DoD/FEA Exhibit 1

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

CHARLES W. KING

On Behalf of
THE DEPARTMENT OF DEFENSE
And
ALL OTHER FEDERAL EXECUTIVE AGENCIES

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1 **DIRECT TESTIMONY OF**

2 **CHARLES W. KING**

3 **QUALIFICATIONS**

4 **Q. PLEASE STATE YOUR NAME, POSITION AND BUSINESS ADDRESS.**

5 A. My name is Charles W. King. I am President of the economic consulting firm of
6 Snavely King Majoros & O'Connor, Inc. ("Snavely King"). My business address
7 is 1111 14th Street, N.W., Suite 300, Washington, D.C. 20005.

8 **Q. PLEASE DESCRIBE SNAVELY KING.**

9 A. Snavely King, formerly Snavely, King & Associates, Inc., was founded by the
10 late Carl M. Snavely and myself in 1970 to conduct research on a consulting basis
11 into the rates, revenues, costs and economic performance of regulated firms and
12 industries. The firm has a professional staff of 12 economists, accountants,
13 engineers and cost analysts. Most of its work involves the development,
14 preparation and presentation of expert witness testimony before federal and state
15 regulatory agencies. Over the course of its 40-year history, members of the firm
16 have participated in over 1000 proceedings before almost all of the state
17 commissions and all Federal commissions that regulate telecommunications,
18 utilities or transportation industries.

19 **Q. HAVE YOU PREPARED A SUMMARY OF YOUR QUALIFICATIONS**
20 **AND EXPERIENCE?**

21 A. Yes. Attachment A is a summary of my qualifications and experience.

22 **Q. HAVE YOU PREVIOUSLY SUBMITTED TESTIMONY IN**
23 **REGULATORY PROCEEDINGS?**

24 A. Yes. Attachment B is a tabulation of my appearances as an expert witness before
25 state and federal regulatory agencies. It shows that I have testified before the
26 public utility commissions of over 40 states, including Utah, and I have appeared

1 before all federal agencies that regulate telecommunications, utilities,
2 transportation and postal services.

3 **Q. FOR WHOM ARE YOU APPEARING IN THIS PROCEEDING?**

4 I am appearing on behalf of the consumer interests of the Department of Defense
5 ("DoD") and all other Federal Executive Agencies ("FEA") in Utah.
6
7 **<u>INTERESTS OF DoD/FEA</u>**
8
9 **Q. WHY HAS DoD/FEA INTERVENED IN THIS CASE?**
10
11 A. The Department of Defense and all other Federal Executive Agencies have a
12 substantial presence in the State of Utah. Total federal employment in Utah, both
13 civilian and active military, is about 36,000 personnel. Major military facilities
14 include Tooele Army Depot, Dugway Proving Ground, and Hill Air Force Base.
15 In addition, Federal presence also exists at many facilities of the Department of
16 Veterans Affairs, including a Regional Office in Salt Lake City, as well as clinics
17 in Fountain Green, Roosevelt, St. George and other localities. The Forest
18 Service's Intermountain regional headquarters is in Ogden. The U.S. General
19 Services Administration owns 15 Federal buildings, totaling 1.9 million rental
20 square feet and leases more than 1.4 million square feet in 83 buildings in Utah.
21 Federal tenants include the Forest Service, the Bureau of Indian Affairs, the
22 Bureau of Land Management, the Bureau of Reclamation, the Fish and Wildlife
23 Service, the Department of Energy, and the Environmental Protection Agency, in
24 addition to scores of smaller entities.[1]
25
26 This very substantial presence makes DoD/FEA one of the largest users of
27 telecommunications service in the state of Utah. It is important to DoD/FEA that

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[1]DoD/FEA obtains a broad variety of services, and has a wide range of sizes of customer serving sites (including small-business sized offices such as Armed Forces recruiters, Post Offices, as well as USDA Forest Service and Farm Service/Agricultural agents) and number and kind of urban/rural locations throughout the state.

services in the affected exchanges are provided in an efficient manner, at reasonable cost, and with the highest service quality and performance. DoD/FEA is concerned that any change in Qwest's corporate governance be seamless and not degrade retail services, and that CenturyLink be willing and able to offer state-of-the-are retail business services of the nature that DoD/FEA operations require.

Moreover, the DoD/FEA interest goes beyond the locations directly affected by the transition. Where possible, DoD and FEA telecommunications services are procured under contract through competitive bidding procurement. The effectiveness of the competitive procurement process is, of course, dependent upon there being a number of financially strong and technically capable entities that can submit bids. If the proposed transfer is approved, it is important to DoD/FEA that CenturyLink's competitors have the opportunity to access Federal installations on a fair and reasonable basis through CenturyLink facilities and that CenturyLink be able to render service to Federal locations even outside of its service territories. Moreover, CenturyLink itself must be a sophisticated competitive bidder capable of providing the full range of telecommunications services at reasonable costs to the Federal government.

The merged company will also be a wholesale provider of services and facilities to competitive retail telecommunications providers. The service quality performance, the practices, and the operations of that company must support fair and effective competition among carriers in providing services to business customers and the general public in Utah.

Unfortunately, the record of recent telecommunications acquisitions has not been encouraging.

PREVIOUS TELECOMMUNICATIONS ACQUISITIONS

Q. WHAT PREVIOUS TELECOMMUNICATIONS ACQUISITIONS ARE YOU REFERRING TO?

A. Recently, Verizon communications has conducted three major Verizon landline spin-offs to acquiring companies. The first was the acquisition of Verizon's Hawaiian landline assets by The Carlyle Group ("Carlyle"). The second was the purchase of Verizon's northern New England wireline operations by FairPoint Communications ("FairPoint"). The third and most recent was the acquisition Verizon's non-metropolitan operations in 14 states by Frontier Communications.

Q. PLEASE DESCRIBE THE HAWAIIAN TELEPHONE TRANSACTION.

A. The Hawaiian transaction provides a case study of the difficulties that ill-advised telephone company acquisitions can lead to. It was unsuccessful in almost all respects, resulting in severe service degradation to Hawaiians and in the financial failure of the successor company.

In 2004, Verizon sought approval to sell its Hawaiian assets to Carlyle, a private equity enterprise. Carlyle created a new entity, Hawaiian Telcom, Inc. ("HT"), to provide the local exchange services previously offered by Hawaiian Telephone. The applicants in that case stated that after the transition HT "will have the financial fitness and ability to fund the continuing operations of Verizon Hawaii through the revenue generated from the existing and proposed operations."[2] Likewise, the applicants stated that they ". . . acknowledge the importance of ensuring a seamless transition for customers and have conducted a rigorous process to select a world-class systems integrator to replicate the full functionality of the systems currently provided by Verizon."[3] In 2005, the Hawaii Public

[2] Application, Docket No. 04-0140, June 21, 2004, pp. 13-14.
[3] *Id.*, p. 15.

1 Utilities Commission ("HPUC") approved the transfer subject to numerous
2 conditions.[4]
3
4 In its decision approving the sale, the HPUC stated that it would initiate an
5 investigation of HT's service quality approximately six months after HT assumed
6 the back-office operations that Verizon previously provided on a national basis to
7 all of its service territories, including Hawaii. This service quality proceeding,
8 HPUC Docket No. 2006-0400, confirmed that the transition from Verizon was far
9 from seamless or harmless to customers. Although the HPUC has not yet
10 rendered a decision in that proceeding, it is undisputed that for more than a year
11 following the cutover from Verizon's back-office operations, HT was unable to
12 collect data – even manually – as to six service standards for which the HPUC
13 required reports.[5] Thus, the full extent of the problems associated with the
14 transfer could not even be quantified.
15
16 As to the seven service standards for which HT <u>was</u> able to file reports, five dealt
17 with call answering time. HT's ability to answer calls was lacking compared to
18 the experience under Verizon. For example, during the nine months following the
19 cut-over, HT's percent of residential installation and billing office calls answered
20 in 20 seconds ranged from a low of 8.01 percent to a high of 70.37 percent,
21 compared to the objective of 85 percent and Verizon's 2005 percentage of 87.46
22 percent. Likewise, the answering time achieved for business installation and
23 billing office calls following the cut-over ranged from 12.83 percent to 78.82
24 percent compared with the objective of 85 percent and Verizon's achieved rate of
25 88.23 percent.[6] In an effort to repair the damage caused by the non-functioning
26 systems, HT had to replace the contractor working on the transition.[7]
27

[4] Docket No. 04-0140, Decision and Order No. 21696, March 16, 2005.
[5] HT's Post-Hearing Brief, HPUC Docket No. 2006-0400, filed November 9, 2007 at p. 118, note 101. The missing reports included crucial data such as the percent of trouble reports cleared within 24 hours, the percent of installation and repair commitments met and customer trouble reports per 100 lines.
[6] HT's February 15, 2007 Statement of Position, HPUC Docket No 2006-0400, pp. 39-41.
[7] *Id.,* pp. 74-77.

1 HT admitted in its pleadings that service suffered as a result of the transition from
2 Verizon and that it created erroneous bills and was unable to handle adequately
3 incoming calls.[8] HT candidly admitted that "… the cutover did unfortunately
4 create some negative impacts on its customers." [9] Finally, HT agreed with the
5 assessment of the Consumer Advocate that its "… retail customers following
6 cutover experienced long waiting times to reach [its] contact center, extremely
7 slow and long transaction processing times, high levels of fall out, long waiting
8 times to repair, missed or delayed installation and repair commitments and billing
9 errors."[10]
10
11 The cutover from Verizon's back-office operations also caused significant
12 problems for HT's wholesale customers. One Competitive Local Exchange
13 Carrier ("CLEC"), Time Warner Telecom of Hawaii, L.P. ("TWTC"),
14 summarized the problems as follows:

> 15 HT's conversion to its new back office systems was a failure by any
> 16 measure. Immediately following cutover, virtually none of the
> 17 wholesale back office systems were functioning. Today, 19 months
> 18 after cutover, they are still not functioning at the same level as the
> 19 Verizon systems. Although HT has made significant progress in
> 20 addressing its issues, those efforts are not complete.
> 21
> 22 HT violated the Merger Decision and the Stipulation by failing to
> 23 provide the same or similar functionality for wholesale service as
> 24 previously provided by Verizon, and by failing to remain on the
> 25 Verizon systems until HT's new systems were fully tested and
> 26 operational. These violations significantly harmed TWTC and HT's
> 27 other customers. [11]

28
29 In summary, the applicants in the Hawaii sale promised a seamless transition to
30 HT's back-office systems, but the record in that case – including HT's own

[8] *Id.,* pp. 53-57.
[9] HT's August 31, 2007 Final Position Statement, HPUC Docket No. 2006-0400, p. 21.
[10] *Id.,* p. 7.
[11] Time Warner Telecom of Hawaii, L.P., dba Oceanic Communications' Post-hearing Brief, HPUC Docket No. 2006-0400, November 9, 2007, p. 2 (footnote omitted). The text of the brief contains a detailed description of HT's numerous failures in connection with providing wholesale service after acquiring the Verizon exchanges, and the adverse impact that the failures had on Time Warner and its customers. Another CLEC, Pacific LightNet, Inc., filed a Post-hearing Brief asserting that the flawed transfer of operations caused it to incur additional expense to resolve interconnection problems and billing errors.

1 pleadings -- shows that both wholesale and retail customers suffered significantly
2 from the failure of automated systems, dropped calls, long call answering and
3 holding times, billing errors and costly manual efforts to correct the deficiencies.
4 HT was not able to track repair and installation times, so that data for these
5 critical service quality metrics could not even be assessed in determining the
6 adverse effects of the transition to HT's systems.
7
8 On December 1, 2008, HT filed for Chapter 11 bankruptcy protection.[12] The
9 public explanation for the bankruptcy was the impending inability to refinance its
10 debt, but the costs and lost customers resulting from HT's poor service quality
11 probably contributed to the Company's inability to service its debt.
12
13 **Q. PLEASE DESCRIBE VERIZON'S SALE OF NEW ENGLAND**
14 **OPERATIONS TO FAIRPOINT.**
15
16 A At the beginning of 2007, FairPoint was an incumbent local exchange
17 telecommunications company with about 330,000 access lines. In that year,
18 Verizon New England, Inc., FairPoint, and affiliated firms announced a planned
19 $2.4 billion transaction, similar in some respects to that proposed in Utah (but
20 smaller in size), under which FairPoint would obtain Verizon's landline
21 businesses in Maine, New Hampshire and Vermont.
22
23 The proposed transaction was controversial and the implementation of the sale
24 was seriously flawed. In Vermont, for example, the Public Service Board initially
25 denied the application. The petitioners submitted a revised proposal in which
26 they improved the transaction from the standpoint of ratepayers in several ways.
27 The revised proposal bettered FairPoint's financial standing after the acquisition
28 by substantially reducing the initial debt and decreasing dividends. In addition,
29 the proposal was revised to include a Performance Enhancement Plan, which was

[12] See Hawaiian Telcom Communications, Inc., Securities and Exchange Commission Form 8-K filed December 1, 2008, and HT's December 1, 2008 Press Release contained in that filing.

1 designed to prompt more investment and improve service quality by mandating
2 that FairPoint set aside funds when it fails to meet certain specified service
3 standards. Also, FairPoint agreed to an independent monitor of the transition
4 from Verizon's systems to its own, with the objective of making the transition
5 more seamless and further safeguarding consumers.[13]
6
7 The Vermont Public Service Board approved the transfer with additional
8 conditions on February 15, 2008.[14] Following the transaction, there began a series
9 of "cutover" problems that are still not fully resolved. Indeed, service
10 deteriorated to the extent that the Board called for an investigation into whether
11 the Company should be allowed to continue its operations in the state if it cannot
12 overcome its customer service, billing and operational problems.[15]

13 On October 26, 2009, FairPoint announced that it had filed for Chapter 11
14 bankruptcy protection. [16]

15 **Q. HAVE THERE BEEN SERVICE PROBLEMS WITH THE SALE OF**
16 **VERIZON'S EXCHANGES TO FRONTIER COMMUNICATIONS?**

17 A. On May 13, 2009, Frontier Communications and Verizon entered into an
18 Agreement and Plan of Merger (the "Merger Agreement") under which Frontier,
19 through the acquisition of stock, would acquire approximately 4.8 million access
20 lines owned by subsidiaries of Verizon in Arizona, Idaho, Illinois, Indiana,
21 Michigan, Nevada, North Carolina, Ohio, Oregon, South Carolina, Washington,
22 Wisconsin and West Virginia as well as a small number of access lines in
23 California bordering Arizona, Nevada and Oregon. After Federal and state
24 regulatory approvals, the sale was consummated in the spring of 2010 and is so
25 recent that it cannot yet be determined whether this transition will be more

[13] Vermont Public Service Board Docket No. 7270, Order entered February 15, 2008.
[14] *Id.*
[15] Vermont Docket No. 7270 Information Page at http://www.state.vt.us/psb/document/. This testimony has focused on Vermont, but the problems exist in the other states as well. For example, on July 29, 2009, the *Bangor Daily News* reported that the Maine Public Utility Commission refused to waive the financial penalties that FairPoint had incurred for poor service performance.
[16] FairPoint Form 8-K, filed with the Securities and Exchange Commission, October 26, 2009.

successful than the two previous transactions, but there are already disturbing indications.

On July 21, 2010, FiberNet, a competitive local exchange carrier, filed a Petition to Reopen the Frontier/Verizon authorization proceeding in West Virginia. FiberNet cited a number of problems it allegedly experienced when attempting to order wholesale services through the Frontier's operational support system (OSS). FiberNet asserted that the various problems have created delays in providing service to FiberNet customers and increased costs for FiberNet. FiberNet requested that the Commission reopen this matter and direct Frontier to provide an OSS that is functionally equivalent to the system previously provided by Verizon. The West Virginia Public Service Commission has established a complaint proceeding to deal with FiberNet's alleged problems.[17] DoD/FEA Exhibit 2 is a copy of the Commission's Order. It remains to be seen whether the difficulties experienced by FiberNet are discrete to that company or are part of a wider deterioration in service.

Additionally, it appears that the very favorable cost-benefit ratios claimed by Frontier may have begun to unravel. Frontier and Verizon had stated that Frontier expected the fully implemented transaction would yield annual operating expense savings of $500 million.[18] Recently, however, Frontier revealed a significant increase in systems integration costs that cuts into the previously heralded savings:

> While we anticipate that certain expenses will be incurred, such expenses are difficult to estimate accurately, and may exceed current estimates. For example, our estimate of expected 2010 capital expenditures related to integration activities has recently increased from $75 million to $180 million, attributable in large part to costs to be incurred in connection with third-party software licenses necessary to operate the Spinco business after the closing of the merger. Accordingly, the benefits from the merger may be offset by costs incurred or delays in integrating the companies.[19]

[17] West Virginia PSC Order of August 16, 2010 in Case No. 09-0871-T-PC.

[18] Verizon Communications Inc. and Frontier Communications Corp. Application to the Federal Communications Commission, *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), p. 3.

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

Q. WHAT IS THE LESSON FROM THESE PREVIOUS ACQUISITIONS?

A. All of these transactions were described as seamless and of no harm to consumers, much as this transaction in Utah has been described by CenturyLink and Qwest. Events proved otherwise in each case. In view of this history, this Commission must view with great suspicion the Applicants' statements that there will be no impact on customers from the transfer. Indeed, in CenturyLink's Amendment No. 1 to SEC Form S-4, filed July 16, 2010, the company noted many operational risks that it will face after the merger is approved that could adversely impact its service to customers. I have attached an excerpt from this document as DoD/FEA Exhibit 3.

I therefore believe it is important that this Commission establish safeguards to ensure that the difficulties that arose in these previous transactions will not be repeated in Utah.

OBJECTIVE OF THIS INTERVENTION

Q. DO YOU OPPOSE THIS TRANSACTION?

A. Not necessarily. Although I have some reservations which I will discuss, there are a number of features of this transaction that are more promising than those of the previous acquisitions. CenturyLink is a much larger, more experienced and financially healthier company than the Carlyle Group, FairPoint or Frontier. Unlike the previous acquisitions, this transaction is a stock transfer that involves no new debt. So far, the record of CenturyLink's acquisitions has been relatively trouble-free. The combined company will display a much stronger balance sheet relative to that of Qwest at the present time. With appropriate conditions, I believe the merger may be in the public interest.

Q. WHAT, THEN, IS YOUR CONCERN IN THIS PROCEEDING?

A. I am concerned that the transition from Qwest to CenturyLink be as seamless as possible and that there be no rate increases, disruptions, or other service quality losses arising from this transaction. In this testimony, I recommend several conditions that should be imposed on the merged company as part of the approval of the transaction.

These conditions relate to two principal areas of concern to DoD/FEA. The first is the financial stress than may be imposed on the merged company's Utah operations. The second is the maintenance of adequate service quality in the Utah exchanges.

FINANCIAL STRESS ON UTAH OPERATIONS

Q. WHY ARE YOU CONCERNED ABOUT THE FINANCIAL HEALTH OF THE UTAH OPERATIONS?

A. CenturyLink asserts that the merger of its company with Qwest will generate annual synergies of $625 million.[20] These synergies are expected to take the form of reduced corporate overheads, network and operational efficiencies, IT support, increased purchasing power, and the combining of the two companies' advertising and marketing programs.

How many of these synergies will accrue to Utah is open to question. Certainly, there will be no synergies from combining operations in Utah because CenturyLink currently has no presence in the state. The Application is emphatic that Qwest will continue to operate exactly as it does now, so that subscribers will see no difference in the services following the transaction relative to the present.

[20] Testimony of Jeff Glover, Exhibit GCB-1, p. 13.

1 If so, then the greatest benefits of the synergies will be found elsewhere,
2 presumably in those states where both CenturyLink and Qwest operate.
3
4 Moreover, CenturyLink's emphasis on "go to market" local control of its
5 operations[21] suggests that corporate consolidation will have little effect in Utah.
6 If control is to be devolved to the regional offices, how can there be much benefit
7 from combining two national companies?
8
9 What is likely to affect Utah is the cost of the synergies. The Applicants estimate
10 that there will be one-time operating costs of $650 to $850 million to achieve the
11 planned synergies nationwide. On top of that an additional $150 to $200 million
12 in capital costs will be required.[22] These costs will be incurred before the benefits
13 of the synergies are felt, so that they represent a net new requirement for funds.
14 Left unstated is where the money for these transition costs will come from.
15
16 It is possible that some of the money might come from new bond and stock issues,
17 but there are downsides to these sources of funds. At present, CenturyLink is
18 rated by S&P just above the critical BBB- rating that qualifies its bonds for
19 "investment grade," meaning that fiduciary funds, such as pension funds can buy
20 the bonds. Qwest is rated just below that threshold. The combined company will
21 thus be on the cusp of investment grade bond ratings. Any substantial increase in
22 debt would push the company below that important threshold, eliminating a
23 portion of its potential bond market and possibly increasing its interest costs.
24 Furthermore, additional stock sales would dilute the value of the existing shares,
25 depriving the stockholders of the full promised benefits of the merger. It is
26 therefore likely that the Company will avoid these financing sources if it can find
27 the needed funds elsewhere.
28

[21] See Testimony of Jeremy Ferkin, pp. 17-19.
[22] Testimony of Jeff Glover, Exhibit GCB-1, p. 13.

An important source of funds elsewhere will be the company's customers, and that is the source of my concern. Utah presents the unfortunate condition where the opportunities for synergy benefits are limited, but the need to raise synergy capital will be fully felt. As an alternative to bond or stock sales, CenturyLink may look to its local operations, including those in Utah, to meet the urgent requirement to increase revenue.

Q. WHERE MIGHT THE MERGED COMPANY FIND ADDITIONAL REVENUE IN UTAH?

A. Qwest has broadly three markets in Utah, residential, small commercial and large "enterprise" commercial. The Company's ability to extract additional revenue from these markets varies considerably.

The principal constraint on revenue generation in the residential market is the cost of alternative wireless telephone service, which neither Qwest nor CenturyLink can provide. According to the FCC's statistical reports, there are currently more wireless than wireline subscriptions in Utah. The most promising approach for Qwest to preserve and expand revenue in the residential market is to offer bundles of services: "triple play" telephone, cable TV and Internet access, or even "quadruple play" with the addition of wireless service from other providers. In light of the fierce competition for these services, it is unlikely that Qwest could sustain significant rate increases either for its residential wireline service or its residential multi-service bundles.

Small business wireline service is another matter. Businesses require fixed telephone access with publicly available number identification. They may use wireless in addition to wireline, and they may use VoIP for long-distance service, but they are still heavily dependent on the conventional telephone, at least for inbound local access. Cable TV companies that offer telephone services over their facilities do not have the same marketing advantage for business users

1 because businesses are usually not interested in broadcast television capabilities at
2 the workplace. Therefore, while Cable TV companies market heavily to
3 businesses, they are somewhat less of a competitive threat than in the residential
4 market. In recent years, Competitive Local Exchange Carriers ("CLECs")
5 provided some competition, but that competition is shrinking, as demonstrated by
6 the following table:

Wireline Service in Utah

Date	ILEC Lines	CLEC Lines	Total Lines	CLEC Share
31-Dec-02	1,075,061	194,352	1,269,413	15.3 %
31-Dec-03	993,796	241,454	1,235,250	19.5 %
31-Dec-04	923,458	286,966	1,210,424	23.7 %
31-Dec-05	924,423	260,478	1,184,901	22.0 %
31-Dec-06	894,463	244,772	1,139,235	21.5 %
31-Dec-07	843,787	211,581	1,055,368	20.0 %
31-Dec-08	776,000	134,000	910,000	14.7 %

7
8 Source: FCC Reports on Local Competition
9
10 From these indications, I suspect that the merged company will probably seek
11 additional revenues from the small business market. That additional revenue is
12 likely to take the form of unilateral rate increases.
13
14 The "enterprise" market is the most competitive of the three major segments of
15 wireline telephone market. Most services in this category are procured through
16 competitive bidding and the prices paid are generally subject to contract and not
17 publicly disclosed. Even if the prices were publicly identified, they would likely
18 not be comparable to price list services because so much of enterprise service
19 comes in the form of "bundles" of service elements.
20
21 But enterprise service does not exist in a vacuum. The ultimate ceiling on any
22 competitive bid is the price that would be paid if the same services were
23 purchased from the carrier's public price list. When the public prices increase,
24 that ceiling increases, providing more headroom for the competitors to increase

their bids. Thus, even though enterprise customers can solicit competing bids, they still may experience an upward shift in those bids when the list prices for basic business services increase.

Based on the foregoing, I believe that basic business services are most susceptible to unilateral rate increases motivated by the need to raise revenue to implement the merger.

Q. IS IT IN THE PUBLIC INTEREST FOR THE MERGED COMPANY TO EXTRACT UNILATERAL RATE INCREASES IN THE UTAH MARKETS TO FUND THE MERGER?

A. No. This transaction is in the public interest only if the public is no worse off with the merger than without it. If the merged company increases its rates unilaterally to fund the merger, then its customers would have been better off if the merger had never taken place. This is particularly true in Utah where, as I have noted at pages 11-12, above, the alleged benefits of the merger are somewhat problematic.

Q. WHAT IS THE RESOLUTION OF THIS PROBLEM?

A. The resolution is to impose a temporary price cap on basic business services to be effective until the synergies of the merger begin to be realized. By then, the need for additional revenue to fund the transition will have abated.

Q. WHAT BASIC BUSINESS SERVICE PRICES SHOULD BE CAPPED?

A. The basic business service rates that should be capped are single and multiple line business rates, PBX and Centrex charges, and the rates for special access services.

1 **Q. HOW LONG SHOULD THIS TEMPORARY PRICE CAP REGIME**
2 **LAST?**
3
4 A. The best way to determine the duration of the integration from two companies to
5 one is to examine the absorption of the Embarq into CenturyLink.[23] The Embarq
6 merger was formally authorized in the middle of 2009, and CenturyLink reports
7 that at present about a quarter of the Embarq's lines have been integrated into its
8 systems. It predicts that all lines will be fully integrated by the third quarter of
9 2011.[24] That is a period of two years.
10
11 Qwest is a much larger company than Embarq, so it is likely that the integration
12 will take somewhat longer. I therefore recommend that the price caps should
13 extend for three years after the consummation of the merger.

14 **Q. WON'T COMPETITION CONSTRAIN THE COMPANY'S ABILITY TO**
15 **RAISE RATES UNILATERALLY?**

16 A. To some extent competition will constrain the merged company's ability to raise
17 prices unilaterally, but no one knows the extent of that constraint. I suspect that
18 there are niches in business markets where Qwest's successor company can exert
19 sufficient market power to allow it to raise prices without major market share
20 losses. It is to guard against this possibility that I make the foregoing
21 recommendation to impose price caps on basic business services.
22
23 **Q. ARE YOU PROPOSING TO REIMPOSE RATE REGULATION?**
24
25 A. No. I am suggesting a condition that will ensure that end-users of the merged
26 company's services will be no worse off for the merger having been
27 consummated. As noted earlier, the absence of harm to the public is a necessary

[23] Embarq was the spinoff of Sprint's wireline services. On July 1, 2009, Embarq was acquired by CenturyTel, which then changed its name to CenturyLink. See Testimony of Jeremy Ferkin, pp. 16-17.
[24] *Id.*

requirement to a finding that the transaction is in the public interest. My proposal is for a price cap only on a handful of basic services, not a regulation of rates.

SERVICE QUALITY CONCERNS

Q. WHY ARE YOU CONCERNED ABOUT THE SERVICE QUALITY RESULTING FROM THIS TRANSACTION?

A. As noted earlier in my testimony, several recent large wireline acquisitions have resulted in severe service quality degradation. I am concerned that this pattern not be repeated in Utah following the acquisition of Qwest by CenturyLink. This concern is amplified by the service quality indicators published by the Federal Communications Commission ("FCC") that are recorded in DoD/FEA Exhibit 4 attached to this testimony. In every case but one, CenturyLink scores no better or worse than Qwest. These comparisons do not bode well for the service quality that can be expected following the transfer of Qwest to CenturyLink ownership, for two reasons.

The first reason has already been noted: the pressure to finance the implementation of the merger. While revenue enhancement may be one source of the funds for the merger implementation, another source could be cost cutting in the form of reduced resources, including capital investment and the manpower devoted to plant maintenance and customer service. Obviously, this kind of cost cutting would lead to a deterioration of service performance.

The other reason for concern is the incompatibility of the Qwest and CenturyLink operating support systems. CenturyLink has no existing operations in Utah and will be entering the state for the first time. CenturyLink will be operating with previous employees of Qwest, as well as Qwest's protocols and Information Technology systems with which CenturyLink's management and staff will have had little experience.

1 **Q. THE APPLICANTS STATE EMPHATICALLY THAT QWEST WILL**
2 **CONTINUE TO OPERATE AS IT DOES NOW, SO WHY ARE YOU**
3 **CONCERNED?**

4 A. While the corporate entity Qwest will continue, the Applicants' claimed network
5 and operational synergies can only be realized through the integration of Qwest's
6 operations support systems with those of CenturyLink. Certainly that is the
7 pattern being followed by CenturyLink in its integration of Embarq's operations
8 into its own. Qwest's billing, operating and customer service systems are not the
9 same as CenturyLink's, and if CenturyLink is to have uniform systems
10 nationwide, it will eventually have to cut all protocols over to a common format.
11 As I have noted, in previous cases this cutover has proved to be difficult, costly
12 and highly disruptive to both retail and wholesale customers.

13 For these reasons, it is important for the Utah Commission to maintain close
14 surveillance over CenturyLink's service performance. To be a deterrent against
15 service degradation, the Commission should monitor the merged company's
16 service performance and be prepared to react quickly, if need be by imposing
17 sanctions if service quality deteriorates.

18 **Q. DOES THE UTAH COMMISSION CURRENTLY HAVE QUALITY**
19 **STANDARDS FOR TELECOMMUNICATIONS SERVICE?**
20

21 A. Yes. Section R746-340-8 of the Utah Administrative Code specifies a number of
22 rules regarding service quality for incumbent telecommunications carriers. For
23 example, a local exchange carrier must complete 95 percent of all new, transfer
24 and change orders within three business days on a wire center basis. It must repair
25 85 percent of all out-of-service troubles in one business day on a wire center
26 basis. Failure to meet installation or repair commitments made to a customer
27 results in an automatic $10 credit for a residential customer and $40 for a
28 business customer. A carrier must correct all billing errors within one week and
29 ensure that calls to all business offices experience no more than a 35-second
30 queue time on average.

1
2 **Q. ARE THESE STANDARDS ADEQUATE FOR PURPOSES OF**
3 **MAINTAINING HIGH SERVICE QUALITY?**
4
5 A. I believe they are. My one concern relates to the reporting of the service quality
6 metrics listed in section R746-340-8. They are currently recorded each month but
7 reported to the Commission only quarterly. This arrangement builds in a delay of
8 several months between the time the service performance falls below any standard
9 and the time that failure is known to the Commission. Further delays may be
10 encountered in prescribing and enforcing remedial action.
11
12 In light of the possibility of service deterioration resulting from the merger, I
13 recommend that the merged company's metrics be reported to the Commission on
14 a monthly basis for the first three years following the consummation of the
15 merger. This recommendation imposes no hardship on the company because it
16 already records the metrics on a monthly basis.
17
18 If there is a general degradation of service, the Commission should require
19 CenturyLink to take immediate ameliorative action. If these actions do not
20 resolve the problems, the Commission should consider the imposition of direct
21 sanctions.
22
23 **Q. DO YOU HAVE ANY OTHER CONCERNS REGARDING SERVICE**
24 **QUALITY?**
25
26 A. Yes. Section R746-340-8 contains a provision whereby a carrier can be exempted
27 from the service standards if it can demonstrate that sufficient competition exists
28 to allow operation of the market to assure adequate user service quality. In light
29 of the concerns I have expressed, I recommend that any such application by the
30 merged company be rejected if it is filed within three years of the consummation
31 of the merger.

SUMMARY OF RECOMMENDATIONS

Q. PLEASE SUMMARIZE YOUR RECOMMENDATIONS.

A. In this testimony, I have recommended that:

- The Commission should impose a three year cap on single and multiple-line business rates, PBX and Centrex rates, and the rates for special access service,
- The reporting of the merged company's section R746-340-8 metrics for the merged company should be increased from quarterly to monthly,
- If there is a general deterioration in service performance, the Commission should require immediate ameliorative action and be prepared to impose direct sanctions for continued poor performance, and
- Any application by the merged company for a waiver from the section R746-340-8 service quality standards should be disallowed during the first three years following the consummation of the merger.

Q. DOES THIS COMPLETE YOUR TESTIMONY?

A. Yes. It does, although I should note that there are some aspects of this transaction that I have not addressed. These include such issues as the likelihood of cost savings from the transaction, the quality and extent of the merged company's broadband services, the extent to which past obligations will affect the new entity, and the wholesale market policies and the interfaces between the Company and its CLEC competitors. My silence on such issues does not mean that they are not important to DoD/FEA or that DoD/FEA will not address them later in this proceeding. [25]

[25] I should also note that the discovery process is not completed. It is possible that further responses may require supplemental testimony.