.0, pp 4-5.

19. Consistent with the approach taken in the last two dockets, Qwest could have framed its request to fit the differing levels of competition in Washington's very different communities. Even during the case, the company could have proposed alternatives to the Commission to focus on those exchanges, or groups of exchanges where competition is most pronounced.⁶ Staff also could have recommended alternatives, as it did in UT-000883.

customers with 1-3 lines at a location; (c) business customers with 4-24 lines at one location; and (d) business customers with 25 or more lines at one location.

⁵ UT-990022 (high capacity circuits for Seattle, Spokane, and Vancouver) and UT-000883.

⁶ Qwest acknowledges that its data can be reviewed at the wire center, exchange, zone, or other level less than statewide. Qwest's Opening Brief ¶ 21 but makes no alternate recommendation, apparently suggesting that the Commission or other parties must take on the burden of proof to properly construct a geographic market.

20. Instead, Qwest has rejected any suggestion that its statewide definition is overbroad and that a more granular approach be adopted. It has continued to insist upon an “all or nothing” market definition, presumably hoping that the higher levels of activity in the more urban exchanges will dominate the picture, while the less favored parts of the state are simply carried along with the tide. It is Qwest’s choice to take this approach. On the other hand, it is not the job of other parties, nor that of this Commission, to unravel the petition and reconstitute it in some more reasonable form.

21. It is entirely discretionary with the Commission whether to grant any petition, it is not required to grant competitive classification. As a legal matter, the only issue before the Commission is whether Qwest has carried its burden of proof that effective competition is present for the listed services, in a properly defined product and geographic market, and whether, even then, the classification is in the public interest.

22. The statute does not require the Commission to sort through a mass of data filed by a company and determine what the petition should have requested. If the choice presented to this Commission is “all or nothing,” Public Counsel submits that Qwest has fallen far short of showing effective competition in “all” of its service territory – accordingly, the only reasonable choice left to the Commission is to grant Qwest “nothing.”

IV. STATUTORY FACTORS

A. Number and Size of Alternative Providers

1. Table D: Qwest overstates the true CLEC presence in wholesale price zones.

23. Qwest's Opening Brief states that “37 CLECs provide services throughout the state” Qwest's Opening Brief ¶ 24. Qwest then calculates average CLECs per deaveraged zone. A review of the cited source, Ex. 208C, shows how these calculations exaggerate CLEC activity. First, it is apparent from the exhibit that the “37 CLECs” do not each provide service in every Qwest exchange throughout the state. Second, the number of CLECs with market share above minimal levels is much lower than the gross averages presented in the brief. Public Counsel has

prepared Confidential Table D (attached) to show the much smaller number of CLECs in each wire center with market shares above 1, 2, and 5 percent.⁷ The following summary is illustrative of what the table shows in more detail:

	Average No. of CLECs per wire center (per Qwest's Opening Brief, ¶ 24)	Average No. CLECs per wire center with > 5% Market Share
Zone 1	24.5	[Begin Confidential] * [End Confidential]
Zone 2	11.8	[Begin Confidential] *** [End Confidential]
Zone 3	13.3	[Begin Confidential] *** [End Confidential]
Zone 4	11.4	[Begin Confidential] *** [End Confidential]
Zone 5	5.5	[Begin Confidential] *** [End Confidential]

24. Table D additionally breaks the data down by wire center to show a better picture of the small number of CLECs with significant market shares in many parts of Qwest's service territory.⁸ This information is obscured by Qwest's use of zone-wide averages.

2. Staff overstates CLEC presence in smaller wire centers.

25. Staff's Opening Brief ¶ 46 asserts that CLECs are serving smaller wire centers in Washington: "For example, there are at least eight to 11 CLECs serving smaller wire centers such as Graham, Sequim, Longview, Moses Lake and Shelton. Three to six CLECs are serving the combined exchanges of Easton and Ephrata. Wilson, Ex. 232." A more granular inspection of CLEC activity in these wire centers, using Staff Ex. 209C, reveals a different picture.

- In Easton, for example, there **[Begin Confidential]** ***** **[End Confidential]**.

⁷ The table is based on Exs. 208C and 209C. Ex. 208C indicates the number of CLECs offering service in each wire center. Ex. 209C provides more granular detail with numbers of lines and market share for each CLEC by wire center. Both of these Staff exhibits are based on CLEC wholesale data from Qwest.

⁸ See also, Table A, attachment to Public Counsel's Initial Brief.

- In Ephrata, **[Begin Confidential]** *****

 *******[End Confidential]**. *See also* Public Counsel Initial Brief, Table A. Qwest market share in Easton is **[Begin Confidential]** *******[End Confidential]**, and **[Begin Confidential]** *** **[End Confidential]** in Ephrata.
- In Shelton, while Staff's Exhibit 232C indicates **[Begin Confidential]** ** **[End Confidential]** CLECs operate, the Qwest data in Ex. 209C shows that **[Begin Confidential]** *****

 ***** **[End Confidential]**. *See also*, Public Counsel Initial Brief, Table A.
 Qwest's market share in Shelton is **[Begin Confidential]** ***** **[End Confidential]**.

The trend in the other exchanges mentioned by Staff -- Graham, Sequim, Longview, and Moses Lake -- is the same, with most CLECs having **[Begin Confidential]** *******[End Confidential]** market share in those exchanges. Exhibit 209C; Public Counsel Initial Brief, Table A.

3. Staff testimony establishes that minimal CLEC presence will not discipline Qwest as the dominant incumbent.

26. At the hearing, Staff witness Wilson and Chairwoman Showalter discussed whether a market with 25 or 40 CLECs was more competitive. Mr. Wilson that at that level “the number itself is not so important as the proof in the pudding of customers being served and market share[.]” Tr. 1485. He went on to address the situation where only a small number of CLECs were competing:

Q. [Chairwoman Showalter] Now I assume if you get down to too low a number, such as two that answer would be different, that at some point the absolute number if it's low enough suggests a duopoly or some situation that's not very competitive?

A. That's right, gain [sic] theory suggests you get those small numbers, you know like a tennis game with two, then people collude and bad things can happen. *Also, it isn't enough to discipline the incumbent more dominant provider.* But I would like to note that that type of phenomenon I think in Washington state as a whole,

if we saw that happening everywhere, *it would be a concern*. If it were happening in certain areas, there might be other explanatory factors as well.

Q. But if it did occur in certain areas, *if for example it came to pass that say rural areas only had two providers, that would be a cause for concern wouldn't it?*

A. *Yes, I think so*. I have tried in the Staff analysis to focus particular attention on those most vulnerable areas of our state. Tr. 1485-86 (emphasis added).

As Public Counsel Tables A and D show, by highlighting the data in existing exhibits such as Exs. 208C, 209C and 55C, many areas of Washington face the very risks identified above by Mr. Wilson. The actual number of CLECs with more than a minimal market share is so small (one or two or less in many cases) that there is not enough presence to discipline the incumbent provider. This is particularly true in some of the most rural areas of the state.

4. Data issues.

27. There are two main bodies of data in the case, (1) the wholesale data provided by Qwest in its direct testimony and exhibits, for example Ex. 55 of Mr. Teitzel, and Staff exhibits which build on that data, for example, Exs. 208C and 209C of Mr. Wilson; and (2) the additional CLEC data produced in response to Order No. 6 (and subsequently), analyzed by Staff and incorporated in Staff exhibits such as Ex. 204C and Ex 232C. Both sets of data have their imperfections and the Commission is faced with a record that does not provide absolute precision on many points. Both Qwest and Staff rely on both bodies of data, more or less interchangeably. *See generally* Qwest's Opening Brief, Sections D.1.b and c. Staff's Opening Brief at ¶¶ 42-43 gives weight to the Qwest exhibits as demonstrating sufficient support for the petition. On the last day of the hearing, Staff witness Wilson testified that "Staff concluded that the actual core of the case...is [Qwest] Exhibit 55C which is the Qwest wholesale data." Tr. 1477. In general, the Qwest exhibits and related Staff exhibits provided more detailed information by CLEC, by wire center, and by exchange. Staff did not do any analysis of particular companies in the CLEC response because there was no time. Wilson, Tr. 1381.

28. The CLEC data reviewed in Staff's testimony is used to provide "additional augmentation to core data." Tr. 1477; *see also*. Staff's Opening Brief ¶¶44-46. There is

acknowledgement, however, that the CLEC data has its limitations. Qwest points out that differences between Staff and Qwest data may relate to several factors: (1) timing differences,⁹ (2) confusion on the part of CLECs between different types of services, and (3) Staff's inclusion of Qwest's exclusion of analog business services served over special access and digital facilities. Qwest's Opening Brief ¶ 48, note 43. Mr. Wilson concluded that the CLEC data was not "clean and consistent" enough to be used to calculate an HHI, and continued to support the HHI analysis based upon Qwest-provided data. Tr. 1377-1378.

29. There have been numerous corrections to the CLEC data, and an element of judgment was required to interpret the responses received, in part because some CLEC employees did not understand what to provide. In addition, a number of CLECs did not report location data, so that for approximately one third of the total CLEC access lines included in Staff's aggregations, no information was available to estimate number of customers served. Tr.1381.

30. Public Counsel's approach to the data has been to generally refer on brief to the Qwest data on wholesale competition, supplemented by the CLEC-supplied data on owned loops. Where possible, Public Counsel uses the Staff data to support points, but where data is not available in the form or detail required, citations are given to the Qwest and Staff exhibits which do provide data. None of these exhibits have been withdrawn or disavowed by the company or Staff, and as noted, continue to be cited by all sides.

31. A final point regarding data -- the data that the Commission will have available as a result of the Triennial Review proceedings appears likely to be more detailed, more comprehensive and of better quality than the information available here (see discussion below). The Commission will without question be in a better position to evaluate Washington's telecommunications market after the conclusion of that case than it is at present.

⁹ Qwest suggests that CLEC data provided in response to Order No. 06 is more recent than the Qwest year-end 2002 data. Order No. 06, however, asked CLECs to provide data as of December 31, 2002, the same vintage as Qwest data. Order No. 06, Ordering Paragraphs 2, 3.

B. Extent to Which Services Are Available

32. Qwest’s brief questions Ms. Baldwin’s testimony that business customers in some small exchanges might be surprised to learn there is competition. To rebut this point, Qwest cites to the Spokane phone book. Qwest's Opening Brief ¶ 29. As Commissioner Oshie pointed out, however, the fact that a company is listed in the information pages of the Spokane directory, doesn’t mean that the company provides service to every small community covered by the listings in the book. Testimony at the public hearing and letters in Ex. 800 reflect a perception on the part of some customers that competitive choice is not available to them. Public Counsel Initial Brief, Section IV.E.2.

33. Staff’s brief cites to the testimony of Integra witness Slater as evidence of the type of CLEC presence found in rural areas and serving small customers. Staff's Opening Brief ¶ 51. Notably, Staff does not mention Mr. Slater’s opinion that it would be a “grave mistake” if the Commission were to grant the petition, Tr. 879, and that it would be a “great surprise” to him if it did so. *Id.* When asked by Chairwoman Showalter if Integra would pull back from the state of Washington if the petition were granted, he noted that their existing investment would be an issue, but went on to say:

I am certainly not eager to walk away from that [investment]. But by the same token, I would make a business determination on how I really do feel about *the risks that I would perceive to have substantially increased as a result of that determination. And it would certainly go in the direction of us de-emphasizing our willingness to compete in Washington.* *Id.* (emphasis added).

Staff also minimizes Mr. Slater’s clear testimony that it has already “pulled back” from areas of Washington where competitive classification has been granted. *See e.g.* Tr. 862-63.

C. Ability to Make Functionally Equivalent or Substitute Services Available

1. Wholesale services.

34. Qwest’s discussion on this issue lends further support to the conclusion that different types of entry should be given different weight in the competition analysis. Qwest cites the migration of CLECs to UNE loops and eventually to owned loops in search of a greater ability to

differentiate their services and improve their competitive position. Qwest's Opening Brief ¶¶ 33-34. This underlines Public Counsel's point that while these are the most significant forms of entry because they reflect committed investment, they also are the least prevalent form of entry at this time in Qwest's service territory. *See* Public Counsel Initial Brief., Tables B and C. Ex. 416C.

Staff usefully recapitulates in its brief the Commission's holding "discounting the competitive importance of total service resale" and its underlying rationale. Staff's Opening Brief ¶ 56. This is an important point because much of the market share and market activity data in this case includes resale information. While the contribution of resale to CLEC market share is diminishing significantly, the inclusion of resale data in Staff and Qwest exhibits contributes to a false impression of the significance of CLEC activity. The Commission should adhere to its prior decision discounting resale from consideration.

2. CLEC-owned loops.

35. In Staff's Opening Brief ¶ 65, Staff suggests that "in many cases" CLECs compete using their own loops rather than leased facilities. Characteristic of the broad brush analysis in this case, this statement fails to inform the Commission that the data provided in Staff's own exhibits shows that **[Begin Confidential]** [End Confidential]** out of 68 Qwest exchanges **[Begin Confidential] *****[End Confidential]** have no owned loops. *See e.g.* Table C (attached to Public Counsel Initial Brief); Staff Ex. 204C.

D. Other Indicators Of Market Power

1. Market share analysis.

36. Qwest attempts to suggest that the Commission has had little concern for market concentration or market share evidence. Qwest's Opening Brief ¶ 41. This is at odds with the Commission's own description of its analysis in UT-000883, where the order specifically mentions market concentration data as a critical component of the decision as to which specific

exchanges would receive competitive classification and which would not. UT-000883, Seventh Supplemental Order, ¶¶ 75-76.

37. Qwest cites the AT&T decision, as it has before, as precedent for the proposition that a loss of 25% market share establishes effective competition. Qwest's Opening Brief ¶ 42. Even if it were appropriate to mechanically apply a number from a different case involving a different market and service, Qwest would still need to address the fact that in a very large number of its exchanges it has more than a 75 percent market share. In fact, at the time they filed this petition, the data Qwest provided showed that in every exchange Qwest's market share exceeded **[Begin Confidential]** ***** **[End Confidential]**. Exs. 54C and 415C. Perhaps it is this fact that causes Qwest to repeatedly focus on the statewide average market share figures.

38. Likewise, in the nearly three pages devoted to market share in Staff's brief, only statewide average market shares are cited. Staff's Opening Brief ¶ 69-75. Staff concludes by acknowledging that its calculated statewide market share for Qwest of 71.88 percent "may be a relatively high market share." Presumably, Staff would agree that the many Qwest exchanges with over **[Begin Confidential]** ***** **[End Confidential]** market share -- **[Begin Confidential]** ***** **[End Confidential]** than the statewide figure -- are also "relatively high." Staff, like Qwest, would prefer the Commission to focus on statewide averages rather than on the exchange level data.

39. Qwest reiterates a point made throughout the case that its own exhibits understate the degree of CLEC competition because Qwest did not have information on CLEC owned loops. Qwest's Opening Brief ¶ 44. As Public Counsel has pointed out elsewhere, only about **[Begin Confidential]** ***** **[End Confidential]** of Qwest exchanges have CLEC owned loops, however. Consequently, for over **[Begin Confidential]** ***** **[End Confidential]** of Qwest service territory, the data in Qwest's exhibits does not overstate its market position.

40. Qwest challenges the market share calculations in Public Counsel testimony and exhibits. Public Counsel's arguments on brief, however, focus on the data in Qwest and Staff testimony and exhibits, and Qwest's failure to carry its burden of proof.

2. Different modes of entry must be given different weight.

41. Staff's brief misunderstand Public Counsel's argument regarding measuring market share. Staff's Opening Brief, ¶24. In general, Public Counsel has employed the market share figures available from the record which are based on CLEC wholesale activity. What Public Counsel urges is that the Commission not give equal weight, in evaluating effective competition, to any form, no matter what mode. Total service resale should be discounted in the analysis for example, because, as the Commission has found, it does not constrain price. At the other end of the spectrum, there is no dispute that facilities-based entry is the strongest evidence of commitment to compete. The point to keep in mind is that the latter form of entry represents only a small percentage of activity in the market. As noted elsewhere, it is not relied upon by Qwest as the primary basis for its petition, and with good reason, since such entry is quite limited in Washington. Public Counsel Initial Brief, Confidential Table B.

3. Market concentration.

42. Qwest chastises Public Counsel and others for refusing to provide a market concentration "bright line" for the Commission to use in determining when effective competition is present. Qwest's Opening Brief ¶79. There are several responses to this criticism. First, the HHI itself provides a bright line, a set of gradations to distinguish between high, moderate, and unconcentrated levels. Second, no purpose would be served by such a theoretical exercise when the evidence does not indicate a "close call" as to whether markets are concentrated or not. Third, Qwest has the burden of proof in this case. It is not the task of other parties to establish a theoretical target for some future petition to meet.¹⁰

¹⁰ Qwest states that Public Counsel witness Baldwin suggested that an HHI of 5000 offered a guidepost. Ms. Baldwin made clear that an HHI is characteristic of a duopoly, not a competitive market. Tr. 824.

43. Staff's brief refers to oral testimony of Ms. Baldwin which supposedly concedes that that "[m]arket share and HHI are minor parts of the overall analysis" of effective competition. Staff's Opening Brief ¶ 80. Examining the transcript at the cited line and page, Tr. 828, lines 17-20, reveals that Ms. Baldwin said nothing of the sort. Most of the citation is Commissioner Oshie's question about whether market concentration equals market power. Ms. Baldwin states that "there are other factors absolutely," Tr. 828, line 20, but goes on to explain that they are not "as strong a tool," Tr. 829, line 13. She finishes by cautioning that "if you haven't gotten to diminished market concentration, the rest is not --- you can look at it, but if you can't find that Qwest's market share has diminished substantially, I don't see how you can consider any of these services competitive." Tr. 829, lines 16-20.
44. Public Counsel strongly disagrees with Mr. Shooshan's suggestion that Qwest's position as the bottleneck provider of wholesale elements for competitors should be viewed as somehow mitigating its market power. Tr. 532. Qwest does not give away its wholesale facilities, but earns revenue from them, even when a line is "lost" to a CLEC. By comparison, a loop provided over a CLEC's own facility represents far more significant market share erosion. Qwest's wholesale provisioning obligations, therefore, actually cushion and limit the loss. By contrast, in a market without the UNE feature, for example in auto sales, loss of a customer to a competitor causes 100 percent revenue loss. Tr. 826-827.
45. There are a number of HHI exhibits in the record, including two from Staff and three from Public Counsel. At this stage of the case, Public Counsel recommends that the Commission look primarily to the HHI in Staff Exhibits 208C and 209C. Public Counsel HHI exhibits 403C and 404C are similar.¹¹ As Staff acknowledges, "a traditional HHI analysis yields numbers consistent with a highly concentrated market." Staff's Opening Brief ¶ 80, citing Wilson, Ex. 201T at 24:12.

¹¹ Public Counsel does not suggest that the Commission rely upon its Exhibit 405C (updated in Ex. 425C) at this stage, since the exhibit was designed to illustrate the effect of a presumption that 50 percent of the owned line data included analog data. Qwest's brief focuses on this Public Counsel HHI analysis, not mentioning Exs 403C and 404C which are based on Mr. Teitzel's data. Qwest's Opening Brief ¶ 80.

4. Ease of entry.

46. Staff's discussion on ease of entry particularly notes the significance of UNE-P as an CLEC entry path:

CLEC reliance on resale is diminishing, and CLECs are relying more on UNE-P as an entrance strategy. UNE-P is one of the most effective means of entering the local market and has enhanced competition over the last few years. The economics of UNE-P is more advantageous for CLECs than the economics of resale. Staff's Opening Brief ¶ 85 (citations omitted).

Regardless of how effective UNE-P may be, Qwest is actively seeking to have it removed as an option by virtue of its UT-033044 petition and its federal court challenges to the Triennial Review Order. Staff seeks to both tout the effectiveness of UNE-P as an entry strategy, but dismiss its significance when the impact of the Triennial Review Order is discussed.

47. Staff states in its brief that "[t]here is evidence of CLECs purchasing UNE loops in most exchanges in Qwest's service territory." Staff's Opening Brief ¶ 86, citing Mr. Wilson's testimony at Tr. 622:14-16. Mr. Wilson actual testimony was not quite so confident:

Q. [Mr. Levin] Based on the results of your survey, what percentage of exchanges had --- did CLECs report providing UNE loop facility – UNE loop-based services in?

A. I haven't made that calculation. It was most of them.

Q. UNE loop services were provided in most exchanges?

A. I think so.

Staff did not provide a reference to an exhibit verifying Mr. Wilson's calculation. The evidence of CLEC wholesale activity for business services provided by Qwest tells a different story.¹² Teitzel Exhibit 54C shows that of 68 Qwest exchanges, only **[Begin Confidential]** [End Confidential]** have CLECs providing service by UNE-loop. This information is also displayed separately in Baldwin Exhibit 416C. These exhibits indicate the **[Begin Confidential]** [End**

¹² See Qwest's Opening Brief ¶ 48, n. 43 for Qwest's view of why Staff and company numbers differ.

Confidential] towns and cities in every part of the state that have no CLEC UNE-loop service.¹³ Staff prefers to focus on statewide averages to defuse the impact of this type of statistic, arguing that unserved exchanges represent only **[Begin Confidential] ***** [End Confidential]** of lines statewide. Staff's Opening Brief ¶ 86, n. 14. A review of the lists of communities in Exhibits 54C and 416C shows however, the broad geographic extent of limited entry.

5. Other factors: Qwest dominant pricing behavior was ignored in the Staff and Qwest briefs.

48. While making much of the other factors to be considered as a counterweight to market share and market concentration figures, a factor that Qwest and Staff do not address is perhaps the most revealing -- Qwest's dominant pricing practices. While Qwest repeatedly asserts the need for pricing flexibility and the intensity of competitive pressure, it makes no significant use of the pricing flexibility available to it under existing law, it maintains prices at a significant margin above cost, and it has not taken advantage of the competitive classification it has in some of its most highly competitive exchanges. *See* Public Counsel Initial Brief, Section IV.D.5

49. In denying Qwest's last request for competitive classification of these same services in UT-000883, the Commission specifically reminded Qwest of its other options to compete:

Our decision to deny Qwest's petition as filed does not constrain the company from using other tools to compete with other providers of local exchange services. Qwest can use banded rate tariffs, offer business services through a competitive affiliate, offer promotions, offer winback incentives, and lower prices in response to competition. Seventh Supplemental Order, ¶ 70. (citing Staff testimony).

It follows that a critical part of evaluating Qwest's petition in this case must be to examine whether and to what extent Qwest followed the Commission's advice, particularly in view of the close relationship between the two petitions. Unlike the UT-000883 case, Staff did not engage in or present such an analysis to the Commission in this docket and remains silent on the question in its brief. Public Counsel and other parties, however, have addressed the question and have

¹³ Moreover, as Public Counsel's Confidential Table B shows, Qwest's evidence in this case is that **[Begin Confidential] ***** [End Confidential]** of Qwest exchanges have no lines served by CLECs via UNE loop *or* owned loops.

provided evidence for the Commission to review this question. That evidence shows that Qwest continues to engage in pricing behavior indicative of market power.

E. Qwest Has Failed To Show It Does Not Provide Service To A Significant Captive Customer Base

50. Both Qwest and Staff refer to Ms. Baldwin's testimony regarding the definition of captive customers. Qwest's Opening Brief ¶¶ 90-91; Staff's Opening Brief ¶ 92, n. 15. The statute does not provide a definition for the term. Of course, the easy case is one where an incumbent has a 100 percent monopoly. No competitors of any kind are present. Customers have no choice. This is the definition offered by Staff and Qwest. *Id.* The inquiry is not so simple, however.
51. It is true that simply because a customer has not selected an alternative provider it is not necessarily captive. On the other hand, the fact that a small fraction of customers, perhaps the larger businesses in the area, have chosen a competitor, does not mean that the remaining small business customers cannot be found to be captive. The theoretical availability of service does not necessarily equal the practical availability of service. Real barriers may remain that *render* these options meaningless in practice, leaving some customers captive: for example (1) inadequate information: customers are captive if they do not understand that they can select a carrier other than Qwest, if they do not realize, for example, that they can keep their telephone number; (2) carriers selectively target their marketing campaign to large businesses and do not earnestly seek out small businesses or remote exchanges; (3) incumbency advantage: the risk-averse customers will choose to stay with the well-established entrenched provider of basic essential services. In some cases, then, the failure to select an alternative carrier is a bellwether for captivity, an indicator of the existence of remaining captive customers.

V. OTHER ISSUES

A. Impact of Other Dockets

1. Cost Dockets.

52. There are now pending proposals to defer review of Qwest and Verizon recurring and non-recurring UNE rates in dockets UT -023003 and 033034.¹⁴ If granted, it appears that in this respect, imminent changes in these ILEC UNE rates will not occur in the near term. The deferral proposals do not apply to the “core/fringe” geographic deaveraging proposal of Staff, however. Adoption of “core/fringe” deaveraging could potentially cause major changes in the Washington market structure, even without revisions to underlying UNE rate.

53. Paralleling Public Counsel’s recommendations in this docket, the Joint Motion bases the request for deferral on the combination of developments resulting from of the FCC Triennial Review Order and the new TELRIC rulemaking. Verizon’s Response “agrees that the FCC’s recent proposal to revisit the core legal standard that will govern all of the issues in these proceedings weighs strongly in favor of deferral.” Response, p. 1. Verizon also agrees with Joint Movants that “the pending Commission inquiry about the scope of unbundling obligations supports deferral here.” Verizon Response, p. 2, n. 2. While Public Counsel does not necessarily suggest it is necessary to defer any competitive classification proceeding to the conclusion of the TELRIC case, these pleadings reflect a consensus among Washington’s major ILECs and CLECs that the FCC proceedings will have an important impact on the competitive landscape in the state.

2. The Triennial Review Proceedings.

a. Qwest’s stance on UNE-P is fundamentally inconsistent.

54. While the uncertainty about the cost structure discussed above is of concern, Public Counsel believes the most compelling reason for the Commission to deny this petition, in addition to its flaws on the merits, is the impact of the pending TRO impairment proceedings.

¹⁴ Joint Motion to Exclude Qwest Rate Issues (Joint Motion); Response of Verizon Northwest Inc. to Joint Motion to Exclude Qwest Rate Issues (Verizon Response)..

This context of surrounding events is simply too important to ignore, though Qwest and Staff suggest the Commission do so.

55. It is particularly troubling that Qwest simultaneously seeks to eliminate unbundled switching, and hence UNE-P, on the grounds that competition does not require its availability, while at the same time relying on the availability of UNE-P entry as one of the fundamental proofs of competition in Washington. Simultaneously, having failed before the FCC, Qwest is now seeking through federal court action to achieve the elimination of UNE-P.

56. Qwest suggests that elimination of UNE-P is not a significant concern because competitors can still use resale and UNE-L. Instead, Qwest asserts that “in virtually all parts of the state, competitors are using resale or loops or both *in addition to* UNE-P.” Qwest's Opening Brief ¶ 95 (emphasis in original). Staff makes essentially the same argument, stating that “substantial competition exists without UNE-P” and that “in any event, CLECs will continue to have access to UNE loops and resale.” Staff's Opening Brief ¶ 102.

57. This is misleading. As Table B attached to Public Counsel's Initial Brief shows, in **[Begin Confidential]** *******[End Confidential]** of Qwest's territory **[Begin Confidential]** *****[End Confidential]** of 68 exchanges), in all parts of the state, there are exchanges where, when non-price constraining resale is not considered, and UNE-P is no longer available, there is zero CLEC presence. Said another way, if UNE-P were removed, in **[Begin Confidential]** ** **[End Confidential]** of 68 exchanges there would be zero CLEC relevant presence, because in those exchanges there are zero CLEC lines via UNE-loop, zero CLEC lines via owned loops, and any resale lines are not considered to be price constraining. **[Begin Confidential]**

***** **[End Confidential]**. Ex. 209C.

b. The Mass Market Impairment docket (UT-033044) will in the near term provide the Commission with a more complete understanding of the Washington telecommunications market.

58. The FCC has delegated to the Commission the authority to rebut the FCC's finding of impairment by conducting a granular, market by market analysis concerning impairment for mass market switching. Because of the nature of the analysis required by the FCC's Triennial Review Order, the Commission can expect that at its conclusion, less than nine months from now, it will have a much better picture of the Washington telecommunications marketplace than it does today. The Commission's Order No. 3 Requiring Disclosure of Information in UT 033044 provides an excellent overview of the type of detailed record that will be developed. Information that is required to be disclosed by carriers includes:

- all switches used by a carrier
- the physical location of the switch including the address, CLLI code, and LATA
- whether the switch is owned or leased and if not owned the nature of the arrangement
- information about switch type, capacity, geographic area served, initial cost and number of initially equipped lines
- all Qwest wire centers served by the identified switches
- the number of voice grade equivalent lines served by the identified switches in each wire center¹⁵
- the number of lines provided to residential customers, mass market business (1-3 lines at one location); medium business (4-24 lines at one location); and large business (25 or more lines at one location).¹⁶
- monthly revenues per line for each type of service provided broken down by each component of revenue including services, features, taxes, and fees

¹⁵ Note that the impairment analysis will examine all voice grade equivalent lines serving the mass market, not just lines providing analog services as in this case. It is significant that the FCC's analysis, which is exceedingly granular as to all aspects of the market, makes no distinction between analog and digital services. This again suggest that the Qwest market definition in the instant docket is improperly drawn.

¹⁶ As noted above, contrast this with the recommendation by Staff for a Commission finding that no separate mass market segment exists for small business.

- average monthly costs per line broken down by cost component
- detailed information about plans for wholesaling, leasing or reselling switch capacity
- end-user customer churn rate
- all transport facilities
- all Qwest wire centers to which the CLEC provides transport facilities for other carriers
- interconnection points with non-Qwest carriers
- list of all fiber rings owned or controlled in Washington and their locations
- collocation information for each Qwest wire center
- extensive information about facilities in “collocation hotels”

Other information is also requested. *See* Docket No. UT-033044, Order No. 03, Order Requiring Disclosure, CLEC Questions 1-31. The information will not be masked or aggregated so that parties can “more effectively and adequately evaluate the evidence” and present it to the Commission. *Id.* ¶ 9.

59. Qwest’s non-impairment petition states “[b]ecause switching impairment is a market-specific concept, it is necessary to identify geographic markets – geographic areas within which firms do or can offer services in competition with ILEC services to residential and small business customers over non-ILEC switches – where there is sufficient evidence to rebut the national finding.” Qwest Petition, p. 12. Qwest’s petition details the careful fact-finding analysis it believes must be carried out and, by contrast with this case, argues that geographic market definition is so complex and data dependent it could not meet the Commission’s requirement to identify markets where it asserts non-impairment. Qwest Petition, p. 15. Qwest is asking the Commission, within the space of a few months, to issue an order in this docket defining the business market as competitive based on the presence of UNE-P, with the market statewide, analog-based, and undifferentiated by customer size, while in the TRO docket it defines the market competitive without UNE-P, segmented by customer size, geographically more granular,

and based on voice grade equivalent lines. Public Counsel urges the Commission to decline to go down this path.

B. Cost Floor

60. Qwest and Staff each reassure the Commission that specific price floor issues do not need to be resolved as a part of this docket, or as a condition to a grant, since RCW 80.33.330(3), (4), and (6) provide adequate guidance to resolve any disputes that arise. It appears, however, that Qwest and Staff do not agree on the fairly important question of the whether an imputation test is the way to determine if prices are below cost.

61. In Staff's view, "the Commission has held that it is appropriate to determine the cost floor for price listed services by applying an imputation test." Staff's Opening Brief ¶ 107. Staff sees the imputation test as the method to determine whether the legal requirement that Qwest not price below cost is met. Staff's Opening Brief ¶10, relying *inter alia* on WAC 480-80-204(6) Id. ¶107. Staff supports a TELRIC-based cost floor. Id.

62. Qwest, on the other hand, opposes an imputation requirement because "it fails to acknowledge that there is significant facilities based competition." Qwest's Opening Brief ¶102 and n. 95. Qwest also disagrees with Staff's view that TELRIC is the correct pricing methodology for determining the price floor, preferring the use of TSLRIC. Id. ¶101. These disagreements belie the proponents' reassurances that the price floor requirement can be easily enforced at some future date.

VI. CONCLUSION

63. For the foregoing reasons, Public Counsel urges the Commission to deny Qwest's petition for competitive classification of analog basic business, PBX, and Centrex services

throughout its Washington service territory. Public Counsel supports the development of competitive choices for consumers in Washington. Approval of this petition will not advance that goal.

DATED this 7th day of November, 2003.

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