BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

Joint Application of Qwest Communications International, Inc. and CenturyTel, Inc. for Approval of Indirect Transfer of Control of Qwest Corporation, Qwest Communications Company, LLC, and Qwest LD Corporation	DOCKET NO. 10-049-16

DIRECT TESTIMONY

OF

AUGUST H. ANKUM, PH.D.

ON BEHALF OF

TW TELECOM OF UTAH, LLC; MCLEODUSA TELECOMMUNICATIONS SERVICES, INC. D/B/A PAETEC BUSINESS SERVICES; INTEGRA TELECOM OF UTAH, INC., ELECTRIC LIGHTWAVE, LLC, AND ESCHELON TELECOM OF UTAH, INC.; AND, LEVEL 3 COMMUNICATIONS, LLC

Exhibit Joint CLECs 1

August 30, 2010

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1 # I. PROFESSIONAL QUALIFICATIONS

2 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

3 A. My name is August H. Ankum. My business address is QSI Consulting, 150
4 Cambridge Street, Suite A603, Cambridge, Massachusetts, 02141.

5 **Q. WHAT IS QSI CONSULTING, INC. AND WHAT IS YOUR POSITION**
6 **WITH THE FIRM?**

7 A. QSI Consulting, Inc. ("QSI") is a consulting firm specializing in regulatory and
8 litigation support, economic and financial modeling, and business plan modeling
9 and development. QSI provides consulting services for regulated utilities,
10 competitive providers, government agencies (including public utility
11 commissions, attorneys general and consumer councils) and industry
12 organizations. I am a founding partner and currently serve as Senior Vice
13 President.

14 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND**
15 **WORK EXPERIENCE.**

16 A. I received a Ph.D. in Economics from the University of Texas at Austin in 1992,
17 an M.A. in Economics from the University of Texas at Austin in 1987, and a B.A.
18 in Economics from Quincy College, Illinois, in 1982.

19 My professional background covers work experiences in private industry and at
20 state regulatory agencies. As a consultant, I have worked with large companies,
21 such as AT&T, AT&T Wireless, Bell Canada and MCI WorldCom ("MCIW"), as

1 well as with smaller carriers, including a variety of competitive local exchange
2 carriers ("CLECs") and wireless carriers. I have worked on many of the
3 arbitration proceedings between new entrants and incumbent local exchange
4 carriers ("ILECs"). Specifically, I have been involved in arbitrations between
5 new entrants and NYNEX, Bell Atlantic, USWEST, BellSouth, Ameritech, SBC,
6 GTE and Puerto Rico Telephone. Prior to practicing as a telecommunications
7 consultant, I worked for MCI Telecommunications Corporation ("MCI") as a
8 senior economist. At MCI, I provided expert witness testimony and conducted
9 economic analyses for internal purposes. Before I joined MCI in early 1995, I
10 worked for Teleport Communications Group, Inc. ("TCG"), as a Manager in the
11 Regulatory and External Affairs Division. In this capacity, I testified on behalf of
12 TCG in proceedings concerning local exchange competition issues, such as
13 Ameritech's Customer First proceeding in Illinois. From 1986 until early 1994, I
14 was employed as an economist by the Public Utility Commission of Texas
15 ("PUCT") where I worked on a variety of electric power and telecommunications
16 issues. During my last year at the PUCT, I held the position of chief economist.
17 Prior to joining the PUCT, I taught undergraduate courses in economics as an
18 Assistant Instructor at the University of Texas from 1984 to 1986.

19 A list of proceedings in which I have filed testimony is attached hereto as Exhibit
20 Joint CLECs 1.1.

21 **Q. DO YOU HAVE EXPERIENCE WITH THE ISSUES IN THIS**
22 **PROCEEDING?**

1 A. Yes. I have been involved in telecommunications since 1988, and over the course
2 of my career, I have worked and testified on virtually all issues pertaining to the
3 regulation of incumbent local exchange companies, including those governing
4 their wholesale relationship with dependent competitors, such as competitive local
5 exchange carriers ("CLECs"). I have also worked on numerous proceedings
6 involving competitive and market dominance issues, including those pertaining to
7 the FCC's triennial review cases and merger analyses.

8 **Q. ON WHOSE BEHALF ARE YOU FILING THIS DIRECT TESTIMONY?**

9 A. My testimony is being filed on behalf of the following CLECs: tw telecom of
10 Utah llc; McLeodUSA Telecommunications Services, Inc. d/b/a PAETEC
11 Business Services; Integra Telecom of Utah, Inc., Electric Lightwave, LLC, and
12 Eschelon Telecom of Utah, Inc.; and, Level 3 Communications, LLC.

13 II. PURPOSE AND SUMMARY

14 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

15 A. The purpose of my testimony is to evaluate whether the proposed merger between
16 CenturyLink[1] and Qwest is in the public interest.

17 Having reviewed the companies' Joint Application,[2] supporting testimony and
18 data request responses, I believe it is not. As I will demonstrate, the proposed

[1] I will use CenturyLink (as opposed to CenturyTel) to refer to the company seeking to acquire Qwest, unless referring specifically to the legacy CenturyTel company that existed prior to the merger with Embarq. When referring to both CenturyLink and Qwest in the context of the proposed merger, I will use the term "the Companies."

1 transaction should either be rejected *in total* or in the alternative, approved only if
2 and when the Commission has imposed firm, specific, and enforceable conditions
3 on CenturyLink and Qwest (hereafter "the Joint Applicants" or "the Companies")
4 in order to safeguard the state of competition and wholesale customers.

5 **Q. PLEASE SUMMARIZE YOUR FINDINGS AND RECOMMENDATIONS.**

6 A. As discussed herein, and in the testimony of my colleague Mr. Timothy Gates, the
7 information provided by CenturyLink and Qwest is inadequate to demonstrate
8 that the proposed transaction is in the public interest. Moreover, the information
9 indicates that the proposed transaction would post a serious risk to wholesale
10 customers, such as CLECs, when CenturyLink and Qwest seek to integrate their
11 two companies post-merger. The proposed transaction will potentially jeopardize
12 the viability of CLECs and will likely harm competition in Utah.

13 Specifically, my testimony will discuss the following:

14 • The economic incentives underlying mergers.
15 • A brief overview of past mergers in the telecommunications industry,
16 demonstrating a troublesome history of mergers and the likelihood of
17 failure.
18 • The potential harm and absence of any public benefit from the
19 proposed transaction.
20 • The need for conditions and commitments to prevent or mitigate the
21 risk of harm to competition resulting from the proposed transaction
22 and ensure that the merger is in the public interest.
23 • Some specific conditions and commitments that should be required of
24 CenturyLink and Qwest as prerequisites for approving the merger. (A
25 complete list is provided by Mr. Gates.)

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[2] CenturyTel, Inc. and Qwest Communications International, Inc. Joint Application for Expedited Approval of Indirect Transfer of Control, filed May 19, 2010 ("Joint Application").

1 **Q. DO YOU HAVE SOME PRELIMINARY OBSERVATIONS REGARDING**
2 **THE PROPOSED TRANSACTION?**

3 A. Yes. Mergers are often seen as a means of expeditiously growing a company, not
4 organically (through competitive success and customer acquisitions with superior
5 product offerings), but by means of a short cut: by buying another company and
6 its products and customers. While proposed mergers are invariably touted by the
7 merging companies as generating significant benefits, through potential synergies,
8 increased economies of scale and scope, etc., in practice, it is very difficult to
9 predict which mergers will be successful and which ones will not. An interesting,
10 in retrospect ironic, example of supposed experts misjudging mergers is found in
11 an issue of the *Harvard Business Review* dedicated to mergers and acquisitions,
12 which published the minutes of a roundtable discussion on the resurgence of
13 mergers and acquisitions in the late nineties as follows:[3]

14 **Moderator:** The announcement in January of the merger between
15 ***America Online*** and ***Time Warner*** marked the convergence of the two
16 most important business trends of the last five years: the rise of the
17 internet and the resurgence of mergers and acquisitions. […]
18
19 **Moderator:** I'm sure some of you are familiar with the studies
20 suggesting that most mergers and acquisitions do not pan out as well
21 as expected. Has that been your experience…Are mergers and
22 acquisitions worth it?
23
24 **Participant:** I would take issue with the idea that most mergers end up
25 being failures. I know there are studies from the 1970's and '80's that
26 will tell you that. But when I look at many companies today – in
27 particular new economy companies like ***Cisco*** and ***WorldCom*** – I have
28 a hard time dismissing the strategic power of M&A.

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[3] Dennis Carey, "Lessons from Master Acquirers: A CEO Roundtable on Making Mergers Succeed," *Harvard Business Review on Mergers and Acquisitions*, 2001, at pp. 2-3.

1 Rather than illustrate the success of mergers, the examples cited in this discussion
2 show the opposite. Of the three companies mentioned (AOL/Time Warner,
3 Cisco, and WorldCom), two were brought down by failed mergers, while the
4 third, Cisco, is still prospering after its mergers, putting the failure rate of mergers
5 at two out of three, which is about where the academic literature puts it.[4]

6 **Q. ARE YOU SAYING THAT MERGERS ARE UNDESIRABLE?**

7 A. No. Mergers and acquisitions may spawn innovative and profitable companies.
8 At issue in this case, however, is the merit of the *instant transaction,* and an
9 examination of past mergers and their failures (discussed below) should alert the
10 Commission to various pitfalls of mergers and underscore the importance of
11 carefully examining the impact of the proposed merger on all affected parties,
12 including competitive carriers and their end-user customers. As discussed below,
13 this merger raises serious public interest concerns that need to be weighed
14 carefully against the backdrop of general merger risks and past merger failures.

15 **Q. DO MERGERS OF ILECS RAISE UNIQUE ISSUES, NOT NECESSARILY**
16 **RELEVANT TO MERGERS BETWEEN OTHER TYPES OF**
17 **COMPANIES?**

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[4] This observation is found in many publications. See for example: Richard Dobbs, Marc Goedhart, and Hannu Suonio, "Are Companies Getting Better at Mergers and Acquisitions," *McKinsey Quarterly*, December 2006, at p. 1: "McKinsey research shows that as many as two-thirds of all transactions failed to create value for the acquirers"; Cartwright, Sue and Cooper, Cary, *Managing Mergers, Acquisitions & Strategic Alliances*, Butterworth-Heinemann, reprinted 2001, Section 3, Mergers and Acquisition Performance – a Disappointing History, discusses a number of studies, in line with the McKinsey studies; Pritchett, Price, After the Merger, *The Authoritative Guide for Integration Success*, McGraw-Hill, 1997, Chapter 1, Section Statistics on Merger Success and Failure, sets the failure rate at between 50% and 60%.

1 A. Yes. A merger involving a large ILEC such as Qwest touches on many public
2 interest issues, particularly the public's interest in local exchange competition. To
3 appreciate the public interest stake in this merger, it is important to recall the
4 starting points of the ILECs' network investments.

5 Until the early 1990s, ILECs had a government-sanctioned monopoly to provide
6 local services to captive ratepayers. In exchange, ILECs operated in a rate-
7 regulated environment. Rate regulation meant that if an ILEC had increased
8 operating costs, or was required to invest new capital to build out local
9 infrastructure (*e.g.*, middle-mile or last-mile loop facilities), the ILEC had the
10 ability to pass along those increased capital or operating costs by securing a rate
11 increase from the state regulators. Those regulated rates provided for a rate of
12 return that the ILEC was permitted to earn. Of course, ILECs often earned more
13 than their authorized rate of return, and sometimes they earned less (which meant
14 the ILEC was entitled to pursue higher rates). Not only was the ILEC able to
15 secure rate increases when it proved its case to regulators, its monopoly status
16 then assured it that every business and residential customer in its local exchange
17 market would pay those regulated rates to obtain local service. Some states
18 provided an alternative form of regulation, but the bottom line was that the ILEC
19 had certainty that its Commission-approved rates would be paid by all its
20 customers subscribing to local services. Thus, a material portion of the ILEC
21 infrastructure in place today, especially the local loop infrastructure, was built
22 when the ILEC was guaranteed that the cost of its investment would be paid for
23 by captive customers through regulated rates that included an appropriate rate of

1 return. That monopoly environment with its guarantees of an adequate rate of
2 return is in stark contrast to the current competitive environment in which CLECs
3 must compete for every customer. The Telecommunications Act of 1996 resulted
4 in CLEC entry into local exchange markets under provisions allowing them to use
5 portions of the ILECs' networks and services, generally at TELRIC rates. This
6 mandate allowing CLEC access to ILEC networks has created competition where
7 none existed prior to 1996. However, a merger, such as the one proposed in the
8 instant proceeding, could upset the wholesale relationship between ILEC and
9 CLECs, and harm competition in Utah. Without reasonable, reliable and
10 nondiscriminatory access to Qwest's and CenturyLink's networks, CLECs cannot
11 get access to customers. As a result, an ILEC merger like the one between
12 CenturyLink and Qwest in this case has unique and profound public interest
13 implications not present in mergers in other industries or between two CLECs.

14 **Q. DO CLECS DIFFER FROM OTHER AT-RISK STAKEHOLDERS IN THE**
15 **PROPOSED MERGER?**

16 A. Yes. An examination of past telecom mergers teaches us that the risks and gains
17 of a merger are not evenly distributed among all stakeholders.

18 CenturyLink's and Qwest's shareholders, for example, can sell their shares if they
19 anticipate that things will go awry, or, alternatively, hold on to their shares to reap
20 whatever benefits they may anticipate: it is a risk-return tradeoff each shareholder
21 is free to either assume or walk away from. However, this freedom of choice
22 does not exist for other, captive stakeholders. Specifically, retail customers in

1 captive segments of retail markets have little or no choice and neither do
2 wholesale customers, such as CLECs, who critically depend on CenturyLink and
3 Qwest for loops, transport, collocation and a variety of other wholesale network
4 inputs. That is, captive retail and wholesale customers will not only reap *no gains*
5 if the proposed transaction is successful, they may experience great harm when
6 things go awry (as they have in so many of these ventures). This asymmetry in
7 the risk-return profiles between various stakeholders is profound. Hence, the
8 need for a regulatory review process to determine whether the proposed
9 transaction is in the interest of *all* stakeholders.

10 **Q. IS THERE A DIVERGENCE BETWEEN A PUBLIC INTEREST**
11 **ANALYSIS AND THE PRIVATE RISK-RETURN ANALYSIS GUIDING**
12 **CENTURYLINK AND QWEST?**

13 A. Yes. CenturyLink and Qwest need only consider their private risk-return trade-
14 offs. In contrast, the Commission must consider the broader public interest,
15 including the transaction's potential impact on other stakeholders who will likely
16 not benefit from the proposed transaction, but may be harmed. Naturally, this is a
17 broader analysis, and less likely to result in a finding that the proposed transaction
18 should be permitted to move forward as proposed.

19 **Q. ARE THERE ASPECTS TO THIS MERGER THAT ARE**
20 **PARTICULARLY TROUBLING?**

21 A. Yes. I have already noted that most mergers are not successful, even as measured
22 by the ultimate impact of the merger on shareholders. Yet more troubling in this

1 case is the fact that CenturyTel is seeking to acquire a much larger Bell Operating
2 Company ("BOC") while it is still integrating the recently acquired Embarq, a
3 company that was already about four times larger than the original CenturyTel. If
4 the successful outcome of mergers is generally in question, the outcome of this
5 one is particularly so.

6 What comes to mind is the experience of WorldCom, a one-time darling of Wall
7 Street that in rapid succession acquired a number of firms of increasing size and
8 complexity, culminating in the fateful acquisition of MCI and ultimately the
9 financial collapse of WorldCom. While WorldCom was brought down by a
10 number of missteps, some of them criminal, it is fair to say that its demise
11 stemmed in significant part from the failure to successfully integrate the various
12 acquired companies and the escalating challenges of ever-larger acquisitions.
13 CenturyTel's proposed acquisition of Qwest on the heels of its recent acquisition
14 of Embarq presents some disturbing similarities to the experience of WorldCom
15 and other failed acquisitions.

16 The table below gives the approximate line counts of CenturyTel (as it existed
17 before its Embarq acquisition), Embarq and Qwest, and demonstrates explosive
18 growth.

19

1

	Year	Access Lines[5]	% of Post-Merger Total
CenturyTel	2009	1,300,000	8%
Embarq	2009	5,700,000	34%
Qwest	2010	10,000,000	59%
Total		**17,000,000**	**100%**

2

3 This exponential growth path raises questions, specifically about the ability of
4 CenturyLink's management to handle the challenges of post-merger integration.
5 Again, organic growth through customer acquisition, as a result of superior
6 product offerings, is different from growth through mergers and acquisitions.
7 With respect to organic growth, management proves its abilities to manage
8 growth on an ongoing basis and exponential growth is a sign that management is
9 doing things right. By contrast, growth by means of acquisitions may signify that
10 management is able to maneuver nimbly in financial markets, but little, if
11 anything, about management's ability to run a much larger organization. It is the
12 latter, however, that the Commission is tasked, among other issues, to evaluate.

13 Further, while CenturyLink may have integrated smaller firms, the company's
14 current attempt to swallow a BOC should give regulators pause. To be sure, the
15 challenge of integrating and running Qwest, with its unique BOC obligations,
16 comparatively enormous customer base, substantial wholesale responsibilities,
17 and complex set of operational support systems, is particularly daunting and far

[5] Line counts are taken from CenturyLink's testimony. The line counts in CenturyLink's testimony appear to be approximate line counts. See Direct Testimony of Jeremy Ferkin, May 27, 2010 ("Ferkin Utah Direct"), at p. 16 and Exhibit JF-1; and Direct Testimony of Jeff Glover, May 27, 2010 ("Glover Utah Direct"), at p. 4.

1 beyond anything CenturyLink has faced to date. Whatever may be CenturyLink's
2 proven track record, integrating and managing a BOC is not a part of it.[6]

3 **Q. DOES THE FACT THAT SBC AND VERIZON WERE ABLE TO**
4 **ACQUIRE AND INTEGRATE FELLOW BOCS SUGGEST THAT**
5 **CENTURYLINK WILL BE ABLE TO DO THE SAME WITH QWEST?**

6 A. No. First, SBC and Verizon were large BOCs themselves. Given their common
7 genealogy as Baby Bells, SBC's and Verizon's management knew what they were
8 acquiring and how to run a BOC, with all the attendant regulations and
9 obligations to which it is subject. Further, the BOCs still had a common corporate
10 culture and were mostly working with common engineering practices inherited
11 from Ma Bell. Also, when, for example, SBC acquired Ameritech, SBC was
12 larger than Ameritech – not, as is the case here, smaller by a factor of 10 (using
13 CenturyTel as the base). Nevertheless, regulators imposed substantial conditions
14 as prerequisites to approving those BOC mergers in spite of the advantages
15 inherent in mergers between BOCs as compared to a non-BOC's acquisition of a
16 BOC such as Qwest.

---

[6] Also, as has been suggested in the literature, the integration process is always different. As Cooper and Cartwright note: "Different acquisitions are likely to result in quite different cultural dynamics and potential organizational outcomes. Consequently, acquiring management cannot assume that because they were successful in assimilating one acquisition into their own culture, that same culture and approach to integration will work equally successfully with another acquisition." Garry L. Cooper and Sue Cartwright, *Managing Mergers, Acquisitions & Strategic Alliances*, Butterworth-Heinemann, 2nd Edition, reprinted 2001, at p. 25.

1 **Q. WHY SHOULD THE COMMISSION BE PARTICULARLY CONCERNED**
2 **ABOUT POTENTIAL ADVERSE IMPACTS ON CLECS AND THEIR**
3 **END USERS?**

4 A. Because CLECs depend on Qwest and CenturyLink for interconnection and
5 critical wholesale network inputs that are essential to their ability to provide
6 competitive local exchange services. CLECs are generally captive customers of
7 Qwest and CenturyLink for these wholesale network inputs. Further, CLECs
8 compete with CenturyLink and Qwest for business and residential customers,
9 which creates a perverse incentive structure in which CenturyLink and Qwest
10 may have disincentives to provide CLECs with quality, reasonably priced,
11 nondiscriminatory wholesale services and network access. In light of this, and the
12 fact that the economic health of CLECs is critical to local exchange competition,
13 it is important for the Commission to ensure that CLECs' interests are considered
14 and protected.

15 **Q. WHAT IS YOUR RECOMMENDATION?**

16 A. I recommend that the Commission reject the proposed transaction. As discussed
17 herein and in the testimony of Mr. Gates, this proposed transaction poses serious
18 risks to the public interest, including the public's interest in robust competition
19 from the many wholesale CLEC customers of Qwest and CenturyLink.
20 However, if the Commission nevertheless decides to approve the transaction, then
21 it should recognize the potential hazards faced by captive CLECs and their end
22 user customers, and impose on CenturyLink and Qwest a set of stringent

1 conditions and commitments, discussed herein and by Mr. Gates, in order to
2 safeguard wholesale customers and competition.

3 III. STANDARD FOR REVIEW

4 **Q. WHAT IS THE APPROPRIATE STANDARD FOR THE COMMISSION**
5 **TO USE IN REVIEWING CENTURYLINK'S AND QWEST'S PROPOSED**
6 **REORGANIZATION?**

7 A. I am not a lawyer, but I have reviewed the Commission's orders approving public
8 utility merger and transfer of control transactions over the past decade, in order to
9 understand the standard of review the Commission has applied in similar cases.
10 The most relevant case appears to be the Commission's approval, with conditions,
11 of the Qwest-US West merger in June 2000.[7] While the Commission has
12 approved several telecommunications mergers and transfers of control since that
13 time, for both large and small companies, for the most part they have involved
14 CLEC operations and have been informally adjudicated pursuant to Utah Admin.
15 R746-349-7 (Informal Adjudication of Certain CLEC Merger and Acquisition
16 Transactions) or Rule 746-110-1 (Requests – allowing for informal adjudication
17 when the Commission determines that the matter can reasonably be expected to
18 be unopposed and uncontested).[8]

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[7] *In the Matter of the Merger of the Parent Corporations of Qwest Communications Corporation, LCI International Telecom Corp. and US West Communications, Inc.*, Docket No. 99-049-41 Report and Order, June 9, 2000 ("Qwest-US West Merger Order"), at p. 11.

[8] See, *e.g.*., *In the Matter of the Joint Application of Broadweave Networks, Inc. and Veracity Communications, Inc. for Approval of a Transaction to Combine the Companies in Veracity Networks, LLC*, Docket Nos. 09-2410-01/09-2461-01, Order Approving Merger (Final

1 In the *Qwest-US West Merger Order*, the Commission made the following
2 determinations concerning how to apply the legal standard for review:

> 3 In reviewing the proposed merger, the Commission must determine if
> 4 it is in the public interest. Utah Code Ann. §§ 54-4-28, 54-4-29 and
> 5 54-4-30. In the context of mergers involving monopoly electric
> 6 providers, ***we have interpreted the public interest standard to require***
> 7 ***that the applicants show that the transaction provides a net positive***
> 8 ***benefit to the public***. [Citations omitted]
>
> 9 In the recent ScottishPower/PacifiCorp Merger Order, we quoted
> 10 language from the Utah Power & Light PacifiCorp Merger Order on
> 11 the application of this standard: "Our task is to consider them all
> 12 [positive benefits and negative impacts], giving each its proper weight,
> 13 and determine whether on balance the merger is beneficial or
> 14 detrimental to the public." *ScottishPower/PacifiCorp Merger Order* at
> 15 27. Most of the parties in this Docket have urged the Commission to
> 16 apply that standard here.
>
> 17 Joint Applicants cite Commission orders in eight telecommunications
> 18 proceedings involving mergers, acquisitions or reorganizations since
> 19 the passage of the Utah Telecommunications Reform Act, L. Utah
> 20 1995, ch. 269, and the federal Telecommunications Act of 1996, P.L.
> 21 104, 110 Stat. 57 (1996), in support of their argument that the net
> 22 positive benefit standard does not apply in the new
> 23 telecommunications environment. Joint Applicants note that the
> 24 Commission found the public interest satisfied by a showing that a
> 25 transaction would result in a more effective competitor and increased
> 26 competition, would not cause harm to the public or customers, and
> 27 would not change the manner in which service was provided to the
> 28 public. Joint Applicants point out that none of these orders mentions a
> 29 net positive benefit standard.
>
> 30 Earlier in this proceeding, the Commission explained that this matter is
> 31 different from the telecommunications transactions covered by the
> 32 orders cited by Joint Applicants. Although some of those matters
> 33 involved very large telecommunications companies, none of them had

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Order), November 18, 2009; *In the Matter of the Joint Application of DIECA Communications, Inc., d/b/a Covad Communications Company, and CCGI Holding Corporation for Approval of an Indirect Transfer of Control of DIECA Communications, Inc., d/b/a Covad Communications Company, to CCGI Holding Corporation*, Docket No. 07-2277-01, Order Approving Transfer of Control, February 20, 2008; and *In the Matter of the Joint Application of AT&T Inc. and BellSouth Corporation for Approval of Agreement and Plan of Merger*, Docket No. 06-087-02, Order Approving Merger, May 16, 2006.

> the local service presence of US West in this state. In fact many of them had no local exchange customers at all. They were potential competitors.
>
> The present case is clearly different from the cases cited by the applicants. In addition, unlike US West, none of the companies in the cited cases served customers who were "captive", i.e., customers who have no competitive alternatives.
>
> ***The Commission finds that in order for this merger to be in the public interest there must be a definable net benefit. We will continue to apply the net benefit standard in this Docket***.[9]

Given that the instant case again involves "the local service presence of US West [now Qwest] in this state" and customers with few or no competitive alternatives (including CLECs dependent upon Qwest's wholesale services), my understanding is that the Commission will follow those determinations and adopt a standard for approving the Companies' proposed transaction that will require the Joint Applicants to show that the transaction provides a definable net benefit to the public.

In order to find that ILEC mergers are in the public interest, state commissions frequently impose conditions that minimize threats of harm to the public interest,[10] including threats to competition.[11] Even so, from an economic

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[9] *Qwest-US West Merger Order*, at p. 11 (citations omitted, emphasis added).

[10] See, *e.g.*, *In the Matter of the Merger of the Parent Corporations of Qwest Communications Corporation, LCI International Telecom Corp., USLD Communications, Inc., Phoenix Network, Inc. and US West Communications, Inc.,* Minnesota PUC Docket No. P-3009, 3052, 5096, 421, 3017/PA-99-1192 (*"MN PUC U S West/Qwest Merger Docket"*), Order Accepting Settlement Agreement and Approving Merger Subject to Conditions (June 28, 2000)("Order Accepting Settlement"), at p. 5.

[11] *In the Matter of Verizon Communications Inc. and Frontier Communications Corporation,* Oregon PUC Docket UM 1431, Order No. 10-067, February 24, 2010 ("*Oregon PUC Frontier-Verizon Order")*, at p. 6.

1 perspective, these types of conditions are not only appropriate, but also they are
2 required to satisfy the public interest standard.

3 **Q. CAN YOU GIVE AN EXAMPLE OF THE TYPES OF CONDITIONS**
4 **THAT STATE COMMISSIONS HAVE ADOPTED TO HELP ENSURE**
5 **THAT A PROPOSED ILEC MERGER OR ACQUISITION WILL**
6 **SATISFY THE PUBLIC INTEREST STANDARD?**

7 A. Yes. For example, in the *Oregon PUC Frontier-Verizon Order*, the Public Utility
8 Commission of Oregon ("Oregon PUC") imposed several additional conditions in
9 order to "mitigate the risks of the transaction and help meet the 'no harm' public
10 interest standard ***required*** for our approval."[12]

11 One condition was that Frontier commit to spending a total of $25 million for
12 broadband deployment and enhancement over the following three years.[13] The
13 Oregon PUC properly imposed broadband conditions in the merger context in
14 order to address concerns that Frontier would otherwise insufficiently fund and
15 manage its provision of broadband services after the merger, leaving the public
16 with less access to broadband services than if Frontier and Verizon remained
17 separate entities.[14] The Oregon PUC's order also included conditions relating to
18 FiOS video services "provided pursuant to local franchise agreements, rather than
19 pursuant to Oregon PUC authority," stating that the "conditions help meet the

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[12] *Oregon PUC Frontier-Verizon Order*, at p. 1 (emphasis added).

[13] *Id.*, at pp. 1, 15-16, and Ex. B. pp. 9-11 (also listing requirements for periodic reports to the Commission, detailing in which wire centers the merged entities would deploy broadband services, and listing specific commitments to particular wire centers).

[14] *Oregon PUC Frontier-Verizon Order*, at p. 15.

1 required standard for approval of the transaction.[15] Accordingly, without offering
2 a legal opinion, it appears to me that the statutorily required public interest
3 standard contemplates that the Commission may use its authority to impose a
4 broad range of merger conditions to protect the public interest in a vibrant state
5 telecommunications environment. That is why, in the *Oregon PUC Frontier-*
6 *Verizon Order*, the Oregon PUC imposed its broadband conditions upon finding
7 that they "help meet the 'no harm' standard for approval of the transaction."[16]
8 Similarly, other states have adopted broadband related conditions when approving
9 telecommunications utility mergers under a public interest standard.[17]

10 **Q. ARE THERE OTHER STANDARDS TO CONSIDER IN REVIEWING**
11 **THE JOINT APPLICATION?**

12 A. Yes. The mandates of the Telecommunications Act of 1996 are also critical in
13 reviewing the proposed merger. Nevertheless, CenturyLink's Application makes
14 only a vague reference to "…the laws governing interconnection."[18] The

[15] *Id.* at p. 17.

[16] *Id.* at p. 16.

[17] See, *e.g.*, Maine PUC's approval of the FairPoint-Verizon transaction, *In the Matter of Verizon New England Inc., Northern New England Telephone Operations Inc., Enhanced Communications Of Northern New England Inc., Northland Telephone Company Of Maine, Inc., Sidney Telephone Company, Standish Telephone Company, China Telephone Company, Maine Telephone Company, And Community Service Telephone Co., Re: Joint Application for Approvals Related to Verizon's Transfer of Property and Customer Relations to Company to be Merged with and into FairPoint Communications, Inc.*, Maine PUC Docket No. 2007-67, and *In the Matter of PUC Investigation into Verizon Maine's Alternative Form of Regulation*, Docket No. 2005-155, Order, February 1, 2008, at p. 9 ("To grant approval pursuant to Section 1101, the Commission must find the sale to be in the public interest.") and p. 17 ("As part of the Amended Stipulation, FairPoint has committed to expanding DSL availability to reach 82% addressability of Maine access lines within two years of closing and 90% addressability in five years (possibly six), which represents a significant benefit to Maine consumers.").

[18] See, Joint Application at p. 13.

1 Application and testimony provide no analysis of the Act's requirements or how
2 they will be met under the proposed merger.[19] This lack of information and
3 commitment is a common theme in all of CenturyLink's and Qwest's applications
4 and testimony I have reviewed in the various states in which the Companies are
5 applying for regulatory approval, and should be a source of great concern for the
6 Commission.

7 IV. ECONOMICS AND REVIEW OF TELECOM 8 MERGERS

9 *A. Mergers Seek to Increase Private Shareholder Value which* 10 *May Cause Them to Be at Odds with the Public Interest*

11 **Q. IN GENERAL TERMS, WHAT MAY CAUSE FIRMS TO MERGE OR**
12 **ACQUIRE OTHER FIRMS?**

13 A. The incentives for mergers and acquisitions are manifold but center around the
14 notion that shareholder value can potentially be increased by merging and
15 streamlining the resources of the pre-merger firms. The benefits from the merger
16 may stem from: the ability to lower costs, through increasing the post-merger
17 firm's economies of scale (*e.g.*, allowing it to achieve lower per unit costs) and
18 scope (*e.g.*, increasing the firm's efficiency by being able to offer a broader array
19 of services at larger volumes); capturing synergies associated with merging and
20 streamlining overhead and operational support systems; and/or improving the
21 Merged Company's overall competitiveness and market share by broadening its

[19] See, for example, Ferkin Utah Direct at pp. 5-6 and p. 12.

1 product offerings and access to a larger customer base, or otherwise from
2 capitalizing on joint talents and expertise. The notion is that bigger is better.

3 Of course, these are all stock, theoretical considerations raised in mergers, but it is
4 always a question whether or not these benefits will actually materialize.
5 Furthermore, even on a theoretical level, there are serious doubts about whether
6 such alleged benefits are likely to result from a merger between firms such as
7 those in this transaction, or whether benefits could more likely be achieved by the
8 firms individually, through contractual agreements or simply through endogenous
9 growth.[20]

10 **Q. WHAT IS THE DIFFERENCE BETWEEN A HORIZONTAL AND A**
11 **VERTICAL MERGER?**

12 A. A horizontal merger is a merger between two firms that offer a comparable set of
13 services in comparable segments of a market or industry. The objective of a
14 horizontal merger is typically to broaden the reach of the firm and to increase its
15 overall market share.

16 A vertical merger, by contrast, seeks to integrate the operations of an upstream
17 firm with those of a downstream firm to whom it provides, typically, critical
18 inputs. Vertical integration may be motivated, for example, by a desire to leverage
19 the market power the upstream firm has into downstream markets.

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[20] For example, see Joseph Farrell and Carl Shapiro, "Scale Economies and Synergies in Horizontal Mergers," *Antitrust Law Journal*, Vol. 68, pages 67 – 710.

1 While these types of mergers differ conceptually, they both allow the acquiring
2 firm to grow and potentially capture certain economies and synergies in addition
3 to other potential benefits.

4 **Q. WHAT SHOULD BE THE ULTIMATE OBJECTIVE OF A MERGER**
5 **FROM THE *COMPANY'S* PERSPECTIVE?**

6 A. While a merger may be motivated by a variety of considerations and objectives,
7 including management's personal ambitions, the ultimate objective of a merger
8 from the perspective of the firms' management should be to increase shareholder
9 value – which is also how the management should evaluate its success or
10 failure.[21]

11 **Q. DO MANAGEMENT'S OBJECTIVES TO INCREASE SHAREHOLDER**
12 **VALUE POTENTIALLY CONFLICT WITH THE COMMISSION'S**
13 **OBJECTIVE TO PROTECT THE PUBLIC INTEREST AND FURTHER**
14 **COMPETITION IN UTAH?**

15 A. Yes. Even if we ignore for the moment the possibility that this merger, like many
16 others, may go awry, an ILEC's pursuit of profit and increased shareholder value
17 through the acquisition of another ILEC inherently conflicts in many ways with
18 the Commission's mandate to promote the public interest and competition. For
19 example, the public interest is best served by a vibrant and competitive market for

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[21] While mergers are at times motivated by other considerations, such as strategic or personal ambitions of the CEO, ultimately, from the firm's perspective, the "numbers" have to work to increase shareholder value. See, for example, Robert G. Eccles, Kersten L. Lanes, and Thomas C. Wilson, "Are You Paying Too Much for that Acquisition," *Harvard Business Review on Mergers and Acquisitions*, 2001, pages 45 - 73.

1 telecommunications services; yet it is in the Companies' interests to strengthen
2 their already dominant market positions in order to realize benefits that justify the
3 merger. Given that CLECs rely on CenturyLink's and Qwest's wholesale
4 services to compete with the Companies, private and public interests diverge. This
5 is why, among other reasons, mergers between ILECs, such as CenturyLink and
6 Qwest, should raise serious concerns about the companies' responsibilities in
7 wholesale markets and the continued viability of retail competition. Specific
8 concerns about how this merger may harm the public interest are discussed in a
9 separate section below.

10 **Q. DO THE FEDERAL TRADE COMMISSION (FTC) AND DEPARTMENT**
11 **OF JUSTICE (DOJ) REVISED HORIZONTAL MERGER GUIDELINES**
12 **(2010) (*HMG*) PROVIDE THE COMMISSION WITH GUIDANCE?**

13 A. Yes. While the focus of an FTC or DOJ antitrust review of the proposed merger
14 differs from and is narrower than the Commission's public interest evaluation, the
15 HMG provides useful guidance on how to assess various claims put forth by the
16 merging companies regarding the alleged benefits of the proposed transaction.
17 Specifically, the HMG stresses that "most merger analysis is necessarily
18 predictive, requiring an assessment of what will likely happen if a merger
19 proceeds as compared to what will likely happen if it does not."[22] The HMG then
20 goes on to note that, in a merger analysis, there is no single uniform formula to be
21 applied, but "rather, it is a fact-specific process through which the agencies,

[22] FTC and DOJ, *Horizontal Merger Guidelines* For Public Comment, Released on April 20, 2010, at p. 1.

1 guided by their extensive experience, apply a range of analytical tools to the
2 reasonably available and reliable evidence [...]"[23] These observations are
3 important because, as discussed in the testimony of Mr. Gates and herein, the
4 applicants have provided insufficient information to conduct a "fact-specific"
5 investigation of the likely outcome of the proposed merger. (As part of the
6 framework for the Commission's predictive analysis, I discuss below a number of
7 previous mergers that subsequently went awry and show that past applicants made
8 claims similar to those made by Qwest and CenturyLink, demonstrating that the
9 mere promise of benefits in no way ensures that benefits will in fact ensue.) For
10 their part, the Companies' near-total absence of factual analysis is disconcerting,
11 given the far reaching implications of the proposed transaction and its potential
12 impact on a broad array of stakeholders, including CLECs, and the fact that the
13 Commission must ultimately make its public interest judgment based on hard
14 facts provided by the applicants.

15 **Q. WOULD THE APPROVAL OF CENTURYLINK'S AND QWEST'S**
16 **SHAREHOLDERS SIGNIFY THAT THE MERGER IS IN THE PUBLIC**
17 **INTEREST?**

18 A. No. Shareholders should consider only how shareholder value will be affected,
19 which revolves mostly around the question of whether it will increase future
20 earnings; obviously, shareholder value is but one component of a much broader
21 and more complex evaluation necessary for a public interest finding. In short, the

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[23] *Id.*

1 Commission should not succumb to the belief that the "invisible hand" of the
2 market place will safeguard the public interest in this merger.

3 ### *B. A Cautionary Tale: Brief Review of Mergers that Went Awry*

4 **Q. CAN ANYTHING BE LEARNED BY CONSIDERING THE OUTCOMES**
5 **OF OTHER RECENT MERGERS AND ACQUISITIONS INVOLVING**
6 **ILEC OPERATIONS?**

7 A. Yes. The old adage that "those who do not heed the lessons of history are
8 doomed to repeat them" readily applies to regulatory review of ILEC mergers and
9 acquisitions. I believe it is crucial that the Commission consider the proposed
10 Qwest-CenturyLink transaction in light of other, recent mergers and acquisitions.
11 As I shall explain, there are several such cases in which the merging companies'
12 initial high expectations and promised public benefits failed to materialize, in
13 some cases instead leading to financial failure, including Chapter 11 bankruptcies.

14 **Q. WHAT ARE POSSIBLY THE TWO MOST PROMINENT MERGERS**
15 **AMONG TELECOMMUNICATIONS COMPANIES TO RESULT IN**
16 **FAILURES?**

17 A. There are two mergers that stand out: the acquisition of MCI by WorldCom in
18 1998 and the acquisition of US WEST, a BOC, by Qwest in 2000.

19 **Q. WHAT HAPPENED IN THE WORLDCOM-MCI MERGER AND WHAT**
20 **WENT WRONG?**

1 WorldCom, which had its genesis in LDDS, experienced precipitous growth in
2 the 1990s, fueled largely by a series of acquisitions,[24] culminating in the $37
3 billion acquisition of MCI in 1998. Following the acquisition, the company had
4 to file for Chapter 11 bankruptcy protection in 2002, after having destroyed much
5 of the shareholder value of both WorldCom and MCI. While the reasons for
6 WorldCom's collapse are many, it can be explained in part by the failure to
7 successfully integrate the operations of the acquired companies. As the
8 Bankruptcy Court found:

> 9 Another challenge for WorldCom involved its integration of acquired
> 10 assets, operations and related customer services. Rapid acquisitions
> 11 can frustrate or stall integration efforts. Public reports, and our
> 12 discussions with WorldCom employees, raise significant questions
> 13 regarding the extent to which WorldCom effectively integrated
> 14 acquired businesses and operations.[25]

15 **Q. WHAT HAPPENED IN THE US WEST-QWEST MERGER AND WHAT**
16 **WENT WRONG?**

17 Qwest was founded in 1996 as a largely fiber-based company, installing facilities
18 along lines of the Southern Pacific Railroad to offer mostly high-speed data
19 services. Like WorldCom, Qwest Communications grew aggressively through a
20 series of acquisitions,[26] positioning Qwest not only as a provider of high speed

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[24] Among the companies acquired were: Advanced Communications Corp. (1992), Metromedia Communication Corp. (1993), Resurgens Communications Group (1993), IDB Communications Group, Inc (1994), Williams Technology Group, Inc. (1995), and MFS Communications Company (1996).

[25] *Re: WORLDCOM, INC., et al. Debtors*, Chapter 11 Case No. 02-15533 (AJG) Jointly Administered, First Interim Report of Dick Thornburgh, Bankruptcy Court Examiner, November 4, at p. 12.

[26] Qwest acquired such companies as Internet service provider SuperNet in 1997, LCI, a long distance carrier in 1998, and Icon CMT, a web hosting provider, also in 1998.

1 data to corporate customers, but also as a rapidly-growing provider of residential
2 and business long distance services.

3 In 2000, Qwest acquired US WEST. The total value of the transaction at the time
4 was considered approximately $40 billion.[27] About ten years after the merger,
5 Qwest's market capitalization is now approximately $10 billion.[28] This represents
6 a stunning loss in shareholder value.[29]

7 **Q. WHAT LESSIONS CAN BE LEARNED FROM THESE TWO MERGERS**
8 **IN EVALUATING THE MERGER AT ISSUE IN THIS CASE?**

9 The lesson to be learned from the WorldCom/MCI and Qwest/US WEST mergers
10 is, among others, that an applicant's ability to put together a merger, get Wall
11 Street's approval and shepherd a proposed transaction through the various steps of
12 an approval process in no way demonstrates an ability to successfully run the
13 post-merger firm. Further, generic claims of "synergies," which, as I will discuss
14 in more detail later in my testimony, invariably accompany all merger proposals,
15 mean little or nothing unless they are adequately substantiated by fact-based
16 analyses – and in the instant Application they surely are not.

17 **Q. ARE THERE MORE RECENT ILEC MERGERS THAT THE**
18 **COMMISSION SHOULD PAY PARTICULAR ATTENTION TO WHEN**
19 **CONSIDERING THE CENTURYLINK-QWEST APPLICATION?**

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[27] Qwest 2000 Annual Report, at p. 1.

[28] See Money.cnn.com, Ticker Q.

[29] In 2000, Qwest boasted: "Qwest Communications Reports Strong Third Quarter 2000 Financial Results While Successfully Integrating ***$77 Billion*** Company." (Emphasis added.) See http://news.qwest.com/index.php?s=43&item=1571

1 A. Yes. There are three major ILEC transactions within the past five years that I
2 think offer particularly sobering lessons to the Commission as it considers
3 CenturyLink's proposed acquisition of Qwest. In particular, I am referring to:

4-6
- **Hawaiian Telcom:** The Carlyle Group's acquisition of Verizon Hawaii (renamed Hawaiian Telcom), followed by Hawaiian Telcom's filing for Chapter 11 bankruptcy protection in 2008;

7-9
- **FairPoint:** FairPoint's acquisition of Verizon's operations in northern New England (Maine, New Hampshire, and Vermont), followed by FairPoint's Chapter 11 bankruptcy filing in October 2009; and

10-13
- **Frontier:** Frontier Communication's July 2010 acquisition of approximately 4.8 million access lines from Verizon in rural portions of fourteen states, which is giving rise to cut-over problems with back-office and OSS systems reminiscent of the prior two transactions.[30]

14 As I will demonstrate, the track record of these types of mergers is not good. (Mr.
15 Gates discusses a different set of problems associated with these mergers.)

16 **Q. HAVE YOU PREPARED AN EXHIBIT THAT SUMMARIZES THE**
17 **PROMISED BENEFITS AND ACTUAL OUTCOMES OF THESE ILEC**
18 **TRANSACTIONS?**

19 A. Yes. My Exhibit Joint CLECs 1.2, "The Promises vs. Realities of Recent ILEC
20 Mergers and Acquisitions," supplies a summary of the promised benefits and
21 actual outcomes of the Carlyle-Hawaiian Telcom and FairPoint-Verizon
22 transactions. In addition, the Exhibit summarizes the more recent Frontier-
23 Verizon and CenturyTel-Embarq transactions in the same manner, to the extent

[30] Frontier Communications, Fact Sheet dated 5/19/2009, "Frontier Communications to Acquire Verizon Assets, Creating Nation's Largest Pure Rural Communications Services provider," downloaded from Frontier's Investor Relations webpage, http://phx.corporate-ir.net/phoenix.zhtml?c=66508&p=irol-irhome

1 possible, given that integration activities pursuant to these transactions are still
2 on-going, so that their full impacts and outcomes have yet to be realized.

3 In each case, at the time the transaction was first proposed, the companies
4 involved made numerous claims and assurances concerning the anticipated
5 benefits of their transactions, in their FCC applications, public press releases, and
6 testimony to state PUCs. My Exhibit summarizes those claimed benefits and
7 compares them to the actual outcomes realized to date, in the areas of (1)
8 deployment of broadband and other new services, (2) service quality, both retail
9 and wholesale, (3) job creation, and (4) the financial stability and performance of
10 the company post-transaction.

11 **Q. WHAT DOES EXHIBIT JOINT CLECS 1.2 SHOW?**

12 A. Exhibit Joint CLECs 1.2 shows the enormous gulf between the anticipated
13 benefits claimed by company management in these types of ILEC transactions,
14 and the ensuing realities. In all cases, company management claimed their
15 proposed transactions would spur accelerated deployment of broadband and other
16 new services, create jobs,[31] improve service quality and/or be seamless to
17 customers, including CLECs relying on wholesale services obtained via
18 Operations Support System ("OSS"), and improve the post-transaction company's
19 financial stability and performance. Unfortunately, as the Exhibit vividly shows,
20 the reality has been far different, particularly for the two earlier transactions

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[31] In the instant proceeding, I am not aware of any claims of job creation made with respect to the CenturyTel-Embarq merger, and in fact as noted in the Exhibit, CenturyLink had cut approximately 1,000 jobs (out of a base of 20,000) by early 2010.

1 (Hawaiian Telcom and FairPoint). Their outcomes included:

2 • Little or no demonstrated progress in broadband deployment:

3 ➢ After its acquisition by Carlyle, Hawaiian Telcom added only 3,247 net
4 retail broadband lines from 2006 through 3Q 2008;[32]

5 ➢ FairPoint's Chapter 11 reorganization plan includes delays/cut-backs to its
6 broadband deployment commitments, and eliminates a cap on DSL rates
7 so that customers may face higher rates; one Commissioner in Maine
8 charged that "FairPoint has used the bankruptcy proceeding as an
9 opportunity to renege on its promises to Maine consumers especially in
10 the area of broadband build out."[33]

11 • Severe declines in retail and wholesale service quality:

12 ➢ For Hawaiian Telephone, "very significant slow-downs in call answer and
13 handling times in its customer contact centers and errors in its
14 billing…;"[34]

15 ➢ For FairPoint, triggering the maximum payment under Vermont's Retail
16 Service Quality Plan in 2009, and widespread disruptions to wholesale
17 customers due to OSS systems failures, order fall-outs, and manual
18 processing work-arounds;

19 • Net job losses rather than gains:

20 ➢ Hawaiian Telephone's employment level had fallen to approximately 1450
21 by March 2010, a 15% decline from its pre-sale level of 1700
22 employees;[35]

23 ➢ FairPoint's Chapter 11 reorganization plan defers previously-negotiated
24 raises in union contracts, and creates a task force to cut operating expenses
25 by millions of dollars.[36]

26 • Financial weakness and instability:

27 ➢ Hawaiian Telcom: Chapter 11 bankruptcy filing, December 2008; reported
28 annual rate of return as of June 2009: −29.3%;

29 ➢ FairPoint: Chapter 11 bankruptcy filing, October 2009; VT Public Service

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[32] The 3,247 value is the difference between Hawaiian Telcom's total retail broadband lines, as of 9/30/2008, 93,567, and, as of 12/31/2006, 90,320 (source: Hawaiian Telcom, 3Q2008 Form 10-Q at p. 23 and 2007 Form 10-K, at p. 50), respectively.

[33] Dissent of Commissioner Viafades, MPUC Order 7/6/10.

[34] Hawaii PUC Annual Report 2008-2009, at p. 58.

[35] See Hawaiian Telcom Holdco, Inc. Form 10-A, filed 5/26/10, at p. 12 and *Honolulu Star-Bulletin, "Hawaiian Telcom Gets CEO."* 10/14/04.

[36] Nashua Telegraph 2/9/10.

1 Board, "FairPoint's actual performance throughout 2008 and 2009 turned
2 out to be worse than the Board's most pessimistic assumptions."[37]

3 **Q. WHAT KIND OF OUTCOMES DO THE FRONTIER-VERIZON AND**
4 **CENTURYTEL-EMBARQ TRANSACTIONS APPEAR TO BE HAVING?**

5 A. The Frontier-Verizon and CenturyTel-Embarq outcomes are largely pending
6 because those transactions are so recent, but the preliminary indications are also
7 troubling. As noted in my Exhibit Joint CLECs 1.2, Frontier's integration of the
8 former Verizon exchanges has been marred by recent wholesale OSS failures,
9 ordering delays, under-staffed Access Order centers, and trouble report backlogs.
10 These problems are documented in detail in the testimony of Mr. Gates. Already,
11 they appear to belie Frontier's pledge that "this transaction will be seamless for
12 retail and wholesale customers."[38]

13 For its part, CenturyLink portrays its ongoing integration of Embarq's ILEC
14 operations in 18 states as "highly successful"[39] and "on track"[40] or even "ahead of
15 schedule"[41] relative to some systems integration activities, but here again there
16 are signs of strain.

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37 VT PSB Order 6/28/10 at p. 58.

38 Frontier-Verizon FCC Application, Exhibit 1 (description of the Transaction and Public Interest Statement.), at p. 4.

39 FCC WC Docket No. 10-110, Reply Comments of CenturyLink, Inc. and Qwest Communications International, Inc., filed July 27, 2010, at p. 10.

40 *Id*, at p. 9.

41 FCC WC Docket No. 10-110, Reply Comments of CenturyLink, Inc. and Qwest Communications International, Inc., filed July 27, 2010, Exhibit (Declaration of William E. Cheek), at ¶ 2.

1 As Mr. Gates shows in his direct testimony, the CLECs tw telecom and Socket
2 Telecom have been dealing with EASE (OSS) system failures in the legacy
3 Embarq territories since late 2009.

4 **Q. ARE CENTURYLINK AND QWEST NOW MAKING THE SAME SORTS**
5 **OF CLAIMS CONCERNING THE FUTURE BENEFITS FROM THE**
6 **PROPOSED TRANSACTION AS THESE OTHER COMPANIES DID?**

7 A. Yes. When I consider the proposed CenturyLink-Qwest merger in this context,
8 what is particularly troubling to me is that so many of the promises and
9 assurances that CenturyLink and Qwest are making now to secure their merger
10 are highly similar to those made to regulators by the prior companies, before their
11 transactions' failures. Compare for example, the following claims:

12 • Claims of a strong track record of successful telecommunications acquisitions:

13 ➢ Carlyle Group: "Carlyle has a track record of successful
14 telecommunications investments…"

15 ➢ FairPoint: "FairPoint has long-term experience in the telecommunications
16 industry. In fact, FairPoint has been acquiring telecommunications
17 companies since 1993…"[42]

18 ➢ Frontier: "Frontier has a strong record of successfully integrating
19 acquisitions…"

20 ***CenturyLink-Qwest:*** *"CenturyLink's management team has some of the*
21 *longest and most successful tenure in the industry with a proven track*
22 *record of successful mergers and acquisitions."*[43]

23 • Claims that proposed transaction will accelerate broadband deployment:

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[42] FairPoint-Verizon FCC Application, at p. 17.

[43] CenturyLink-Qwest's FCC Application, "Application For Consent To Transfer Control," filed May 10, 2010, at p. 10 ("CenturyLink-Qwest FCC Application").

- Hawaiian Telcom: "In short order we will offer new services to our customers, including expanded broadband..."[44]

- "FairPoint plans to increase broadband availability from current levels in Maine, New Hampshire, and Vermont within twelve months after the completion of the merger…"[45]

- "Frontier believes that… it can dramatically accelerate broadband penetration in these new markets over time."[46]

CenturyLink-Qwest: *"the transaction will help to accelerate deployment of broadband services in unserved and underserved areas for both residential and business customers."*[47]

- Claims that transaction will be seamless and non-disruptive to customers:

  - FairPoint: "...will enhance service quality and promote competition…"[48]

  - Frontier: "this transaction will be seamless for retail and wholesale customers"[49]

CenturyLink-Qwest: *"The merger will not disrupt service to any retail or wholesale customers..."*[50]

- Claims that transaction will improve financial strength and stability:

  - FairPoint: "the proposed transaction will … improv[e] its overall financial flexibility and stability"[51]

  - Frontier: "the transaction will transform Frontier by strengthening its balance sheet."[52]

CenturyLink-Qwest: *"the transaction will... create a service provider*

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[44] Carlyle Press Rel. 5/21/04

[45] FairPoint-Verizon FCC Application, at p. 18.

[46] Frontier-Verizon FCC Application, Exhibit 1 (Description of the Transaction and Public Interest Statement), at p. 3.

[47] CenturyLink-Qwest FCC Application, at p. 2.

[48] FairPoint-Verizon FCC Application, at p. 18.

[49] Frontier-Verizon FCC Application, Exhibit 1 (Description of the Transaction and Public Interest Statement), at p. 4.

[50] CenturyLink-Qwest FCC Application, at p. 37.

[51] FairPoint-Verizon FCC Application, at p. 19.

[52] Frontier-Verizon FCC Application, Exhibit 1 (Description of the Transaction and Public Interest Statement), at p. 4

1 *with improved financial strength and the financial f1exibility to weather*
2 *the impacts of changing marketplace dynamics..."*[53]

3 **Q. CENTURYLINK PROJECTS THAT IT WILL REAP $625 MILLION IN**
4 **ANNUAL OPERATING EXPENSE AND CAPITAL COST SYNERGIES**
5 **FROM 3-5 YEARS AFTER THE MERGER CLOSES. WERE HAWAIIAN**
6 **TELCOM AND FAIRPOINT ABLE TO ACHIEVE THE SYNERGIES**
7 **THEY ORIGINALLY PROJECTED IN CONNECTION WITH THEIR**
8 **MERGER/ACQUISITION TRANSACTIONS?**

9 A. No, they were not. In the Hawaiian Telcom case, I am not aware of any specific
10 quantification of transaction synergies made by the parties at the time of their
11 application for regulatory approvals. However, Carlyle did tell the Hawaii PUC
12 that it expected to realize operational efficiencies by creating new back office
13 systems located in Hawaii, to replace Verizon's centralized, legacy systems. As
14 the Hawaii PUC stated at the time the transaction was approved:

15 In re-establishing these functions, Carlyle plans to replace Verizon's
16 numerous legacy systems with updated and flexible application
17 systems. Carlyle specifically represents that it will achieve increased
18 economies of scale and improved operating efficiencies from replacing
19 multiple and duplicative systems with a single application.[54]

20 As Mr. Gates describes in depth in his direct testimony, the build-out of these new
21 systems went seriously awry, and contributed to the financial downfall of the
22 company. Instead of producing synergistic operating efficiencies and cost

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[53] CenturyLink-Qwest FCC Application, at p. 2.

[54] In the Matter of the Application of Paradise Mergersub, Inc., GTE Corporation, Verizon Hawaii Inc. Bell Atlantic Communications, Inc. and Verizon Select Services Inc. for Approval of a Merger Transaction and Related Matters, Hawaii PUC Docket No. 04-0140, Decision and Order No. 21696, March 16, 2005, at p. 48.

1 reductions, development delays and failures in the new systems caused Hawaiian
2 Telcom to incur millions of dollars of additional, unanticipated operating
3 expenses. The company's Form 10-Q SEC filing for the third quarter of 2006
4 documents over $33 million in such incremental expenses for just the first nine
5 months of 2006, including $22.3 million paid to Verizon to continue using its
6 systems after the planned cutover date, and another $11.3 million for "[t]hird-
7 party provider services and other services required as a result of the lack of full
8 functionality of back-office and IT systems."[55] The Form 10-Q filing explains
9 that:

> 10 Because BearingPoint was unable to deliver the expected full system
> 11 functionality by the April 1, 2006 cutover date and has continued to be
> 12 unable to deliver full functionality, it has been necessary for us to
> 13 incur significant incremental expenses to retain third-party service
> 14 providers to provide call center services and other manual processing
> 15 services in order to operate our business. To help remediate
> 16 deficiencies we engaged the services of an international strategic
> 17 partner with expertise in general computer controls and change
> 18 management as well as specific expertise with information technology
> 19 process controls. In addition to the costs of third-party service
> 20 providers, we also incurred additional internal labor costs, in the form
> 21 of diversion from other efforts as well as overtime pay.[56]

22 The filing goes on to say that the company expected to continue to incur
23 significant incremental systems-related costs through the last quarter of 2006 and
24 on into fiscal year 2007.[57]

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[55] Hawaiian Telcom Communications, Inc. Form 10-Q, filed November 14, 2006, at p. 26.

[56] *Id.*, at p. 26.

[57] *Id.* at p. 26. Note that the company's Form 10-K filing for year 2007 does not provide a similar quantification of systems-related incremental expenses, and the SEC's "EDGAR" filings database does not list a year 2008 Form 10-K for the company, presumably because of its Chapter 11 bankruptcy that year.

1 **Q. DID FAIRPOINT MANAGE TO ACHIEVE ITS CLAIMED**
2 **TRANSACTION SYNERGIES?**

3 A. No. Like Hawaiian Telcom, FairPoint also fell far short of its initial synergy
4 projections for the Verizon transaction, which were largely driven by expected
5 efficiency improvements in back-office and OSS systems. In an April 2007 filing
6 with the SEC, FairPoint stated that "FairPoint estimates that within six months
7 following the end of this transition period, which is expected to occur in 2008, the
8 combined company will realize net costs savings on an annual basis of between
9 $60 and $75 million from internalizing these functions or obtaining these services
10 from third-party providers."[58] In reality, FairPoint experienced severe operational
11 difficulties and cost over-runs during its post-transaction efforts to integrate the
12 legacy Verizon exchanges into its back-office and OSS systems, as Mr. Gates
13 documents in his direct testimony. By the time the company filed its Form 10-K
14 for 2009, it was forced to admit that:

> 15 Because of these Cutover issues, during the year ended December 31,
> 16 2009, we incurred $28.8 million of incremental expenses in order to
> 17 operate our business, including third-party contractor costs and
> 18 internal labor costs in the form of overtime pay. The Cutover issues
> 19 also required significant staff and senior management attention,
> 20 diverting their focus from other efforts.[59]

21 Once again, as in the Hawaiian Telcom case, the fact that forecasted operating
22 efficiencies and synergies failed to materialize, and instead were replaced by
23 substantial, unanticipated expense increases, contributed heavily to FairPoint's
24 financial distress and subsequent filing for Chapter 11 bankruptcy protection.

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[58] FairPoint Communications, Inc., Form S-4, filed April 3, 2007, at p. 14.

[59] FairPoint Communications, Inc., Form 10-K, filed May 27, 2010, at p. 16.

1 **Q. DOES FRONTIER APPEAR TO BE ON TRACK TO REALIZE THE**
2 **SYNERGIES IT CLAIMED WILL BE PRODUCED BY ITS RECENT**
3 **ACQUISITION OF VERIZON EXCHANGES?**

4 A. No, it does not, judging from the most recently-available public information that I
5 have been able to review. In their joint Application to the FCC, Frontier and
6 Verizon stated "When fully implemented, Frontier expects to yield annual
7 operating expense savings of $500 million" from the transaction.[60] However,
8 Frontier's Form 10-Q filed May 16, 2010, already admits to a major unanticipated
9 cost increase with respect to systems integration that detracts from those savings:

> 10 While we anticipate that certain expenses will be incurred, such
> 11 expenses are difficult to estimate accurately, and may exceed current
> 12 estimates. For example, our estimate of expected 2010 capital
> 13 expenditures related to integration activities has recently increased
> 14 from $75 million to $180 million, attributable in large part to costs to
> 15 be incurred in connection with third-party software licenses necessary
> 16 to operate the Spinco business after the closing of the merger.
> 17 Accordingly, the benefits from the merger may be offset by costs
> 18 incurred or delays in integrating the companies.[61]

19 **Q. WHAT CONCLUSIONS DO YOU REACH BASED ON YOUR**
20 **ASSESSMENT OF THESE PRIOR ILEC MERGER AND ACQUISITION**
21 **EXPERIENCES?**

22 A. Based on my overall assessment of the prior ILEC merger and acquisition
23 experiences set forth above, my conclusions are as follows:

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[60] Verizon Communications Inc. and Frontier Communications Corp., *Consolidated Application for Transfer of Control and Assignment of International and Domestic Section 214 Authority*, May 28, 2009, Exhibit 1 (Description of the Transaction and Public Interest Statement), at p. 3.

[61] Frontier Communications, Inc., Form 10-Q, filed May 16, 2010, at p. 56

1 • Mergers and acquisitions involving the transfer and integration of ILEC
2 local telephone operations carry a high degree of risk of failure, even
3 when implemented by highly-experienced management teams and well-
4 financed companies;

5 • When pursuing these types of transactions, company management tends to
6 overstate the anticipated benefits and understate the risks and
7 uncertainties;

8 • The integration of a Bell Operating Company's ILEC operations, in
9 particular, can prove to be extremely expensive and difficult, and
10 integration failures can be so costly as to not only eliminate the forecasted
11 transaction cost savings and other synergies, but to place the post-
12 transaction company under severe financial pressure.

13 Taken as a whole, I believe that these experiences demonstrate that regulators
14 must be extremely skeptical of management's pre-transaction claims and
15 assurances, and cognizant that such transactions involve significant
16 uncertainties and risks. From a public interest standpoint, those risks simply
17 may not be worth accepting, particularly because, as discussed previously, the
18 risks and gains are unevenly divided between shareholders and the broader
19 public interest, including captive customers such as CLECs. The economic
20 viability of CLECs may be threatened if things go awry, but unlike
21 shareholders, CLECs stand to gain little, if anything, if the merger is successful
22 from a shareholder standpoint. At a minimum, this asymmetric division of risks
23 must be mitigated by establishing concrete conditions, with meaningful
24 consequences for nonperformance, prior to the transaction's regulatory
25 approval.

1 2 # V. A CENTURYLINK/QWEST MERGER IS LIKELY TO HARM THE PUBLIC INTEREST

3 ## *A. Overview*

4 **Q. PLEASE PROVIDE A BRIEF DESCRIPTION OF THE PROPOSED**
5 **MERGER BETWEEN CENTURYLINK AND QWEST?**

6 A. In this proceeding, CenturyLink, formerly CenturyTel, seeks approval for the
7 acquisition of Qwest Communications. The merger entails a stock swap of $10.6
8 billion. CenturyLink will also assume approximately $12 billion in Qwest debt.
9 The overall value of the merger is about $22 billion. The Merged Company will
10 operate in 37 states, and serve some 5 million broadband customers and 17
11 million phone lines.

12 **Q. DOES THIS REPRESENT AN EXTRAORDINARY GROWTH FOR**
13 **CENTURYTEL?**

14 A. Yes. If the proposed transaction is consummated, CenturyTel will have grown
15 from a small rural company with about 1.3 million lines to a nationwide company
16 of about 17 million lines – over the course of a mere three years. The table
17 below, presented previously in the introduction, summarizes its growth:

18

1

	Year	Access Lines[62]	% of Post-Merger Total
CenturyTel	2009	1,300,000	8%
Embarq	2009	5,700,000	34%
Qwest	2010	10,000,000	59%
Total		**17,000,000**	**100%**

2

3 As discussed previously, it is important to note that this growth is not the result of
4 superior product offerings and customer growth, but rather achieved through
5 putting together a number of companies that were struggling[63] to hold their own
6 in rapidly changing telecom retail markets.[64]

7 **Q. DOES THE PROPOSED MERGER ENTAIL ANY SIGNIFICANT**
8 **BENEFITS OF VERTICAL INTEGRATION?**

9 A. For the most part, this is a horizontal merger. As noted, the proposed merger
10 seeks to integrate the operations of CenturyLink and Qwest. An evaluation of this
11 merger is further complicated by CenturyLink's ongoing and, as of yet,
12 incomplete efforts to integrate the recently acquired Embarq. Therefore,
13 assessing the synergies claimed with respect to CenturyLink's acquisition of

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62 Line counts are taken from CenturyLink's testimony. The line counts in CenturyLink's testimony appear to be approximate line counts. See Direct Testimony of Jeremy Ferkin, May 27, 2010 ("Ferkin Utah Direct"), at p. 16 and Exhibit JF-1; and Direct Testimony of Jeff Glover, May 27, 2010 ("Glover Utah Direct"), at p. 4.

63 Both companies, for example, continue to experience access line losses. For CenturyLink see http://ir.centurylink.com/phoenix.zhtml?c=112635&p=irol-newsArticle_Print&ID=1422603&highlight; for Qwest, see, 2010 Quarterly Earnings at http://investor.qwest.com/qtrlyearnings

64 This does not mean that the companies are not dominant in wholesale markets and continue to control the wholesale relationship with CLECs that require access to the Join Applicant's network.

1 Qwest involves considerations of integrating the operations of three incumbent
2 LECs. That is, in essence, this case concerns a predominantly *horizontal* merger
3 across the geographically separate serving areas of three incumbent LECs,
4 CenturyTel, Embarq and Qwest, all three of which are generally in the same line
5 of business in different service areas.

6 **Q. DOES THE FACT THAT CENTURYLINK IS SEEKING TO PUT**
7 **TOGETHER THE OPERATIONS OF THREE ILECS LIMIT THE**
8 **EXTENT TO WHICH SYNERGIES CAN BE REALIZED?**

9 A. Yes. Because the proposed transaction would involve the integration of three
10 ILECs operating in different service areas, the benefits from the potential merger
11 are necessarily limited, which may explain why CenturyLink and Qwest refer to
12 the alleged benefits in vague terms, like "capitalizing on," "leveraging,"
13 "extending," and so forth. Those vague assertions leave one wondering why,
14 under the right management, such benefits could not be achieved by each of the
15 firms individually.

16 While mergers often fail to enhance shareholder value, there are types of mergers
17 and acquisitions that tend to expand a company's abilities and service offerings.
18 For example, when Microsoft acquired Forethought, which had developed a
19 presentation program, it allowed Microsoft to expand its suite of software
20 programs to include Microsoft PowerPoint, and to eventually market a powerful
21 bundle of programs, Microsoft Office, to students and business users. Similarly,
22 Microsoft's acquisition of Visio Corporation allowed it to further expand its

1 product line by integrating Microsoft Visio. I am not asserting that all of
2 Microsoft's dozens of acquisitions have been successes; rather, I am illustrating
3 an essential difference between these acquisitions by Microsoft and
4 CenturyLink's acquisition of Qwest. While the Microsoft acquisitions are a clear
5 example of how an acquisition can add to a company skills and products that were
6 not previously present, the CenturyLink-Qwest merger is an example, for the
7 most part, of adding more of the same in the hope that something better will
8 emerge, under the motto "Bigger is Better."

9 It is unclear how putting together three ILECs, with a shrinking landline base, is
10 going to result in a sustained turnaround, let alone substantial merger benefits.
11 CenturyLink's claims of merger benefits notwithstanding, there is little inherently
12 new or novel in the proposed combination of these ILECs, with largely
13 overlapping business models.

14 **Q. DOES THE MERGER APPEAR TO ENHANCE THE FINANCIAL**
15 **POSITION OF THE FIRMS?**

16 A. No, not really. Looking at how financial markets seem to be responding to the
17 proposed merger, there hardly seems to be a flurry of excitement; in fact, rating
18 agencies have recognized the increased riskiness of the post-merger firm.[65] Also,
19 using a traditional measure of the weighted average cost of capital ("WACC"), it

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[65] See the April 2010 ratings reports for CenturyLink issued by Morgan Stanley, Moody's, and Standard and Poor's, which were reproduced as the three exhibits to Mr. Glover's direct testimony, Exhibits JSG-2, JSG-3, and JSG-4, respectively.

1 is not clear how the Merged Company is better positioned to attract capital.[66] In
2 fact, given that the Merged Company would be no less risky and that CenturyLink
3 would be assuming Qwest's massive debt load, there is reason to conclude that
4 financial markets will be less (rather than more) forthcoming in financing
5 CenturyLink's future network expansions.

6 ***B. Vertical Effects***

7 **Q. YOU NOTED THAT THE PROPOSED MERGER DOES NOT, ON ITS**
8 **FACE, REVEAL COMPLEMENTARY SKILLS AND PRODUCTS. DOES**
9 **THIS SUGGEST THAT THE DRIVE TO ACHIEVE MERGER BENEFITS**
10 **AND SYNERGIES WOULD INVARIABLY PIT CENTURYLINK**
11 **AGAINST ITS WHOLESALE CLIENTS, SUCH AS CLECS?**

12 A. Yes. To justify the merger and the associated costs of integration, CenturyLink is
13 promising regulators and shareholders merger benefits estimated at about $625
14 million over a period of three to five years.[67] As noted, the premerger companies
15 are struggling to hold their own in changing telecom retail markets and it is not
16 clear that the merger will soon, if ever, generate revenues and profits to recoup the
17 upfront costs of integration. This raises concerns about cost cutting measures that
18 may negatively impact wholesale services.

19 Trimming wholesale costs not only saves money on services that are not subject
20 to significant competition, it does so without the likelihood of revenue

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[66] See CenturyLink's and Qwest's Response to Staff Data Request No. 3, Oregon Docket No. UM 1484, showing an increase in the post-merger weighted average cost of capital.

[67] See Glover Utah Direct, at p. 5.

1 repercussions: *i.e.*, the cost savings directly improve the bottom line. That is,
2 there are added incentives to cut costs in segments of the companies' operations
3 that are not subject to competitive pressures: most notably, the wholesale business
4 charged with meeting the Section 251 and Section 271 obligations under the
5 Telecommunications Act of 1996. In sum, this dynamic places post-merger
6 CenturyLink at odds with captive CLEC wholesale customers.

7 **Q. SHOULD THE COMMISSION CONSIDER THE IMPACT OF THE**
8 **MERGER ON CLECS AND COMPETITION?**

9 A. Yes. As discussed previously, a public interest review requires consideration of
10 how the merger is likely to impact competition and CLECs, and in turn, CLEC
11 end user customers . In fact, the Commission has recognized this as a key
12 consideration. The public interest would be harmed if the competitive landscape
13 becomes distorted by significant cost cutting that causes a deterioration in
14 wholesale service provisioning. Showing that these concerns are not idle, Mr.
15 Gates discusses in more detail the potentially harmful impact of the merger on the
16 Merged Company's provisioning and how it could seriously impair – *as mergers*
17 *have elsewhere* – the viability of competitors.

18 **Q. HAS THE FCC NOTED THE IMPORTANCE OF CONSIDERING THE**
19 **IMPACT ON WHOLESALE SERVICES AND COMPETITORS?**

20 A. Yes. Part of the FCC's analytical framework in reviewing mergers is to look not
21 only at the horizontal effects of a merger but also the vertical effects, related to

1 the post-merger impact on wholesale markets. Recognizing the potential harm a
2 merger may cause to competitors and competition itself, the FCC notes:

3 [w]e need to consider the vertical effects of the merger – specifically,
4 whether the merged entity will have an *increased incentive* or *ability*
5 to injure competitors by raising the cost of, or discriminating in the
6 provision of, inputs sold to competitors.[68] (Emphasis added.)

7 As discussed above, it appears that CenturyLink may have an increased incentive
8 as well as an increased ability to negatively impact its competitors due to the
9 larger scope of its operations.

10 **Q. DOES THIS RAISE CONCERNS NOT JUST WITH RESPECT TO UNES**
11 **BUT ALSO SPECIAL ACCESS SERVICES?**

12 A. Yes. Local competition remains critically dependent on the availability of UNEs,
13 interconnection and special access services at reasonable rates and terms. The
14 proposed merger may negatively impact the provision of special access services,
15 which are already being provisioned at unreasonably high rates and on terms and
16 conditions that are hampering competitors.[69] In fact, in view of these concerns,
17 the FCC has recently decided to revisit its regulations of special access services.[70]
18 This merger may further unsettle special access markets.

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[68] In the Matter of A&T Inc. and BellSouth Corporation Application for Transfer of Control, Memorandum Opinion and Order, WC Docket No. 06-74, Para. 23.

[69] See for example, United States Government Accountability Office, Report to the Chairman, Committee on Government Reform, House of Representatives, *Telecommunications: FCC Needs to Improve Its Ability to Monitor and Determine the Extent of Competition in Dedicated Access Services*, November 2006. ("*GAO Report*").

[70] *In the Matter of Special Access Rates for Price Cap Local Exchange Carriers AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services,* WC Docket No. 05-25, RM-10593. The FCC conducted a workshop on revising special access pricing on July 19, 2010.

1 **Q. ARE THESE CONCERNS ESPECIALLY IMPORTANT GIVEN THE**
2 **SUBSTANTIAL AMOUNT OF DEBT CENTURYLINK WILL BE**
3 **ASSUMING BY ABSORBING QWEST?**

4 A. Yes. CenturyLink is taking on an enormous amount of debt and other risks, so
5 much so, that it is negatively impacting its credit rating[71] This draws into question
6 the claim that the Merged Company would be a financially stronger entity.
7 Moreover, to deal with this debt, and to placate shareholders and financial
8 markets, CenturyLink has stated that it will use its free cash flow to pay down this
9 debt.[72] Given the dearth of information CenturyLink and Qwest have provided to
10 support the alleged merger savings, CenturyLink's stated intentions to pay off its
11 debt raises still more questions about its ability to provide and maintain quality
12 wholesale services and OSS to CLECs, not just for its own pre-merger operations
13 but especially for Qwest's, which are subject to Section 271 obligations. Again,
14 when asked to provide details supporting its projected merger savings,
15 CenturyLink and Qwest respond that those savings have not been calculated at a
16 detailed level or have not yet been developed.[73] Circular answers like "[t]he

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[71] See the April 2010 ratings reports for CenturyLink published by Morgan Stanley, Moody's, and Standard and Poor's, which were reproduced as the three exhibits to Mr. Glover's direct testimony, Exhibits JSG-2, JSG-3, and JSG-4, respectively. As Moody's notes in its report (p. 1):

> The negative rating outlook for CenturyTel reflects the considerable execution risks in integrating a sizeable company so soon after another large acquisition (Embarq in July 2009) while confronting the challenges of a secular decline in the wireline industry. The negative outlook also considers the possibility that the Company may not realize planned synergies in a timely manner, especially if competitive intensity increases.

[72] See, for example, Glover Utah Direct, at p. 17.

[73] See my Exhibit Joint CLECs 1.4 at p. 7; see also, *e.g.*, CenturyLink's Response to Integra's Second Set of Information Requests, #53 ("CenturyLink has not estimated synergy savings or

1 combined companies regulated entities will benefit from synergies post merger in
2 the form of lower costs to the extent synergies are achieved,"[74] are not reassuring,
3 much less credible evidence on which the Commission can base findings that the
4 transaction is in the public interest. The absence of, and refusal to provide,
5 anything approaching a detailed analysis of the Companies' projected merger
6 savings leaves unaddressed the required comparison with the profound risks
7 posed by this transaction.

8 In sum, a major concern is that, under the pressure of its debt load, the promises
9 of merger savings to shareholders and regulators, and significant integration costs,
10 CenturyLink will be forced to cut costs when integrating the two companies,
11 leading to a degradation of services to wholesale customers and harm to
12 competition. Worse, of course, is the possibility that this merger could fail as so
13 many have, causing upheaval in wholesale markets and impairing retail
14 competition just when consumers need the benefits of competition most.

15 **Q. DOES MR. GATES DISCUSS A NUMBER OF MERGER CONDITIONS**
16 **THAT COULD SERVE TO ADDRESS CONCERNS ABOUT VERTICAL**
17 **EFFECTS?**

18 A. Yes. As the FCC noted in previous mergers, economically efficient access by
19 CLECs to the ILECs' network elements serves to constrain the ILECs' ability to

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one-time merger costs by state"); and Iowa Utilities Board Docket No. SPU-2010-0006, CenturyLink's June 16, 2010 Response to OCA Set 1, #13F ("Synergies were estimated at the total enterprise level only and not by entity or by state"); and June 29, 2010 Updated Response to OCA Set 1, #13F ("No estimate of synergies by Post Merger entity has been conducted.").

[74] CenturyLink Response to Integra's Second Set of Information Requests, #141.

1 exploit market power in wholesale markets to the detriment of competition in
2 downstream, retail markets.[75] In view of this, it is of paramount importance that
3 the Commission take action to ensure reliable, nondiscriminatory access to the
4 post-merger ILEC's wholesale network elements and services, including action
5 that safeguards the wholesale ordering and provisioning processes currently in
6 place. Mr. Gates discusses conditions that serve this important purpose.

7 ### *C. Horizontal Effects*

8 **Q. IN ADDITION TO THE POTENTIAL HARM FROM VERTICAL**
9 **EFFECTS, IS THE MERGER LIKELY TO CAUSE HARM DUE TO**
10 **HORIZONTAL EFFECTS?**

11 A. Yes. A merger of CenturyLink and Qwest reduces competition in areas and for
12 services in which the companies compete. While, for the most part, the
13 companies operate in their own separate service areas, there are some instances in
14 which they do compete. Clearly, a merger would eliminate this competition, and
15 in doing so harm the public interest.

16 For example, as is evident from CenturyLink's own testimony, the companies
17 serve large numbers of exchanges that are adjacent. As is increasingly common,
18 ILECs often set up CLEC subsidiaries through which they compete in adjacent
19 exchanges. For example, CenturyLink operates as a CLEC in Minneapolis in

[75] For example, see *In the Matter of AT&T Inc. and BellSouth Corporation Application for Transfer of Control*, WC Docket No. 06-74, Memorandum Opinion and Order, December 31, 2006, at Para. 60.

1 competition with Qwest.[76] The merger will eliminate any incentives for this type
2 of competition between the two companies. The harm may, in fact, be larger than
3 meets the eye in the sense that it eliminates not just actual instances of such
4 competition but also *potential* ones.

5 **Q. IS THE ELIMINATION OF SUCH COMPETITION AND POTENTIAL**
6 **COMPETITION IN LOCAL MARKETS TROUBLING IN LIGHT OF**
7 **THE FACT THAT LARGE SEGMENTS OF LOCAL EXCHANGE**
8 **MARKETS STILL LACK SIGNIFICANT COMPETITION?**

9 A. Yes. The areas in which CenturyLink and Qwest are potential competitors are
10 often largely rural and populated by captive ratepayers with few alternative
11 providers of local exchange service. Elimination of potential competition in those
12 areas is therefore especially troubling.

13 *E. Uncertainty and Harm Will Result If the Merger Is Approved*
14 *As Filed*

15 **Q. HAS CENTURYLINK SUBSTANTIATED ITS CLAIMS ABOUT THE**
16 **TRANSACTION CAUSING NO HARM?**

17 A. No. The basis for CenturyLink's claim that the proposed transaction will do no
18 harm is its repeated statements that there will be no "immediate" changes made
19 following the merger. For instance, CenturyLink states:

20 "***Immediately*** upon completion of the Transaction, end-user and
21 wholesale customers will continue to receive service from the

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[76] Http://www.centurylink.com/Pages/AboutUs/CompanyInformation/Regulatory/tariff Library.js; sessionid=055C224C462B5CB0FDF05EF67BB97A646E4E4AE78F.dotcomprd19

> same carrier, at the same rates, terms and conditions and under the same tariffs, price plans, interconnection agreements, and other regulatory obligations as ***immediately*** prior to the Transaction; as such, the Transaction will be transparent to the customers."[77]

What is important is what this statement does ***not*** include. Specifically, it does not state how long customers will continue to receive service under the same rates, terms and conditions. Indeed, the footnote that follows the above statement is very disconcerting:

> In view of the current rapidly changing communications market, any provider, including post-Transaction CenturyLink, must constantly review its pricing strategy and product mix to respond to marketplace and consumer demands. While rates, terms and conditions will be the same immediately after the Transaction as immediately before the Transaction, ***prices and product mixes necessarily will change over time as marketplace, technology, and business demands dictate.*** The affected entities will make such changes only following full compliance with all applicable rules and laws. (Emphasis added.)

A fair reading of CenturyLink's Application and the companies' supporting testimony indicates that changes will indeed take place and yet there are no specifics about what those changes might be or how and when they might be made.

Q. DO THE COMPANIES' REPRESENTATIONS REGARDING TRANSPARENCY SATISFY THE PUBLIC INTEREST STANDARD?

A. No. The companies' vague and limited representations are meaningless, and certainly fail to demonstrate that the public interest will be protected. Obviously, CenturyLink could implement changes within months, weeks, or even days after

[77] Joint Application, at p. 6 (emphasis added). See also, Direct Testimony of Jeremy Ferkin, May 27, 2010 ("Ferkin Utah Direct"), at p. 6.

1 closing the transaction and still purport to have made no "immediate" changes.
2 For example, shortly after the transaction closes, the Merged Company could
3 implement layoffs[78] or require that CLECs re-negotiate all "evergreen" ICAs
4 using CenturyLink's template ICA or attempt to change Qwest's OSS. As I
5 discussed earlier in my testimony, the Commission's merger approval authority
6 under Utah law is intended to ensure that mergers are in the public interest. This
7 important authority certainly does not contemplate approval of a merger based on
8 the vague, limited assurances offered by the Companies. The bottom line (and the
9 reason why the proposed transaction is of such concern to CLECs) is that the
10 proposed merger provides absolutely no certainty for wholesale (or retail)
11 customers and the Companies have provided no meaningful assurance that the
12 transaction will not harm wholesale customers in the Qwest or CenturyLink
13 territories.

14 **Q. GIVEN CENTURYLINK'S CLAIM OF *BUSINESS AS USUAL*
15 "IMMEDIATELY" FOLLOWING THE TRANSACTION, WHY DO YOU
16 BELIEVE THAT CHANGES WILL BE MADE?**

17 A. Because CenturyLink has stated that changes are coming. For example, in
18 response to discovery, CenturyLink states:

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[78] According to the Associated Press, Qwest already made significant job cuts last year on a territory-wide basis, "decreasing its work force by 8.5 percent last year, or roughly 2,800 positions." See "Qwest Q4 profit falls 39 percent", February 16, 2010 at http://www.oregonlive.com/business/index.ssf/2010/02/qwest_q4_profit_falls_39_perce.html ; also, according to Timothy Donovan, president of Local 7200 of the Communications Workers of America, based in Minneapolis, about 6,000 workers are likely to lose their jobs. See, "CenturyTel-Qwest deal is a rural double-down," *Star Tribune*, April 22, 2010 at http://www.startribune.com/business/91876019.html.

1 Upon merger closing, there will be no immediate changes to
2 Qwest's or CenturyLink's Provisioning Systems. CenturyLink has
3 not evaluated its processes and compared them to Qwest's
4 processes at this time. Integration planning is in the early stages
5 and decisions have not been made at this time. However, because
6 the transaction results in the entirety of Qwest, including
7 operations and systems, merging into and operating as a subsidiary
8 of CenturyLink, it will allow a disciplined approach to systems and
9 practices and allow integration decisions to proceed in an orderly
10 manner. The merger is intended to bring about improved
11 efficiencies and practices in all parts of the combined company, ***so***
12 ***changes could be expected over time.*** To the extent any changes
13 are made, CenturyLink will comply with all applicable state and
14 federal laws and rules, as well as the provisions of any applicable
15 interconnection agreements and tariffs, in the same manners as
16 they would apply notwithstanding the merger. In addition, any
17 changes will occur only after a thorough and ***methodical review of***
18 ***both companies' systems and processes to determine the best***
19 ***system to be used*** on a go-forward basis from ***both a combined***
20 ***company and a wholesale customer perspective***.[79]

21 Though CenturyLink has put CLECs on notice to expect changes, CenturyLink
22 has provided no detail about what will change, when it will change or how
23 CenturyLink will determine which is the "best system"[80] to use. This is

[79] CenturyLink Response to Integra's Second Set of Information Requests, #35(h) (emphasis added). See also, CenturyLink SEC Form S-4/A, filed July 16, 2010, at p. 16 ("There are a large number of systems that must be integrated, including, billing, management information, purchasing, accounting and finance, sales, payroll and benefits, fixed asset, lease administration and regulatory compliance.")

[80] To my knowledge, CenturyLink has not provided any substantive details about the "methodical review" or what it means to perform the review from "both a combined company and a wholesale customer perspective." In the instant case, CenturyLink objected to discovery seeking such information, see CenturyLink Response to Integra's Second Set of Information Requests, No. 49. In response to similar discovery in Oregon, CenturyLink supplied responses that provided little additional detail, other than to say that "[i]t has not been determined whether third-party testing will be included in the assessment process." Oregon PUC Case 1484, CenturyLink Response Joint CLECs Fifth Set of Information Requests, No. JC-53a. In a nutshell, CenturyLink's response is that it will evaluate the different systems and processes, take input from interested CLECs, and then base its decision on "operational efficiencies for the Company [CenturyLink], in general." Oregon PUC Case 1484, CenturyLink Response to Joint CLECs Fifth Set of Information Requests, No. JC-53b. If CenturyLink is truly concerned about the "wholesale customer perspective," then CenturyLink will not replace Qwest's existing OSS post-transaction. As evidenced by the

1 particularly problematic when it comes to OSS because only Qwest's existing
2 systems (*i.e.*, not CenturyLink's existing OSS) have been tested under a Section
3 271 review.

4 **Q. CENTURY*LINK GOES EVEN FURTHER AND CLAIMS THAT THERE*
5 *ARE NO "POTENTIAL* HARMS THAT COULD RESULT FROM THE
6 MERGER."[81] IS THIS TRUE?**

7 A. No. As discussed previously, this merger poses a substantial risk of harm to
8 CLECs and competition based on (1) the nature and history of mergers such as
9 this; (2) the prospect of cuts aimed at achieving the enormous synergies claimed
10 by the Companies; and (3) the inherent competitive disincentive to providing
11 quality wholesale services to carriers with whom the Merged Company will
12 compete. The potential for substantial harm is further illustrated by the
13 bankruptcies and system meltdowns that have transpired in the wake of recent
14 mergers. Contrary to CenturyLink's claim, there ***are*** unquestionably "potential
15 harms that could result from the merger."

16 For instance, despite CenturyLink's best efforts, if it attempts to integrate any
17 OSS or other systems from the CenturyLink region to Qwest's region and such an
18 attempt fails (as in the case of FairPoint), CLECs would likely suffer substantial
19 harm. As another example, the Companies' projected synergies and one-time
20 integration costs pose a serious threat to the public interest in at least two respects.

CLEC proposed conditions, it is clearly the CLECs' perspective that Qwest's existing OSS is preferable to existing CenturyLink OSS.

[81] Ferkin Utah Direct, at p. 12 (emphasis added).

1 First, the pressure to achieve their estimated $625 million in synergies may drive
2 cuts or inattention to the provision of quality wholesale services, including OSS
3 used to support those services. Second, failure to achieve its estimated synergies
4 or higher than expected integration costs could seriously impede the Merged
5 Company's ability to pay down its debt, attract capital and make the investments
6 necessary to ensure adequate service. The free cash flow that CenturyLink claims
7 it will use to reduce debt and invest in its network is based on its estimated $625
8 million in operating and capital synergies, along with its estimated $650-$800
9 million in one-time operating costs and $150-$200 million in one-time capital
10 costs.[82] However, if CenturyLink fails to achieve those synergies or if its
11 integration costs significantly exceed the estimates (despite CenturyLink's best
12 efforts to achieve these targets), its ability to pay down debt will be diminished,
13 thereby leaving the merged company highly leveraged and potentially unable to
14 make the needed investments to maintain service quality or the dividends to
15 satisfy shareholders.

16 **Q. HAS CENTURYLINK ACKNOWLEDGED THE POTENTIAL FOR**
17 **HARM RELATED TO FAILING TO ACHIEVE ESTIMATED SYNERGY**
18 **SAVINGS?**

19 A. Yes. CenturyLink made this very point to the SEC and its shareholders when it
20 stated that the inability to successfully integrate Qwest and CenturyLink could
21 prevent CenturyLink from:

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[82] See *e.g.*, Glover Utah Direct, at pp. 4-5 and p.4, fn. 5.

1 achiev[ing] the cost savings anticipated to result from the merger,
2 which would result in the anticipated benefits of the merger not being
3 realized in the time frame currently anticipated or at all.[83]
4
5 While the Joint Applicants' prefiled testimony in the instant case sidesteps the
6 issue, in other states they have acknowledged the potential harms or "integration-
7 related risks" associated with beginning the integration of Qwest before the
8 integration of Embarq is complete.[84]

9 **Q. HAS THE FCC PREVIOUSLY REJECTED CLAIMS THAT THERE ARE**
10 **NO POTENTIAL HARMS RESULTING FROM A MERGER OF THIS**
11 **TYPE?**

12 A. Yes. When evaluating the SBC/Ameritech merger – a merger involving two
13 ILECs – the FCC found harm resulting from the transaction in three areas:

14 • It removes one of the most significant potential participants in each of the
15 applicant's local markets, for mass market and enterprise customers
16 • It substantially reduces the ability of regulators to implement and oversee
17 the market-opening provisions of the 1996 Act because the ability to

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[83] CenturyLink SEC Form S-4A, filed July 16, 2010, at p. 17.

[84] *See, e.g.*, Washington Utilities and Transportation Commission Docket No. UT-100820, Direct Testimony of G. Clay Bailey (CenturyLink), filed May 21, 2010, at p. 18 ("Q. Does the merger with Qwest include incremental financial risks because the Embarq transaction was only consummated at the end of June, 2009? A. CenturyLink believes that the integration-related risks are manageable for several reasons. …"). See also, the "Risk Factors" discussion found in CenturyLink's SEC Form S-4A, filed July 16, 2010, identifying, among others, the following as merger-related risks: (1) "substantial expenses in connection with completing the merger and integrating the business, operations, networks, systems, technologies, policies and procedures of Qwest with those of CenturyLink"; (2) "CenturyLink expects to commence these integration initiatives before it has completed a similar integration of its business with the business of Embarq, acquires in 2009, which could cause both of these integration initiatives to be delayed or rendered more costly or disruptive than would otherwise be the case"; (3) "the inability to successfully combine the businesses of CenturyLink and Qwest in a manner that permits the combined company to achieve the cost savings anticipated to result from the merger, which would result in the anticipated benefits of the merger not being realized in the time frame currently anticipated or at all." S-4A, at pp. 16-17.

compare the practices of BOCs and ILECs is diminished, which increases the incumbent's market power

- It increases the incentive and ability of the Merged Company to discriminate against its competitors, particularly with respect to the provision of advanced services.

The FCC found that these harms would have been fatal to the merger application but for the extensive list of conditions that were placed on the merger to offset the harm.[85] The harms identified by the FCC apply to the proposed transaction.

Q. ARE THERE OTHER REASONS TO TAKE ISSUE WITH CENTURYLINK'S AND QWEST'S CLAIM OF "NO HARM"?

A. Yes. The uncertainty surrounding the potential merger and what may take place afterward is causing significant uncertainty for CLECs, which, in and of itself, causes harm. CLECs need certainty to plan their businesses and make prudent investments, and the proposed transaction results in uncertainty in virtually every aspect of the CLECs' relationship with the Merged Company.

F. Harm Due to a Lack of Certainty (Business Planning)

Q. IS THERE A GENERAL NEED FOR CERTAINTY IN BUSINESS RELATIONSHIPS?

A. Yes. In a general sense, when a business relies upon another business for services or parts, it is critical to have a contract in place that is specific and

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[85] *In re Applications of AMERITECH CORP., Transferor, and SBC COMMUNICATIONS INC., Transferee, For Consent to Transfer Control of Corporations Holding Commission Licenses and Lines Pursuant to Sections 214 and 310(d) of the Communications Act and Parts 5, 22, 24, 25, 63, 90, 95 and 101 of the Commission's Rules*, CC Docket No. 98-141, Memorandum Opinion and Order, ¶¶ 348-349.

1 unambiguous. For instance, if Ford is purchasing tires for its vehicles from
2 Firestone, it is very important for Ford to know and understand what type, size,
3 quality and quantity of tires will be delivered to each manufacturing plant and
4 when. Not surprisingly, the cost of the tires is also important for Ford in setting
5 the prices for vehicles. If Firestone announced that it was being acquired by
6 Tires, Inc. (a fictional company) on December 31, 2010, Ford would likely ask
7 Firestone a litany of questions about what Ford could expect in 2011 – *e.g.*,
8 whether Firestone will deliver the same type and size of tires Ford needs, whether
9 the quality of the tires will be the same, whether the tires will be delivered to the
10 manufacturing plant in a timely manner, etc. If Firestone came back to Ford and
11 said "we don't know and won't know until 2011", Ford would (a) start looking to
12 another tire supplier that can provide more certainty, (b) ask Firestone to provide
13 commitments that can be relied upon in 2011, or (c) both. The point is that Ford
14 would demand certainty so that it could continue to produce vehicles and deliver
15 them to the showroom. Likewise, CLECs – who rely on ILEC-provided services
16 – need certainty in order to deliver their services to the local market place.

17 **Q. DO CLECS HAVE THE SAME OPTIONS WITH REGARD TO**
18 **SUPPLIERS AS FORD DID IN YOUR PREVIOUS ANALOGY?**

19 A. No. Unlike Ford, the CLECs cannot shop elsewhere for the critical wholesale
20 services they purchase from the ILECs in the Companies' territories. That means
21 that certainty in relation to the services CLECs purchase from ILECs is even more
22 important.

1 **Q. HAS CENTURYLINK ACKNOWLEDGED THE HARM THAT RESULTS**
2 **FROM UNCERTAINTY RELATING TO THE PROPOSED**
3 **TRANSACTION?**

4 A. Yes. In its Form S-4A filing (at page 16) CenturyLink states:

5 In connection with the pending merger, some customers or vendors
6 of each of CenturyLink and Qwest may delay or defer decisions,
7 which could negatively impact the revenues, earnings, cash flows
8 and expenses of CenturyLink and Qwest, regardless of whether the
9 merger is completed.

10 CLECs are wholesale customers of Qwest and CenturyLink, and CenturyLink is
11 correct that the pending merger can result in delayed or deferred decisions from
12 these wholesale customers. And while CenturyLink focuses on the potential
13 negative impacts on revenues, earnings, cash flows and expenses of Qwest and
14 CenturyLink resulting from this uncertainty, CenturyLink ignores that this
15 uncertainty also could cause negative impacts on CLEC revenues, earnings, cash
16 flows and expenses. Likewise, in its recent Reply Comments to the FCC,
17 CenturyLink states that, "the transaction will bring much-needed stability to the
18 incumbent local exchange carrier ('ILEC') sector",[86] but ignores that CLECs also
19 need stability and that the proposed transaction causes severe *un*certainty for
20 CLECs. Because the Merged Company will be pursuing merger-related synergy
21 savings for a three-to-five year period after the merger, the uncertainty for the
22 Merged Company's CLEC wholesale customers will continue well beyond the
23 date of merger approval.

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[86] FCC WC Docket No. 10-110, Reply Comments of CenturyLink, Inc. and Qwest Communications International, Inc., filed July 27, 2010, at p. 9.

1 **Q. HAS THE COMMISSION SEEN REPRESENTATIONS SIMILAR TO**
2 **THE COMPANIES' THAT CERTAIN DECISIONS WILL NOT BE MADE**
3 **UNTIL AFTER THE MERGER CLOSES BEFORE?**

4 A. Yes. In regard to dozens of issues in this proceeding, the Companies have stated
5 in initial testimony and in discovery that the relevant decisions have not been
6 made yet and will not be made until after the merger. That has been the
7 Companies' response on almost everything – from which OSS will be used in
8 Utah to the staffing levels and potential headcount reductions that may occur post-
9 merger in the wholesale services support centers for Utah and other legacy Qwest
10 territories.

11 **Q. HAVE YOU PREPARED AN EXHIBIT TO DEMONSTRATE THE**
12 **SIGNIFICANT UNCERTAINTY FACING CLECS DUE TO THE**
13 **PROPOSED MERGER?**

14 A. Yes. Attached as Exhibit Joint CLECs 1.3 is a table which lists many of the
15 important and customer-impacting issues that should be examined in determining
16 whether the proposed transaction will cause "no harm" (*e.g.*, systems integration,
17 operations integration, performance assurance plans, wholesale rates, etc.) and
18 matches that list to what the Companies have said about those issues in discovery
19 responses. This exhibit shows complete uncertainty post-transaction for
20 important issues such as OSS integration, billing systems integration, E911
21 systems, provisioning intervals, wholesale customer service, change management
22 process, network investment, just to name a few. In each area, the Companies
23 were unable or unwilling to provide any plans or describe any changes that will

1 take place – other than to say, *we'll let you know after the merger has been* 2 *approved*. Unfortunately, that is too late. The Companies must demonstrate now 3 that the proposed transaction will do "no harm" and they have failed to 4 demonstrate that, as evidenced by this exhibit.

5 VI. FAILURE TO PROVE BENEFITS RESULTING FROM 6 MERGER

7 **Q. CAN THE COMMISSION VALIDATE CENTURYLINK'S CLAIMS OF 8 BENEFITS RESULTING FROM THE MERGER?**

9 A. No. Although CenturyLink has identified numerous alleged benefits from the 10 proposed transaction, it has substantiated none of them. In discovery in Utah and 11 other states undertaking merger reviews, various parties including CLECs, 12 commission staffs and consumer advocates asked the Companies about their plans 13 regarding the alleged benefits, and in every instance, the Companies have stated 14 that they have no plans and/or that plans cannot be developed until after the 15 transaction is approved. Again, *we'll let you know after the merger has been* 16 *approved*. To demonstrate this point, I developed Exhibit Joint CLECs 1.4 which 17 is a table that lists the alleged benefits resulting from the merger claimed by the 18 Companies and matches that list to what the Companies have said about those 19 alleged benefits in discovery responses. In each instance, there is no substance 20 supporting the alleged benefit. By way of example, despite repeated claims about 21 benefits related to broadband and IPTV deployment as a result of the merger,[87]

[87] See, *e.g.*, Joint Application at pp. 23, 10, and 12.

1 when asked about its post-merger plans, CenturyLink was unable to provide any
2 details (*i.e.*, no plans for rollout, no projection, no timeline) and, in fact,
3 CenturyLink explained that it does not even know whether the Qwest network is
4 currently capable of supporting the advanced services deployment that
5 CenturyLink has identified as a benefit of the merger.[88] Obviously, if the Qwest
6 network is not capable of providing the advanced services that CenturyLink touts,
7 then the alleged benefit of IPTV/advanced services deployment will not be
8 realized post-transaction (or will be delayed indefinitely while the necessary
9 upgrades can be made – a likely scenario given that the Merged Company will be
10 focused on integration efforts and debt reduction post-merger). My Exhibit Joint
11 CLECs 1.4 shows the same results for other alleged benefits, including network
12 investment, free cash flow, debt repayment, synergies, improved access to capital,
13 implementation of CenturyLink's go-to-market model, and others. I was unable
14 to locate a single alleged benefit that CenturyLink could substantiate with facts.

15 **Q. WHAT WOULD THE COMPANIES NEED TO SHOW TO**
16 **SUBSTANTIATE THESE BENEFITS?**

17 A. The FCC has applied the following criteria for determining whether a claimed
18 benefit is cognizable:

[88] See my Exhibit Joint CLECs 1.4 at pp. 1-4, and CenturyLink Response to OR UTC Staff Data Request #33, CenturyLink Response to IA OCA Data Request #004A, and CenturyLink response to WA UTC Staff Data Request #52 ("Once the transaction closes, a review of the marketplace will be done to determine needs of the [Oregon, Iowa, Washington] market. This process also includes an assessment of the capabilities of existing Qwest infrastructure necessary to support advanced communications, data, and potentially entertainment services the combined company may chose to rollout in the future…").

1. "the claimed benefit must be transaction or merger specific (i.e., the claimed benefit 'must be likely to be accomplished as a result of the merger but unlikely to be realized by other means that entail fewer anticompetitive effects')."
2. "the claimed benefit must be verifiable," which requires Applicants to "provide sufficient evidence supporting each claimed benefit…" and allows discounting of "benefits that are to occur only in the distant future…because…predictions about the more distant future are inherently more speculative than predictions about events that are expected to occur closer to the present" and
3. "marginal cost reductions [are more cognizable] than reductions in fixed cost" because "reductions in marginal cost are more likely to result in lower prices for consumers."[89]

Q. DO THE COMPANIES' ALLEGED BENEFITS MEET THESE CRITERIA?

A. No. None of the alleged benefits is "verifiable" because no evidence was provided to support the benefits; rather, the Companies make unsupported predictions about what may transpire in the distant future. To the contrary, the available evidence casts doubt on whether the alleged benefits will actually be realized. The alleged benefits also fail to satisfy the FCC's three-part criteria for other reasons. For example, the alleged benefit of broadband deployment does not meet the first prong (merger specific). Legacy Qwest has deployed broadband to 86% of its customers.[90] To expand this deployment, Qwest filed an application in March, 2010, for a federal stimulus grant from the Broadband Initiatives Program (BIP) "to extend broadband at speeds of 12 to 40 Mbps to rural communities throughout its local service region." Qwest has stated that "[t]he

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[89] *In the Matter of Applications Filed for the Transfer of Control of Embarq Corporation to CenturyTel, Inc.*, WC Docket No. 08-238, Memorandum Opinion and Order, released June 25, 2009 ("*CenturyTel/Embarq Merger Order*"), at ¶ 35.

[90] Integra, et al., Comments, WC Docket No. 10-110, at p. 67, citing Joint Applicants' FCC Application at 13.

1 Transaction will not have any impact on this request."[91] What this means is that
2 advanced deployment in Qwest's legacy territory is not merger-specific: Qwest is
3 pursuing it independent of the merger. The Communications Workers for
4 America (CWA) agreed with this assessment in their comments to the FCC on the
5 proposed transaction:

> 6 Although the Applicants claim that the proposed merger will result
> 7 in accelerated broadband deployment and increased bandwidth,
> 8 they provide no concrete, verifiable broadband commitments. The
> 9 Applicants do not indicate the number of new households, small
> 10 businesses, or anchor institutions that will have access to
> 11 broadband; the upgraded capacity that will be delivered; nor the
> 12 new markets that will be served with IPTV expansion.[92]

13 When CenturyLink was asked specifically about the third prong – *i.e.*, to identify
14 the marginal cost reductions resulting from the merger, CenturyLink responded:
15 "Those cost savings are not broken out between fixed or marginal cost."[93] As
16 such, it is impossible to tell what portion, if any, of the estimated synergies would
17 result in lower prices for consumers, and in turn, impossible for the Companies to
18 substantiate benefits under the third prong. If the Companies cannot provide
19 reasonable verification that their alleged benefits satisfy the FCC's test, the
20 merger should not be approved.

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[91] See, *e.g.*, Direct Testimony of Mark S. Reynolds, Exhibit MSR-1T, Washington UTC Docket No. UT-100820, May 21, 2010, at p. 10. Qwest described its grant application in more detail in response to Montana Consumer Counsel Data Request 58: "Qwest Corporation's project proposes deployment of High Speed Access within its current 14-state ILEC footprint. Over 500,000 living units (LUs) in [the 14 states] will be served with speeds ranging up to 40 Mbps downstream. About 90% of the LUs proposed for new or upgraded broadband service are in rural areas…And, if funded, the project's $467 M investment will create more than 23,000 jobs for local economies in the 14 states…" Again, this project is being pursued independently of the proposed transaction.

[92] Comments of Communications Workers of America, WC Docket No. 10-110, July 12, 2010, at p. 13.

[93] CenturyLink Response to Integra's Second Set of Information Requests, #55(a).

1 **Q. HAVE THE COMPANIES IDENTIFIED ANY BENEFITS THAT WOULD**
2 **ACCRUE TO CLECS FROM THE MERGER?**

3 A. No. CenturyLink has not identified a single direct benefit that would accrue to
4 CLECs. CenturyLink's Application makes a sweeping statement that it is seeking
5 expedited approval so that "consumer, business, and wholesale customers and
6 shareholders" will all benefit sooner from "the combined firm['s] greater financial
7 strength and flexibility to compete" and "significant economies of scale and
8 scope" it claims the transaction would create – but in no sense does it explain how
9 CLECs would benefit from these alleged changes.[94] To my knowledge, the only
10 place in the instant proceeding where a CenturyLink or Qwest witness discusses
11 benefits to wholesale customers is in the following Q&A from Qwest's witness
12 Mr. Fenn:

> 13 **Q PLEASE SUMMARIZE HOW WHOLESALE CUSTOMERS**
> 14 **WILL BENEFIT FROM THE MERGER TRANSACTION.**
> 15 A. The additional financial resources, combined network capacity and
> 16 geographic reach afforded by the merger will allow the combined
> 17 company to continue to serve the wholesale market as valued
> 18 customers. For example, as the demand for broadband wireless
> 19 services has mushroomed, the need for additional fiber capacity to
> 20 serve cellular tower sites (often referred to as wireless backhaul)
> 21 has increased dramatically. As noted above, Qwest is already
> 22 committing significant resources to serve the increased demand
> 23 from wireless carriers in its region, and the combined entity will
> 24 provide the resources to continue this investment.[95]

25 The first sentence of the answer does not identify any benefit. First, it simply
26 says that the Merged Company will "continue to serve the wholesale market" –

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94 Joint Application at pp. 16-17.

95 Direct Testimony of Jerry Fenn (Qwest), May 27, 2010 ("Fenn Utah Direct (Qwest)"), at pp. 23-24. The Joint Application also makes a passing reference to "deploy additional fiber-to-the-cell-tower capabilities…" at p. 10.

1 something that would occur independently of the proposed transaction. Second,
2 the reference to the size of the Merged Company's footprint ("geographic
3 reach") does not translate to benefits to wholesale customers unless the
4 efficiencies that come along with that larger footprint are realized by the local
5 market as well – such as lower transaction costs across the footprint. The
6 remainder of the answer applies to fiber to cell towers – a claim that, even if
7 substantiated, relates to benefits that would accrue largely, if not solely, to the
8 Merged Company, and not to CLECs.

9 **Q. HAVE CLECS RECEIVED ASSURANCE THAT THEY WILL SHARE IN**
10 **ANY MERGER RELATED SAVINGS?**

11 A. No. Take the larger footprint discussed above as an example. Due to this larger
12 footprint, and associated alleged economies, the Merged Company is expecting
13 $575 million in annual operating cost savings (from such sources as corporate
14 overhead, network and operational efficiencies, IT support, increased purchasing
15 power) and $50 million in annual capital expenditure savings. [96] As a result of
16 these synergies (the realization of which is speculative) the cost-structure of the
17 combined company would decline. This should, in turn, result in lower rates for
18 network elements and interconnection leased by CLECs because these cost-based
19 rates should reflect the reductions in forward-looking costs resulting from the
20 merger-related synergy savings. However, when asked if the Merged Company
21 would adjust its cost-based wholesale rates to reflect these cost savings,
22 CenturyLink replied: "CenturyLink has not evaluated or reached any conclusions

[96] Glover Utah Direct, at p. 11, Fenn Utah Direct (Qwest), at p. 12.

1 concerning this issue at this time…"[97] And without a concrete commitment that
2 allows CLECs to rightfully share in the cost-savings the combined company
3 achieves, this will undoubtedly be very low on CenturyLink's priority list post-
4 transaction. The end result is that the Merged Company will enjoy a cost
5 advantage over its competitors, which is the antithesis of the federal pricing
6 standards for network elements and interconnection.

7 Another example is transaction costs. As the Merged Company integrates its
8 business across its 37 state serving territory, transaction costs for the Merged
9 Company should decrease as its service offerings, practices, systems, etc. become
10 increasingly uniform. By way of example, whereas before the transaction both
11 Qwest and CenturyLink would have negotiated (and potentially arbitrated)
12 interconnection agreements with a CLEC like tw telecom separately, after the
13 transaction, the combined company could negotiate with the CLEC in a unified
14 fashion (similar to how CenturyLink currently negotiates and arbitrates
15 agreements for its separate rural and non-rural affiliates). This lowers the
16 combined company's wholesale transaction costs, and unless this benefit is shared
17 by CLECs, it will create a competitive advantage for the combined company
18 which already enjoys more bargaining power than the CLEC in ICA negotiations.

19 VII. RECOMMENDATIONS AND CONDITIONS

20 Q. WHAT IS YOUR RECOMMENDATION WITH RESPECT TO THE
21 PROPOSED TRANSACTION?

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[97] CenturyLink Response to Integra's Second Set of Information Requests, #55(b).

1 A. I recommend that the Commission deny the merger as proposed. The Companies
2 have not met the "net benefit" public interest standard under Utah law and have
3 failed to materially substantiate the alleged benefits from the merger. However, if
4 the Commission nevertheless approves the merger, it should do so only if the
5 transaction is subject to robust, enforceable conditions to ensure that the proposed
6 transaction ultimately serves the public interest.

7 In addition to the conditions discussed by Mr. Gates, I recommend that the
8 Commission impose the conditions discussed below. (A full set of conditions is
9 provided as Exhibit Joint CLECs 2.8 to Mr. Gates testimony.)

10 *A. Wholesale Service Availability*

11 **Q. PLEASE IDENTIFY THE PROPOSED CONDITIONS RELATING TO**
12 **WHOLESALE SERVICE AVAILABILITY.**

13 A. There are nine conditions in this category – conditions 1, 6, 8, 9, 10, 12, 14 and 28
14 (the numbers correspond to the full list of conditions found in Exhibit Joint
15 CLECs 2.8):

16
17
18
19
- Condition 1 provides that the Merged Company will make available and not discontinue for the Defined Time Period any wholesale service offered to a CLEC at any time between the merger filing date and the closing date (except as approved by the Commission).

20
21
- Condition 6 provides that the Merged Company will assume or take assignment of all obligations under Qwest's "Assumed Agreements"[98] (which

[98] All obligations under Qwest's interconnection agreements, interstate tariffs (including the Annual Incentive contract tariff), and intrastate tariffs, Commercial agreements, and other existing arrangements with wholesale customers ("Assumed Agreements").

includes Qwest's interconnection agreements, Commercial agreements[99] and tariffs) and AFOR plans without requiring the wholesale customer to execute any documents to effectuate the assumption or assignment. Further, this condition also states that the Merged Company shall offer and not terminate or change the rates, terms and conditions under the Assumed Agreements for at least the Defined Time Period (or until the expiration date, whichever is longer) unless requested by the wholesale customer or required by change of law. Finally, this condition also states that the Merged Company will offer Commercial Agreements in CenturyLink legacy ILEC territory at prices no higher and time periods no shorter than those offered in the legacy Qwest territory.

- Condition 8 states that the Merged Company will allow extensions of existing interconnection agreements for at least the Defined Time Period (or expiration date whichever is later).
- Condition 9 states that the Merged Company will allow requesting carriers to use its pre-existing ICA as basis for negotiating a new ICA. For ongoing negotiations, this condition states that the existing negotiations draft will continue to be used for negotiations and that CenturyLink will not substitute negotiations proposals made prior to the closing date with CenturyLink's negotiations template interconnection agreement.
- Condition 10 states that in the CenturyLink ILEC territory, the Merged Company will allow a requesting carrier to opt into any ICA to which Qwest is a party in the same state. In situations in which there is no Qwest ILEC in the state, the condition allows the carrier to opt into any ICA to which Qwest is a party in any state in which it is an ILEC. This condition permits the state Commission to modify the ICA if the Merged Company demonstrates technical infeasibility or that the prices are inconsistent with the TELRIC-based prices in the state in question. This condition also carves out CenturyLink territories that currently operate under a rural exemption, but does not preclude a regulatory body from finding that the rural exemption should cease to exist, and in those instances, the merger condition would apply to those areas.
- Condition 12 states that the Merged Company will not seek to avoid obligations under Assumed Agreements on the grounds that it is not an ILEC. This condition also states that the Merged Company will waive its right to seek rural exemptions.
- Condition 14 states that for the Defined Time Period the Merged Company will not seek to reclassify wire centers or file new forbearance petitions in relation to its obligations under Sections 251 or 271 of the Act.

[99] Commercial" agreements include but are not limited to wholesale metro Ethernet agreements, OCN (SONET) agreements, Local Services Platform (*e.g.*, QLSP) agreements, Dark Fiber agreements, Broadband for Resale agreements, and line sharing agreements.

1 2 3 4 • Condition 28 states that, at the CLEC's option, the Merged Company will interconnect with CLEC at a single point of interconnection per LATA, regardless of whether the merged entity operates in that LATA via multiple operating affiliate companies or a single operating company.

5 **Q. WHY ARE THESE CONDITIONS NECESSARY?**

6 A. The concern underlying these conditions is that the availability of wholesale
7 services should be stable over the foreseeable future to offset the substantial
8 uncertainty and risks of degraded wholesale services associated with the proposed
9 merger, including the risks that stem from the Merged Company's efforts to
10 achieve synergy savings post-merger. These conditions help ensure that the
11 Merged Company does not direct its integration efforts to the detriment of
12 wholesale customers by withdrawing services or significantly changing the
13 offerings Qwest currently makes available.

14 These conditions also recognize that the Merged Company will be a larger carrier
15 with a bigger footprint, possibly resulting in economies and efficiencies, as the
16 Companies claim. To serve the public interest, any such economies and
17 efficiencies should accrue in part to the benefit of captive wholesale customers
18 and the general public as well as the merged company; otherwise, the Merged
19 Company will enjoy an unreasonable cost advantage over its captive
20 customers/competitors. As a result, if the Companies' claims of merger savings
21 are accurate, those savings should decrease the costs associated with providing
22 wholesale services and interconnection to CLECs. Allowing the Merged
23 Company to be the sole beneficiary of the economies and efficiencies resulting
24 from the merger would have an anti-competitive and discriminatory impact on the

1 merged company's captive wholesale customers, who depend on wholesale
2 services from, and interconnection with, the ILEC to compete. Such a result
3 would be inconsistent with the pro-competitive mandate of the Act, FCC orders,
4 and state law, and contrary to the public interest.

5 **Q. THESE CONDITIONS INVOLVE THE MERGED COMPANY**
6 **CONTINUING TO MAKE AVAILABLE WHOLESALE SERVICES THAT**
7 **QWEST CURRENTLY PROVIDES FOR THE DEFINED TIME PERIOD.**
8 **WHY IS THIS WARRANTED?**

9 A. Again, wholesale customers need certainty with regard to the elements and
10 services they purchase from Qwest (or the Merged Company) for business
11 planning purposes, and based on the transaction as filed, there is no such
12 certainty. CLECs cannot simply go elsewhere for the wholesale services they
13 need from Qwest and CenturyLink both now and post-merger, so certainty in this
14 area is absolutely essential.

15 **Q. REGARDING CONDITION 1, WHY IS IT IMPORTANT THAT THE**
16 **MERGED COMPANY CONTINUE TO PROVIDE WHOLESALE**
17 **SERVICES THAT IT PROVIDED ANYTIME BETWEEN THE MERGER**
18 **FILING DATE AND CLOSING DATE?**[100]

[100] "Merger Filing Date" when used in the list of conditions, "refers to May 10, 2010, which is the date on which Qwest and CenturyLink made their merger filing with the FCC." "Closing Date" when used in the list of conditions, "refers to the closing date of the transaction for which the Applicants have sought approval from the Federal Communications Commission (FCC) and state commissions (the 'transaction')."

1 A. The withdrawal of wholesale services after the Filing Date would signal a move
2 toward the Merged Company impeding competition, and in turn, result in a
3 merger-related harm. Even if a condition requires the Merged Company to
4 maintain the wholesale services available at the Closing Date for a period of time,
5 it would not cover the wholesale services that were eliminated between the Filing
6 Date and Closing Date. This concern is based on past experience. One historical
7 example is when Qwest (f/k/a US WEST) attempted to withdraw Centrex (also
8 known as CENTRON in Minnesota) almost simultaneously with the passage of
9 the Telecommunications Act of 1996. The Act was signed into law on February
10 8, 1996. On February 5, 1996, Qwest filed a notice to grandfather and ultimately
11 terminate CENTRON services. After the Minnesota Commission rejected that
12 termination request; Qwest then followed up with a second request to terminate
13 CENTRON on April 30, 1996.[101] Qwest made these filings to withdraw
14 CENTRON despite that Commission's previous finding that "resale of
15 CENTRON under certain conditions is in the public interest…"[102] Yet, in the
16 relatively brief time between passage of the Act in February 2006 and issuance of
17 the FCC's Local Competition Order to implement the local competition
18 provisions of the Act in August 8, 1996, Qwest attempted to withdraw a
19 wholesale service that was found to be in the public interest. Though Qwest was

[101] *In the Matter of the Request of US WEST Communications, Inc.to Grandparent CENTRON Services With Future Discontinuance of CENTRON, CENTREX and Group Use Exchange Services,* Order Denying Petition, Minnesota PUC Docket No. P-421/EM-96-471, February 20, 1997 ("Minnesota CENTRON Order"), at pp. 1-2.

[102] Minnesota CENTRON Order at p. 8.

1 ultimately unsuccessful in Minnesota,[103] competitors were still required to expend
2 substantial time and money combating Qwest's anti-competitive conduct.

3 **Q. WHAT ARE THE KEY COMPONENTS OF CONDITION 6?**

4 A. There are at least two important aspects that I will discuss. First, Condition 6
5 prevents the Merged Company from requiring wholesale customers to execute
6 documents to implement assignment of the obligations of existing Assumed
7 Agreements. Second, this Condition requires the merged company to continue
8 offering the terms and conditions of any Assumed Agreement, including any
9 assumed commercial agreements for a reasonable period of time after the merger,
10 which should be at least as long as the period of synergy savings projected by the
11 Companies.

12 **Q. WHY SHOULD THE MERGED COMPANY BE PROHIBITED FROM**
13 **REQUIRING WHOLESALE CUSTOMERS TO EXECUTE ANY**
14 **DOCUMENTS IN ORDER FOR THE MERGED COMPANY TO TAKE**
15 **RESPONSIBILITY FOR QWEST'S EXISTING ICAS, TARIFFS AND**
16 **AFOR PLANS (CONDITION 6)?**

17 A. First, when asked whether CenturyLink would assume or take assignment of
18 Qwest's obligations under ICAs, tariffs, etc., CenturyLink replied:

> 19 Qwest Corporation does not cease to exist as a result of the parent-
> 20 level Transaction but remains an ILEC, subject to the same terms
> 21 and obligations of its interconnection agreements, tariffs,
> 22 commercial agreements, line sharing agreements, and other

[103] Minnesota CENTRON Order at p. 13.

1 existing arrangements with wholesale customers immediately after
2 the merger as immediately prior to the merger.[104]

3 Since Qwest does not cease to exist as a result of the transaction, there should be
4 no reason for wholesale customers to have to execute additional documents in
5 order for the Merged Company to assume the obligations under the existing
6 wholesale agreements (*e.g.*, ICAs) and tariffs. Second, the transfer of control
7 should be as smooth and seamless as possible, and requiring wholesale customers
8 to receive, review, negotiate and execute documents for this purpose could result
9 in disruption or delay during the transfer of control. And that disruption and
10 delay would be exacerbated if wholesale customers disagree with the terms
11 included in the documents the Merged Company wants wholesale customers to
12 execute, resulting in parties seeking resolution of those disputes before this
13 Commission.[105]

14 **Q. WHY SHOULD THE MERGED COMPANY BE REQUIRED, AS IT**
15 **WOULD BE BY CONDITION 6, TO CONTINUE MAKING QWEST'S**
16 **COMMERCIAL AGREEMENTS AVAILABLE FOR THE DEFINED**
17 **TIME PERIOD FOLLOWING THE MERGER?**

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[104] CenturyLink response to Integra's Second Set of Information Requests, #113(a).

[105] This is not a theoretical concern. For example, in Iowa, the Companies and PAETEC had difficulty agreeing to the terms of the proprietary agreement that would govern the access and use of confidential information in the merger case in that state. Although PAETEC suggested that the parties use a proprietary agreement that had previously been used between Qwest and PAETEC, the Companies insisted on different terms. This caused significant delay in accessing the proprietary information associated with the Companies' discovery responses in Iowa. This delay was particularly burdensome in this instance because the Companies have requested expedited approval of the merger.

1 A. As discussed above, this aspect of Condition 6 is essential to provides certainty
2 and protection for wholesale customers and competition in the face of the
3 uncertainty and risks associated with this proposed merger. Many CLECs have
4 existing Commercial Agreements with Qwest, including agreements for the
5 provision of dark fiber, line sharing or the combined switch platform that used to
6 be known as UNE-P. Those CLECs have built their business plans significantly
7 around the availability of the products provided under those commercial
8 agreements and the specific terms set forth in those agreements. Retail customers
9 in turn receive competitive services based on CLEC access to these wholesale
10 services from Qwest under these commercial agreements. Importantly, these
11 CLECs generally have no alternative to Qwest for the products or services, such
12 as dark fiber or line sharing, provided under these commercial agreements.
13 Condition 6 would provide an assurance to the retail and wholesale customers
14 currently relying on services provided under these commercial agreements that
15 those services will remain available following the merger.

16 CenturyLink does not currently make similar products available under
17 commercial agreements (*e.g.,* dark fiber, line sharing), although it may offer them
18 through grandfathered contracts that are not commercially available to other
19 CLECs. CenturyLink is the acquiring company in this merger. The fact that
20 CenturyLink does not currently make these products commercially available
21 further increases the risk to CLECs that these products will be withdrawn or the
22 terms of their availability materially changed as a result of the merger. Based on
23 the post-merger risks and incentives discussed throughout my testimony, I believe

1 there is a great risk that, without Condition 6, CenturyLink (as the acquiring
2 company) will not assume the obligations of Qwest's Commercial Agreements or
3 will materially change them in a way that would be detrimental to CLECs and
4 competition. This would result in extensive disruption to CLECs who rely on
5 those products. Those CLECs would, in turn, lose their existing customers who
6 purchase the CLEC services that rely on these wholesale products purchased from
7 Qwest. Condition 6 at least minimizes the uncertainty and risk associated with
8 the merger for a defined period.

9 **Q. WILL CONDITION 6 RESULT IN OTHER PUBLIC INTEREST**
10 **BENEFITS?**

11 A. Yes. Condition 6 would result in the Merged Company offering the same
12 commercial agreements at the same rates in CenturyLink's legacy territory as
13 Qwest provides in its legacy territory. The Companies have boasted of the
14 national breadth[106] and local depth of the Merged Company[107] as "key" benefits
15 of the proposed merger. These benefits (or economies) should not accrue only to
16 the Merged Company, however, or else the transaction will further entrench the
17 Merged Company's monopoly position. One way to allow those economies to
18 accrue to the benefit of competition is for the Merged Company to offer the same
19 commercial agreements in legacy CenturyLink territory as it does in legacy Qwest
20 territory.

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[106] Joint Application at p. 15 ("national telecommunications company"); Fenn Utah Direct (Qwest) at pp. 14-15 and 22-23.

[107] Ferkin Utah Direct, at p. 8 ("A key benefit will come from leveraging each company's operational and network strengths, resulting in a company with an impressive national presence and local depth.").

1 CenturyLink's service territory includes 10 of the 14 states in which Qwest
2 operates as a BOC, with more than two hundred adjacent exchanges[108] and more
3 exchanges in close proximity. Once the companies merge, all of these exchanges
4 will be under a single umbrella and there is no reason why commercial
5 agreements from the Merged Company in one exchange should not also be
6 available in the adjacent or neighboring exchange. This would provide
7 consistency across the Merged Company's territory for those carriers who
8 currently operate in both Qwest and CenturyLink territories and may encourage
9 new competitors to enter the legacy territories of CenturyLink or Qwest.

10 **Q. CONDITION 8 WOULD EXTEND EXISTING INTERCONNECTION**
11 **AGREEMENTS (INCLUDING ICAS IN "EVERGREEN" STATUS) FOR**
12 **AT LEAST THE DEFINED TIME PERIOD (OR DATE OF EXPIRATION**
13 **WHICHEVER IS LATER). HAVE OTHER ILECS AGREED TO A**
14 **SIMILAR COMMITMENT TO SECURE MERGER APPROVAL?**

15 A. Yes. A similar provision was offered as a voluntary commitment to the FCC by
16 AT&T and BellSouth.[109] Likewise, a similar condition was adopted by the Illinois
17 Commerce Commission,[110] Public Utilities Commission of Ohio,[111] and Oregon
18 PUC[112] as a condition of the Frontier/Verizon merger. While the time period for

[108] CenturyLink's and Qwest's FCC Application, Exhibit 5, cited at Comments of Joint Commenters, WC Docket No. 10-110, July 12, 2010, at p. 18.

[109] AT&T/BellSouth FCC merger order, Appendix F, "UNEs" commitment #4.

[110] ICC Order No. 09-0268, Conditions Appendix, Condition 5.

[111] 2010 Ohio PUC Lexis 142, *17.

[112] 2010 Ore. PUC LEXIS 64, *141.

1 extension in previous decisions has ranged between 2.5 years and 3 years, the
2 Defined Time Period is tied to the facts of this case.[113]

3 **Q. WHY IS IT IMPORTANT TO REFERENCE "EVERGREEN" ICAS IN**
4 **THIS CONDITION?**

5 A. The reference to "evergreen" ICAs (or ICAs that continue in renewal status past
6 their expiration date) is particularly important in this instance because Qwest
7 currently operates under evergreen ICAs with numerous carriers and has for
8 several years. For example, PAETEC operates under evergreen ICAs with Qwest
9 in all 14 Qwest BOC states. The Qwest/PAETEC ICAs in Minnesota and Iowa
10 have been in place since the 1997-1998 timeframe, and ICAs in other states have
11 been in place since the 1999-2002 timeframe.[114] This means that terms and
12 conditions under these "evergreen" ICAs have been acceptable to both companies
13 for an extended period, and each carrier's respective network configuration
14 (trunking, collocation arrangements, points of interconnection, traffic exchange,
15 etc.) are based on those terms and conditions. Requesting carriers should not be
16 required to endure the disruption and expense to renegotiate and (potentially)
17 arbitrate the terms under which they have operated with Qwest for, in some cases,
18 more than a decade – particularly given that the Merged Company will have its
19 hands full post-merger as it tries to deliver on its synergy savings estimates and
20 integrate the two companies.

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[113] Mr. Gates discusses the "Defined Time Period" in his direct testimony.

[114] See also, Opening Comments of Leap Wireless International, Inc., WC Docket No. 10-110, July 12, 2010, at p. 5 ("Leap's agreements with Qwest have been in this 'evergreen' status for several years, which reflects both parties' satisfaction with the existing ICAs.").

1 **Q. WHAT IS THE CONCERN BEING ADDRESSED BY CONDITION 9?**

2 A. First, a number of CLECs are in the process of negotiating a replacement ICA
3 with Qwest, and have expended considerable time and effort doing so. Those
4 ongoing negotiations should not be disrupted mid-stream with new ILEC
5 proposals from the Merged Company that replace those previously offered by
6 Qwest in negotiations. Accordingly, the Merged Company should continue to
7 honor Qwest's negotiations draft in these ongoing negotiations and not replace it
8 with CenturyLink's new positions. Otherwise, the proposed transaction will
9 directly result in increased costs to CLECs as they may have to negotiate new
10 issues or re-negotiate issues currently closed.

11 Condition 9 also states that the Merged Company will allow a requesting carrier
12 to use its pre-existing ICA, including ICAs entered into with Qwest, as the basis
13 for negotiating a replacement ICA. The existing ICAs between CLECs and
14 Qwest have been approved by state commissions as compliant with federal and
15 state law, sometimes after lengthy and contentious arbitration cases in which
16 considerable amounts of scarce CLEC resources are expended. The CLECs
17 should not have to start this process all over again by negotiating agreements from
18 scratch, particularly because doing so would signal a reluctance on the Merged
19 Company's part to make available the same wholesale offerings Qwest has
20 provided for years. Further, the negotiations template proposal that CenturyLink
21 may introduce is a complete mystery at this point,[115] and CLECs should not be

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[115] See, *e.g.*, CenturyLink response to Integra's Second Set of Information Requests, #114 ("Currently, CenturyLink has separate template agreements for legacy CenturyTel and legacy

1 forced to negotiate from scratch all over again based on what CenturyLink may
2 come up with as its new ICA, going-in negotiations proposal. The same condition
3 was adopted by the Oregon PUC as a condition of the Frontier/Verizon merger.[116]

4 **Q. IS THERE ANOTHER REASON WHY CLECS SHOULD BE ABLE TO**
5 **USE THEIR PRE-EXISTING ICAS WITH QWEST FOR THE BASIS OF**
6 **NEGOTIATING A REPLACEMENT ICA?**

7 A. Yes. As Mr. Gates explains, Qwest's Statement of Generally Available Terms
8 (SGATS) was reviewed during the 271 approval process.[117] These "generally
9 available terms" were incorporated into CLEC ICAs, many of which are part of
10 currently-effective ICAs. For example, the framework, general numbering
11 scheme, and many sections of the current Qwest-Integra interconnection
12 agreement in Minnesota are substantially similar to Qwest's Minnesota SGAT
13 terms.[118] In addition, CLECs have used Qwest's SGAT "as a key source to help

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Embarq companies but is in the process of finalizing a single CenturyLink template for interconnection agreements.") At this point, there is no indication as to what CenturyLink's template agreement may look like once it is finalized.

[116] 2010 Ore. PUC LEXIS 64, 124.

[117] *See, e.g.,* Colorado PUC Evaluation at 26 ("This retelling of bringing Qwest's SGAT into compliance with the 14-point competitive checklist only begins to touch on the volume and breath of issues that arose in Colorado's six SGAT workshops.... After evaluating these six staff workshop reports and the enormous record behind these reports, the [Colorado PUC] concluded Qwest's SGAT complies with the 14-point checklist."); *see also* Idaho PUC Consultation, Exhibit A, at 3 ("The checklist items were addressed in the context of Qwest's SGAT, and so the focus of the workshops was the SGAT terms required to comply with the checklist items. Qwest accordingly has filed the SGAT with the reports showing the terms as they were developed through the workshops and subsequent reports.").

[118] Compare Arbitrated Agreement for Terms and Conditions for Interconnection, Unbundled Network Elements, Ancillary Services, and Resale of Telecommunications Services Provided by Qwest Corp. for Eschelon Telecom of Minnesota, Inc. in the State of Minnesota, Minnesota PUC Docket No. IC-06-768 (10/6/08) with Minnesota SGAT Third Revision, Section 12 (3/17/03).

1 frame interconnection agreement ('ICA') negotiation positions"; "as a resource
2 for attempting to resolve disputes with Qwest such as in billing, carrier relations,
3 and Change Management Process ('CMP') contexts"; and "as an internal
4 resource" to, among other things, confirm state commission-approved terms and
5 filed requirements.[119] By contrast, CenturyLink's interconnection agreement
6 terms were not reviewed under a 271 approval process, but instead, are currently
7 in the process of being developed.[120]

8 **Q. CONDITION 10 ALLOWS CARRIERS IN CENTURYLINK'S LEGACY**
9 **TERRITORY TO OPT INTO QWEST ICAS IN THE SAME STATE.[121]**
10 **WHAT IS THE RATIONALE FOR THIS CONDITION?**

11 A. The same rationale that applies for Condition 6 applies here. The FCC previously
12 adopted a similar condition in conjunction with the AT&T/BellSouth merger,
13 which required AT&T/BellSouth to make available to any CLEC any ICA

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[119] Joint CLEC responses to Staff's First Set of Data Requests, ACC Docket No. T-01051B-08-0613, at 2 (2/18/09).

[120] PAETEC has proposed a condition to the FCC requiring the Merged Company to offer a multistate ICA that extends the Qwest terms and conditions into the CenturyLink ILEC region. See, Comments of Joint Commenters, WC Docket No. 10-110, July 12, 2010, at p. 56. PAETEC made this recommendation to the FCC to reduce the transaction costs associated with Section 252 ICAs with the Merged Company, similar to how the FCC addressed this issue in the GTE/Bell Atlantic Merger. *See*, *In re Application of GTE Corporation and Bell Atlantic Corporation For Consent to Transfer Control of Domestic and International Sections 214 and 310 Authorizations and Application to Transfer Control of a Submarine Cable Landing License,* Memorandum Opinion and Order, CC Docket No. 98-184, FCC-00-221, June 16, 2000 ("FCC GTE/Bell Atlantic Merger Order"), Condition X. This issue is of particular concern regarding the proposed transaction because of the way the Qwest multistate ICA has evolved and the fact that legacy CenturyLink's multistate ICA is still in development (and likely will continue to be under development during the integration process).

[121] CenturyLink's service territory overlaps 10 of the 14 states in which Qwest operates as an ILEC. Under this condition, if there is no Qwest ILEC in the state, the carrier may opt into any ICA in which Qwest is an ILEC in any state.

1 (negotiated or arbitrated) to which a AT&T/BellSouth ILEC is a party in any state
2 within the AT&T 22-state footprint, subject to state-specific pricing and technical
3 feasibility. Notably, the CLEC-proposed condition permits the state commission
4 to modify the ICA before opt in if the Merged Company demonstrates technical
5 infeasibility or if the TELRIC-based prices in the ICA are inconsistent with the
6 TELRIC-based prices in the state in question.

7 **Q. WOULD THIS OPT-IN CONDITION ALLOW CARRIERS TO**
8 **"CHERRY-PICK THE BEST ICA TERMS"[122]?**

9 A. No. This condition does not allow a carrier to pick-and-choose ICA terms.

10 **Q. PLEASE EXPLAIN THE BUSINESS NEED FOR CONDITION 12.**

11 A. There is a material risk that the Merged Company will seek to avoid its
12 obligations as an incumbent LEC under Section 251(c) of the Act post-merger.
13 While CenturyLink has entered into interconnection agreements with requesting
14 carriers, CenturyLink has also expressly reserved the right to invoke the
15 protections of Sections 251 (f)(1) and 251(f)(2) of the Act and thereby avoid its
16 obligations as an incumbent LEC under Section 251(c). For example, in a recent
17 Order approving two CenturyLink interconnection agreements, the Idaho Public
18 Utilities Commission summarized CenturyLink's position as follows:

> 19 [CenturyLink's] Application states that CenturyLink is a "rural
> 20 telephone company," as that term is defined in the Act, 47 U.S.C. §
> 21 153. CenturyLink goes on to state that, pursuant to Section
> 22 251(f)(1) of the Act, it is exempt from Section 251(c) of the Act.
> 23 Notwithstanding that exemption, the companies have agreed and

[122] CenturyLink's and Qwest's Reply Comments, WC Docket No. 10-110, July 27, 2010, at p. 32.

1 entered into this Agreement for purposes of exchanging local
2 traffic. The Company also states that "execution of the Agreement
3 does not in any way constitute a waiver of limitation of
4 CenturyLink's rights under Section 251(f)(1) or 251 (f)(2) of the
5 Act." The Company "expressly reserves the right to assert its right
6 to an exemption or waiver and modification of Section 251 (c) of
7 the Act, in response to other requests for interconnection by CLEC
8 or any other carriers."[123]

9 Condition 12 will ensure that the Merged Company does not pull the rug out from
10 underneath wholesale customers in their relationships with the Merged Company.

11 **Q. PLEASE EXPLAIN THE BUSINESS NEED FOR CONDITION 14.**

12 A. Condition 14 states that the Merged Company will not reclassify as "non-
13 impaired" any wire centers or file any new forbearance petitions related to
14 obligations under sections 251 or 271 of the Act for the Defined Time Period.
15 This condition is needed to provide critical certainty for wholesale customers
16 related to the bottleneck inputs they purchase from the Merged Company, while
17 the Merged Company integrates the two companies and pursues synergy
18 savings.[124] As discussed above, this merger poses a substantial risk to CLECs as
19 the post-merger ILEC's effort to achieve enormous projected synergy savings
20 intersects with the ILEC's inherent disincentive to provide competing CLECs

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[123] *In re Application of CenturyTel of Idaho, Inc. d/b/a CenturyLink for Approval of its Interconnection Agreement with Bullseye Telecom, Inc. Pursuant to* 47 *U.S.* C. § *252(e),* Order No. 31095, Idaho PUC Case Nos. CEN-T-10-01 & CGS-T-10-01, paragraph 1 (adopted May 28, 2010).

[124] Qwest recently withdrew its four pending forbearance petitions relating to the Denver, Minneapolis-St. Paul, Phoenix, and Seattle Metropolitan Statistical Areas, see *In the Matter of Qwest Corporation for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Denver, Minneapolis-St. Paul, Phoenix, and Seattle Metropolitan Statistical Areas -- WC Docket 07-97*, Letter from Hirisha J. Bastiampillai, Senior Attorney, Qwest Corporation, to Marlene H. Dortch, Secretary, FCC, August 18, 2010. While this is a step in the right direction, it does not in itself eliminate the need for Condition 14.

1 with reliable, reasonably priced access to wholesale services. Further, to the
2 extent the merger results in any cost savings through economies of scope and
3 scale, those benefits will accrue to the merging companies and not their captive
4 CLEC customers. The proposed temporary moratorium on non-impairment
5 reclassifications and forbearance will help mitigate the risk this merger poses to
6 the public's interest in competition and provide some measure of public interest
7 benefit to captive wholesale customers and competition. To adequately protect
8 the public's interest in competition, it is essential to provide CLECs with a period
9 of certainty during which the terms and conditions of access to the wholesale
10 inputs they need to provide competitive local exchange services continue.

11 **Q. DOES THE FCC'S RECENT DECISION REJECTING QWEST'S**
12 **FORBEARANCE PETITION IN THE PHOENIX MSA SHOW WHY**
13 **CONDITION 14 IS NEEDED?**

14 A. Yes, in three distinct respects. First, the FCC's June 2010 decision on Qwest's
15 forbearance petition in the Phoenix, Arizona MSA applies a new analytical
16 framework for the evaluation of BOC forbearance petitions, which replaces the
17 approach that the FCC developed in its 2005 decision granting Qwest forbearance
18 in the Omaha MSA, and has applied in subsequent reviews of BOC petitions
19 seeking similar relief.[125] While that new framework appears to be a substantial
20 improvement, its introduction alone will tend to heighten the uncertainty

[125] *In the Matter of Petition of Qwest Corporation for Forbearance Pursuant to 47 U.S.C. §160(c) in the Phoenix, Arizona Metropolitan Statistical Area*, WC Docket No. 09-135, Memorandum Opinion and Order, FCC 10-113, (rel. June 22, 2010) ("*Phoenix Forbearance Order*"), at ¶¶ 16-24.

1 surrounding future forbearance petitions to the FCC, given that the BOCs
2 vigorously pursued previous FCC rejections of their forbearance decisions in the
3 courts,[126] and may well test the new framework in the same way. Adopting
4 Condition 14 for the Defined Time Period would avoid the uncertainty created by
5 these events during that interim period.

6 Second, in the *Phoenix Forbearance Order*, the FCC explains the anti-
7 competitive opportunities that would be created for a dominant ILEC – such as
8 the Merged Company – if Sections 251 and/or 271 obligations were to be
9 eliminated prematurely:

10 …the Commission has long recognized that a vertically integrated
11 firm with market power in one market – here upstream wholesale
12 markets where…Qwest remains dominant – may have the
13 incentive and ability to discriminate against rivals in downstream
14 retail markets or raise rivals' costs…assuming that Qwest is profit-
15 maximizing, we would expect it to exploit its monopoly position as
16 a wholesaler and charge supracompetitive rates, especially given
17 that (absent regulation) Qwest may have the incentive to foreclose
18 competitors from the market altogether.[127]

19 Given that the merger will enhance the Merged Company's incentive and ability
20 to discriminate against rivals in downstream retail markets and/or raise rivals'
21 costs, Condition 14 is needed to ensure that the Merged Company does not act on
22 these anti-competitive incentives, and to avoid the uncertainty (and costs)
23 imposed on wholesale customers when a petition for forbearance is filed.

[126] See, *e.g.*, *Id.*, ¶ 19, describing the D.C. Circuit Court's remands of the FCC's *Verizon 6 MSA Forbearance Order* and *Qwest 4 MSA Forbearance Order* in 2009.

[127] *Phoenix Forbearance Order*, ¶ 34.

1 And third, the justification invoked by the FCC for moving to its new analytical
2 framework shows why Condition 14's temporary moratorium on forbearance
3 petitions is essential to preserve competition during the post-merger transition
4 period. In the *Phoenix Forbearance Order*, the FCC all but declares that the grant
5 of forbearance to Qwest in the Omaha MSA was a mistake, finding that in the
6 *Omaha Forbearance Order* "the Commission eliminated all unbundled loop and
7 transport obligations based largely on predictive judgments…" that were not
8 borne out in the marketplace.[128] In hindsight, the Commission found that the
9 analytical framework applied in the *Omaha Forbearance Order* was seriously
10 flawed in that it was "not supported by current economic theory,"[129]
11 "inappropriately assumed that a duopoly always constitutes effective
12 competition,"[130] and "appears inconsistent with Congress' imposition of
13 unbundling obligations as a tool to open local telephone markets to competition in
14 the 1996 Act."[131] The FCC ultimately concluded that the outcome of that
15 forbearance has been a substantial reduction in competitive activity in the Omaha
16 MSA, as "the record indicates that McLeodUSA has removed most of its
17 employees from the Omaha marketplace, has limited its operations primarily to
18 serving its existing customer base, and has ceased sales of residential and nearly

[128] *Id.*, ¶ 26.
[129] *Id.*, ¶ *28*.
[130] *Id.*, ¶ *29*.
[131] *Id.*, ¶ *32*.

1 all business services in Omaha;" while Integra abandoned its plans to enter the
2 Omaha market after the Commission released the *Omaha Forbearance Order.*[132]

3 **Q. HAVE CLECS SOUGHT TO REVERSE THE FCC'S GRANT OF**
4 **FORBEARANCE IN THE OMAHA MSA IN THE CONTEXT OF THE**
5 **FCC'S CENTURYLINK-QWEST MERGER REVIEW PROCEEDING?**

6 A. Yes. For example, a group of CLECs including Access Point, Inc., Covad
7 Communications Company, and McLeodUSA Telecommunications Services Inc.
8 (among others) has proposed the following condition in their initial comments in
9 the FCC's on-going proceeding to review the CenturyLink-Qwest merger
10 transaction, which were filed jointly with several other CLECs:

> 11 Applicants shall voluntarily stipulate that McLeodUSA's Petition
> 12 for Modification be granted and thereby, relinquish forbearance
> 13 relief obtained in Omaha in WC Docket No. 04-223 and comply
> 14 with Section 251(c)(3) UNE obligations throughout the Omaha
> 15 MSA.[133]

16 Taking this step as a voluntary commitment would be the most efficient way to
17 redress the Omaha situation. While the Commission need not take any action
18 with respect to those CLECs' proposal to the FCC, adoption of Condition 14 by
19 the Commission in the instant case would be compatible with and complementary
20 to that proposal.

21 **Q. PLEASE EXPLAIN THE BUSINESS NEED FOR CONDITION 28.**

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[132] *Id.*, ¶ *34*.

[133] Access Point, Inc., Covad Communications Company *et al.*, Comments of Joint Commenters, July 12, 2010, WC Docket No. 10-110, at p. 67.

1 A. As Mr. Gates explains, increased efficiencies can be gained by establishing a
2 single POI per LATA with the Merged Company. Because those efficiencies will
3 be enjoyed by the Merged Company in part because of its network footprint, the
4 same benefits should flow through to CLECs interconnecting with the Merged
5 Company. Just as the purported financial benefits of the merger should be shared
6 by captive CLECs, as discussed above, any operational benefits of accruing to the
7 Companies should also flow to the CLECs. This would also lower barriers to
8 entry for competitors who would be permitted to capitalize on the increased scale
9 and efficiencies of the Merged Company

10 ***B. Wholesale Rate Stability***

11 **Q. PLEASE IDENTIFY THE PROPOSED CONDITIONS RELATING TO**
12 **WHOLESALE RATE STABILITY.**

13 A. There are three conditions in this category – conditions 2, 3, and 7:

14-16
- Condition 2 states that the Merged Company will not recover or seek to recover through fees paid by CLECs (and hold CLECs harmless from) one-time transfer, branding, or any other transaction-related costs.

17-19
- Condition 3 states that the Merged Company will not recover or seek to recover through fees paid by CLECs (and hold CLECs harmless from) any increases in overall management costs that result from the transaction.

20-29
- Condition 7 states that the Merged Company shall not increase prices for wholesale services above the level at merger announcement, or create new rate elements for functions that are currently recovered in existing rates, for the Defined Term Period. This condition also states that the Merged Company will continue to offer any term and volume discount plan offered at merger announcement (without change) for at least the Defined Time Period, and will honor existing contracts on individualized term pricing plan arrangements for the duration of the term. This condition also states that in the legacy CenturyLink territory the Merged Company will comply with its obligation to provide transit in ICAs and at rates no higher than the cost-based

1 rates approved for Qwest (or the current tandem transit rate, whichever is
2 lower).

3 **Q. WHY ARE THESE CONDITIONS NECESSARY?**

4 A. Just as certainty and consistency for wholesale service availability is critical to
5 offset the uncertainty resulting from the merger, so is stability for wholesale
6 service rates. Wholesale rates should, if anything, decrease after the merger.
7 Because the Merged Company's overall cost structure should decrease to the
8 extent synergy savings are achieved post-merger, wholesale rates – which would
9 be based on the cost structure of the Merged Company – should decrease as well.
10 However, at this point, CLECs are not seeking rate reductions, but instead taking
11 the conservative position that rates should not increase for at least the Defined
12 Time Period (Condition 7). This provides a degree of protection for captive
13 wholesale customers that the Merged Company will not seek to increase their
14 rates (or create new rate elements) during the Merged Company's pursuit of
15 synergies and revenue enhancements.

16 These conditions would also hold wholesale rates harmless from the one-time
17 transaction related costs associated with marrying the two companies – costs that
18 have traditionally not been recovered through wholesale rates. Finally, Condition
19 24 is necessary to prevent the Merged Company from adopting as a "best
20 practice" in Qwest's territory anti-competitive charges assessed in legacy
21 CenturyLink ILEC territory, which are discussed in detail in Mr. Gates'
22 testimony.

1 **Q. REGARDING CONDITIONS 2 AND 3, HAS CENTURYLINK AGREED**
2 **TO HOLD WHOLESALE CUSTOMERS HARMLESS FROM ONE-TIME**
3 **MERGER RELATED COSTS AND INCREASES IN OVERALL**
4 **MANAGEMENT COSTS RESULTING FROM THE MERGER?**

5 A. No. When asked whether CenturyLink would seek to recover through wholesale
6 rates or fees paid by CLECs "any one-time transfer, branding or any other
7 merger-related costs" or "overall management costs," CenturyLink did not
8 provide a straightforward answer. Instead, CenturyLink stated that it would
9 record costs according to FCC Part 32 and would use forward-looking cost studies
10 to develop UNE rates – rates that would include the Merged Company's
11 management cost structure post-merger.[134] CenturyLink's response ignores the
12 issue – *i.e.*, that wholesale customers should not have to pay for any of the costs
13 of the merger and CenturyLink's merging of the two companies. This is
14 especially true since CenturyLink claims there will be almost $700 million in
15 savings associated with the merger. These principles have been recognized in

[134] CenturyLink Responses to Integra Minnesota Data Request Set 2, #97 and #98. To make matters worse, there is uncertainty surrounding what cost models the Merged Company will use post-merger. This, too, is concerning because (a) the market participants in Qwest's region (including my firm QSI Consulting and my CLEC clients) have spent many hours reviewing and understanding Qwest's cost models for wholesale services (which are mostly consistent across Qwest's 14-state region) – work that would be undermined by a decision of the Merged Company to import legacy CenturyLink cost models into Qwest' region post-merger; and (b) I personally reviewed some of CenturyLink legacy cost studies in my prior work for cable CLECs and can say with first-hand knowledge that the sophistication, transparency and auditability of CenturyLink's cost studies is inferior to Qwest's legacy cost studies.

1 numerous previous mergers[135] and the same principle has been applied to retail
2 service rates.[136]

3 **Q. CONDITION 7(A) STATES THAT THE MERGED COMPANY WILL**
4 **CONTINUE TO OFFER ANY TERM AND VOLUME DISCOUNT PLANS**
5 **OFFERED AS OF THE MERGER ANNOUNCEMENT DATE FOR AT**
6 **LEAST THE DEFINED TIME PERIOD. IS THERE AN EXAMPLE**
7 **DEMONSTRATING THE NEED FOR THIS CONDITION?**

8 A. Yes. On April 30, 2010 (after the Merger Announcement Date[137]), Qwest filed a
9 "Product Notification"[138] (with an effective date of June 1, 2010) "to change its
10 Regional Commitment Program (RCP) from a unit based plan to a revenue based
11 plan and raise the commitment level from 90% to 95% of the total Company-
12 provided in-service DS1 and DS3 Revenue."[139] This change was made to the
13 entire 14-state Qwest ILEC territories covered by its Tariff F.C.C. No. 1
14 (interstate access tariff). A RCP is a pricing plan that allows DS1 and/or DS3
15 customers to receive price reductions for committing to a minimum volume on
16 DS1 and/or DS3 circuits for a certain period of time.[140] As of May 31, 2010 (the

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[135] Conditions substantially similar to proposed conditions 2 and 3 were adopted by the Oregon PUC in the Verizon/Frontier merger proceeding.

[136] See, ICC order in Verizon/Frontier merger, and Oregon PUC order in Embarq/CenturyTel merger.

[137] The Merger Announcement Date, when used in this list of conditions, refers to April 21, 2010, which is the date on which Qwest and CenturyLink entered into their merger agreement.

[138] PROD.RESL.04.30.10.F.07809.DS1_DS3_Services

[139] Product Notification: PROD.RESL.04.30.10.F.07809.DS1_DS3_Services, filed April 30, 2010.

[140] Qwest Corporation, Tariff F.C.C. No. 1, 3rd revised page 7-100.

1 day before the effective date of Qwest's Product Notification), the former RCP
2 provisions were no longer available to wholesale customers, and the new, less
3 favorable terms are required going forward.[141] As Integra informed Qwest, these
4 RCP changes "greatly diminish the value of the RCP" by "increasing the risk
5 associated with the plan" and were put in place shortly before "some of these
6 plans are about to expire."[142] I have attached Qwest's Product Notification and
7 Integra's correspondence with Qwest on this issue as Exhibit Joint CLECs 1.5.
8 The point here is that Qwest is taking steps after the Merger Announcement Date
9 and before the Closing Date to raise barriers to entry and enhance its revenues at
10 the expense of wholesale customers, either in terms of degraded services or higher
11 rates. While this is one example, there can be no question that the Companies are
12 geared towards improving the combined company's financial condition, and
13 because it is most profitable for them to boost revenues at the expense of their
14 competitors, there are (and/or will be) likely other similar examples. CenturyLink
15 has stated that "[o]ne of the Transaction's key benefits is the resulting financial
16 condition of the combined company" and a "financially stronger company
17 can…compete against cable telephony providers, wireless carriers, VoIP
18 offerings, and CLECs…"[143] I do not object to robust competition with the
19 Merged Company so long as the competition is fair, but what I do object to in this

[141] Qwest Corporation, Tariff F.C.C. No. 1, 3rd revised page 7-100.

[142] See Exhibit Joint CLECs 1.5. It is my understanding that Integra's current RCP expires in the fall 2011. At that time, the new, less favorable RCP terms put in place by Qwest after the Merger Announcement Date will be the only RCP terms available.

[143] Joint Application at p. 19; for similar statements from Qwest, see Fenn Utah Direct (Qwest), at p. 22.

1 instance (and what this example shows) is the Companies' attempting to hinder
2 the CLECs' ability to compete with the Merged Company before the proposed
3 transaction is even approved. That is why it is important to provide protections
4 for the time period between the Merger Announcement Date and Closing Date as
5 well as for the Defined Time Period.

6 VIII. ADDITIONAL CONSIDERATIONS

7 A. *If the Merger Leads to Lower Costs, Wholesale Prices Should*
8 *Come Down Commensurably with Costs*

9 **Q. IF THE MERGER IS APPROVED, SHOULD WHOLESALE**
10 **CUSTOMERS SHARE THE BENEFITS?**

11 A. Yes. As discussed, mergers are driven by the objective to increase shareholder
12 value, which, if it actually happens, is a good thing, since it balances for
13 shareholders the potential risks and rewards for owning the company. In the
14 telecommunications industry, however, retail competition relies critically on
15 access to the ILECs' wholesale services, as provided for in the
16 Telecommunications Act of 1996. This means that in the telecommunications
17 industry there are other significant stakeholders likely to be impacted by the
18 merger: CLECs and their customers. Given that in this merger CLECs are being
19 subjected to significant risks, standard economic theory suggests that they
20 likewise should be allowed to reap potential benefits. Specifically, to the extent
21 that the merger may generate benefits in terms of lower overall network and

1 overhead costs (due to realized efficiencies), cost reductions should flow through
2 to CLECs in the form of, for example, lower transaction costs in relation to
3 dealing with the Merged Company.

4 **Q. ARE ANY ADDITIONAL SAFEGUARDS APPROPRIATE TO ENSURE**
5 **THAT MERGER-DRIVEN COST REDUCTIONS WOULD FLOW**
6 **THROUGH ON A NON-DISCRIMINATORY BASIS TO ALL**
7 **WHOLESALE CUSTOMERS, RATHER THAN JUST AFFILIATES OF**
8 **THE MERGED COMPANY?**

9 A. Yes. To the extent that UNEs and interconnection are required to be priced at
10 TELRIC, forward-looking cost savings should be reflected in lower UNE and
11 interconnection rates as a matter of law. Similarly, with respect to the pricing of
12 other wholesale products, such as special access services, the Merged Companies
13 should be expected to pass through merger-related cost savings at least in part to
14 their wholesale customers in a nondiscriminatory manner.

15 ***B. A Post-Merger CenturyLink Should Waive Future Claims of***
16 ***Rural Exemptions***

17 **Q. WHAT IS THE RURAL EXEMPTION?**

18 A. The Federal Telecommunications Act of 1996 generally requires all ILECs to
19 interconnect their networks and exchange traffic with other telecommunications
20 carriers (Section 251, Section 252). Section 251(f), however, provisionally
21 exempts rural ILECs from the obligations under Section 251(c) until they receive
22 a bona fide request for interconnection from a telecommunications carrier. Once

1 such a request is made, the exemption may be terminated by a state commission,
2 if the commission finds that certain conditions are satisfied. Specifically, Section
3 251(f)(1) generally states that the state commission shall terminate the rural
4 exemption from the 251(c) obligations if the request: (1) is not unduly
5 burdensome; (2) is technically feasible; and (3) is consistent with universal
6 service policies detailed in section 254 (other than subsections (b)(7) and
7 (c)(1)(D).)

8 Many rural carriers have been hiding behind the rural exemption to avoid
9 competition at the expense of rate payers and the public interest at large. In fact,
10 the FCC has taken note and stated that it will clarify the rural exemption so as to
11 prevent abuse:

> 12 There is evidence that some rural incumbent carriers are resisting
> 13 interconnection with competitive telecommunications carriers,
> 14 claiming that they have no basic obligation to negotiate
> 15 interconnection agreements. […] Without interconnection for voice
> 16 service, a broadband provider, which may partner with a competitive
> 17 telecommunications carrier to offer a voice-video-Internet bundle, is
> 18 unable to capture voice revenues that may be necessary to make
> 19 broadband entry economically viable. Accordingly, to prevent the
> 20 spread of this anticompetitive interpretation of the Act and eliminate a
> 21 barrier to broadband deployment, the FCC should clarify rights and
> 22 obligations regarding interconnection to remove any regulatory
> 23 uncertainty. In particular, the FCC should confirm that all
> 24 telecommunications carriers, including rural carriers, have a duty to
> 25 interconnect their networks.[144]

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[144] FCC's *Connecting America, the National Broadband Plan*, at p. 49.
http://www.broadband.gov/download-plan/

1 **Q. SHOULD THE MERGED COMPANY WAIVE ITS RIGHT TO SEEK**
2 **ANY FURTHER RURAL EXEMPTIONS UNDER SECTION 251(F)(1) OR**
3 **SUSPENSIONS AND MODIFICATIONS UNDER SECTION 251(F)(2)?**
4 A. Yes. The rural exemption is intended for small rural carriers whose economic
5 viability may be threatened if they were obligated to incur costs to implement all
6 the unbundling and resale provisions of the Telecommunications Act of 1996,
7 such as the costs associated with the development of sophisticated OSS. These
8 considerations are not relevant with respect to a post-merger CenturyLink because
9 it will provide service (through its affiliates) in 37 states, thus becoming the third
10 largest ILEC in the country, behind AT&T and Verizon. Surely Congress did not
11 intend to exempt the largest incumbent service providers in the nation from their
12 statutory obligations under Section 251. Hence, I recommend that the Merged
13 Company commit to waive its right to seek the exemption for rural telephone
14 companies under Section 251(f)(1) and its right to seek suspensions and
15 modifications for rural carriers under Section 251(f)(2) of the Communications
16 Act.

17 **Q. THE STATUTE ESTABLISHES A SEPARATE PROCESS FOR STATE**
18 **COMMISSIONS TO TERMINATE A RURAL EXEMPTION. DOES**
19 **YOUR RECOMMENDATION INTERFERE WITH THAT PROCESS?**
20 A. No. The imposition of a condition to waive the rural exemption would not
21 interfere with the existing statutory process for terminating an exemption. That
22 process would remain available for competitors to utilize in individual cases. But
23 note that those cases can substantially increase competitors' cost of obtaining

1 interconnection with companies like CenturyLink. Given the circumstances of
2 this transaction, and the fact that CenturyLink will become the third largest ILEC
3 in the nation, it is appropriate to predicate approval of the transaction on
4 Condition 12.

5 **Q. ARE YOU AWARE OF ANY CIRCUMSTANCES IN WHICH A**
6 **COMPANY HAS WAIVED ITS RURAL EXEMPTION, AS YOU HAVE**
7 **RECOMMENDED?**

8 A. Yes. In fact, CenturyLink has recently waived, at least partially, certain
9 protections from the rural exemption in Oregon in order to negotiate a formal
10 interconnection agreement with another carrier. The Oregon PUC determined
11 that federal law, including the statutory process for terminating an exemption,
12 does not preclude a carrier's ability to waive the rural exemption.[145] The Oregon
13 PUC cited state commission decisions in Washington and North Carolina as
14 support for its findings.[146] Notably, the Oregon PUC also cited as support for its
15 conclusion that waivers are permissible the fact that transaction costs associated
16 with a rural exemption termination proceeding can be quite burdensome on the
17 parties, and the state commission. The order explains: "The administrative
18 burden on a state commission and the parties involved in a section 251(f)(1)(B)

[145] *See In the Matter of Western Radio Services Company Request for Interconnection Agreement of CenturyTel of Eastern Oregon, Inc*., Order Answering Certified Questions, ARB 864, 2009 Ore. PUC LEXIS 421 at **18-23, (Ore. PUC Dec. 14, 2009).

[146] *Id*. at 19.

1 proceeding relieved by a voluntary waiver is significant and should not be
2 ignored."[147]

3 ## IX. SUMMARY AND CONCLUSION

4 **Q. PLEASE SUMMARIZE YOUR TESTIMONY AND STATE YOUR**
5 **CONCLUSIONS.**

6 A. In this testimony, I have discussed the troublesome history of mergers and
7 demonstrated that the Commission should prepare for the possibility that this
8 merger, like many others, could fail or otherwise create havoc for the industry.
9 Based upon the serious risks to the public interest inherent in this merger
10 proposal, I recommend that the Commission reject the proposed transaction. In
11 the event that the Commission nevertheless decides to approve it, I recommend
12 that the Commission require the Companies to agree to certain conditions and
13 commitments necessary to protect CLECs and the competitive process. To that
14 purpose, I have identified and discussed specific conditions and commitments that
15 should be required of CenturyLink and Qwest as prerequisites for the merger
16 approval. (A complete list is provided by Mr. Gates in his testimony.)

17 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

18 A. Yes, it does.

[147] *Id*. at 19-20.