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Introduction and Qualifications

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Glenn Blackmon, Ph.D. My business address is 1300 S Evergreen Park Drive SW, Olympia, Washington, 98504. My e-mail address is blackmon@wutc.wa.gov.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by the Washington Utilities and Transportation Commission ("WUTC") as Assistant Director-Telecommunications.

Q. PLEASE STATE YOUR QUALIFICATIONS TO PROVIDE TESTIMONY IN THIS PROCEEDING.

A. I hold Ph.D. and master's degrees in public policy from Harvard University and a bachelor's degree in economics from Louisiana State University. I have been employed at the WUTC since August 1995 and assumed my current position in April 1996. I previously served as the WUTC's economics advisor in the interconnection case, Docket UT-941464, and the major U S WEST general rate case, Docket UT-950200.

In my current position, I have testified before the WUTC in various proceedings, including U S WEST's most recent general rate case (Docket UT-970766), the GTE/Bell Atlantic merger case (Docket UT-981367), the Qwest/U S WEST merger case (Docket UT-991358), the generic cost and price case (Docket UT-960369), and the WorldCom/Sprint merger case (Docket UT-991991).

1 Prior to working at the WUTC, I was a consultant in private practice, where my
2 clients included both regulated companies and consumer advocates, and I was an analyst
3 for the Washington State Senate Energy and Utilities Committee. In addition to the
4 telecommunications cases that I mentioned earlier, I have presented testimony as an
5 expert witness before the WUTC in electric and natural gas cases, as well as before the
6 Illinois and Idaho commissions.

7 I am the author of a book, *Incentive Regulation and the Regulation of Incentives*
8 (Boston: Kluwer Academic Publishers, 1994). I have authored or co-authored articles on
9 utility regulation and economic theory published in *American Economic Review*, *Journal*
10 *of Regulatory Economics*, *Yale Journal on Regulation*, *Journal of Risk and Uncertainty*,
11 and *Public Utilities Fortnightly*.

12
13 **Q. PLEASE DESCRIBE YOUR WORK AT THE WUTC AS IT SPECIFICALLY**
14 **RELATES TO ISSUES OF COMPETITION AND APPROPRIATE**
15 **REGULATORY TREATMENT OF COMPETITIVE SERVICES.**

16 A. During the time I have headed the telecommunications staff we have undertaken a broad-
17 based and successful effort both to promote competition and to reform the regulatory
18 treatment of companies and services to match the increasing level of competition. In
19 1997, Staff initiated a case in which the WUTC classified GTE-Northwest's toll service
20 as competitive, after the company had begun allowing customers to choose their 1-plus
21 carrier for local toll calls (UT-990767).

1 In 1999, Staff, after having successfully challenged U S WEST's refusal to grant
2 dialing parity to its competitors, joined with the company in a competitive classification
3 process that permitted the company to begin pricing flexibly on the same day that
4 consumers began having 1-plus choice (UT-990021).

5 More recently, Staff undertook, again on its own initiative, a project to classify
6 almost 150 long-distance and operator service companies as competitive (UT-990985, et
7 seq.). The purpose of this effort was to reduce the level of regulation based on the
8 presence of effective competition in the long-distance market.

9 In another 1999 case, I participated with other staff in the case in which the
10 WUTC established that a "relevant market" for a service could be a defined geographic
11 area, rather than the entire state, and granted pricing flexibility to U S WEST for high-
12 capacity private line service within certain urban zones (UT-990022).

13 Finally, I have been actively involved in legislative activities in which changes to
14 the competitive classification laws themselves were contemplated, and I led the
15 successful effort in 1998 to amend the laws to streamline the process by which the
16 WUTC considers competitive classification petitions.

17
18 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

19 A. I will present Staff's recommendation in this case, which is to grant pricing flexibility to
20 Qwest within the requested wire centers of four of the nine exchanges that are the subject
21 of this proceeding, but only for customers served on a DS-1 or larger circuit. I also will

1 offer a possible alternative of granting the classification with respect to smaller customers
2 as well, but only if Qwest agrees to specified conditions. I also will respond to assertions
3 made by Qwest about the reasons why the WUTC might approve this petition and the
4 overall state of competition in the business local exchange market.

5
6 **Response to Qwest Testimony on Pricing Flexibility and Competition**

7 **Q. DO YOU AGREE WITH QWEST ABOUT THE REASONS WHY THE WUTC**
8 **MIGHT APPROVE THIS PETITION?**

9 A. No. Qwest asserts that its "hands [are] tied" by existing regulatory requirements and it
10 should be given more pricing flexibility in order to generate revenues that will mitigate
11 the need for future rate increases. Exhibit _____ DLT-1T at 3. I disagree completely
12 both with how the company characterizes the current regulatory structure and how
13 competitive classification affects customers of non-competitive services. The reality is
14 that Qwest has many tools at its disposal that it could be using to be more competitive
15 with other providers of local exchange service. Qwest appears not to want to use those
16 tools, probably because they involve lowering prices for consumers. I also disagree with
17 the suggestion that the WUTC should help Qwest preserve market share in one part of its
18 business in order to generate profits that will avoid rate increases in another part of its
19 business. The WUTC's role is much simpler in a case such as this: to look for effective
20 competition and to grant pricing flexibility if and only if it finds effective competition.

1 **Q. PLEASE REVIEW THE TOOLS THAT ARE AVAILABLE TO QWEST FOR**
2 **RESPONDING TO COMPETITION AND HOW QWEST HAS USED THEM.**

3 A. Besides seeking pricing flexibility for a particular service as it is doing in this case, Qwest
4 can:

5 1. Introduce new services - As Qwest notes, it has introduced some services that
6 appear to be specifically designed to respond to offerings of its competitors, including
7 Centrex 21 and Integrated T-1 service.

8 2. Offer promotions - Qwest can offer waivers of the initial charges for a service or a
9 period of free service, and these promotions can be targeted to particular types of
10 customers and particular geographic areas. Qwest asserts that its use of promotions is
11 hampered by a 30-day notice requirement, but there actually is no such requirement. The
12 Legislature in 1997 changed the law, at the WUTC's request, to allow such promotions to
13 be filed on 10-day notice. Moreover, it is difficult to reconcile Qwest's claim that a 30-
14 day notice is burdensome with the fact that Qwest is voluntarily providing competitors
15 with even more than 30-day notice of many of its promotions.

16 3. Offer winback incentives - In Docket UT-990149 the WUTC allowed Qwest to
17 offer a waiver of installation charges and up to two months of free service to business
18 customers who had switched to alternative providers.

19 4. Use banded rate tariffs - In 1996, the WUTC authorized the company to offer any
20 service under a banded rate. A banded rate has a ceiling and floor, and price changes
21 within that range can be made on 10-day notice without WUTC approval. (Before 1996,

1 the WUTC had required that the company justify its use of banded rates each time it
2 proposed them.) Qwest has recently introduced two new services with banded rate
3 pricing. Qwest suggests that banded rates are not useful, because any change in the
4 ceiling and floor require a 30-day notice. This is correct (except that it omits the
5 opportunity to seek a waiver of the 30-day notice requirement), but it misses the point.
6 Qwest should not need to change the ceiling and floor, and changes within the band are
7 quick and easy. Qwest can set the floor at its cost, and surely it would not want to price
8 below its cost. Qwest can set the ceiling at the current tariff price for existing services,
9 and surely it would not need to raise prices to respond to competition. For new services,
10 it can set the ceiling where it wishes. Banded rates therefore provide Qwest with a great
11 deal of pricing flexibility without any need to demonstrate that a service is subject to
12 effective competition.

13 5. Lower prices in response to competition - Qwest can lower prices on 10-day
14 notice, as long as it promises not to seek an offsetting price increase from other
15 customers. This is exactly comparable to what competitors have, since they have a 10-
16 day notice provision and have no ability to raise prices to captive customers. Qwest
17 attempts to suggest that it cannot limit any price decrease to areas where it faces
18 competition, but this is not accurate. It is true, as Qwest says, that in 1996 the WUTC
19 "ordered Qwest to charge state-wide rates for its basic business products and services,"
20 but the implication that the WUTC ordered it to freeze rates at that level is wholly
21 incorrect. Exhibit _____ DLT-1T at 5. The WUTC took the company's skewed rate

1 structure – in which rural rates were lower than urban rates and multi-line rates were
2 higher than single-line rates – and moved it significantly closer to cost. The company
3 was free then to propose further steps along those lines, and it still is today.

4 Indeed, in 1997 the company proposed a rate reduction limited to the Spokane
5 exchange, where it said it was facing substantial competition. The WUTC did not reject
6 that filing, as one would think from the claims in Qwest's testimony. Rather, the
7 company withdrew the filing after it lost its appeal of the 1996 rate case and was required
8 to reduce business rates statewide below the level it had chosen for the supposedly
9 competitive area of Spokane.

10 6. Offer business service through a competitive affiliate - Qwest does not even
11 mention this option in its testimony, but probably the single most effective tool that
12 Qwest has left untouched is to establish its own competitive local exchange company.
13 Other incumbent local exchange companies have taken this option, including the
14 corporate parents of Verizon Northwest, Mashell Telecom, YCOM Networks, and
15 Ellensburg Telephone. Such an affiliate does not have to build and operate its own
16 network. It can resell the services of its regulated affiliate or interconnect and use
17 unbundled network elements of the regulated company.

18 The other companies' affiliates have been granted competitive classification by the
19 WUTC under RCW 80.36.320, which gives the companies even more regulatory relief
20 than Qwest could ever get by filing a petition for competitive classification of a service
21 under RCW 80.36.330. The downside of this approach, from Qwest's perspective, would

1 be that the affiliate would have to stand in line with the other competitive local exchange
2 companies for interconnection, provisioning, and repairs.

3

4 **Q. HOW DO YOU RESPOND TO THE QWEST ARGUMENT THAT IT NEEDS**
5 **PRICING FLEXIBILITY BECAUSE IT CANNOT OFFER LONG-DISTANCE**
6 **SERVICE AS THE COMPETITIVE LOCAL EXCHANGE COMPANIES CAN?**

7 A. I do not dispute the claim that some customers are attracted to competitors because of
8 their ability to include long-distance service in their offering, though I am dubious that
9 this is as big a factor as Qwest claims. In any case, Qwest can get into the long-distance
10 business as soon as it demonstrates that it has opened its local network to competition.
11 Indeed, it is somewhat ironic that Qwest would offer this as a rationale for pricing
12 flexibility, since opening its local network to competition would also make it much easier
13 for the WUTC to grant competitive classification of Qwest's business local exchange
14 service.

15

16 **Q. DO YOU CONTEND THAT, BECAUSE QWEST HAS NOT MADE USE OF THE**
17 **OTHER PRICING TOOLS AVAILABLE TO IT UNDER WUTC REGULATION,**
18 **THE PETITION FOR COMPETITION CLASSIFICATION SHOULD BE**
19 **DENIED?**

20 A. No. The law does not say that a company has to use banded rates or a competitive
21 affiliate or 10-day notice promotions or price reductions before it can seek competitive

1 classification. The WUTC should decide the competitive classification petition on its
2 merits, based on the evidence in this case. However, just as Qwest is not obligated to use
3 the tools it already has, the WUTC should feel no obligation whatsoever, in the absence
4 of a showing of effective competition, to grant this pricing flexibility to offset some
5 perceived inequity in the regulatory structure.

6
7 **Staff's Recommendation to Grant Limited Pricing Flexibility**

8 **Q. PLEASE DESCRIBE THE APPROACH USED BY STAFF IN DEVELOPING A**
9 **RECOMMENDATION IN THIS PROCEEDING.**

10 A. Staff has looked at this request from many different perspectives and has used a variety of
11 approaches to assess the merits of Qwest's petition.

- 12 • Staff reviewed in detail the evidence submitted by Qwest in support of its petition.
- 13 • Staff surveyed every company identified by Qwest as a competitor about its activity in
14 these markets. This was the first time the WUTC used its authority under RCW
15 80.36.330(5) to collect competitive data from companies that were not parties to a
16 competitive classification case. The results of that survey are presented in Staff witness
17 Bhattacharya's testimony.
- 18 • Staff reviewed the best evidence available about how easy or difficult it is for competitors
19 to use Qwest's network to offer competitive retail services to business customers.
- 20 • Staff also asked the competitive companies about their business plans, to ascertain
21 whether they were actively contesting all segments of the business market.

- 1 • Staff interviewed telecommunications consulting firms in Spokane and Vancouver who
2 are familiar with the competitive environment there.
- 3 • Finally, Staff did what a potential business customer would do: we contacted the
4 competitors' business offices and inquired about their service.

5

6 **Q. BASED ON THIS ANALYSIS, WHAT IS STAFF'S RECOMMENDATION?**

- 7 A. Staff recommends that the WUTC grant pricing flexibility to Qwest in the requested wire
8 centers of four of the nine exchanges where it is requested -- Seattle, Bellevue, Spokane,
9 and Vancouver. However, Staff recommends that the pricing flexibility be limited at this
10 time to customers served on a DS-1 or larger circuit, unless Qwest agrees to stringent
11 conditions that would protect smaller customers until Qwest has fully opened its network
12 to competition. The petition should be denied at this time in the remaining exchanges.

13

14 **Q. WHAT IS THE BASIS FOR THE RECOMMENDATION TO GRANT LIMITED**
15 **COMPETITIVE CLASSIFICATION WITHIN THE FOUR EXCHANGES?**

- 16 A. Staff has reviewed the structure of the local exchange market and the degree of market
17 concentration in each of the nine exchanges. We conclude that, where large business
18 customers are concerned, there is not a significant captive customer base in the requested
19 wire centers within the Seattle, Bellevue, Spokane, and Vancouver exchanges. Qwest's
20 business local exchange service is subject to effective competition in these geographic
21 areas and for this set of customers.

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Market Structure Analysis

Q. PLEASE EXPLAIN WHAT YOU MEAN BY THE STRUCTURE OF THE LOCAL EXCHANGE MARKET.

A. By the structure of the market I mean the way firms relate to each other, to their suppliers, and to their customers. The structure of the market includes how easy it is for firms to enter and exit the market and how easy it is for customers to change from one competitor to another.

Q. PLEASE DESCRIBE YOUR UNDERSTANDING OF THE BUSINESS LOCAL EXCHANGE MARKET IN THESE EXCHANGES.

A. In each exchange, Qwest is the incumbent local exchange company and the largest single provider of business exchange service. A number of competitors have installed switching equipment that serves an entire metropolitan area and fiber optic rings that pass through the parts of the exchange. Competitors also have collocated their equipment in most of the central offices serving the wire centers that are the subject of this proceeding. Competitors are using a variety of methods to reach the premises of individual customers, including building their own fiber facilities, purchasing special access circuits (such as DS-1 or DS-3) from Qwest, and purchasing unbundled loops from Qwest. Competitors also may seek to serve customers using no facilities of their own, either by reselling Qwest's retail service or by using an end-to-end combination of unbundled network elements, known as the UNE platform or UNE-P.

1 **Q. CAN EVERY COMPETITOR REACH EVERY CUSTOMER THROUGH EVERY**
2 **ONE OF THESE METHODS?**

3 A. No. The viability of each method as a mode of competition varies based on geography,
4 customer size, and availability. Staff believes that there is no evidence to suggest that
5 small business customers have any viable alternative to Qwest's business exchange
6 service, because none of the methods I just listed is reasonably available and financially
7 viable for that market segment. However, the large business segment – i.e., any customer
8 whose demand can justify a DS-1 or larger circuit – does appear to have reasonably
9 available alternatives in some exchanges.

10

11 **Q. PLEASE EXPLAIN HOW STAFF REACHED THIS CONCLUSION.**

12 A. The table in Exhibit _____ BGB-2 summarizes Staff's analysis of the various access
13 methods. Given the competitors' investment in switching and fiber optic transport
14 facilities, the bottleneck to competition in these urban wire centers is the circuit out to the
15 customer's premise.

16

17 **Q. AS A GENERAL MATTER, DO YOU BELIEVE THE WUTC SHOULD**
18 **CONSIDER A COMPETITOR'S SERVICE TO BE A VIABLE ALTERNATIVE**
19 **TO QWEST IF THE COMPETITOR IS USING QWEST'S NETWORK TO**
20 **REACH CUSTOMERS?**

1 A. Yes, if it is priced independently of retail business exchange service and if it is readily
2 available to competitors. The key question in evaluating whether a service is a viable
3 alternative is whether that service can constrain Qwest's ability to exercise market power
4 by increasing prices. Access using either Qwest dedicated access circuits or unbundled
5 network elements obtained from Qwest does represent a potential source of price-
6 constraining competition. The limitations, however, are that special access circuits are
7 not practical for small business and unbundled network elements are not yet a proven
8 commercial product.

9
10 **Q. WHAT DO YOU MEAN WHEN YOU SAY THAT THE ACCESS METHOD**
11 **MUST BE PRICED INDEPENDENTLY OF QWEST'S RETAIL BUSINESS**
12 **EXCHANGE SERVICE?**

13 A. This means that Qwest cannot price its retail service in tandem with the network access
14 service. If Qwest is free to raise network access prices, that network access cannot
15 constrain Qwest's ability to sustain retail prices above a competitive level. DS-1 circuits
16 are, depending on the geographic area, either already classified as competitive or subject
17 to continuing rate regulation by the WUTC. DS-1 prices are regulated either by the
18 competitive market or by the WUTC, but in neither case is Qwest free to raise those
19 prices.

20 Regarding unbundled network elements, by law, prices for these must be set by
21 the WUTC based on Qwest's costs. If Qwest were to raise its retail prices, the prices

1 competitors pay for unbundled network elements would not increase. Customers could
2 avoid the retail increase by switching to competitors.

3

4 **Q. WHY DO YOU CONCLUDE THAT UNBUNDLED NETWORK ELEMENTS**
5 **ARE NOT A VIABLE SOURCE OF PRICE-CONSTRAINING COMPETITION**
6 **FOR QWEST'S BUSINESS EXCHANGE SERVICE?**

7 A. This is, I believe, the key question in this case. If either unbundled loops or the UNE-P
8 were readily available to competitors using proven ordering, provisioning, and repair
9 systems – in the way, for example, that switched access service and the primary
10 interexchange carrier change process is available to long-distance companies – then I
11 believe the WUTC could safely classify all business exchange services as competitive.
12 Indeed, with a viable UNE-P alternative, the classification might well include all areas of
13 the state.

14 Certainly as a legal matter Qwest has a duty to provide reasonable access to its
15 network, and there is every reason to believe that ultimately this access will be provided.
16 However, the WUTC must decide this case based on facts as they exist now. The current
17 situation is that unbundled loops and the UNE-P are not readily available for serving the
18 mass market small business customer segment. They cannot be counted on to constrain
19 Qwest from raising retail prices.

20 There is literally no end to the performance metrics one could consider in
21 attempting to gauge whether unbundled loops are a readily available alternative to retail

1 service, but one very basic measure suggests that competitors are not yet getting
2 comparable service. The first chart in Exhibit _____ (BGB-3C) illustrates the average
3 installation interval, in days, for Qwest's own retail business orders and for competitors'
4 orders for unbundled loops. The second chart in Exhibit _____ (BGB-3C) compares the
5 amount of time required to complete repairs for Qwest's retail customers versus
6 unbundled loops provided to competitors. This chart uses only the repair calls where a
7 technician was dispatched.

8
9 **Q. DOES A DIFFERENCE IN AVERAGE INSTALLATION INTERVAL OR**
10 **AVERAGE REPAIR INTERVAL NECESSARILY IMPLY THAT CUSTOMERS**
11 **ARE CAPTIVE TO QWEST'S BUSINESS LOCAL EXCHANGE SERVICE?**

12 A. Not necessarily. Effective competition does not require that service from a competitor be
13 a perfect substitute for Qwest service. However, these data suggest that a customer who
14 chooses service from a competitor can expect to wait [CONFIDENTIAL] to obtain
15 service, if that competitor is using an unbundled loop from Qwest to reach that customer.
16 Not only is the expected interval longer, but an order through a competitor is
17 [CONFIDENTIAL] as likely to be "held for facilities reasons." These held orders
18 require construction work by Qwest and typically result in a delay of weeks rather than
19 days. The longer interval and the greater likelihood of a held order, as well as the slower
20 repair service illustrated in the second chart, are hurdles that any competitor would have
21 to overcome in winning a potential customer.

1 **Q. IS THERE ANY REASON TO BELIEVE THAT QWEST'S PERFORMANCE IN**
2 **PROVISIONING UNBUNDLED LOOPS MAY IMPROVE IN THE NEAR**
3 **FUTURE?**

4 A. One must always be cautious about these things, but I believe there is. One reason to
5 expect better performance is that Qwest agreed in a settlement with Staff in the merger
6 case (UT-991358) to a set of performance standards that include provisioning unbundled
7 loops. If Qwest fails to meet those standards, it must compensate the competitors who
8 receive slow service and it must make up to \$20 million in payments to the state treasury.
9 A second reason is that Qwest is actively pursuing approval for long-distance entry in this
10 state. While a finding of effective competition may not require parity in provisioning,
11 approval of long-distance entry does. It is reasonable to expect (though not certain) that
12 the systems used to order, provision, and repair loops for competitors will improve
13 enough to achieve comparability with Qwest's own retail performance.

14
15 **Q. HOW DOES THE INTRODUCTION OF THE UNE PLATFORM FACTOR INTO**
16 **THE ANALYSIS OF WHETHER QWEST IS SUBJECT TO EFFECTIVE**
17 **COMPETITION?**

18 A. The unbundled network element platform, or UNE-P, is now being offered by Qwest and
19 other incumbent local exchange companies as a result of a recent requirement of the
20 Federal Communications Commission. It would, in theory at least, provide the backstop
21 mechanism by which competitors could compete against Qwest for any business

1 customer in any exchange. UNE-P is in essence a bundled set of unbundled elements; it
2 represents all the network elements needed to provide local exchange service to a
3 customer. It differs from resale in that (1) the price is based on cost rather than on
4 Qwest's retail prices, and (2) access charges are collected by the competitor rather than by
5 Qwest. UNE-P also avoids the need for collocation space in each central office and the
6 expense and delays that collocation entails.

7 However, UNE-P will not be the "magic bullet" for retail pricing flexibility until
8 Qwest is required to reduce its non-recurring charges and systems are firmly established
9 for mechanized ordering, provisioning, and repair of UNE-P facilities. Qwest currently
10 charges a competitor the full non-recurring charge for each network element included in
11 the UNE-P. This results in a charge of over \$200 to switch an existing customer from
12 Qwest retail service to the UNE-P.

13 Market Concentration Analysis

14 **Q. PLEASE EXPLAIN WHY STAFF IS RECOMMENDING THAT THE PETITION**
15 **BE DENIED WITH RESPECT TO BUSINESS LOCAL EXCHANGE SERVICE**
16 **IN AUBURN, ISSAQUAH, KENT, RENTON, AND TACOMA.**

17 **A.** Staff recommends that the WUTC deny the petition unless both the structural factors and
18 the market share data support a finding of effective competition. The structural factors
19 are similar across the nine exchanges, since competitors are operating in each area and
20 have similar access to collocation space and unbundled network elements. However, it is
21

1 not enough to say that competitors *could* serve customers in any particular market; to
2 grant competitive classification, the WUTC must conclude that effective competition
3 *actually* exists in that market. In these five exchanges, the market concentration index
4 values are all above 5,000. The 5,000 value is, as Staff witness Bhattacharya explains,
5 what would obtain in a market with only two competitors, each holding 50 percent of the
6 market. Given the uncertainties about the structural characteristics of this market --
7 particularly questions about competitors' ability to get timely provisioning and repair -- a
8 market concentration index above 5,000 is inconsistent with a conclusion that effective
9 competition exists. Therefore Staff recommends that the petition be denied with respect
10 to these exchanges.

11
12 **Q. HASN'T STAFF RECOMMENDED COMPETITION CLASSIFICATION OF**
13 **SERVICES IN OTHER CASES WHEN THE MARKET CONCENTRATION**
14 **INDEX WAS WELL ABOVE 5,000?**

15 A. Yes. Staff recommended competitive classification of the local toll services of both GTE
16 and U S West when each company had significantly more than half of the relevant
17 market. The market concentration index values would have been substantially above
18 5,000 in each case. This illustrates why the WUTC must always consider both structural
19 factors and market concentration. In the case of local toll services, the structural factors
20 strongly suggested that it was easy for firms to enter and leave the market and for
21 customers to switch among companies. The process for long-distance carriers to get

1 access service had a proven track record with well-known costs and operating systems.
2 Similarly, the process for a customer to change long-distance companies was well
3 established. The structure of the market was sufficiently pro-competitive that even the
4 very high then-current market concentration index values did not disqualify the services
5 from competitive classification.

6 However, in this case, the market structure is much less certain. The mechanisms
7 for competitors to obtain network access and for customers to switch to those competitors
8 are not proven. Therefore, we must look at how many customers have actually switched
9 to a competitive provider. That evidence suggests that only in Seattle, Bellevue,
10 Spokane, and Vancouver is market concentration low enough to warrant competitive
11 classification of Qwest's services, even within the medium- to large-sized business
12 segment.

13
14 **Basis for Recommending Denial of Pricing Flexibility for Small Business Service**

15 **Q. OTHER THAN YOUR CONCLUSION THAT UNBUNDLED ELEMENTS ARE**
16 **NOT A VIABLE METHOD OF GETTING ACCESS AT THIS TIME, ARE**
17 **THERE OTHER FACTORS THAT SUPPORT THE RECOMMENDATION TO**
18 **DENY PRICING FLEXIBILITY FOR SERVICE TO SMALL BUSINESS**
19 **CUSTOMERS?**

20 **A.** Yes, our conclusion that competitors cannot economically and practically reach small
21 business customers is reinforced by the fact that Staff has yet to see any real-world

1 evidence that competitors are actually vying for these customers. Competitors are not yet
2 seeking the business of small business, and Qwest is not being forced to fight for that
3 market segment. One can argue about whether competitors should be pursuing that
4 market, but until they are, those customers remain a significant captive customer base of
5 Qwest.

6
7 **Q. WHY DO YOU CONCLUDE THAT COMPETITORS ARE NOT SEEKING**
8 **SMALL BUSINESS CUSTOMERS?**

9 A. We have examined the business cases of the competitors and reviewed the actual, on-the-
10 ground practices of these firms. Here is what we found about the extent to which
11 competitors are offering service to small business:

12 GST - The GST web site says the company offers service to "medium to large-
13 sized businesses." All of the specific services described in the "Local Telephone
14 Services" section require a T-1 (DS-1) or larger connection.

15 Nextlink - Staff called the telephone number listed for Nextlink in the Spokane
16 telephone directory and stated an interest in getting local service there for two business
17 lines in downtown Spokane. The Nextlink representative said a sales person would have
18 to get back to us, but no one ever returned the call.

19 AT&T/TCG - Staff used AT&T's web site to obtain information on small business
20 local service offered by this firm. The web site says that "Small Business Customers can
21 order services on-line" and has a utility that tells users whether AT&T is offering small

1 business local service in any particular area. Using that utility, we determined that AT&T
2 is not offering service in Seattle, Spokane, Bellevue, or Vancouver.

3 Electric Lightwave - Staff used the inquiry form on Electric Lightwave's web page
4 to ask about getting two business lines in downtown Spokane. A company spokesman
5 called a few days later to say that Electric Lightwave was unable to offer service to
6 customers ordering less than a full T-1 (DS-1) circuit.

7 The real-world responses (or non-responses) of these companies are particularly
8 relevant to the WUTC's determination, because they are among the most active providers
9 of competitive local exchange service in this state. Our interviews with firms that advise
10 businesses on local telephone service confirmed that Qwest faces significant competition
11 for large businesses but very little competition for small businesses. Moreover, this
12 experience is entirely consistent with comments that the WUTC has received from
13 various small business owners who, upon receiving notice of Qwest's petition, called to
14 say they would be very glad to find out about competitors but were aware of no one
15 offering them a choice for local telephone service.

16
17 **Q. WHY DO YOU CONCLUDE THAT QWEST IS NOT HAVING TO FIGHT TO**
18 **RETAIN THE SMALL BUSINESS SEGMENT?**

1 A. This conclusion is based on the observed activities of all firms in the market, particularly
2 on the fact that Qwest has not reduced small business prices in these markets relative to
3 the prices it charges in other, less competitive markets. It is hard to imagine that a firm
4 would let 40 percent of its market switch to competitors without responding by cutting
5 prices. Qwest continues to charge the same price -- \$26.89 per month -- in the
6 purportedly competitive areas that it charges in areas where it has no competition. This is
7 simply not the behavior of a firm that is facing effective competition.

8

9 **Q. IN SOME MARKETS, STAFF IS REPORTING THAT QWEST HAS LOST 40**
10 **PERCENT OF ITS BUSINESS LINES. HOW CAN THOSE STATISTICS BE**
11 **RECONCILED WITH THE CLAIM THAT SMALL BUSINESS IS NOT BEING**
12 **SERVED BY COMPETITORS?**

13 A. Staff has only been able to determine how many *lines* are being served by competitors,
14 not how many *customers* purchase those lines. It is often said that 20 percent of the
15 business customers pay 80 percent of the revenues. I don't know if that particular statistic
16 is true, but I agree that a minority of business customers purchase a majority of the lines.
17 With a skewed distribution of lines across customers, competitors could easily achieve an
18 overall 40 percent market share in an exchange even if it had few or no small business
19 customers.

20

1 **Alternative Recommendation of Classification with Conditions**

2 **Q. ARE THERE ANY ALTERNATIVES TO DENYING THE PETITION WITH**
3 **RESPECT TO BUSINESS CUSTOMERS WHO ARE NOT SERVED BY A DS-1**
4 **OR LARGER CIRCUIT?**

5 A. Yes. As I noted earlier, the key problem with competition in the low end of the business
6 market is that it relies on service using unbundled loops, which are a promising but still
7 unproven source of competition for Qwest's retail service. Since there is some reason to
8 believe that this alternative will become more viable over time, particularly with the
9 development of the UNE-P, the WUTC could consider granting the pricing flexibility for
10 all customer segments with limitations imposed on Qwest's discretion with regard to
11 small business service.

12 The necessary conditions under this approach should be designed to ensure that
13 small business customers are no worse off than they would have been had their service
14 remained in the tariff. These conditions would include:

- 15 1. Qwest may not revise the terms under which it offers service within these
16 wire centers in any way, including any reduction in its obligation to serve;
- 17 2. Qwest must continue to offer all customers the customer service
18 guarantees offered under their consumer bill of rights tariff; and
- 19 3. Qwest may not increase prices or reduce availability, relative to the levels
20 currently in its tariff, of any business local exchange service within these wire centers.

1 These conditions would expire, and Qwest would have unconditioned pricing
2 flexibility of its business local exchange service in these wire centers, upon approval by
3 the Federal Communications Commission of its application to provide long-distance
4 service under Section 271 of the Telecommunications Act of 1996.

5
6 **Q. PLEASE EXPLAIN WHY YOU ARE OFFERING THIS ONLY AS AN**
7 **ALTERNATIVE RECOMMENDATION.**

8 A. As a general matter, I believe it is undesirable for the WUTC to impose any restrictions,
9 beyond those in the statutes, on a grant of competitive classification. The WUTC should
10 generally either grant the pricing flexibility or deny it. However, in this case the WUTC
11 may conclude that circumstances, such as the pending long-distance application, warrant
12 this approach. In any case, I do not think the WUTC should take this approach unless
13 Qwest agrees to it, since it could be seen by Qwest as subjecting it to the worst of both
14 worlds: the WUTC regulation of non-competitive services and the consumer protection
15 act provisions that apply to competitive services. If Qwest believes this is an unworkable
16 approach, Staff would continue to recommend that the petition be denied with respect to
17 customers served by circuits smaller than a DS-1.

18
19 **Q. DOES THIS CONCLUDE YOUR TESTIMONY AT THIS TIME?**

20 A. Yes.

21

Access method	Geographic scope	Customer size requirements	Provisioning issues	Overall assessment
Competitive fiber	Rings cover less than the full wire center. No access for customers off the ring.	None if the customer is in a building connected to a fiber ring. Not economical to connect single-line businesses.	Fiber facilities are expensive and time-consuming to install. Once completed, adding customers is quick and easy.	Too narrowly available to justify competitive classification for an entire wire center.
Qwest special access	Available throughout the wire center.	Cost-effective only for customers with enough demand to justify a DS-1 or larger circuit.	Ordering and provisioning systems are well-established. Orders are more likely to be held or denied than are business exchange orders.	Justifies competitive classification of business exchange service for customers served by DS-1 or larger circuits.
Qwest unbundled loop	Available throughout the wire center, after collocation space is obtained.	None.	Not yet a ready source of access for competitors. Orders for unbundled loops take longer to fill than Qwest retail orders.	Would justify competitive classification for entire wire centers with collocation if it were readily available, but it is not.
Qwest unbundled network element platform	Available throughout the wire center, with no collocation requirements.	Well-suited for mass market/small business segment.	Ordering and provisioning issues unresolved, particularly high non-recurring charges.	Would justify competitive classification if it were readily available, but it is not.
Resale of Qwest retail service	Available throughout the wire center.	None.	Fewer unresolved ordering issues.	Not a price-constraining source of competition.