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KRISTIN K. MAYES

IN THE MATTER OF THE APPLICATION OF QWEST COMMUNICATION CORPORATION D/B/A QWEST LONG DISTANCE FOR EXTENSION OF ITS EXISTING CERTIFICATE OF CONVENIENCE AND NECESSITY TO INCLUDE AUTHORITY TO PROVIDE RESOLD AND FACILITIES-BASED LOCAL EXCHANGE AND RESOLD LONG DISTANCE SERVICES, AND PETITION FOR COMPETITIVE CLASSIFICATION OF PROPOSED SERVICES, AND PETITION FOR COMPETITIVE CLASSIFICATION OF PROPOSED SERVICES WITHIN THE STATE OF ARIZONA.

DOCKET NO. T-02811B-04-0313

STAFF'S NOTICE OF FILING SUPPLEMENTAL TESTIMONY OF ELIJAH ABINAH

Staff of the Arizona Corporation Commission hereby files the Supplemental Testimony of Elijah Abinah, Assistant Director of the Utilities Division, in the above-referenced matter.

RESPECTFULLY SUBMITTED this 5th day of August, 2005.

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BEFORE THE ARIZONA CORPORATION COMMISSION

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

IN THE MATTER OF THE APPLICATION OF QWEST COMMUNICATIONS CORPORATION D/B/A QWEST LONG DISTANCE FOR EXTENSION OF ITS EXISTING CERTIFICATE OF CONVENIENCE AND NECESSITY TO INCLUDEAUTHORITY TO PROVIDE RESOLD ANDFACILITIES-BASED LOCAL EXCHANGE ANDRESOLD LONG DISTANCE SERVICES IN ADDITION TO ITS CURRENT AUTHORITY TO PROVIDE FACILITIES-BASED LONG DISTANCE SERVICES, AND PETITION FOR COMPETITIVECLASSIFICATION OF PROPOSED SERVICESWITHIN THE STATE OF ARIZONA	**DOCKET NO. T-02811B-04-0313**

SUPPLEMENTAL TESTIMONY OF

ELIJAH O. ABINAH

FOR THE

UTILITIES DIVISION

ARIZONA CORPORATION COMMISSION

AUGUST 5, 2005

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At the June 16, 2005, Procedural Conference, the Administrative Law Judge ("ALJ") asked Staff and QCC to address the following issues:

(1) What is the purpose of the Affiliated Interest Rules? If Staff's recommendations in its supplemental filing are adopted, why is it unnecessary for the Commission to reevaluate the limited waiver approved for QC and its affiliates since QC's affiliate would be competing head-to-head with QC's regulated business in the future? What are the risks and benefits of keeping the waiver in place? In the event that all of Staff's recommendation are not adopted, what changes to the waiver would Staff recommend and what procedures would Staff propose for effecting any recommended changes?

(2) Why should QCC be allowed to take customers and their associated revenues away from Qwest, the regulated entity?

(3) If QCC is allowed to compete with QC in the local market for enterprise customers, how should QC and QCC revenues be treated from a ratemaking perspective? What will the effect be on QC's future rates and revenues?

(4) Explain how the Commission can insure that maintenance and expansion of Qwest's infrastructure will not suffer as a result of allowing QCC to take customers and their revenues away from Qwest.

(5) Why are Staff's alternative recommendations in the public interest?

The Affiliated Interest Rules were designed to ensure that reorganizations affecting public utilities and transactions between public utilities and their affiliates would not adversely impact the Arizona utility and ratepayers. In addition to the public interest standard, the Affiliated Interest Rules identify the following factors to be considered: (a) whether the transaction will impair the financial status of the public utility, (b) whether the transaction will prevent the utility from attracting capital on fair and reasonable terms, and (c) whether the transaction will impair the ability of the public utility to provide safe, reasonable and adequate service.

If Staff's initial recommendation is adopted, Staff believes that the limited waiver granted to Qwest Corporation ("QC") and its affiliates, in Decisions 58087 and 64654 should be left intact. If Staff's alternative recommendation is adopted, along with all of the conditions Staff proposes, Staff also believes that sufficient information and reporting will be in place, such that Staff could support a continuation of the limited waiver. If Staff's alternative recommendation is adopted, but not all of the informational and reporting conditions are adopted, Staff believes that the waiver should be narrowed or eliminated.

All of the issues posed by the ALJ raise concerns that Staff has considered as well. However, Staff does not know at this time what the impact of QCC will be on QC's operations. As a result, Staff has proposed an approach in its alternative recommendation which would allow QCC to compete with QC on a more limited basis initially, in the Enterprise market, and impose informational and reporting requirements intended to provide sufficient information to assess the impacts upon QC.

QCC is likely to take away both customers and revenues from QC. This raises concerns with regard to QC's future rates and with the ability of QC to maintain and update its network in the future. To initially address these concerns, if the Commission adopts Staff's alternative recommendation, the Commission should also adopt Staff's informational and reporting requirements which would allow the Commission to assess the actual impact of this loss on the revenues of QC. It is Staff's position that any loss of customers and revenues should be considered and accounted in QCC's next rate review proceeding. With respect to network upgrades and maintenance, while the Service Quality Tariff and aggressive competition in the Enterprise market offer some protection, they are not a "guarantee" that the erosion of QC's customer and revenue base due to QCC will not have an adverse impact upon QC' network. Network maintenance issues should be closely monitored by the Commission if QCC's amended application is granted.

Staff's alternative recommendation is in the public interest only if all of Staff's informational and reporting requirements are adopted and the Commission is satisfied that QCC and QC have presented sufficient assurance that QC's ratepayers will not be harmed by the loss of Enterprise customers and revenues that is likely to occur.

[13] See In the Matter of the Notice of Proposed Adoption of Rules to Provide For Regulation of Public Utility companies with Unregulated Affiliates, Docket No. R-0000-89-194.

INTRODUCTION

Q. Please state your name and business address.

A. My name is Elijah O. Abinah. My business address is 1200 West Washington Street, Phoenix Arizona, 85007.

Q. Where are you employed and in what capacity?

A. I am employed by the Utilities Division ("Staff") of the Arizona Corporation Commission ("ACC" or "Commission") as the Assistant Director.

Q. How long have you been employed with the Utilities Division?

A. I have been employed with the Utilities Division since January 2003.

Q. Please describe your educational background and experience.

A. I received a Bachelor of Science degree in Accounting from the University of Central Oklahoma in Edmond, Oklahoma. I also received a Master of Management degree from Southern Nazarene University in Bethany, Oklahoma. Prior to my employment with the ACC, I was employed by the Oklahoma Corporation Commission for approximately eight and a half years in various capacities in the Telecommunications Division.

Q. What are your current Responsibilities?

A. As the Assistant Director, I review submissions that are filed with the Commission and make policy recommendations to the Director regarding those filings.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to provide responses to the issues raised by the Administrative Law Judge in the July 11, 2005 Procedural Order in the matter.

STAFF RECOMMENDATIONS CONCERNING THE AFFILIATED INTEREST RULES WAIVER

Q. What is the Purpose of the Affiliated Interest Rules?

A. The Commission adopted the Affiliated Interest Rules in Decision No. 56844 on March 14, 1990.[3] The stated purpose of the Rules is to "to regulate the formation of public utility holding companies and certain transactions between a public service corporation and affiliated interests."[4] Attachment B to Decision No. 56844 contains a separate concise explanatory statement or reasons for adoption of the Rules. It states in part:

> "Article 8 is designed to insure that utility ratepayers are insulated from the dangers proven to be inherent in holding company structure and diversification. Its singular purpose is to ensure that ratepayers do not pay rates for utility service that include costs associated with holding company structure, financially beleaguered affiliates, or sweetheart deals with affiliates intended to extract capital from the utility to subsidize non-utility operations. The rules provide procedures by which holding companies may be formed, identify affiliated activities which require Commission approval, provide for review of transactions between a public utility and its affiliated interests, and prescribe reporting requirements for the affected utilities.
>
> The rules implement the following general principles. First, utility funds must not be commingled with non-utility funds. Second, cross-subsidization of non-utility activities by utility ratepayers must be prohibited. Third, the financial credit of the utility must not be affected by non-utility activities. Fourth, the utility and it s affiliates must provide the Commission with the information necessary to carry-out regulatory responsibilities."[5]

The Rules contain three primary sections. R14-2-803 governs the organization or reorganization of Public Utility Holding Companies. It requires any utility or affiliate intending to organize a public utility holding company to notify the Commission and provide certain information to the Commission regarding the reorganization. The Commission may reject the proposal if it determines that it would impair the financial status of the public utility, otherwise prevent it from attracting capital at fair and reasonable

[4] Decision No. 56844, Finding of Fact 2.
[5] Decision No. 56844, Attachment B, pps. 2-3.

terms, or impair the ability of the public utility to provide safe, reasonable and adequate service.

R14-2-804 governs Commission review of transactions between public utilities and affiliates. It requires open access to the affiliates' books and records to the extent necessary to fully audit, examine or otherwise investigate transactions between the public utility and the affiliate. It also requires Commission approval of certain transactions between the utility and any affiliate.

Finally, R14-2-805 requires that on or before April 15 of each calendar year, all public utilities meeting the requirements of R14-2-802 and public utility holding companies to file a description of their diversification plans for the current year that have been approved by the Boards of Directors.

Q If Staff's recommendations in its Supplemental Staff Report are adopted, why is it unnecessary for the Commission to look at the current waiver from the Affiliated Interest Rules held by Qwest Communications Corporation's ("QCC's") parent Qwest Corporation ("Qwest" or "QC"), given that Qwest's competitive affiliate would be allowed to compete head-to-head for Qwest's regulated business?

A. QC was granted a limited waiver to R14-2-803 in Decision No. 58087 on November 23, 1992. The waiver was reaffirmed and extended to all QC's affiliates in Decision No. 64654 on March 25, 2002. The limited waiver to R14-2-803 requires QC, its affiliates, QCC, or its parent Qwest Communications International, Inc. to file a notice of intent to organize or re-organize a public utility holding company only for those re-organizations or organizations that are likely to result in increased capital costs to QC, result in additional costs allocated to Arizona jurisdiction, or result in a reduction of QC's net operating income.

Neither Decision 58087 nor Decision 64654 granted QC or its affiliates a waiver of A.A.C. R14-2-804, which allows for Commission oversight of any future financial transactions between QC and any prospective affiliated competitive provider. In addition, no waiver was granted to QC or its affiliates of A.A.C. R14-2-805, which requires the utility and holding company to file information on their diversification plans.

If Staff's initial recommendation is adopted, there of course would be no need for reevaluation of the limited waiver, since Staff's initial recommendation was to deny QCC's request for an expanded CC&N within QC's service territory. If Staff's alternative recommendation (including all of the conditions contained therein) is adopted, Staff believes that enough safeguards and information would be available to Staff, such that Staff could continue to support the limited waiver of A.A.C. R14-2-803. There are no known risks, of which Staff is aware, associated with keeping the waiver in place under these conditions.

If the Staff's alternative recommendation is adopted, but all of the conditions contained therein are not adopted, Staff would have a concern that it would not have sufficient information available to it in order to determine the actual impact of QCC upon QC and how ratepayers are being affected. While it does not appear that QCC's request to compete head on with QC is a "reorganization" under R14-2-803 as that term is used under the rules, certainly QCC's application raises many of the same concerns identified by all sections of the rules, including R14-2-803, i.e., whether QCC's ability to take away customers from QC will "impair the financial status of the public utility, otherwise prevent it from attracting capital at fair and reasonable terms, or impair the ability of the public utility to provide safe, reasonable and adequate service."

Q. In the event that all of Staff's recommendations are not adopted, what changes to the waiver would Staff recommend and what procedures would Staff propose for effecting any recommended changes?

A. If Staff's alternative recommendation is adopted, but not all of Staff's conditions are accepted, Staff would be concerned that continuation of the limited waiver would not be in the public interest. If Staff is unable to obtain the information contained in several of its conditions which would allow it to better determine the impact of this transaction on QC, Staff would recommend reevaluation of QC and its affiliates' current limited waiver. Staff would recommend that the exemption be significantly narrowed in that event so that any reorganization that was likely to have any impact upon the Arizona operations of Qwest be subject of review in the future, or that the waiver be eliminated entirely.

QCC CUSTOMERS AND ASSOCIATED REVENUES

Q. Why should QCC be allowed to take customers and their associated revenues away from QC?

A. Staff recognizes that while QCC has no stated intentions to "migrate" customers and revenues from QC, such migration could occur, nonetheless. If QCC's primary objective or intent to operate as a competitive LEC in QC's service territory in the large and medium size business market was to "migrate" customers away from QC, Staff would recommend rejection of QCC's application.

QCC has stated in its responses to Staff data requests, that its purpose in requesting an expansion of its certificate is to provide "one-stop" shopping to the Enterprise market. It stated that many requests for proposals require that a responding entity be able to provide services through a single contract and a unified bill and customers relationship, and not deliver the requested services through different entities, billing mechanisms, or affiliates. QC recently reiterated in response to STF 6-003, that "[b]ecause of Section 272 limitations applicable only to Bell Operating Companies (QC), unless the CC&N requested by QCC in this docket is granted, no Qwest company is legally allowed to provide the 'one stop' total solutions enterprise customers increasingly require." While Staff, through its alternative recommendation, has attempted to accommodate the Company in this regard, both QCC and QC are opposed to some of the recommended conditions proposed by Staff which require them to provide information that Staff needs to track the impact QCC will have on QC's operations.

Staff is not certain at this time what the exact impact will be upon QC, but it is concerned that this loss of customers and revenues may have an adverse impact upon QC. However, Staff believes that at a minimum if QCC's amended application is granted, it is important that QC's customers not be held responsible for any adverse impact caused by any loss of customers and their associated revenues from QC to QCC in QC's next rate review. It is for this reason, that Staff, as part of its alternative recommendation, has requested that certain information and reporting requirements be imposed upon QC and QCC so that the impact can be understood and quantified. It is also important that this information be available for examination and consideration in QC's next rate review. While QCC argues that the appropriate venue to examine this information is in QC's next rate case (See QCC Response to STF 06-005), QCC does not explain how the Commission is to obtain the information if QC and QCC are not ordered to provide it in this case, since the information that Staff will need will not have been tracked by either entity.

QCC argues that the Staff is treating it differently and discriminating against them because the Staff is requesting this information of QC and QCC only, and not any other ILEC or CLEC. There is no prior Commission Order authorizing a CLEC affiliated with the ILEC to operate within the ILEC's service territory. Thus, there has been no need to request this information from another ILEC or CLEC.

QCC further argues that QC should not have to provide this information as a result of a Docket in which it is not involved. However, the impact of QCC's request upon QC's business is a big issue in this Docket, therefore, it should not be surprising that some of the information that Staff would need in the future would pertain to QC. Further, I am aware of no restriction, given the nature of this Docket, upon the Commission ordering QC to provide information which to relates to the issues raised, especially when it is the only Qwest entity that has access to the information needed.

In response to STF 06-003, Qwest also relies upon the FCC's Section 272 Non-Accounting Safeguards Order to support QCC's ability to compete with QC in the local exchange business market. However, the FCC was looking at the issue from a policy perspective with respect to the impact of a Section 272 affiliate offering local service in the affiliated RBOC's service territory on competition in the local market and whether competition would be harmed. Because of the impact upon local ratepayers, this Commission must look at additional factors including the impact upon the financial viability of QC, in determining whether QCC's amended application is in the public interest.

In summary, Staff is not certain at this time what impact that QCC will have on QC's operations. It is for this reason that Staff has put forth a position in its Supplemental Staff Report that recommends that the Commission proceed slowly by allowing QCC to compete only in the Enterprise market to begin with. While the "migration" issue is a concern, it is less of a concern in Staff's opinion if QCC is limited to providing competitive local exchange service to Enterprise customers initially.

QWEST REVENUES AND FUTURE RATES

Q. What is the difference in the way Qwest and QCC revenues would be treated from a ratemaking perspective, and what will the effect of the difference be on Qwest's revenues and future rates?

A. Staff's position is that any QC customers and associated revenues lost to QCC should be accounted for and considered in QC's next rate review proceeding. Similarly, it is Staff's position that with respect to any analysis of "competition" in the future, the affiliated ILEC and CLEC should be treated as one company. This approach has been used by at least one other state in Qwest's region when determining the effective level of competition in the ILEC's service territory. [6]

[6] e.g., Nebraska C-3335, C-1839

Qwest argues that the Commission should not bother with this issue at this time, but rather should wait to address it during QC's next rate review proceeding.[7] As already discussed, however, it is necessary that the Commission order the Companies to begin providing the information now, so that it will be available for the next rate review proceeding. Otherwise, the Companies will simply not track the information and the information will not be available when needed.

QCC also argues that there is no need for the Commission to look at this issue since even if a QC customer is lost to QCC, QC will be compensated by QCC for use of its network either on a resale basis or unbundled network element basis. However, this still does not address the overall impact upon QC and the concern that even if wholesale revenues were taken into account, QC and its customers may still be worse off.

It is for these reasons, that Staff is taking a more cautious approach to begin with and recommending that at most, the Commission approve QCC's amended application to provide competitive local service within QC's service territory to large business customers only. If Staff's proposed conditions are adopted, the Commission will have the information necessary to account for any impact in QC's next rate review proceeding.

MAINTENANCE AND EXPANSION OF QWEST'S INFRASTRUCTURE

Q. How can the Commission insure that maintenance and expansion of Qwest's infrastructure will not suffer as a result of allowing QCC to take customers and their revenues away from Qwest?

[7] See Qwest Response to STF 06-005.

A. Staff agrees that in any public interest analysis, consideration of QCC's application upon maintenance and expansion of QC's infrastructure is an appropriate consideration. Neither Staff or the Company can provide any "guarantee" that maintenance and expansion of QC's infrastructure will not suffer if business customers were simply to be migrated to QCC. Certainly, if QC loses many of its business customers to QC and other competitors, a serious concern arises with respect to how QC will be able to maintain and update its network.

In response to STF 06-006, QC states that it has strong incentives to maintain its network in Arizona now. QC states that its Service Quality Tariff provides strong incentive to the Company to provide adequate levels of service. QC also relies upon the presence of aggressive competitors in the Arizona market which it states will require the Company to maintain a high quality of service it it is to compete successfully.

Staff is not convinced that these two factors alone provide the degree of assurance the Commission may want in this regard. Indeed, if QC loses many of its largest customers to other providers, it may not have either the incentive or ability to maintain or update its network.

However, again, because Staff does not have the answers to these questions at this time, Staff has chosen through its alternative recommendation, to encourage the Commission to proceed in a cautious manner at this time, by approving QCC's amended application with conditions. Staff is hopeful, that if the conditions it has proposed are adopted, that Staff and the Commission will have the information necessary to evaluate questions such as this in the future. The Commission will also have an array of information available to it to determine whether further expansion of the Company's certificate would be in the public interest.

Information that facilitates future Commission decisions must answer key questions such as: WHO are the providers, WHAT are they providing, WHERE are services provided, WHEN are services provided, WHY are services provided and HOW are services provided? The reports and information that Staff has recommended as conditions for QCC's limited CLEC authority should provide many of the answers or serve as key indicators for Staff to pursue additional information.

STAFF'S ALTERNATIVE RECOMMEDATIONS

Q. Why are Staffs alternative recommendations in the Supplemental Staff Report in the public interest?

A. Staff does not believe that QCC's application will have an adverse impact upon competition in the Enterprise market. On page 3 of its Supplemental Staff Report, Staff stated the following regarding the impact of QCC's application on competition in the Enterprise Market:

"While Staff does not take the position that the market is sufficiently competitive to warrant competitive relief for QC in the context of its current Price Cap application, the presence of an affiliated CLEC should not be injurious to the overall competitive situation given the known presence of strong business brands, such as MCI and AT&T. The Enterprise Market may, in fact, welcome another competitor since QC's presence in the Enterprise Market has substantially diminished. Staff also notes that no CLEC has filed objections to QCC's application. QCC has explained that it seeks to serve customers desirous of interlata solutions that cannot be offered by QC. Additional competitive alternatives for the Enterprise market appear to have more upside than downside."

Staff continues to support the position stated in its Supplemental Staff Report with respect to the impact on competition in the local Enterprise market and adds to it as follows:

The high growth that Arizona has experienced in the last decade and continues to experience has been characterized as largely in the residence and small business markets. This growth, nonetheless, is likely to stimulate large company divisions and even company headquarters to locate in Arizona. These large company divisions and company headquarters are at the core of the Enterprise Market. The mergers of SBC/AT&T and Verizon/MCI, if they are consummated, should result in increased competition from two robust providers in the Enterprise Market. Staff believes that the Enterprise Market can benefit from the addition of another well established brand. Adding a third robust brand to the Enterprise Market has the potential to improve communication services and minimize corresponding price increases adding to the economic reasons for large company divisions and headquarter companies to seek Arizona as an operating base.

Staff further notes that the companies resulting from the above noted mergers, if they do occur, will have at least as much financial and marketing strength as Qwest in the Enterprise Market. SBC/AT&T and Verizon/MCI do not need the Commission's protection from Qwest. In the Enterprise Market, quite the opposite may be true. As such, any Qwest CLEC operation should have minimal chances of harming customers in the Enterprise Market. Staff believes that Qwest's CLEC authority will help ensure that the Enterprise Market does not gradually move in the direction of the potential duopoly that may be arising with Qwest and Cox in the Small Business and Residence markets. This belief, of course, is conditional on the ability of Staff to ensure the QCC does not receive unfair support from its QC affiliate nor that QCC does not deter QC from its Small Business and Residence focus. Such assurance can be supported through the use of the reports and information requested by Staff.

Overall, given the competitive nature of the Enterprise market in the larger metropolitan areas in Arizona, Staff believes that QCC's entry into that market should not have an adverse impact on competition and that with the conditions contained in Staff's Supplemental Report, the Commission and Staff should be able to gather enough data to determine its impact upon QCC and Arizona ratepayers. Staff should also be able to gather enough data to determine whether an expansion of QCC's CC&N, if and when QCC files an application for same, is in the public interest.

Without all of the information requested by Staff in its conditions, Staff cannot state that QCC's amended application is in the public interest, because there will be no way of tracking its impact on QC, now or in the future.

STAFF'S RESPONSE TO QCC'S JUNE 10, 2005 NOTICE OF FILING SUPPLEMENTAL AUTHORITY

Q. What is Staffs response to QCC's June 10, 2005 Notice of Filing Supplemental Authority and Post Hearing Submissions?

A. QCC's June 10, 2005 filing concerns rules adopted by the Nebraska Commission to require ILECs whose affiliated CLECs serve the same service territory as served by the ILEC to (1) file all commercial agreements between the ILEC and the affiliated CLEC with the

Commission, (2) file annually the number of resold lines provided by the ILEC to the affiliated CLEC, and (3) refrain from any discriminatory practices in favor of the affiliated ILEC. QCC's filing also contained the orders of other state commission's in QC's region which have already ruled on this issue.

Staff notes that the Nebraska ("NE") order conflicts with the position taken by QCC in this matter. QCC has argued that an ACC decision granting QCC's authority to provide CLEC services in Arizona should not place obligations on QC because QC is "not a party to the 04-0313 application." The Nebraska order clearly places reporting obligations on the part of QC even though the CLEC authority was granted to QCC in an application to which QC was not a party. Staff further notes that the rules imposed by the Nebraska order are not dissimilar from those requested by Staff in Arizona. Staff believes that the Commission has full authority in this matter and can place any reporting requirements deemed necessary and appropriate on QC.

Q. Does this conclude your testimony?

A. Yes, it does.