

# Attachment 9

BEFORE THE MINNESOTA OFFICE OF ADMINISTRATIVE HEARINGS  
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BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION  
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Commissioner  
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Commissioner

In the Matter of a Commission Investigation  
Into Qwest's Compliance with Sec. 272  
of the Telecommunications Act of 1996's  
Separate Affiliate Requirements

MPUC Docket No. P-421/CI-01-1372  
OAH Docket No. 12-2500-14487-2

**AFFIDAVIT OF CORY W. SKLUZAK**

**ON BEHALF OF AT&T**

**REGARDING SECTION 272**

**PUBLIC DOCUMENT –  
TRADE SECRET DATA HAS BEEN EXCISED**

**December 5, 2001**

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1                   **PUBLIC VERSION OF AFFIDAVIT OF CORY W. SKLUZAK**  
2                                           **REGARDING SECTION 272**

3  
4           AT&T Communications of the Midwest, Inc., AT&T Local Services on behalf of TCG  
5 Minnesota, and AT&T Broadband Phone Company of Minnesota, Inc. (collectively "AT&T")  
6 hereby submit this Affidavit of Cory W. Skluzak addressing Qwest Corporation's ("Qwest")  
7 compliance with Section 272 of the Telecommunications Act of 1996.

8                                           **I.     AFFIANT**

9           1.     My name is Cory W. Skluzak. My business address is 1875 Lawrence Street,  
10 Suite 1000, Denver, Colorado 80202.

11          2.     I am employed by AT&T Corp. ("AT&T") as a policy analyst in the Access  
12 Management Group. As such, I provide analysis of various pricing and costing activities of local  
13 exchange carriers ("LEC") for the western region, and provide analysis for a number of subject  
14 matter areas, including revenue and cost analysis functions. I have previously filed testimony,  
15 and/or testified at workshops or hearings, on Section 272 matters, in the Multistate proceeding,  
16 Arizona, Washington, Nebraska, Colorado and Oregon.

17          3.     I have a Bachelor of Science degree in Business Administration with a major in  
18 Accounting from the University of South Dakota in Vermillion, South Dakota. I have a degree  
19 in law from the University of Colorado in Boulder, Colorado. I was formerly licensed as a  
20 certified public accountant in Colorado. I am licensed as an attorney in Colorado, but I do not  
21 currently function in the capacity of an attorney for AT&T.

22          4.     After obtaining my undergraduate degree, I worked several years as a certified  
23 public accountant with the firm of Deloitte, Haskins & Sells conducting financial audits. After  
24 law school, I was a judicial law clerk, an insurance defense litigator and an attorney with the  
25 State of Colorado's Attorney General's office dealing with the State Land Board Commission.

1 From 1995 to the end of 1999, I was an owner and manager of two manufacturing companies  
2 engaged in the manufacture of fiberglass products and the manufacture and marketing of  
3 specialized tools. I began my employment with AT&T in December 1999.

## 4 II. SCOPE OF AFFIDAVIT

5 5. The purpose of this affidavit is to discuss the failure of Qwest Corporation,  
6 formerly U S WEST Communications, Inc., ("Qwest" or "QC"), Qwest Long Distance, Inc.  
7 formerly U S WEST Long Distance, Inc. ("Qwest LD"), and its new Section 272 affiliate, Qwest  
8 Communications Corporation ("QCC"),<sup>1</sup> to meet its burden of establishing that it will operate in  
9 compliance with Section 272 of the Telecommunications Act of 1996 (the "Act") if, and when,  
10 Qwest is granted authorization to provide in-region interLATA services.

11 6. Section 272 of the Act bars Qwest from providing in-region interLATA service  
12 unless it provides such service through an affiliate that meets the separation and  
13 nondiscrimination requirements of this section. The qualifying conditions in Section 272, along  
14 with the 14-point checklist of Section 271, are necessary legal requirements that Qwest must  
15 meet to provide in-region, interLATA telecommunication services. These requirements are  
16 imposed by the 1996 Act and are not simply a charade or obstacle created by its competitors.

17 7. My affidavit focuses on why Qwest, Qwest LD and now QCC fail to comply,  
18 presently and historically, with the structural and transactional safeguards of Section 272(b), (and

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<sup>1</sup> After the merger of Qwest Communications International, Inc. and U S WEST, Inc., the name of U S WEST Long Distance, Inc. was changed to Qwest Long Distance, Inc. It should be noted that, according to Qwest's testimony, Qwest Long Distance, Inc., was to have merged with QCC sometime in June 2001. I was unable to determine from my review, or from the direct testimony filed by Qwest and QCC, whether this merger has yet occurred. The obligations of the Bell Operating Company ("BOC" or "RBOC") and the Section 272 affiliate to comply with the Act commenced the date it was enacted, or February 8, 1996. Therefore, the BOC and the Section 272 affiliates had an obligation to comply with the Act since February 8, 1996, regardless of the number of entities or the name of such entities. Creating a new Section 272 affiliate does not restart the clock on the BOC's obligations or make the issues of past compliance irrelevant.

1 consequently the provisions of Section 272(a)), the nondiscrimination safeguards of Section  
2 272(c) and (e) and the joint marketing restrictions of Section 272(g).<sup>2</sup>

3 8. I conducted on-site reviews, or tests, of affiliated transactions in four phases: the  
4 initial review, a follow-up review, a supplemental review, and a second supplemental review.<sup>3</sup>  
5 This affidavit will summarize the results of these three distinct on-site reviews and describe how  
6 those results are applicable and probative of Qwest's compliance with Section 272.

7 9. The initial on-site review of affiliated transactions between Qwest and the then  
8 existing Section 272 affiliate, Qwest LD, occurred in August 2000 and covered a period ending  
9 in June 2000. The scope and procedures of this review are discussed below in conjunction with a  
10 discussion of Section 272(b)(5) compliance. Qwest created an additional Section 272 affiliate  
11 after the initial on-site review was completed. The information gathered during that initial on-  
12 site review and testing procedures, however, remains viable and probative as a predictive  
13 judgment of the BOC's and Section 272 affiliate's adherence to Section 272.

14 10. In April, 2001, I conducted a follow-up on-site review of affiliated transactions  
15 between Qwest and the former Section 272 affiliate and attempted to review and test such  
16 transactions with the new Section 272 affiliate. This follow-up review generally covered the  
17 period from July 2000 to December 2000. The scope and procedures of this follow-up review  
18 are discussed below in conjunction with a discussion of Section 272(b)(5) compliance.

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<sup>2</sup> During my review of affiliated transactions for the month of July, 2001, I noticed an invoice under the Work Order for Technical Accounting that implied the merger of another affiliate into QCC. **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]** I could find no mention of this significant event in either affidavit. Qwest should be made to come forth with all details surrounding this merger and how the PUC can determine compliance of this entity with the requirements of section 272.

<sup>3</sup> The terms "review" and "test" will be used in this affidavit interchangeably. However, in general, the on-site visits were reviews of accounting details and certain sampling procedures were used to "test" individual billable transactions.

1           11.     In May 2001, I conducted a supplemental on-site review of affiliated transactions  
2 between Qwest and QCC. This review was made necessary by the lack of detail presented the  
3 previous month as to affiliated transactions between Qwest and QCC. This supplemental review  
4 generally covered a period from July 2000 to the present. The scope and procedures of this  
5 supplemental review are discussed below in conjunction with a discussion of Section 272(b)(5)  
6 compliance.

7           12.     During the week of November 25, 2001, I reviewed additional affiliated  
8 transactions between Qwest and QCC for the time period of May through October 2001. This  
9 review was made to refresh the previous testing. Although the same conventions used for the  
10 previous reviews were followed, only QCC's expenses were reviewed and fewer selections were  
11 made due to time constraints.

12  
13           13.     Based on the results of these reviews, I refute statements made in the affidavits of  
14 the QCC witness, Judith Brunsting, and of the Qwest witness, Marie Schwartz, who state that  
15 QCC and Qwest currently comply, and/or prospectively will comply, with Section 272 and the  
16 Federal Communication Commission's ("FCC") implementing orders.

17  
18           14.     AT&T is not the only entity to dispute Qwest's assertions of compliance with this  
19 section. The most recent state order, dated November 14, 2001, pertaining to Qwest's  
20 compliance with section 272 was that of the Washington administrative law judge ("ALJ")  
21 dealing with such matters. The ALJ found Qwest not in compliance with section 272  
22 requirements, and listed specific areas of concern, including the "transition period" transactions

1 between Qwest and QCC, Qwest's compliance with GAAP and the adequacy of Qwest's Internet  
2 Website postings.<sup>4</sup>

3  
4 **III. PURPOSE OF SECTION 272 AND THE ROLE OF THE MINNESOTA PUBLIC**  
5 **UTILITIES COMMISSION**

6 **A. The Purpose of Section 272**

7 15. Through a variety of accounting and non-accounting safeguards, Section 272  
8 attempts to prevent a BOC from discriminating against its competitors and in favor of its long-  
9 distance affiliate, and to prevent a BOC from subsidizing its affiliate by recovering the affiliate's  
10 costs through the BOC's local and exchange access service customers.

11 16. Section 272 demands that Qwest treat its competitors as it treats its Section 272  
12 affiliate. It provides a scheme, through the various safeguards, for the competition to evaluate  
13 whether a goal of this section -- to insure a level playing field for all competitors -- is fulfilled.<sup>5</sup>

14 17. Compliance with these safeguards is "*of crucial importance*" to protect consumers  
15 of Qwest from paying higher prices for local service because of improper cross-subsidization of  
16 QCC. Compliance is equally important to protect the competitive process in the interLATA  
17 market from Qwest's ability to leverage its market power over local services into the long  
18 distance market. Section 272 is not an afterthought. The FCC has stated that its "findings  
19 regarding Section 272 compliance constitute independent grounds for denying an application  
20 [filed under 271]."<sup>6</sup>

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<sup>4</sup> *In the Matter of the Investigation Into US WEST Communications, Inc.'s Compliance with Section 271 of the Telecommunications Act of 1996*, Docket Nos. UT-003022 & 003040, Washington Utilities and Transportation Commission, Twentieth Supplemental Order (Workshop Four): Checklist Item No. 4; Emerging Services, General Terms and Conditions, Public Interest, Track A, and Section 272, November 14, 2001. ("WA ALJ's 272 Order").

<sup>5</sup> *Application by Bell Atlantic New York for Authorization Under Section 271 of the Communications Act to Provide In-Region, InterLATA Service in the State of New York*, CC Docket No. 99-295, Memorandum Opinion and Order, FCC 99-404, (Rel. Dec. 22, 1999), ¶ 402 ("Bell Atlantic New York Order").

<sup>6</sup> *Id.*

1           18.     In the *Ameritech Michigan Order*, the FCC ruled that BOCs bear the burden of  
2 proof under Section 271(d)(3) to establish that they will operate in compliance with Section 272  
3 if granted interLATA authority.<sup>7</sup> “Paper promises do not, and cannot, satisfy a BOC's burden of  
4 proof.”<sup>8</sup> This admonition regarding “paper promises” is particularly relevant to Qwest given its,  
5 and U S WEST’s, history with regard to sections 271 and 272. The requirement that Qwest  
6 come forward with specific, tangible evidence is especially appropriate in the context of Section  
7 272 compliance, because most of the evidence relevant to such a determination lies exclusively  
8 in the hands of Qwest and QCC.

9     **B.     The Role of the Minnesota PUC**

10           19.     Review of Section 272 compliance is relevant in state proceedings because  
11 Qwest’s compliance with Section 272 is required in order for Qwest to satisfy the requirements  
12 of Section 271. Furthermore, documentation of such compliance will contribute to the detailed  
13 and extensive record the FCC will rely upon when reviewing Qwest’s Section 271 application.

14           20.     To the extent possible based on the state’s procedural schedule, the FCC has  
15 stated that a state proceeding is a proper forum to develop an evidentiary record with the  
16 opportunity to cross-examine the witness.<sup>9</sup> Additionally, the FCC has only 90 days from the date  
17 of filing to review an RBOC’s Section 271 application before rendering its decision.  
18 Consequently, the FCC requires applications to be complete when filed and has stated that, “[w]e  
19 will consider carefully state determinations of fact that are supported by a detailed and extensive

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<sup>7</sup> *Application of Ameritech Michigan Pursuant To Section 271 of the Communications Act of 1934, as amended, To Provide In-Region, InterLATA Services in Michigan*, CC Docket No. 97-137, Memorandum Opinion and Order, FCC 97-298 (Rel. Aug. 19, 1997), ¶¶ 43, 371 (“*Ameritech Michigan Order*”).

<sup>8</sup> *Id.*, ¶ 55.

<sup>9</sup> The FCC stated the following in the *BellSouth South Carolina Order*: “...we emphasize that parties should make every effort to present their views to the state commission in the first instance, where such views can be adequately addressed by other interested parties and subjected to cross-examination.” *Application of BellSouth Corporation, et al. Pursuant To Section 271 of the Communications Act of 1934, as amended, To Provide In-Region, InterLATA Services in South Carolina*, CC Docket No. 97-208, Memorandum Opinion and Order, FCC 97-418 (Rel. Dec. 24,

1 record, and believe the development of such a record to be of great importance to our review of  
2 Section 271 applications.”<sup>10</sup>

3 21. Thus, to facilitate the FCC’s review of Qwest’s Section 271 application, it is in  
4 Qwest’s best interest to demonstrate compliance with Section 272 requirements in the state  
5 record with substantive evidence, because the FCC will rely upon such a detailed record in  
6 assessing whether an RBOC has met the “preponderance of evidence” standard.<sup>11</sup>

7 22. The goal of the PUC relative to Section 272 should be to hold Qwest to its burden  
8 of proving compliance through actual support of its claims. For example, the PUC should be  
9 concerned about the effects of unfettered joint marketing between Qwest and QCC, given past  
10 violations of Section 271 by U S WEST, Qwest and Qwest LD. If the PUC shares these  
11 concerns, it should make them known to the FCC and provide recommendations to mitigate  
12 them.

13 23. Additionally, under the Act, the PUC plays an integral role in overseeing QCC,  
14 through efforts such as participating in the joint Federal/State audit required by Section 272(d) to  
15 determine compliance with accounting and non-accounting safeguards, without regard to the  
16 concept of materiality.

17 24. QCC acknowledges that the FCC’s review regarding Section 272 requires a  
18 predictive judgment regarding the future behavior of the BOC.<sup>12</sup> This predictive judgment is  
19 based on past and present practices.<sup>13</sup> This sets the stage for a broad review by the PUC.

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1997), ¶ 27 (*emphasis added*) (“*BellSouth South Carolina Order*”).

<sup>10</sup> *Ameritech Michigan Order*, ¶ 30.

<sup>11</sup> *Id.*, ¶¶ 45 - 46.

<sup>12</sup> *Brunsting Affidavit* at 3, n. 3.

<sup>13</sup> *Application of BellSouth Corporation, BellSouth Telecommunications, Inc., and BellSouth Long Distance, Inc., for Provision of In-Region, InterLATA Services in Louisiana*, CC Docket No. 98-121, Memorandum Opinion and Order, FCC 98-271 (Rel. Oct. 13, 1998), ¶ 321 (“*BellSouth Louisiana II Order*”).

1           25.     Although Qwest acknowledges the propriety of a review of “past practices,” that  
2 acknowledgement is undercut by QCC’s statement that it need “only demonstrate that it will  
3 comply with the requirements of Section 272.”<sup>14</sup> Given the past and present history of Qwest,  
4 QCC and Qwest LD in failing to comply with Section 272 and in violating Section 271, it is  
5 understandable why Qwest and QCC wish to divert the PUC’s attention from the past and  
6 present to its future “paper promises”. The PUC will look in vain in the affidavits filed by Qwest  
7 and QCC for the past practices I discuss in this affidavit. These include: the former U S WEST’s  
8 and Qwest’s several past violations of Section 271 as found by the FCC; the failure to post  
9 transactions to its separate affiliate website; the failure to maintain separations between its  
10 employees, officers and directors; and the failure to prevent discrimination in services provided  
11 to Qwest/U S WEST LD and now QCC.

12           26.     The FCC has stated that “the past and present behavior of the BOC applicant” is  
13 “highly relevant” because such behavior provides “the *best* indicator of whether [the applicant]  
14 will carry out the requested authorization in compliance with the requirements of Section 272.”  
15 (emphasis added)<sup>15</sup> Thus, the FCC will examine both Qwest’s “paper promises” of asserted  
16 compliance with Section 272 and evidence presented of Qwest’s noncompliance with section  
17 272 safeguards as indicators of its future behavior.<sup>16</sup>

18           27.     The Minnesota PUC also retains the authority to impose and subsequently enforce  
19 any requirements or mechanisms relating to Qwest’s and QCC’s provision of intrastate  
20 interLATA service.<sup>17</sup> Thus, this PUC may condition or delay Qwest’s entry into intrastate  
21 interLATA service.

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<sup>14</sup> Brunsting Affidavit at 2 - 3.

<sup>15</sup> *BellSouth Louisiana II Order*, ¶ 321.

<sup>16</sup> *Id.*

<sup>17</sup> *Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934*,



- 1 e. Prove compliance with the FCC's accounting principles as required under Section  
2 272(c)(2).
- 3 f. Prove adequate compliance with, and evidentiary support for, the fulfillment  
4 requirements of Section 272(e).
- 5 g. Provide sufficient detail to determine future compliance with Section 272(g)  
6 concerning joint marketing, especially given its past history of violation.
- 7

8 **V. STRUCTURAL, TRANSACTIONAL, AND ACCOUNTING REQUIREMENTS**  
9 **OF SECTION 272**

10 30. Section 272 of the Act contains accounting and non-accounting safeguards  
11 intended to ensure that the BOCs do not use their monopoly power in local exchange services to  
12 discriminate in favor of their Section 272 affiliate, and to discourage and detect improper  
13 transactions between the BOC and the Section 272 affiliate. In its *Ameritech Michigan Order*,  
14 the FCC confirmed that the obligations and restrictions under Section 272 were of "crucial  
15 importance,"<sup>19</sup> and that the BOCs and their Section 272 affiliates have been required to comply  
16 with those obligations and restrictions since the date the 1996 Act was passed on February 8,  
17 1996.<sup>20</sup>

18 **A. Section 272(a) – Separate Affiliate**

19 31. To comply with this section, it is not enough to simply state that a separate 272  
20 affiliate has been established. The FCC has stated that a BOC, to comply with section 272(a)  
21 must meet the requirements of section 272(b)(5), and may not provide certain services, including  
22 the origination of certain interLATA services, except through a structurally separate affiliate.<sup>21</sup>

<sup>19</sup> *Ameritech Michigan Order*, ¶ 346.

<sup>20</sup> *Id.*, ¶ 371.

<sup>21</sup> See *BellSouth Louisiana II Order*, ¶ 323, where the FCC used this process to find that BellSouth did not satisfy Section 272(a).

1           32.     In its discussion regarding compliance with Section 272(a), Qwest states that it  
2     “will not provide in-region interLATA services originating within the BOC 14-state region as  
3     long as the structural separation obligation of Section 272 applies to this activity.”<sup>22</sup> It should be  
4     noted that Qwest had been providing such in-region interLATA services for a number of years,  
5     and these activities were found by the FCC to have violated Section 271.<sup>23</sup> The PUC should  
6     review assurances made by Qwest and QCC cautiously.

7           33.     Others who have reviewed Qwest records have expressed concerns similar to  
8     those AT&T raises here. A third-party audit commissioned by Qwest, for example, has made  
9     note of transactions that fail to comply with the requirements of Section 271.<sup>24</sup> The  
10    transactions in question involve infeasible rights of use (IRUs). Qwest’s scheme has its  
11    corporate customers purchasing an IRU, Qwest would then transport the in-region interLATA  
12    calls on that IRU to an out of region point of presence (“POP”) and then transport those calls in  
13    an apparent circumvention of the requirements of Section 271.

14          34.     These and other Qwest current and past practices raise substantial questions about  
15    Qwest’s current and future willingness to comply with the requirements of Section 271, much  
16    less Section 272.

17  
18    **B. Section 272(b)(2) – Books, Records and Accounts**

19          35.     The FCC has interpreted this section to require the BOC’s Section 272 affiliate to  
20    maintain its books, records and accounts pursuant to Generally Accepted Accounting Principles

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<sup>22</sup> Affidavit of Marie Schwartz dated October 1, 2001 (“Schwartz Affidavit”) at 9.

<sup>23</sup> For example, see *AT&T Corp. v. U S WEST Communications, Inc.*, File No. E-97-28, Memorandum Opinion and Order, DA01-418 (Rel. Feb. 16, 2001), for the most recent violation of Section 271.

<sup>24</sup> Letter from Arthur Andersen LLP to Dorothy Atwood (June 6, 2001) and filed with the FCC’s Common Carrier Bureau (discussing audit of Qwest’s required divestiture of its in-region interLATA services and pursuant to CC Docket No. 99-272). This letter is further discussed in this testimony in the section entitled “Past History and Future Violations”.

1 (“GAAP”) and maintain them separate from the BOC.<sup>25</sup> To determine compliance with this  
2 section the FCC has looked to such evidence as: different charts of accounts, use of separate  
3 accounting software maintained at a separate location and a regular audit program for the  
4 affiliate that ensures GAAP compliance.<sup>26</sup>

5 36. QCC asserts that its “books, records, and accounts are maintained in accordance  
6 with generally accepted accounting principles (“GAAP”) and consolidated into Qwest  
7 Communications International Inc.’s financials.”<sup>27</sup> AT&T disputes this assertion of GAAP  
8 compliance.

9 37. Based upon my initial and follow-up on-site reviews Qwest, Qwest LD and QCC  
10 have not demonstrated that they have been complying, or will comply, with this section for the  
11 following reasons:

12 a. Qwest LD, which will or has become part of QCC, had not accounted for  
13 activity as incurred nor had it accrued expenses from year to year. During  
14 my initial on-site review, which is discussed more fully below, I found  
15 numerous examples of transactions occurring in 1999 that were not  
16 expensed until the year 2000. One of the transactions was for \$1,640,580  
17 for work performed by Qwest Consumer Services for Qwest LD from  
18 January through December, 1999, yet this amount was not recognized as  
19 an expense until it was paid in January, 2000.<sup>28</sup> Qwest states that it  
20 “utilizes accrual accounting for its transactions between affiliates.”<sup>29</sup> But  
21 Qwest LD is not using accrual accounting based on the selections that I  
22 tested and evidenced by the debit hitting an expense account, nor is it  
23 timely accounting for transactions between affiliates or following the  
24 accounting concept of matching expenses with revenues.

25 b. The only transactions between Qwest and Qwest LD that are accounted  
26 for as “affiliate transactions” are those involving payments.<sup>30</sup> There is a

<sup>25</sup> *BellSouth Louisiana II Order*, ¶ 328.

<sup>26</sup> *Id.*

<sup>27</sup> Brunsting Affidavit at 10.

<sup>28</sup> Qwest’s Section 272 affiliate website: [http://www.uswest.com/about/policy/docs/ld\\_1999\\_transactions.html](http://www.uswest.com/about/policy/docs/ld_1999_transactions.html). Note that since the initial write-up of this statement, Qwest has removed from its Section 272 website the specific reference to this amount which was contained within a posted summary entitled “1999 Services Provided by U S WEST to U S WEST Long Distance”.

<sup>29</sup> Qwest Response to AT&T Multistate Data Request No. 56.

<sup>30</sup> Qwest Response to AT&T Multistate Data Request No. 17. “The procedures for capturing affiliate transactions

1 concern that transactions not involving the exchange of money could  
2 occur and not be accounted for and reported.

3 c. According to testimony filed by QCC, its accounting and finance  
4 functions are performed by the Services Company, which is not the BOC,  
5 but is the parent of both the BOC and the 272 affiliates.<sup>31</sup> QCC also states  
6 that "BOC employees provide payroll services".<sup>32</sup> Confusing the issue, as  
7 discussed below in further on-site testing, is the existence of work orders  
8 *and* task orders indicating that QCC is both paying for and receiving  
9 payment for finance services. The PUC is urged to inquire into this matter  
10 and clear up the contradictory testimony presented by Qwest and QCC.

11 d. To determine compliance with this section, Qwest LD must be auditable.  
12 Under Section 272(d), an audit of the Section 272 affiliate is not mandated  
13 until twelve months after Section 271 approval. Given Qwest LD's  
14 present and historical failure to fully account for and disclose its required  
15 transactions, it is suggested that an opening examination should be  
16 required to verify that all accounting safeguards are in place and  
17 operational prior to Qwest LD's/QCC's provision of long distance service.

18 e. Qwest engaged Arthur Andersen to review and "supplement" processes for  
19 affiliate transactions,<sup>33</sup> and audits for 10-K's (which include QCC).<sup>34</sup>  
20 However, the "audit" of affiliate transactions is limited in scope to one line on  
21 the ARMIS reports and, as will be discussed below, Qwest's ARMIS report  
22 submissions for affiliated transactions are of dubious value. Finally, as is  
23 discussed below, it appears that no audit has been performed on Qwest's  
24 ARMIS reports for 2000 as it has opted to audit that year and 2001 sometime  
25 in 2002.

26 38. Even with respect to the records I reviewed as part of my supplemental reviews,  
27 Qwest and QCC are not utilizing GAAP required accrual accounting, or timely billing and  
28 accounting for their affiliated billable transactions. I initially discovered this problem during the  
29 review of Qwest LD's actual accounting documentation, and I continued to encounter this  
30 problem during subsequent on-site reviews. Further, Qwest and QCC are not GAAP compliant  
31 where they have completely failed to book billable transactions between them for a nine-month  
32 period beginning July 2000, until the latter half of April 2001.

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include downloading all payments to and payments from affiliates from the company's financial systems."

<sup>31</sup> Brunsting Affidavit at 12. However, QSC is the parent of both QC and QCC.

<sup>32</sup> *Id.*, at 14 - 15.

<sup>33</sup> Schwartz Affidavit at 20.

1           39.     Qwest asserts, as additional evidence of compliance with Section 272(b)(2), that  
2 “[a]nnual reports are filed publicly via the FCC’s Automatic Reporting and Management  
3 Information Systems (“ARMIS”) [which] are accompanied by the report of independent  
4 accountants, Arthur Andersen ....”<sup>35</sup> This assertion appears to cast a veil of legitimacy, as the  
5 inferential logic is that Arthur Andersen has reviewed the ARMIS reports which proves GAAP  
6 compliance. However, as Ms. Schwartz explains in a footnote to her testimony, “... the audit  
7 engagement [regarding the annual ARMIS reports] for the year 2000 will be combined with 2001  
8 and the report will be issued in 2002.”<sup>36</sup> As the footnote to Ms. Schwartz’s textual assertion of  
9 “additional evidence” appears to be contradictory, the Arthur Anderson report (or lack of report)  
10 can be given no probative value. It is noted that Qwest’s ARMIS reports will not be audited for  
11 the initial one and one-half years since it acquired US WEST; until some time in the year 2002.

12           40.     I reviewed the ARMIS report for Qwest for the year 2000; the most recent report  
13 posted by the FCC.<sup>37</sup> For services purchased by Qwest from QCC, I did not see an amount or a  
14 line entry. The absence of any information, or any dollar amount, should be of concern. With no  
15 amounts being reported, no probative value can be placed on Qwest’s assertion that its ARMIS  
16 reports are audited. Another ramification is that Qwest failed to report affiliated transactions for  
17 2000. The PUC should question Qwest as to this situation and whether Qwest has also failed to  
18 report Qwest LD’s affiliated transactions correctly.

19           41.     For services sold by Qwest to QCC, a total of \$1,545,000 has been entered.  
20 These amounts do not reconcile to the total amounts that I discovered during my supplemental  
21 on-site testing. For affiliated transactions between Qwest and QCC, it appears that a single

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<sup>34</sup> Brunsting Affidavit at 10.

<sup>35</sup> Schwartz Affidavit at 14.

<sup>36</sup> *Id.*, at 14, n. 10.

<sup>37</sup> FCC’s ARMIS website, Report 43-02, Table 12 “Analysis of Services Purchased from or Sold to Affiliates.”

1 amount of services sold by Qwest to QCC is all that Arthur Anderson had the opportunity to  
2 review. Such would not afford an opportunity to review the transactions making up that total  
3 ARMIS amount.<sup>38</sup>

4 42. As Qwest has not filed any ARMIS report for 2001, no probative value can be  
5 given to Qwest's assertions regarding ARMIS reports and its new Section 272 affiliate.

6 43. QCC asserts, as further evidence of compliance with this section, that its financial  
7 results are consolidated with those of QCI's financial statements included in the SEC Form 10-  
8 K, which includes Arthur Andersen's unqualified opinion as to adherence to accounting  
9 principles.<sup>39</sup> Once again, given the complete failure to account for affiliated transactions between  
10 Qwest and QCC, the seeming legitimacy of an Arthur Andersen "unqualified" opinion as to QCI  
11 should not be deemed probative of QCC's financial activities. Further, QCC's parent company,  
12 QSC, is not directly audited either. Indeed the audit of QCI may not have included any affiliated  
13 transactions between Qwest and Qwest LD.

14 44. QCC states that QCI is subject to federal securities statutes.<sup>40</sup> QCI, however,  
15 recently filed the company's Form 10Q (for the three months ended March 31, 2001) which  
16 completely omits any accounting of affiliated transactions with QCC.<sup>41</sup> QCC's affiliated  
17 transactions with Qwest could not have been correctly reported in the 10-K, 10-Q or the ARMIS  
18 report, as no billable transactions for the period July 2000 through March 2001 were accounted  
19 for in that period. Thus, when QCC states that QCI's financial statements in the 10-K form

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<sup>38</sup> Qwest states that Arthur Andersen was engaged to supplement the internal affiliate transaction processes during the transition from Qwest Long Distance to QCC and that over 140 interviews were conducted to ensure that all transactions had been identified. Schwartz Affidavit at 15. Given the extent of Arthur Andersen's involvement and the addition of supplemental procedures, Qwest has yet to explain, much less justify, its complete failure to book billable affiliated transactions with QCC spanning a nine-month period and straddling two financial years.

<sup>39</sup> Brunsting Affidavit at 10.

<sup>40</sup> *Id.*

<sup>41</sup> See, <http://www.qwest.com/cgi-bin/ir/secFilings.cgi?script=irSECFilings>, for a listing of recent SEC documents

1 include the “consolidated results of the 272 Affiliate” it must be underscored that this does not  
 2 include affiliated transactions.

3 **C. Section 272(b)(3) – Separate Officers, Directors and Employees**

4 45. Section 272(b)(3) requires that QCC have “separate officers, directors, and  
 5 employees from the [BOC] of which it is an affiliate.” In prior orders, the FCC used as evidence  
 6 of compliance the names of officers and directors submitted by the BOC and affiliates, and  
 7 whether separate payrolls and administrative operating systems are present.<sup>42</sup> In its *Ameritech*  
 8 *Michigan Order*, the FCC found that that the intent of the separate officers and directors  
 9 requirement is “that there be some form of independent management and control of the two  
 10 entities”.<sup>43</sup> In that order, the FCC was concerned about the fact that the presidents of both the  
 11 BOC and the separate 272 affiliate reported to the same officer of the parent corporation of both  
 12 entities.

13 46. Qwest’s position is that it need only prove that its officers, directors and  
 14 employees are separate from those of QCC.<sup>44</sup> However, this begs the question of what is meant  
 15 by “separate”. Assistance can be found in the audit procedures of the section 272(d) biennial  
 16 audit. Audit procedures are used to test for separate officers, directors and employees and  
 17 require the auditor to do the following:

18 Obtain the functional organizational chart of each Section 272 affiliate ...  
 19 and inspect it to determine whether any departments report either  
 20 *functionally or administratively (directly or indirectly)* to an officer of the  
 21 BOC.<sup>45</sup>

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filed by QCI.

<sup>42</sup> *BellSouth Louisiana II Order*, ¶ 330, n. 1032.

<sup>43</sup> *Ameritech Michigan Order*, ¶ 360.

<sup>44</sup> Brunsting Affidavit at 17.

<sup>45</sup> See *General Standard Procedures For Biennial Audits Required Under Section 272 of the Communications Act of 1934, As Amended, as of December 16, 1998*. (“*Biennial Audit Procedures*”) at Objective III, Procedure 3 (emphasis added). Also see, Schwartz Affidavit, Exhibit Qwest/537, p. 25.

1 The PUC should determine how Qwest employees are “functioning” rather than solely  
 2 focusing on administrative separation via which employees are on which payroll. The  
 3 quoted language above dictates that a BOC should not be allowed to ignore substance  
 4 with form.

5 47. In addition, the *Biennial Audit Procedures* require an independent auditor to  
 6 perform the following tests:

7 Obtain a list of officers and employees who transferred from the BOC at  
 8 any time to each Section 272 affiliate, and ... determine whether the  
 9 company’s internal controls ... have been implemented. Also, interview  
 10 these employees to determine whether they used any proprietary  
 11 information (e.g., customer proprietary network information (CPNI),  
 12 Network Planning Manuals, Plant Traffic Practices, Operation, Installation  
 13 and Maintenance (OI&M) Practices) obtained while they were employees  
 14 of the BOC or whether any of the above information is made available to  
 15 them through friends and acquaintances still employed by the BOC.<sup>46</sup>

16 Obtain a list of all employees of each Section 272 affiliate since February  
 17 8, 1996, the date of the Act [and] ... inspect company’s files which  
 18 indicate employee’s employment history within the BOC family of  
 19 companies and document whether they were employees of the BOC or any  
 20 of its affiliates at any time. Also, document number of employees,  
 21 number of times, and dates each employee transferred back and forth  
 22 between the BOC or any other affiliate and the Section 272 affiliate since  
 23 February 8, 1996.<sup>47</sup>

24 48. Based upon my initial and follow-up on-site reviews, I noted the following  
 25 deficiencies of Qwest, Qwest LD and QCC with respect to this section:

26 a. In September 2000, Qwest LD’s President, Ms. Kamelia J. Davidson, who  
 27 was also Qwest LD’s sole director, reported directly to an officer of Qwest  
 28 Inc., Drake Tempest. Mr. Tempest was the Executive Vice President,  
 29 General Counsel, Chief Administrative Officer and Secretary of Qwest,  
 30 Inc. As both Qwest LD and Qwest are wholly-owned subsidiaries of  
 31 Qwest Inc., there was a situation analogous to the one described above in  
 32 the *Ameritech Michigan Order*. The FCC’s concern in *Ameritech* was that  
 33 the presidents of the BOC and the 272 affiliate were reporting to the same

<sup>46</sup> See *Biennial Audit Procedures*, Objective III, Procedure 5. Also see, Schwartz Affidavit, Exhibit 272.14, p. 25.

<sup>47</sup> *Id.* at Objective III, Procedure 6 at 25.

1 officer of the *parent corporation*. Drake Tempest and Robin Szeliga are  
 2 now the current directors of QCC and they are no longer a director or  
 3 officer of Qwest.<sup>48</sup> However, I am unsure to whom Mr. Tempest reports  
 4 to at Qwest Services Corp. Mr. Tempest is also Executive Vice President,  
 5 General Counsel, Chief Administrative Officer and Secretary of QCC.<sup>49</sup>  
 6 Mr. Tempest also holds the position of Executive Vice President, General  
 7 Counsel and Chief Administrative Officer of Qwest Communications  
 8 International, Inc., (QCI) the parent of both Qwest and QCC. Similarly,  
 9 Mr. Joseph Nacchio is Chairman, Chief Executive Officer and President of  
 10 QCC and Chairman and Chief Executive Officer of Qwest  
 11 Communications International, Inc. No information on the officers and  
 12 directors of Qwest Service Corporation ("QSC") the parent of Qwest and  
 13 QCC was provided.<sup>50</sup> QSC is, in turn, owned by Qwest Communications  
 14 International, Inc.<sup>51</sup>

- 15 b. The concern for true independence between Qwest and QCC is  
 16 heightened, as Mr. Tempest is also the General Counsel of QCC and  
 17 Qwest Communications International, Inc. As an attorney, it is  
 18 foreseeable that Mr. Tempest may invoke the attorney-client privilege  
 19 should a question arise as to issues regarding QCC or Qwest.
- 20 c. QCC and Qwest employees will have an incentive to engage in "off-the-  
 21 record" transactions, which will be especially difficult to identify and  
 22 evaluate through any internal or external audit.
- 23 d. QCC employees formerly employed by Qwest have an incentive to take  
 24 with them, and use, Qwest proprietary information without accounting for  
 25 this acquisition of information and without offering this information to  
 26 competitors.
- 27 e. The converse of the above would also be present. During my initial on-  
 28 site review of some of Qwest LD's financial records, I noted several  
 29 transactions pertaining to bonuses or "team awards" paid to former  
 30 employees of Qwest LD that had since been rehired by Qwest. I could not  
 31 determine the names or even the number of employees, as this information  
 32 had been blacked out for my review. The use of the word "rehired"  
 33 connotes that these employees were once employed at Qwest (or  
 34 U S WEST), went to the LD affiliate and then returned to Qwest. After  
 35 returning to Qwest the employees received "Team Awards." The choice  
 36 by Qwest to black out this information raises an appearance of  
 37 impropriety. I reviewed terminated Work Order RMLD099 on Qwest  
 38 LD's website called "Go For The Gold/Bold Goal". This is a program

<sup>48</sup> Brunsting Affidavit, Exhibit JLB-272.7.

<sup>49</sup> *Id.*

<sup>50</sup> The characterization of QSC as a shared services affiliate that provides services to the BOC and QCC is misleading where it is the parent company of both the BOC and the 272 affiliate.

<sup>51</sup> Brunsting Affidavit, Exhibit 272.3.

1 from USWC/Qwest that rewards employees for customer referrals and  
2 cost saving ideas. USWLD employees were allowed to participate in this  
3 program.

4 f. The incidence of employee migration is not isolated to the periods that I  
5 observed. Results from prior AT&T on-site reviews noted that numerous  
6 employees resigned from the LD affiliate to become employees at the then  
7 U S WEST. In 1997 alone, 22 employees transferred. Since Qwest LD  
8 had an approximate average of 93 employees, that means that *over 23%* of  
9 the employees of Qwest LD were rehired by Qwest.

10 g. The free-flow movement of employees between Qwest and Qwest LD is  
11 of concern in that proprietary information is also flowing back and forth  
12 between the companies. Indeed, as was stated above, the independent  
13 auditor is required to document this type of migration.

14 49. The Qwest witness states that she oversaw a comparison of payroll registers.<sup>52</sup> It  
15 is unknown if Ms Schwartz personally compared the payroll registers, if she simply reviewed the  
16 work product of other personnel, or if she is attesting to another's work product without any  
17 personal involvement. Nor does she state if she compared social security numbers as required by  
18 the biennial audit procedures.

19 50. QCC states that Qwest employees "provide payroll services" to it.<sup>53</sup> Thus, these  
20 two entities do not have separate payroll administration, which the FCC looks to as evidence of  
21 compliance with this section.

22 51. As part of my supplemental review, I scanned QCI's Form 10-Q (for the first  
23 quarter, 2001) which is available on QCI's public web site. I noted that Robin Szeliga,  
24 Executive Vice President and Chief Financial Officer of QCI signed the Form 10-Q. I discuss  
25 elsewhere in this affidavit that Ms. Szeliga had signed the FCC-required certification statements  
26 for both QCC and Qwest in her capacity as a Senior Vice President of Qwest. As the  
27 certification statement is to be signed by an officer of the corporation, by signing both

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<sup>52</sup> Schwartz Affidavit at 16.

1 certifications, the implication is that Ms. Szeliga was an officer of both Qwest and ACC, as well  
2 as an executive officer for QCI, which is the parent of both Qwest and QCC.<sup>54</sup> Per additional  
3 data requests, Ms. Szeliga is also Executive Vice President and Chief Financial Officer of QCC  
4 and of Qwest Long Distance.<sup>55</sup> These additional titles, as well as Ms. Szeliga's status as one of  
5 the two directors of QCC, are confirmed by QCC's affidavit.<sup>56</sup> In summary, it appears that Ms.  
6 Szeliga is presently, or has been involved with QCC, Qwest Long Distance, Qwest and QCI as a  
7 director, officer and employee. Ms. Szeliga is wearing many hats and such is a violation of the  
8 FCC's dictate that there be some form of independent management and control as to Qwest and  
9 QCC.<sup>57</sup>

10       52. My supplemental on-site review revealed a widespread pattern of "employee  
11 sharing", or "employee lending". As was previously discussed, Qwest and QCC employees may  
12 be "separated" in form by which entity cuts them a payroll check, but to the extent that the  
13 employees are primarily devoted to working at the other entity, there is not *functional*  
14 *separation*. This is why simply checking payroll lists is an inadequate indication of employee  
15 separation. It is AT&T's position that where a Qwest employee is dedicated primarily to QCC  
16 that employee is functionally not a separate employee, and this practice is utilized by Qwest to  
17 circumvent the FCC's "shared employees" rules.

18       53. An overarching issue is whether safeguards are sufficient to prohibit information  
19 flows between Qwest and QCC. Qwest has failed to demonstrate that existing controls could

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<sup>53</sup> Brunsting Affidavit at 15.

<sup>54</sup> If Ms. Szeliga was not an officer of both corporations, this would be a violation of the requirement that the certification be signed by an officer of the corporation.

<sup>55</sup> Response to AT&T Multistate Data Request No. 107, Exhibit A. Note that there are two "Exhibit A's" filed by Qwest and this is the second Exhibit A (Directors and Officers Lists).

<sup>56</sup> Brunsting Affidavit, Exs. JLB-272.7.

<sup>57</sup> After AT&T brought this situation to Qwest's attention in the multistate proceeding, Qwest moved to address the situation. See, Schwartz Affidavit at 24.

1 possibly prohibit information flow given the rampant practice of “employee sharing or  
2 borrowing”.

3 54. From my supplemental review, I noted deficiencies with respect to Section  
4 272(b)(3) and I list them as follows:

5 a. **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED].**  
6 The logical inference is that the specifically mentioned employees are now  
7 with QCC. This is a further continuation of the free flow of employees  
8 between the BOC and the 272 affiliate. The employees of these two  
9 entities are hopelessly intertwined. QCC employees formerly employed by  
10 Qwest have an incentive to take with them, and use, Qwest proprietary  
11 information without accounting for this acquisition of information and  
12 without offering this information to competitors.

13  
14 **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]**  
15 b. This type of employee sharing arrangement skirts the requirements  
16 of Section 272(b)(3) that QCC have employees separate from  
17 Qwest. Once again, Qwest retains the “form” but in functional  
18 substance there is no separation. QCC and Qwest employees will  
19 have an incentive to engage in “off-the-record” transactions, which  
20 will be especially difficult to identify and evaluate through any  
21 internal or external audit.

22 **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]**  
23 c. To the extent that the intent of Section 272(b)(3) is that there be some  
24 form of independent management and control as between Qwest and  
25 QCC, this selection represents another violation.

26 **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]**  
27 d. This is another example of the policy of “employee sharing” and the  
28 functional intertwining of the two entities’ employees.

29 **PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]**  
30 e. Per QCC’s Affidavit, Exhibit JLB-272.7, Mr. Nacchio is QCC’s  
31 Chairman, CEO and President. The FCC’s intent for this section is that  
32 there be independent management and control as to the BOC and the 272  
33 affiliate. Given this invoice, it appears that there is not independent  
34 management and control between Qwest and QCC.

35 **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]**  
36 f. Once again, with QCC employees devoted 100% of the time to Qwest,  
37 how can there be functional separation of employees? This appears to  
38 contradict Qwest’s own internal prohibition on the “sharing” of

1 employees. Although Qwest would have the PUC contain its review to a  
 2 narrowly focused comparison of payroll registers, this selection is yet  
 3 another example of how such a single comparison would continue to allow  
 4 for the circumvention of the separation of the two entities' employees and  
 5 management. As a functional and practical matter Section 272(b)(3) has  
 6 been violated.

7 **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]**

- 8 g. Per the task order, QCC is providing recruitment services for QC –  
 9 “Qwest Communications Corporation obtains and processes job openings,  
 10 develops and administers the compensation guidelines for management  
 11 new hires, and trains recruiters for interviewing job applicants. Recruiters  
 12 also analyze testing results to ensure reliable measurements of skills  
 13 and/or abilities.” Thus, QCC is hiring Qwest’s employees. This clearly  
 14 does not help Qwest’s employee separation dictate as to QCC. It is a  
 15 further violation of Section 272(b)(3). An odd corollary to this is that  
 16 Qwest provides to QCC almost exactly the same services under a posted  
 17 work order for interim human resources services. Why are there both a  
 18 work order *and* a task order providing the same services (in the work  
 19 order, QCC is receiving, and in the task order, QCC is providing)? The  
 20 PUC is urged to inquire into the rationale behind this peculiar situation  
 21 whereby circular servicing is occurring.

22 **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]**

- 23 h. He is also one of only two directors of QC per Brunsting’s Exhibit JLB-  
 24 272.8. Once again, where this individual is an employee of QCC, an  
 25 executive officer with QCI (the parent of Qwest), and a director of Qwest  
 26 there is a violation of the separation of management. QCC states that to  
 27 meet its burden of proof, it need “only provide evidence that its officers,  
 28 directors, and employees are separate from those of the BOC.”<sup>58</sup> QCC’s  
 29 paper promises have been rebutted by the results obtained from the on-site  
 30 reviews.

31 **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]**

- 32 i. There is no difference between when these employees are acting as Qwest  
 33 employees and when they are functioning as QCC employees. The PUC’s  
 34 inquiry should be as to the functional operation and not who cuts the  
 35 payroll check.

36 **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]**

- 37 j. This invoice is related to the above, but now the percentages are much  
 38 less. Qwest, at a minimum, should be required to explain why this is,  
 39 what type of work is being performed at QCC and whether there is  
 40 functional separation of these Qwest employees.

<sup>58</sup> Brunsting Affidavit at 13.

1 **D. Section 272(b)(5) – Affiliate Transactions – Public Disclosure Requirement and**  
2 **AT&T On-site Reviews**

3 55. To satisfy the public disclosure requirements of Section 272(b)(5), a BOC must  
4 disclose detailed information regarding the terms and conditions of each transaction between the  
5 BOC and its Section 272 affiliate, including the rates for each transaction. The Section 272  
6 affiliate must provide, at a minimum: a detailed written description of the asset transferred or the  
7 service provided in the transaction, and post the transaction's terms and conditions on the  
8 Section 272 affiliate's Internet home page within 10 days of the transaction.<sup>59</sup> The description  
9 "should be *sufficiently detailed to allow us to evaluate compliance with our accounting rules,*"  
10 and they must be made available for public inspection at the BOC's principal place of business  
11 and must include a statement certifying the truth and accuracy of such disclosures.<sup>60</sup> The FCC  
12 also stated:

13 Failing to disclose fully the details of the transactions between the BOC  
14 and its Section 272 affiliate is contrary to Section 272(b)(5) because it  
15 impairs our ability to evaluate compliance with our accounting safeguards  
16 and deprives unaffiliated parties of the information necessary to take  
17 advantage of the same rates, terms, and conditions enjoyed by the BOC's  
18 Section 272 affiliate.<sup>61</sup>

19 56. The FCC rejected BellSouth's assertion that only summaries of its affiliate  
20 transactions were required, finding that full disclosures must include a description of the rates,  
21 terms, and conditions of all transactions, as well as the frequency of recurring transactions and  
22 the approximate date of completed transactions.<sup>62</sup>

23 57. The FCC noted in its *Ameritech Michigan Order* that public disclosure  
24 requirements have been in effect *since the passage of the 1996 Act on February 8, 1996*, and that

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<sup>59</sup> *BellSouth Louisiana II Order*, ¶¶ 332 - 339.

<sup>60</sup> *Id.* (emphasis added).

<sup>61</sup> *Id.*, ¶ 335.

<sup>62</sup> *Id.*, ¶ 337.

1 the requirement for posting of data on the Internet became effective with the implementation of  
2 the *Accounting Safeguards Order* on August 12, 1997.<sup>63</sup> In short, public disclosure has now been  
3 required for five years and posting has been required for almost four years.

4 58. Qwest states that “there is no specific requirement that the 272 Affiliate meet  
5 Section 272 obligations now; rather it must only demonstrate that it will comply with the  
6 requirements of Section 272 ....”<sup>64</sup> This statement is misleading by itself. Qwest has been under  
7 an obligation to disclose transactions since February 8, 1996, and post the transactions with,  
8 U S WEST LD, Qwest LD, and now QCC, since August 12, 1997.

9 Nor can Qwest make this assertion simultaneously with its claim that Qwest has an unbroken and  
10 unblemished record of section 272 compliance.<sup>65</sup> Qwest LD did not activate its web site until  
11 September 28, 1998, although the *Accounting Safeguards Order* became effective on August 12,  
12 1997. Therefore, Qwest waited over a year to post any transactions to the website, although  
13 Qwest knew about its obligations since the release date (December 24, 1996) of the order. This  
14 is a clear violation of section 272. The Washington ALJ, in her recent order, also called into  
15 question Qwest’s “contention that it has always been in compliance with section 272  
16 requirements.”<sup>66</sup>

17 59. As has been previously noted, Qwest arbitrarily chose to cease posting its  
18 affiliated transactions with Qwest LD on December 31, 2000, despite the imminent merger of

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<sup>63</sup> See *Ameritech Michigan Order*, ¶ 371 (emphasis added). *Implementation of the Telecommunications Act of 1996: Accounting Safeguards Under the Telecommunications Act of 1996*, CC Docket No. 96-150, Report and Order, FCC 96-490 (Rel. Dec. 24, 1996) (“*Accounting Safeguards Order*”).

<sup>64</sup> Brunsting Affidavit at 2 - 3.

<sup>65</sup> It is curious to note that in previous state workshops (e.g., Washington, Arizona, Colorado), Qwest’s testimony is that Qwest LD was in existence in 1996 and established a five-year history of section 272 compliance since the date of the 1996 Act. However, in the Minnesota testimony, Qwest is now claiming that Qwest LD did not become a 272 affiliate until 1998, and the “five-year history” has now been changed to the ambiguous “many years”. Schwartz Affidavit at 7. QCC’s affidavit undercuts Qwest’s where it states that US WEST formed (in 1996) US WEST LD (n/k/a Qwest LD) to “provide in-region, interLATA telecommunications services ... once Section 271 authority was granted.” Brunsting Affidavit at 7.

1 Qwest LD into QCC. This decision has resulted in a further violation of Qwest's Section 272  
2 duties. In order to make a predictive judgment of the future behavior of a BOC under Section  
3 272, the FCC has stated it will "look to the past and present behavior of the BOC applicant as the  
4 best indicator of whether it will carry out the requested authorization in compliance with the  
5 requirements of Section 272."<sup>67</sup>

6 60. Qwest asserts that it posts and makes public all transactions between Qwest and  
7 Qwest LD, and now Qwest and QCC, to its web site to satisfy the FCC's public disclosure  
8 requirements.<sup>68</sup> AT&T disagrees with these paper promises and states that these assertions are  
9 untrue and were made with the full knowledge by Qwest and QCC that postings were not made  
10 in a timely manner during the so-called "transitional phase".

11 **1. AT&T's Initial On-Site Review and Testing of Financial Records Up to and**  
12 **Through June, 2000.**

13 61. To test Qwest and Qwest LD's compliance with Section 272(b)(5), AT&T  
14 requested, through AT&T Multistate Data Request No. 53, an inspection of the financial records  
15 of Qwest and Qwest LD. Made available to me in August 2000 were the payments made by  
16 "U S WEST LD, Inc. to U S WEST Communications, Inc. For Services Provided" for the period  
17 May, 1999 up and through June, 2000. Also made available were the year-to-date balance sheets  
18 and income statements, as well as the trial balances of the LD affiliate from 1995 up through  
19 December 31, 1999.

20 62. For services provided by Qwest to Qwest LD (expenses to Qwest LD), I used a  
21 bilateral approach to testing the posting and adequacy of affiliate transactions from April 1,  
22 1999, to June, 2000, by: 1) examining transactions posted to the web site and tracing back to

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<sup>66</sup> *WA ALJ's 272 Order*, p. 114. The language in this order is in sharp contrast to the Nebraska PUC's holding. *See*, Schwartz Affidavit at 7.

<sup>67</sup> *Ameritech Michigan Order*, ¶ 347 (emphasis added).

1 supporting documentation, and 2) examining transaction detail and tracing to the affiliate  
2 website.

3 **a. Testing Procedures: From the Website transactions listing to the**  
4 **accounting detail.**

5 63. To complete previous testing<sup>69</sup> for the year 1999, I selected 17 "billed amounts"  
6 for 1999 services provided by "U S WEST" to "U S WEST LD" from the affiliate website for  
7 1999 transactions and attempted to trace back to documentation that would support these  
8 amounts. Documentation includes the various work orders and agreements on the website, as  
9 well as the invoice-level detail. These 17 selections totaled an approximate net amount of  
10 \$1,974,736, which was 56 % of the net total dollar amount for the year 1999. Two of the 17  
11 selections were non-cash accounting reversals in the amount of \$183,702.

12 **b. Testing Procedures: From the Accounting Detail to the Website**

13 64. To complete the other half of the bilateral testing, I selected items representing the  
14 payment detail from Qwest LD to Qwest, and attempted to trace them to the 1999 and 2000  
15 website transaction listings.

16 65. The scope of my testing included selecting 12 "tag numbers" from a tag summary  
17 sheet that purported to represent all payments made by Qwest LD to Qwest. There were separate  
18 summary sheets for the period May, 1999 to December, 1999 and for the year 2000 up and into  
19 June. Each tag represented a separate "authorization for payment" and, presumably, a separate  
20 check to Qwest. Each tag represented one or more invoices to be paid. Each invoice represented  
21 one or more billing activities. The tags were numbered sequentially. For example, for the year

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<sup>68</sup> See generally, Brunsting Affidavit at 19 - 21.

<sup>69</sup> Previous testing for the years ended 1996, 1997 and 1998 and for the period up to March 31, 1999, was performed by Warren Fischer, who was my predecessor at AT&T on Section 272 subject matters. I am adopting the testing that he previously performed and his subsequent work product. I have reviewed and familiarized myself with Mr. Fischer's testing procedures, documentation, and workpapers and personally met with him to become

1 2000 through June there were tags numbered 800 through 873. The assumption would be that  
2 there were 73 payments made in the year 2000 through June.

3 **c. Results of AT&T's On-Site Review and Testing**

4 66. As to the 17 items selected for testing from the website transaction postings, I  
5 found the following problems in attempting to follow an "audit trail" for the 17 selections:

- 6 a. I was unable to trace/find supporting detail of any kind for 3.  
7 b. I was unable to find supporting accounting detail for an additional 3.  
8 c. I was unable to find accounting detail or explanations behind 2 more  
9 selections that were reversals from previous periods.  
10 d. 8 selections were traced to both the accounting detail and to the applicable  
11 agreement or document posted on the website. For 2 of these, I could  
12 determine that they were not posted within 10 days; and, for the remaining  
13 6, I could not make a determination as to timely posting.  
14 e. For 1 selection, I was unable to properly trace it, as it was a summary of  
15 numerous billings.

16 67. That accounts for the 17 selections, but I found additional problems beyond  
17 whether there was an audit trail or proper posting.<sup>70</sup> I have listed these additional problems and  
18 other non-compliance problems and issues encountered in my additional testing procedures  
19 below:

- 20 a. 2 selections were from the area of the 1999 transactions list denoted as  
21 "Exhibit ( ) – Public Relations." I was unable to find any supporting detail  
22 for these transactions, and I was unable to trace the transactions to any  
23 agreement, document, work order, task order or the like on the website. In  
24 fact, it is stated on the 1999 transactions listing that there is "No Current  
25 Work Order" for public relations and the 9 transactions listed under this  
26 subgrouping. To the extent that Qwest makes the argument that all  
27 "transactions" were posted and in a timely fashion through the use of

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knowledgeable about his procedures and conclusions.

<sup>70</sup> The FCC has looked to the maintenance of an audit trail of past Internet postings as assurance of compliance. *Application by SBC Communications Inc., Southwestern Bell Communications Services, Inc. d/b/a Southwestern Bell Long Distance pursuant to Section 271 of the Telecommunications Act of 1996 to Provide In-Region, InterLATA Services in Texas*, CC Docket No. 00-65, Memorandum Opinion and Order, FCC 00-238 (Rel. June 30, 2000), ¶ 404. ("SBC Texas Order").

1           “agreements,” then there is a violation for transactions without a work  
2           order.

3           b.       One selection from the website was in the amount of \$419,769 for “billing  
4           and collection services to USWLD” for January through December 1999.  
5           This selection represents 12% of the entire billing amount from Qwest to  
6           Qwest LD for 1999. I was unable to properly trace this amount to the  
7           invoice detail because there were 15 separate tags, or authorizations for  
8           payment, from May through December, 1999 for these services. Thus, the  
9           total amount is a *summary* of at least 15, and most likely more, as I did not  
10          get to see the tags for the period of January through April. This violates  
11          the FCC’s rulings that there be no summaries of transactions. “True-ups”  
12          are discussed below.

13          c.       Several transactions were not properly recorded in the period of activity.  
14          They were expensed as paid, usually in the year 2000, without setting up  
15          an accrual. One transaction alone represented almost 47% of the entire  
16          billing amount from Qwest to Qwest LD for 1999. This transaction was  
17          for services provided from January through December 1999 but not paid  
18          and expensed until the following year. The failure to record transactions  
19          within ten days of occurrence is a violation of the FCC requirements but  
20          also hinders a proper examination by interested parties and the FCC’s  
21          investigation into compliance with accounting procedures. This finding  
22          runs counter to Qwest’s stated position that it “utilizes accrual accounting  
23          for its transactions between affiliates.”<sup>71</sup>

24          d.       Recurring transactions such as work performed by Qwest Consumer  
25          Services or rent for office space and furniture are billed monthly, are  
26          separate transactions and, with an accounting system purportedly adhering  
27          to GAAP, should be timely accounted for and posted to the website  
28          monthly rather than waiting until the following year. To the extent that  
29          Qwest does not provide such a billing “float” to non-affiliates, there is an  
30          issue of discrimination.

31          e.       As to all the 1999 individual or specific transactions occurring on or  
32          before June 1, 1999, there were no postings as of that date. AT&T’s  
33          previous testing found that even 1998 individual transactions had not yet  
34          been posted. This is a violation of the *Accounting Safeguards Order* that  
35          requires posting of the terms, conditions and actual rates paid in each  
36          transaction to the Internet within *10 days* of the transaction.<sup>72</sup> The Internet  
37          posting requirement is continuous, not occasional.

<sup>71</sup> Qwest’s Response to AT&T Multistate Data Request No. 56.

<sup>72</sup> See *Accounting Safeguards Order*, ¶ 122.

- 1 f. For the year 2000, I found *no* individual transactions or “billed amounts”  
2 that had been posted to the website; and, therefore, I was unable to trace  
3 back to supporting documentation.
- 4 g. Qwest differentiates between “current transactions” and “specific  
5 transactions.” Current transactions are found in the website under “active  
6 documents” (now called “current transactions”) and specific transactions  
7 are found under “terminated transactions.” Specific transactions are the  
8 product of an annual “true-up” of individual transactions from the prior  
9 year. The difference in transactions is confusing and should be rectified  
10 by requiring Qwest to comply with Section 272(b)(5) by properly posting  
11 specific or individual transactions, when they occur, and not wait for a  
12 true-up.
- 13 h. “True-ups” are posted annually, in May, for prior year’s transactions,  
14 pursuant to the “Overview” section of the website. Thus, no separate  
15 transactions were posted for all of 1999 until May 2000, at the earliest. In  
16 AT&T’s prior testing of the transactions with Qwest’s Section 272  
17 affiliate, it was found that no “specific transactions” and therefore no true-  
18 ups had been posted to the website for either 1998 or 1999 year-to-date as  
19 of June 1, 1999. There is a problem with timeliness when transactions are  
20 not posted until the following May, but the problem is exacerbated when  
21 even this tardy deadline is not being followed.
- 22 i. Qwest has stated in the past that the annual “true-ups will remain listed on  
23 the site until the following year’s true-up is posted as a replacement.”  
24 There is FCC guidance<sup>73</sup> on this matter, and it is logical that the products  
25 of the true-up -- specific transactions -- would continue to be useful and  
26 should not be purged.
- 27 j. The accounting transactional detail is referred to as “back-up detail” and is  
28 now only available for inspection at Qwest under confidential  
29 agreement.<sup>74</sup>
- 30 k. The FCC further requires that the certifying statement be at Qwest’s  
31 principle place of business. Prior AT&T on-site testing, in 1998 and twice  
32 in 1999, failed to locate such statement. I attempted to view such  
33 statement and all publicly available records of affiliate transactions  
34 pursuant to Qwest’s posting on their website by calling the listed number.  
35 It is stated that “Records of all affiliate transactions may be viewed  
36 between the hours of 8:00 a.m. and 5:00 p.m., Monday through Friday, at  
37 U S WEST Communication’s principle place of business.”<sup>75</sup> Several  
38 phone calls to several different personnel ultimately resulted in the

<sup>73</sup> The FCC has looked to the maintenance of an audit trail of past Internet postings as additional assurance of compliance. *See SBC Texas Order*, ¶ 404.

<sup>74</sup> Schwartz Affidavit at 22 -23.

<sup>75</sup> Section 272 website address: <http://www.uswest.com/about/policy/docs/furtherInfo.html>.

1 response from Qwest's legal department that AT&T could not view such  
2 records unless specifically requested in a formal data request. Subsequent  
3 calls, including one to a Qwest attorney, did not provide access to the  
4 public documents at Qwest's offices. Thus, I was unable to verify if such  
5 a certifying statement is on file, or even exists, and whether affiliate  
6 transactions are made publicly available as promised on the website.

- 7 l. In my testing from the detail and tracing to the website, I noted that there  
8 was a gap in the tag numbers provided to me.<sup>76</sup>
- 9 m. I was unable to trace any of the 9 tag selections from the year 2000 to a  
10 "Transactions" listing for services provided by Qwest to Qwest LD. As of  
11 the date of my testing there was no transactions listing for the year 2000 as  
12 I found for past years.
- 13 n. I was unable to properly trace 3 tag selections from the year 1999 into  
14 transaction detail listed on the 1999 transactions website or into any  
15 "agreements" posted on the website. All three of these transactions  
16 pertained to "team awards paid to employees" of Qwest LD that had been  
17 rehired by Qwest. I was unable to read any of the employee names, or the  
18 number of employees transferring, because the detail provided to me had  
19 been blacked out as to those details.
- 20 o. In testing from the 2000 detail selections to the posted "agreements," I had  
21 a very difficult time. For example, I selected a tag number from the 2000  
22 payment summary sheet for "Application Support Services." The tag  
23 number consisted of three separate invoices of which I chose one. The  
24 invoice that I selected had the December bill for more than 15 separate  
25 project numbers. Each project number had a billable amount. To trace  
26 that billable amount associated with the project number into the website  
27 agreement consisted of going to the website: to "Active Documents;" to  
28 "Master Services Agreement, Amendment # 3;" to Agreement No. AR  
29 96001; to Exhibit C - Information Technologies Services;" to Work Order  
30 No. ITLD079 - Information Technologies Services, only to find that  
31 separate project numbers are not delineated. This was unfortunate, as  
32 many of the projects have rather obtuse descriptions in the accounting  
33 detail, like "CEW 980501-78 USWLD-Exp Card Fl." Whether by design  
34 or not, the method that Qwest had chosen to post transactions has the  
35 result of obfuscating the very purpose of posting - to provide information  
36 to the FCC to determine compliance and to non-affiliated entities to  
37 determine whether to purchase products or services.

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<sup>76</sup> The year 1999 ended with tag number 748. The year 2000 began with the tag number 800. Qwest's former attorney, Charles Steese, instructed me to forward any discrepancies through formal data requests. Thus, I was unable to reconcile the omission of the missing tag numbers. During my follow-up testing, I noted that an explanation page has been added in the tag binders explaining that Qwest follows a convention whereby tag numbers for each year start with the next "100" in sequence. This would explain the apparent gap in tag numbers from one year to the next.

1 p. There were 38 tariffed transactions listed under the heading "1998  
2 Tariffed Services Purchased by U S WEST Long Distance from  
3 U S WEST Communications" and the exact same list of 38 was listed  
4 under 1999.<sup>77</sup> I was unable to determine to which year the list of tariffed  
5 transactions applied to. Once again, simply because this omission is past  
6 history does not discount the probative value of it in the determination of  
7 future behavior.

8 **2. AT&T's Follow-up On-Site Testing of Financial Records From June, 2000**  
9 **to Present**

10 68. During my April 2001 review, for Qwest LD, the former 272 affiliate, Qwest  
11 made available to me the detail of payments made by Qwest LD to Qwest (expenses of Qwest  
12 LD) for services provided by Qwest for the year 2000 (to complete my previous testing of that  
13 year) and into 2001. I also received for Qwest LD, billing detail of payments made by Qwest to  
14 Qwest LD (revenues of Qwest LD) for services provided by Qwest LD for the years 1999 and  
15 2000. Also made available were balance sheets and income statements for Qwest LD for 2000  
16 and the first 3 months of 2001.

17 69. For QCC, the new 272 affiliate, Qwest made available to me a binder entitled  
18 "QC-QCC 2000 Billing Detail". The binder contained photocopies of what was available on the  
19 public website and some detail of payments made by QCC to Qwest (expenses of QCC) for  
20 services provided by Qwest and received by QCC for the year 2000. I did not receive for QCC:  
21 detail of payments made by QCC to Qwest (expenses of QCC) for services provided by Qwest  
22 and received by QCC for the year 2001; detail of payments made by Qwest to QCC (revenues of  
23 QCC) for services provided by QCC for the year 2001; financial statements for QCC for any  
24 period. Qwest personnel instructed me that such financial statements would not be made  
25 available until early May.<sup>78</sup>

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<sup>77</sup> Section 272 Affiliate Transactions website at <http://www.uswest.com/about/policy/docs/tariffServices.html>.

<sup>78</sup> Given that QCC's statements are consolidated with Qwest Communications International, Inc.'s and the latter's statements were made public for the first quarter, it is curious as to why QCC's would not be available. Qwest

1           70.     Finally, the detail that supported QCC's payment for services provided by Qwest  
2 for 2000 was not as thorough as the detail provided for Qwest LD. The impact of this is  
3 discussed below in the section discussing testing of expenses.

4           a.     **Procedures for Follow-Up Testing for Expenses of the 272 Affiliate:  
5 From the Website Specific Transactions Listing to the Accounting  
6 Detail.**

7           71.     I reviewed affiliated transactions that were expenses of, and revenues to, the 272  
8 affiliate I will first discuss the review of affiliated expenses. For the follow-up testing of the 272  
9 affiliate's expenses (payments from the affiliate for services provided by Qwest), I used a  
10 bilateral approach to test the posting and adequacy of affiliate transactions from June 2000 to the  
11 present by: 1) examining expense transactions posted to the website and tracing back to  
12 supporting documentation, and 2) examining expense transaction detail and tracing to the  
13 affiliate website.

14           72.     As I discussed in my testimony on the initial on-site review and corresponding  
15 testing for the period ended June, 2000, *supra*, I found no specific or individual accounting  
16 transactions (Qwest refers to these as "billed data" or "billed amounts") posted to the websites of  
17 either Qwest LD or QCC. During my follow-up testing, once again, I found no postings of  
18 specific accounting transactions to the website for all of 2000. I was advised by Scott Hamilton,  
19 FCC Regulatory Accountant for Qwest, that starting January 1, 2000, specific "billed amounts"  
20 were no longer posted to the website. Thus, I was unable to trace back specific, or "billable",  
21 transactions to supporting documentation such as posted work orders and service agreements.  
22 This type of information should be posted (as was Qwest's practice prior to January of 2000), as  
23 it assists unaffiliated interexchange carriers ("IXCs") in observing what Qwest and its 272

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advised that the information in this paragraph will be made available for inspection on or after May 4, 2001. On

1 affiliates are *actually* doing versus simply posting general work orders for prospective  
2 transactions. It is worth repeating the FCC's guidance on the subject of transaction detail: a  
3 failure to fully disclose the details of the transactions is against Section 272(b)(5) "because it  
4 impairs the FCC's ability to evaluate compliance with our accounting safeguards and deprives  
5 unaffiliated parties of the information necessary to take advantage of the same rates, terms, and  
6 conditions enjoyed by the ... affiliate."<sup>79</sup>

7 **b. Procedures for Follow-Up Testing for Expenses of the 272 Affiliate:**  
8 **From the Accounting Detail to the Website**

9 73. To complete the other half of the bilateral testing for the Section 272 affiliates'  
10 expenses, I first selected items representing the payment detail from Qwest LD to Qwest for  
11 services provided by Qwest, and attempted to trace them to the 2000 and 2001 website  
12 transaction listings.

13 74. For Qwest LD, the scope of the follow-up testing included selecting 13 "tag  
14 numbers" from tag summary sheets that purported to represent all payments made by Qwest LD  
15 to Qwest. There were separate summary sheets for the periods tested of June through December  
16 2000 and into March of 2001. Each tag represented a separate "authorization for payment" and,  
17 presumably, a separate check to Qwest. Each tag represented one or more invoices to be paid.  
18 Each invoice represented one or more billing activities.

19 75. For QCC, testing of its expenses was compromised. As previously mentioned,  
20 the supporting documentation which purportedly supported QCC's payment for services  
21 provided by Qwest for 2000 was not as thorough as the detail provided for Qwest LD. The QCC  
22 detail provided did not contain such supporting detail as tag numbers, invoices and

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June 5, 2001, I was presented with a single piece of paper representing QCC's financial statements. The review and receipt of this will be discussed below.

<sup>79</sup> *BellSouth Louisiana II Order*, ¶ 335.

1 authorizations to pay, as did the detail for Qwest LD.<sup>80</sup> This type of detail is important to create  
2 an audit trail<sup>81</sup> and to allow the FCC to “evaluate compliance with the Commission’s rules and to  
3 facilitate the detection of potential anticompetitive conduct.”<sup>82</sup>

4 **c. Results of Follow-Up Review and Testing of Section 272 Affiliates’**  
5 **Expenses**

6 76. Following are specific problems and items of interest discovered during my  
7 follow-up review and corresponding testing of Qwest LD’s and QCC’s expenses.

8 77. From a review of Qwest LD’s website, it appears that transactions between Qwest  
9 LD and Qwest after January 1, 2001, are no longer posted. Given that Qwest LD was to have  
10 been merged into QCC in May, 2001 and become one entity, it is of concern that no public  
11 postings of Qwest LD’s transactions will be made after December 31, 2000. The FCC clearly  
12 mandates that the Section 272 affiliate must provide detailed written descriptions of transactions  
13 posted to an Internet home page.

14 78. As was noted in my initial testing, there continues to be long periods of time  
15 before a specific or “billable” transaction is paid by the Section 272 affiliate. Also, these specific  
16 transaction amounts are being expensed as they are being paid rather than being accrued in a  
17 timely manner – even when two years are implicated. The problem of not timely recording  
18 transactions and accruing amounts, especially at year-end, does not appear to be isolated. In this  
19 follow-up, and in prior testing, I found many examples of this and it appears to be the unstated  
20 accounting policy. Because the Section 272 affiliate is receiving very generous extended

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<sup>80</sup> A further request was made for this information; supporting detail was provided and a supplemental review was performed as will be discussed below.

<sup>81</sup> Once again, for additional assurance of compliance, the FCC has looked to the maintenance of an audit trail of past postings. See *SBC Texas Order*, ¶ 404.

<sup>82</sup> *SBC Texas Order*, ¶ 405.

1 payment terms, it is receiving preferential, and thus discriminatory, treatment to the extent that  
2 such terms and conditions are not extended to other companies. Further, failure to post in a  
3 timely manner and accrue specific transactions casts doubt on the validity of the internal  
4 accounting system and the reporting results generated from such a system and hinders a proper  
5 examination of actual activity by interested parties and the FCC's investigation into compliance  
6 with its accounting procedures.

7 79. Specific examples of failure to accrue and untimely accounting, found during my  
8 follow-up review and testing, include:

9 a. One of my selections was [**PUBLIC DOCUMENT – TRADE SECRET**  
10 **DATA HAS BEEN EXCISED**]  
11 These amounts should have been accrued at year-end 1999 and  
12 such payment is not timely.

13 b. More egregious were two invoices I pulled and inspected  
14 corresponding to [**PUBLIC DOCUMENT – TRADE SECRET DATA**  
15 **HAS BEEN EXCISED**]  
16 These amounts should have been accrued at year-end and payment  
17 is not timely.

18 c. Corresponding to posted work order MMLD039, I pulled and inspected  
19 [**PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN**  
20 **EXCISED**]  
21 Again, accounting is not being accomplished in a timely manner.  
22 The accounting also violates section 5 of the web-posted work  
23 order that mandates billing "on a minimum of a quarterly basis."  
24 Finally, as will be discussed in more detail in the section below  
25 discussing past history, in February 2001, the FCC found this  
26 calling card program to be a provision of in-region, interLATA  
27 service and to be a violation of Section 271.<sup>83</sup> Thus, Qwest LD  
28 was directly involved in the provision of in-region long-distance  
29 service prior to Section 271 approval. The FCC looks to past and  
30 present behavior as the best predictive indicator of future  
31 compliance with Section 272.

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<sup>83</sup> *AT&T Corp. v. U S WEST Communications, Inc.*, File No. E-97-28, DA01-418, Memorandum Opinion and Order (Rel. Feb. 16, 2001).

1           80.     I was unable to trace one of the invoices, corresponding to a selected tag number,  
2 into the web-posted work orders. For example, on **[PUBLIC DOCUMENT – TRADE**  
3 **SECRET DATA HAS BEEN EXCISED]**. This transaction purported to correlate to the work  
4 order for Card services. I traced to that posted work order, numbered MMLD039, and I could  
5 not see where that work order covers this transaction. This casts doubt on the validity of Qwest's  
6 chosen method to post blanket work orders and service agreements to represent its actual specific  
7 transactions and underscores the need and importance for Qwest and QCC to post the specific  
8 transactions to the website.

9           81.     One of the billable amounts I selected off a summary sheet was in the amount of  
10 **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]**. The question  
11 arises as to the independence of these employees and whether safeguards are sufficient to  
12 prohibit information flows between Qwest and QCC. Pursuant to Section 272(b)(3), QCC and  
13 Qwest are required to have separate employees. It is AT&T's position that where a Qwest  
14 employee is dedicated to QCC, that employee is not a separate employee. This also  
15 demonstrates why simply checking payroll lists is inadequate.

16           82.     The FCC rules require that a statement be available certifying that an officer of  
17 the BOC has examined postings to the website and such are true and accurate. I examined  
18 certification statements for QCC and Qwest, on file at Qwest, and noted that Robin Szeliga, a  
19 Senior Vice President of Qwest, signed both on March 20, 2001. As the certification requires a  
20 signature by a Qwest officer, presumably Ms. Szeliga is an officer of Qwest. However, when I  
21 compared that name to a listing of QCC's and Qwest's Officers and Directors in the testimony of  
22 Ms. Brunsting,<sup>84</sup> Ms. Szeliga was listed as Executive Vice President, Chief Financial Officer and  
23 a Director of QCC. In addition, to a violation of the separation requirements of Section

1 272(b)(3), this raises a doubt as to whether Qwest and QCC have a valid certification statement  
2 on file and whether Ms. Szeliga had personal knowledge of what she was certifying.

3 **d. Follow-Up Review and Testing on the 272 Affiliates' Revenues for**  
4 **Services Provided by the Affiliates to Qwest**

5 83. It should initially be noted that the FCC makes no distinction in its disclosure  
6 rules between a Section 272 affiliate's expenses versus its revenues. The rule applies to  
7 "transactions." Thus, a review and testing of the Section 272 affiliates' revenue side is  
8 appropriate and necessary.<sup>85</sup>

9 84. For the April 2001 follow-up review of the Section 272 affiliates' revenues  
10 (payments from Qwest to the Section 272 affiliates for services provided by the affiliates), I first  
11 revisited the review and testing done on my initial on-site review in August 2000. At that time,  
12 no information was made available to review payments from Qwest to Qwest LD for services  
13 provided by Qwest LD.

14 **e. Procedures to Follow-Up Testing for Revenues of Qwest LD and**  
15 **QCC**

16 85. For my follow-up testing on revenues, I received and reviewed billing detail of  
17 payments made by Qwest to Qwest LD (revenues of Qwest LD) for the years 1999 and 2000.

18 86. As was previously noted, I did not receive any detail of payments made by Qwest  
19 to QCC (revenues of QCC) for services provided by QCC for the year 2001 in the QCC binder  
20 that was given to me. Nor did I receive any QCC financial statements.

21 87. I reviewed the Service Agreements (SA) and related "task orders" (which  
22 signifies services provided by the Section 272 affiliate to Qwest) for both Qwest LD and QCC.

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<sup>84</sup> Brunsting Affidavit, Exhibits. JLB-272.7 & 272.8.

<sup>85</sup> Indeed, one of the reasons that the FCC applies its affiliate transaction rules to transactions between BOCs and Section 272 affiliates was to detect and protect against the flow of subsidies. *See Accounting Safeguards Order*,

1           **f. Results of Follow-Up Review and Testing for Revenues of Qwest LD**  
2           **and QCC**

3           88. Following are specific problems and items of interest discovered during my follow-  
4 up review and testing of Qwest LD's and QCC's revenues.

- 5           a. Due to the lack of billing detail or financial statements, I cannot determine  
6 if QCC received any payments from Qwest for 2001. At a minimum, lack  
7 of an audit trail hinders the ability of Qwest and QCC to comply with the  
8 public disclosure rules of Section 272(b)(5) and the failure to post a  
9 sufficiently detailed description impairs the FCC's ability to evaluate  
10 compliance with the FCC's accounting safeguards which, in part, are  
11 designed to detect and protect against the flow of improper subsidies.  
12 During my supplemental testing, I was able to review such detail and the  
13 results of that review are discussed below.
- 14           b. On QCC's website, under "Services Agreement", or SA, there are listed 3  
15 Task Orders. Task Order #2, which provides for the leasing of transport  
16 capacity on QCC's fiber optic network, estimates annual revenues of  
17 \$464,484 to QCC for the leasing of transport capacity at \$38,707 per  
18 month. As billing is suppose to occur on a monthly basis, my failure to  
19 see any revenue billing detail may mean that Qwest is receiving  
20 preferential billing treatment (extended payment terms beyond the posted  
21 terms and conditions) and/or the internal accounting system is faulty.
- 22           c. Also under QCC's SA, per Task Order # 1, Qwest has contracted for QCC  
23 to provide financial services, which include "financial analysis, financial  
24 advice, budgeting, accounting, and payroll support" in the amount of  
25 \$400,000 per year. The PUC should question the rationale behind this  
26 task order, or the logic as to why Qwest would find it necessary to contract  
27 with its Section 272 affiliate for such financial services. The inquiry into  
28 the rationale is magnified where QCC has contracted (see QCC's Work  
29 Order – Finance Services on the website) with Qwest to be provided for  
30 almost the same services. Such circular servicing may be a vehicle to  
31 provide reinvesting to QCC and subsidize future losses on its long-  
32 distance offerings. It must be further noted that QCC states that its  
33 "accounting and finance functions are performed on behalf of the 272  
34 affiliate by the Services Company."<sup>86</sup> Thus why would a task order be  
35 necessary for the provision of financial services by QCC? There is much  
36 inconsistency on the provision and receiving of financial services which  
37 assumedly include payroll services. The PUC should inquire and  
38 determine if safeguards are being circumvented.

---

¶ 176.

<sup>86</sup> Brunsting Affidavit at 12.

1 d. On Qwest LD's website is listed Task Order # 9901 for card services  
2 pertaining to the 1-800-4USWEST Calling Card products and Qwest LD's  
3 provision of network design, development and maintenance, product  
4 design and management and product and market development. As was  
5 discussed above, the FCC found this calling card scheme to be an illegal  
6 venture into in-region, interLATA long distance. Thus, any revenues  
7 received by Qwest LD, and now QCC with the imminent merger, under  
8 this scheme were ill-gotten.

9 e. I reviewed accounting detail supporting Qwest LD revenues. For the first six  
10 months of 2000, most of the revenue came from **[PUBLIC DOCUMENT – TRADE SECRET**  
11 **DATA HAS BEEN EXCISED]**No explanation was provided in the detail as to this dramatic  
12 change. Due to the FCC's concern as to the detection and protection against flows of subsidies,  
13 the PUC should inquire of Qwest about this revenue stream, what it consists of, where it went to  
14 and whether QCC is now the recipient of it.

15 h. I was unable to determine, from the detail provided, the reason for a billable  
16 amount/accounting entry in June 2000. **[PUBLIC DOCUMENT – TRADE SECRET DATA**  
17 **HAS BEEN EXCISED]**. Due to the FCC's concern as to the detection and protection against  
18 flows of subsidies, the PUC is urged to inquire of Qwest about this revenue amount.

19 **3. Supplemental Review of QCC's Affiliated Transactions with Qwest**  
20 **Corporation**

21 **a. Background for the Supplemental On-Site Review and Testing**

22 89. Previously, I stated that I did not receive certain accounting detail of the specific  
23 transactions between QCC and Qwest which included detail of payments made by QCC to Qwest  
24 (expenses of QCC), detail of payments made by Qwest to QCC (revenues of QCC) and financial  
25 statements for QCC for any period. Due to the failure to receive such detail, I concluded above  
26 that testing of QCC's expenses and revenues with Qwest were compromised and no conclusions  
27 could be reached regarding specific transactions.

1           90.     AT&T made a request of Qwest on April 30, 2001, for the needed accounting  
2 detail. Qwest agreed to make such detail available starting on May 8, 2001.

3                   **b.     Detail Provided and Procedures Used for Supplemental On-Site**  
4                   **Review and Testing**

5                           **(i)     For QCC's Expenses**

6           91.     For QCC's expenses (for services provided by Qwest), Qwest made available to  
7 me a "Summary of QCC Billing in April 2001 [and] Monthly Reconciliation to Section 272  
8 Website" which contained **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN**  
9 **EXCISED]**. Also provided were copies of the invoices and supporting details, including the  
10 related posted work order and relevant amendments.

11           92.     What was not provided were QCC's "Authorization for Payments" for these  
12 invoices as they will not be made available until May 22, 2001. All of the tendered invoices  
13 from QC to QCC were dated sometime in the latter half of April 2001. This means that they will  
14 not be paid until sometime in the latter half of May 2001, or later. These **[PUBLIC**  
15 **DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]** invoices represent  
16 services provided by QC to QCC for the period July 2000 through April 2001, generally. The  
17 impact of this will be further developed below.

18           Also, QCC's financial statements were not provided. Qwest personnel informed me that  
19 these financial statements would not be made available until early May, which I found of  
20 concern given that QCC's statements are consolidated with Qwest Communications  
21 International, Inc.'s ("QCI"), and the latter's statements were made public for the first quarter  
22 ended March 31, 2001. On June 5, 2001, I traveled to Qwest and was presented with a single  
23 piece of paper representing QCC's financial statements which was entitled **[PUBLIC**  
24 **DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]**

1 Qwest personnel did not present the income statement to me and stated that the balance sheet  
2 was all that was available to me. I was given no explanation as to why QCC's income statement  
3 or cash flow statement was not presented. The balance sheet was insufficiently detailed to allow  
4 me to trace any revenue or expense amounts associated with Qwest Corporation for the purpose  
5 of comparing such with other filed reports such as the ARMIS report. Either by design or not,  
6 there were no descriptions in this consolidated balance sheet for affiliated receivables or  
7 payables with Qwest. Whether such affiliated amounts were included in the general receivable  
8 and payable amounts is unknown. In summary, this insufficiently detailed consolidated balance  
9 sheet provided no documentation to clear up the apparent underreporting or lack of reporting of  
10 affiliated transactions as between Qwest and QCC.

11 93. To test QCC's expenses from the accounting detail, I selected **[PUBLIC**  
12 **DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]** invoices from the  
13 summary sheets and traced to a copy of the invoice and supporting documentation. From the  
14 invoice, I traced to the applicable web-posted work order and amendments, if any.

15 (ii) For QCC's Revenues

16 94. For QCC's revenues (for services provided *for* Qwest), Qwest made available to  
17 me a "Summary of QC Billing in April 2001 [and] Monthly Reconciliation to Section 272  
18 Website" which contained **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN**  
19 **EXCISED]** Also provided were copies of something called "affiliate billing forms" with "ASF"  
20 numbers and corresponding detail, including the related posted task order and relevant  
21 amendments. The billing forms, assumedly, are what QCC uses to invoice QC for services  
22 provided.

23 95. To test QCC's revenues from the accounting detail, I selected all **[PUBLIC**  
24 **DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]** and traced to a copy of the

1 “affiliate billing form” and supporting documentation. From the billing form, I traced to the  
2 applicable web-posted task order and amendments, if any.

3 **c. Results of Supplemental On-Site Testing and Impact on Section**  
4 **272(b)(5)**

5 96. Findings from the supplemental on-site testing impact and supplemental data  
6 requests upon Qwest’s and QCC’s compliance with subsection 272(b)(5) will be discussed  
7 immediately below and the impact upon other sections will be discussed elsewhere in this  
8 testimony. This data demonstrates that Qwest’s past behavior indicates that Qwest’s assurances  
9 of future compliance with Section 272 are unsupported “paper promises” and that the  
10 Commission should expect that Qwest will not carry out its obligations under Section 272.

11 **(i) General Discussion of Supplemental On-Site Review**

12 97. I discovered that, alarmingly, QCC and Qwest had not billed *any* of their  
13 affiliated transactions for the period July 2000 to present *until April 2001*.<sup>87</sup> Qwest admitted this  
14 in the documentation provided to me. On the summary sheets were notes that stated [**PUBLIC**  
15 **DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED**] The implications of this  
16 on Qwest’s compliance with Section 272(c)(2) and other 272 sections are discussed elsewhere in  
17 this testimony. It is disconcerting that there would be such a total failure by Qwest to account  
18 for affiliated transactions with QCC given that it made the decision as early as the second week  
19 of September, 2000 to use another entity as its Section 272 affiliate and purportedly began the  
20 transition process in early October, 2000. Equally disturbing are the statements made by Ms.  
21 Brunsting and Ms. Schwartz, in their respective affidavits, asserting compliance with the posting  
22 requirements despite Qwest’s admission as noted above.

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<sup>87</sup> This may explain why billable detail of accounting transactions was not made available to me for my previous on-site testing; *i.e.*, there was nothing available for my review. It further may explain the failure of Qwest to tender any 2001 financial statements for QCC when initially requested.

1           98.     Qwest asserts that payments to and from QCC “are tracked and reconciled to  
2 ensure compliance with the requirements of Section 272(b) [and] the processes for capturing  
3 transactions between Qwest Corp. and the 272 affiliate are the same as for all affiliates.”<sup>88</sup> If the  
4 reconciliation procedures that are *actually carried out* extend to all affiliated transactions, then  
5 the problem of failing to accrue and timely account for transactions is much more widespread  
6 than just as to Section 272 affiliated transactions.

7           99.     To comply with Section 272(b)(5), QCC must provide detailed written  
8 descriptions of transactions with Qwest, and the rates, terms and conditions must be posted on  
9 the website within 10 days of the transaction. Further, the written description must be  
10 sufficiently detailed to allow the FCC to determine compliance with its accounting rules.

11                           **(iii) Results of Supplemental Testing of Expenses of QCC**

12           100.    As was noted above in my affidavit discussing the results of the first two phases  
13 of on-site reviews, there continues to be long periods of time before a specific or “billable”  
14 transaction is billed, and consequently paid by QCC. Also, the unstated accounting policy  
15 continues (from Qwest LD and now to QCC) that there are no year-end, and certainly no month-  
16 end, accruals of expenses. This is because billable amounts are being expensed as invoiced. The  
17 importance of this is that when QCC receives very generous extended payment terms, it is  
18 receiving preferential, and thus discriminatory, treatment to the extent that such terms and  
19 conditions are not extended to other companies. Because specific billable transactions are not  
20 posted to the website, a third party would be unable to view *actual* terms and conditions and  
21 make a decision based upon what is *actually* occurring.

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<sup>88</sup> Qwest Response to AT&T Multistate Data Request 104.

1           101. Qwest asserts that it is well aware that nondiscrimination requirements extend to  
2 any good, service, facility or information that it provides to QCC.<sup>89</sup> However, this is a “mere  
3 paper promise.” What is actually occurring are such discriminatory practices as the extension of  
4 very favorable payment terms and the failure to post work orders within a 10-day period.

5           102. The failure to account in a timely manner and accrue specific transactions casts  
6 doubt on the validity of the internal accounting system and the reporting results generated from  
7 such a system. This, in turn, hinders a proper examination of actual activity by interested  
8 parties and the FCC’s investigation into compliance with its accounting procedures.

9           103. QC states that there are no discrepancies between actual billing and Internet  
10 postings since April.<sup>90</sup> What QC does not admit is that for the months of January and February  
11 the error rate was 100% as no transactions were posted.

12           104. As a result of my supplemental on-site review, additional examples of failure to  
13 accrue and untimely accounting include:

- 14           a. Of the 18 invoices selected for testing, 12 invoices wholly or  
15 partially were for services provided in 2000 (often starting in July  
16 2000). None of these invoices were billed until the latter half of  
17 April 2001. Thus, no year-end accruals were made by QCC for  
18 these 12 invoices selected which represent \$12.1 million of  
19 services provided.
- 20           b. None of the 18 selected invoices were billed until the latter half of  
21 April 2001. None were accounted for in a timely fashion.
- 22           c. One of my selections was **[PUBLIC DOCUMENT – TRADE SECRET**  
23 **DATA HAS BEEN EXCISED]**
- 24  
25           c. At a minimum, these amounts should have been accrued at year-  
26 end 2000 and the payment is not timely. Another selection was  
27 **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS**  
28 **BEEN EXCISED]**

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<sup>89</sup> *Id.* at 111.

<sup>90</sup> Schwartz Affidavit at 24; Exhibit MES-272.11.

- 1           d.     Once again, part of this amount should have been accrued at year-  
2                    end, billing is not timely, QCC is receiving discriminatory  
3                    extended payment terms and the associated task order was not  
4                    timely posted.
- 5           e.     The admission made by Qwest and QCC, as noted in the  
6                    accounting detail, that [**PUBLIC DOCUMENT – TRADE**  
7                    **SECRET DATA HAS BEEN EXCISED**] does not adequately  
8                    explain why transactions for the July – December 2000 time period  
9                    were not billed, accrued and reconciled. Note that QCC was  
10                   officially designated the 272 affiliate in January 2001 and such a  
11                   change was contemplated at least since September 2000.
- 12          f.     Qwest's failure to bill QCC in a timely manner violates the web-  
13                    posted Master Services Agreement (MSA) which states that  
14                    "Qwest Corp. shall submit invoices to QCC for Services ... on a  
15                    monthly basis unless otherwise specified in the Work Order."<sup>91</sup>  
16                    The failure to adhere to its internal procedures is further evidence  
17                    that Qwest's actions "speak louder" than its paper promises.

18           105.   Qwest and QCC assert that they consistently post and make public all transactions  
19                    between Qwest and Qwest LD, and now Qwest and QCC, to its web site to satisfy the FCC's  
20                    public disclosure requirements.<sup>92</sup> This claim is demonstrably false. Not one work order (for  
21                    services provided by QC for QCC) was posted to the Internet website prior to March 27, 2001.<sup>93</sup>  
22                    That means that all 18 invoices that I reviewed (which represented activity well before March 27,  
23                    2001) were not posted within the 10 days in which the FCC requires Qwest to post detailed  
24                    written descriptions of transactions. As most of the invoices reflect activity extending back to  
25                    July 2000, the 10 day requirement could have been a 10 week requirement and Qwest still would  
26                    not have complied with it. This is a gross violation of the *Accounting Safeguards Order* that  
27                    requires posting of the terms, conditions and actual rates paid in each transaction to the Internet  
28                    within 10 days. The Internet posting requirement is continuous, not occasional. The practical  
29                    importance of posting in a timely manner is to provide information to competitors on goods,

<sup>91</sup> See Section 272 website at [http://www.qwest.com/about/policy/docs/qcc/MSA\\_qcc.html](http://www.qwest.com/about/policy/docs/qcc/MSA_qcc.html).

<sup>92</sup> See generally, Brunsting Affidavit at 19 - 21.

1 services, facilities or information that Qwest is providing to QCC. By shielding this information  
2 until the end of March, 2001 Qwest discriminates in favor of QCC.

3 (iv) Results of Supplemental Testing of Revenues of QCC

4 106. I tested all **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN**  
5 **EXCISED]** of the “invoices” (a/k/a “affiliate billing forms”) presented to me that represent  
6 billings from QCC to QC for services provided by QCC and cover a period commencing in July  
7 2000 and running into March 2001.

8 107. The same problems that I discovered in my review of QCC’s expenses were  
9 evident with its revenues: lack of accrual accounting, untimely accounting and improper posting  
10 for *all* **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]**  
11 of the invoices representing over \$5 million of transactions. Further, at least 7 of the **[PUBLIC**  
12 **DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]** invoices highlight the  
13 widespread and troubling practice of the liberal “sharing” of employees between the two entities  
14 that impacts upon Section 272(b)(3). As was discussed in that section, this practice of Qwest’s  
15 sharing employees casts doubt upon the actual independence from QCC.

16 108. Another issue that arose during my supplemental testing was whether Qwest is  
17 discriminating in the provision of services, goods, facilities or information on a *de facto* basis  
18 where it sets exorbitantly high rates for services. Although, Qwest may be following the FCC’s  
19 guidelines on pricing affiliated services, there are many examples of very high hourly billable  
20 rates for services (see specific examples below). By setting such high rates, competitors may be  
21 functionally excluded from utilizing these services and discrimination “in substance” is achieved.

---

<sup>93</sup> The web-posted date of 2005 must be in error. See Section 272 Internet site Posting Summary at <http://www.qwest.com/about/policy/docs/qcc/postSummary.html>.

1 The corollary concern to setting high rates for services is that it may be a mechanism for Qwest  
2 to flow subsidies back to QCC.

3 109. Following are specific problems and items of interest discovered during my  
4 supplemental review of QCC's revenues.

- 5 a. Several of the billable amounts raise the question of whether Qwest is  
6 flowing improper subsidy amounts to QCC. For example **[PUBLIC**  
7 **DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]**  
8 This raises questions as to improper subsidy flow via high bill  
9 rates. A corollary is that by setting such high bill rates, Qwest may  
10 effectively prevent competitors from using such services and thus  
11 *de facto* discrimination is achieved.
- 12 b. Another example of high billing rates for “borrowed” or “shared”  
13 employees was **[PUBLIC DOCUMENT – TRADE SECRET DATA**  
14 **HAS BEEN EXCISED]**. Once again, the question is raised whether the  
15 high billing rates of such personnel are designed to flow subsidies back to  
16 QCC and whether such high rates is *de facto* discrimination. Further, the  
17 work order associated with this activity was not posted until March 29,  
18 2001, and did not contain any rates or an estimated total amount. Such is  
19 a violation of the FCC's 10 day posting requirement.
- 20 c. Review of QCC's web “Posting Summary”<sup>94</sup> reveals that no Task Orders  
21 (once again, a task order is for services provided from QCC to Qwest)  
22 were posted before March 27, 2001. Also, no Task Order was signed prior  
23 to March 27, 2001, except for the Task Order for leasing of fiber optic  
24 lines.<sup>95</sup> As all **[PUBLIC DOCUMENT – TRADE SECRET DATA**  
25 **HAS BEEN EXCISED]** of the invoices that I examined for QCC's  
26 Section 272 affiliated revenues pertained to services provided for a period  
27 generally starting in July or August 2000, there is a gross violation of the  
28 10 day requirement to post to the Internet site.
- 29 d. QCC violates the Service Agreement purportedly signed on either January  
30 19, 2001, per the document, or March 23, 2005 [sic], per the posting  
31 summary and posted to the website. The Service Agreement states that  
32 “QCC shall submit invoices to Qwest Corp. for Services provided in  
33 accordance with the terms and conditions of this [Service Agreement]  
34  
35

<sup>94</sup> Once again, the years used are 2005, 2006, etc. and appear to be incorrect. See  
<http://www.qwest.com/about/policy/docs/qcc/postSummary.html>.

<sup>95</sup> As the task order of “Lease of Fiber Optic Lines” was signed on February 27, 2005 [sic], and not posted until  
March 27, 2005 [sic], there is a violation of the 10 day posting requirement. Also, an earlier review (on April 29,  
2001) of the web Posting Summary had this task order being signed on February 26, 2001, and posted on March 26,  
2001. There is no explanation for this change, but it raises the point of accountability of web postings and how  
Qwest can manipulate posting dates and other data to fit the FCC's requirements without oversight.

1 Agreement on a monthly basis unless otherwise specified in the  
2 Task Order.” None of the invoices that I reviewed followed the  
3 monthly procedure. Qwest and QCC are flouting their posted  
4 agreements and certainly are not adhering to the FCC’s  
5 requirements as to terms and conditions.

6 e. **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN**  
7 **EXCISED]** My review of that posted Task Order reveals that such lease  
8 does not provide Qwest with any ownership interest of QCC’s network,  
9 that the primary account that Qwest should expense these amounts to is  
10 Account # 6232 and that the Task Order was signed by Qwest on February  
11 21, 2001. The posting summary states that this Task Order was not posted  
12 until either March 26, 2001, or March 27, 2005 [sic], thus there is a  
13 violation of the posting requirement. **[PUBLIC DOCUMENT – TRADE**  
14 **SECRET DATA HAS BEEN EXCISED]**. Beyond the posting  
15 requirement violations, there is a concern that a transfer of ownership in  
16 network assets may be occurring given the description and the untraceable  
17 account code used. Simply because the task order states that there is no  
18 ownership transfer is of dubious value given the actual description used on  
19 the accounting detail.

20  
21 f. **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN**  
22 **EXCISED]** This task order was not posted until March 28 or 29, 2001.  
23 That means that Qwest utilized QCC’s equipment starting back in July 1,  
24 2000, and the related task order was not posted until almost 9 months  
25 later. Thus, competitors would have looked in vain on the Internet site for  
26 this type of service. This is a discriminatory practice by Qwest and a  
27 serious violation of Section 272(b)(5).  
28

29 **4. QCC’s so-called “transition phase”.**

30 110. At a Section 272 workshop held in Denver, Colorado on June 7-8, 2001, in the  
31 Multistate Section 271 proceeding, Qwest’s attorney stated that QCC did not officially become  
32 the section 272 affiliate until March 26, 2001 and therefore, QCC’s section 272 obligations did  
33 not commence until that date. This revelation came as a surprise to me. Based on Qwest’s and  
34 QCC’s testimony (filed in the multistate proceeding), statements on their Section 272 website, I  
35 believed (and still believe despite Qwest’s recent revelation) that QCC became the primary  
36 operational Section 272 affiliate sometime in January, 2001.<sup>96</sup> Following is a partial listing of

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<sup>96</sup> Qwest has chosen to remove the language to this effect from its current website.

1 evidence pointing to QCC becoming a Section 272 affiliate sometime prior to, or in January  
2 2001, and upon which I reasonably relied upon:

- 3 a. "While QCC ("272 Affiliate") was not designated a Section 272 affiliate  
4 until January 2001, the BOC has identified and posted any transactions  
5 identified with QCC ("272 Affiliate") back to the Qwest-US WEST  
6 merger date on June 30, 2000."<sup>97</sup>
- 7 b. "In January 2001, QCC was identified as the 272 subsidiary of the  
8 future."<sup>98</sup> It is noted that in testimony filed previously in other venues,  
9 Ms. Brunsting simply states "to offer interLATA telecommunications  
10 service", but has added the phrase "of the future" in her Minnesota  
11 testimony.
- 12 c. The Master Services Agreement (the "MSA") between Qwest and QCC is  
13 dated January 1, 2001, and per Article 2 of the agreement the effective  
14 date was January 19, 2001.<sup>99</sup> As it is Qwest's position that the MSA is a  
15 "transaction", it should have been posted to the website within 10 days.  
16 This is a violation of the posting rule.
- 17 d. On QCC's Section 272 website *was* the following note: "To view  
18 transactions between Qwest Corporation and Qwest Long Distance prior  
19 to January 2001, please click here:  
20 <http://www.qwest.com/about/policy/docs/qcc.html>."<sup>100</sup> This language has  
21 now been changed, but the quote is in the original.
- 22 e. On Qwest Long Distance's Section 272 website *was* the following note:  
23 "To view transactions between Qwest Corporation and Qwest  
24 Communications Corporation beginning in January 2001, please click  
25 here: <http://www.qwest.com/about/policy/docs/long>  
26 [distance/overview.html](http://www.qwest.com/about/policy/docs/long_distance/overview.html)."<sup>101</sup> Once again, Qwest has deleted this quoted  
27 language. The obvious inference of the two complimentary statements is  
28 that QCC, beginning in January 2001, became the operational Section 272  
29 affiliate.
- 30 f. Also on Qwest LD's Section 272 website *was* the following note: "Qwest  
31 Long Distance was the Section 272 affiliate of Qwest Corporation from

<sup>97</sup> Schwartz Affidavit at 23. The quote is from Ms. Schwartz's testimony filed in previous state proceedings. She has now added the qualifying phrases "of the future" and "did not become operational until March 26, 2001" to her original written testimony. AT&T's attorneys are reviewing whether QCC should be considered a Section 272 affiliate since the date of the merger.

<sup>98</sup> Brunsting Affidavit at 7.

<sup>99</sup> Schwartz Affidavit, Exhibit 272.7, p.3.

<sup>100</sup> QCC's Section 272 website at: <http://www.qwest.com/about/policy/docs/qcc/overview.html>.

<sup>101</sup> Qwest LD's Section 272 website at: [http://www.qwest.com/about/policy/docs/long\\_distance.html](http://www.qwest.com/about/policy/docs/long_distance.html).

1 February 8, 1996 through December 31, 2000.”<sup>102</sup> This language has now  
2 been removed.

3 g. Conversely, on QCC’s Section 272 website *was* the following note:  
4 “*Qwest Communications Corporation is its [Qwest’s] Section 272 affiliate*  
5 *as of January 2001.* This web site includes the transactions between  
6 Qwest Corporation and Qwest Communications Corporation. Prior to  
7 January 2001, Qwest Long Distance operated as the Section 272 affiliate.”  
8 (emphasis added) Qwest has removed this language from its current  
9 website.

10 h. During my on-site reviews, I was not given any accounting detail of  
11 billable transactions for Qwest LD after the January 1, 2001 date. The  
12 inference from Qwest’s actions was that Qwest LD, after January 1, 2001,  
13 was not the operational Section 272 affiliate.

14 111. Another reason that I was surprised at Qwest’s pronouncement that QCC did not  
15 become the operational Section 272 affiliate until the latter part of March 2001 is the recent  
16 timeline of events. Qwest states that it reevaluated the entity to serve as its Section 272 affiliate  
17 as early as August 2000.<sup>103</sup> Accordingly, Qwest notified several state commissions requesting a  
18 delay in Section 272 workshops on the eve of the filing of its response to AT&T’s testimony.

19 112. On September 15, 2000, an e-mail was sent by Qwest attorney Andrew Crain to  
20 the “Section 271 superlist” in the Multistate proceedings that stated that “*Qwest is in the process*  
21 *of developing a transition plan* for another subsidiary to become Section 272 compliant. As a  
22 result, Qwest recommends that the Section 272 topic be addressed in the second workshop,  
23 rather than the first.”<sup>104</sup> (emphasis added) Thus, since at least the middle of September 2000,  
24 Qwest had commenced the transition to QCC, and was not merely in a reevaluation process.

25 113. Putting the timing aspects of section 272 requirements aside, the PUC should not  
26 lose sight of the fact that QCC still had an obligation to follow FCC rules and state regulations

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<sup>102</sup> *Id.*

<sup>103</sup> Schwartz Affidavit at 6.

<sup>104</sup> On September 15, 2000, the second workshop in the Multistate proceeding was scheduled to start on January 16, 2001.

1 governing affiliate transactions during the so-called transition phase. As the Washington ALJ  
2 stated:

3 It appears that Qwest did not follow FCC rules or Commission  
4 regulations governing affiliate transactions with respect to these  
5 services. (footnote omitted) Whether or not QCC was a section  
6 272 affiliate should not affect Qwest's duty to abide by the affiliate  
7 transaction rules that were in effect while the transactions were  
8 taking place.<sup>105</sup>

9  
10  
11 **5. What is a "transaction"?**

12  
13 114. A transaction is an event that captures a discrete accounting activity. Based on  
14 observations while conducting my testing, Qwest LD, and now QCC track billable activities  
15 which, in turn, can be traced to invoices. Either the billable activity or the invoice, if it only  
16 contains one activity, should be the transaction and should be publicly reported and disclosed.  
17 This type of specific transaction posting would allow determinations to be made of errors and  
18 departures from GAAP and contravention of FCC safeguards, such as whether specific  
19 transactions are occurring in a discriminatory fashion. Qwest, however, fails or refuses to post  
20 actual transactional details and thus does not comply with Section 272(b)(5).

21 115. Qwest has adopted the approach of the former U S WEST in choosing to report  
22 documents it collectively calls "agreements" rather than individual transactions. This approach  
23 does not rise to a summary of the transaction, let alone a detailed description that would permit  
24 the FCC to determine if such transactions are nondiscriminatory.<sup>106</sup>

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<sup>105</sup> WA ALJ's 272 Order, p. 114.

<sup>106</sup> The FCC has held that "our interpretation of Section 272 (c )(1) as a flat prohibition against discrimination will work in conjunction with the Section 272(b)(5) disclosure requirement to deter anticompetitive behavior." *Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended*, CC Docket No. 96-149, First Report and Order, FCC 96-489 (Rel. Dec. 24, 1996), ¶ 324 ("Non-

1           116. Qwest claims to be adequately disclosing its affiliated transactions but fails to  
2 mention the purposes behind the public inspection requirement of Section 272(b)(5). These  
3 purposes are twofold: to assist the FCC in determining that such transactions are conducted in  
4 compliance with FCC accounting safeguards, and to make sure information of such services are  
5 available to unaffiliated third parties.<sup>107</sup> The FCC would be unable to determine compliance  
6 with their accounting rules if specifically accounted for transactions are not posted. Also, third  
7 parties could not avail themselves of services or goods if Qwest does not post them in a timely  
8 manner.

9           117. Full disclosure must include a description of the rates, terms, and conditions of all  
10 transactions, as well as the frequency of recurring transactions and the approximate date of  
11 completed transactions.<sup>108</sup> It is not sufficient to post an agreement with the terms and  
12 conditions on the website and leave it at that. Qwest has attempted to comply with the 10-day  
13 posting requirement on the separate affiliate website by posting master agreements within 10  
14 days of their execution and individual transactions, referred to Qwest as “back-up detail”<sup>109</sup> can  
15 only be viewed upon special request.

16           118. The Washington ALJ shared AT&T’s concerns for the adequacy of Qwest’s  
17 Internet postings: “Qwest must expand the descriptions of services rendered in its agreements  
18 to ensure that its website adequately describes the scope and type of services provided under the  
19 agreements.”<sup>110</sup> AT&T urges the Minnesota PUC to adopt the same requirement.  
20

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*Accounting Safeguards Order*”).

<sup>107</sup> See, *BellSouth Louisiana II Order*, ¶ 335.

<sup>108</sup> *Id.* at ¶ 337. The FCC found that BellSouth failed to comply with its obligations where it disclosed only basic contractual terms of its agreements while withholding the actual transactional details.

<sup>109</sup> Schwartz Affidavit at 22.

<sup>110</sup> *WA ALJ’s 272 Order*, p. 116.

1 **E. Section 272(b)(5) – “Arm’s Length” Requirement**

2 119. The second requirement of Section 272(b)(5) is that all transactions between  
3 Qwest and Qwest LD, and Qwest and QCC, must be negotiated at “arm’s length” and include the  
4 recording of a transaction’s cost in accordance with a specified hierarchy of valuation  
5 methodologies.<sup>111</sup>

6 120. The results of the on-site reviews that AT&T conducted demonstrates that many  
7 transactions do not comply with the “arm’s length” requirement due to the many instances of  
8 intermingled management, “employee sharing” and failure to timely post offered services and  
9 goods. Regarding cost valuation requirements, the high rates used for services act as a practical  
10 barrier for third parties to use such services. Even to the extent that transactions, as disclosed by  
11 Qwest, do not clearly violate this “arm’s length” standard, the Commission cannot conclude that  
12 no such violation is occurring in light of Qwest’s failure to comply with the posting requirements  
13 of Section 272(b)(5) and the FCC’s accounting principles.

14 121. QCC’s web-posted Service Agreement with Qwest, for example, contains Article  
15 10 “Notices” which directs that all written notices, demands or other communications are to be  
16 made to the other party’s address. Listed for QCC and Qwest are the exact same address, same  
17 suite and same organization. As both entities affirmatively state that all transactions will be  
18 conducted at arm’s length and the two companies are to operate independently, such a close  
19 affinity belies Qwest’s assertions of compliance with this section.

20 **F. Section 272(c)(2) – Accounting Principles**

21 122. Whereas the requirements of Section 272(b) apply to Qwest LD and QCC,  
22 Section 272(c)(2) applies to Qwest and can be viewed as a companion to the Section 272(b)(2)

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<sup>111</sup> *BellSouth Louisiana II Order*, ¶ 339.

1 accounting requirements for the Section 272 affiliate. This section requires Qwest to account for  
2 all transactions with Qwest LD and QCC pursuant to accounting principles designated or  
3 approved by the FCC. As was mentioned in the initial on-site review and testing discussion of  
4 this affidavit, AT&T was unable to review the supporting detail for receipts of money from  
5 Qwest to Qwest LD. These affiliate transactions, for 1999 alone, totaled almost \$29 million. In  
6 my follow-up testing, I was presented with detail of these amounts, which I attempted to trace  
7 into corresponding task orders. Payments from Qwest to Qwest LD, and now to QCC, should be  
8 subjected to close scrutiny because of the potential for improper subsidization.<sup>112</sup>

9 123. Based upon its initial and follow-up review, the following items deserve scrutiny  
10 in determining Qwest's compliance with this section:

- 11 a. Because Qwest has failed to properly disclose specific, billable  
12 transactions between it and QCC/Qwest LD, a full evaluation of the  
13 compliance of affiliate transactions cannot be accomplished.<sup>113</sup>
- 14 b. The only transactions between Qwest and QCC/Qwest LD that are  
15 accounted for as "affiliate transactions" are those involving payments.<sup>114</sup>  
16 There is a concern that transactions not involving the exchange of money  
17 may occur and not be accounted for and reported.
- 18 c. Qwest focuses on the audit of its ARMIS Report, but admits that the  
19 auditor's compliance statement is "general in nature" and "does not focus  
20 specifically on the relationship between the BOC and the 272 affiliate."<sup>115</sup>  
21 Also, the audit relates to the ARMIS data, which includes only summary  
22 information about transactions with Section 272 affiliates.<sup>116</sup> Thus, the  
23 audit that Qwest discusses is not an audit specifically of the Section 272  
24 affiliate and its specific transactions and is not probative of compliance  
25 with Section 272. The FCC has stated that the accounting requirements of

<sup>112</sup> One reason that the FCC applied its existing affiliate transaction rules to transactions between BOCs and Section 272 affiliates was to detect and protect against flows of subsidies. *See Accounting Safeguards Order*, ¶ 176.

<sup>113</sup> *BellSouth Louisiana II Order*, ¶ 340.

<sup>114</sup> Qwest Response to AT&T Multistate Data Request No. 17. "The procedures for capturing affiliate transactions include downloading all payments to and payments from affiliates from the company's financial systems."

<sup>115</sup> Schwartz Affidavit at 28.

<sup>116</sup> *Bell Atlantic New York Order*, ¶ 411, n. 1268. It appears that the FCC reviews the ARMIS data and CAMs to compare the total amount of affiliate transactions. In the footnote to this cite it appears that the FCC relies upon the independent auditor's reviews of ARMIS data. However, Qwest has opted not to have an audit engagement for the year 2000 in 2001. *See Schwartz Affidavit*, at 14, n. 10.

1 section 272 (c )(2) “pertain to the BOC’s ‘dealings’ with its separate  
2 affiliate.”<sup>117</sup>

3 124. Subsequent to my initial and follow-up reviews, I conducted a supplemental on-  
4 site review of QCC’s transactions. Based upon my supplemental review, AT&T continues to  
5 dispute Qwest’s and QCC’s assertions of compliance with Section 272(c)(2).

6 125. Pursuant to Section 272(c)(2), Qwest is required to account for all transactions  
7 with QCC pursuant to accounting principles “designated or approved” by the FCC.<sup>118</sup> Despite  
8 Qwest’s transactions with QCC, its section 272 affiliate, stretching back to July 2000, there was  
9 *no accounting booked until April of 2001* and, thus by definition, Qwest has not met the  
10 requirements of this section which call for adherence to FCC accounting principles including  
11 GAAP. Washington’s ALJ noted that “It appears that Qwest did not follow FCC rules or  
12 Commission regulations governing affiliate transactions with respect to these services.”<sup>119</sup>

13 126. Qwest relies upon the filings of its 10K report and its Cost Allocation Manual  
14 (“CAM”) together with the annual audit as evidence that the BOC accounts for transactions in  
15 accordance with the accounting principles approved by the FCC.<sup>120</sup> Once again, “mere paper  
16 promises” does not equate to compliance. The FCC has stated that an audit of a BOC’s CAM  
17 information and ARMIS data will not conclusively prove compliance with Section 272(c)(2).<sup>121</sup>  
18 Further, as has been noted under the discussion for Section 272(b)(2), this assertion cannot be  
19 true where no affiliated transactions between Qwest and QCC were accounted for during a nine-  
20 month period commencing in July 2000, until April 2001, and where Qwest’s ARMIS data for  
21 QCC affiliated transactions is either underreported or not reported at all. As previously

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<sup>117</sup> *Bell Atlantic New York Order*, ¶ 415.

<sup>118</sup> *Id.* See also, 47 C.F.R. Sec. 32.37

<sup>119</sup> *WA ALJ’s 272 Order*, p. 114.

<sup>120</sup> Schwartz Affidavit at 14, 29

<sup>121</sup> *BellSouth Louisiana II Order*, ¶ 340.

1 discussed, the FCC has stated that the accounting requirements of section 272(c) pertain to the  
2 BOC's "dealings" with the 272 affiliate. The auditor's opinion as to the BOC's 10K report does  
3 not specifically address dealings between Qwest and QCC.

4 127. Qwest's assertion that it "has implemented the proper internal controls and  
5 processes to satisfy the requirements of Section 272(c)"<sup>122</sup> is conclusory. If Qwest had proper  
6 internal controls, then proper GAAP accounting would have been employed and accounting of  
7 billable transactions would have been occurring in a timely manner. Such was not, and has not  
8 been, the case. Qwest has not demonstrated compliance with this section.

9 128. Qwest's asserts that "[n]either the FCC's review ... nor the audits conducted by  
10 independent auditors have revealed discrepancies with [Qwest's] corporate accounting  
11 procedures for affiliate transactions in the past three years."<sup>123</sup> As a result of my on-site reviews,  
12 I have presented discrepancies with Qwest's accounting for affiliated transactions with Qwest  
13 LD and QCC. Such discrepancies are recent and they rebut the presumption of compliance that  
14 Qwest asserts.

15 129. As was previously mentioned, Qwest admitted the failure to account for billable  
16 transactions in the documentation provided to me. On the summary sheets were notes that stated  
17 **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]**

18 Once again, failure to timely bill and reconcile cannot be excused and is a violation of the  
19 FCC's accounting principles. The PUC is urged to inquire as to why these practices were not  
20 accomplished for 2000 activity and what effect that has on Qwest's FCC (ARMIS) and SEC  
21 filings.

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<sup>122</sup> Schwartz Affidavit at 29.

<sup>123</sup> *Id.*, at 28.

1 **G. Section 272(c) (1) – Nondiscrimination Safeguards**

2 130. Section 272(c)(1) establishes requirements for the BOC. Under this section, a  
3 BOC must provide to unaffiliated entities the same goods, services, facilities, and information  
4 that it provides to its Section 272 affiliate at the same rates, terms, and conditions. In other  
5 words, Qwest is required to treat unaffiliated entities as it treats QCC.<sup>124</sup>

6 131. A *prima facie* case of unlawful discrimination under this section is established if  
7 it can be shown that a BOC has not provided an unaffiliated entity with the same goods, services,  
8 facilities, and information that it provides to its Section 272 affiliate at the same rates, terms and  
9 conditions.<sup>125</sup> Neither can the BOC use a third affiliate to provide services to the Section 272  
10 affiliate to circumvent the requirements of this section. To do so would create a loophole around  
11 the separate affiliate requirement.<sup>126</sup>

12 132. Qwest provided copies of documents between a third affiliate known as  
13 U S WEST Advanced Technologies (“AT”) and other Qwest affiliates.<sup>127</sup> Among the agreement  
14 or project reports provided were several between AT and Qwest LD. AT&T believes that  
15 several of the services provided by AT for Qwest LD constitute discrimination in the provision  
16 of information and the development of new services. Failure to also offer such services and  
17 information to an unaffiliated entity constitutes noncompliance with this section.

18 133. Included in these reports were the following projects, with pertinent comments,  
19 where the long distance affiliate was the client or the project had implications for Qwest LD:

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<sup>124</sup> *Non-Accounting Safeguards Order*, ¶ 202.

<sup>125</sup> *Id.*, ¶ 212.

<sup>126</sup> The FCC has stated that the affiliate transaction rules govern “chain transactions” where an unregulated affiliate stands between the BOC and the Section 272 affiliate in the provision of assets, information, or services. *Accounting Safeguards Order*, ¶¶ 183, 251; *Non-Accounting Safeguards Order*, ¶ 309; *Ameritech Michigan Order*, ¶ 373. Because Qwest and QCC are both subsidiaries of Qwest Services Corporation, the possibility exists that QSC is being used, or will be used, to circumvent the nondiscrimination provisions.

<sup>127</sup> Response to AT&T Multistate Data Request No. 16, Confidential Attachment C, Books 1 & 2 (the “Montana

1 [PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]  
2

3 Note that this ties in directly with section 272(g) and concerns about the effect of joint  
4 marketing on the competitive landscape.

5 134. To the extent that these services are offered to Qwest LD and not to other  
6 unaffiliated entities, Qwest is circumventing the non-discrimination safeguards by using AT and  
7 violating the provisions of Section 272(c)(1). To illustrate, using examples (a) and (g) above,  
8 AT was used to develop cost savings for U S WEST LD (n/k/a Qwest LD) for a service that was  
9 uniquely provided by the BOC, U S WEST. This appears to be a circumvention of the  
10 prohibition of the BOC transferring local exchange and exchange access facilities and  
11 capabilities to an affiliate.<sup>128</sup>

12 135. Similarly, Qwest revealed during the Colorado 272 workshop that product  
13 design, planning and development services for Qwest and QCC would be provided by Qwest  
14 Services Corp. (“QSC”) and therefore, such services were not required to be posted, and made  
15 available, to unaffiliated parties.<sup>129</sup> Again, this shifting of services to QSC, the parent of both  
16 Qwest and QCC, appears to be a circumvention of the non-discrimination requirements of this  
17 section.

18 136. Examination of a recent invoice from Qwest to QCC for May, 2001 revealed that  
19 certain financial services (for “Bismarck Bankruptcy” per the work order) were provided for the  
20 time period October 2000 – April 2001. However, the work order was not signed until May 11,  
21 2001. The presumption is that it wasn’t posted until sometime after the signature. Thus, this

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Affiliate Interest Reports filed with the Montana Public Service Commission in 1999 and 2000 for transactions in 1998 and 1999, respectively”).

<sup>128</sup> *Non-Accounting Safeguards Order*, ¶ 309.

1 appears to be a violation of the 10-day posting rule and the provision of services to QCC on a  
2 discriminatory basis.

3 137. Examination of numerous invoices by AT&T revealed that there was a lack of  
4 timely accounting and billing for services rendered to Qwest LD and QCC. The 272 affiliates  
5 have been receiving preferential treatment due to the billing delay and, as such, discriminatory  
6 behavior is present.

7 138. A companion to the above is the historical lack of interest being charged on  
8 outstanding amounts payable by Qwest LD and QCC. Although Qwest claims to have rectified  
9 this situation, I noted at least one invoice from April 2001 where this did not appear to be the  
10 case. **[PUBLIC DOCUMENT – TRADE SECRET DATA HAS BEEN EXCISED]**

11 139. Discrimination may be occurring in relation to Qwest's bill printing and  
12 processing work order.<sup>130</sup> The work order shows a fully distributed cost to QCC of \$ 0.07/page.  
13 Inquiry to AT&T personnel reveals that Qwest is charging AT&T a much higher price. Further  
14 investigation is necessary to determine if Qwest is discriminating on the basis of price as well as  
15 the nature of the service (Qwest provides mailing as well as printing for QCC).

16 140. The FCC noted a number of items that it reviewed to determine if BellSouth was  
17 meeting its nondiscrimination obligation.<sup>131</sup> The items that Qwest has not provided any  
18 information on are as follows:

- 19 a. Qwest has not stated whether it will inform QCC of planned network  
20 outages before public notice is given pursuant to FCC rules.
- 21 b. Qwest has not stated its commitment to continue participating in public  
22 standard-setting bodies.

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<sup>129</sup> A more complete discussion of this matter can be found in the joint marketing section below.

<sup>130</sup> See <http://www.qwest.com/about/policy/docs/qcc/currentDocs.html>

<sup>131</sup> *BellSouth Louisiana II Order*, ¶¶ 342 - 347.

- 1 c. Qwest has not stated that it is committed not to discriminate in favor of  
2 Qwest LD in the “establishment of standards relating to interconnection or  
3 interoperability of public networks.”
- 4 d. Qwest has not stated that it would not discriminate in the processing of  
5 PIC orders.
- 6 e. Qwest has not stated that it would comply with the FCC’s prohibition  
7 against the use of its Official Services Network to provide interLATA  
8 services.
- 9 f. The number of Qwest LD’s or QCC employees, who are former  
10 employees of Qwest, and *vice versa*, creates a concern that there will be an  
11 improper flow of confidential information between the two entities.
- 12 g. Finally, Qwest has not yet proved that it will provide nondiscriminatory  
13 access to its OSS.

14 141. Finally, as has been previously noted, my supplemental review disclosed that  
15 QCC had failed to post its various work and task orders in a timely manner. Thus QCC was  
16 provided goods, services, facilities and information on an exclusive basis for many months.  
17 Such is a *prima facie* case of unlawful discrimination under this section.

18 **H. Section 272(e) – Fulfillment of Certain Requests**

19 142. This section provides for certain requirements in the provision of exchange  
20 service (*i.e.* local service) and exchange access services (*i.e.* switched access services), and  
21 specifically mandates imputation for the BOC’s own provisioning in subsection 272(e)(3) and  
22 mandates nondiscrimination in the provisioning of interLATA or intraLATA facilities or  
23 services to its 272 affiliate in subsection 272(e)(4).

24 143. Qwest states that this section is to ensure “that the BOC treats the 272 Affiliate  
25 similarly to other IXCs with respect to special and switched access.”<sup>132</sup> It further states that  
26 “the 272 Affiliate will be required to pay for access charges under the same rates, terms and

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<sup>132</sup> Schwartz Affidavit at 31.

1 conditions that any other IXC would be charged” and concludes “[t]herefore, there is no unfair  
2 advantage.”<sup>133</sup>

3 144. Given that Qwest’s intrastate switched access rates for Minnesota are multiples  
4 above economic cost (and even its own interstate rates) and contain non-cost based rate elements  
5 such as the carrier common line charge, there is indeed an unfair advantage. This is true because  
6 the BOC is consolidated with the parent company, QSC, which, in turn, is consolidated with  
7 QCI. Also, the 272 Affiliate, QCC, is consolidated. Thus, Qwest is merely paying out access  
8 charges from one pocket and transferring to another.<sup>134</sup>

9 The mandate in 272(e)(3) should be of particular concern in light of the recent order  
10 issued by the Kansas Corporation Commission. The Kansas Commission has recently opened a  
11 docket, on its own motion, to investigate whether the rates and practices of Southwestern Bell  
12 Communications (“SBC”) and the 272 affiliate (“SBCS”) in offering long distance services are  
13 unjust, unreasonably discriminatory, or unduly preferential.<sup>135</sup> The PUC should review and use  
14 this section *before* Qwest is granted interLATA authority as a safeguard against anti-competitive  
15 pricing that will result in price squeezes.

16 145. The Kansas Commission further agreed to investigate allegations that preferential  
17 pricing from Southwestern Bell Telephone Company (“SWBT”) was occurring where access  
18 revenue was being collected by SWBT and then reinvested in SBCS to allow the latter to price  
19 long distance at or below cost.<sup>136</sup> This method of preferential pricing implicates Section  
20 272(e)(4), which requires that services or facilities must be “made available to all carriers at the

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<sup>133</sup> *Id.* at 32.

<sup>134</sup> At least two states, Montana and Arizona, have current dockets to examine Qwest’s above cost access rates and the interplay of such with the section 271 application process.

<sup>135</sup> *Order on Petitions to Intervene, Emergency Motion for Suspension of Specific Rate Tariffs, and Petition for Reconsideration or Modification*, Docket Nos. O1-SBLC-693-TAR, O1-SBLC-323-TAR, and O1-SBLC-594-TAR.

<sup>136</sup> *Id.* at 17.

1 same rates and on the same terms and conditions, and ... the costs are appropriately allocated.”  
2 It is worth repeating that the Section 272 standards for compliance are set out in the FCC’s  
3 *Accounting and Non-Accounting Safeguards Orders*, which were designed to “discourage and  
4 facilitate the detection of improper cost allocation and cross-subsidization between the BOC and  
5 its Section 272 affiliate.”<sup>137</sup> The FCC recognized the practical impact of improper cost  
6 allocation: “an overallocation of costs to the BOC’s local operations means an underallocation of  
7 costs to the affiliate’s long-distance operations, which would allow the affiliate to undercut  
8 inefficiently its interexchange competitors by providing a long-distance service at a low price  
9 that underestimates the true costs of that service.”<sup>138</sup>

10 146. Qwest has already displayed its intent in its filing to obtain pricing flexibility for  
11 its intraLATA toll services in the State of Colorado. Qwest applied for the premature  
12 elimination of the requirement to impute switched access rates into the price floor for the  
13 provision of intraLATA toll services. The Colorado Commission, in rejecting this application,  
14 wisely stated:

15 Before we eliminate the current imputation requirement for switched access,  
16 Qwest *must demonstrate* that there are comparable (in quality), widely-available,  
17 economically-feasible, and price-constraining alternatives to Qwest’s switched  
18 access services.<sup>139</sup>

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<sup>137</sup> *Application of Verizon New England Inc., Bell Atlantic Communications, Inc. (d/b/a Verizon Long distance), NYNEX Long Distance Company (d/b/a Verizon Enterprise Solutions) and Verizon Global Networks Inc., For Authorization to Provide In-Region, InterLATA Services in Massachusetts*, CC Docket No. 01-9, Memorandum Opinion and Order, FCC 01-130 (Rel. April 16, 2001), ¶ 226 (“*Verizon 271 Order*”).

<sup>138</sup> *Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended*, CC Docket No. 96-149, Second Order on Reconsideration, FCC 97-222 (Rel. June 24, 1997), ¶ 12.

<sup>139</sup> *Application of U S WEST Communications, Inc., for the Commission to Open an Investigatory Docket to Eliminate on an Expedited Basis the Requirement that U S WEST Impute Switched Access Rates into the Price Floor of its IntraLATA Long Distance Service*, Decision Denying Exceptions, Adopted January 24, 2001, Colorado Docket No. 00A-201T, Section 5, at 13 (emphasis added).

1           147. Qwest states that the requirements of Section 272 are “designed to prohibit anti-  
2 competitive behavior, discrimination, and cost shifting.”<sup>140</sup> From a review of the Section 272  
3 affiliate website it is apparent that Qwest is, and will be, performing many functions for QCC  
4 and correspondingly will have multiple opportunities to engage in cost shifting. The  
5 Commission should minimize these opportunities by mandating that QCC include the long-run  
6 incremental costs associated with these functions in the price floor and impute tariff rates for  
7 access charges and other tariffed services.<sup>141</sup>

8           148. Given the current environment where the conventional wisdom is that toll service  
9 will soon be bundled, below cost or free, with high-end data service, the PUC also should assure  
10 itself, as Colorado did in the switched access imputation case, that Qwest and QCC will adhere  
11 to the provisions of Section 272(e) by implementing the suggestions listed in the paragraph  
12 below. To not do so may invite a “Kansas scenario” where the Kansas Commission finds itself  
13 in an investigation docket a month after the FCC permitted SBCS to provide long distance  
14 service.

15           149. The FCC has provided guidance in several of its past orders as to what evidence it  
16 will look at in determining compliance with section 272(e).<sup>142</sup> Based on a review of past FCC  
17 orders, Qwest’s affidavit is lacking in the following respects.

- 18           a. Qwest and QCC did not provide specific performance standards for  
19 measuring its requirements of Section 272(e)(1).
- 20           b. Qwest has yet to prove nondiscriminatory access to its OSS, and this may  
21 result in a finding that Qwest does not comply with Section 272(e)(1).
- 22           c. There presently is no performance measure or measures for access. Qwest  
23 should be required to develop such a measure or measures, obtain

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<sup>140</sup> *Id.* at 2.

<sup>141</sup> For example, a QCC work order for the “Sales of QCC Products and Services”, that includes Qwest’s service in selling QCC’s out-of-region long distance, is estimated to cost QCC over \$3 million/year. It would be expected that such cost would be included into QCC’s price floor so that it is not offering long distance services below cost.

<sup>142</sup> See generally, *BellSouth Louisiana II Order*, *Bell Atlantic New York Order*.

1 approval of the measures, and demonstrate that it is prepared to collect and  
2 report this data.

3 d. Given the recent developments in Kansas and the Commission's ruling in  
4 Colorado, a concrete statement should be made by Qwest that imputation  
5 will be implemented for all services, which includes interLATA and  
6 intraLATA long distance services, in order to fully comply with the non-  
7 discrimination requirements.<sup>143</sup>

8 e. Qwest has made no affirmative assurance that it will maintain records  
9 tracking the quality of service to QCC for telephone exchange and  
10 exchange access services,<sup>144</sup> nor whether such will be posted to its  
11 website.

## 12 **I. Section 272 (g) -- Joint Marketing**

### 13 **1. Overview**

14 150. Qwest and QCC, in their affidavits, provide broad and vague and often untrue  
15 assertions as to QCC's compliance with Section 272(g) and rely heavily on the *BellSouth South*  
16 *Carolina Order*. Qwest states that "... it is critical to recognize that once the BOC obtains  
17 Section 271 approval, the BOC and the 272 Affiliate may jointly market services without regard  
18 to the nondiscrimination provisions of Section 272(c)."<sup>145</sup> But, that is not true as certain  
19 activities remain subject to the nondiscrimination provisions. Such a broad statement is typical  
20 of Qwest's blithe approach to its compliance with this section.

21 151. Although Section 272(g)(3) provides that certain activities permitted under  
22 subsection (g) are not be considered to violate the nondiscrimination provisions of Section  
23 272(c), the FCC clarified this subsection in its *Non-Accounting Safeguards Order*:

24 Some of the activities identified by the parties appear to fall clearly within  
25 the scope of Section 272(g)(3) and hence would be excluded from the  
26 Section 272(c) nondiscrimination requirements. For example, activities

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<sup>143</sup> BellSouth stated that if its Section 272 affiliate used exchange access for the provision of its own service, BST (the BOC) would impute to itself the same amount it would charge an unaffiliated interexchange carrier. *BellSouth Louisiana II Order*, ¶ 354.

<sup>144</sup> *Verizon 271 Order*, ¶ 230, n 746.

<sup>145</sup> Schwartz Affidavit at 32.

1 such as customer inquiries, sales functions, and ordering, appear to  
2 involve only the marketing and sale of a Section 272 affiliate's services, as  
3 permitted by Section 272(g). *Other activities identified by the parties,*  
4 *however, appear to be beyond the scope of Section 272(g), because they*  
5 *may involve BOC participation in the planning, design, and development*  
6 *of a Section 272 affiliate's offerings. In our view, such activities are not*  
7 *covered by the Section 272(g) exception to the BOC's nondiscrimination*  
8 *obligations.*<sup>146</sup>

9 152. This begs the question of what activities are subject to the nondiscrimination  
10 requirements. The FCC stated that “[w]e see no point to attempt at this time to compile an  
11 exhaustive list of the specific BOC activities that would be covered by section 272(g). We  
12 recognize that *such determinations are fact specific and will need to be made on a case-by-case*  
13 *basis.*”<sup>147</sup>

14 153. Qwest's affidavit specifically discussing section 272(g) fails to provide adequate  
15 evidence of a program of compliance with this section.<sup>148</sup> Qwest's “Section 272 Employee  
16 Training” does contain a brief mention of section 272(g) provisions which states that section  
17 272(g) “Provides one clear exception to Section 272(c) nondiscrimination requirements – Once  
18 Section 271 authority is secured, QC may jointly market in-region, interLATA long distance  
19 services with QCC.”<sup>149</sup> Thus, even the brief mention in the employee training is couched in  
20 terms of what Qwest can do free of the nondiscrimination safeguards. It does not advise  
21 employees that certain joint activities such as product design, planning and/or development  
22 services are still subject to the nondiscrimination safeguards contain in section 272(c).

23 154. Qwest's affidavit fails to state QCC's intention to market information services  
24 and whether Qwest will also permit other information service providers to market and sell  
25 telephone exchange services. Rather, Qwest relies on a hypothetical “if” scenario that does not

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<sup>146</sup> See *Non-Accounting Safeguards Order*, ¶ 296 (emphasis added).

<sup>147</sup> *Id.* (emphasis added)

<sup>148</sup> *Bell Atlantic New York Order*, ¶ 419.

1 rise to the requisite intent.<sup>150</sup> Such failure means that Qwest has not demonstrated that it will  
2 comply with section 272(g)(1).<sup>151</sup>

3 155. A recent Order in the instant docket granted a motion to compel discovery that  
4 includes marketing scripts and plans.<sup>152</sup> The PUC should carefully review and, if necessary  
5 require modifications to, Qwest's joint marketing scripts and related marketing activities with  
6 QCC. Given the effect that other BOCs' entry into interLATA services has had on the  
7 competitive landscape in New York and Texas,<sup>153</sup> close scrutiny is warranted to mitigate Qwest's  
8 ability to leverage its status as the dominant local exchange provider. Qwest should not be  
9 allowed to use the cloak of secrecy, especially regarding marketing scripts, to shield the impact  
10 of its joint marketing on the competitive landscape in Minnesota.

11 156. Section 272 (g)(2) prohibits Qwest from marketing interLATA services provided  
12 by QCC until authorized to do so under section 271(d). Qwest has been violating this section  
13 and its assertion that it "does not currently market ... in-region, interLATA services" is untrue.<sup>154</sup>  
14 As was discussed in a recent filing by the Minnesota Attorney General (on behalf of the  
15 Minnesota Department of Commerce) in July 2001, Qwest began marketing QCC's interLATA  
16 services by running an ad in the *Minneapolis Star-Tribune*.<sup>155</sup> We are in agreement with the

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<sup>149</sup> Schwartz Affidavit, Exhibit MES-272.16, p. 12.

<sup>150</sup> *Id.* at 32.

<sup>151</sup> *BellSouth Louisiana II Order*, ¶ 356.

<sup>152</sup> *In the Matter of a Commission Investigation Into Qwest's Compliance with Section 272 of the Telecommunications Act of 1996's Separate Affiliate Requirements*, Docket No. P-421/CI-01-1372, Minnesota Public Utilities Commission, November 20, 2001, *Fourth Prehearing Order and Order Compelling Discovery*. ("272 Discovery Order").

<sup>153</sup> On its web-based "Public Policy" page, Qwest boasts: "The response to Verizon's and SBC's entry into the long-distance market is astounding. In six months, more than one million customers in New York have signed up with Verizon's long-distance service. SBC is signing up customers just as fast in Texas." Such statements and statistics underscore the incredible advantage the local monopoly BOC has once Section 271 approval is granted and concretely demonstrates the regional remonopolization of telephone services by the BOCs.

<sup>154</sup> Schwartz Affidavit at 32.

<sup>155</sup> *In the Matter of a Commission Investigation Into Qwest's Compliance with Section 272 of the Telecommunications Act of 1996's Separate Affiliate Requirements*, Docket No. P-421/CI-01-1372, Minnesota Public Utilities Commission, November 15, 2001, *Supplemental Memorandum of Law in Support of its Motion to*

1 Attorney General's conclusion that Qwest has commenced the joint marketing of QCC's  
2 interLATA long-distance, and such is a violation of section 272 (g)(2). The PUC should demand  
3 of Qwest whatever is necessary to restore the competitive landscape and mitigate the  
4 discriminatory advantage gained by QCC over its competitors.

5 157. As discussed above, QCC revealed for the first time in Colorado Section 272  
6 workshops that marketing-related services such as product design, planning and development  
7 services for QC and QCC would be provided by Qwest Services Corporation ("QSC") and that  
8 such services are not required to be posted and made available to unaffiliated parties.<sup>156</sup> In  
9 previous written testimony, Qwest and QCC gave the impression that joint design, planning and  
10 development services would be posted and made available and certainly never mentioned that  
11 QSC would provide such services.

12 158. QSC is not just another services affiliate; it is the direct parent or owner of both  
13 QC and QCC. By shifting services to Qwest Services Corp., QC and QCC can now participate  
14 in joint planning, design and development free of the strictures of the section 272-  
15 nondiscrimination safeguards. This "shell game" is emblematic of QC's approach to section 272  
16 to circumvent where possible and accomplish the bare minimum to pass the form test. The PUC  
17 should carefully weigh these and other Qwest machinations when tendering its recommendation  
18 to the FCC.

19 159. To balance the BOC's joint marketing of its section 272 affiliate's services, the  
20 FCC stated<sup>157</sup> that the BOC must also fulfill the equal access requirements of Section 251(g)  
21 described in the *Non-Accounting Safeguards Order*.<sup>158</sup> Qwest must inform callers that they have

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*Compel Discovery*, at pp. 5 – 6.

<sup>156</sup> Colorado TR 92, 84, 89 – 90.

<sup>157</sup> *BellSouth South Carolina Order*, ¶ 239.

<sup>158</sup> *Non-Accounting Safeguards Order*, ¶ 292.

1 a choice of long distance carriers and offer to read, in random order, the names and, if requested,  
2 the telephone numbers of all available interexchange carriers. Qwest has not made this  
3 affirmative statement in its affidavit. The PUC should require that Qwest do so.

#### 5 VI. PAST HISTORY AND FUTURE COMPLIANCE

6 160. "Those who do not remember the past are condemned to repeat it." This quote is  
7 especially apt in the context of Section 272(g). The FCC has stated, "[p]ast and present behavior  
8 of the BOC applicant provides the best indicator of whether [the applicant] will carry out the  
9 requested authorization in compliance with Section 272."<sup>159</sup>

10 161. In developing a record and determining what weight to give to the evidence  
11 presented in Qwest's Section 271 application, the PUC and the FCC should look through the  
12 prism of Qwest's (and the former U S WEST's) rich history of violations pertaining to Section  
13 271. Such history should be part of the calculus in determining whether the evidence provided  
14 by Qwest, QCC and Qwest LD is sufficient to demonstrate that they will comply with the  
15 requirements of Section 272.

16 162. In September 1999, the FCC found that the former U S WEST's "provision of  
17 nonlocal directory assistance service to its in-region subscribers constitutes the provision of in-  
18 region, interLATA service as defined in Section 271(a) of the Act."<sup>160</sup> U S WEST had petitioned  
19 for forbearance from the requirements of Section 272 to provide nonlocal directory assistance  
20 service. In essence, U S WEST was attempting to carve out an exception for itself as to the  
21 requirements of Section 272.

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<sup>159</sup> *Bell Atlantic New York Order*, ¶ 402.

<sup>160</sup> See *Petition of U S WEST Communications, Inc. for a Declaratory Ruling Regarding the Provision of National Directory Assistance*; *Petition of U S WEST Communications, Inc. for Forbearance*, CC Docket No. 97-172,

1           163. The FCC wrote: "... the record indicates that U S WEST refuses to provide  
2 unaffiliated entities with access to all of the telephone numbers that it uses to provide nonlocal  
3 directory assistance service..." and "[t]he record further reveals that U S WEST does not provide  
4 unaffiliated entities with access to the in-region telephone numbers it uses to provide nonlocal  
5 directory assistance at the same rates, terms and conditions it imputes for itself."<sup>161</sup> The FCC  
6 recognized that U S WEST had a competitive advantage in the provisioning of directory  
7 assistance service by virtue of the fact that it had a "...more complete, accurate, and reliable  
8 database than its competitors."<sup>162</sup>

9           164. In its order, the FCC concurred with AT&T's position that "Section 272 seeks to  
10 prevent BOCs from, among other things, leveraging their monopoly over local exchange services  
11 into interLATA markets."<sup>163</sup> The FCC recognized that Section 272 was a bulwark to prevent a  
12 BOC such as U S WEST (and now Qwest) from unfairly using its dominant position and  
13 monopoly power to gain an unfair competitive advantage not only in an incidental service like  
14 directory assistance, but especially with regard to in-region, interLATA service.<sup>164</sup> The FCC  
15 ordered U S WEST to "make available to unaffiliated entities all of the in-region directory listing  
16 information it uses to provide region-wide directory assistance service at the same rates, terms,  
17 and conditions it imputes to itself. Thus, to the extent U S WEST charges unaffiliated entities  
18 for the in-region directory information it uses to provide nonlocal directory assistance on an  
19 integrated basis, it must impute to itself the same charges."<sup>165</sup>

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Memorandum Opinion and Order, FCC 99-133 (Rel. Sept. 27, 1999), ¶¶ 2, 63.

<sup>161</sup> *Id.*, ¶ 34.

<sup>162</sup> *Id.*, ¶ 35.

<sup>163</sup> *Id.*, ¶ 52, n. 111.

<sup>164</sup> *Id.*, ¶ 54.

<sup>165</sup> *Id.*, ¶ 37 (footnotes omitted).

1           165.   Furthermore, the FCC concluded that "U S WEST's provision of nonlocal  
2   directory assistance service to its in-region subscribers constitutes the provision of in-region,  
3   interLATA service."<sup>166</sup>

4           166.   On or about May, 1998, Qwest entered into two separate business agreements  
5   with Ameritech and with U S WEST to provide Qwest's long distance service under their own  
6   brand names before these two BOCs had gained Section 271 authorization to provide in-region  
7   long distance service. On September 28, 1998, the FCC issued its Memorandum Opinion and  
8   Order, which found that Qwest, the former U S WEST Communications, Inc., and Ameritech  
9   Corp. had violated Section 271 by entering into the agreement and providing Qwest's long  
10   distance service.<sup>167</sup> The FCC wrote: "It is clear on this record that Ameritech's and U S WEST's  
11   business arrangements with Qwest pose the competitive concerns that Section 271 seeks to  
12   address, and we accordingly find them unlawful under the Act."<sup>168</sup>

13           167.   The illegal marketing alliance entered into by Qwest and U S WEST was an  
14   attempt to flout the plain requirements of Section 271 of the Act. Qwest and U S WEST's  
15   argument before the FCC basically was that their clearly calculated attempt to circumvent  
16   Section 271 should be excused because the marketing alliances would serve the public interest.  
17   The FCC noted that in its internal strategy sessions, U S WEST recognized the benefits of  
18   offering a combined package of services and began considering how to offer in-region  
19   interLATA service prior to Section 271 approval and quoted one of U S WEST's admitted goals  
20   to "[p]reposition customers for U S WEST Long Distance by providing the convenience of one-

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<sup>166</sup> *Id.*, ¶ 63.

<sup>167</sup> See *AT&T v. Ameritech Corporation et al.*, File Nos. E-98-41, E-98-42 and E-98-43, Memorandum and Opinion and Order, FCC 98-242 (Rel. Oct. 7, 1998), ¶¶ 38, 64.

<sup>168</sup> *Id.*, ¶ 52.

1 stop shopping.”<sup>169</sup> Upon completion of the negotiations with Qwest to provide its interLATA  
2 services, U S WEST commenced an aggressive marketing campaign in six of its states that  
3 included marketing through inbound telemarketing.<sup>170</sup>

4 168. The FCC found that the record indicated that U S WEST was actively  
5 recommending Qwest’s long distance service over other IXC’s service (“U S WEST’s marketing  
6 materials instruct its representatives to encourage its customers to select Qwest over all other  
7 long distance carriers.”).<sup>171</sup>

8 169. Violations of Section 271 are not limited to pre-merger U S WEST  
9 Communications, Inc. On February 16, 2001, the FCC released its Opinion and Order that  
10 concluded that Qwest was providing in-region, interLATA service in violation of Section 271.<sup>172</sup>  
11 Through its 1-800-4USWEST calling card service, the FCC found the following: (1) U S WEST  
12 was permitted to accumulate “a significant base of customers”; (2) it was enabled to “amass  
13 goodwill as a full-service provider with its local service customers”; (3) it held itself out as  
14 providing long distance service through promotional materials; and (4) it controlled “numerous  
15 functions, including marketing and customer care, that are typically performed by a reseller of  
16 long distance service.”<sup>173</sup>

17 170. Because of its initial conclusion and findings, the FCC passed on consideration of  
18 other claims, including discrimination in providing transport services and circumvention of  
19 Section 272 safeguards.

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<sup>169</sup> *Id.*, ¶¶ 14, 41.

<sup>170</sup> *Id.*, ¶ 16.

<sup>171</sup> *Id.*, ¶ 60.

<sup>172</sup> *AT&T Corp. v. U S WEST Communications, Inc.*, File No. E-99-28, Memorandum Opinion and Order, DA01-418 (Rel. Feb. 16, 2001).

<sup>173</sup> *Id.*, ¶ 30.

1           171. Among the evidence that was presented to the FCC was U S WEST's marketing  
2 tactics of using bill inserts and other mailings aimed at its local subscriber base and exercising  
3 exclusive control over the marketing of the service.<sup>174</sup>

4           172. On April 16, 2001, Arthur Andersen, LLP released its post-merger Report on  
5 Qwest Communications International, Inc.'s Statement of Management Assertions dated  
6 April 16, 2001. The Statement was required by the FCC order approving the merger of  
7 U S WEST, Inc. and Qwest Communications International, Inc. Attachment I to the Report of  
8 Independent Public Accountants states that the auditors "noted that the account records of 458  
9 customers included prohibited in-region InterLATA service component codes." Of these,  
10 "certain non-metered services (e.g., private line services) for 266 customers were billed and  
11 branded as Qwest services."

12           173. The audit report raises questions whether Qwest's parent was unlawfully  
13 providing Section 271 long distance services *after* the merger. In a subsequent letter Arthur  
14 Andersen has adjusted the number of incorrectly billed customers from 266 to 255.<sup>175</sup> Also,  
15 despite the merger between U S WEST and QCI occurring almost eleven (11) months ago, the  
16 independent auditor is unable to proffer an opinion as to Qwest's management assertions. On  
17 page one of the letter, Arthur Andersen states that it has "not yet completed our work and  
18 accordingly, we are unable to express, and we do not express, any opinion on management's  
19 assertions [regarding their compliance with the Final Divestiture Plan] as of any date or for any  
20 period subsequent to April 16, 2001."<sup>176</sup>

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<sup>174</sup> *Id.*, ¶ 3.

<sup>175</sup> Letter from Arthur Andersen LLP to Dorothy Atwood (June 6, 2001) and filed with the FCC's Common Carrier Bureau (discussing audit of Qwest's required divestiture of its in-region interLATA services and pursuant to CC Docket No. 99-272).

<sup>176</sup> *Id.*

