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BEFORE THE ARIZONA CORPORATION COMMISSION

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Arizona Corporation Commission

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IN THE MATTER OF QWEST )  
CORPORATION'S COMPLIANCE )  
WITH SECTION 271 OF THE )  
TELECOMMUNICATIONS )  
ACT OF 1996 )

Docket No. T-00000A-97-0238

**QWEST CORPORATION'S EXCEPTIONS REGARDING  
SECTION 271 SUB-DOCKET -- STAFF REPORT AND RECOMMENDATION  
AND REQUEST FOR HEARING**

Qwest Corporation respectfully submits these exceptions in response to the Section 271 Sub-Docket — Staff Report and Recommendation (Staff Report). Qwest further requests a hearing with respect to the penalties proposed by Staff.

**I. Introduction**

Staff recommends that the Commission impose contempt penalties on Qwest totaling \$7,415,000 based on Qwest's settlement agreements with CLECs that contain nonparticipation clauses. Staff calculated this penalty by assessing the statutory maximum penalty for each day on which it claims these agreements were in effect.

Qwest objects to the proposed penalty because such penalties can only be based on a violation of a requirement that specifically describes the conduct that is prohibited. The rule of procedure upon which Staff bases its recommendation does not prohibit settlement agreements with nonparticipation provisions. No party has identified any Commission order, rule, or requirement that prohibits such agreements. Therefore, Qwest cannot be penalized for contempt because it has not violated any requirement.

Setting aside the absence of the prerequisite violation, Qwest objects to the proposed penalty because the statute on which Staff bases its per day penalty assessment does not confer authority upon the Commission to impose contempt penalties on a daily basis. Further, no additional penalty arising from the nonparticipation agreements is warranted because Staff eliminated the impact of those agreements by holding a workshop at which any CLEC that had not participated had the opportunity to present any issues they had not previously raised and because Staff has already recommended penalties based on these clauses in the 252(e) docket.

In addition to the monetary penalty, Staff recommends that the Commission impose non-monetary penalties, including an expansive prohibition barring Qwest from entering into any agreement that includes any limitation on a CLEC's participation in regulatory proceedings in Arizona. Qwest objects to this prohibition because it effectively prevents any settlements with CLECs. This broad prohibition will preclude Qwest and CLECs from settling even individual disputes of the kind that Commission has indicated are appropriately settled. The prohibition is unnecessary because Qwest has committed to submit resolutions and settlements of disputes in cases of general applicability to the Commission for review. Staff supports this commitment and recommends that the Commission include this in its order. Because this process addresses the

Commission's stated concerns regarding nonparticipation agreements, no further regulatory obligations regarding settlement agreements are necessary.

Finally, in accordance with the Commission's December 12, 2002 Procedural Order, Qwest requests a hearing on the amount of the proposed fine and implementation of other remedies.

**II. No Penalty Is Appropriate Because the Necessary Predicate -- a Violation of an Existing Commission Order, Rule, or Requirement -- Has Not Been Established.**

A contempt penalty is not warranted here because the predicate for such a penalty does not exist: Qwest's agreements with CLECs that include clauses by which a CLEC agrees that its claims have been resolved and therefore withdraws from the contested case -- referred to in this case as "nonparticipation clauses" -- do not violate any Commission order, rule, or requirement.

**A. A Contempt Penalty must be based on a Violation of a Narrowly Drawn Order or Rule that Specifies the Prohibited Conduct.**

Arizona law provides that a contempt proceeding can be based only on a violation of a specific order, rule, or requirement of the Commission. A.R.S. § 40-424(A) provides as follows:

If any corporation or person fails to observe or comply with any order, rule or requirement of the commission or any commissioner, the corporation or person shall be in contempt of the commission and shall, after notice and hearing before the commission, be fined by the commission in an amount not less than one hundred nor more than five thousand dollars, which shall be recovered as penalties.

This requirement is consistent with hornbook law regarding contempt: "Punishment [for contempt] can only rest on a clear, intentional violation of a specific, narrowly drawn order; specificity is an essential prerequisite of a contempt citation."<sup>1</sup> The essence of contempt is that a

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<sup>1</sup> 17 Am. Jur. 2d Contempt § 157 (1990) (citations omitted) (emphasis added).

party fully understands, but chooses to ignore, a specific mandate; contempt cannot be based upon a vague requirement.<sup>2</sup>

Moreover, the specific, narrowly drawn mandate must give Qwest fair notice of the conduct prohibited or required. A regulatory requirement must, at minimum, “give fair notice that certain conduct is proscribed.”<sup>3</sup> A rule may be enforced only when “those subject to the rule are reasonably able to determine what conduct is appropriate.”<sup>4</sup> Under this “fair notice doctrine,” “the well-established rule in administrative law [holds] that the application of a rule may be successfully challenged if it does not give fair warning that the allegedly violative conduct was prohibited.”<sup>5</sup> The doctrine “has now been thoroughly ‘incorporated into administrative law,’” and is grounded in the due process clause of the United States Constitution.<sup>6</sup>

Thus, in order for Qwest to be penalized for entering into settlements containing nonparticipation agreements, those agreements must violate a specific, narrowly drawn mandate that fairly warns Qwest that entering into such agreements is prohibited. While, as discussed below, Staff points to a rule of practice and procedure that describes a party's rights in a hearing

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<sup>2</sup> *International Longshoremen's Assn. v. Philadelphia Marine Trade*, 389 U.S. 64, 77 (1967) (“We do not deal here with a violation of a court order by one who fully understands its meaning but chooses to ignore its mandate. We deal instead with acts alleged to violate a decree that can only be described as unintelligible. The most fundamental postulates of our legal order forbid the imposition of a penalty for disobeying a command that defies comprehension.”) (citations omitted).

<sup>3</sup> *Rabe v. Washington*, 405 U.S. 313, 314 (1972); see also *Palmer v. City of Euclid*, 402 U.S. 544 (1971); *Rabeck v. New York*, 391 U.S. 462 (1968).

<sup>4</sup> *In re N.P.*, 361 N.W.2d 386, 394 (Minn. 1985).

<sup>5</sup> *United States v. Chrysler Corp.*, 158 F.3d 1350, 1355 (D.C. Cir. 1998).

before the Commission, that rule does not contain any mandate regarding -- or even mention of -- settlements that resolve pending issues between the parties and that include withdrawal from a pending case. No party has identified any Commission order, rule, or requirement that provides that entering into settlement agreements with these types of nonparticipation clauses is prohibited.

**B. Procedural Rule 14-3-104 does not Prohibit Any Conduct.**

In its Report, Staff only points to one of the Commission's rules of practice and procedure as a basis for the contempt penalty it recommends.<sup>7</sup> Staff cites Rule 14-3-104, entitled "Appearances, rights of parties, representation by attorney, conduct and former employees." Specifically, Staff cites subsection A:

Rights of parties. At a hearing a party shall be entitled to enter an appearance, to introduce evidence, examine and cross-examine witnesses, make arguments, and generally participate in the conduct of the proceeding.

This rule cannot form the predicate for a contempt penalty because it does not impose any requirements or prohibit any conduct whatsoever, much less impose the specific, narrowly drawn mandate that is an essential prerequisite for contempt. Instead, the rule simply describes a party's rights at hearing. Neither the rule itself nor any precedent cited by Staff provides that a party

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<sup>6</sup> *General Electric Co. v. EPA*, 53 F.3d 1324, 1329 (D.C. Cir. 1995) (quoting *Satellite Broadcasting Co. v. FCC*, 824 F.2d 1, 3 (D.C. Cir. 1987)).

<sup>7</sup> Staff Report, ¶74. Staff also generally refers to its procedural orders in the Section 271 proceeding, offering one example of an order that Staff describes as "specifically designed to create a very open, collaborative process." Staff Report, ¶75. However, a review of that order, as well as the Commission's other procedural orders in the Section 271 proceeding, reveals no specific, narrowly drawn requirements relating to settlement. Accordingly, Qwest's arguments in this section relating to procedural Rule 14-3-104 apply equally to the Commission's procedural orders.

may not knowingly relinquish such rights, much less that a third party may not settle or offer to settle a matter in return for a release or other consideration constituting such relinquishment.

More specifically, the acknowledgement in Rule 14-3-104 of a party's rights to elect to participate in a Commission proceeding is not the kind of rule contemplated by the contempt statute because it does not require a party to take or refrain from taking any particular action. In fact, the rule cannot be read to provide any notice regarding any conduct. The rule does not mention settlements or waivers and, therefore, simply cannot fairly be read to set forth any requirement that prohibits Qwest from entering into settlement agreements that include nonparticipation provisions. Because the rule imposes no duty on Qwest, Qwest cannot be in violation of its provisions.

To find otherwise, and to impose penalties under the circumstances, would raise serious due process concerns. A statute must, at minimum, "give fair notice that certain conduct is proscribed."<sup>8</sup> Rule 14-3-104 does not give any notice, much less fair notice, that it prohibits entering into settlement agreements pursuant to which a party waives rights described in the rule, and it would be both unconstitutional and unfair for the Court or the Commission to penalize Qwest for failing to anticipate and comply with a standard that no authority had ever defined. "Where, as here, the regulations and other policy statements are unclear, where the petitioner's interpretation is reasonable, and where the agency itself struggles to provide a definitive reading

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<sup>8</sup> *Rabe v. Washington*, 405 U.S. 313, 314 (1972); see also *Palmer v. City of Euclid*, 402 U.S. 544 (1971); *Rabeck v. New York*, 391 U.S. 462 (1968).

of the regulatory requirements, a regulated party is not 'on notice' of the jury's ultimate interpretation of the regulations, and may not be punished."<sup>9</sup>

Moreover, it would be particularly unfair to attempt to read a prohibition against settlements with nonparticipation agreements into Rule 14-3-104 because Arizona public policy actually encourages parties to waive the very rights described in the rule as part of settlement agreements.

A waiver, often in the form of a release, is an important part of every compromise and settlement, without which the settlement of disputes would be rendered all but impossible.<sup>10</sup> Arizona law recognizes the long-established principle that public policy favors settlement.<sup>11</sup> This is consistent with the general principle of administrative law favoring settlement of administrative proceedings.<sup>12</sup> In settlements, parties may choose to waive whatever rights they see fit,<sup>13</sup> including the right to initiate or participate in regulatory proceedings. In fact, Arizona law allows a party to completely release and abandon an entire claim; once abandoned, the claim

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<sup>9</sup> *General Electric*, 53 F.3d at 1333-34.

<sup>10</sup> 66 Am. Jur. 2d Release § 2 (2001).

<sup>11</sup> See, e.g., *United Bank of Arizona v. Sun Valley Door & Supply, Inc.*, 149 Ariz. 64, 68, 716 P.2d 433, 437 (Ariz. Ct. App. 1986) ("Public policy favors settlement."); *Speed Shore Corp. v. Denda*, 605 F.2d 469, 473, citing *Williams v. First National Bank*, 216 U.S. 582 (1910) ("It is well recognized that settlement agreements are judicially favored as a matter of sound public policy."); *Shell Oil Company v. Christie*, 125 Ariz. 38, 39, 607 P.2d 21, 22 (Ariz. Ct. App. 1979) ("settlements of litigation are favored").

<sup>12</sup> *Arctic Slope Regional Corp. v. F.E.R.C.*, 832 F.2d 158, 164 (D.C. Cir. 1987).

<sup>13</sup> See, e.g., *Romska v. Opper*, 594 N.W.2d 853, 857 (Mich. App. 1999) ("[The Michigan Court of Appeals] is aware of no legal rule in Michigan that precludes settling parties from waiving whatever rights they choose.").

is extinguished and cannot be raised in any forum -- including regulatory proceedings.<sup>14</sup> Thus, not only can a party waive its right to participate in a regulatory proceeding, but it can waive its right to initiate a proceeding at all -- including the right to enter an appearance, introduce evidence, examine and cross-examine witnesses, and make arguments. Once a party enters into such an agreement, sometimes called a covenant not to sue, that agreement is enforceable under Arizona law.<sup>15</sup> Thus, under Arizona law, a party may waive all of the rights Rule 14-3-104 describes.

Parties routinely enter into such agreements and waive such rights to resolve disputes. The record demonstrates that this is exactly what occurred with the settlement agreements at issue here. The parties to those agreements entered into them voluntarily, through the deliberate exercise of their business judgment, to advance their legitimate business interests. For example, Eschelon voluntarily entered into those settlement agreements that it believed to be beneficial and refused to accept those proposals with which it did not agree.<sup>16</sup>

Given that Arizona law allows parties to waive all of the rights described in Rule 14-3-104 -- and their rights to initiate a regulatory proceeding in the first place -- there is no reasonable

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<sup>14</sup> *Cunningham v. Goettl Air Conditioning*, 194 Ariz. 236, 241, 980 P.2d 489, 494 (1999) ("When a party executes a release agreement, he or she abandons 'a claim or right to the person against whom the claim exists or the right is to be enforced or exercised.' The claim, once abandoned, is extinguished."), *citing* 66 Am. Jur. 2d Release § 1, at 678 (1973).

<sup>15</sup> *See, e.g., Hovatter v. Shell Oil Co.*, 111 Ariz. 325,328, 529 P.2d 224, 226 (1974) ("Covenants not to sue should be construed in harmony with the intent of the parties."); *Hall v. Schulte*, 172 Ariz. 279, 283, 836 P.2d 989, 993 (Ariz. Ct. App. 1992) ("When construing covenants not to sue, or any other contract, it is clear that if there are no ambiguities, interpretation is a question of law, and that merely because the parties disagree as to the meaning of an agreement, such disagreement does not create ambiguity. The interpretation which is placed on the agreement should be one that gives reasonable, lawful and effective meaning to all the terms.").

<sup>16</sup> *See, e.g.,* Deposition, Richard A. Smith, at 70:2-71:15 (Oct. 26, 2002).

basis upon which any prohibition against settlements including such waiver provisions can be read into the rule. The rule simply does not contain any such prohibition.

Because Rule 14-3-104 contains no specific, narrowly drawn requirement, it cannot form the necessary predicate for a contempt penalty. The statutory prerequisite has not been met and there is, therefore, no basis upon which to impose any contempt penalties.

**C. Due Process Precludes a Contempt Finding Based on a New Meaning or Application of Rule 14-3-104**

As fully discussed below in Section IV of these exceptions, Qwest believes that the Commission's concerns regarding the propriety of settlements that include nonparticipation agreements applies only in certain circumstances. While the Commission apparently perceives a distinction between issues that can appropriately be settled and those that should not, no articulation of this distinction exists. As discussed above, Rule 14-3-104 plainly contains no indication of any such distinction.

Setting aside Rule 14-3-104's failure to define *any* situation in which it would be inappropriate for a party to waive the rights the rule describes, Qwest now understands that the Commission does not favor nonparticipation agreements under certain circumstances. The Commission may, therefore, choose to expand the meaning or application of its existing orders, rules, or requirements to address settlements and releases. If the Commission decides to adopt a new interpretation of Rule 14-3-104 to address settlement agreements in this proceeding, however, fundamental notions of due process preclude the Commission from holding Qwest in

contempt based on violation of such a newly expanded rule.<sup>17</sup> Where punitive proceedings serve “as the initial means for announcing a particular interpretation’ – or for making its interpretation clear,”<sup>18</sup> an agency may not impose liability on a regulated party unless that party, “acting in good faith” and reviewing the regulations and public statements of the agency, “would be able to identify, with ‘ascertainable certainty,’ the standards with which the agency expects parties to conform.”<sup>19</sup> It would be unfair for the Commission to penalize Qwest for failing to anticipate and comply with an undefined requirement.

Because Qwest did not violate any existing Commission order, rule, or requirement, it would be inappropriate for this Commission to impose any contempt penalty.

### **III. Staff's Calculation of its Recommended Penalty is Flawed.**

Staff recommends that the Commission impose a penalty of \$7,415,000. As fully discussed below, Staff's proposed penalty is not consistent with the law, the facts, or sound public policy.

#### **A. Staff Erred in Calculating its Recommended Penalty on a Per Calendar Day, Per Occurrence Basis.**

Even assuming that the imposition of some penalty is authorized based on Rule 14-103-4 – which as demonstrated above it is not – a major premise of Staff's recommended penalty of \$7,415,000 is that A.R.S. § 40-424 allows the Commission to levy fines of up to \$5,000 per

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<sup>17</sup> *State v. Powers*, 20 Ariz. 123, 126, 23 P.3d 668, 671 (Ariz. App. 2001) (“Moreover, we recognize that a judicial expansion of statutory language can violate a defendant's due process right to fair warning.”)

<sup>18</sup> *General Electric*, 53 F.3d at 1329 (quoting *Martin v. OSHRC*, 499 U.S. 144, 158 (1991)).

<sup>19</sup> *Id.* (quoting *Diamond Roofing*, 528 F.2d at 649).

calendar day.<sup>20</sup> This interpretation of § 40-424 is inconsistent with the plain meaning of the statute under Arizona law, the statute's legislative history, and the purposes associated with "per day" penalties for "contempt."

**1. Section 40-424 Provides No Authority to Assess a Per Day Penalty.**

The plain language of § 40-424 contains no provision allowing for the assessment of penalties on a per day basis. The statute reads as follows:

§ 40-424. Contempt of corporation commission; penalty.

A. If any corporation or person fails to observe or comply with any order, rule or requirement of the commission or any commissioner, the corporation or person shall be in contempt of the commission and shall, after notice and hearing before the commission, be fined by the commission in an amount not less than one hundred nor more than five thousand dollars, which shall be recovered as penalties.

B. The remedy prescribed by this article shall be cumulative.

Thus, the statute does not authorize the Commission to impose a penalty for each day on which an alleged violation occurred.

Moreover, Arizona law prohibits any reading of the statute that would add any terms by implication. The Commission has no implied powers.<sup>21</sup> Instead, its powers are derived only from a strict construction of the Arizona Constitution and implementing statutes.<sup>22</sup>

A simple review of the statute reveals that it makes no provision for assessing a penalty on a per day basis. Because the Commission possesses only those powers that can be derived from a strict reading of the statute, no additional provision allowing the Commission to assess

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<sup>20</sup> Staff Report, ¶90.

<sup>21</sup> See, e.g., *Rural/Metro Corp. v. ACC*, 129 Ariz. 116, 117, 629 P.2d 83, 84 (Ariz. 1981).

the penalty on such a basis can be implied in that statute. Moreover, the Arizona Constitution expressly limits the Commission's power to impose fines to assessing a penalty on a per violation, not a per day, basis.<sup>23</sup> These provisions must be strictly construed and cannot be read to confer any implied powers. Thus, the Commission simply has no power to assess a contempt penalty on a per day basis.

Further, as set forth below, the legislative history of § 40-424 confirms that the Commission was never intended to have the power to assess penalties for contempt on a per day basis.

**2. The Legislative History of the Statute Demonstrates that the Legislature Intended to Preclude the Commission from Assessing Contempt Penalties on a Daily Basis.**

In addition to confirming that the statute does not -- and has never -- provided for the per day assessment of contempt penalties, the legislative history of § 40-424 demonstrates that the legislature expressly intended not to grant that power to the Commission. In order to fully understand § 40-424, it is necessary to review its history in conjunction with that of its companion statute, § 40-425.

Sections 40-424 and 40-425 were originally drafted in 1912 as part of Act 90, relating to public service corporations. Section 40-424 has survived in substantially the same form since

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<sup>22</sup> See, e.g., *Southern Pacific Co. v. ACC*, 98 Ariz. 339, 345, 404 P.2d 692, 696 (Ariz. 1965).

<sup>23</sup> Arizona Const., art. 15, sections 16 and 19, read as follows (emphasis added):

Section 16. If any public service corporation shall violate any of the rules, regulations, orders, or decisions of the corporation commission, such corporation shall forfeit and pay to the state not less than one hundred dollars nor more than five thousand dollars *for each such violation*, to be recovered before any court of competent jurisdiction.

that time, with relatively minor changes. This statute has never contained language authorizing the Commission to impose contempt penalties for each day on which a violation occurs. The predecessor to § 40-424, which was originally designated § 81, appears in the table below in the left column and the current version of § 40-424 appears in the right:

<p>Act 90, § 81</p> <p>In case any public service corporation, corporation or person shall fail to observe, obey or comply with any order, decision, rule, regulation, direction, demand or requirement, or any part or portion thereof, of the commission or any commissioner, such public service corporation, corporation or person shall be in contempt of the commission and shall be fined by the commission a sum not less than one hundred dollars nor more than five thousand dollars, to be recovered before any court of competent jurisdiction, in this state.</p> <p>Procedure had in such contempt proceedings shall be the same as in courts of record in this state. The remedy prescribed in this section shall not be a bar to or affect any other remedy prescribed in this act, but shall be cumulative and in addition to any such other remedy or remedies.</p>	<p>§ 40-424.</p> <p>A. If any corporation or person fails to observe or comply with any order, rule or requirement of the commission or any commissioner, the corporation or person shall be in contempt of the commission and shall, after notice and hearing before the commission, be fined by the commission in an amount not less than one hundred nor more than five thousand dollars, which shall be recovered as penalties.</p> <p>B. The remedy prescribed by this article shall be cumulative.</p>
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As shown above, the changes to § 40-424 consist of paring down "any order, decision, rule, regulation, direction, demand or requirement, or any part or portion thereof" to include only "any order, rule, or requirement," streamlining the statement that the remedy is cumulative, and other insignificant wording changes. Thus, § 40-424 does not now, nor has it ever, provided for the daily assessment contempt penalties.

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Section 19. The corporation commission shall have the power and authority to enforce its rules, regulations, and orders by the imposition of such fines as it may deem just, *within the limitations prescribed in section 16 of this article.*

Section 40-425, on the other hand, underwent a significant change. Subsection B of the predecessor to § 40-425, which was originally designated § 76, appears in the table below in the left column and the current version of § 40-425(B) appears in the right (emphasis added):

<p>Act 90, § 76(b) Every violation of the provisions of this act, or of any order, decision, decree, rule, direction, demand or requirement of the commission, or any part or portion thereof, by any corporation or person is a separate and distinct offense, and <i>in case of a continuing violation each day's continuance thereof shall be and be deemed to be a separate and distinct offense.</i></p>	<p>§ 40-425(B) Each violation is a separate offense, <i>but violations continuing from day to day are one offense.</i></p>
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Thus, the predecessor statute, § 76, specifically provided that each day on which a continuing violation occurred constituted a separate offense. Thus, because the penalty applied to each offense, the original version of § 40-425 provided for the per day assessment of penalties.

This very aspect of Act 90 was among those challenged in *Van Dyke v. Geary*.<sup>24</sup> In that case, the court found that Act 90's imposition of penalties, including the per day assessment of monetary penalties, to be unconstitutional.<sup>25</sup> After the *Van Dyke* case was decided, the Arizona legislature changed the language in subsection (b) of the statute, which provided that each day of a continuing violation constituted a separate offense, to its current form.<sup>26</sup> Section 40-425(B) now provides that "[e]ach violation is a separate offense, *but violations continuing from day to day are one offense.*"

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<sup>24</sup> *Van Dyke v. Geary*, 218 F. 111 (D. Ariz. 1914)

<sup>25</sup> *Id.* at 121.

<sup>26</sup> *See* Rev. Code 1928, § 15-728.

This legislative history is instructive because it explains the differing approaches to the same end result -- *i.e.*, no per day assessment of penalties -- in the language of § 40-424 and § 40-425. First, it shows that the Arizona legislature deliberately omitted the authority to assess per day penalties from § 40-424 because it included the ability in one statute and did not include it in the substantively identical companion statute. In other words, if the legislature intended to authorize the Commission to impose per day penalties under § 40-424, it would have done so expressly, as it did in § 40-425.

Contrary to Staff's claim,<sup>27</sup> the absence from section § 40-424 of the language now included in § 40-425 explicitly providing that a continuing violation constitutes a single offense does not suggest that the Commission is authorized to impose a per day fine under the former. As discussed above, this interpretation not only impermissibly expands the authority § 40-424 confers, but it is also directly contrary to the legislative history of both statutes. The legislative history establishes that the inclusion of language in § 40-425 explicitly providing that a continuing violation constitutes a single offense was intended to expressly eliminate the daily assessment of fines after the original statute's provision permitting the per day assessment was struck down. No such language exists in § 40-424 because that statute never allowed the daily assessment of penalties. No change was necessary.

The legislative intent is clear: the current forms of these statutes are not intended to and do not confer any authority upon the Commission to assess penalties on a per day basis.

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<sup>27</sup> Staff's Initial Post-Hearing Brief, *In the Matter of Qwest Corporation's Compliance with Section 252(e) of the Telecommunications Act of 1996*, Docket No. RT-00000F-02-0271, at 19-20

**3. Staff's Rationale for Proposing Per Day Contempt Penalties Requires an Unreasonable Reading of the Statutes.**

In addition to being contrary to the language and legislative history of the statute and constitution, Staff's construction of §40-424 as authorizing a per day penalty is unreasonable.

Section 424 applies only to violations of the Commission's orders, rules, and requirement. Section 425, however, applies to Constitutional and statutory violations, in addition to violations of the Commission's orders, rules, and requirements. Thus, Staff's reading of these statutes would limit penalties for Constitutional and statutory violations, while authorizing exponentially greater penalties for violations of Commission rules. As noted above, the Commission has only those powers conferred on it by the Constitution and implementing statutes. Given that the Commission has only derivative authority, it would make no sense for violation of a Commission order to result in exponentially greater penalties than a violation of the Constitution, the very organic law of the State of Arizona.

**B. No Additional Penalty is Necessary because the July 2002 Workshop Remedied the Impact of the Settlement Agreements on the Section 271 Proceeding.**

Staff has already addressed the impact of the nonparticipation agreements by holding a workshop in July 2002 to ensure that all outstanding issues were identified and addressed. Staff's stated purpose for this workshop "was to allow any CLEC the opportunity to raise any issue which it believed it had been precluded from raising due to an unfiled agreement with Qwest."<sup>28</sup> Eschelon and McLeod fully availed themselves of this opportunity. As Staff states, "[t]he July 30-31, 2002 Workshop provided CLECs which had not participated in the Section 271 proceeding the opportunity to present all issues which they had not previously presented. Staff,

in its reports on this Workshop, proposes resolutions for all of these issues."<sup>29</sup> The July 2002 workshop provided CLECs the opportunity to raise any issues that they did not previously raise and Staff has or will propose resolutions for all such issues, thus neutralizing the impact of the nonparticipation agreements. No additional penalty is necessary or warranted to address that impact.

It is important to note that the FCC, DOJ, and several other state commissions have considered the effect of these same settlement agreements on Section 271 proceedings. In the *Qwest 9-State Order*, the FCC found that the nine-state record contained no persuasive evidence of any specific harm arising from the nonparticipation agreements:

The Colorado Commission, Iowa Board and Wyoming Commission have explicitly found that they were not presented with any evidence that could lead them to conclude that the record was incomplete or flawed, nor did the commissions of any of the other application states find the concerns raised by the unfiled agreements sufficiently severe or urgent to recommend denying or delaying approval of Qwest's applications. Given that there is no persuasive evidence of specific harm in our record, we cannot conclude that the nonparticipation of some competitive LECs renders Qwest's application contrary to the public interest.<sup>30</sup>

In its *Qwest 3-State Order*, the FCC found "that commenters have provided no evidence that the records developed by the state commissions are wanting because certain competitive

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<sup>28</sup> Staff Report, ¶78.

<sup>29</sup> Staff Report, ¶92.

<sup>30</sup> Memorandum Opinion and Order, *In the Matter of Application of Qwest Communications International, Inc. for Authorization to Provide In-Region, InterLATA Services in the States of Colorado, Idaho, Iowa, Montana, Nebraska, North Dakota, Utah, Washington, and Wyoming*, WC Docket No. 02-314 (Dec. 20, 2002), ¶ 492.

LECs did not participate."<sup>31</sup> Similarly, in its evaluation of Qwest's first application, the DOJ stated that "the fact that certain CLECs did not participate [in the three-year ROC OSS test process] does not appear to have had a significant impact on the result."<sup>32</sup>

After considering evidence presented at *en banc* workshops, the Colorado Public Utilities Commission squarely addressed the issue in its comments supporting Qwest's Section 271 application for authority in Colorado:

In a "but for" world, the potential impact of CLEC *non*participation in the collaborative process is, at worst, close to nil. Smaller CLECs have elected to avoid the § 271 process altogether for a variety of reasons. Several CLECs have consistently participated, and others have participated when and as it was in their best interests to do so. The vast majority of impasse issues in Colorado have similarly been presented to the multistate facilitator, the Washington Commission, and the Arizona [Commission] for resolution. At the end of the day, no SGAT provisions would be worded differently, prices would not be adjusted, and impasse issue resolutions would not be modified. Such certainty is the incremental benefit of holding open, exhaustive § 271 proceedings.<sup>33</sup>

The Washington Utilities and Transportation Commission similarly rejected the notion that Qwest's settlement agreements raise issues relating to a Section 271 proceeding in its comments supporting Qwest's Section 271 application for authority in Washington:

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<sup>31</sup> Memorandum Opinion and Order, *In the Matter of Application of Qwest Communications International, Inc. for Authorization to Provide In-Region, InterLATA Services in New Mexico, Oregon and South Dakota*, WC Docket No. 03-11 (Apr. 15, 2003), ¶ 132.

<sup>32</sup> Evaluation of the United States Department of Justice, *In re: Application by Qwest Communications International, Inc. for Authorization to Provide In-Region, InterLATA Services in the States of Colorado, Idaho, Iowa, Nebraska, and North Dakota*, WC Docket No. 02-148 (July 23, 2002), at 5.

<sup>33</sup> Evaluation of the Colorado Public Utilities Commission, *In re: Application by Qwest Communications International, Inc. for Authorization to Provide In-Region, InterLATA Services in the States of Colorado, Idaho, Iowa, Nebraska, and North Dakota*, WC Docket No. 02-148 (July 2, 2002), at 64-65.

There will always be complaints about Qwest's behavior, competitive or anti-competitive, and this Commission has resolved and will continue to resolve those complaints. The issue here is whether there is anything that is sufficient to delay or give pause to our review of an application by Qwest under section 271. We do not find the evidence presented by the parties, individually or collectively, sufficiently unusual or disturbing to preclude a finding that an application would be in the public interest.<sup>34</sup>

Thus, the FCC, DOJ, and several other state commissions have found Qwest's settlement agreements do not impact this Commission's Section 271 record or recommendation.

Finally, as a general matter, penalties must be proportionate to the offense.<sup>35</sup> In evaluating the lawfulness of a potential fine, courts consider the seriousness of the offense itself and whether the proposed fine for that offense is proportional to fines given for the same or similar offenses in other cases. These legal principles should guide the Commission here.

As discussed above, no existing order, rule, or requirement of the Commission prohibits nonparticipation agreements. However, even if there were such a requirement, the Commission must then evaluate the relative harm caused by Qwest's violation of that requirement. As discussed above, the July 2002 workshop provided CLECs the opportunity to raise any issues that they did not previously raise and Staff has proposed resolutions for those issues. Further, the FCC, DOJ, and other commissions have found that the existence of nonparticipation agreements does not negatively impact Qwest's Section 271 applications. Accordingly, no additional penalty is necessary or warranted to address the impact of the nonparticipation agreements. .

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<sup>34</sup> Comments of the Washington Utilities and Transportation Commission, *In re: Application by Qwest Communications International, Inc. for Authorization to Provide In-Region, InterLATA Services in Montana, Utah, Washington, and Wyoming*, WC Docket No. 02-189 (July 26, 2002) at 32, quoting WUTC's 39<sup>th</sup> Supplemental Order ¶ 331.

<sup>35</sup> See *United States v. Bajakajian*, 524 U.S. 321 (1998).

**C. Any Penalty Imposed in this Proceeding must be Offset Against Any Penalty Imposed in the Section 252(e) Proceeding based on Nonparticipation.**

Although the precise extent to which the \$15,047,000 in penalties proposed in the Section 252(e) proceeding are based on the inclusion of nonparticipation agreements is unclear, Staff has plainly based some significant portion of that penalty on those agreements. In its late-filed exhibit in the Section 252(e) proceeding, Staff includes numerous references to nonparticipation clauses in explaining how it calculated its proposed penalty.<sup>36</sup> It would be unfair to impose penalties in both proceedings based on the very same conduct. Accordingly, any penalty imposed in this proceeding must be offset against any penalties imposed in the Section 252(e) proceeding, to the extent that the penalties in the 252(e) proceeding are based upon nonparticipation clauses.

**III. Staff's Proposed Prohibition against Nonparticipation Agreements would Broadly Preclude Any Settlement Agreement.**

In addition to the monetary penalty discussed above, Staff broadly recommends that Qwest be prohibited from entering into any agreement in which a CLEC foregoes any right to participate in "Arizona proceedings." Specifically, Staff states as follows:

86. Qwest should also be prohibited from including any language in future Interconnection Agreements, or in any other verbal or written agreements or otherwise binding documents which limit CLEC participation in Arizona proceedings, prohibit CLECs from filing complaints with the ACC, or in any other way infringe on CLEC rights and/or interfere with normal Arizona regulatory proceedings. Should such language recur in the future, significant monetary penalties should be levied against Qwest.<sup>37</sup>

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<sup>36</sup>See Staff's Notice of Filing Post Exhibit, dated April 1, 2003, Section 252(e) docket.

<sup>37</sup> Staff Report, ¶86.

Qwest's primary concern is that this language is so broad as to prohibit Qwest from entering into any agreement pursuant to which a CLEC waives any rights in Arizona.

As a practical matter, because such a prohibition would preclude a standard release, this prohibition would preclude Qwest from entering into any settlement agreements with CLECs of any kind in Arizona. This proposed penalty would have significant consequences for both CLECs and Qwest. Qwest's business relationships with CLEC would immediately suffer because Qwest would no longer be able to reach reasonable compromise agreements regarding issues that arise during the course of day to day operations. Without the practical ability to settle issues, the parties would be forced to litigate every significant issue that arises. This would impose a particularly harsh burden on small CLECs.

Qwest does not believe that this Commission's concerns regarding nonparticipation agreements is as far-reaching as this proposed prohibition. Indeed, Chairman Spitzer recognized that settlement of cases can be "appropriate."<sup>38</sup> Thus, the Commission recognizes that settlements, including waivers of the rights such as those described in Rule 14-3-104, are appropriate under certain circumstances. For example, the Commission recognizes that it is entirely appropriate for a company to settle an inter-carrier dispute by agreeing to pay money to the other company -- in return for that company's agreement to dismiss a complaint filed before the Commission and not to bring any other action on the basis that was settled.<sup>39</sup> Assuming that the Commission is not troubled by such a settlement, it is clear that the Commission sees a

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<sup>38</sup> Transcript of December 13, 2002, at 37.

<sup>39</sup> *See, e.g.*, Transcript of June 19, 2002, at 23 (Chairman Spitzer recognizes the distinction between settling a dispute on a private matter and a proceeding like the Section 271 docket that has broader implications).

distinction that separates the kinds of issues it believes are appropriate for settlement from the issues that the Commission believes should not be settled. Staff's proposed blanket prohibition does not recognize that distinction.

Qwest now understands that the Commission does not favor nonparticipation agreements in circumstances where such provisions may impair the Commission's regulatory oversight. The Commission has indicated that those circumstances involve proceedings that have general applicability, such as merger dockets and Section 271 proceedings. Although Qwest believed in the past that the resolution of issues pending in any docket was encouraged under Arizona law, Qwest has committed to submit in the future all resolutions and settlements of disputes in cases of general applicability (including for example Alternative Forms of Regulation (AFORs), mergers and acquisitions, and others of that type) to the Commission for review.<sup>40</sup> As part of the Commission's review, it can determine whether the agreement should be disapproved as against the public interest.

Qwest's proposed approach presents a reasonable balancing of the Commission's concerns and Qwest's and the CLECs' legitimate need to be able to resolve their disputes in the ordinary course of business by allowing the Commission to review the terms of resolutions and settlements of disputes in cases of general applicability. Staff agrees that Qwest's proposed filing of resolutions and settlements of disputes in cases of general applicability addresses the Commission's concerns, as evidenced by Staff's recommendation that the Commission incorporate that proposal in its order.<sup>41</sup> Because this proposal adequately addresses the concerns

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<sup>40</sup> Pre-Filed Rebuttal Testimony of Larry B. Brotherson, at 10:11-16.

<sup>41</sup> Staff Report, ¶85.

expressed by the Commission, Staff's inclusion of the additional prohibitions and potential penalties is unnecessary, in addition to being so broad as to hinder both CLECs and Qwest from conducting business with one another.

Finally, because the Staff's language is imprecise, the meaning of this prohibition is not clear. Specifically, Staff's proposed prohibition applies to "in any other way infring[ing] on CLEC rights and/or interfer[ing] with normal Arizona regulatory proceedings." Qwest is aware of no existing Commission orders, rules, or requirements relating to infringement of CLEC rights or interference with normal regulatory proceedings. Absent any definition of the meaning of those terms, this prohibition would not provide any fair warning of the conduct that is prohibited.

Accordingly, Qwest requests that the Commission reject Staff's proposed prohibition.

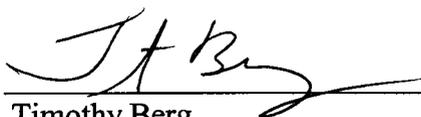
#### **IV. Conclusion**

As demonstrated above, Staff's rationale for its recommended monetary penalty is not supported by the facts, the law, or sound public policy. Qwest cannot be assessed penalties for contempt because it has not violated any existing order, rule, or requirement of this Commission. Further, even if such a violation had occurred, Staff's penalty calculation is erroneous as a matter of law because it is based on an impermissible interpretation of the Commission's power to impose fines. Finally, Staff's proposed prohibition against settlements would interfere with Qwest's ability to resolve even those disputes with CLECs that the Commission believes are appropriately settled.

For the foregoing reasons, Qwest asks that the Commission reject Staff's recommended monetary penalty and Staff's proposed prohibition against settlements, as described above.

RESPECTFULLY SUBMITTED this 16<sup>th</sup> day of May, 2003.

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