

Attachment 9

Before the
STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS
FOR THE MINNESOTA PUBLIC UTILITIES COMMISSION

In the Matter of a Commission
Investigation into Qwest's
Compliance with Section 272 of the
Telecommunications Act of 1996's
Separate Affiliate Requirement

PUC Docket No. P-421/CI-01-1372
OAH Docket No. 7-2500-24487-2

Affidavit

of

LEE L. SELWYN

on behalf of the

Minnesota Department of Commerce

December 5, 2001

REDACTED VERSION

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AFFIDAVIT OF LEE L. SELWYN

1 Introduction and Summary

2

3 Lee L. Selwyn, of lawful age, declares and says as follows:

4

5 1. My name is Lee L. Selwyn; I am President of Economics and Technology, Inc.
6 ("ETI"), Two Center Plaza, Suite 400, Boston, Massachusetts 02108. ETI is a research and
7 consulting firm specializing in telecommunications and public utility regulation and public
8 policy. My Statement of Qualifications is annexed hereto as Attachment 1 and is made a part
9 hereof.

10

1 2. I have presented testimony before this Commission on a number of occasions dating
2 back to the mid-1970s. I have testified in a number of Northwestern Bell rate cases, Docket
3 P-421/GR-75-496 for the Minnesota Retail Federation, in Dockets 77-1509, 79-388, 80-306
4 and 79-388 on Remand for the Minnesota Department of Public Service, in Docket 83-102
5 and in Docket 83-600 on behalf of the Minnesota Business Utility Users Council (MBUUC).

6

7 3. In the late 1970s and early 1980s, I served as a consultant to the Minnesota
8 Department of Public Service in connection with several matters before the (then) Minnesota
9 Public Service Commission. This work involved the development of a specialized data base
10 management and retrieval system and the creation of a data base containing over 100,000
11 elements of information covering the more than one hundred operating telephone companies
12 and the nearly 700 telephone exchanges under the Department's administrative jurisdiction.
13 This effort was undertaken as part of the Minnesota Statewide Telecommunications Policy
14 Guidelines Development project. In addition, I also served as a DPS Staff witness in two
15 Northwestern Bell general rate cases and in a case involving the Restructured Private Line
16 (RPL) tariff.

17

18 4. I have participated in numerous regulatory proceedings involving public utility
19 affiliate relationships and inter-affiliate transactions and transfers. These have included
20 merger proceedings before the California PUC involving Pacific Telesis Group and SBC, and
21 Bell Atlantic and GTE, before the Illinois Commerce Commission involving SBC and
22 Ameritech, before the Connecticut Department of Public Utility Control involving SBC and
23 SNET, and before the Maine PUC involving NYNEX and Bell Atlantic. I also participated in
24 written comments filed with the FCC regarding both the SBC/Ameritech and Bell

1 Atlantic/GTE merger applications. I have participated in a number of Section 271
2 proceedings, including those in Pennsylvania, New Jersey and California. I have also
3 submitted testimony before several state commissions addressing proposals for structural
4 separation of ILEC wholesale and retail operations. I participated in proceedings before the
5 California PUC involving Pacific Bell's reorganization of its Information Services" (primarily
6 voice mail) business into a separate subsidiary, and the spin-off of Pacific Telesis Group's
7 wireless services business into a separate company. I have participated in a number of
8 matters involving the treatment of transfers of yellow pages publishing from the ILEC to a
9 separate directory publishing affiliate, including the recent case before the Washington
10 Utilities and Transportation Commission addressing imputation of (then) US WEST yellow
11 pages revenues. Here in Minnesota in the early 1980s, I sponsored testimony addressing the
12 affiliate transactions between (then) Northwestern Bell and Bell Telephone Laboratories for
13 the so-called "Business Information Systems" development activity. Most of these
14 engagements were on behalf of commission staffs and state consumer/ratepayer advocacy
15 agencies.

16

17 5. I have been asked by the Telecommunications Division of the Minnesota Department
18 of Commerce ("DOC" or "Department") to review the evidence being offered by Qwest
19 Corporation ("Qwest," "Qwest BOC," or "Company") in connection with its forthcoming
20 application, to be filed with the FCC and with the Minnesota PUC pursuant to Section
21 271(d)(2)(B), for authority under Section 271 of the *Telecommunications Act of 1996*
22 ("TA96" or "Act") to provide in-region interLATA long distance services within the State of
23 Minnesota. As part of my analysis, I have been asked to provide an assessment of the
24 Company's claims as to the current state of competition in the Minnesota local telecommuni-

1 cations market, to provide an analysis of the potential impact upon competition in the
2 Minnesota interLATA long distance market that would result from Qwest's entry into the
3 long distance market while the Company continues to maintain overwhelming dominance of
4 the local telephone service market in the state, and to provide an opinion as to whether "the
5 requested authorization is consistent with the public interest, convenience, and necessity." In
6 addition to my review of the Application, testimony and supporting exhibits filed by Qwest in
7 this proceeding, I have also reviewed the Company's responses to data requests propounded
8 by the DOC and by other parties. Copies of the Qwest responses to which I will refer are
9 provided in Attachment 2 to this Affidavit.

10

11 **Qwest has interpreted and applied the structural separation requirements of Sections**
12 **272(a) and (b) as permitting the long distance affiliate to so extensively "contract" with**
13 **the BOC for sales, marketing, billing and other services as to effectively create what**
14 **amounts to a fully integrated operation of its local and long distance businesses.**

15

16 6. The purpose of this Affidavit is to address Qwest's claims as to its compliance with
17 the "separate affiliate" requirements set out at Sections 272(a) and 272(b) of the *Act*. In
18 Affidavits submitted on behalf of Qwest by Judith L. Brunsting and Marie E. Schwartz, the
19 Company indicates that it intends to engage in "joint marketing" of local exchange services
20 provided by Qwest Corporation (the "Qwest BOC") and interLATA long distance services to
21 be provided by its Section 272(a) long distance affiliate, Qwest Communications Corporation
22 ("QCC" or "272 Affiliate"), once it receives Section 271 authority.¹ "Joint marketing" is an
23 activity that is permitted (or more accurately, not prohibited) by Section 272(g) of the *Act*. A
24 "joint marketing" program of the type being contemplated by Qwest will necessarily involve

25 1. Schwartz (QC), at 32-33.

1 the use by both the BOC and long distance entities of a common pool of personnel,
2 equipment, real estate, and various other corporate resources. As I will discuss, Ms.
3 Brunsting and Ms. Schwartz maintain that the use of this common pool of resources is
4 permitted by the Section 272(g) "joint marketing" provisions.

5

6 7. A BOC's ability to engage in joint marketing of its own local services with its
7 affiliate's long distance service is found at Sections 272(g)(2) and (3) of the 1996 *Act*:

8

9 272(g)(2): BELL OPERATING COMPANY SALES OF AFFILIATE
10 SERVICES— A Bell operating company may not market or sell interLATA
11 service provided by an affiliate required by this section within any of its in-
12 region States until such company is authorized to provide interLATA services in
13 such State under section 271(d).

14

15 272(g)(3): RULE OF CONSTRUCTION— The joint marketing and sale of
16 services permitted under this subsection shall not be considered to violate the
17 nondiscrimination provisions of subsection (c).

18

19 The "nondiscrimination provisions" being referred to here are found at subsection (c)(1) of
20 Section 272:

21

22 (c) NONDISCRIMINATION SAFEGUARDS— In its dealings with its affiliate
23 described in subsection (a), a Bell operating company--

24

25 (1) may not discriminate between that company or affiliate and any other entity
26 in the provision or procurement of goods, services, facilities, and information, or
27 in the establishment of standards.

28

29 But subsection 272(c)(2), which is *not* superseded by subsection 272(g)(3) (which refers
30 specifically to "the nondiscrimination provisions of subsection (c)") and thus applies to all
31 joint marketing activities as well, states that a Bell operating company

31

1 (2) shall account for all transactions with an affiliate described in subsection
2 (a) in accordance with accounting principles designated or approved by the
3 Board.
4

5 Hence, the *Telecommunications Act* does not so much *permit* BOC joint marketing of its
6 affiliate's long distance service, but rather does not expressly prohibit it. Rather, the *Act*
7 merely sanctions the operation of a BOC, having satisfied the requirements of Section 271(c),
8 to enter into the long distance arena and to jointly market its (local) services with the long
9 distance services being offered by the Section 272(a) affiliate, subject to all of the separate
10 affiliate provisions set forth at Section 272(b). *Nothing in subsection 272(g)(3) in any way*
11 *exempts Qwest or its Section 272(a) interLATA affiliate QCC from the requirements of*
12 *Section 272(b) with respect to any "joint marketing" activities.*

13

14 8. Structural separation of the BOC and long distance entities is required by Section
15 272(a) for the first three (3) years following Qwest's receipt of Section 271 authority in a
16 particular state, and may thereafter be extended indefinitely by the FCC. Interactions between
17 the structurally separated BOC and long distance entities with respect to the use or provision
18 of common or shared resources must conform to a set of five conduct provisions set out at
19 Section 272(b), which require that Qwest's long distance affiliate:

20

21 (1) shall operate independently from the Bell operating company;

22

23 (2) shall maintain books, records, and accounts in the manner prescribed by
24 the Commission which shall be separate from the books, records, and
25 accounts maintained by the Bell operating company of which it is an
26 affiliate;

27

28 (3) shall have separate officers, directors, and employees from the Bell
29 operating company of which it is an affiliate;

1 (4) may not obtain credit under any arrangement that would permit a
2 creditor, upon default, to have recourse to the assets of the Bell
3 operating company; and
4

5 (5) shall conduct all transactions with the Bell operating company of which
6 it is an affiliate on an arm's length basis with any such transactions
7 reduced to writing and available for public inspection.
8

9 The various interactions described in the two Qwest Affidavits submitted in this docket
10 embrace a broad range of corporate activities and functions, the nature and extent of which
11 raise serious questions as to the actual, *de facto* extent of "separation" that will prevail in
12 practice as between these two supposedly separate corporate units. A significant portion,
13 although by no means all, of these interactions center around the "joint marketing" activity.
14 It is for this reason that the Department of Commerce sought discovery of the specific
15 marketing plans, marketing scripts and associated employee training materials that Qwest will
16 utilize in support of the "joint marketing" activity.² When Qwest declined to provide this
17 information in response to DOC information requests, the Department on November 9, 2001
18 filed a Motion with the Administrative Law Judge to Compel Qwest to produce this material.
19 The Department's Motion was granted on November 20 in the ALJ's *Fourth Prehearing*
20 *Order*. The ALJ's ruling permits parties to supplement their December 5, 2001 submissions
21 with additional testimony arising from their examinations of the joint marketing materials, and
22 I would therefore anticipate that I will be submitting a supplemental affidavit with respect to
23 those materials at a later date.
24

25 2. Qwest response to DOC 15032.

1 9. In my view, the permissive “joint marketing” language at Section 272(g) only implies
2 the right of a BOC and its long distance affiliate to *collaboratively* (“jointly”) participate in
3 marketing activities with respect to their respective local and long distance offerings). Read
4 in the context of the structural separation requirements of Sections 272(a) and (b), it does not,
5 and should not be interpreted to, permit the long distance affiliate to effectively *transfer*
6 virtually all of its long distance service sales and marketing activities to the BOC affiliate by,
7 for example, contracting for services of the affiliate’s employees to perform what amounts to
8 the full extent of the long distance affiliate’s sales and marketing functions. Such an
9 arrangement would have the effect of creating what amounts to fully integrated operation of
10 the local and long distance businesses, and as such would effectively make the Section 272(a)
11 separate affiliate requirement a nullity.

12
13 10. The purpose of the Section 272(a) separate affiliate requirement and the Section
14 272(b) code of conduct was *and is* to forestall the potential for discriminatory and anti-
15 competitive conduct arising out of the ability, as an *economic* matter, for the Qwest BOC to
16 extend its market power in the *local* telecommunications market into the adjacent long
17 distance market.³ The Commission’s evaluation of Qwest’s compliance with the separate
18 affiliate requirements of Sections 272(a) and (b) must be made in the context of the history
19 and background that gave rise to the separate affiliate requirement in the 1996 federal
20 legislation. That history begins with the US Department of Justice’s 1974 antitrust case

21 3. *Conference Report on S. 652, Telecommunications Act of 1996* (House of
22 Representatives- February 01,1996) Congressional Record, H1171.

1 against the pre-divestiture Bell System⁴ in which the DoJ alleged, *inter alia*, that the Bell
2 companies were using their local service monopoly to prevent competition in the adjacent
3 long distance market. The *Modification of Final Judgment* (“MFJ”), the 1982 Consent
4 Decree under which the former Bell System was broken up and the Bell Operating
5 Companies (“BOCs”) were divested from AT&T,⁵ prohibited the divested BOCs from
6 offering interLATA long distance services. This *structural remedy* was adopted in order to
7 prevent the BOC local service monopolies from using their monopoly market power in the
8 local services market to block competition in the adjacent long distance market. And because
9 the BOCs were themselves precluded from providing long distance services, they were made
10 to be *indifferent* as to which long distance carrier their customers might individually select.
11 Section 271 of the federal *Telecommunications Act of 1996* replaced the MFJ long distance
12 “line of business” restriction with a process by which BOCs could enter the “in-region” long
13 distance market, provided that they implemented a series of specific measures that would
14 have the effect of irreversibly opening their previously monopolized local telecommunications
15 markets to competitive entry. To the extent that the *local* market itself becomes competitive,
16 the BOCs’ ability to exert market power in the adjacent long distance market would be
17 attenuated. Conversely, if a BOC such as Qwest is allowed to offer in-region long distance
18 service in a less-than-fully-competitive local market, then the BOC would have the ability to
19 engage in precisely the same type of anticompetitive conduct that the *MFJ* was intended to
20 prevent.

21 4. *United States v. Western Electric Company, Inc., et al*, Civil Action No. 74-1698
22 (D.D.C.).

23 5. *U.S. v. Western Electric Co. et al.*, 552 F. Supp. 131 (D. D.C., 1982), *aff’d sub nom.*
24 *Maryland vs. U.S.*, 460 U.S. 1007 (1983); and *Modification of Final Judgment*, sec. VIII.B.

1 11. In establishing the Section 272(a) and (b) separate affiliate requirements, Congress
2 clearly sought to create a transition between the outright prohibition of long distance entry
3 that had prevailed under the MFJ with a transitional separate affiliate mechanism that could
4 be extended by the FCC beyond the minimum three-year period,⁶ so as to provide safeguards
5 against anticompetitive behavior that had been unnecessary under the pre-1996 outright prohi-
6 bition against long distance entry.⁷ That congressional purpose is not served if all that the
7 structural affiliate requirement entails are nominal bureaucratic constructs satisfied by the
8 BOC and its affiliate maintaining merely facial separation. Yet on the basis of the two Qwest
9 Affidavits, as well as agreements already entered into by Qwest and its 272 Affiliate, it is
10 evident that Qwest seeks to interpret and apply the separate affiliate requirement in precisely
11 that superficial manner.

12

13 12. The scope and extent of interactions between the Qwest BOC and long distance
14 entities are broad and deep. Among the specific “joint” activities in which Qwest states it
15 will engage are these:

16

- 17 • Qwest BOC and long distance affiliate employees will occupy the same Qwest
18 buildings and in some cases will be located on the same floors.⁸ Their specific
19 corporate affiliation will be identified by colored dots on their security badges.⁹

20

21 6. 47 U.S.C. Sec. 272(f)(1).

22 7. *Infra*, footnote 3.

23 8. Qwest response to DOC 15029.

24 9. *Id.* See also Brunsting (QCC), at 14; Schwartz (Qwest Corporation), at 17.

- 1 • While employees of each of the two entities will be on only one company's
2 payroll,¹⁰ any employee of one of the two entities may be "loaned" to the other for
3 up to four (4) months per 12-month period.¹¹ During this "loan" period, that
4 employee will be under the supervision and authority of the company he or she is
5 loaned to, not the company issuing the employee's paycheck.¹²
6
7 • An employee of one entity may be assigned to perform "services" on behalf of the
8 other entity under an affiliate agreement entered into between the two entities
9 without such employee being considered to have been "loaned" by one entity to the
10 other or otherwise "shared" by the two entities.
11
12 • Administrative services such as payroll,¹³ human resources,¹⁴ accounting and
13 financial functions,¹⁵ and computer systems¹⁶ will be provided by the Qwest BOC
14 or the Qwest service company to QCC.
15
16 • The Qwest long distance entity will have very few employees of its own to support
17 the *in-region* long distance business; QCC currently employs only 3,916 people the
18 majority of whom are likely engaged in Qwest's *national* (i.e., out-of-region)
19 interexchange carrier operations (since Qwest is currently not providing in-region
20 long distance services in any of its fourteen states). QCC has designated only 168
21 employees as Minnesota personnel.¹⁷
22
23 • Assuming that QCC contracts with the Qwest BOC for the provision of "joint
24 marketing" services, the two entities will then be using the same personnel to market

25 10. Schwartz (Qwest Corporation), at 16.

26 11. Brunsting (QCC), at 15.

27 12. Qwest response to DOC 15044.

28 13. *Finance Services Work Order*, Affiliate Transaction (included in Attachment 3).

29 14. *Human Resources Work Order*, Affiliate Transaction (included in Attachment 3).

30 15. Brunsting (QCC), at 12.

31 16. *Information Technologies Services Work Order*, Affiliate Transaction (included in
32 Attachment 3).

33 17. Qwest response to DOC 15034(a).

1 local Qwest BOC and QCC long distance services. It is unclear at this point whether
2 these individuals will be employees of the BOC or of the Qwest service company.
3

4 • The Qwest BOC will provide billing and collection services on behalf of the Qwest
5 long distance entity,¹⁸ and Qwest BOC customer service representatives will provide
6 billing inquiry services for and on behalf of QCC.¹⁹ Billing and collections services
7 to be provided by the Qwest BOC to QCC appear to have been contracted for under
8 terms and conditions that differ from those being offered by the Qwest BOC to
9 nonaffiliated interexchange carriers.
10

11 In short, Qwest seems to view the separate affiliate provisions of Section 272 as requiring
12 little more than a set of perfunctory facial “compliance” measures that in no way undermine
13 its “right” to operate the local and long distance businesses as a functionally integrated
14 activity. Indeed, Qwest’s position is succinctly articulated by Ms. Brunsting herself:

15
16 It is important to note that while Congress anticipated the need for structural
17 separation between a BOC and the Section 272 subsidiary, the *Act* specifically
18 contemplates that a BOC and its Section 272 subsidiary would be affiliates under
19 a single parent company. The very structure utilized by Qwest Communications
20 International Inc. is contemplated by the terms of Section 272 and FCC
21 decisions. *As affiliates, the 272 Affiliate and BOC have unique financial and*
22 *business obligations and responsibilities to their boards of directors and*
23 *ultimately to their shareholders, notwithstanding Section 272 requirements.*²⁰
24

25 Ms. Brunsting and Qwest seem to miss the point: The “financial and business obligations and
26 responsibilities” that the various Qwest entities have to their respective boards of directors, to
27 the parent Qwest Communications International Inc., and ultimately to its shareholders, would

28 18. Qwest response to DOC 15027; see also *Provision of Billing and Collection Services*
29 *Affiliate Agreement* (included in Attachment 3).

30 19. *Provision of Billing and Collection Services Affiliate Agreement* (included in
31 Attachment 3).

32 20. Brunsting (QCC), at 17, emphasis supplied.

1 *require* profit-maximization and any lawful self-dealing. The purpose of Section 272 is thus
2 specifically to *constrain* and limit what would otherwise be actions taken in the parent
3 company's and its shareholders' own self-interest. Ms. Brunsting's brazen suggestion, as
4 revealed in her "notwithstanding Section 272 requirements" qualification, that the Section 272
5 requirements are subordinate to Qwest's "obligations and responsibilities" to directors and
6 shareholders, sets out the theme for all of Qwest's "compliance" actions.

7

8 13. As I shall discuss in detail in the following sections of this Affidavit, what Ms.
9 Brunsting and Ms. Schwartz describe as "compliance" with Section 272(b) is in reality a
10 transparent portrayal of a highly and fully integrated local/long distance business operation
11 that ignores fundamentally the purpose of the separate affiliate requirement and the very
12 specific conduct limitations that are imposed by Section 272(b).

13

14 **The FCC has determined that state commissions retain authority to enforce the**
15 **requirements of Section 272 once the FCC has granted a BOC 271 authority, and thus**
16 **the Minnesota PUC must now determine whether Qwest can be expected to comply with**
17 **Section 272 to prevent backsliding and anticompetitive conduct by Qwest post-271.**

18

19 14. The FCC has recognized that, where the policies of a state place more stringent
20 competitive requirements on a BOC than those of the federal statute or the FCC, the State has
21 the authority to enforce those requirements. The *Telecommunications Act of 1996* confirms
22 that states have authority beyond the requirements of the *federal* Act. Section 253(b) states:

23

24 (b) STATE REGULATORY AUTHORITY—Nothing in this section shall affect
25 the ability of a State to impose, on a competitively neutral basis and consistent
26 with section 254, requirements necessary to preserve and advance universal
27 service, protect the public safety and welfare, ensure the continued quality of
28 telecommunications services, and safeguard the rights of consumers.

1 15. The FCC has found, in the *Non-Accounting Safeguards Order*, that in the event that
2 the FCC determines that the BOC has complied with Section 271, a state Commission has the
3 authority to impose *any* requirements it deems necessary short of delay or denial of entry into
4 the intrastate interLATA market.²¹ In addition to the duties that the Minnesota Commission
5 holds with respect to Sections 271 and 272, the Commission is also bound by the
6 requirements of the Minnesota statutes regarding, *inter alia*, nondiscriminatory treatment of
7 competing providers,²² consumer protection,²³ and, if applicable, affiliate transactions
8 between a regulated utility and its affiliates.²⁴ The FCC's *Non-Accounting Safeguards Order*
9 clarifies the intent of the 1996 *Act* and gives the FCC full authority to grant *rights of entry*
10 interLATA authority, including intrastate interLATA authority:

11
12 In this regard, based on what we find is clear congressional intent that the
13 Commission is authorized to make determinations regarding BOC entry into
14 interLATA services, we reject the suggestion by the Wisconsin Commission
15 that, after the [FCC] has granted a BOC application for authority under
16 section 271, a state nonetheless may condition or delay BOC entry into
17 intrastate interLATA services.²⁵
18

19 21. *Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the*
20 *Communications Act of 1934, as amended*, CC Docket No. 96-149, *First Report and Order*,
21 released December 24, 1996, 11 FCC Rcd 21905, 21929 ("*Non-Accounting Safeguards*
22 *Order*").

23 22. See, e.g., Minn. St. Ch. 237.07; 237.09; 237.12; 237.121; 237.163, Subd. 7.

24 23. See, e.g., Minn. St. Ch. 237.66; 237.662, 237.663.

25 24. Minn. St. Ch. 237.65; 216B.48.

26 25. *Non-Accounting Safeguards Order*, 11 FCC Rcd 21929 (footnotes omitted).

1 However, while the FCC affirmed its authority to grant interLATA entry, the Wisconsin
2 Commission's concerns as presented in its reply comments in the *Non-Accounting Safeguards*
3 proceeding "respecting universal service, public welfare, service quality and consumer
4 safeguards, or section 271(c), respecting state advancement of competition beyond federal
5 minimums",²⁶ were not dismissed. Instead, the FCC expressly held that "a state would
6 retain authority to enforce obligations relating to a BOC's provision of intrastate interLATA
7 service, such as those identified by the Wisconsin Commission, through mechanisms other
8 than denial or delayed of [sic] entry into the intrastate interLATA market."²⁷ Thus, all
9 authority in limiting or placing obligations upon BOC provision of intrastate interLATA
10 service remains with the state, and it is the duty of the state commission to consider whether
11 additional restrictions on Qwest's activity are necessary to protect competition in the intrastate
12 interLATA market.

13

14 16. As a means for ensuring that a BOC maintains the appropriate competitive
15 safeguards after receiving Section 271 authority, the *Act* sets out various structural and
16 procedural requirements at Section 272. Enforcement of these safeguards, provided for under
17 Section 272(d), requires a joint federal/state biennial audit. The *Act* specifically requires that,
18 when reviewing the audit, the states consider "particularly whether such company has
19 complied with the separate accounting requirements under subsection (b)."²⁸ Considering

20 26. *Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the*
21 *Communications Act of 1934, as amended*, CC Docket No. 96-149, *Reply Comments of the*
22 *Public Service Commission of Wisconsin*, at 7.

23 27. *Non-Accounting Safeguards Order*, 11 FCC Rcd 21929, footnote 97.

24 28. 47 U.S.C. Section 272(d)(1).

1 this Commission's authority in reviewing Section 272 compliance two years from now (in the
2 event that Qwest obtains Section 271 authority at this time), the Commission needs to
3 consider, *at this time*, Qwest's plans for compliance with the requirements of Section 272 as
4 these will apply during the time period between now and the completion of the first biennial
5 audit. Qwest Minnesota should not be allowed a "free ride" during the critical first years of
6 its interLATA operation, at most promising some sort of vague after-the-fact compliance in
7 its dealing with those CLECs that are by that time still active in the market.

8

9 17. This Commission's findings with respect to Section 272 are instrumental to the long
10 term viability of both local and long distance competition in Minnesota. In the *Non-*
11 *Accounting Safeguards Order*, the FCC clearly recognized the capacity of a BOC to backslide
12 on checklist compliance after it receives 271 authority:

13

14 Moreover, we need to ensure that the market opening initiatives of the BOCs
15 continue after their entry into the long distance market. It is not enough that the
16 BOC prove it is in compliance at the time of filing a section 271 application; it
17 is essential that the BOC must also demonstrate that it can be relied upon to
18 remain in compliance. This may be demonstrated in various ways. For
19 example, we must be confident that the procedures and processes requiring BOC
20 cooperation, such as interconnection and the provision of unbundled network
21 elements, have been sufficiently available, tested, and monitored. Additionally,
22 we will look to see if there are appropriate mechanisms, such as reporting
23 requirements or performance standards, to measure compliance, or to detect
24 noncompliance, by the BOCs with their obligations. Finally, the BOC may
25 propose to comply continually with certain conditions, or we may, on a case-by-
26 case basis, impose conditions on a BOC's entry to ensure continuing compliance.
27 The section 271 approval process necessarily involves viewing a snapshot of an
28 evolving process. *We must be confident that the picture we see as of the date of*

1 *filing contains all the necessary elements to sustain growing competitive entry*
2 *into the future.*²⁹
3

4 Insofar as Section 272 sets forth the structural and transactional requirements designed to
5 ensure continued compliance, enforced by the regulatory authority to undertake the biennial
6 review, Section 272 provides the regulatory framework to prevent this backsliding. In this
7 Section 272 proceeding, the Commission must determine not only that Qwest is in compliance
8 with the Section 272 requirements, but that the nature of this “compliance” is sufficient to
9 prevent backsliding on checklist items, and to ensure that Qwest is unable to engage in anti-
10 competitive activities. To the extent that Qwest has not as yet fully disclosed the full extent
11 of its various affiliate agreements applicable to services to be provided by and other transfers
12 from QC to QCC and vice versa, the Commission does not have a record before it to support
13 a finding that Qwest will comply with Sections 272(a) and (b) were it granted Section 271
14 authorization.

15

16 **The Minnesota PUC has previously prohibited as anticompetitive the type of joint**
17 **marketing of local and long distance service that Qwest contemplates pursuing following**
18 **Section 271 approval.**
19

20 18. The *source* of Qwest’s ability to use its joint marketing authority to exercise market
21 power in the long distance market *arises directly from its near-monopoly position in the local*
22 *market*. Experiences in both New York and Texas, the first two states in which BOCs have
23 obtained Section 271 authority, confirm the extraordinary marketing advantage, *available*

24 29. *In the Matter of Application of Ameritech Corp. Pursuant to Section 271 of the*
25 *Communications Act of 1934, as amended, to Provide In-Region, InterLATA Services in*
26 *Michigan*, CC Docket No. 97-137, *Memorandum Opinion and Order*, Rel. August 19, 1997
27 (*Michigan 271 Order*), at para. 19, 12 FCC Rcd 20555, emphasis supplied.

1 *solely to BOCs*, stemming from their use of this “inbound channel” to “sell” their affiliate’s
2 long distance service to *local service* customers. This advantage has not been overlooked by
3 Wall Street. As a February 8, 2001 Credit Suisse First Boston (“CSFB”) report commented:

4
5 We’ve been watching this industry for almost 20 years and we have never seen
6 consumer share gained at the rate of VZ in NY and SBC in TX (the former 20%
7 share in 12 mos and the latter 18% share in 6 months).³⁰
8

9 In considering whether Qwest has satisfied the requirements of Section 272, it is essential that
10 the Commission recognize that what Qwest seeks in its application is not simply the right to
11 enter yet another isolated line of business, but the right to *integrate* local and long distance
12 service into a single package, to make the two services essentially indistinguishable from the
13 consumer’s perspective, and to leverage its dominance of the local market to similarly come
14 to dominate the long distance market as well. CSFB makes the point profoundly clear in its
15 comparison of (pre-merger) GTE’s approach to selling long distance services through a
16 separate CLEC affiliate vs. Verizon’s and SBC’s ability to offer long distance services
17 directly to their ILEC customers:

18
19 In stark contrast to Verizon’s huge and quick 20% consumer LD share gains in
20 NY State, LD subscribership was flat in the GTE franchise areas in ’00 despite
21 GTE’s benefitting from similar pre-established branding and billing relationships.
22 The difference is that GTE has not leveraged the inbound channel and also had
23 been running its LD effort through its “CLEC”, in effect forcing customers to
24 switch to the GTE CLEC both their local service from GTE’s ILEC and their
25 LD service from another LD customer. Not very successful if you ask us and
26 certainly worthy of change given the empirical evidence that VZ’s and SBC’s

27 30. “VZ: Analyst Mtg Provides Comprehensive ‘01 Outlook,” Credit Suisse First Boston,
28 09:47am EST, 8-Feb-01 (“CSFB Report”).

1 use of the inbound channel and separate LD sub (but not bundled with local)
2 have been extraordinarily successful.³¹

3
4 19. As the CSFB report observes, this preemptive use of the “inbound channel” by both
5 Verizon and SBC to “sell” their long distance service to *new* local service customers has been
6 the principal explanation for their extraordinary success in acquiring customers in the first
7 year in which they have been permitted into the long distance business. Indeed, SBC has
8 apparently been sufficiently satisfied with its market performance that it has recently elected
9 to *increase* its interstate long distance rates in Texas. As reported in the *Ft. Worth Star-*
10 *Telegram*, February 2, 2001:

11
12 Southwestern Bell announced it was raising the interstate rate on its flagship
13 plan from 9 cents a minute to 10 cents a minute for new customers seven
14 months after entering the long-distance market in Texas. Current
15 subscribers will see no change in their domestic U.S. calling charges, said
16 Shawn Ramsey, a San Antonio-based spokeswoman for Southwestern Bell, a
17 unit of SBC Communications.

18
19 Ramsey defended the increase, which doesn’t require approval by the state’s
20 Public Utility Board, by saying the plan is superior to many offered by the
21 major long-distance services. “We beat the pants off of them,” she said.
22 “We’ve got great rates any way you slice or dice it.” Asked if the higher
23 rate reflects a need to boost profits, she said: “We’ve been in the market
24 about eight months now. We’ve learned a lot and made a number of
25 changes that reflect what we’ve seen. And we’ve changed our plan
26 accordingly.”³²

27
28 31. *Id.*

29 32. “SW Bell raises interstate rate; current subscribers unaffected; PUC approval not
30 needed,” *Ft. Worth Star-Telegram*, February 2, 2001.

1 20. A BOC's ability to separately *and preemptively* identify *and recommend* its own
2 affiliate's long distance service affords it a substantial advantage over its long distance rivals
3 in being the first to offer and to sign up a new local service customer for long distance
4 service. The FCC itself has recognized the advantage to an IXC of appearing early (or even
5 first) on the list of service providers by its *express requirement*, as set forth in the *Non-*
6 *Accounting Safeguards Order*, that the names of IXCs be read to inbound callers *in random*
7 *order*.³³ The practical effect of the physical impossibility of simultaneously making the
8 BOC affiliate recommendation while contemporaneously reading the full list of available
9 IXCs, together with the BOC's right to make its "recommendation" *prior to identifying any*
10 *alternative long distance providers*, affords it an enormous marketing advantage in selling
11 long distance services. This preemptive use of the "inbound channel" by both Verizon and
12 SBC to "sell" their long distance service to *new* local service customers has been the principal
13 explanation for their extraordinary success in acquiring customers in the first year in which
14 they have been permitted into the long distance business.³⁴ Indeed, as I have noted above,
15 SBC has apparently been sufficiently satisfied with its market performance in Texas that it
16 has recently elected to *increase* its interstate long distance rates.

17 33. *Non-Accounting Safeguards Order*, 11 FCC Rcd 22046, citing *In the Matter of*
18 *Investigation of Access and Divestiture Related Tariffs, Allocation Plans Waivers and Tariffs,*
19 *Memorandum Opinion and Order*, 101 FCC 2d (1985) at 950.

20 34. Verizon has reported that through the end of the third quarter of 2001, after just 21
21 months since it began offering long distance service in New York, its long distance affiliate
22 Verizon Long Distance has captured 31.7% of the residential subscribers in Verizon New
23 York's service areas. Verizon Press Release, "Verizon Communications Reports Solid 3Q
24 Earnings And Provides Outlook for Remainder of 2001," October 30, 2001. SBC has
25 reported that through the third quarter of 2001, *less than nine months* following its Section
26 271 entry in Texas, the Company has signed up 21% of its 10-million Texas access lines for
27 SBC long distance. *SBC Investor Briefing*, April 23, 2001, at 7.

1 21. There are, in fact, a number of reasons why a customer might initiate a contact with
2 a LEC and, to the extent that the BOC continues to enjoy overwhelming market dominance,
3 most such contacts will inevitably be with the BOC in areas in which the BOC offers local
4 exchange service as an ILEC. Contacts initiated by customers would take place where the
5 customer needs to place an order for new telephone service, for an additional access line, or
6 to add or change service features. Customers may also initiate contacts for bill inquiries,
7 repair service, or to obtain information about new services that might become available such
8 as, for example, ADSL. Data provided in this Commission's consideration of Qwest
9 Corporation's *Alternative Form of Regulation Service Quality Plan* indicates that, in
10 September 2001, Qwest in Minnesota received 290,953 calls regarding billing and collection,
11 and 183,732 calls ordering installation (of these, 20,350 calls were new connect orders, for
12 which a customer would need to choose a PIC).³⁵ Thus, Qwest has the ability to address
13 approximately 475,000 potential customers each month, during calls *initiated by the customers*
14 *themselves* and at a time when they are already thinking about their telephone service.

15

16 22. Indeed, at least with respect to these types of sales at the time of the initial local
17 service contact, the BOC need spend little if any resources actually advertising or otherwise
18 marketing its long distance services. The inbound caller has already made the contact with
19 "the phone company" for basic telephone service and, unless that customer is a student of
20 telecommunications industrial organization and regulation, there is a strong likelihood that the

21 35. "Qwest Quarterly Service Settlement Report," a monthly report regarding Minnesota
22 customers, as required by the Commission's *Order in Qwest Corporation's Alternative Form*
23 *of Regulation (AFOR) Service Quality Plan*, Docket No. P-421/AR-97-154, filed November
24 15, 2001.

1 customer will simply accept the BOC service representative's "recommendation" as the only
2 and obvious choice. That selling long distance services to "inbound" *local* service customers
3 is a centerpiece of Qwest's long distance marketing strategy can be reasonably inferred from
4 the discussion of this subject in the Brunsting and Schwartz Affidavits,³⁶ from the existing
5 practices of Verizon and SBC in New York, Texas, and in their other "271" states, and from
6 Qwest's own refusal to confirm its intention to use the same competitively-neutral script that
7 the Commission had previously ordered with respect to intraLATA marketing.³⁷

8

9 23. The Minnesota PUC has considered and addressed this very same preemptive joint
10 marketing of local and long distance services on "inbound" local service contacts in the
11 context of *intraLATA* toll services. Prior to 1996, all intraLATA toll calls in Minnesota that
12 were dialed on a "1+" basis were automatically routed to then-US WEST. Although IXC's
13 were permitted to offer competing intraLATA toll service in the state, customers desiring to
14 utilize those competing services were required to dial an access code (in the form of
15 '10XXX', where 'XXX' was (at that time) a 3-digit "Carrier Identification Code") preceding
16 *each call* to designate an intraLATA toll carrier *other* than US WEST. In 1996, the PUC
17 ordered US WEST to provide "intraLATA equal access" allowing customers to designate an
18 intraLATA Presubscribed Interexchange Carrier ("LPIC") in addition to the customer's
19 interLATA Presubscribed Interexchange Carrier ("PIC").³⁸ If an LPIC other than US WEST

20 36. Brunsting (QCC), at 21-24; Schwartz (QC), at 31-33.

21 37. Qwest response to DOC 15047.

22 38. *In the Matter of an Investigation into IntraLATA Equal Access and Presubscription*,
23 Minnesota PUC Docket No. P-999/CI-87-697, *Order Establishing US West Business Practices*
24 *for IntraLATA Presubscription*, January 12, 1996.

1 was selected, intraLATA calls dialed on a 1+ basis would be routed to the customer's chosen
2 IXC. Although US WEST was prohibited from offering *interLATA* service in Minnesota, the
3 IXCs' *intraLATA* services were now competing directly with those being offered by US
4 WEST.

5

6 24. The MPUC specifically addressed the manner in which US WEST customer service
7 representatives would be using inbound sales and other customer contacts to "sell" US WEST
8 intraLATA toll services:

9

10 The Commission agrees with commenting parties that US WEST must not use
11 its position as the dominant local carrier to achieve a superior competitive status
12 in the opening intraLATA toll market. When a customer contacts US WEST
13 seeking new service, or for any other reason that relates to US WEST's position
14 as the customer's local service provider, US WEST's customer service
15 representatives should not influence the customer's choice of intraLATA toll
16 carrier or persuade the customer to subscribe to US WEST.

17

18 The Commission will not at this time require US WEST to establish a separate
19 group of customer service representatives to market the Company's intraLATA
20 services, as some commenting parties have suggested. The Commission will,
21 however, require US WEST to do any necessary training or monitoring to ensure
22 that its service representatives do not handle their customer contacts in anything
23 but a competitively neutral fashion.

24

25 The Commission agrees with the Department that US WEST should be required
26 to submit for Commission approval a proposed script which its customer service
27 representatives will follow when contacted by customers seeking service. The
28 script should cover the Company's proposed method of informing the customer
29 regarding intraLATA toll carrier choice. The script must not contain language
30 which seeks to leverage US WEST's dominant local carrier position into
31 competitive advantage in the intraLATA toll arena.

32

33 Following that order, US WEST submitted a script for the Commission's approval. As
34 described in the Commission's April 2, 1996 *Order Denying Reconsideration*, US WEST had

1 proposed a sales script that specifically suggested that the customer select US WEST's own
2 intraLATA service:

3
4 You now need to choose a company to carry your local long distance. Many
5 companies provide this service. I'd be glad to read you a list of the companies
6 available to you, or I can arrange for US WEST to provide this service for
7 you.³⁹
8

9 In rejecting the script proposed by US WEST, the Commission reiterated its original
10 conclusion that this use of inbound contacts was anticompetitive:

11
12 In the January 12, 1996, Order, the Commission stated that the Company "script
13 must not contain language which seeks to leverage US WEST's dominant local
14 carrier position into competitive advantage in the intraLATA toll arena." Order
15 at p. 8.

16
17 US WEST's proposed script would place competitors at a disadvantage vis a vis
18 the incumbent carrier. Only US WEST's name would be mentioned. Customers
19 would face the alternatives of listening to a list of unnamed carriers or of having
20 US WEST "arrange to provide the service" for the customer. These distinctions
21 definitely do not promote a competitively neutral environment as the intraLATA
22 toll market opens.

23
24 Furthermore, US WEST cannot say that it will have any disadvantage under the
25 Staff's proposed language. Far from requiring US WEST to "advertise" other
26 carriers, the language will simply require notice that a selection of carriers is
27 available. Since all potential players will be placed on the same footing, US
28 WEST will have the same opportunity as its competitors to win customers
29 through advertising and quality of service. The Commission has found that
30 competition in the intraLATA toll market place is in the public interest. The
31 Commission's imposition of reasonable language requirements is part of its right
32 and duty to regulate the provision of intraLATA toll service so that true
33 competition exists.

34 39. *In the Matter of an Investigation into IntraLATA Equal Access and Presubscription,*
35 Minnesota PUC Docket No. P-999/CI-87-697, *Order Denying Reconsideration and Clarifying*
36 *Order*, April 2, 1996, at 6.

1 The Commission denies US WEST's request to reconsider its Order
2 requirements regarding service representative contacts with customers. The
3 Commission will require US WEST's representatives to use the script approved
4 by Commission Staff when dealing with new, transferred, or changed PIC
5 service.⁴⁰
6

7 The specific script that was approved by the Commission was the one that had been
8 recommended by the Commission Staff:

9
10 You now need to choose a company to carry your local long distance calls.
11 Many companies provide this service. I'd be glad to read you a list of the
12 companies available to you.⁴¹

13

14 25. The concern that was raised by competing IXCs and that was addressed and resolved
15 by the Commission with respect to *intraLATA* toll services applies with equal force in the
16 case of *interLATA* services. Indeed, while nominally being offered by a "separate affiliate,"
17 Qwest's long distance service would be marketed by Qwest BOC employees during inbound
18 new local service order and other contacts *initiated by the customer*. Moreover, the similarity
19 between the names of the two Qwest entities — Qwest Corporation and Qwest Communica-
20 tions Corporation - whether purposefully or not will nevertheless have the effect of creating
21 customer confusion with respect to the identity of the entity that is actually providing the
22 interLATA service — the local Qwest phone company vs. the Qwest long distance entity.
23 Accordingly, absent the application of comprehensive competitively-neutral marketing rules,
24 the Commission's 1996 conclusion with respect to *intraLATA* services marketing contacts can
25 be readily paraphrased to apply to the marketing of QCC *interLATA* services:

26 40. *Id.*, at 7-9.

27 41. *Id.*, at 5.

1 *Qwest's proposed script would place competitors at a disadvantage vis a vis the*
2 *incumbent carrier. Only Qwest's name would be mentioned. Customers would*
3 *face the alternatives of listening to a list of unnamed carriers or of having*
4 *Qwest "arrange to provide the service" for the customer. These distinctions*
5 *definitely do not promote a competitively neutral environment as the interLATA*
6 *toll market opens.*

7

8 26. As I have previously noted, state commissions are expressly authorized by the FCC
9 "to enforce obligations relating to a BOC's provision of intrastate interLATA service....," such
10 as "respecting universal service, public welfare, service quality and consumer safeguards, or
11 section 271(c), respecting state advancement of competition beyond federal minimums."⁴²
12 Thus, the authority to limit or impose obligations on the BOC with respect to its and its
13 affiliate's provision of intrastate interLATA service remains with the state. This Commission
14 may therefore clearly apply to Qwest's interLATA "joint marketing" activities the very same
15 competitively neutral marketing rules that it had previously adopted with respect to
16 intraLATA services.

17

18 **Qwest has failed to show that it has implemented separate ownership and servicing of all**
19 **BOC and Section 272 affiliate operating, installation and maintenance facilities and**
20 **functions.**

21

22 27. Section 272(b)(1) requires that a 272 affiliate "shall operate independently from the
23 Bell operating company." In interpreting this subsection, the FCC has determined that

24 42. *Non-Accounting Safeguards Order*, 11 FCC Rcd 21929, footnote 97, referencing *Reply*
25 *Comments of the Public Service Commission of Wisconsin*, at 7.

1 “operate independently” does not have, in its view, a “common sense” interpretation.⁴³
2 Therefore, the FCC concluded that it is free to define this provision consistent with its
3 reading of Congressional intent. Here the FCC reads the Congressional intent of Section
4 272(b)(1) as “ensur[ing] the operational independence of a section 272 affiliate from its
5 affiliated BOC.”⁴⁴ On the basis of that reading, the FCC proceeds to draw a very narrow
6 definition of the “operate independently” requirements of Section 272(b)(1):

7
8 We decline to read the “operate independently” requirement to impose a
9 blanket prohibition on joint ownership of property by a BOC and a section
10 272 affiliate. Rather, we limit the restriction to joint ownership of
11 transmission and switching facilities and the land and buildings where those
12 facilities are located. We conclude that the prohibition we have adopted
13 should ensure that the section 272 affiliate’s competitors gain nondiscriminatory
14 access to those transmission and switching facilities that both section
15 272 affiliates and their competitors may be unable to obtain from other
16 sources.⁴⁵
17

18 In addition to requiring that a BOC and its Section 272 affiliate do not share ownership of
19 switching and transmission facilities, the BOC and 272 affiliate are also prohibited from
20 contracting with each other for one entity to provide operating, installation, or maintenance
21 services with respect to the other’s facilities:

22
23 As stated above, we believe that a prohibition on joint ownership of
24 transmission and switching facilities is necessary to ensure that a BOC

25 43. *In the Matter of Implementation of the Non-Accounting Safeguards of Section 271 and*
26 *272 of the Communications Act of 1934, as amended*, CC Docket No. 96-149, *Third Order on*
27 *Reconsideration*, released October 1, 1999, 14 FCC Rcd 16299, 16305 (“*Third Order on*
28 *Reconsideration*”).

29 44. *Non-Accounting Safeguards Order*, 11 FCC Rcd 21985.

30 45. *Id.*, at 21983.

1 complies with the nondiscrimination requirements of section 272.
2 Consistent with that approach, we further interpret the term “operate
3 independently” to bar a BOC from contracting with a section 272 affiliate to
4 obtain operating, installation, or maintenance functions associated with the
5 BOC’s facilities. Allowing a BOC to contract with the section 272 affiliate
6 for operating, installation, and maintenance services would inevitably afford
7 the affiliate access to the BOC’s facilities that is superior to that granted to
8 the affiliate’s competitors.
9

10 By limiting the meaning of the Section 272(b)(1) “operate independently” clause to what is
11 known as “OI&M” (operation, installation and maintenance) functions, the FCC draws the not
12 particularly demanding requirement that the 272 affiliate must deal with the *facilities* of the
13 BOCs in the same manner as all other competitors. The 272 affiliate would not be able to
14 leverage its relationship with the BOC in order to gain a competitive advantage from superior
15 access to BOC underlying network operations.
16

17 28. Despite the FCC’s narrow delineation of this requirement, however, Qwest has failed
18 to demonstrate compliance with it. All that Qwest has done is to provide statements by its
19 two affiants averring that the Qwest BOC and QCC will not jointly own any network
20 facilities or share OI&M functions.⁴⁶ In its data request #15010, the Department asked
21 Qwest for more specific information that, if provided, would permit an independent
22 assessment as to Qwest’s compliance with Section 272(b)(1):
23

- 24 a) Please provide a map of all transmission and switching facilities, which
25 QCC will use to provide interLATA long distance services in
26 Minnesota, and identify who owns these facilities.
27
28 b) If any transmission facilities are owned by anyone other than QCC,

29 46. Brunsting (QCC), at 8-9; Schwartz (QC), at 10-11.

- 1 please provide all documentation or contracts showing the terms and
2 conditions under which QCC will obtain these facilities.
3
- 4 c) Please identify all locations, including the address of QCC switching
5 facilities, that will be used to route Minnesota interLATA calls, and the
6 owner of each of the switching facilities.
7
- 8 d) Will any of the switching facilities mentioned in (c) be used to route
9 intraLATA traffic? Local traffic? EAS traffic?
10
- 11 e) Who owns the land and/or buildings in which the QCC switching
12 facilities are located?
13
- 14 f) Please provide all documentation, contracts or collocation agreements
15 identifying the terms and conditions under which QCC will locate its
16 switching facilities.
17
- 18 In its response, Qwest states that it is “still in the process of completing its network strategy,”
19 but in other respects has refused to provide any of this information.⁴⁷ Although Qwest now
20 claims that its network is incomplete and unknown, in addressing the benefits of its merger
21 with US WEST, the Company stated:
- 22
- 23 The post-merger company will also have incentives to satisfy Section 271
24 quickly because the new company, unlike US West, will already own an
25 interLATA network. This means that the merged company will be able to re-
26 enter the in-region interLATA market immediately upon Section 271 relief with
27 its own high-capacity, state-of-the-art network. It will not have to incur the
28 expense and delay associated with constructing new facilities or depend on
29 having to resell the services of another carrier.⁴⁸
30

31 47. Qwest response to DOC 15010.

32 48. *In the Matter of the Merger of the Parent Corporations of Qwest Communications*
33 *Corporation, LCI International Telecom Corp., USLD Communications, Inc., Phoenix*
34 *Network, Inc. and US WEST Communications, Inc.*, Docket No. P3009, 3052, 5096, 421,
35 3017/PA-999-1192, Reply Comments of Qwest and US WEST filed January 18, 2000, at 7.

1 Ms. Brunsting's and Ms. Schwartz's assurances are hollow without the details as to the actual
2 ownership of facilities and responsibilities for OI&M functions. Hence, the Commission has
3 no factual basis, beyond the unsupported assertions by Ms. Brunsting and Ms. Schwartz, upon
4 which to find that Qwest is currently complying with the "operate independently"
5 requirements of Section 272(b)(1).

6

7 29. Furthermore, Qwest's claim that the two entities do not jointly own *in a legal sense*
8 any network facilities does not address the possibility of some alternative ownership or
9 sharing arrangement that would, from an economic perspective, be for all practical purposes
10 entirely equivalent to joint legal ownership. For example:

11

12 • The BOC and QCC entities could create a type of "condominium" arrangement
13 whereby the ownership of the common facility would be divided between the two
14 entities with respect to identifiable network elements, such as specific strands in a
15 fiber optic cable.

16

17 • The parent company or some other Qwest affiliate could be the legal owner of
18 facilities that both the BOC and QCC would then lease.

19

20 The statements made by the two Qwest witnesses would not preclude either of these
21 arrangements;⁴⁹ if one or both were being pursued by Qwest, the effect would be an evasion

22 49. Ms. Brunsting (at 8) states: "The 272 Affiliate does not and will not jointly own, with
23 the BOC, telecommunications transmission and switching facilities, or the land and buildings
24 (continued...)"

1 of the “operate independently” requirement. Indeed, with respect to the “third party”
2 ownership approach, the FCC has found that, should the parent corporation own any of these
3 facilities or provide any OI&M services for both the BOC and the 272 affiliate, the parent
4 would be subject to the same 272(b)(1) requirements as the BOC and the 272 affiliate.⁵⁰

5 Neither Qwest affiant has stated that the two entities will not use in common switching and
6 transmission facilities owned by the Qwest parent company or by another Qwest affiliate.⁵¹

7
8 30. In prohibiting joint ownership of switching and transmission facilities, the FCC has
9 attempted to ensure that a BOC would continue to deal with the 272 affiliate with respect to
10 the affiliate’s use of BOC facilities in a competitively neutral manner. This means that the
11 affiliate would be required to purchase the use of BOC facilities on the same terms and
12 conditions as would any nonaffiliated competitor, which usually means pursuant to tariff.
13 Joint ownership would allow the affiliate access to facilities and service on terms equivalent
14 to those available to the BOC itself, and significantly more favorable than terms available to
15 competitors. Condominium ownership, unless also offered to nonaffiliated competitors, would
16 have the same effect, affording the affiliate superior access to whatever facilities in the BOC

17 49. (...continued)
18 on which such facilities are located.” Ms. Schwartz states (at 11): “The BOC and the 272
19 Affiliate do not and will not jointly own telecommunications switching or transmission
20 facilities, or the land or buildings where those facilities are located, so long as such restriction
21 applies under the rules.”

22 50. *Non-Accounting Safeguards Order*, 11 FCC Rcd 21992.

23 51. All that they have committed to with respect to their dealings with other Qwest entities
24 is that “no switching and transmission facilities have been transferred from the BOC to the
25 272 affiliate” [Schwartz at 11] and that “[n]either the BOC nor any other Qwest affiliate
26 performs any OI&M functions associated *with the 272 Affiliate’s* switching and transmission
27 facilities.” [Schwartz at 12, emphasis supplied].

1 central office that the 272 affiliate “owns,” while allowing the BOC to deny access to similar
2 facilities (perhaps based on a lack thereof) to the affiliate’s competitors. The FCC clearly
3 never intended to permit such a loophole:

4
5 To the extent that a section 272 affiliate jointly owned transmission and
6 switching facilities with a BOC, the affiliate would not have to contract with
7 the BOC to obtain such facilities, thereby precluding a comparison of the
8 terms of transactions between a BOC and a section 272 affiliate with the
9 terms of transactions between a BOC and a competitor of the section 272
10 affiliate.⁵²
11

12 The *Non-Accounting Safeguards Order* continued to specifically disallow this type of
13 “condominium” arrangement in a BOC’s central office:

14
15 Moreover, the ban on joint ownership of facilities should protect local
16 exchange competitors that request physical collocation by ensuring that a
17 BOC’s section 272 affiliate does not obtain preferential access to the limited
18 available space in the BOC’s central office.⁵³
19

20 In the example cited above, where a portion of the strands in a fiber optic cable are owned by
21 the 272 affiliate and the rest by the BOC, the Section 272 affiliate would have its own access
22 to the BOC’s central office, and would not need to obtain a dark fiber UNE. Where a
23 competitor requires the same access, it would be required to lease dark fiber from the BOC at
24 tariff prices, assuming that the BOC had dark fiber capacity available. The 272 affiliate
25 would have what amounted to outright ownership of what would normally be considered a
26 BOC’s dark fiber. Until Qwest provides evidence that it is not participating in this type of

27 52. *Non-Accounting Safeguards Order*, 11 FCC Rcd 21983.

28 53. *Id.* (footnotes omitted).

1 “condominium” arrangement, as well as that it has not transferred any of its network assets to
2 its parent corporation or to another Qwest affiliate for the purpose of avoiding the 272(b)(1)
3 requirements, Qwest has failed to show that its proposed long distance affiliate satisfies the
4 FCC’s “operate independently” requirement. Qwest has thus not met its burden to
5 demonstrate that it is in compliance with even the FCC’s limited scope of the Section
6 272(b)(1) “operate independently” provision. Moreover, to the extent that Qwest’s carefully
7 worded “commitment” would not preclude it from pursuing other creative forms of
8 “ownership,” the Commission has no firm basis to conclude that Qwest satisfies or will in the
9 future satisfy Section 272(b)(1).

10

11 **This Commission should view the “operate independently” requirement as embracing**
12 **any operational practices that work to blur the distinction or otherwise achieve**
13 **functional integration between the BOC and its Section 272 Affiliate.**

14

15 31. The FCC has interpreted the Section 272(b)(1) “operate independently” requirement
16 as being limited solely to *network* operations. Yet network operations are only one part of a
17 BOC’s myriad of operating functions. Section 272(b)(1) needs to be read in conjunction with
18 the overall Section 272(a) separate affiliate requirement and with the other four subsections of
19 272(b), which collectively outline a comprehensive code of conduct that cannot be interpreted
20 as in any sense permitting *integrated* “operations” in the non-network functions of the BOC
21 and long distance entities. As the ALJ has found in the *Fourth Prehearing Order*, the issue
22 of who has ultimate control over policy in a corporate entity is properly within this
23 proceeding,⁵⁴ and it is entirely appropriate for this Commission to apply a broader inter-

24 54. *Fourth Prehearing Order*, November 20, 2001, at footnote 7.

1 pretation of “operate independently” if it concludes that limiting this requirement solely to
2 “network operations” is insufficient to foreclose the potential for anticompetitive and
3 discriminatory acts on the part of Qwest.

4
5 32. Indeed, the narrow “network operations” interpretation of “operate independently”
6 cannot be squared with Section 272(b)(5), which obligates the BOC and its 272 affiliate to
7 deal with each other “on an arm’s length basis.” As Ms. Brunsting has conceded,⁵⁵ the
8 management and Board of Directors of Qwest International Inc., the parent company of the
9 Qwest BOC and QCC entities, is ultimately responsible to Qwest’s shareholders. As such,
10 the parent company’s role is to make decisions that are in the best interests of the overall
11 corporation, even if such decisions may adversely affect the fortunes of individual
12 components thereof. Thus, and absent the “arm’s length” transaction requirement of Section
13 272(b)(5), the Qwest parent company may determine that it should sacrifice profits in one
14 subsidiary to benefit another if by so doing it could increase overall corporate profits. For
15 example, if the 272 Affiliate were able to purchase services or obtain information from the
16 BOC entity at less than fair market value (or for “free”), the affiliate could then underprice its
17 competitors, allowing it to capture market share and realize higher overall corporate profit.
18 But an “arm’s length transaction” requirement obligates each of the entities to operate vis-a-
19 vis each other not with the goal of maximizing *corporate* profits, but rather with the objective
20 of *maximizing profits in each of the affiliate entities on a stand-alone basis*. The “arm’s
21 length” requirement thus precludes the BOC entity, for example, from affording favorable
22 treatment to the 272 Affiliate if by so doing the financial or business interests of the BOC

23 55. Brunsting (QCC), at 17.

1 entity would be compromised *even if the overall financial or business interests of the parent*
2 *Qwest International, Inc. would be enhanced.* Thus, the 272(b)(5) requirement works to
3 impose an “operate independently” obligation with respect to *all* facets of the BOC’s and its
4 272 Affiliate’s activities and operations, *even where that causes overall Qwest corporate*
5 *profits to be less than they would be under fully integrated operations with all transactions*
6 *between and among affiliates based upon the best interests of the parent corporation rather*
7 *than the best interests of each affiliate standing on its own.*

8

9 33. Significantly, the mere fact that transactions between the BOC and 272 Affiliate
10 must be recorded may not by itself preclude the entities from engaging in conduct that
11 focuses upon overall corporate results rather than upon individual affiliate impacts. For
12 example, the BOC entity will provide billing and collection services for the long distance
13 affiliate, for which it will be compensated under the affiliate agreement. In reality, of course,
14 the BOC will be preparing and mailing bills to its local service customers anyway, so the
15 incremental cost of including the 272 affiliate’s long distance charges is at or near zero. In
16 setting its own retail prices, the affiliate may simply ignore its billing “costs” (i.e., its
17 “payments” to the BOC for billing and collection services), enabling it to offer lower prices
18 than competing IXCs, who must incur the actual, out-of-pocket cost to bill their long distance
19 customers on a stand-alone basis. Thus, the 272 Affiliate could offer “discount toll plans”
20 with no monthly charge or minimum commitment, even if that may result in the revenues
21 being obtained from some low-use customers falling below the nominal “billing” payment it
22 makes to the Qwest BOC, because QCC’s “loss” will still translate into a net “profit” for
23 Qwest International, Inc. as a whole.

24

1 34. As another example, consider the types of “tie-in” arrangements that Verizon Long
2 Distance and Verizon New York have pursued as part of their “joint marketing” program.⁵⁶
3 In New York, Verizon Long Distance (“VLD”) was offering a \$4.60 credit when a customer
4 selected the basic VLD Schedule “C” (\$0.10 per minute, no minimum, no monthly charge)
5 calling plan and also subscribed to the Verizon BOC’s “Value Pack” service, a package of
6 local exchange service and selected vertical features.⁵⁷ The Schedule C rate plan was
7 targeted at the relatively low-use customer who would be attracted by the absence of either a
8 monthly charge or minimum usage commitment. If, for example, such a customer were to
9 make no long distance calls at all during a given month, VLD would sustain a loss of at least
10 \$4.60 in that it would still have to “pay” the credit to Verizon New York while receiving no
11 offsetting long distance revenue from the customer. Verizon New York, however, would
12 realize \$17.99 in actual revenues from the customer (the price of Value Pack service)⁵⁸ plus
13 the additional \$4.60 “payment” from Verizon Long Distance. VNY gains \$22.59 while VLD
14 “loses” \$4.60, which still results in a net gain to the consolidated Verizon bottom line of
15 \$17.99, erasing the VLD “loss” when examined at the parent level. VLD’s ability to offer
16 this “promotion” and to potentially sustain the “losses” arising therefrom is solely and

17 56. It should be noted that at the time that this affidavit was filed, the Department had not
18 had sufficient opportunity to review the joint marketing scripts and plans provided by Qwest
19 as compelled by the *Fourth Prehearing Order*. To the extent that the materials to be
20 provided by Qwest reveal analogous marketing plans, the Department will file supplemental
21 testimony relating thereto.

22 57. Bell Atlantic Communications, Inc. d/b/a Verizon Long Distance, New York PSC
23 Tariff No. 1, Original Promotional Attachment No. 5. Package No. 1 Promotion and Rate
24 Schedule (Section 3.5.3).

25 58. <http://www22.verizon.com/foryourhome/SAS/StateSelector.asp?ID=choosefeat>, accessed
26 11/28/01.

1 uniquely attributable to its affiliate relationship with the Verizon BOC. From the perspective
2 of any *competing* non-affiliated interexchange carrier attempting to make a comparable
3 “promotional” offer, that same \$4.60 “payment” would be a real *cash payment*, representing a
4 true out-of-pocket cost to the IXC. In Verizon’s case, even though the inter-affiliate
5 “payment” is (presumably) actually being recorded on the two entities’ respective books, VLD
6 is behaving as if no such “payment” is actually taking place. Were QC/QCC to engage in
7 similar “promotional” or “tie-in” offers, the effect would be to impose an anticompetitive
8 price squeeze on its long distance rivals.

9
10 35. QCC has expressly “reserve[d] the right to utilize any and all vendors and sales
11 sources, including but not limited to, those available through joint marketing with QC (Qwest
12 Corporation).”⁵⁹ The Qwest BOC’s provision of “joint marketing” services to the 272
13 affiliate, assuming that it is pursued, provides perhaps an even more compelling example of
14 less-than-arm’s length behavior. In addition to furnishing personnel to support this function,
15 the BOC would also be providing its affiliate with unfettered access to the BOC entity’s
16 customer base and to the customer-initiated contacts that arise as a consequence of the
17 Qwest’s BOC’s near-monopoly control of the local service market. Competing long distance
18 providers must engage in extensive advertising, direct mail, and telemarketing to promote
19 their service, and do not get anywhere near the quantity of inbound customer contacts as does
20 the BOC, and those which IXCs do receive are primarily the result of the IXCs’ advertising
21 and other promotional efforts, undertaken at not inconsiderable cost to those IXCs.

22

23 59. Qwest response to DOC 15037.

1 36. Customer acquisition is among the most costly aspects of an interexchange carrier's
2 operation. Without the benefit of the embedded ubiquitous customer base that is uniquely
3 available to QCC, other IXCs must pursue active marketing strategies involving extensive
4 media advertising, telemarketing, direct mail, and special promotions (cash, airline miles,
5 etc.). When spread over the number of sales that are actually consummated, these costs can
6 amount to hundreds of dollars per customer acquired. I am aware of at least one analysis that
7 has put such cost at "up to \$300 to \$600 in sales support, marketing and commissions" per
8 customer acquired.⁶⁰ Qwest has itself recently provided this Commission with information
9 as to its own customer acquisition costs. In testimony filed in the *Termination Liability*
10 *Assessments* proceeding, Qwest estimated its customer acquisition cost at 12.7% of retail
11 revenues.⁶¹ Qwest witness D. M. Gude identified Qwest's up-front "sales costs" as
12 including the following activities: "Third Party Sales Commissions, Custom System Design,
13 Account Sales/Service, and Telemarketing."⁶² The prevailing industry customer
14 acquisition cost represents the fair market value of the customer acquisition services that the
15 Qwest BOC provides to QCC. I have been unable to identify any specific provision in any
16 Qwest/QCC affiliate agreements or other documents under which QCC's "payments" to the
17 BOC entity for any customer acquisition services that may be provided will be more than a
18 minute fraction of this fair market value.

19 60. See Borna, Claude, "Combating Customer Churn," in *Business and Management*
20 *Practices*, Vol. 11, No. 3; Pg. 83-85; ISSN: 0278-4831, Horizon House Publications, Inc.,
21 Telecommunications Americas Edition (March, 2000).

22 61. *In the Matter of Qwest Corporation's Refiling of its Proposed Tariffs Regarding*
23 *Termination Liability Assessments as Applied to Resale Arrangements*, MPUC Docket No.
24 P-421/AM-00-1165, P-421/C-98-10, Direct Testimony of D. M. Gude, Attachment DMG-1.

25 62. *Id.*, at 11.

1 37. The Qwest BOC and 272 Affiliate cannot be considered to “operate independently”
2 unless the Section 272(b)(5) arm’s length transaction requirement is satisfied. Ms. Brunsting
3 and Ms. Schwartz testify that transactions are being recorded, but afford no evidence that the
4 dollar amounts being reflected on the two entities’ books bear any resemblance to the proper
5 valuation of the services provided, i.e., the amounts that firms dealing with each other on a
6 truly arm’s length basis would demand. Consequently, there is no basis for the Commission
7 to conclude that either Sections 272(b)(1) or 272(b)(5) are being satisfied by Qwest.

8
9 **Qwest’s application of the arm’s length standard, as required by the *Accounting***
10 ***Safeguards Order’s* interpretation of Section 272(b)(5), is insufficient.**
11

12 38. Section 272(b)(5) provides that, to the extent a BOC and 272 affiliate contract with
13 each other for services, those services must be conducted on an arm’s length basis, the terms
14 reduced to writing, and made publicly available. The affidavits of Ms. Brunsting and Ms.
15 Schwartz provide a sampling of these affiliate agreements, and refer to Qwest’s web posting
16 for the complete set.⁶³ Each contract includes a brief description of services to be provided,
17 the employees providing the service, and the rate at which the service will be charged. In
18 order to assess the validity of the pricing method assigned by Qwest to the services, the
19 Department propounded information request DOC 15025, asking that Qwest describe and
20 provide supporting documentation pertaining to the basis for the specific transfer prices and
21 transfer pricing methodology for each of the affiliate transaction work orders recorded on the
22 Qwest affiliate transaction website. The parts of this data request not publicly available on
23 Qwest’s website are reproduced here as Attachment 3.

24 63. Brunsting (QCC), at 19-20; Schwartz (Qwest Corporation), at 21.

1 39. FCC affiliate transaction requirements, as set forth in the *Accounting Safeguards*
2 *Order* and applied to Section 272(b)(5) by the *Non-Accounting Safeguards Order*, define the
3 process for determining an arm's length transaction.⁶⁴ For services provided from the BOC
4 affiliate (Qwest Corporation) to the 272 affiliate (Qwest Communications Corporation) where
5 the total billing for that service is estimated annually at over \$500,000, non-tariffed services
6 must be provided at the greater of fair market value or fully distributed cost. To ensure that
7 the appropriate pricing method is used, Qwest provides a Fair Market Value Questionnaire to
8 be filled out concurrently or prior to the execution of the contract. This Questionnaire asks
9 the respondent to specify

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- (1) if the estimated annual billing for this service is greater than \$500,000;
- (2) whether benchmarking studies have been performed (and if so, the studies must be attached to the worksheet); and
- (3) whether an external market exists for the service, and any explanation/studies this would entail.

20 Copies of this questionnaire as provided to the Department (and appended hereto in
21 Attachment 3) indicate consistent misrepresentation, omissions, and errors in this document.

22

23 40. Primarily, and most egregiously, the fair market value questionnaire for consumer

24 64. *Accounting Safeguards under the Telecommunications Act of 1996*, CC Docket No. 96-
25 150, *Report and Order*, 11 FCC Rcd 17539, 17607. and *Non-Accounting Safeguards Order*,
26 11 FCC Rcd 21996 and 21997.

1 markets—joint marketing services⁶⁵ dated 09/05/01 states that <<BEGIN TRADE SECRET
2 END TRADE SECRET>> As
3 a result, no fair market value study or benchmarking report was undertaken. However,
4 contrary to the “anticipations” of Qwest Corporation, billing data provided in response to the
5 Department’s Information Request #15031, total billing for November for the <<BEGIN
6 TRADE SECRET END TRADE SECRET>>⁶⁶ that
7 have provided services to support or benefit QCC indicates that this staff alone invoices
8 charges for <<BEGIN TRADE SECRET END TRADE SECRET>> for just the
9 month of September. This same invoice indicates a previous balance of <<BEGIN TRADE
10 SECRET END TRADE SECRET>> (on which no payments were made and no
11 late charges were assessed).

12

13 41. This information strongly suggests that there may already have been several
14 violations of the arm’s length requirement for joint marketing services, even before Qwest is
15 allowed into the in-region interLATA service business. The balances indicated in the invoice
16 cited above (which, it should be noted, is just one of the invoices for service under the
17 consumer markets section of the joint marketing work order for that time period) clearly
18 indicate that Qwest’s assertions that the total billing for this service would be less than

19 65. See *Fair Market Value Questionnaire*, ASF Number: CSMK 311, included in
20 Attachment 3.

21 66. See *Affiliate Billing Request Form*, BART BAN# BIQCC030, and Invoice NO:
22 A681201, included in Attachment 3.

1 The FCC reiterated this position in the *Third Order on Remand*. In that order, the FCC
2 states:

3
4 The broad interpretation of the “joint marketing and sale of services” exception
5 BellSouth advocates would create a loophole that would allow potential BOC
6 discrimination in countless activities. Section 272(c)(1) would provide little
7 protection against BOC discrimination were we to construe section 272(g)(3) as
8 exempting all activities that may impact on marketing and sales activities from
9 the nondiscrimination requirements.⁶⁹

10

11 43. The *Joint Marketing Work Order* between the Qwest BOC and QCC defines the
12 Agreement as including the following services:

13

14 *Planning for In-region InterLATA (Local Access and Transport Area)*
15 *Services* – Includes planning functions required to be ready to sell
16 interLATA services when 271 relief is granted. Also includes pre-
17 implementation activities such as sales operations functions, budgets,
18 establishing sales expectations, planning sales and promotion functions,
19 developing marketing and customer segmentation plans such as provisioning
20 billing, order entry and management, customer care, reporting, training, and
21 compensation; and determining requirements for changes to systems and
22 processes.

23

24 *Qwest Communications Corporation (QCC) Sales* – Providing various
25 aspects of selling QCC products and services inside and outside the 14 state
26 region such as private line data and out of region long distance. Includes
27 activities such as direct sales, supporting alternative sales channels, support
28 for planning for out of region sales, managing marketing efforts for out of
29 region services, and development of training for Section 272 products,
30 services, policies and processes for sales and sales support personnel.
31

32 Although these descriptions are vague as to the actual development services being provided,
33 the amount billed in October 2001, as discussed above, certainly indicates that a large

34 69. *Third Order on Reconsideration*, 14 FCC Rcd 16325.

1 quantity of work is being provided in connection with these planning services. If the services
2 do, as they appear to from their broad descriptions, entail the 272 affiliate's contracting with
3 the BOC for marketing *planning* functions, then the joint marketing work order violates the
4 FCC interpretation of Section 272(g)(1) as well as Section 272(b)(5).

5
6 44. In addition to the *Joint Marketing Work Order*, several other of the Qwest Affiliate
7 Transactions appear to violate Section 272(b)(5). The *Information Technologies Work Order*
8 contains provisions for "Facilities Management" (floor space in the Qwest Corporation Zuni
9 facility), "Network Access" (access to internal communications and network services),
10 "Processing Services" (end user computing for QCC employees), "Operations Services"
11 (computer attendant), and "Training Services" (Information Technologies Performance
12 Solutions Training). The first provision of this work order, "Facilities Management," appears
13 to be in lieu of a formal real estate lease between QC and QCC for office space in Denver,
14 Colorado. However, unlike a lease, QCC and QC have failed to define the *amount* of office
15 space to be provided to QCC. Either Qwest and QCC have contracted for an undetermined
16 amount of office space, rendering the contract overly vague, or Qwest and QCC have failed
17 to reduce the amount of space covered under this contract to writing, an express violation of
18 Section 272(b)(5)'s requirement that all agreements be reduced to writing and made publicly
19 available. In addition, while Qwest claims that the estimated annual billing for this "service"
20 is below \$500,000, the Department has no way of testing this assertion without knowing the
21 amount of space for which QCC has contracted.

22
23 45. In provisioning network access to *Qwestnet* and network access to internal
24 communications, Qwest provides the following statement to support its fully distributed cost

1 pricing methodology:

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Qwest Corporation provides its affiliates access to its internal computer network as well as internal communications. The network further provides access to shared corporate information such as employee directories and corporate polities which include proprietary information. When taking this service to market, it is important to consider both tangible and intangible aspects of the service. Access and the components of access can be taken to market, i.e., the hardware, software, and employee values can be identified in the market place. However, the intangible portion must also be identified. The intangible portion is what the affiliates are accessing. The affiliates are able to access the Qwest internal network, Global Village, e-mail network, and the underlying data in those network. It should also be noted that some affiliates (such as Section 272 organizations) are limited in the information and applications that are made available to them to comply with appropriate requirements. The value of being able to access information in the network cannot be identified in the markets as no such service can be identified. The network contains information that exists as a result of the aggregation of knowledge within Qwest.

As a result, a similar comprehensive service does not exist in the market. In order to obtain a similar service in the market place, the vendor would have to be able to provide the physical network along with access to a mainframe network and its associated applications. This would also include access to a knowledge repository, access to a communications network, and support for all the above. Therefore, this service cannot be taken to market.

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Based upon this agreement, which is applicable to all affiliates of Qwest, the value of Qwest's internal network is the sum of its tangible (hardware, software) and intangible (Qwest corporation data, including proprietary information) attributes. The pricing has therefore been based upon the fully distributed cost, since (by Qwest's reasoning) no outside market exists that would encompass both tangible and intangible attributes. However, from the caveat regarding the restriction of information to Section 272 affiliates, QCC is presumably not benefitting from the intangible value of Qwestnet. Therefore, with regard to the benefits received by the 272 affiliate, those tangible services are available on the market, and a full

1 market value study should have been performed. To the extent that any information on
2 Qwestnet is *not* blocked from a section 272 affiliate's access, this agreement would constitute
3 contracting for information that would violate the Section 272(b)(1) "operate independently"
4 requirement, as well as the Section 272(c)(1) nondiscrimination safeguards.

5
6 46. That Qwest has entered into many of these affiliate agreements as a way of
7 justifying integrated operation is illustrated in the external market rationale of the Information
8 Technology ("IT") Operations service *Fair Market Value Questionnaire*. Qwest maintains
9 that the mainframe includes "application systems in the area of payroll, human resources,
10 accounting, network, and customer billing. ... The mainframes allow users to find and
11 retrieve information, create/maintain files, store data, print reports/bills, as well as print
12 payroll checks." In justifying why this service was not "taken to market" in order to
13 determine a fair market value, Qwest states:

14
15 Short of placing a RFP in the marketplace, we feel that it will not be
16 possible to obtain market quotes through reasonable efforts. Placing an RFP
17 in the market place with no intent of outsourcing the program would be a
18 poor business practice and could possibly damage Qwest's reputation in the
19 marketplace. Thus, taking this service to market is not feasible.
20

21 The service in question is provided by Qwest to QCC, the unregulated QCC has a strong
22 incentive to operate efficiently in order to maximize profits, and any incentive it would have
23 to contract with its BOC affiliate for IT Operations service would stem from its desire to
24 participate in any economies of scale that such a contract would afford. Qwest, however,
25 clearly indicates that, regardless of the economies of scale that may or may not exist in this
26 case, QCC has no intention of contracting with an outside provider for this service. QCC