

1 **Public Interest Analysis**

2 *Potential Harm*

3

4 **Q. You have been discussing the potential benefits of the merger. Are there any potential**  
5 **detrimental effects which could arise from the merger of Qwest and US West?**

6 A. Yes. There are aspects of the proposed merger which may not be in the public interest. First,  
7 the merger could hinder the development of local competition in US West's region by  
8 eliminating a viable competitor (Qwest) and by strengthening the competitive position of the  
9 dominant carrier (US West). Second, there is a significant risk that the merger will have the  
10 effect of diverting of US West's resources away from the 14 state in region, redirecting these  
11 resources towards Qwest's ventures in other parts of the country and the world. Even within  
12 the region, Qwest may concentrate on retaining and expanding its share of key business and  
13 urban markets, while giving little attention to its residential, suburban and rural customers. Third,  
14 there is a risk that within Arizona, the combined company will be even less motivated to  
15 provide high quality service at a reasonable price. Given its national and international  
16 broadband orientation, Qwest may view residential and rural customers in Arizona as a cash  
17 cow, whose primary role is to help finance its global expansion.

18

19 **Q. Could you explain how the merger might eliminate a potential competitor in US West's**  
20 **local markets?**

21 A. Qwest is predominantly an interexchange carrier, but the company and its affiliates have some  
22 operational experience in local markets. Qwest explains its experience as follows:

23

24 Qwest subsidiaries have resold local services to a number of customers,  
25 including an imbedded base of residential customers....Through such efforts,  
26 Qwest has been able to offer resold local service to its customers in large areas  
27 of the regions served by incumbent local providers Bell Atlantic, BellSouth,

1 SBC and Ameritech. To meet the challenges of local television service, Qwest  
2 has formed a new division called QwestLINK that will be responsible for  
3 Qwest's local market expansion throughout the United States. The employees  
4 of QwestLINK have been recruited from companies with years of experience  
5 in the provision of local telephone service, including SBC, MCI metro, ELI and  
6 Nextel to name just a few. [Response to Staff IR 1-27].  
7

8 Qwest's current plans for local market expansion include shifting people and resources "to  
9 accelerate building 25 local broadband networks". [Response to AT&T IR 1-26, Attachment  
10 A]. Businesses in four California cities will be the first to receive integrated voice and data  
11 services over Qwest's local network. To date, however, most of Qwest's local services have  
12 been provided through resale of incumbents' services.  
13

14 **Q. What type of local service presence does Qwest have within US West's region?**

15 A. In its Application filed with the FCC, Qwest states that it "does not have material local  
16 facilities-based activity in the US West Region". [FCC Application, p. 13]. Also, Qwest  
17 explains that all resale customers in US West's region "have now been migrated to other  
18 service providers". [Response to AT&T IR 1-11]. I have not found any data regarding the  
19 number of resale customers Qwest had in US West's region prior to its merger plans.  
20 However, the timing of Qwest's plan to merge with US West and its decision to divest itself of  
21 its local in region customers is not coincidental. Instead, it appears that Qwest decided to merge  
22 with US West, rather than compete with this dominant carrier.  
23

24 **Q. Would Qwest have been a viable local competitor if it had not chosen to merge with US  
25 West?**

26 A. Yes. Qwest is well-positioned to be a major competitor to USWC in the provision of local and  
27 other bundled services within Arizona and in other parts of the 14 state region. Qwest has built  
28 an long haul network throughout the USWC region, and it is currently building local networks in

1 various markets across the country. Until recently, Qwest was actively reselling in region local  
2 services. Also, several Qwest subsidiaries operate as CLECs in various markets in region and  
3 out of region. [See, Response to AT&T IR 1-2, Attachment C]. There is every reason to  
4 assume that, absent the merger, Qwest would become an aggressive entrant into US West's  
5 local markets in the Phoenix and Tucson areas.

6  
7 **Q. Could the merger affect the likelihood that other potential competitors will enter US**  
8 **West's market?**

9 A. Yes. In April of 1999, Qwest announced a deal with BellSouth in which BellSouth purchased  
10 approximately 10 percent of Qwest's outstanding shares for \$1.93 billion.  
11 [\[www.bellsouthcorp.com\]](http://www.bellsouthcorp.com). Terms of the deal may also give BellSouth the right to purchase an  
12 additional 10 percent of Qwest. [See, Comments of Allegiance Telecom, October 1, 1999,  
13 FCC Docket 99-272]. After the merger, BellSouth will effectively own a significant share of  
14 US West. Given this investment, BellSouth will be less likely to become a competitor in the 14  
15 state region. Other carriers may also be discouraged from entering the US West region—not  
16 necessarily because of a direct conflict of interest, but simply because the Qwest/US West  
17 combination may enjoy an even more dominant position than US West and other RBOCs that  
18 are largely confined to their own region, and don't control a nationwide fiber network.

19  
20 **Q. Eliminating or discouraging potential competitors will further strengthen US West's**  
21 **competitive position. Are there other aspects of the merger that will increase US**  
22 **West's ability to dominate its markets?**

23 A. Yes. The merger will create a unique competitive powerhouse, combining a dominant local  
24 exchange carrier with a nationwide broadband network. This combination will allow Qwest to  
25 offer service packages that will be very hard for prospective competitors to match.  
26 Accordingly, the combined company may gain an even greater ability to stifle competition and

1 protect its dominant share of the market in the 14 state region.

2  
3 **Q. Has US West been successful in maintaining its market share, to date?**

4 A. Yes. Up to date, detailed market share data is, unfortunately, not readily available. The FCC  
5 maintains certain databases containing information provided by large ILECs. However, the  
6 data is not fully current, and it does not include statistics for facilities-based competitors.  
7 Nonetheless, such data can be used to get a general feel for the extent to which competitors are  
8 successfully entering incumbents' markets. Table 4 below shows the number of switched  
9 access lines for US West and other large ILECs, as of December 31, 1998. Also shown are  
10 the number of access lines being resold by competitors and the number of loops that are being  
11 rented to CLECs.

12  
13 **Table 4**  
14 (000)

15

ILEC	Total Switched Lines	UNE Loops	Resold Lines	Percent UNEs and Resale
Ameritech	21,054	100	450	2.6%
Bell Atlantic	41,429	91	619	1.7%
BellSouth	24,104	41	543	2.4%
GTE	17,008	23	100	0.7%
SBC	36,778	67	823	2.4%
Sprint	7,545	30	54	1.1%
US WEST	16,695	8	149	0.9%
US West-Arizona	2,720	1	11	0.4%

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1 As shown, as of the end of 1998, competitors were renting or reselling 0.9 percent of US  
2 West's lines in its 14 state region. This compares to 1.1 to 2.6 percent for other large ILECs.  
3 In Arizona, competitors were only renting or reselling 0.4 percent of US West's lines.

4 As I explained, this data does not include lines provided by facilities-based competitors.  
5 Also, the data is 14 months old. Given the trend towards competition, and the fact that some  
6 competitors are providing service over their own facilities, it is reasonable to assume that today,  
7 US West's share of the Arizona market has declined below 99 percent. Undoubtedly, some  
8 parts of the state are seeing more competitive activity than some other parts of the state, but the  
9 overall trend is quite gradual. Keep in mind that by December 1998, the date of these statistics,  
10 the 1996 Federal Act had been in effect for nearly three years.

11 I expect competitors will continue to refine their business plans, and will increasingly  
12 gain credibility with customers. Over time, they can be expected to provide an increasingly  
13 more significant competitive challenge to US West (or Qwest). However, even the most  
14 generous interpretation of the market data suggests that competitive entry is not an easy  
15 process, and it will be a long time before US West no longer dominates Arizona markets. It  
16 may be even longer if US West has the ability to use Qwest's services and facilities to offer  
17 services and packages that can't be matched by competitors. In fact, the Companies' estimated  
18 synergies include increased revenues from \*\*\***Highly Confidential**

19 **Highly Confidential**\*\*\* [Response to Staff IR 1-29, Attachment B].

20 Qwest expects to slow market share losses by a \*\*\***Highly Confidential**

21 **Highly Confidential**\*\*\* [Id.].

22  
23 **Q. Let's discuss your second concern. Can you explain why you think Qwest may focus on**  
24 **urban areas and large telecommunications intensive business customers?**

25 **A.** Qwest bills itself as "a leader in reliable, scalable and secure broadband Internet-based data,  
26 voice and image communications". [Qwest Press Release, November 2, 1999]. Qwest also has

1 explained that advanced services are “key drivers” of the proposed merger. [Response to Staff  
2 IR 1-26]. Clearly there is demand for such services in all market segments; consumer, small  
3 business and large business. However, by far the easiest way to generate traffic for its national  
4 broadband network is to sign up large business customers, including banks, governmental  
5 agencies, financial service companies and the like. Large, communications intensive customers,  
6 with their relatively high traffic volumes, can easily generate the high volumes of traffic which  
7 Qwest needs to fully utilize its extensive national network. These high revenue customers are  
8 also likely to be subject to be targeted by AT&T, MCI Worldcom, and other nationally-  
9 oriented competitors. The intense competition for these high volume customers creates a further  
10 incentive for Qwest to focus its attention on serving these large business customers. A similar  
11 set of incentives exists with respect to urban markets, relative to rural ones. Upon completion of  
12 the merger, there will be even less focus on small, rural markets, with a corresponding increase  
13 in the attention given to the largest urban markets. While customers in Phoenix and Tucson may  
14 be indifferent to (or even benefit from) this shift in emphasis, there is reason to be concerned  
15 about the quality of service and level of attention that will be paid to rural communities served  
16 by US West in Arizona.

17  
18 **Q. Let’s discuss the third potential effect of the merger. Can you explain the risk that**  
19 **revenues and resources will be diverted away from Arizona towards Qwest’s ventures**  
20 **in other markets?**

21 A. Qwest is a globally oriented corporation, which has been “implementing its strategy of being a  
22 leading broadband Internet communications company through its national high capacity fiber  
23 communications network”. [Qwest S-4, p. I-17]. In addition to its nationwide broadband  
24 network, Qwest is building an extensive pan-European network, and it is installing submarine  
25 networks across both the Atlantic and Pacific Oceans. [[www.qwest.com](http://www.qwest.com), 1998 Annual  
26 Report]. Qwest recently reported that its European network has been extended to 11,800

1 miles. [Qwest Press Release, January 10, 2000]. According to the Companies Synergies  
2 Analysis, **\*\*\*Highly Confidential**

3 **Highly Confidential\*\*\***. [Response to  
4 StaffIR 1-29, Attachment B]. From the perspective of consumers in Arizona, there clearly is a  
5 risk that the amount of management attention, investment capital and other resources devoted to  
6 this region will decline, as Qwest expands its global operations and concentrates on growing its  
7 out of region broadband business.

8  
9 **Q. Are you suggesting that US West should be prohibited from pursuing out-of region**  
10 **ventures?**

11 A. Certainly not. Carriers should be free to compete nationally or globally as they choose.  
12 However, what may be good for management and stockholders isn't necessarily risk-free for  
13 customers. The Commission should be aware of the fact that this merger poses some clear  
14 downside risks for consumers in Arizona. Implementing a merger between two large companies  
15 can be challenging doing this at the same time that one of the companies is rapidly growing on a  
16 national and international basis can be even more difficult. As well, I am concerned that in the  
17 pursuit of its national and international goals, Qwest may not give much attention to the  
18 relatively prosaic challenge of delivering high quality service to consumers in Arizona. Likewise,  
19 there is reason to be concerned that Qwest will concentrate its capital in out-of-region markets  
20 where it perceives the greatest growth opportunities, and correspondingly invest too little in the  
21 infrastructure and resources that are needed to improve service quality. Stated simply, the  
22 combined company may view the consumers of Arizona as captive ratepayers that are capable  
23 of providing large amounts of cash flow, regardless of how much service deteriorates. By  
24 maximizing revenues in markets where it has monopoly power, and minimizing the costs of  
25 serving these markets (even at the expense of service quality), Qwest may be able to better  
26 achieve its overall corporate goals. Qwest may be in a better position to fuel its expansion

1 plans elsewhere in the world if it treats Arizona and other in-region markets as “cash cows.”  
2 This strategy would emphasize cash flows generated, rather than strengthening customer  
3 relationships and achieving the highest possible level of customer satisfaction and service  
4 quality.

5  
6 **Q. Have you reviewed indicators of the service quality currently provided by US West, in  
7 comparison with other incumbent LECs?**

8 A. Yes. I reviewed data compiled by the FCC from periodic ARMIS reports filed by major  
9 ILECs. I also have reviewed data provided during discovery by US West in this proceeding. In  
10 general, the ARMIS data shows US West’s current level of service is less than stellar; a further  
11 deterioration could drop US West to the bottom of the group. In reaching this conclusion, I  
12 looked at five major components of the ARMIS service quality report for the five Regional Bell  
13 Operating Companies (US West, Ameritech, BellSouth, BellAtlantic, and SBC).

14 The first component of the report contains measures of customer dissatisfaction with the  
15 company’s installation, repair, and business office services. The report also delineates between  
16 three customer groups: residents, small businesses, and large businesses. As shown on Page 1  
17 of Schedule 1, US West currently performs quite well among residents in each of the three  
18 service categories. Its business office operations received the lowest dissatisfaction rating of the  
19 five ILECs (2.2%). But the ratings worsen for small businesses and grow even higher for large  
20 businesses. Although it again gets good marks for business office service (5.2%), the  
21 company’s small business customers give it the highest installation disapproval rating (12.8%).  
22 Large businesses report dissatisfaction with US West at the highest rate in each of these three  
23 service areas.

24 The second report contains the percentage of installation orders that a company  
25 successfully executes and the average number of days it takes to complete these orders. As  
26 shown on Page 2 of Schedule 1, by this measure of service quality, US West was similar to the

1 other ILECs. It successfully completed 98.3 out of every 100 service commitments and it  
2 completed these installations in an average of 1.3 days. While three of the other ILECs met a  
3 higher percentage of their commitments, and two had shorter installation intervals, the  
4 differences are not very substantial.

5 The third section deals with the total number of circuit-specific trouble reports referred  
6 to the ILEC and the speed with which these reports were resolved. US West had the second  
7 highest rate of trouble reports, exceeded only by BellSouth. The Company did not perform  
8 poorly in the number of total trouble reports per 1,000 access lines, but it did struggle in  
9 responding to service outages. The most severe type of report, calling for an immediate  
10 response, is an out-of-service report. In this category, US West had a typical volume of  
11 reports—165 per 1,000 lines. However, its average time to repair was 26 hours, which places it  
12 last among these companies. It took US West 5 hours longer than Bell Atlantic, BellSouth or  
13 SBC to repair a line that was out of service, as shown on Page 4 of  
14 Schedule 1.

15 While it can be very distressing when a telephone line is out of service, this problem  
16 only affects a few consumers at any one time. In contrast, the switches which route calls  
17 through the local network are vital to everyone on the network. When a switch fails to function  
18 properly, hundreds or thousands of customers can be inconvenienced. Accordingly, an  
19 important measure of service quality is the percentage of time these switches are not functioning  
20 properly. The ARMIS report contains data on the number of switches that go down, and the  
21 average amount of time a switch stays down. As shown on Page 5 of Schedule 1, in this area  
22 US West's current level of service quality is well below par. Despite the fact that it operates  
23 the second fewest switches (1,446), US West had the most switches with downtime (941) and  
24 by far the highest percentage of switches with downtime (65%). Furthermore, the company  
25 had the most total downtime minutes (11,161) and highest number of downtime minutes per  
26 switch (7.7).

1           The final component of the ARMIS report analyzes customer complaints. Only those  
2           complaints that are severe enough to be filed with state commissions or the FCC are included in  
3           this measure of service quality. If a problem is relatively minor, most customers will just  
4           grumble to themselves, or complain to the carrier, but they won't take the extra time and effort  
5           to contact a regulatory agency. Page 6 of Schedule 1 summarizes the volume of residential and  
6           business customer complaints to state regulatory agencies. This data captures all types of  
7           problems which are severe enough to motivate a customer to complain to regulators—everything  
8           from delayed installations, to lack of dial tone, to billing problems, to noisy phone calls.

9           This data suggests that there is already a serious problem with service quality in the 14-  
10          state US West region. The Company outpaces all of the other ILECs in the absolute number of  
11          business and residential complaints to state agencies, but even more tellingly, it had by far the  
12          highest rate of complaints per 10,000 access lines. US West business customers are motivated  
13          to file complaints with their state commissions at a 364% higher rate than the next worst  
14          performer (Ameritech). The same conclusion applies to residential customers, who file 7.2  
15          complaints per 10,000 access lines, compared to 2.0 complaints for the second worst carrier--  
16          BellAtlantic. In evaluating customer satisfaction or service quality, it is not unreasonable to  
17          evaluate a firm on a "best in class" basis—judging how well or how poorly a specific firm  
18          performs relative to the best performer. In this case, the discrepancy between US West's  
19          complaint rate and that of the best performer—SBC—is truly extreme. In the US West region,  
20          both business and residence consumers are motivated to complain to their state commission at  
21          more than ten times the rate of complaints lodged by consumers in the SBC region.

22  
23   **Q.    You have spoken of existing deficiencies in US West service quality over its 14-state**  
24   **region. Do Arizona customers receive better service than those in the region as a**  
25   **whole?**

26   **A.    No. For each of the categories in the ARMIS report that I outlined above, I computed the**

1 corresponding data for strictly US West's Arizona operations. Service quality measures for the  
2 state were similar to, or lower than, those for US West in nearly every category. More  
3 specifically, in 11 of the 15 categories US West-Arizona performed worse than the region-wide  
4 average. As shown on Pages 1-6 of Schedule 1, Arizona had poorer results in the percent of  
5 installation commitments met (97.8), average time to installation (2.8 days), total trouble reports  
6 per 1,000 access lines (395), and business and residential complaints per 10,000 lines (3.6,  
7 8.3), among others. With the exception of the switching measures and installation and business  
8 office dissatisfaction among residents, Arizona service quality appears to be worse than the  
9 average for the region. Moreover, US West-Arizona falls below the other four ILECs in every  
10 service category except total trouble reports per 1,000 access lines and some of the  
11 dissatisfaction measures.

12  
13 **Q. You've demonstrated that US West's current level of service quality is well below par,  
14 and that Arizona is not exempt from these problems. Is there any indication of a  
15 favorable trend--that the problems are becoming less severe over time?**

16 A. No. One would think that the trend towards increased competition would motivate the major  
17 ILECs, including US West, to improve service quality, in an effort to build customer loyalty.  
18 Unfortunately, the data fails to demonstrate any such favorable trend. To the contrary, the data  
19 seems to indicate that, if anything, service quality has declined somewhat in the past three years.

20 The company states that it "continually strives to provide the highest service quality to  
21 all its customers and will continue to do so." [STF 01-009] This statement of goals contrasts  
22 with the reality that service complaints to the Arizona Corporation Commission have increased  
23 from 2,330 in 1997 to 2,867 in 1998 to 3,524 during the first 11 months of 1999. [STF 02-  
24 065] Further, the percentage of consumer and small business service outages repaired in less  
25 than 24 hours has fallen from 66.7% in 1998 to 61.0% in 1999 year-to-date. The analogous  
26 percentage of repairs made in less than 48 hours also decreased from 85.5% to 83.6%. [STF

1 02-052 Subset No. 25]

2 One additional illustration of these negative trends can be found in a series of graphs  
3 that accompany the 1998 ARMIS report. Since local telephone service is of such vital  
4 importance to our daily lives, if you ask a consumer, they will likely tell you that even one  
5 problem with their local service is one too many. Needless to say, repeated service problems  
6 are especially exasperating. According to the ARMIS data, and Schedule 2, the incidence of  
7 residential and business customers reporting repeat local troubles has increased by  
8 approximately 10% since 1995. In addition, the graphs indicate that from 1997 to 1998, the  
9 average local service repair times, the state complaint rate, and installation times for local  
10 service each worsened from the prior level.

11  
12 **Q. Has the Commission taken any steps in an effort to help ensure that US West provides**  
13 **good quality service to its customers?**

14 **A.** Yes. In an order raising local rates, the Commission required US West to “file a plan within 90  
15 days of the date of this Decision which should be designed to improve quality of service.”  
16 [Decision No. 59147, p. 1, ln. 19-21] The Plan mandated that the company maintain detailed  
17 records of customer complaints and other reports. It also regulated the relationship between  
18 the company and the public and set standards for billing records. Moreover, it included a  
19 general penalty clause. The clause reads as follows,

20  
21 “In addition to the waiving of installation charges, pro rata credits on monthly  
22 bills, free monthly service, payment for alternative service, and 1/3 credit of  
23 applicable tariff rates ... a penalty of not less than one hundred dollars  
24 (\$100.00) nor more than five thousand dollars (\$5,000) per each incident of  
25 violating the standards listed in this tariff may be imposed on the company by  
26 the Commission.” [Plan p. 35-36]

27  
28 The Plan went on to outline standards for time to installation, answer times, the

1 maximum number of trouble reports, call completion, and other factors involved in the provision  
2 of local phone service. By imposing monetary penalties when the company violates the Plan's  
3 enumerated standards, the Commission has demonstrated a commitment to ensuring quality  
4 local service for US West customers in Arizona.

5  
6 **Q. Given the trend towards increased competition, and the Commission's commitment to**  
7 **service quality, why hasn't US West provided better service?**

8 A. First, it must be recognized that there is a vast difference between opening a market to  
9 competition and achieving effective competition. For the time being, US West continues to be  
10 shielded from competitive pressures by the advantages of incumbency and the fact that it is  
11 difficult for new entrants to gain a foothold in the market. As a number of competitors increases,  
12 and some of these firms find ways to convince customers to try an alternative, US West may  
13 eventually succumb to competitive pressures. For the time being however, the quality of  
14 service provided by US West is primarily a function of management's priorities and goals,  
15 rather than a function of market pressures. Regardless of their size, there are limitations on  
16 what corporate organizations can accomplish at any one time. There is every reason to be  
17 concerned that after the merger, management's priorities and goals will shift even farther away  
18 from delivering the highest quality service in the 14 state region that it already dominates.  
19 Instead, management may concentrate on exploiting the opportunities for rapid growth in  
20 markets throughout the rest of the nation and the world.