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BEFORE THE ARIZONA CORPORATION COMMISSION

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2005 DEC -2 P 1: 54  
AZ CORP 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

**AUIA'S POST-HEARING BRIEF**

Pursuant to the instructions of the Administrative Law Judge at the close of hearing, the ARIZONA UTILITY INVESTORS ASSOCIATION (AUIA) hereby submits its post-hearing brief in the above-captioned matter.

**INTRODUCTION**

AUIA and other parties to the proposed settlement agreement have documented fully in their pre-filed testimony the many benefits that flow to consumers from the price cap plan that forms the substance of the agreement. Every party to the settlement has asserted that it meets the Commission's public interest standard and urges the Commission to adopt it as the resolution to this case.

AUIA will not use this space to recount all of the returns recognized by the settling parties except to outline the broad public interest that is served by the settlement.

There is universal agreement that Qwest requires an infusion of new revenue to offset significant loss of market share and that it needs to have greater flexibility in product pricing and marketing in order to compete effectively. The proposed price cap plan addresses

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1 both of these needs prospectively and it does so without imposing a general rate  
2 increase on Qwest's customers.

3 The risk is all on Qwest to find the right balance between revenue needs and  
4 competitive pressures, but it is critical to consumers for Qwest to have the economic  
5 opportunity because, while Qwest is no longer a pure monopoly, it still provides  
6 the backbone of telecommunications service in Arizona and is the state's provider of  
7 last resort.

8 At hearing, the only party to offer testimony in opposition to the settlement  
9 agreement was the Residential Utility Consumers Office (RUCO). At bottom, RUCO  
10 produced two recommendations to the Commission:

11 1) To require Qwest to apply a \$12 million credit to customers' bills, amortized  
12 over one year, to indemnify the productivity adjustment incurred on April 1, 2005  
13 under the old price cap plan.

14 2) To reject the settlement agreement entirely and proceed to a litigated  
15 hearing.

16 While RUCO may view these recommendations as separable, they must be  
17 viewed together in terms of arriving at a rational price cap plan that serves the  
18 interests of consumers, Qwest and other providers, as the settlement does.

19 Taken together, the RUCO proposals do not advance the cause of consumers  
20 any further than the settlement agreement does. In fact, the recommendation to  
21 undertake a fully litigated proceeding entails substantially more risk to consumers  
22 than the settlement agreement, based on the positions taken by the all of the parties  
23 in their pre-filed direct cases. Clearly, several more months of delay in reaching a  
24 decision in this case will be damaging to the company and its shareholders.

25 RUCO's statements are, in some cases, contradictory and sprinkled with  
26 errors, omissions and misstatements about the settlement agreement. In addition,  
27 RUCO's expressed concerns are very broad and vague and RUCO does not tell us  
28 what they expect to achieve or how they expect to get there through a litigated  
29 proceeding. All of this leads to serious doubt about what would be achieved by  
30 rejecting the settlement agreement and extending this proceeding any further.

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1 THE PRODUCTIVITY ADJUSTOR

2 The settling parties have agreed to dispense with the productivity adjustor  
3 (PA) in the revised price cap plan as being inappropriate in today's market. As Staff  
4 witness Matthew Rowell put it, "In an environment in which revenues are declining  
5 and customers are being lost, a productivity adjustor is no longer appropriate. In  
6 such an environment, competition provides an incentive for the company to operate  
7 efficiently."<sup>1</sup>

8 In her responsive testimony, RUCO witness Marylee Diaz Cortez did not  
9 explicitly advocate continuing the PA, but she disagreed with the settlement  
10 agreement's method of disposing of the \$12 million PA incurred on April 1, 2005.

11 Ms. Diaz Cortez urges the Commission to dispose of the obligation by forcing  
12 Qwest to issue a \$12 million credit to customers' bills, pro-rated for the number of  
13 months the old plan remained in effect beyond April 1 and amortized over the first  
14 year of the new price cap plan. She recommends that the credit be applied to  
15 charges for basic residential and business services,<sup>2</sup> although the current plan  
16 requires only that the PA be applied to Basket 1 services.

17 At hearing, Ms. Diaz Cortez conceded that Decision No. 67734 does not specify  
18 a method for providing customers with the benefit of the PA and that the current  
19 plan doesn't require that it be applied to basic business and residential services or to  
20 residential rates at all.<sup>3</sup>

21 The settlement agreement proposes to subtract the PA liability from Qwest's  
22 first-year revenue requirement under the new price cap plan and to reduce by that  
23 amount the revenues available from flexible pricing in the new mix of Basket 2  
24 services.<sup>4</sup>

25 Staff witness Elijah Abinah testified that Qwest has previously met the  
26 requirements of the PA by reducing rates on 15 different Basket 1 services and that  
27 nine of those services would now be located in Basket 2. Thus, he concluded that

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<sup>1</sup> See Tr. @ 306-307

<sup>2</sup> See RUCO Ex. 8 @ 6-7

<sup>3</sup> See Tr. @ 480, 486 & 491

<sup>4</sup> See Staff Ex. 38 @ 6

1 applying the \$12 million to this group of services closely approximates the previous  
2 application of the PA.<sup>5</sup>

3 Mr. Abinah also argued that RUCO's proposal would produce ratepayer  
4 confusion by briefly lowering basic rates and then causing them to increase again  
5 automatically.<sup>6</sup>

6 In the view of the settling parties, the proposed disposition of the PA meets  
7 the requirement of Decision No. 67734 that the new price cap plan "include full  
8 credit" to ratepayers for the value of the productivity adjustment.<sup>7</sup>

9 Every party to this case has acknowledged that Qwest is financially stressed.  
10 RUCO, in fact, identified a revenue deficiency of \$160 million in its direct case.<sup>8</sup> In  
11 such circumstances, it makes little sense to kick off a rate relief program by forcing  
12 the company to relinquish nearly \$12 million in cash proceeds.

13 AUIA is constrained to point out, without assigning blame in any direction,  
14 that the April 1, 2005 productivity adjustment is an issue in this case only because the  
15 revised price cap plan was not adjudicated in the 20 months (now 28) after Qwest  
16 filed for revisions.

17 The Commission should reject RUCO's argument and adopt the treatment of  
18 the productivity adjustment in the settlement agreement.

19 **LITIGATION SHOULD BE A NON-STARTER**

20 RUCO witness Dr. Ben Johnson urges the Commission to reject the settlement  
21 agreement and order a fully litigated hearing on the parties' original positions. In  
22 addition to criticisms of specific provisions of the new price cap plan, he asserts that  
23 the plan fails to address three broad issues: geographic cost differences; geographic  
24 competitive differences; and the need for an improved Arizona universal service  
25 fund (AUSF).<sup>9</sup>

26 In discussing these differences, Dr. Johnson makes the rather obvious point  
27 that cost differentials exist between service areas and that higher service costs and  
28 stronger barriers to entry tend to prevail in rural areas as compared with higher

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<sup>5</sup> Ibid

<sup>6</sup> See Staff Ex. 38 @ 7

<sup>7</sup> Ibid

<sup>8</sup> See Diaz Cortez Direct, RUCO Ex. 6 @ 2, Tr. @ 487

<sup>9</sup> See RUCO Ex. 14 @ 15

1 density urban centers. He complains that the settlement agreement does not  
2 adequately address these differences.<sup>10</sup>

3 Beyond that observation, Dr. Johnson fails to explain what objectives RUCO  
4 would seek in a litigated hearing. Nevertheless, he asserts that “no further  
5 testimony needs to be submitted,” and “the Commission can go directly to a full  
6 hearing...”<sup>11</sup>

7 Yet, his testimony at hearing was that, “We don’t have enough data to know  
8 on net balance how well or how poorly Qwest is doing on the competitive  
9 battlefield.”<sup>12</sup> Elsewhere, Dr. Johnson asserted that Qwest’s services should be  
10 assigned to baskets primarily on the basis of competitive intensity.<sup>13</sup>

11 Qwest witness Jerrold Thompson responded that Dr. Johnson’s approach to  
12 aligning services within baskets would require a very long and complex process of  
13 examining market conditions and the competitiveness of Qwest services within  
14 individual wire centers.<sup>14</sup>

15 Under cross-examination, Dr. Johnson indicated that under his proposal as  
16 many as 150 wire centers “would be appearing in different baskets, depending on  
17 the degree of competition.”<sup>15</sup> Exactly how the Commission could perform this  
18 analysis based on the information in the record is a mystery.

19 Given the fact that there was virtually no agreement on major issues in the  
20 parties’ direct cases, such as Qwest’s proposal to create competitive zones, it is hard  
21 to comprehend how a litigated hearing would produce a well reasoned result  
22 without sending the key parties back to the drawing board to find a consensus.

23 Dr. Johnson is somewhat more explicit in discussing the need for an  
24 improved AUSF.<sup>16</sup> RUCO may be correct that a more robust AUSF is necessary to  
25 help equalize service costs in rural areas. Indeed, Qwest’s direct case included a  
26 proposal to beef up the Arizona AUSF.

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<sup>10</sup> See RUCO Ex. 14 @ 15-16

<sup>11</sup> See RUCO Ex. 14 @ 24

<sup>12</sup> See Tr. @ 407

<sup>13</sup> See RUCO Ex. 14 @ 11-12

<sup>14</sup> See Qwest Ex. 35 @ 16

<sup>15</sup> See Tr. @ 455-56

<sup>16</sup> See RUCO Ex. 14 @ 19-20

1           However, the reasoning that prevailed among the settling parties was that  
2 AUSF revisions should be considered in a separate commission docket, in large part  
3 because providers other than those involved in this proceeding would be affected  
4 by AUSF adjustments.<sup>17</sup>

5           Staff witness Rowell testified that a separate generic AUSF docket has been  
6 established and RUCO has offered no changes there, nor did Dr. Johnson  
7 recommend any in his direct testimony in this proceeding.<sup>18</sup> In addition, Mr. Rowell  
8 asserted that the record lacks any real evidence that changes to the AUSF would  
9 promote rural competition.<sup>19</sup>

10           The need for AUSF improvements is not a sufficient reason to reject the  
11 settlement agreement in this case.

12 **RUCO CRITICISMS ARE OFF BASE**

13           If RUCO's objectives in a litigated hearing are less than precise, their criticisms  
14 of the amended price cap plan are less than accurate.

15           Dr. Johnson's chief concern is that the settlement agreement will give Qwest  
16 excessive price flexibility in rural areas where it has relatively little competition.<sup>20</sup>

17           However, as Mr. Thompson testified, Qwest is subject to statewide pricing  
18 under the settlement agreement until the Commission orders a new pricing  
19 structure, effectively obviating Dr. Johnson's concern.<sup>21</sup> Mr. Rowell also testified  
20 that Qwest would be unable to raise rural rates without raising rates in urban areas  
21 where the company would be at risk for losing customers to competitors.<sup>22</sup>

22           Such an elementary misinterpretation of the settlement agreement is  
23 disturbing and it casts serious doubt on the outcome of a litigated proceeding.

24           Dr. Johnson's complaint about excessive price flexibility exposes a series of  
25 contradictions in RUCO's positions.

26           Mr. Rowell demonstrated that geographic pricing flexibility, which RUCO  
27 supported, and the basket structure advocated by RUCO in its direct case would  
28 allow for more pricing flexibility than is contained in the settlement agreement. He

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<sup>17</sup> See Staff Ex. 39 @ 13

<sup>18</sup> See Staff Ex. 39 @ 14

<sup>19</sup> See Tr. @ 328

<sup>20</sup> See RUCO Ex. 14 @ 12 & 19

<sup>21</sup> See Qwest Ex. 35 @ 14-15

<sup>22</sup> See Staff Ex. 39 @12, See Tr. @312-314

1 noted that Dr. Johnson, in his direct testimony,<sup>23</sup> advocated a 25% cap on rate  
2 increases for services that are currently in Basket 1, but now criticizes the settlement  
3 agreement for including most of those services in a new basket with a similar 25%  
4 cap.<sup>24</sup>

5 Indeed, Dr. Johnson's conflicting views continued on cross-examination when  
6 he testified that all residential local exchange services should be placed in a basket  
7 with moderate price flexibility in all wire centers except Phoenix main and Tucson  
8 main. When asked whether that would expose all residential service to extreme  
9 price changes, he said, "Yes, that's true in a sense."<sup>25</sup>

10 There are more discrepancies in RUCO's interpretation of the price cap plan:

11 • Dr. Johnson asserted in his responsive testimony that Basket 2 revenues can  
12 be increased by \$43.8 million when, in fact, the increases can't exceed \$13.8 million.<sup>26</sup>

13 At hearing, he corrected this error, calling it "a typo."<sup>27</sup>

14 • Dr. Johnson wrongly testified that zone increment charges will no longer be  
15 hard capped, when, in fact, they will be reduced and placed in Basket 1, and he  
16 claimed that Caller ID Block is moving to Basket 2 when it is remaining in Basket 1.<sup>28</sup>

17 Dr. Johnson also corrected these errors at hearing, saying they were mistakes  
18 "based on the testimony of the people who wrote the settlement."<sup>29</sup>

19 • Dr. Johnson asserted that Qwest could raise rates for additional access lines  
20 to unlimited monopoly levels, but provided no support for that assertion.<sup>30</sup>

21 • In his analysis of the amended rate cap plan, as he was warning of too much  
22 price flexibility, he failed to note that it would transfer six services from Basket 3 to  
23 Basket 1.<sup>31</sup>

24 • Finally, Dr. Johnson claimed that Qwest will have "complete freedom" to  
25 raise prices for local exchange packages, when, in reality, the settlement agreement

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<sup>23</sup> See Johnson Direct @ 184

<sup>24</sup> See Staff Ex. 39 @ 3 & 4-6

<sup>25</sup> See Tr. @ 458-459

<sup>26</sup> See RUCO Ex. 14 @ 13; See Staff Ex. 39 @ 8

<sup>27</sup> See Tr. @ 396

<sup>28</sup> See RUCO Ex. 14 @ 10 & Qwest Ex. 35 @ 9; See RUCO Ex. 14 @ 11 & Staff Ex. 39 @ 10

<sup>29</sup> See Tr. @ 423

<sup>30</sup> See RUCO Ex. 14 @ 13; See Staff Ex. 39 @ 9

<sup>31</sup> See Tr. @ 424-425

1 provides several limitations on package increases, including the overall revenue  
2 limitation on Basket 3.<sup>32</sup>

### 3 RUCO IGNORES REVENUE NEEDS, CONSUMER GAINS

4 In his opposing testimony, Dr. Johnson avoids any real discussion of Qwest's  
5 revenue requirement and which rates and charges would have to be increased to  
6 cure the deficiency.<sup>33</sup> This, in spite of RUCO's determination that the company is  
7 facing a revenue deficiency of \$160 million.

8 Dr. Johnson seems to believe that an acceptable price cap plan would only  
9 allow Qwest to reduce prices. He complains that the changes allowed in the  
10 settlement agreement "go almost entirely in the opposite direction..."<sup>34</sup>

11 He is absorbed by his disproven theory that the new price cap plan "will  
12 enable Qwest to extract additional revenues and profits from markets where the  
13 Company continues to enjoy a substantial degree of monopoly power..."<sup>35</sup> and he is  
14 unmoved by the Commission's legal responsibilities in setting rates.

15 Rather than fulfilling a revenue deficiency by imposing a general rate increase,  
16 the settlement agreement provides Qwest an opportunity to increase annual  
17 revenues by \$31.8 million through increased but limited price flexibility. In  
18 satisfaction of the Commission's legal responsibilities, the agreement also includes a  
19 determination of fair value and a finding that the permitted range of rates is just and  
20 reasonable. All of these matters would have to be litigated anew under Dr.  
21 Johnson's recommendation to the Commission.

22 Through Dr. Johnson's testimony, RUCO also chooses to ignore the  
23 substantial consumer benefits that would be delivered by the settlement agreement.  
24 Briefly, these include:

- 25 • Some \$4.5 million of annual price reductions, including zone increment
- 26 charges and non-published listings.
- 27 • An additional \$1 million in assistance for the qualified medically needy.
- 28 • A two-thirds increase in the construction credit for rural residential
- 29 installations.

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<sup>32</sup> See RUCO Ex. 14 @ 14; See Qwest Ex. 35 @ 13

<sup>33</sup> See Qwest Ex. 35 @ 3

<sup>34</sup> See RUCO Ex. 14 @ 21

<sup>35</sup> See RUCO Ex. 14 @ 22



1 **CERTIFICATE OF SERVICE**

2  
3 An original and 15 copies of the referenced brief  
4 filed this 2nd day of December, 2005, with:

5  
6 Docket Control  
7 Arizona Corporation Commission  
8 1200 W. Washington Street  
9 Phoenix, AZ 85007

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11 Copies of the referenced brief hand delivered  
12 this 2nd day of December, 2005, to:

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16 William A. Mundell, Commissioner  
17 Adam Stafford, Executive Assistant  
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