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BEFORE THE ARIZONA CORPORATION COMMISSION
2001 JAN 12 P 4:56

AZ CORP COMMISSION
DOCUMENT CONTROL

WILLIAM A. MUNDELL
Chairman
JIM IRVIN
Commissioner
MARC SPITZER
Commissioner

IN THE MATTER OF THE APPLICATION
OF U S WEST COMMUNICATIONS, INC.,
A COLORADO CORPORATION, FOR A
HEARING TO DETERMINE THE EARNINGS
OF THE COMPANY, THE FAIR VALUE OF
THE COMPANY FOR RATEMAKING
PURPOSES, TO FIX A JUST AND
REASONABLE RATE OF RETURN THEREON
AND TO APPROVE RATE SCHEDULES
DESIGNED TO DEVELOP SUCH RETURN.

DOCKET NO. T-01051B-99-0105

COMMENTS OF QWEST
CORPORATION CONCERNING
STAFF'S TIMELINE OF
SIGNIFICANT EVENTS AND
DETAILED SUMMARY OF
SETTLEMENT AGREEMENT

Pursuant to the Procedural Order (dated January 2, 2001),
Qwest Corporation hereby provides written comments on the
timeline of significant events and detailed summary of the
Settlement Agreement filed by Staff on January 8, 2001.

TIMELINE

The timeline filed by Staff is generally both complete and
accurate. What should be clear from the timeline is the
already protracted length of this proceeding and the related
attempt to update Qwest's depreciation rates.

Qwest's (then U S WEST Communications, Inc.) last rate
case was filed in 1993 with a Commission decision issued in

1 January 1995. The depreciation rates incorporated in those
2 rates and charges were set in October 1990. (See Decision No.
3 57128.) In June 1995, the Commission adopted rules mandating
4 competition in the local exchange and intraLATA toll markets.
5 Similarly, the United States Congress has also mandated
6 competition through the enactment of the Telecommunications Act
7 of 1996. As a result, the Commission has issued numerous
8 certificates of convenience and necessity to competitive
9 providers and approved hundreds of interconnection and resale
10 agreements between Qwest and these competitors.
11

12 As demonstrated by Staff's timeline, Qwest commenced its
13 efforts to enter the competitive marketplace by petitioning for
14 a change in its depreciation rates in October 1995. The
15 Commission did not act on Qwest's petition, and Qwest renewed
16 its request with an updated depreciation filing in November
17 1997. At the time of Qwest's renewed application, the
18 depreciation rates were approximately seven years old. Almost
19 two years later, the Commission ordered Qwest to file a rate
20 case as a condition of permitting the consideration of Qwest's
21 depreciation rates to go forward outside a rate case. Qwest
22 filed its rate application on January 8, 1999. However, final
23 depreciation rates were not adopted until May 4, 2000.
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1 The Settlement Agreement represents a reasonable
2 compromise of contested issues, and ends a rate case that has
3 been pending since January 1999, a period of twice the time
4 contemplated by the Commission time clock rule. Sufficient
5 time has elapsed for the Commission to move away from the
6 traditional form of public utility regulation as the means for
7 controlling Qwest's earnings and making decisions about
8 allowable costs of Qwest's individual services. The Settlement
9 Agreement establishes price cap regulation that more closely
10 mirrors the effects of a fully competitive market. The
11 Commission should support such a goal through the adoption of
12 the Settlement Agreement.
13

14 SUMMARY OF SETTLEMENT AGREEMENT

15 The Settlement Agreement enables the Commission to make
16 the important transition from earnings to price cap regulation.
17 In addition to an immediate decrease of \$14.2 million for
18 basic/essential services, the Agreement provides for phased
19 reductions in rates for Basket 1 services over a three-year
20 period. Additionally, consumers benefit directly from Qwest's
21 increased efficiencies through a productivity factor, which
22 includes a 0.5% consumer dividend.
23

24 The Settlement Agreement also contains a number of
25 significant benefits to consumers and competitors. It subjects
26

1 Qwest to new penalties in the form of bill credits for failing
2 to meet service quality standards. Under the Agreement, Qwest
3 must lower charges made to long-distance carries by \$15 million
4 over three years, with the result that long-distance prices for
5 calls within Arizona should be reduced.

6
7 The price cap plan provides Qwest with the incentives to
8 become more efficient and innovative, and to make new
9 investments more rapidly. Qwest will be able to offer a
10 variety of new services and service packages that will respond
11 more directly to consumer needs, and will have the flexibility
12 to price these new offerings to meet market demands.

13 Finally, the Settlement Agreement protects competition by
14 preventing Qwest from raising rates for either non-
15 competitive/basic service or wholesale service in order to
16 subsidize its competitive new service offerings. Establishing
17 a price floor at TSLRIC-coupled with continued application of
18 the Commission's imputation rules-prevents any anti-competitive
19 behavior or cross-subsidization. Simply put, the Settlement
20 Agreement allows Qwest to enter the competitive market place on
21 a more equal footing while providing adequate protection to
22 Arizona consumers and other service providers.

23
24 Qwest agrees with Staff's written summary describing the
25 terms and conditions of the Settlement Agreement. Qwest
26

1 submits the following specific comments on Staff's summary as
2 further clarification.

3 Paragraph 2: Revenue Requirement Deficiency (Page 3).

4 Staff originally supported a rate increase of \$7.2
5 million, while Qwest sought a total revenue increase of \$201.2
6 million. To arrive at the \$42.9 million revenue requirement,
7 the Settlement Agreement employs Staff's original rate base—the
8 lowest of those presented by all parties. (Only three parties,
9 i.e., Qwest, Staff and RUCO, submitted fair value rate bases as
10 required by the Arizona Constitution.) Additionally, the
11 Settlement Agreement adopts Staff's 11.75% return on equity,
12 again closer to the lowest equity return of 11.5% (RUCO) than
13 to Qwest's proposed 14%.
14

15 Paragraph 3: Rate Design (Pages 5-6).

16 The proposed rate design consists of two components. The
17 first component is an immediate net increase of \$17.6 million.
18 However, included within this component are rate decreases
19 totaling \$14.2 million and \$5.0 million in Basket 1 and Basket
20 2 services, respectively. All of the increases associated with
21 this component are on Basket 3 services.
22

23 The second component of the rate design is the ability to
24 increase Basket 3 prices in the future by no more than \$25.3
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1 million. Therefore, all of the increases in the Settlement
2 Agreement, both immediate and future, are to Basket 3 services.

3 The Commission has already designated all services
4 identified in Basket 3 as competitive, or found that sufficient
5 competition exists to justify flexible pricing of these
6 services in prior Qwest dockets. As a result, Qwest already
7 has the ability to increase its rates for Basket 3 services,
8 without any limitation on the amount of revenue realized from
9 such increases. In fact, the Commission's only restriction on
10 Basket 3 prices today is a maximum rate for each service
11 element. In many cases, the maximum rate ceiling is double the
12 rate currently charged by Qwest.
13

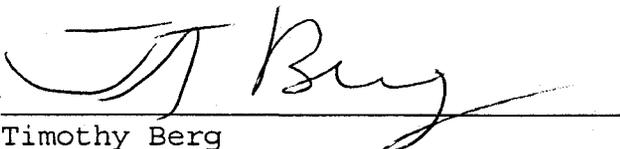
14 The Settlement Agreement provides that Qwest may only
15 recover up to \$25.3 million in overall revenue from rate
16 increases for competitive or flexibly priced services that
17 Qwest may (or may not) elect to implement in the future. This
18 \$25.3 million cap on revenue represents a significant
19 restriction on Qwest's ability to increase prices for Basket 3
20 services. Further, because all of the increases permitted by
21 the Settlement Agreement are applied to only Basket 3 services
22 (while all revenue decreases relate to non-competitive or
23 wholesale services), Qwest's ability to realize any net revenue
24 increases in Basket 3 will be subject to its success in the
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1 competitive marketplace. Thus, Qwest is not guaranteed the
2 recovery of either the initial Basket 3 increases or the
3 subsequent potential Basket 3 increases of \$25.3 million.

4 In conclusion, the Settlement Agreement represents a fair
5 compromise of contested claims in a rate case with many complex
6 issues and a long, difficult procedural history. The
7 Settlement Agreement results in just and reasonable rates for
8 Qwest, including a finding of the fair value of Qwest's
9 property devoted to public service in Arizona and an equitable
10 rate of return on that fair value. The price cap plan provides
11 Qwest with the ability to respond to the changing competitive
12 environment, yet includes adequate protections for customers
13 and competitors during this time of transition. The Commission
14 should find that the Settlement Agreement is in the public
15 interest and approve the Agreement as submitted by Staff and
16 Qwest.
17
18

19 RESPECTFULLY SUBMITTED this 12th day of January, 2001.

20 FENNEMORE CRAIG, P.C.

21
22
23 By 

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1 ORIGINAL AND TEN of the foregoing
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7 COPY of the foregoing hand-delivered
8 This 12th day of January, 2001, to:

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