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BEFORE THE ARIZONA CORPORATION COMMISSION

MARC SPITZER
Chairman

WILLIAM A. MUNDELL
Commissioner

JEFF HATCH-MILLER
Commissioner

MIKE GLEASON
Commissioner

KRISTIN K. MAYES
Commissioner

Arizona Corporation Commission

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IN THE MATTER OF QWEST
CORPORATION'S FILING AMENDED
RENEWED PRICE REGULATION PLAN

Docket No: T-01051B-03-0454

IN THE MATTER OF THE INVESTIGATION
OF THE COST OF TELECOMMUNICATIONS
ACCESS

Docket No. T-00000D-00-0672

**NOTICE OF FILING REBUTTAL TESTIMONY
OF TIMOTHY GATES ON BEHALF OF
TIME WARNER TELECOM OF ARIZONA LLC**

Time Warner Telecom of Arizona LLC hereby files the rebuttal testimony of
Timothy J. Gates in the above-referenced matter.

1 RESPECTFULLY SUBMITTED this 12th day of January, 2005.

2 LEWIS AND ROCA

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BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

MARC SPITZER, Chairman
WILLIAM A. MUNDELL
JEFF HATCH-MILLER
MIKE GLEASON
KRISTIN K. MAYES

IN THE MATTER OF QWEST)	DOCKET NO. T-01051B-03-0454
CORPORATION'S FILING AMENDED)	
RENEWED PRICE REGULATION)	
PLAN.)	
)	
IN THE MATTER OF THE)	DOCKET NO. T-00000D-00-0672
INVESTIGATION OF THE COST OF)	
TELECOMMUNICATIONS ACCESS)	
)	

Rebuttal Testimony Of Timothy J Gates

On Behalf of Time Warner Telecom of Arizona, Inc.

January 12, 2005

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1 **Witness Introduction**

2 **Q. PLEASE STATE YOUR NAME, OCCUPATION AND BUSINESS**
3 **ADDRESS.**

4 A. My name is Timothy J Gates. My business address is QSI Consulting, 819
5 Huntington Drive, Highlands Ranch, Colorado 80126.

6 **Q. WHAT IS QSI CONSULTING, INC. AND WHAT IS YOUR POSITION**
7 **WITH THE FIRM?**

8 A. QSI Consulting, Inc. ("QSI") is a consulting firm specializing in traditional and
9 non-traditional utility industries, econometric analysis and computer aided
10 modeling. I currently serve as Senior Vice President.

11 **Q. ARE YOU THE SAME TIMOTHY GATES WHO FILED DIRECT**
12 **TESTIMONY IN THIS PROCEEDING ON BEHALF OF TIME WARNER**
13 **TELECOM OF ARIZONA ("TWTA"), A CERTIFICATED**
14 **COMPETITIVE LOCAL EXCHANGE CARRIER ("CLEC") IN**
15 **ARIZONA?**

16 A. Yes, I am.

17 **Purpose of Rebuttal Testimony**

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

19 A. The purpose of my rebuttal testimony is to respond to certain positions taken in
20 the rebuttal testimonies of Mr. Teitzel and Mr. McIntyre on behalf of Qwest.
21

Testimony of Scott A. McIntyre

22
23
24 **Q. HAVE YOU REVIEWED THE REBUTTAL TESTIMONY OF MR.**
25 **MCINTYRE?**

26 A Yes, I have.

27 **Q. PLEASE ADDRESS MR. MCINTYRE'S DEFINITION OF SPECIAL**
28 **ACCESS.**

29 A. Mr. McIntyre seems to confuse a very simple concept. He says at page 11 of his
30 testimony that private line circuits are referred to as special access "...because
31 they bypass the public switched network and its associated switched access
32 charges." This is not a correct statement or definition. Special access is simply a
33 dedicated circuit between two points. A company will select a dedicated circuit
34 between two points when the traffic justifies moving from switched services to
35 dedicated services.

36 **Q. MR. MCINTYRE STATES AT PAGE 11 THAT CLECS "CAN USE THE**
37 **SWITCHED NETWORK TO CARRY THIS TRAFFIC." DO YOU**
38 **AGREE?**

39 A. Yes. But Mr. McIntyre misses the point with his statement. Of course CLECs
40 could use either dedicated or switched services from a technical perspective. The
41 point is that under certain traffic situations, dedicated circuits become more
42 economical for CLECs and for ILECs for that matter. Mr. McIntyre admits as
43 much when he notes that "Such circuits provide a significant advantage over

44 paying for switched access, but they are not a necessary element from a network
45 perspective.”

46 **Q. WHAT DETERMINES WHEN A CLEC USES SWITCHED ACCESS OR**
47 **SPECIAL ACCESS FOR MANAGING TRAFFIC?**

48 A. It is Qwest’s pricing of those two respective services, combined with traffic
49 patterns that provide the incentive for carriers to use one or the other.

50 **Q. DOES MR. MCINTYRE PROVIDE ANY SUPPORT FOR HIS CLAIM**
51 **THAT “PRIVATE LINE HAS BEEN HIGHLY COMPETITIVE FOR**
52 **MANY YEARS.”? (MCINTYRE AT 12)**

53 A. No. Mr. McIntyre provides no support for his statement. Not only does he
54 provide no support for his statement, but he seems to ignore the fact competitors
55 can leave the market.

56 **Q. BUT AT PAGE 13 OF HIS TESTIMONY HE STATES THAT THERE ARE**
57 **“CURRENTLY MORE THAN 25 PROVIDERS IN ARIZONA WITH**
58 **TARIFFS OFFERING PRIVATE LINE (OR SPECIAL ACCESS)**
59 **SERVICES.” ISN’T THAT EVIDENCE OF COMPETITION?**

60 A. Not necessarily. Simply because a provider has a tariff on file does not mean that
61 they are actually offering a service that is competitive with that offered by
62 Qwest.¹ Nor is it any indication that such carriers striving to gain a toehold in the
63 market have competitive options throughout the market. The is precisely the
64 dilemma in with which TWTA is faced in Arizona, that being that it is restricted
65 from accessing certain segments of the market because Qwest is the only

¹ In response to TWTA Request 02-003, Qwest admitted that it “...has no reasonable way of knowing if the provider(s) listed are currently providing service in accordance with their tariffs.”

66 alternative available in many locations. Although Qwest does not provide any
67 support for its claim that 25 carriers provide special access service, even if it was
68 true, TWTA faces a monopoly supplier of critical inputs in order to reach many
69 customers. In other words, Qwest maintains pockets of monopoly control for
70 special access at multiple lucrative locations within the areas for which Qwest
71 seeks additional pricing flexibility. So long as Qwest controls these highly sought
72 after segments of the market, it maintains significant market power, which is a
73 recipe for disaster should Qwest receive additional pricing flexibility as a result of
74 this proceeding.

75 **Q. MR. MCINTYRE STATES THAT “THE PRIVATE LINE MARKET IS**
76 **EASY TO ENTER.” IS THAT CORRECT?**

77 A. I think Mr. McIntyre is overreaching with that statement. Because of the
78 investment and time required, entry is not easy, quick or cheap. But I would not
79 dispute the fact that in most situations, entry into the private line business would
80 be somewhat less expensive and time consuming than entering the retail
81 telecommunications business.

82 **Q. AT PAGE 14, MR. MCINTYRE SUGGESTS THAT IT MIGHT BE MORE**
83 **ECONOMICAL FOR TWTA TO BUILD FACILITIES ITSELF AS**
84 **OPPOSED TO PURCHASING SERVICES FROM QWEST. DO YOU**
85 **HAVE ANY COMMENTS ON THAT POSITION?**

86 A. Yes. I think that is an odd statement for Qwest to make, from at least a couple
87 perspectives. First, you would think that Qwest would want to keep carriers on its
88 network as opposed to giving them incentives to build alternative networks.

89 Second, Mr. McIntyre's statement seems to suggest that its rates do not reflect the
90 most cost efficient, forward looking network. In fact, in response to TWTA
91 Request No. 02-004, Qwest states "It is Qwest's position that in certain
92 circumstances alternative providers can build facilities more economically than
93 buying services from Qwest." This seems to indicate that Qwest's pricing
94 assumptions do not reflect forward-looking assumptions, and, as such, result in
95 higher rates than would be expected in a competitive environment.

96 **Q. DO YOU DISPUTE MR. MCINTYRE'S SUGGESTION THAT TWTA**
97 **DOES PROVIDE ITS OWN FACILITIES IN CERTAIN AREAS?**
98 **(MCINTYRE AT 14)**

99 A. No. That is the way competition develops over time. In the situation discussed
100 by Mr. McIntyre, TWTA had facilities close to the building in question, but was
101 denied access. Absent this denial of access, TWTA might have provided an
102 attractive competitive alternative for businesses in that building. That does not
103 mean, however, that CLECs can always use their own facilities to provide service.

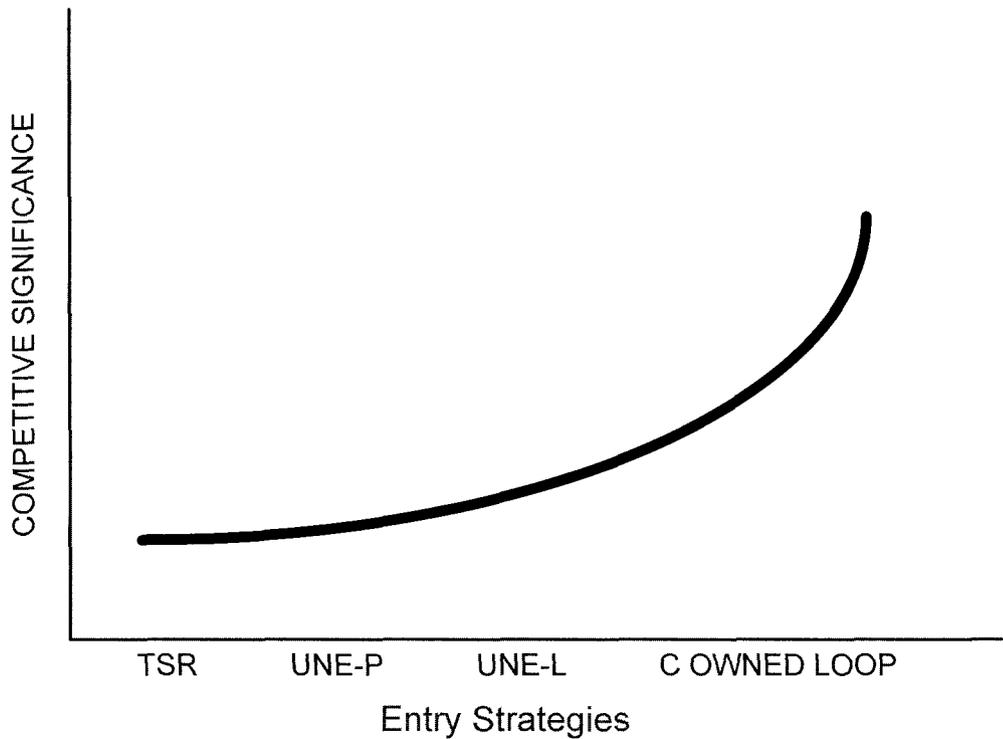
104 Initially providers enter the market through total service resale ("TSR") or
105 limited build-out. Then, over time, new entrants will use UNEs and ultimately
106 build facilities (assuming that no barriers to entry such as the ones discussed in
107 my direct testimony exist) to serve customers once the market and economics
108 justify the investment. If, however, barriers such as restricted access to buildings
109 do exist, investment in facilities would be of little value to a competitive carrier.
110 Under these circumstances, only one alternative exists – to buy special access
111 from Qwest.

112 **Q. PLEASE EXPLAIN THE CONTINUUM OF ENTRY STRATEGIES THAT**
113 **CLECS EMPLOY AND THEIR RELATIVE COMPETITIVE**
114 **SIGNIFICANCE.**

115 A. The continuum would be from the least effective form of competition (TSR) to
116 the most effective form of competition (CLEC-owned loop) with the following
117 strategies in increasing order of competitive significance – TSR – UNE-P – UNE-
118 L – CLEC-Owned Loop. In other words, TSR has the least impact on Qwest and
119 a CLEC that builds its own loops has the greatest competitive impact on Qwest.

120 The chart below provides a graphic representation of the continuum.

**Competitive Significance of Entry Strategies
Used by CLECs**



121

122 **Q. ARE YOU SUGGESTING THAT THE COMMISSION SHOULD FOCUS**
123 **EXCLUSIVELY ON FACILITIES-BASED COMPETITION IN**
124 **DETERMINING WHETHER QWEST HAS MET ITS BURDEN WITH**
125 **RESPECT TO R14-2-1108(B)?**

126 A. Yes. While the Federal Telecom Act does not express a preference for one form
127 of entry over the other, it is clear that facilities-based competition is the ultimate
128 goal, and for good reason. Carriers use resale and UNEs to quickly enter the
129 market, gain customers and hopefully some profits, to allow them to build their
130 own facilities over time. It is only with facilities-based competition that new
131 entrants can gain their independence from Qwest and truly differentiate their
132 services from those of the incumbent. As such, the Commission should give
133 significant weight to facilities-based entry (CLEC-owned loops and CLECs
134 purchasing Qwest UNE-Loops) and no weight to resale-based entry (resale and
135 CLEC use of Qwest UNE-P loops).

136 **Q. WHY IS FACILITIES-BASED COMPETITION IMPORTANT TO THE**
137 **DEVELOPMENT OF EFFECTIVE COMPETITION IN**
138 **TELECOMMUNICATIONS?**

139 A. There are two markets that directly impact retail competition – the retail market
140 and the wholesale market. Qwest is the sole supplier of wholesale inputs for
141 CLECs providing retail services via UNE-P and/or resale.

142 Without a network of its own, a carrier is relegated to a “resale” role in the
143 market. Successful marketing normally requires product differentiation and price
144 competition. It is difficult, if not impossible, for a carrier to differentiate its

145 product when it is reselling all or part of the incumbent's product. The reseller is
146 dependent upon the underlying carrier for quality of service, features, speed to
147 market, and facilities. Just as important, the reseller is dependent upon the
148 underlying carrier for its cost of service. In other words, the cost that the reseller
149 pays Qwest becomes the most important cost of the reseller, and is probably the
150 only cost over which the reseller has no control or influence whatsoever.

151 Qwest's Wholesale Product Catalog describes the activities of CLEC
152 resellers as follows: "Resale CLECs purchase Qwest's products and services, at a
153 resale rate either through a separate negotiated agreement with Qwest or a tariff,
154 and resell these products and services to their end-users."² Because of Qwest's
155 monopoly in the wholesale market, it is not appropriate to include services offered
156 by CLECs through resale or UNE-P in any market share or competitive analysis.

157 **Q. ARE YOU SUGGESTING THAT CLEC USE OF RESOLD QWEST**
158 **SERVICES AND CLEC USE OF QWEST UNE-P SERVICES DOES NOT**
159 **MEET THE STANDARD OF "...FUNCTIONALLY EQUIVALENT OR**
160 **SUBSTITUTE SERVICES....?"**

161 A. That's correct. As discussed above, TSR and UNE-P are *Qwest-provided services*
162 *on behalf of the CLEC*. In fact, the CLECs are dependent upon Qwest for the
163 timing of service delivery, quality of service and features. As such, it is Qwest
164 making these finished services "available", albeit on behalf of the CLEC. When
165 CLECs offer services via resale or UNE-P they are not "an alternative provider of
166 the service."

² See <http://qwest.com/wholesale/pcat/resale.html>

167 **Q. IF CLECS BUILD THEIR OWN FACILITIES, WOULD SERVICES**
168 **OFFERED OVER THOSE FACILITIES BE CONSIDERED EFFECTIVE**
169 **COMPETITION?**

170 A. Yes, if the CLEC offered services that were comparable in terms of rates, terms
171 and conditions. Simply overbuilding the Qwest network is not sufficient to result
172 in effective competition unless that network can provide “competitive” alternative
173 services.

174 **Q. WHY IS IT IMPORTANT FOR THE COMMISSION TO CONSIDER THE**
175 **IMPORTANCE TO THE MARKET OF FACILITIES BASED**
176 **COMPETITION IN THE CONTEXT OF THIS PROCEEDING?**

177 A. Because, as I will discuss later in this rebuttal testimony, and as I have discussed
178 in my direct testimony, TWTA has, in several instances, been denied the
179 opportunity to compete in this manner.

180 **Q. GIVEN THIS BACKGROUND WHAT IS YOUR RECOMMENDATION**
181 **TO THE COMMISSION REGARDING MR. MCINTYRE’S REBUTTAL**
182 **OF YOUR TESTIMONY?**

183 A. Mr. McIntyre’s rebuttal is vague and unconvincing. The apparent purpose of Mr.
184 McIntyre’s rebuttal of my testimony is to show that Qwest does not have a
185 monopoly on dedicated services. His limited rebuttal, however, does not address
186 the facts that show competition for such services is limited at best. In my direct, I
187 showed (based on Qwest data) that Qwest does not face significant competition
188 for these services and that it is earning supracompetitive revenues. Mr. McIntyre
189 did not address the Qwest ARMIS report that I discussed (Gates Direct at 13)

190 showing an incredible 74 percent rate of return on special access services in
191 Arizona or the fact that Qwest is raising rates at the federal level (Gates Direct at
192 31).

193 The Commission should disregard Mr. McIntyre's rebuttal of my
194 testimony on special access services and find that competition is not sufficient in
195 Arizona to discipline Qwest's pricing. Instead, the Commission should use this
196 opportunity to move Qwest's special access rates closer to cost, which, according
197 to Qwest, would result in more purchases from its intrastate tariff. This would
198 also eliminate the ability of Qwest to disadvantage its competitors who must rely
199 upon Qwest's services for the foreseeable future. This is especially important to
200 the competitive side of the market given the impending demise of UNE-P.

201 **Testimony of David L. Teitzel**

202 **Q. HAVE YOU REVIEWED THE REBUTTAL TESTIMONY OF MR.**
203 **TEITZEL?**

204 **A. Yes, I have.**

205 **Q. AT PAGE 56 OF HIS TESTIMONY, MR. TEITZEL SUGGESTS THAT**
206 **TWTA SEEKS PRICE REDUCTIONS FOR SPECIAL ACCESS BUT**
207 **PROVIDES NO MEANS "...TO OFFSET THOSE REVENUE**
208 **REDUCTIONS." PLEASE COMMENT.**

209 **A. From this testimony,³ it is clear that Mr. Teitzel believes that Qwest has an**

³ Mr. Teitzel's testimony is in reference to my direct testimony at page 5. In that passage, I refer to implicit subsidies in general, but cite as a specific example, the implicit subsidies which flow to Qwest from its Special Access services. Presumably, Mr. Teitzel's testimony refers to implicit subsidies flowing to Qwest from its special access services.

211 inalienable right to monopoly revenues – even to revenues derived from services
212 that it claims are highly competitive.⁴ There are two fundamental issues with Mr.
213 Teitzel’s testimony in this area. First, Mr. Teitzel is incorrect in his assertion that
214 there is a prerequisite that in order for Qwest to reduce the rates it currently
215 charges for critical wholesale inputs such as special access services, Qwest’s
216 current monopoly-like revenues must be somehow replaced. This Commission
217 and society at large for that matter are not responsible for ensuring that Qwest
218 continues to earn a certain level of return on its services.

219 Second, if services such as special access were indeed highly competitive
220 as Qwest suggests, then it would not be enjoying tremendous profitability or
221 seeking to increase rates at the FCC in the first place. In other words, if special
222 access services were really competitive, such services would not be the source of
223 implicit subsidies. Qwest cannot have it both ways. It cannot support a claim that
224 other carriers in Arizona offer services that are competitive to Qwest, while
225 simultaneously extracting from those carriers revenues which are clearly a source
226 of implicit subsidies to Qwest for the very wholesale services on which
227 “competitors” rely to compete with Qwest.

228 **Q. DOES MR. TEITZEL EVEN DISPUTE YOUR TESTIMONY THAT**
229 **SPECIAL ACCESS CONTAINS IMPLICIT SUBSIDIES OR THAT**
230 **THOSE IMPLICIT SUBSIDIES SHOULD BE ELIMINATED?**

231 A. No he does not. Instead, Mr. Teitzel criticizes my testimony because it does not
232 identify “a means to offset those revenue reductions.” This suggestion is

⁴ See Rebuttal of McIntyre at 12.

233 ludicrous, particularly when viewed in the context of Qwest's petition. Qwest is
234 claiming in this proceeding that it is subject to competition in the State, and yet
235 expects the Commission to guarantee its revenue streams – through replacement
236 revenues -- from these services.

237 **Q. IF QWEST REDUCED ITS INTRASTATE PRIVATE LINE RATES,**
238 **WOULD YOU EXPECT TO SEE STIMULATION FOR THAT SERVICE?**

239 A. Yes. Qwest admitted in response to discovery that price "...is a key driver of
240 customer behavior, especially when both intrastate and interstate traffic is
241 involved."⁵ As noted in response to TWTA Request No. 02-011, "...for 2004,
242 over 98 percent of Arizona special access revenue was interstate and governed by
243 FCC interstate tariffs." Given Qwest's statements and a general understanding of
244 economics, one could assume that a reduction in intrastate special access/private
245 line rates would result in a shift from interstate to intrastate services. Further,
246 and more importantly, a reduction in intrastate special access rates might actually
247 result in more traffic remaining on the Qwest network and the elimination of
248 incorrect pricing and investment signals to alternative providers.

249 **Q. AT PAGES 56 AND 57 OF HIS REBUTTAL TESTIMONY, MR. TEITZEL**
250 **IS CRITICAL OF YOUR OPINION THAT THE VAST MAJORITY OF**
251 **QWEST'S OPERATING TERRITORY CLECS MUST RELY UPON**
252 **QWEST FOR SPECIAL ACCESS SERVICES. HOW DO YOU RESPOND**
253 **TO THIS TESTIMONY?**

⁵ See Qwest Response to TWTA Request No. 02-001.

254 A. As an initial matter, I think it is important to recognize that Mr. Teitzel, while
255 criticizing my testimony, fails to offer anything in the way of concrete evidence
256 disputing my statement. Moreover, Mr. Teitzel fails to dispute the main point of
257 my direct testimony, that being that in many cases, Qwest is the monopoly
258 supplier of special access services. In response to a data request from Qwest,
259 TWTA provided a sample listing of building locations in Phoenix to which
260 TWTA has been denied access or has been required to pay some sort of fee to
261 gain entrance.⁶

262 **Q. IS IT UNCOMMON FOR TWTA TO BE DENIED ACCESS OR BE**
263 **REQUIRED TO PAY FOR ACCESS TO BUILDINGS?**

264 A. No. The sample listing discussed above is quite typical for TWTA. For instance,
265 in Phoenix alone, where TWTA is able to gain access to a building, almost a third
266 of the time it must pay a fee. Those fees range from \$3,000 per year to more than
267 \$6,000 per year for each building. In response to TWTA 02-019, Qwest indicated
268 that it had identified no instances as yet where Qwest has been charged for access
269 to a “high rise” building housing business tenants. This disparate treatment of the
270 incumbent and alternative providers should be resolved before Qwest receives any
271 further deregulation.

272 **Q. ON PAGES 57 AND 58, OF HIS REBUTTAL TESTIMONY, MR.**
273 **TEITZEL ATTEMPTS TO PROVIDE ADDITIONAL SUPPORT FOR HIS**
274 **ARGUMENT THAT SPECIAL ACCESS SERVICE IS SUBJECT TO**

⁶ See TWTA Highly Confidential Attachment A to Qwest Request 4-3. It should be noted that this very circumstance was described by Mr. McIntyre at page 14 of his rebuttal. In that testimony, Mr. McIntyre acknowledges that under these circumstances, companies such as TWTA seek facilities from Qwest “as a last resort.”

275 **COMPETITION IN ARIZONA. PLEASE COMMENT ON THIS**
276 **TESTIMONY.**

277 A. Mr. Teitzel indicates on these pages of his testimony that Qwest's intrastate
278 special access is considered a Basket 3 service in Arizona, and that Qwest's
279 interstate special access service is under the jurisdiction of the FCC. While both
280 of these statements are undeniably true, Mr. Teitzel's statements actually assist
281 me in making my point with respect to the dangers of premature deregulation. As
282 discussed in my direct testimony, even though Qwest's special access services are
283 considered – from a regulatory perspective – to be competitive, the competitive
284 market has clearly not prevented Qwest from continuously and significantly
285 increasing prices, or prevented Qwest from exploiting its monopoly power in this
286 area. Obviously, classifying a service as competitive has not made the service
287 competitive, and has not protected consumers from price increases. In fact, the
288 classification has only made it possible for Qwest to price special access services
289 at such levels that it would insist on receiving AUSF support to replace the
290 monopoly-like profits associated with that service. Given Qwest's activities with
291 respect to the pricing of this critical service, and the potential impact on the
292 competitive retail market of this service, I recommend that the Commission
293 investigate the prices for intrastate special access, and revisit its previous finding
294 that special access/private line service is competitive in Arizona.

295 **Q. WHY DO YOU SAY THAT QWEST'S SPECIAL ACCESS PRICES**
296 **RESULT IN MONOPOLY-LIKE PROFITS?**

297 A. As noted in my direct testimony, based on the Qwest 2003 ARMIS Report 43-01,
298 filed April 1, 2004, Qwest was earning a rate of return on special access services
299 of 68% for all fourteen states in Qwest's operating territory. Qwest's rate of
300 return on an Arizona-specific basis was reported to be an incredible 74%.⁷ These
301 levels of returns are certainly not consistent with what could be expected in a
302 competitive market. Qwest has, regardless of the regulatory classification of
303 special access, been successful in extracting monopoly profits.

304 **Q. DOES MR. TEITZEL DISPUTE THAT TWTA HAS BEEN**
305 **DISADVANTAGED WITH RESPECT TO SERVING CUSTOMERS IN**
306 **HIGH RISE BUILDINGS IN ARIZONA?**

307 A. Yes. Although Qwest witness McIntyre does not dispute that TWTA was denied
308 access⁸, beginning on page 60 of his rebuttal testimony, Mr. Teitzel attempts to
309 disparage my testimony by suggesting that the example cited in my direct
310 testimony was an "unsworn, second-hand description" of the situation faced by
311 TWTA with respect to serving its customers via facilities-based competition.
312 Subsequent to my direct testimony's filing, TWTA responded to a data request
313 from Qwest in which TWTA provided several additional examples (in the
314 Phoenix area alone) of where it had been denied access to buildings or had been
315 required to pay substantial lease fees for space in buildings that would
316 accommodate TWTA's facilities.⁹ In addition, I have attached as Highly
317 Confidential Exhibit TJG 1, a list of additional examples in which TWTA has

⁷ Source: Qwest AZ ARMIS 43-01 2003 rows 1915/1910.

⁸ See McIntyre Rebuttal at page 14.

⁹ Qwest Data Request 4-3.

318 encountered barriers of this nature. Suffice it to say that this competitive
319 roadblock is real, and not isolated in nature. Although as Mr. Teitzel notes at
320 page 61 of his rebuttal testimony, Qwest's policies are not at issue with respect to
321 this problem, this situation works in Qwest's favor because, under existing
322 conditions, TWTA, and presumably other CLECs are prevented from competing
323 head to head with Qwest on a facilities basis. Rather, Qwest is in the enviable
324 position in which its competitors are required to pay Qwest in order to compete.
325 Further, as mentioned previously, if competitors buy special access from Qwest in
326 order to provide these services, Qwest realizes, on average 74% returns from such
327 a captive CLEC customer.

328 **Q. MR. TEITZEL, AT PAGE 61 GOES ON TO SUGGEST THAT SINCE IT**
329 **IS BOUND BY THE SECTION 271 CHECKLIST REQUIREMENTS, THE**
330 **COMMISSION NEED NOT CONSIDER THE SITUATION WITH**
331 **RESPECT TO CLEC ACCESS TO BUILDINGS IN THE CONTEXT OF**
332 **THIS PROCEEDING. DO YOU AGREE?**

333 A. No. Regardless of whether Qwest's actions directly result in CLECs being denied
334 access to the marketplace, if such a situation exists, then it represents a roadblock
335 to competition, and a threat to the public interest. Qwest is requesting additional
336 regulatory flexibility in this proceeding based on the premise that competition is
337 "thriving" in Arizona.¹⁰ The examples provided by TWTA with respect to
338 building access denial clearly indicate that competition is far from thriving, but
339 that it is literally being shut out. To suggest that the Commission ignore these

¹⁰ Direct Testimony of David Teitzel, Executive Summary page i.

340 facts is to suggest that the Commission disregard the public interest. Even if the
341 Commission has no authority to fix a problem, it can still consider the problem in
342 exercising its authority over Qwest.

343 **Q. AT PAGE 62 OF HIS REBUTTAL TESTIMONY, MR. TIETZEL**
344 **DISCUSSES QWEST'S ABILITY TO MANIPULATE WHOLESALE AND**
345 **RETAIL PRICES IN ORDER TO DRIVE COMPETITORS FROM THE**
346 **MARKET. PLEASE COMMENT.**

347 A. In my direct testimony, I described a classic price squeeze, in which Qwest could
348 raise wholesale rates and/or lower retail rates until such a time that the wholesale
349 rates for inputs required by CLECs to compete were higher than the rates CLECs
350 must charge in the retail market to be competitive with Qwest. So long as Qwest
351 has the CLEC as its captive customer, it can, by manipulating either wholesale or
352 retail rates, control the strength and viability of its competitors. It is important to
353 note that even though such a price squeeze can be accomplished by manipulating
354 wholesale prices the manipulation of wholesale prices is not necessary. As I will
355 discuss below, Qwest could accomplish the same objectives by setting retail rates
356 at a TSLRIC price floor without increasing wholesale prices. Nevertheless, as
357 discussed previously, Qwest has already begun to manipulate wholesale prices in
358 that it has, since 1999 increased special access rates numerous times, and
359 continues to seek additional increases. Since special access is considered by some
360 CLECs to be a critical input, and necessary in order to provide retail service,
361 CLEC margins are already suffering as a result of Qwest's price squeeze.

362 By providing testimony at page 62 that “this proceeding has nothing to do
363 with pricing flexibility for Qwest’s wholesale services” I believe that Mr. Teitzel
364 is trying to distract the Commission from the real point of this proceeding, that
365 being whether Qwest if granted additional pricing flexibility would have ability to
366 exercise market power in order to act in an anti-competitive manner. Mr. Teitzel,
367 once again appears to be asking this Commission to disregard any and all market
368 factors that are not specifically at issue in this proceeding, and to consider the
369 marketplace in a world in which these factors do not exist. Unfortunately, it is
370 Mr. Teitzel’s mythological world that does not exist.

371 **Q. ALSO AT PAGE 62 OF HIS TESTIMONY, MR. TEITZEL TESTIFIES**
372 **THAT IF QWEST WAS TO INCREASE RATES TO SUPRA-NORMAL**
373 **LEVELS, THAT IT WOULD INVITE ADDITIONAL COMPETITIVE**
374 **PRESSURE, AND THEREFORE, RATES WOULD BE GOVERNED BY**
375 **THE FREE MARKET. DO YOU AGREE?**

376 A. In theory, Mr. Teitzel is correct. If Qwest did not have the ability to manipulate
377 the strength and viability of its competitors, rates would be governed by the free
378 market. However, as I have shown, such is not the case. Because if Qwest has
379 the regulatory freedom to squeeze its competitors, even retail prices that would
380 otherwise attract competitive response would not have that effect. Entering a
381 market in order to offer telecommunications services is very expensive. If a
382 policy exists that would allow Qwest to respond to competitive threats by
383 reducing retail rates to levels that do not recover costs, carriers would run a
384 significant risk of never recovering the investment associated with entering the

385 market. Because a policy would be in place that would allow Qwest to execute
386 such pricing strategies, it is unlikely that Qwest would ever have to respond to a
387 competitive threat.

388 **Q. AT PAGE 63 OF HIS REBUTTAL TESTIMONY, MR. TEITZEL**
389 **TESTIFIES TO THE EFFECT THAT QWEST WOULD NOT HAVE THE**
390 **ABILITY TO DRIVE COMPETITORS FROM THE MARKET BECAUSE**
391 **THE COMMISSION'S RULES MANDATE THAT QWEST MUST SET**
392 **RETAIL RATES AT LEVELS NO LESS THAN THE TSLRIC OF THE**
393 **SERVICE. HOW DO YOU RESPOND?**

394 A. As I discussed in my direct testimony, Qwest admits that this is not true. Qwest
395 witness Teresa K. Million states in her direct testimony that TSLRIC costs “do not
396 by themselves define the appropriate price level”, and further, that carriers must
397 recover costs in addition to TSLRIC in order to “remain a healthy, viable and
398 growing corporation that can continue to invest in new products and services.” She
399 goes on to say that if firms do not recover such costs, “the products are not likely to
400 be offered by the firm.”¹¹ As I discussed in my direct testimony, a TSLRIC price
401 floor is too low to prevent anti-competitive behavior, since it would be impossible
402 for a competing carrier to be viable if it was forced to compete if Qwest offers rates
403 at or below TSLRIC. The Commission, therefore, should take no comfort in Mr.
404 Teitzel’s testimony in that regard.

405 **Q. AT PAGE 64 OF HIS TESTIMONY, MR. TEITZEL TESTIFIES THAT THE**
406 **COMMISSION HAS CONSIDERED THE ISSUE OF PRICE FLOORS**

¹¹ Direct testimony of Teresa K. Million, pages 9 and 10.

407 EXTENSIVELY, AND THAT A CHANGE IN THE COMMISSION'S
408 DECISION SHOULD BE ENTERTAINED IN A SEPARATE
409 RULEMAKING DOCKET.

410 A. I do not disagree with Mr. Teitzel's recommendation that the price floor issue be
411 addressed in a separate docket. I do, however, disagree with Mr. Teitzel's
412 characterization of the issue as having been resolved by the Commission. It is my
413 understanding that the Commission ordered Staff to open a docket to investigate and
414 rectify possible ambiguities involving the pricing of telecommunications services
415 and imputation in particular.¹² In fact, the Commission specifically ordered the
416 following:

417 IT IS FURTHER ORDERED that Commission Staff shall open a
418 docket to investigate and rectify any ambiguities associated with the
419 pricing of competitive telecommunications services, specifically, but
420 not limited to, R14-2-1310(C).¹³
421

422 The rulemaking docket suggested by Mr. Teitzel establishing price floors that would
423 be sufficient to avoid the issues identified by Qwest witness Million (i.e., at some
424 level higher than TSLRIC) should be complete before additional pricing flexibility is
425 granted to Qwest.

426 **Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?**

427 A. Yes
428
429

¹² See Opinion and Order in Docket No. T-01051B-00-369; Decision No. 63487, dated March 30, 2001, at paragraph 12.

¹³ Id. at page 26.

**HIGHLY CONFIDENTIAL REBUTTAL
EXHIBIT TJG_1**

REDACTED