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Qwest (uswest)

T-010518-99-0105

D/B/A or RESPONDENT:

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01 UTILITIES - NEW APPLICATIONS

- NEW CC&N, RATES, INTERIM RATES, CANCELLATION OF CC&N, DELETION OF CC&N (TERRITORY), EXTENSION OF CC&N (TERRITORY), TARIFF - NEW (NEXT OPEN MEETING), REQUEST FOR ARBITRATION (Telecommunication Act), FULLY OR PARTIALLY ARBITRATED INTERCONNECTION AGREEMENT (Telecom. Act.), VOLUNTARY INTERCONNECTION AGREEMENT (Telecom. Act), MAIN EXTENSION, CONTRACT/AGREEMENTS, COMPLAINT (Formal), RULE VARIANCE/WAIVER REQUEST, SITING COMMITTEE CASE, SMALL WATER COMPANY -SURCHARGE (Senate Bill 1252), SALE OF ASSETS & TRANSFER OF OWNERSHIP, SALE OF ASSETS & CANCELLATION OF CC&N, FUEL ADJUSTER/PGA, MERGER, FINANCING, MISCELLANEOUS Specify

02 UTILITIES - REVISIONS/AMENDMENTS TO PENDING OR APPROVED MATTERS

- APPLICATION COMPANY DOCKET NO., TARIFF PROMOTIONAL DECISION NO. DOCKET NO., COMPLIANCE DECISION NO. DOCKET NO.

SECURITIES or MISCELLANEOUS FILINGS

- 04 AFFIDAVIT, 12 EXCEPTIONS, 18 REQUEST FOR INTERVENTION, 48 REQUEST FOR HEARING, 24 OPPOSITION, 50 COMPLIANCE ITEM FOR APPROVAL, 32 TESTIMONY, 47 COMMENTS, 29 STIPULATION, 38 NOTICE OF INTENT (Only notification of future action/no action necessary), 43 PETITION, 46 NOTICE OF LIMITED APPEARANCE, 39 OTHER Specify Closing Brief

12-18-00 Date

Scott S. Wakefield / Ruco Print Name of Applicant/Company/Contact person/Respondent/Atty. 279-5659 x349 Phone

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BEFORE THE ARIZONA CORPORATION COMMISSION

CARL J. KUNASEK
CHAIRMAN

JIM IRVIN
COMMISSIONER

WILLIAM A. MUNDELL
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

RUCO'S CLOSING BRIEF

The Residential Utility Consumer Office ("RUCO") urges the Arizona Corporation Commission ("Commission") to reject the Settlement Agreement that has been proposed by Qwest and Commission Staff.

Background

In January 1999, Qwest Corporation ("Qwest" or the "Company") (formerly known as U S WEST Communications, Inc. ["U S WEST"]) filed an application to increase its retail rates. Because U S WEST was pursuing accelerated depreciation in a separate docket, the Commission had to delay the rate application's procedural schedule. Due to the delay, the test year of U S WEST's original filing became stale and the Commission required U S WEST to update its application for a more recent test year. Qwest filed revised schedules and

1 testimony, based on a test year ended December 31, 1999 (the "1999 TY filing"). The
2 Commission's Utilities Division ("Staff"), RUCO, AT&T Communications of the Mountain States
3 ("AT&T"), the United States Department of Defense and all other Federal Executive Agencies
4 ("DOD") and Cox Arizona Telecom L.L.C. ("Cox") filed testimony on the 1999 TY filing in
5 August, 2000. Qwest subsequently filed rebuttal testimony. Staff, RUCO, AT&T, Cox and
6 DOD filed surrebuttal testimony in September, 2000. Qwest also filed rejoinder testimony.¹

7 Qwest and Staff entered into a Settlement Agreement resolving all issues between
8 them, which they filed on October 20, 2000. In the Settlement Agreement, Staff agreed that
9 Qwest should be allowed to implement a Price Cap Plan and allowed to increase its revenues
10 by almost \$43 million per year. Qwest and Staff filed testimony in support of the Settlement
11 Agreement on October 27, 2000. RUCO, AT&T, Cox and DOD filed testimony on the
12 Settlement Agreement on November 13, 2000. RUCO filed additional testimony on November
13 15, 2000. Qwest and Staff filed rebuttal testimony on the Settlement Agreement on November
14 20, 2000. The Commission held a hearing on the Settlement Agreement on November 29, 30,
15 December 1 and December 4, 2000. The parties were permitted to file briefs on December 18,
16 2000.

17
18 **Procedural Deficiencies Prevent the Commission From Approving the Settlement.**

19 The record before the Commission includes evidence which parties were not permitted
20 to challenge through cross examination. Because the Commission did not permit cross
21

22
23 ¹ The testimony filed by each of the parties relating to the 1999 TY filing will be referred to as the "1999 TY
24 testimony."

1 examination on evidence that would be essential to any approval of the Settlement Agreement,
2 the Commission must disregard that evidence, and cannot approve the Settlement Agreement.

3 In evaluating the non-unanimous Settlement Agreement, the Commission should
4 determine whether the settlement reasonably resolves the issues before it in light of the entire
5 record. See *Mobil Oil Corp. v. Fed. Power Comm'n*, 417 U.S. 283, 313, 94 S.Ct. 2328, 2348,
6 41 L.Ed. 2d 72 (1974); *Business and Professional People for the Public Interest v. Illinois*
7 *Commerce Commission*, 136 Ill. 2d 192, 144 Ill. Dec. 334, 555 N.E.2d 692, 704 (1989). The
8 Settlement Agreement would permit Qwest to increase its rates by almost \$43 million per year.
9 Settlement Agreement², Section 2. In order for this Commission to approve a revenue
10 increase of \$43 million, the Commission must rely, at least in part, on Qwest's 1999 TY
11 testimony in which it claimed a revenue deficiency of \$201 million.³ At the hearing, the Acting
12 Chief Administrative Law Judge ("ACALJ") admitted Qwest's 1999 TY testimony. Hearing
13 Transcript ("Tr.") pg. 61, line 8 – pg. 70, line 20. RUCO and other parties were not permitted to
14 cross examine Qwest's 1999 TY testimony. Tr. pg. 61, line 18 – pg. 70, line 20; pg. 169, line
15 18 – pg. 170, line 15.

16 Cross examination is a fundamental right and is necessary for a fair proceeding. *Div. of*
17 *Finance v. Industrial Commission*, 159 Ariz. 553, 556, 769 P.2d 461 (App. 1989). RUCO has
18 the right to cross examine evidence offered before the Commission. A.A.C. R14-3-104(A) ("At
19 a hearing a party shall be entitled to...examine and cross-examine witnesses..."). The

21 ² The Settlement Agreement is located in the record as an exhibit to Exh. Q-1. For simplicity, references to
22 the Settlement Agreement in this brief will be to the Settlement Agreement, rather than to Exh. Q-1.

23 ³ There is no other evidence in the record on which the Commission could reach a conclusion that a
24 revenue increase of \$43 million is appropriate, as the 1999 TY testimony filed by RUCO, AT&T, and DOD
proposed revenue decreases, and Staff had proposed a revenue increase of only \$7.2 million. See Exh. RUCO-
27, chart on pg. 1.

1 Commission cannot base its decision on evidence for which it has not permitted parties to
2 cross examine. *Jones v. Industrial Commission*, 1 Ariz. App. 218, 222-223, 401 P.2d 172
3 (1965) (agency must grant parties an opportunity to cross examine the evidence on which it
4 bases its decision).

5 The Commission cannot determine that the Settlement Agreement is a fair resolution in
6 light of the entire record, because it has denied RUCO the opportunity to cross examine the
7 only evidence that supports the Settlement Agreement's revenue increase. Therefore, the
8 Commission should not approve the Settlement Agreement.

9
10 **A \$43 million Revenue Increase Is Unreasonable.**

11 The Settlement Agreement permits Qwest to raise its revenues by \$43 million per year.
12 The Commission should reject the Settlement Agreement, because Qwest's rates should be
13 decreased, not increased.

14 The starting level at which prices are set going into a price cap plan is critically
15 important to achieving optimal results. Tr. at 424; Exh. RUCO-14, pg. 8, lines 9-11 (Johnson).
16 Because the Settlement Agreement would establish a moratorium on rate adjustments during
17 the term of the Price Cap Plan (Settlement Agreement, Section 7), if revenues are set too high
18 going into the plan, Qwest's overearnings could continue during the entire term of the plan. Tr.
19 at 425. Setting revenues too high going into the plan would allow Qwest to generate monopoly
20 profits, unrelated to the skills and performance of its labor and management. Exh. RUCO-14,
21 pg. 8, lines 12-14.

22 In several states, local exchange carriers have accepted, or been required to
23 implement, rate reductions in order to gain pricing flexibility under a price cap plan. Exh.
24

1 RUCO-14, pgs. 9-10 (Wisconsin, Maine, New York, Missouri, North Carolina). Other states
2 have implemented phased-in rate reductions, or required substantial additional infrastructure
3 investment as a "trade-off" for pricing flexibility of a price cap plan. Exh. RUCO-14 at 10. Even
4 Staff witness Shooshan, when he originally proposed a price cap plan in this docket, testified
5 that it would be reasonable for Qwest to make some sort of a "trade-off" for gaining the
6 flexibility of price cap regulation. Exh. S-12 at pg. 20.

7 The \$43 million revenue increase permitted by the Settlement Agreement is excessive.
8 Other than the Company, Staff was the only party that proposed any rate increase, and Staff
9 only proposed a \$7.2 million rate increase. RUCO, DOD and AT&T all proposed revenue
10 decreases as follows: RUCO - \$34 million decrease (Exh. RUCO-10, Schedule A); DOD - \$52
11 million decrease (Exh. DOD-3, Attachment 6); AT&T - \$308 million decrease (Exh. ATT-2,
12 exhibit SMG-1) (or a \$45 million decrease when using the directory revenue imputation from
13 the Company's last rate case [Exh. ATT-2, pg. 40, fn 25]). Rather than a rate increase, the
14 evidence suggests that a rate decrease is in order for Qwest.

15 The \$43 million revenue increase in the Settlement Agreement is not an appropriate
16 compromise of the various revenue requirement proposals, because the negotiation between
17 Qwest and Staff that resulted in that revenue increase disregarded adjustments made by
18 parties other than Staff. Qwest and Staff reached agreement on the \$43 million based on
19 Staff's proposed net operating income adjusted for approximately one-half of four of Staff's
20 adjustments. Exh. Q-3, pg. 3, line 16 - pg. 4, line 13; Exh. RUCO-17, Attachment.
21 Adjustments proposed by other parties that were not duplicative of Staff's adjustments were
22 not included in the computation of the \$43 million increase. Tr. pg. 152, lines 10-16; pg. 153,
23 lines 4-7 (Redding). To the degree that RUCO or other parties had proposed adjustments in
24

1 their 1999 TY testimony that were either not proposed by Staff, or were in excess of a similar
2 adjustment proposed by Staff, the Settlement Agreement gives no consideration to those
3 adjustments.

4 The \$34 million rate decrease that RUCO proposed in its 1999 TY testimony was based
5 on a number of adjustments. Many of the adjustments RUCO proposed were also proposed
6 by Staff. However, RUCO did propose several adjustments that were not also proposed by
7 Staff. Exh. RUCO-23, attachment, lines 38, 47, 48. In addition, several adjustments made by
8 RUCO in arriving at its \$34 million decrease recommendation were similar to, but went
9 beyond, adjustments made by Staff in arriving at its \$7.2 million increase recommendation.
10 For example. RUCO's adjustment to revenues (RUCO adjustment E-1) reversed Qwest's
11 annualization of toll revenues. Staff's witness Brosch characterized Qwest's annualization
12 methodology as inherently unreliable (Exh. S-2, pg. 19, lines 16-17), and acknowledged that
13 RUCO's adjustment is consistent with the Commission's decision in Qwest's last rate case. Tr.
14 pg. 503, lines 16-22 (Brosch). However, Staff's revenue annualization adjustment did not
15 adjust Qwest's proposed annualization of toll revenues. Exh. S-2, pg. 19. In addition, RUCO's
16 adjustment to test year salary and wage expense exceeded Staff's similar adjustment by \$7
17 million. Exh. RUCO-23, attachment, line 26. Staff had made no rebuttal to RUCO's
18 adjustments in its September 2000 surrebuttal testimony. Tr. pg. 498, line 23 – pg. 499, line 4
19 (Brosch). Though RUCO's adjustments exceed similar adjustments by Staff, RUCO's
20 adjustments had no impact on the resulting \$43 million rate increase on which Staff settled.
21 Exh. RUCO-17.

22 Finally, the analysis that lead to the Settlement Agreement's \$43 million rate increase
23 included a discounting by half of Staff's software capitalization adjustment. Exh. RUCO-17.

1 RUCO had made a similar adjustment. There is no reason for the Commission to "give away"
2 half of this adjustment when Qwest has been following the requirements of Statement of
3 Position 98-1 since the beginning of the test year. Tr. pg. 154, lines 13-19 (Redding).

4 The Commission should reject the Settlement Agreement, because it would permit
5 Qwest to increase its rates by \$43 million per year, when in fact, the Commission should be
6 decreasing Qwest's rates.

7
8 **The Price Cap Plan is Seriously Flawed.**

9 The Commission should reject the Settlement Agreement because its Price Cap Plan
10 suffers from a number of serious flaws.

11
12 **1. Productivity Offset is Too Low**

13 First, the productivity offset included in the Price Cap Plan is too low. A productivity
14 offset in a price cap plan is necessary to insure that a carrier's reasonably anticipated
15 increases in productivity are passed on to customers through rates. Exh. RUCO-14, pg. 15,
16 lines 21-25. The Price Cap Plan includes a productivity offset of 4.2 percent. Price Cap Plan⁴,
17 Section 2(ii). This productivity factor fails to adequately represent the productivity increases
18 that Qwest is likely to experience over the life of the Price Cap Plan.

19 Other jurisdictions that have a longer history with price cap plans and productivity
20 factors recognize that productivity offsets in excess of 4.2 percent are appropriate. Most
21 recently, the Federal Communications Commission has adopted a 6.5 percent productivity

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23 ⁴ The Price Cap Plan is appended to the Settlement Agreement as Attachment A. For clarity, RUCO will
24 refer to Attachment A as the Price Cap Plan, or the Plan.

1 offset. Exh. RUCO-14, pg. 18, lines 8-9. Previously, the FCC permitted carriers to choose
2 between 4.7, 5.0 and 5.3 percent productivity offsets. Exh. RUCO-14, pg. 18. Most carriers
3 chose the 5.3 percent, demonstrating that they expected productivity to increase in that range
4 or more. *Id.* Further, some states that set productivity factors in the 3-4 percent range several
5 years ago are discovering that carriers operating under such price cap plans are significantly
6 overearning, another indication that the 3-4 percent range is too low. *Id.*

7 In addition, the Price Cap Plan's 4.2 percent productivity offset fails to recognize the
8 productivity increases expected as a result of the recent merger of U S WEST and Qwest. In
9 the merger docket, Qwest and U S WEST estimated that the merger would result in synergies
10 of approximately \$10.5 to \$11 billion during the period 2000 to 2005. Decision No. 6267,
11 Finding of Fact 12. The 4.2 percent productivity factor originally proposed by Staff and
12 incorporated into the Settlement Agreement was based on an analysis of Qwest's historic
13 productivity from 1995 to 1998. Tr. pg. 617-618 (Shooshan). It does not include any savings
14 expected to result from the merger. Tr. pg. 618 (Shooshan). During the term of the Price Cap
15 Plan, Qwest expects to achieve synergies beyond those it historically achieved, yet those cost
16 savings are not reflected in the 4.2 percent productivity factor in the Settlement Agreement
17 Price Cap Plan.

18
19 **2. The Plan Has Too Few Baskets**

20 A second flaw in the Price Cap Plan is the number of baskets it includes. The
21 Settlement Agreement provides that there are only two retail baskets—Basket One for basic
22 and non-competitive services, and Basket Three for services that have been previously
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1 declared competitive, all new services, and new service packages that include at least one
2 service already in Basket Three. Basket Two would contain wholesale services.

3 The Price Cap Plan is flawed because it fails to separate business and residential
4 services into separate baskets. Placing business and residential services together in one
5 basket would permit Qwest to raise the price of some residential services (those not subject to
6 the "hard cap" of Basket One⁵), while at the same time reducing the price of business services.
7 Staff's own witness, Mr. Dunkel, testified that in any regulatory structure adopted by the
8 Commission, the Commission should insure that price restructuring of residential rates be
9 revenue neutral only within the residential class of rates, and that price restructuring of
10 business services be revenue neutral within the business class. Exh. S-9, pg. 35, line 16 – pg.
11 36, line 2. The Price Cap Plan omits this vital protection. Instead, it would permit residential
12 prices to increase while business prices are lowered.

13 The Price Cap Plan also fails to provide separate baskets for services facing various
14 degrees of competition. The Plan either requires that Qwest's pricing is strictly controlled, or is
15 virtually completely flexible. This extreme dichotomy in pricing flexibility ignores the fact that
16 competition tends to emerge gradually, and that few markets can be characterized as purely
17 competitive or purely monopolistic. Exh. RUCO-14, page 22. The Settlement Agreement Price
18 Cap Plan denies the Commission the opportunity to classify services in accordance with the
19 subtle nuances of actual market conditions. See Exh. RUCO-14, page 23.

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21
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23 ⁵ Pursuant to Section 2(c)(i) of the Price Cap Plan, prices for certain basic services in Basket One are
24 capped and cannot be increased during the term of the Price Cap Plan. This "hard cap" is in contrast to other
services in Basket One, whose prices can be increased subject to other restrictions set forth in the Plan.

1 **3. The Plan Mis-classifies New Services and Packages**

2 The Price Cap Plan provides that all new services will be placed in Basket Three, and
3 that new service packages that include at least one service already in Basket Three will be
4 placed in Basket Three. The automatic classification of all such new services and packages
5 as competitive, without actual consideration of Qwest's market power, is a third flaw in the
6 Price Cap Plan.

7 Under its current rules, the Commission grants pricing flexibility to a telecommunications
8 carrier only after the Commission has determined that the carrier lacks market power in the
9 provision of a service. See A.A.C. R14-2-1108, -1109; Tr. pg. 536, lines 14-20 (Dunkel).
10 Staff's witness Dunkel testified in his 1999 TY testimony that the Commission's consideration
11 of market power is important (Exh. S-9, pg. 13, lines 31-32), that new services should have to
12 pass the same competitive test as other services to attain pricing flexibility (*Id.* at pg. 37, lines
13 8-14), and that new packages that contain any services not currently classified as competitive
14 should not be granted competitive pricing flexibility (*Id.*). The Price Cap Plan circumvents the
15 market power assessment that Mr. Dunkel agrees is critical, and automatically permits the
16 Company to price new services and packages flexibly.

17 The danger of permitting all new services to be placed in Basket Three is particularly
18 evident for new services that are ancillary to existing services that are not yet classified as
19 competitive. For example, a new Custom Calling feature should not be placed into Basket
20 Three, because it cannot be obtained apart from local exchange service, which is not yet
21 classified as competitive. Customers desiring the new Custom Calling feature would not have
22 sufficient opportunities to obtain the new feature from other providers, because it can only be
23 obtained from the carrier who provides dial tone to the customer. Until the basic dial tone

1 service is determined to be competitive, Custom Calling features that are ancillary to it should
2 not be placed into Basket Three. See Tr., pg. 449, line 6 – pg. 451, line 5; pg. 472, line 21 –
3 pg. 473, line 4 (Johnson); pg. 627, lines 12-19 (Shooshan).

4 Just because a service is new does not mean that competitive alternatives exist or that
5 Qwest should be granted wide pricing freedom. Exh. RUCO-14, page 25, lines 24-25
6 (Johnson). Instead of automatically placing new services and packages in Basket Three, new
7 offerings should be subjected to the criteria of the Commission's Rule R14-2-1108.

8 9 **4. Lax Pricing Provisions**

10 A fourth flaw in the Price Cap Plan is that its pricing provisions are too permissive,
11 raising the possibility that rates may become unreasonable. The Plan provides that prices for
12 non-hard capped Basket One services may be increased by up to 25 percent per year. Price
13 Cap Plan, Section 2(c)(iii). Qwest witness Teitzel clarified at the hearing that, despite the fact
14 that the language of the Price Cap Plan says that this provision applies to "individual service
15 prices," in fact, it is meant to apply to individual rate elements. Tr. pg. 364, line 21 – pg. 366,
16 line 17 (Teitzel). While this is an improvement in the Price Cap Plan, it still permits Qwest to
17 increase prices too much, especially for services that are less discretionary, such as Call
18 Waiting. See Exh. RUCO-14, pg. 28, lines 4-13 (Johnson); Tr. pg. 442, lines 15-17 (Johnson).

19 In addition to an excessive price ceiling for certain Basket One services, the Price Cap
20 Plan also includes price floor provisions for Basket Three services that undermine the
21 development of competition. First, the Price Cap Plan would permit Qwest to place
22 competitors in a price squeeze. The Price Cap Plan would permit Qwest to use the current
23 1FR price as the floor for new service packages in Basket Three that include basic residential
24

1 service along with other services. Price Cap Plan, Section 4(e), (f). The 1FR rate is currently
2 \$13.18. Tr. pg. 545, lines 11-16 (Dunkel). The price that competitors pay to purchase the loop
3 as an unbundled network element ("UNE") is \$21.98 on a statewide average. Tr. pg. 527,
4 lines 12-13. By using \$13.18 as the price floor for the basic service element of a package,
5 Qwest could undercut the price of its competitors that must pay \$21.98 for the same element in
6 a similar package to residential customers. This sort of price squeeze discourages competitive
7 activity for residential customers, and makes it more difficult or impossible for competitors that
8 are dependent on UNEs to recover their costs or earn a profit. Exh. RUCO-15, pg. 4, lines 15-
9 17 (Johnson); Tr. pg. 428, lines 2-17 (Johnson).

10 Further, the Price Cap Plan would permit Qwest to engage in this price squeeze on a
11 geographically targeted basis. Section 4(g) of the Price Cap Plan allows Qwest to offer new
12 services and packages in Basket Three to select customer groups based on their geographic
13 location. Qwest could use this opportunity to offer deep discounts in market niches where it is
14 facing competitive pressure, while maintaining its rates and revenue stream in other parts of
15 the state. Tr. pg. 428, line 18 – pg. 429, lines 10 (Johnson).

16 Given that the Commission has recently found that there is no effective competition for
17 basic phone service (Decision No. 62672, Finding of Fact No. 26, pg. 28, June 30, 2000), the
18 Commission should reject the Settlement Agreement's Price Cap Plan that would further
19 frustrate the development of competition.

20
21 **5. Inadequate Service Quality Protections**

22 An additional flaw in the Price Cap Plan is that it provides inadequate protections
23 against further service quality deterioration. The proposed Price Cap Plan creates a greater
24

1 incentive for Qwest to sacrifice service quality in search of higher profits. Tr. pg. 430, lines 7-9
2 (Johnson). The Settlement Agreement provides that, for any year in which Qwest becomes
3 subject to penalties under two or more of the five categories defined in Section 2.6 of Qwest's
4 Service Quality Plan Tariff, additional credits of \$2.00 per year for each access line will be
5 imposed. Settlement Agreement, Section 5. The additional credits are not adequate to ensure
6 that Qwest will provide quality service, especially considering the increased incentives Qwest
7 will have to increase profits at the expense of service quality. Exh. RUCO-14, pg. 30, line 26 –
8 pg. 31, line 9 (Johnson).

9
10 **The Settlement Agreement's "No Refund" Provision Is Unlawful.**

11 The Commission should reject the Settlement Agreement because it includes a
12 provision that is unlawful. Section 13 of the Settlement Agreement provides that, if the Price
13 Cap Plan is determined by a court to be unlawful, Qwest would have no obligation to refund
14 revenues collected while the plan was in effect. This provision is contrary to the Arizona law.

15 Arizona's Constitution provides that rates established by the Commission remain in
16 effect during the pendency of any appeal of those rates. A.R.S. Const., Art. XV, § 17.
17 Because the Constitution prohibits a stay of rates while they are on appeal, the Commission
18 must leave the door open for refunds upon a successful appeal. Precluding both pre-appeal
19 stays and post-appeal refunds violates due process. See *Mountain States v. Ariz. Corp.*
20 *Com'n*, 124 Ariz. 433 at 435, 604 P.2d 1144 at 1146 (App. 1979).

21 The Commission should generally order a refund upon a successful appeal, unless
22 doing so would be unjust in the particular circumstances of the case. *Id.* at 436, 604 P.2d at
23 1147. The Commission cannot conclude at this time that it would be unjust to order a refund if

1 the Price Cap Plan were determined to be unlawful, because all the circumstances of the case
2 may not yet be apparent. Circumstances could come to light in the future that would be
3 relevant to the determination of whether to require a refund. Therefore, the Commission
4 should not approve the Settlement Agreement's provision that relieves Qwest of all refund
5 obligations if the Price Cap Plan is ultimately determined to be unlawful.

6
7 **Specific Changes That Clarify Ambiguities.**

8 At the conclusion of the hearing, the ACALJ asked parties to include in their briefs any
9 specific changes to the Settlement Agreement that they believed would clarify ambiguities.
10 The ACALJ indicated that the suggested changes would not waive a party's opposition to the
11 Settlement Agreement. RUCO proposes the following modifications to the Settlement
12 Agreement at the request of the ACALJ. These proposals are in no way meant to indicate that
13 RUCO supports approval of the Settlement Agreement if these modifications are accepted.

14 Section 3(g) of the Price Cap Plan provides "Nothing in this Price Cap Plan is intended
15 to change or modify in any way the imputation requirements contained in A.A.C. R14-1-1310."
16 RUCO proposes two modifications, both of which it believes Qwest and Staff will find
17 agreeable. First, the rule reference should be to R14-2-1310. Qwest witness Teitzel agreed
18 that the Settlement Agreement reference included a typographical error. Tr. pg. 248, lines 2-5.
19 Second, the language is placed in Section 3 of the Price Cap Plan, which sets forth
20 requirements specific to Basket Two. RUCO believes that that language is meant to also
21 apply to the pricing of services in other baskets. Therefore, the language should be either
22 repeated in Sections 2 and 4, or moved to a section of the plan that is not specific to any

1 particular basket. Again, Qwest witness Teitzel testified that the requirements of Rule R14-2-
2 1310 would apply to all services in the Settlement Agreement. Tr. pg. 242, lines 11-16.

3 Section 2(c)(iii) of the Price Cap Plan provides that "Individual service prices within
4 Basket 1, other than those services listed in subpart i) above [services subject to the hard cap],
5 may increase no more than 25 percent within a year." Dr. Johnson had recommended that this
6 provision apply to individual rate elements, rather than individual services. Qwest witness
7 Teitzel clarified at the hearing that the intent was that the provision apply to individual rate
8 elements. Tr. pg. 364-366. Therefore, RUCO proposes that in Section 2(c)(iii), the phrase
9 "Individual service prices" be replaced with "Individual rate element prices."

10 Section 2(c)(i) of the Price Cap Plan provides that the hard cap on certain Basket One
11 services will remain "throughout the term of the Price Cap Plan." The Settlement Agreement
12 itself (not the Price Cap Plan attached) provides that renewal or modification of the Price Cap
13 Plan is subject to approval by the Commission, and that the Plan will continue in effect until the
14 Commission either approves a modification to it, or terminates it. Settlement Agreement, pg.
15 6. The language of these two provisions may permit Qwest to claim that, if the Commission
16 has neither modified nor terminated the plan after three years, the hard cap on certain Basket
17 One services expires at that time. RUCO believes that the language in the Settlement
18 Agreement itself should be clarified as follows (inserted text underlined): "Renewal or
19 modification of the Price Cap Plan at the end of the initial term is subject to approval by the
20 Commission. Until the Commission approves any modifications to the Price Cap Plan, or
21 orders a termination of the Plan after its term, the Plan, including the hard cap on certain
22 Basket One services, shall continue in effect."

1 Finally, the Commission should clarify that the requirement to impute the price of
2 essential facilities and services applies even if the facility or service in question is not essential
3 for some competitors. Exh. RUCO-14 at 29-30. Exh. RUCO-15, pgs 3-4 (Johnson).
4 Currently, ambiguities in the Commission's price imputation rules exacerbate the potential for
5 anticompetitive pricing under the proposed price cap plan. The Commission's Rule R14-2-
6 1310(C) requires Qwest to price its retail services above the sum of the TSLRIC of all
7 nonessential services and facilities, plus the imputed prices of all essential services and
8 facilities. Rule 14-2-1302 defines "essential facility or service". Further, the Commission's
9 unbundling rule (R14-2-1307) lists certain specific services which are classified as essential
10 facilities or services. Rule R14-2-1310(C) does not cross reference the list of services
11 included in Rule R14-2-1307, and therefore, it is unclear whether this list applies to the
12 imputation requirements contained in Rule R14-2-1310(C). It is not clear whether the list
13 contained in Rule R14-2-1307 is all inclusive, or, in the alternative, whether services not
14 included in the list can also be considered "essential facilities or services." For example, the
15 list includes terminating access, but not originating access. Originating access may not be
16 essential for all competitors, but clearly would be essential for most competitors. Exh. RUCO-
17 14, pg. 30, lines 1-3 (Johnson). Nonetheless, Qwest may attempt to impute the price of
18 terminating access, but not originating access, as Qwest believes that originating access is not
19 an essential element. Tr. pg. 338, line 20 – pg. 339, line 2 (Teitzel).

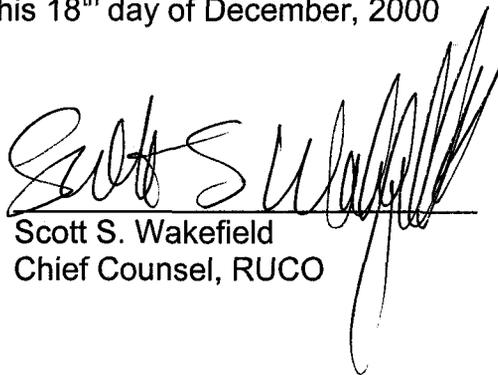
20 The ambiguities in the Commission's imputation rules become more problematic in the
21 context of the proposed Price Cap Plan. Under the Price Cap Plan, Qwest is granted
22 increased pricing flexibility and retail services can more easily be classified as competitive.
23 Qwest should not be allowed the increased pricing flexibility associated with the Price Cap
24

1 Plan until the ambiguities in the Commission's imputation rules are resolved. At a minimum,
2 the Commission should first clarify that the requirement to impute the price of essential
3 facilities and services applies even if the facility or service in question is not essential for some
4 competitors. Exh. RUCO-14 pgs. 29-30; Exh. RUCO-15, pgs 3-4 (Johnson).

5
6 **Conclusion**

7 The Settlement Agreement would allow Qwest to increase its rates at a time when the
8 Commission should be decreasing Qwest's rates. Further, the Price Cap Plan suffers from
9 serious deficiencies that jeopardize the future of competition in Arizona. In addition, the Plan
10 includes an unlawful provision regarding refunds if the Plan is later found to be unlawful.
11 Finally, the procedure by which the Commission is examining the Settlement Agreement is
12 flawed. For these reasons, RUCO recommends that the Commission reject the Settlement
13 Agreement.

14 RESPECTFULLY SUBMITTED this 18th day of December, 2000

15
16 
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