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DEPARTMENT OF THE ARMY
UNITED STATES ARMY LEGAL SERVICES AGENCY
901 NORTH STUART STREET
ARLINGTON VA 22203-1837



November 30, 2005

REPLY TO
ATTENTION OF
Regulatory Law Office
U 4102

Subject: In The Matter Of Qwest Corporation's Filing Of Renewed Price Regulation Plan.
Arizona Corporation Commission, Docket No. T-01051B-03-0454 and In The Matter Of The
Investigation Of The Cost Of Telecommunications Access. Arizona Corporation Commission,
Docket No. T-00000D00-672.

Arizona Corporation Commission
Docket Control
1200 West Washington Street
Phoenix, Arizona 85007

Enclosed for filing with the Arizona Corporation Commission are the original and fifteen copies of the Brief of the Department of Defense and All Other Federal Executive Agencies (DOD/FEA) in the subject proceedings. This Brief is dated December 2, 2005.

Copies of this Brief has been served in accordance with the attached Certificate of Service. Inquiries concerning this matter may be directed to the undersigned at (703) 696-1644.

Sincerely,

Peter Q. Nyce Jr.
General Attorney
Regulatory Law Office

Enclosure

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

BRIEF

of

THE UNITED STATES DEPARTMENT OF DEFENSE

And

ALL OTHER FEDERAL EXECUTIVE AGENCIES

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December 2, 2005

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THE UNITED STATES DEPARTMENT OF DEFENSE
And
ALL OTHER FEDERAL EXECUTIVE AGENCIES

The United States Department of Defense and All Other Federal Executive Agencies
("DOD/FEA") hereby submits this Brief in the above-captioned proceeding.

I. INTRODUCTION

DOD/FEA purchases large quantities of telecommunications service in Arizona. Indeed, the 60,000 civilian and military employees of DOD/FEA in Arizona probably make DOD/FEA the largest user of telecommunications service in the state

Federal legislation, as well as good procurement policy, requires that Government agencies procure supplies and services at the lowest prices in a manner that fosters the introduction of new technologies. For this reason, DOD/FEA strongly supports the Commission's effort to bring the benefits of competitive markets to consumers of all telecommunications services.

Since Qwest Corporation ("Qwest") is the largest incumbent local exchange carrier ("ILEC") in Arizona, its regulation and prices are of particular interest to DOD/FEA. DOD/FEA participated actively in Docket No. T-01051B-99-105, which led to the adoption of the price cap plan now in effect. DOD/FEA supported the current plan in its December 2000 Brief,¹ and the Commission approved the plan in Decision 63487 on March 30, 2001.

II. BACKGROUND

On November 18, 2004, DOD/FEA submitted the Direct Testimony of Richard B. Lee in this proceeding. Mr. Lee recommended several changes to the price cap plan proposed by Qwest in its May 20, 2004, filing. Mr. Lee acknowledged that Qwest faces increased competition in Arizona.² He explained that Qwest should be granted increased pricing flexibility to contend with this increased competition.³ However, he proposed certain limits to Qwest's pricing

¹ See, Brief of DOD/FEA, December 18, 2000.

² Lee Direct, at 4-5 (Exhibit DOD/FEA-1).

³ Id., at 6.

flexibility to the extent that competition is not yet fully effective in constraining Qwest's prices.⁴ On January 12, 2005, DOD/FEA submitted Mr. Lee's Surrebuttal Testimony which further supported his position.

Settlement negotiations began on February 10, 2005. The Residential Utility Consumer Office ("RUCO") withdrew from these negotiations in April, but on August 23, 2005, a Settlement Agreement was signed and filed by DOD/FEA, Qwest, the Arizona Corporation Commission Utilities Division ("Staff"), the regulated subsidiaries of MCI, Inc. ("MCI"), Time Warner Telecom of Arizona, LLC ("Time Warner"), the Arizona Utility Investors Association ("AUIA"), Cox Arizona Telecom ("Cox"), and XO Communications Services, Inc. ("XO") (collectively "the Parties").

The Parties filed testimony in support of the Settlement Agreement on September 6, 2005. DOD/FEA submitted Mr. Lee's Testimony in Support of Settlement at that time.

On October 14, 2005, RUCO and the Arizona Consumers Council ("ACC") filed in opposition to the Settlement Agreement.

On October 28, 2005, the Parties filed rebuttal testimony. DOD/FEA submitted Mr. Lee's Rebuttal Testimony in Support of Settlement at that time.

Hearings in this proceeding were held from November 1 to November 3, 2005.

III. THE COMMISSION SHOULD APPROVE THE SETTLEMENT AGREEMENT

The Settlement Agreement has two principal components. First, the Parties resolve the many contested revenue requirement issues in this proceeding by agreeing that Qwest's

⁴ Id., at 7-10.

jurisdictional revenue deficiency is \$31.8 million.⁵ This revenue deficiency is only about 10 percent of the revenue deficiency originally proposed by Qwest.⁶ Indeed, the deficiency is about \$130 million less than RUCO originally proposed.⁷ Second, the Parties have agreed to a three-year Renewed Price Cap Plan during which none of them will initiate a general rate case.⁸

The Renewed Price Cap Plan establishes four baskets of service.⁹ Each basket is subject to specific pricing rules.

Basket 1 will consist of Retail Services whose prices may not be increased while the Renewed Price Cap Plan is in effect.

Basket 2 will consist of Limited Pricing Flexibility Retail Services. Overall revenue changes to this basket caused by price changes will not exceed \$1.8 million in the first year of the Renewed Price Cap Plan and \$13.8 million in total for the term of the Renewed Price Cap Plan. Increases in individual service prices will not exceed 25 percent within any 12 month period.

Basket 3 will consist of Flexibly-Priced Competitive Services. Overall revenue changes to this basket caused by price changes will not exceed \$31.8 million less Basket 2 price increases in the first year of the Renewed Price Cap Plan, and \$43.8 million less Basket 2 price increases for the term of the Renewed Price Cap Plan.

Basket 4 will consist of Wholesale Services. Switched Access Charge Prices will be

⁵ Settlement Agreement, at Section 2 (Exhibit S-1).

⁶ Qwest Schedule A-1, Rule 103 filing – 6/21/04 update (\$318.5 million) (Exhibit Q-1).

⁷ Direct Testimony of Marylee Diaz Cortez November 18, 2004, at 2 (\$160 million) (Exhibit RUCO-6).

⁸ Settlement Agreement, at Sections 17 and 29 (Exhibit S-1).

⁹ *Id.*, at Sections 10-12.

permanently reduced by \$12.0 million at the start of the first year of the Renewed Price Cap Plan. Other wholesale service prices are capped at the tariffed or contract price levels for the term of the Renewed Price Cap Plan, or until contracts are re-negotiated, or until the Federal Communications Commissions (“FCC”), the Arizona Commission or courts determine that other prices are appropriate.

The Renewed Price Cap Plan described in the Settlement Agreement allows Qwest increased pricing flexibility consistent with the competition it faces. For example, the Renewed Price Cap Plan allows Qwest to introduce promotional offerings upon one day notice¹⁰ and establishes reasonable conditions on service packages.¹¹ The Renewed Price Cap Plan also provides meaningful price flexibility in Basket 2, but limits price increases for individual services to 25 percent in any 12 month period.¹²

Similarly, while the Settlement Agreement requires Qwest to reduce its switched access prices by \$12 million immediately,¹³ it also allows Qwest the opportunity to recover this reduction, and its \$31.8 million revenue deficiency, through Basket 2 and 3 price increases.¹⁴

The Settlement Agreement also includes several specific consumer benefits: a reduction in zone charges, a reduction in residence non-published and non-listed number rates, and an

¹⁰ Id., at Section 22.

¹¹ Id., at Section 23.

¹² Id., at Section 12.

¹³ Id., at Section 8.

¹⁴ Id., at Section 10.

increase in funding for the Telephone Assistance Plan for the Medically Needy.¹⁵

In summary, the Settlement Agreement is balanced, reasonable and in the public interest. It should be approved by the Commission.

IV. THE OPPOSITION ARGUMENTS OF RUCO AND ACC ARE WITHOUT MERIT

Both RUCO and ACC ask the Commission to reject the Settlement Agreement because they disagree with various details of the Renewed Price Cap Plan. As will be explained below, the specific criticisms of the Renewed Price Cap Plan by RUCO and ACC are without merit. More importantly, however, the rejection of this intensely negotiated Settlement Agreement would place a chill over the prospects for resolution of complex matters through good faith negotiation in the future. RUCO quit the negotiations after two months, and ACC never participated at all. Rejection of the Settlement Agreement would suggest that parties in future proceedings might profit by avoiding the “give and take” of negotiations. By opposing an agreement reached by others, the party might find itself able to “take” without “giving”. For this reason, the Commission should only consider the rejection of a fairly negotiated settlement when it clearly fails to serve the public interest.

RUCO believes the following issues are not satisfactorily resolved by the agreement:

- 1) The agreement, as a whole does not address the current status of competition in Arizona, nor will it do anything to further competition in Arizona’s telecom industry;
- 2) Inappropriate placement of certain services in certain baskets;
- 3) Lack of geographic distinction in classifying competitive services;

¹⁵ Id., at Section 13.

- 4) The degree to which pricing freedom is allowed in Basket 2;
- 5) The agreement results in a modified price cap plan that, when compared to the existing plan, negatively impacts residential ratepayer; and
- 6) The manner in which the issue of the April 1, 2005 productivity adjustment (required under the existing plan) is resolved by the settlement.¹⁶

Contrary to RUCO's first point, the Renewed Price Cap Plan clearly recognizes that local service competition has increased significantly in Arizona since the adoption of the original Price Cap Plan in 2001. The Renewed Price Cap Plan allows Qwest increased pricing flexibility consistent with the competition it now faces.

Qwest competitors now serve over 700,000 access lines in Arizona.¹⁷ Four of these competitors participated fully in the negotiations that will allow Qwest to compete on a more equitable basis in the future. Qwest will have at least some pricing flexibility for Limited Pricing Flexibility Retail Services (Basket 2) and Flexibly – Priced Competitive Services (Basket 3).¹⁸ The Renewed Price Cap Plan also allows Qwest to introduce promotional offerings upon one day

¹⁶ Testimony of Marylee Diaz Cortez, October 14, 2005, at 2 (Exhibit RUCO-8). ACC expresses similar concerns.

¹⁷ FCC, Local Telephone Competition: Status as of December 31, 2004, Table 10, shows competitive local exchange switched access lines as 792,272 in Arizona.

¹⁸ Settlement Agreement, Section 12 (Exhibit S-1).

notice¹⁹ and establishes reasonable conditions on service packages.²⁰

The increased pricing flexibility afforded to Qwest not only addresses the current state of competition, it also furthers competition. This increased flexibility will allow Qwest to become a more effective competitor, and this in turn will force its competitors to become more effective. Further competition is also promoted by the Settlement Agreement's special access, imputation and price floor provisions.²¹ The settlement negotiations have thus resulted in provisions which both recognize the current state of competition and further its development.

RUCO's contention that the Settlement Agreement negatively impacts residential ratepayers is also incorrect. First of all, residential and other ratepayers are relieved of responsibility for Qwest revenue deficiencies that could have reached well over \$100 million had the Settlement Agreement not been negotiated. Secondly, Qwest's withdrawal of its proposal for competitive zones allows the significant implicit subsidy of residential rates in less dense areas of Arizona to continue.²² Since Qwest's rates will be the same throughout the state, rural residential rates will benefit from the pressure put on Qwest's rates by competition in urban areas. This lack of "geographic distinction" referred to by RUCO thus serves rural residential ratepayers well.²³ Moreover, the hard-cap on primary residential lines and associated services

¹⁹ Id., at Section 22.

²⁰ Id., at Section 23.

²¹ Id., at Sections 9 and 20.

²² Id., at Section 26.

²³ RUCO witness Johnson is troubled that the Settlement Agreement does not result in changes to the Arizona Universal Service Fund ("AUSF"). Supplemental Testimony in Opposition to Qwest's Settlement Agreement of Ben Johnson, Ph.D., at 3 (Exhibit RUCO-14). Changes to the AUSF, however, must be addressed in the Commission's generic AUSF proceeding, RT-00000H-97-0137.

allows the implicit subsidy of residence lines by business lines to continue.²⁴

Residential ratepayers will certainly benefit from the significant enhancements made to the Service Quality Plan Tariff.²⁵ Consumers living in rural areas of the state will also find the establishment of service more affordable because of the increase in the Line Extension Credit.²⁶

Finally, of course, neither RUCO nor ACC acknowledge the additional consumer benefits specifically included in the Settlement Agreement to benefit residential ratepayers.²⁷ These provisions reduce zone charges, reduce residential non-published and non-listed telephone number rates, and increase funding for the Telephone Assistance Plan for the Medically Needy.

RUCO's criticisms of the placement of certain services in certain baskets, the degree of pricing freedom in Basket 2, and the manner in which the issue of the April 1 productivity adjustment is resolved are also without merit. These detailed matters were thoroughly examined and discussed during the settlement negotiations. Had RUCO not quit these negotiations, or ACC participated, there might well have been somewhat different resolutions to these issues. Ironically, it was RUCO, itself, which initiated the consideration of a third retail basket and thus the changes in basket placement.²⁸ The Commission should not attempt to modify the Parties' comprehensive Settlement Agreement to reward RUCO for its after-the-fact criticisms. Instead, the Commission should commend the Parties, and particularly the Staff, for a complex and difficult job well done.

²⁴ Lee Surrebuttal, at 3-4 (Exhibit DOD/FEA-2).

²⁵ Settlement Agreement, at Section 15 (Exhibit S-1).

²⁶ Id., at Section 13.

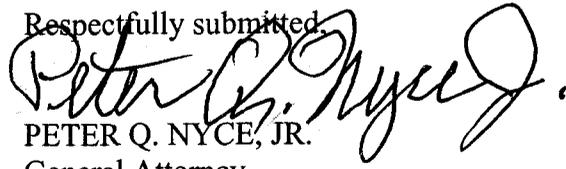
²⁷ Id., at Section 16.

²⁸ Supplemental Testimony in Opposition to Qwest's Settlement Agreement of Ben Johnson, Ph.D., at 10 (Exhibit RUCO-14).

V. CONCLUSION

WHEREFORE, the premises considered, the U.S. Department of Defense and All Other Federal Executive Agencies urge the Commission to approve the proposed Settlement Agreement filed August 23, 2005.

Respectfully submitted,



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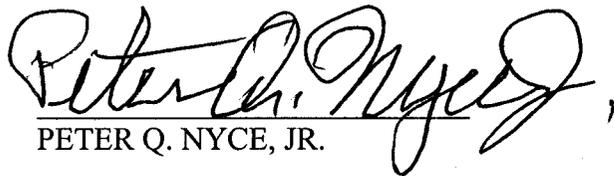
All Other Federal Executive Agencies

Dated this 2nd day of December 2005

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing Brief of the United States Department of Defense and All Other Federal Executive Agencies was sent to the parties on the attached service list either by United Parcel Service - Next Day Air, or by first class mail, postage prepaid on November 30, 2005.

Dated at Arlington County, Virginia, on this 30th Day of November 2005.


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