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Before the
Federal Communications Commission
Washington, DC 20554

DEC 11 2000

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Joint Application by SBC Communications)
Inc., Southwestern Bell Telephone)
Company, and Southwestern Bell)
Communications Services, Inc. d/b/a)
Southwestern Bell Long Distance for)
Authorization Under Section 271 of the)
Communications Act to Provide)
In-region, InterLATA Services in)
Kansas and Oklahoma)

CC Docket No. 00-217

**REPLY COMMENTS OF
Z-TEL COMMUNICATIONS, INC.**

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Dated: December 11, 2000

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Z-Tel Communications, Inc. (“Z-Tel”), by its attorneys, hereby submits its reply comments in response to the Federal Communication Commission’s (“FCC” or “Commission”) Public Notice (DA 00-2414) in the above-captioned proceeding. The Public Notice invites interested parties to respond to the Application of SBC Communications Inc., and its subsidiaries, Southwestern Bell Telephone Company, and Southwestern Bell Communications Services, Inc. d/b/a Southwestern Bell Long Distance (collectively, “Southwestern Bell” or “SWBT”) to provide in-region, interLATA services in Kansas and Oklahoma, pursuant to section 271 of the Communications Act of 1934, as amended (“Act”).

I. INTRODUCTION AND SUMMARY

Z-Tel is a Tampa, Florida-based integrated communications provider that offers bundled packages of local, long distance, and enhanced services to residential customers using the combination of unbundled network elements (“UNEs”) known as the UNE Platform, or “UNE-P.” **As of September 30, 2000, Z-Tel was providing**

integrated local, long distance, and enhanced services to over 250,000 residential consumers. Z-Tel fully expects to provide service to thousands of additional consumers in every state in which Z-Tel has a meaningful opportunity to compete.

By these reply comments, Z-Tel notes its support for the comments filed by AT&T¹ and the Department of Justice (“DOJ”),² and its belief that SWBT has failed to satisfy item two of section 271’s competitive checklist.³ Item two of the competitive checklist mandates that Bell Operating Companies (“BOCs”) provide UNEs in accordance with: (1) the unbundling rules of section 251(c)(3) and (2) the pricing standard of section 252. Southwestern Bell has failed to satisfy either prong of checklist item two.

Southwestern Bell has failed to meet the pricing standards of section 252 for the UNE-P, as evidenced by the tremendous disparity of rates between Kansas and Oklahoma, as well as between those two states and Texas. Although SWBT’s cost of providing UNEs is substantially similar throughout the SWBT five-state region, the rates for identical items vary greatly across Kansas, Oklahoma, and Texas. For example,

¹ Comments of AT&T Corp. in Opposition, *Joint Application by SBC Communications Inc., Southwestern Bell Telephone Company, and Southwestern Bell Communications Services, Inc., d/b/a Southwestern Bell Long Distance for Provision of In-Region, InterLATA Services in Kansas and Oklahoma*, CC Docket No. 00-217 (November 15, 2000) (“AT&T Comments”).

² Evaluation of the United States Department of Justice, *Joint Application by SBC Communications Inc., Southwestern Bell Telephone Company, and Southwestern Bell Communications Services, Inc., d/b/a Southwestern Bell Long Distance for Provision of In-Region, InterLATA Services in Kansas and Oklahoma*, CC Docket No. 00-217 (December 4, 2000) (“DOJ Kansas/Oklahoma Evaluation”).

³ 47 U.S.C. §271(c)(2)(B)(ii).

SWBT states that the operations support systems (“OSS”) used to support UNE service in Kansas, Oklahoma, and Texas are virtually identical, yet OSS-related non-recurring charges (“NRCs”) vary widely across these states.⁴ Similarly, the mix of switches used by SWBT across Kansas, Oklahoma, and Texas to provide retail local exchange service is virtually identical, yet the rates for the unbundled local switching (“ULS”) UNE vary substantially across these jurisdictions.⁵ As such, the broad range and vast disparity of rates between these “virtually identical” offerings demonstrates that SWBT is not providing UNEs in accordance with the cost-based rate requirements of section 252.

Perhaps most importantly, neither the Kansas Corporation Commission (“Kansas Commission”) nor the Oklahoma Corporation Commission (“Oklahoma Commission”) has conducted or is likely to conduct a reasonable UNE rate proceeding.⁶ In refusing to do so, the Kansas and Oklahoma Commissions have demonstrated that they lack any meaningful commitment to the Commission’s cost-based pricing rules, contrary to the FCC’s decision in the *Texas Order*.⁷

⁴ See Declaration of George S. Ford on behalf of Z-Tel Communications, at Table 3, attached hereto at Attachment A (“Ford Declaration”).

⁵ See *id.*, at Table 1.

⁶ Indeed, that these state commission have yet to conduct a reasonable UNE rate case in the nearly five years since the passage of the 1996 amendments to the Act.

⁷ *Application by SBC Communications Inc., Southwestern Bell Telephone Company, And Southwestern Bell Communications Services, Inc. d/b/a Southwestern Bell Long Distance Pursuant To Section 271 Of The Telecommunications Act Of 1996 To Provide In-Region, InterLATA Services In Texas*, Memorandum Opinion and Order, CC Docket No 00-65, FCC 00-238, ¶¶ 234-239 (rel. June 30, 2000) (“*Texas Order*”).

Furthermore, Southwestern Bell's use restrictions on UNEs are inconsistent with section 251(c)(3) of the Communications Act ("Act") and the Commission's implementation rules. SWBT's refusal to allow UNE-P carriers to provide intraLATA toll service over UNEs is an impermissible use restriction that violates the plain language of the Act and the FCC's rules. Until such time as Southwestern Bell demonstrates that its rates are consistent with section 252 and ceases to impose impermissible use restrictions, Southwestern Bell cannot satisfy checklist item two, and the Commission must therefore reject Southwestern Bell's application.

In demonstrating that Southwestern Bell's application fails to satisfy section 271, Z-Tel first provides an overview of its product offering and mass-market entry strategy. Next, Z-Tel demonstrates that Southwestern Bell's rates for UNEs are so excessive that they foreclose mass-market entry and are flatly inconsistent with section 252's cost-based pricing standard. Z-Tel then shows that Southwestern Bell's use restrictions on UNEs violate section 251(c)(3) and the Commission's rules.

II. Z-TEL'S PRODUCT OFFERING AND MASS-MARKET ENTRY STRATEGY

Z-Tel's flagship product is known as "Z-Line Home Edition," which consists of a bundled package of local, long distance, and enhanced services, such as voicemail, caller ID, call waiting, "follow me," and Internet features and functions. Z-Tel first began providing a UNE-P-based residential offering in New York during the summer of 1999, and since that time, Z-Tel has entered a number of other states, including California, Georgia, Illinois, Michigan, Maryland, Massachusetts, Pennsylvania, Oregon, and Texas. Z-Tel has established test customers in Alabama,

Arizona, Louisiana, Virginia, and Washington. As of September 30, 2000, Z-Tel had over 250,000 residential customers.

Z-Tel's fundamental business goal is to provide bundled packages of local, long distance, and enhanced services to as many residential customers in as many states as possible. Whether and to what extent Z-Tel enters a state depends on two primary factors: (1) the quality of the OSS provided by the incumbent and (2) the recurring charges and NRCs for UNEs. If the OSS provided by the incumbent can support large volumes of orders and if the rates are reasonable, then Z-Tel will aggressively mass market its Home Edition product to residential customers in that state.

In states in which Z-Tel cannot mass market its residential offering, Z-Tel often establishes a small base of customers to develop practical operational experience with the incumbent. As one example, in Oregon Z-Tel presently provides service to a limited number of customers, but does not actively market its residential product offering. Qwest's OSS has significant problems, and Qwest's UNE rates in Oregon are excessive (*e.g.*, the NRC for migrating a Qwest retail customer to the UNE-P costs over \$300). Z-Tel is working actively in Oregon to encourage Qwest to improve its OSS and lower its UNE rates. Presently, in spite of some significant pricing issues, Z-Tel is able to market its residential service package aggressively in Southwestern Bell's Texas territory and in some other areas, including Verizon's New York and Pennsylvania territories.⁸ In these

⁸ Even in these jurisdictions where market entry is reasonable, significant pricing issues exist. For example, the \$30.30 UNE-P migration charge in Texas is excessive as compared to other states, and even as compared to recent BOC cost studies. *See*, Ford Declaration at Table 3 (comparing UNE-P migration charges across a number of states).

states, the OSS provided by the incumbent is sufficient to support Z-Tel's mass-market offering.

Although Z-Tel is poised to enter the Kansas and Oklahoma residential local exchange markets, Z-Tel can't realistically conduct an aggressive marketing campaign in Kansas or Oklahoma because the rates for the elements comprising the UNE-P are too high to enable Z-Tel to profitably offer a competitive product.⁹ In particular, the rates for ULS and NRCs for UNE-P-related items are excessive, making it cost-prohibitive to enter these states.¹⁰ Z-Tel would buy the exact same items from Southwestern Bell in Kansas, Oklahoma and Texas, however, the prices of these essentially identical items are so disparate that Z-Tel may not economically be able to market its services in Kansas and Oklahoma.

⁹ See generally, Ford Declaration at Tables 1, 2, and 3 (comparing Kansas, Oklahoma, and Texas UNE rates).

¹⁰ *Id.* Moreover, substantial uncertainty exists regarding the status of UNE recurring charges and NRCs in Kansas and Oklahoma. In its rate analysis, Z-Tel has relied on the rates included the Kansas 271 Interconnection Agreement (*i.e.*, the "K2A") and the Oklahoma 271 Interconnection Agreement (*i.e.*, the "O2A"), which SWBT proffers as the best available rates, terms, and conditions for interconnection and access to UNEs. Discounts and interim proposals described in SWBT's application, such as the interim "zero NRC" proposal provide no meaningful benefit to competitors, as the underlying state commission-approved rates are excessive, neither state commission has demonstrated a commitment to this Commission's cost-based pricing rules, and many of SWBT's proposals are subject to retroactive true-up.

III. SOUTHWESTERN BELL'S JOINT APPLICATION FAILS TO SATISFY CHECKLIST ITEM TWO

Item two of the competitive checklist requires Southwestern Bell to demonstrate that it provides “nondiscriminatory access to network elements in accordance with the requirements of section 251(c)(3) and 252(d)(1)” of the Act.¹¹ Section 252(d)(1) sets the pricing standard of UNEs and section 251(c)(3) relates to the provision of those UNEs. To demonstrate compliance with checklist item two, Southwestern Bell relies on its assertion that it has taken the same regulatory steps in the five-state service area that it has taken in Texas.¹² Indeed, “[t]hroughout its five-state service area, SWBT provides access to UNEs under equivalent terms and conditions, and it offers CLECs access to the same OSS.”¹³ Therefore, SWBT asserts, because this Commission found SWBT’s performance in Texas consistent with section 271, SWBT asserts, its provision of UNEs and OSS “are sufficient ... in both Kansas and Oklahoma as well.”¹⁴

Although processes and procedures may be the same, the rates charged are vastly disparate for Kansas, Oklahoma, and Texas. While far from perfect, the rates for

¹¹ 47 U.S.C. § 271(c)(2)(B)(ii).

¹² Southwestern Bell Brief at 19.

¹³ *Id.*

¹⁴ *Id.*

UNE-P in Texas have made mass-market entry possible,¹⁵ the rates for UNE-P in Kansas and Oklahoma have foreclosed, and will continue to foreclose, mass market competition. Southwestern Bell's UNE-P rates in Kansas and Oklahoma simply do not satisfy the cost-based pricing standard of section 252(d)(1), nor do they comply with the Commission's cost-based pricing rules. Z-Tel concurs with DOJ that the FCC should independently determine whether SWBT's rates in Kansas and Oklahoma are properly cost-based.¹⁶

In addition, the use restrictions proposed by SWBT in Kansas and Oklahoma (but not in Texas), prohibiting UNEP carriers from using UNEs to provide IntraLATA toll service, are inconsistent with section 251(c)(3) of the Communications Act. For the aforementioned reasons, and as explained below, Southwestern Bell has failed to satisfy checklist item two, and thus, its Joint Application must be denied.

A. Southwestern Bell's Rates In Kansas And Oklahoma Do Not Satisfy The Cost-Based Pricing Prong Of Checklist Item Two

The pricing prong of checklist item two requires a BOC to demonstrate that it provides UNEs in accordance with section 252(d)(1) of the Act.¹⁷ Pursuant to section 252(d)(1), determinations by a state commission of just and reasonable rates for network elements must be "based on the cost ... of providing ... the network element ...

¹⁵ As noted previously, Z-Tel believes that the current \$30.30 migration NRC in Texas is excessive. In Michigan, an affiliated jurisdiction, the NRC for an identical UNE-P migration is only \$0.35, and BellSouth, in its recent cost filings, has proposed a UNE-P migration charge of only \$0.20. *See* Ford Declaration at Table 3.

¹⁶ DOJ Kansas/Oklahoma Evaluation at 10.

¹⁷ 47 U.S.C. § 271(c)(2)(B)(ii).

and nondiscriminatory [] and may include a reasonable profit.”¹⁸ In the section 271 context, “a BOC must show that its prices for interconnection and unbundled network elements are based on forward-looking, long-run incremental costs” in order to demonstrate compliance with checklist item two.¹⁹ However, Southwestern Bell’s UNE rates fail to satisfy the cost-based pricing standard of section 252(d)(1), largely because the Kansas and Oklahoma Commissions have failed to conduct effective and reasonable UNE cost proceedings.

1. Although the services and service quality provided by Southwestern Bell are essentially identical, the rates in Kansas and Oklahoma are materially higher than in Texas

Southwestern Bell relies heavily on the validity of its Texas application to support its joint application to provide in-region, interLATA services in Kansas and Oklahoma.²⁰ Although the process, procedures, and OSS used by Southwestern Bell in Kansas and Oklahoma may be “materially indistinguishable” from those in Texas, the rates for these “carbon copies” are materially and substantially higher. So much higher, in fact, that Z-Tel cannot mass market its residential product offering in Kansas and Oklahoma. In Z-Tel’s view, Southwestern Bell’s reliance on Texas must run both ways. Just as Southwestern Bell’s Texas performance supports a presumption that Southwestern Bell is providing the UNE-P in accordance with checklist item two, Southwestern Bell’s

¹⁸ 47 U.S.C. § 252(d)(1).

¹⁹ *Application by Bell Atlantic New York for Authorization Under Section 271 of the Communications Act To Provide In-Region, InterLATA Service in the State of New York*, Memorandum Opinion and Order, 15 FCC Rcd 3953, ¶ 237 (1999)(“*New York Order*”), *aff’d*, *AT&T v. FCC*, 220 F.3d 607 (D.C. Cir. 2000).

²⁰ *See, e.g.*, Southwestern Bell Brief at 18-19.

Texas rates support a presumption that the rates in Kansas and Oklahoma for the UNE-P are inconsistent with checklist item two.

The UNE charges in the five-state region that SWBT partly relies upon to bolster its position are expected to only vary minimally from state to state.²¹ However, when comparing NRCs across Kansas, Oklahoma, and Texas, for example, rate disparities are striking. Indeed, for some services the cost in Oklahoma is 13 times greater than that for the same service, by the same company, utilizing the same OSS in Texas.²² Southwestern Bell's application makes no assertion that its forward-looking cost of providing UNEs is any different in Kansas, Oklahoma, or Texas. Southwestern Bell has not done so, and cannot do so, because Southwestern Bell acts as a single entity when it borrows money, buys equipment, and deploys computer systems, such as the "carbon copy" OSS available in Kansas, Oklahoma, and Texas.

The Commission should not let Southwestern Bell have it both ways. Until such time that the rates for materially-similar services are priced similarly and the excessively high UNE rates are addressed, the Commission should deny Southwestern Bell's Application to provide in-region, interLATA services in Kansas and Oklahoma.

²¹ Order Regarding Non-Recurring Charges for Unbundled Network Elements, *In the Matter of the Application of Sprint Communications Company, L.P., United Telephone Company of Kansas, United Telephone Company of Eastern Kansas, United Telephone Company of South Central Kansas, and United Telephone Company of Southeastern Kansas for the Commission to Open a Generic Proceeding on Southwestern Bell Telephone Company's Rates for Interconnection, Unbundled Elements, Transport and Termination, and Resale*, Docket No. 97-SCCC-149-GIT, November 3, 2000 (Attach. 12 to KCC 271 Report) ("KCC NRC Order") at 2.

²² DOJ Kansas/Oklahoma Evaluation at 16. *See also*, Ford Declaration.

2. The Kansas and Oklahoma Commissions failed to conduct a reasonable UNE cost analysis and to demonstrate a “commitment to TELRIC,” consistent with the *New York* and *Texas Orders*

As noted in the *New York Order*, the Commission will reject an application on pricing grounds “only if basic TELRIC principles are violated or the state commission makes clear errors in factual finding on matters so substantial that the end result falls outside the range that the reasonable application of TELRIC principles would produce.”²³ Similarly, in the *Texas Order*, the Commission declined to take action on numerous SWBT rates on grounds that those rates were interim and the Texas Commission was in the process of conducting a rate case.²⁴ There, the Commission felt secure in supporting interim rates because the Texas Commission had “demonstrated its commitment to [the FCC’s] pricing rules, and provision is made for refunds or true-ups once permanent rates are set.”²⁵

The proceedings in Kansas and Oklahoma provide a stark contrast to the facts presented in the Texas case, and strongly suggest that these state commissions lack a meaningful commitment to the Act’s cost-based pricing standard and the Commission’s pricing rules. SWBT’s UNE rates in Kansas and Oklahoma are neither reasonable, nor in

²³ *New York Order* at ¶ 244 (1999).

²⁴ *Application by SBC Communications Inc., Southwestern Bell Telephone Company, And Southwestern Bell Communications Services, Inc. d/b/a Southwestern Bell Long Distance Pursuant To Section 271 Of The Telecommunications Act Of 1996 To Provide In-Region, InterLATA Services In Texas*, Memorandum Opinion and Order, CC Docket No 00-65, FCC 00-238, ¶¶ 234-239 (rel. June 30, 2000) (“*Texas Order*”). See also, *New York Order*, ¶ 259.

²⁵ *Texas Order*, ¶ 236.

keeping with the Commission's cost-based rate standards, and the Kansas and Oklahoma Commissions have disregarded for the FCC's pricing standards and TELRIC. In keeping with the Commission's position in the *New York* and *Texas Orders*, the state commissions' failure to conduct an adequate analysis of UNE rates, or compliance with cost-based pricing, creates a *de facto* obligation on the part of the Commission to make an independent determination of reasonable UNE rates.

Based upon the unexplained disparity of rates between Kansas, Oklahoma, and Texas, it seems apparent that the standards put forth by the Commission for the state regulatory bodies to follow when setting UNE rates was somehow misconstrued or simply ignored. The Oklahoma Commission's record demonstrates its failure to follow TELRIC standards, adopting prices for unbundled elements based upon an arbitration agreement between SWBT and a single CLEC, where the price was simply the middle ground between the parties. Similarly, the Kansas Commission demonstrated a lack of commitment to TELRIC by explicitly adopting a weighted average of the AT&T and SWBT NRC proposals, rather than conducting a cost-based rate proceeding. The detailed standards put forth by the Commission in its rules and in the *New York* and *Texas Orders* do not call for "compromise" pricing, but "cost-based" pricing. As such, the UNE rates adopted by the Kansas and Oklahoma Commissions cannot be accepted by the FCC as valid or reasonable.

For these reasons, the Commission may – and should – act to ensure that Southwestern Bell is providing UNEs at rates consistent with TELRIC prior to any grant of section 271 authority in Kansas or Oklahoma. Any other result would sanction

Southwestern Bell's entry into the in-region, interLATA markets before the Kansas and Oklahoma local exchange mass markets are irreversibly open to competition.

B. Southwestern Bell's Use Restrictions Are Inconsistent With Section 251(c)(3) of the Communications Act And The Commission's Implementing Rules

Southwestern Bell's refusal to permit UNE-P carriers to use UNEs to provide intraLATA toll service in Kansas and Oklahoma constitutes an unlawful use restriction on UNEs.²⁶ Section 251(c)(3) of the Act requires incumbent LECs to provide "nondiscriminatory access to network elements on an unbundled basis at any technically feasible point on rates, terms, and conditions that are just, reasonable, and nondiscriminatory."²⁷ Interpreting this section, the Commission has concluded that "section 251(c)(3) provides that requesting telecommunications carriers may seek access to unbundled network element to provide a 'telecommunications service,' and exchange access and interexchange services [including intraLATA toll services] are telecommunications services."²⁸ Indeed, the FCC has found that this "interpretation of section 251(c)(3) is compelled by the plain language of the 1996 Act."²⁹

²⁶ See letter from Michael B. Hazzard, Counsel to Z-Tel, to Adam McKinney, Counsel to SWBT, dated Dec. 5, 2000, attached hereto as Attachment B.

²⁷ 47 U.S.C. § 251(c)(3).

²⁸ *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-98, First Report and Order, 11 FCC Rcd 15499, ¶ 356 (1996) ("First Report and Order").

²⁹ *Id.*

The Commission's implementing rules follow from the Act's mandate that a telecommunications carrier may use UNEs to provide any telecommunications service, including intraLATA toll service. Section 51.309 of the FCC's rules, in relevant part, provides:

An incumbent LEC shall not impose limitations, restrictions, or requirements on requests for, or the use of, unbundled network elements that would impair the ability of a requesting carrier to offer a telecommunications service in the manner that the requesting telecommunications carrier intends.³⁰

IntraLATA toll service without question is a telecommunications service, and the FCC's implementing rules make clear that competitors, and not incumbents, have the discretion to determine the telecommunications services that are provided over UNEs. In fact, "[t]he only limitation that the statute imposes on the definition of a network element is that it must be 'used in the provision of a telecommunications service.'"³¹ Neither the Act, nor the FCC's rules, permit any other use restriction.

To date, the Commission has not approved a 271 application that incorporates the type of use restriction put forth by SWBT in its joint Kansas and Oklahoma application.³² Z-Tel urges the Commission to not do so now. Approval of Southwestern Bell's Joint Application would be a wholesale sanctioning and affirmation of UNE use restrictions that are in direct opposition to the Commission's rules and orders.

³⁰ 47 C.F.R. § 51.309.

³¹ First Report and Order, ¶ 261.

³² In Texas, the Public Utility Commission has ordered SWBT to provide competitors with the ability to utilize UNEs to provide intraLATA toll service.

IV. CONCLUSION

For the forgoing reasons, the Commission should reject Southwestern Bell's Joint Application.

Respectfully submitted,



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Dated: December 11, 2000

ATTACHMENT A

DECLARATION OF GEORGE S. FORD
ON BEHALF OF
Z-TEL COMMUNICATIONS, INC.

I. Introduction and Qualifications

My name is George Ford. My business address is 601 South Harbour Island Boulevard, Tampa, Florida 33602. I am the Chief Economist of Z-Tel Communications, Inc. ("Z-Tel") a competitive local exchange carrier ("CLEC") that offers competitive local and long distance exchange services to residential consumers.

I received a Ph.D. in Economics from Auburn University in 1994. My graduate work focused on the economics of industrial organization and regulation with course work emphasizing applied price theory and statistics. In 1994, I became an Industry Economist at the Federal Communications Commission ("FCC" or "Commission") in the Competition Division of the Office of the General Counsel. The Competition Division of the FCC was tasked with ensuring that FCC policies were consistent with the goals of promoting competition and deregulation across the communications industries. In 1996, I left the FCC to become a Senior Economist at MCI Worldcom, where I was employed for just over three years. While at MCI Worldcom, I filed declarations and economic studies on a variety of topics with both federal and state regulatory agencies. In addition to my professional experience, I am an Affiliated Scholar with the Auburn Policy Research Center at Auburn University in Alabama. Through this professional relationship, I have maintained an active research agenda on communications issues and have published research papers in a number of academic journals, including the *Journal of Law and Economics*, the *Journal of Regulatory Economics*, and the *Review of Industrial Organization*, among others. I regularly speak at conferences, both at home and abroad, on the economics of telecommunications markets and regulation.

The purpose of this statement is to summarize for the Commission evidence that shows Southwestern Bell Communications ("SBC") fails to satisfy the competitive checklist and, as a consequence, its 271 application for Oklahoma and Kansas should be rejected. This failure of SBC to satisfy the checklist is based simply on the fact that the evidence convincingly shows that SBC's rates for unbundled local switching ("ULS") and the UNE-Platform ("UNE-P") non-recurring charge ("NRC") are both considerably above long-run, forward-looking cost. Further, besides being a transparent attempt to deter entry and protect switched access profits, the use restriction placed on intraLATA toll traffic effectively sets UNE rates infinitely above cost. Based on the Commission's own standard for reviewing 271 applications (discussed below), SBC's application must be rejected. SBC is required to offer UNEs to CLECs at rates consistent with forward-looking, long-run cost - something the company has failed to do thus far.



II. Requirements for 271 Authorization

In its review of numerous prior 271 applications, the Commission has established a general framework for the review of such applications, giving the process a near “cut and paste” consistency. The Commission’s framework for review is governed by the Communication Act of 1934, as amended (“Act”), and in order to obtain authorization to provide in-region, interLATA services under section 271 of the Act, a Bell Operating Company (“BOC”), such as SBC, must show that:

1. it satisfies the requirements of either section 271(c)(1)(A), known as “Track A” or 271(c)(1)(B), known as “Track B”;
2. it has “fully implemented the competitive checklist” or that the statements approved by the state under section 252 satisfy the competitive checklist contained in section 271(c)(2)(B);
3. the requested authorization will be carried out in accordance with the requirements of section 272; and
4. the BOC’s entry into in-region, interLATA market is consistent with the public interest.¹

The 1996 Act specifies that unless the Commission finds that these four criteria have been satisfied, the Commission “shall not approve” the requested authorization.²

As with most statutes, whether or not a BOC satisfies the statutory requirements is subject to some interpretation. As the Commission recognized in the New York Order: “a determination of whether the statutory standard is met is ultimately a judgment we must make based on our expertise in promoting competition in local markets and in telecommunications regulation generally.”³ Further, the Commission stated that this “judgment” is based on “the totality of the circumstances, including the origin and quality of the information before [the Commission] ... [and] an analysis of specific facts and circumstances.”⁴ The scope of the Commission’s judgment, by its own admission, is limited in that “a strong public interest showing can not overcome a failure to demonstrate compliance with one or more checklist items. The Commission is specifically barred from ‘limit[ing] . . . the terms used in the competitive checklist,’ or forbearing from requiring compliance with all statutory conditions under section 271.”⁵

¹ 47 U.S.C. § 271.

² *Id.*

³ *Application by Bell Atlantic New York for Authorization Under Section 271 of the Communications Act To Provide In-Region, InterLATA Service in the State of New York*, Memorandum Opinion and Order, 15 FCC Rcd 3953, ¶ 46 (1999) (“New York Order”), *aff’d*, *AT&T v. FCC*, 220 F.3d 607 (D.C. Cir. 2000).

⁴ *Id.*

⁵ *Id.*, ¶424.

Thus, satisfying all items on the competitive checklist is a necessary, but not sufficient, condition for 271 approval. The Commission, by law, "shall not approve" a 271 application that fails to satisfy a single checklist item. Satisfaction of the checklist is the most robust requirement of the Act and offers the Commission only lean interpretative scope.

The Commission clarified its interpretation of Checklist Item 2 in the New York Order as follows:

Checklist item 2 of section 271 states that a BOC must provide "nondiscriminatory access to network elements in accordance with sections 251(c)(3) and 252(d)(1)" of the Act. Section 251(c)(3) requires local incumbent LECs to provide "nondiscriminatory access to network elements on an unbundled basis at any technically feasible point on rates, terms, and conditions that are just, reasonable, and nondiscriminatory. . . ." Pursuant to section 252(d)(1), determinations by a state commission of just and reasonable rates for network elements shall be "based on the cost . . . of providing . . . the network element . . . and nondiscriminatory [] and may include a reasonable profit." Based on this statutory mandate, the Commission has determined that prices for interconnection and unbundled network elements (or UNEs) must be based on an incumbent LEC's forward-looking, long-run incremental costs for each network element. It adopted a pricing methodology that encompasses these concepts called TELRIC, or Total Element Long Run Incremental Cost. In order to prove compliance with these statutory provisions, a BOC must show that its prices for interconnection and unbundled network elements are based on forward-looking, long-run incremental costs.⁶

My review of the SBC-OK/KS application focuses on the mandate of both the Act and the Commission requiring that access to unbundled elements must be "on rates, terms, and conditions that are just, reasonable, and nondiscriminatory . . ." and that rates be "based on an incumbent LEC's forward-looking, long-run incremental costs for each network element." The evidence, presented in this document, shows that SBC's proposed rate for unbundled local switching ("ULS") in Oklahoma, and the NRCs in both Oklahoma and Kansas fail to satisfy the conditions set forth by the Act and the Commission. The lack of a cost basis for UNE rates requires the Commission to reject the SBC application on the grounds the company fails to satisfy the competitive checklist (specifically, Item 2).

III. SBC's Unbundled Local Switching and Transport Rates

In June of 2000, the Commission approved the 271 application of SBC for the state of Texas. Critical to that decision was the Commission's finding that the UNE rates in Texas were cost-based, where cost is defined by the TELRIC standard set forth by the Commission. If UNE rates in Texas are, in fact, cost-based, then a comparison of the

⁶ *Id.*, ¶237.



proposed UNE rates in Oklahoma and Kansas to those of Texas is a useful exercise. The costs of some UNEs, primarily loops, are expected to vary by geography due to line density, hardness of the soil, aerial/underground cable mix, and so forth. The cost of many other UNEs, including ULS and NRCs, should not meaningfully vary by location. Thus, if large differences in UNE rates across states are observed and the underlying cost of such UNEs is not significantly sensitive to geography, then it is clear that the rates were established under different standards.

Switching costs are a good example of UNE rates that should not vary much by location. As one Bell Company witness recently observed:

Switching does not vary significantly by geographic location. None of the factors that make loop cost vary are present with respect to switching cost calculations. The physical characteristics of the loop and the placing costs associated with that loop vary by geographic location due to cable type (aerial, buried or underground) and distance (length). However, these factors do not impact switching costs to any great degree. Another factor that influences loop costs, customer density, also has little impact on switching costs since the modularity of digital switching equipment allows BellSouth to grow switches as demand dictates. Also, remote switch entities can be deployed to serve pockets of customers.⁷

Likewise, a panel of witnesses for Verizon New York Inc. ("VZ-NY") recently observed in the New York UNE cost that switching costs do not "differ significantly enough between zones on a forward-looking basis to warrant deaveraging."⁸ According to these BOC experts, neither demand nor geological conditions can explain differences among the switching costs. If switching costs do not vary considerably across the various geographic regions of a particular state, there is little reason to believe the cost will vary across state boundaries. Yet, the ULS rates in Oklahoma and Kansas differ considerably from each other and bear no resemblance at all to the ULS rates in Texas.

The ULS rates in Texas, Oklahoma, and Kansas are provided in Table 1. While the End-Office ULS rates in Texas and Kansas are similar (4% difference), the ULS rate in Oklahoma exceeds the Texas ULS rate by 74%. Rate differences for Tandem ULS are off-the-scale. SBC's rate in Oklahoma is 5,211% higher than the rate in Texas. In Kansas, the Tandem ULS rate exceeds the Texas rate by 4,283%. While some minor variation in the costs of providing service may be expected for any UNE, differences exceeding 4,000% for switching elements are difficult to rationalize.

⁷ Testimony of Doanne Caldwell, p. 33, Florida Docket No. 990649-TP (May 1, 2000).

⁸ VZ-NY Panel Cost Testimony, p. 55, New York Case 98-C-1357 (Feb. 20, 2000).



	ULS End Office	ULS Tandem	UNE Transport · 2	UNE Signaling and Database
<i>Texas</i>	0.001351	0.000018	0.00027	0.000018
<i>Oklahoma</i> Relative to Texas	0.0023482 74% higher	0.000956 5,211% higher	0.0032949 1,120% higher	0.0003467 1,826% higher
<i>Kansas</i> Relative to Texas	0.0014104 4% higher	0.000789 4,283% higher	0.0019756 632% higher	0.0002881 1,501% higher

Unbundled switching is rarely purchased alone. Transport and "Signaling and Database" functions are complementary (in near fixed proportions) to ULS. Table 1 summarizes the rates for Transport and Signaling and Database across the three SBC states. As with ULS rates, both End Office and Tandem, the rates are considerably higher (averaging more than a 1,000% difference) in Oklahoma and Kansas for identical UNEs.

	Monthly Costs (2,000 Minutes)	Relative to Texas (%)
Texas	3.18	
Oklahoma	10.97	245%
Kansas	6.81	114%

Assuming 2000 total minutes, 20% intraswitch, 20% of interswitch traffic is Tandem switched, and two pieces of transport are required for each interswitch minute.

The Department of Justice is correct to focus its attention on the entry deterring effects of above-cost MRCs.⁹ When the differences in switching and transport rates are multiplied by the total minutes to which these charges apply, the impact on a CLEC's costs is substantial. As shown in Table 2, assuming an average customer originates and terminates 2,000 minutes per month (roughly one-hour per day), the CLEC's monthly cost (for UNEs listed in Table 1) per Oklahoma customer is three times that of a Texas customer. In Kansas, the monthly costs are over two times larger than in Texas. These overcharges on switching and transport elements amounts to 19% of the average local bill of \$30 and 10% of the \$50 average local and long distance spending.¹⁰ Clearly, the above-cost rates for switching and transport UNEs substantially reduce the CLEC's net revenues per customer and, consequently, reduce the prospects for competition in Oklahoma and Kansas.

⁹ *Evaluation of the United States Department of Justice*, CC Docket No. 00-217 (December 4, 2000).

¹⁰ The average local bill is computed from the Paragren database for the month of May 1999.

IV. NRCs in Oklahoma and Kansas

The NRC is a prototypical sunk cost and, as such, can be a potent barrier to entry. Should the inflated switching and transport costs in Oklahoma and Texas fail to block competitive entry using UNE-P, the UNE-P NRCs in those states ensure the unprofitability of competitive entry.

Table 3. SBC's UNE-P NRCs in Texas, Kansas, and Oklahoma (and other states)

	UNE-P NRC	SBC Retail Installation Charge*
<i>Texas</i>	\$30.30	\$2.5 - 11.00
<i>Oklahoma</i> Relative to Texas	\$50.63 67% higher	\$11 - 17
<i>Kansas</i> Relative to Texas	\$119.43 294% higher	\$6 - 12
New York	3.73	
Pennsylvania	11.00	
Massachusetts	8.08	
Georgia	2.01	
Michigan	0.35	
Florida#	0.20	
Louisiana#	0.20	

* Installation charges as quoted on SBC's web page.
 # BellSouth's proposed rates in ongoing cost proceedings.

As illustrated in Table 3, the UNE-P NRCs in Oklahoma and Kansas substantially exceed the UNE-P NRC in Texas. It is difficult, if not impossible, to justify charging such disparate rates across states for an identical task performed by the same company presumably using the same operational support systems ("OSS"). These large NRCs also are difficult to reconcile with SBC's retail installation charges. First, the NRCs in all three states exceed the retail installation charges by no less than 175% and upwards of 900%. Second, the retail installation charges are higher in Oklahoma than in Kansas (presumably due to cost differences), but the UNE-P NRC is higher in Kansas than in Oklahoma.

That SBC's NRCs are above-cost is readily apparent when compared to other states. The NRC for UNE-P in Michigan is \$0.35 (an SBC state), in New York \$3.73, and BellSouth has recently proposed NRCs for UNE-P of less than \$0.20.¹¹ If the NRCs in other states are reasonable approximations of cost, then it is abundantly clear that SBC's NRCs in Oklahoma and Kansas exceed cost by a substantial amount.

¹¹ Interestingly, the \$0.20 NRCs in Florida and Louisiana are BellSouth's own cost estimates.



V. IntraLATA Use Restriction

An additional shortcoming of the Oklahoma and Kansas application is that SBC, in both states, refuses to allow CLECs to deliver intraLATA traffic using UNEs. While the attorneys no doubt will debate the legality of such a use restriction, the economics of the restriction are compelling. The use restriction for intraLATA toll is a blatant attempt to deter entry and reduce competition by making UNEs less useful or, in this case, useless. By prohibiting the use of UNEs for intraLATA toll traffic, SBC in effect has raised the price for UNEs delivering intraLATA toll traffic to infinity.¹²

The reason SBC refuses to permit UNE-P carrier to provide intraLATA toll over UNEs is transparent. Using UNEs to deliver intraLATA toll is, in effect, a competitive alternative to switched access. In Oklahoma and Kansas, the current intraLATA switched access rates conservatively are about \$0.045 and \$0.025 per minute, respectively.¹³ These rates greatly exceed that of an intraLATA call delivered over UNEs, which is about \$0.008 per minute.¹⁴ In other words, by refusing to deliver intraLATA toll over UNEs, SBC increases its revenues per minute of intraLATA toll by over two cents per minute.

VI. Conclusion

Fourteen residential customers in Oklahoma and zero residential customers in Kansas are served over UNE-P.¹⁵ It appears as if SBC, the OCC, and the KCC together have effectively precluded competitive entry in the residential, local telecommunications market using UNE-P. Due to above-cost MRCs and NRCs, as well as use restrictions aimed at deterring entry, protecting access profits, and effectively pricing UNEs at infinity, SBC fails to satisfy the competitive checklist and its 271 application should be rejected.

¹² The use restriction is more of a service restriction than an element restriction, which strongly contradicts the underlying logic of TELRIC principles. In the context of contemporary UNE policy, it is difficult to even imagine on what grounds the intraLATA use restriction can be justified.

¹³ Rates derived from the access tariffs are available on the SBC web page. The Oklahoma rate includes \$0.03 High Cost Support Fund Surcharge. My estimates are conservative in that I have not included the intrastate access transport rate in my estimates.

¹⁴ I am assuming the rate includes a minute of originating, terminating, and tandem ULS plus two pieces of transport.

¹⁵ See *Evaluation of the United States Department of Justice*, at p. 6 and 9.



This concludes my Declaration.



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December 5, 2000

VIA FACSIMILE (214) 464-1138 AND OVERNIGHT MAIL

Adam McKinney
SBC Communications, Inc.
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Re: SBC Communications, Inc.'s Unlawful Refusal to Permit Competitors to Utilize Unbundled Network Elements to Provide IntraLATA Toll Service

Dear Adam:

The purpose of this letter is to follow-up on our conversation of Thursday, November 30, 2000 during which you informed me that, with the exception of Texas,¹ SBC Communications, Inc. ("SBC") will not permit competitors, including Z-Tel Communications, Inc. ("Z-Tel"), to utilize unbundled network elements ("UNEs") to provide intraLATA toll calls to end users. Instead, SBC requires competitors to send locally-originated intraLATA toll calls to an interexchange carrier for delivery to SBC as access calls, rather than as UNE calls.

SBC's refusal to permit Z-Tel and others to utilize UNEs to deliver intraLATA toll calls to end users constitutes an unlawful use restriction on UNEs. Section 251(c)(3) requires incumbent LECs to provide "nondiscriminatory access to network elements on an unbundled basis at any technically feasible point on rates, terms, and conditions that are just, reasonable, and nondiscriminatory."² Interpreting this section, the Federal Communications Commission ("FCC") has concluded that "section 251(c)(3) provides that requesting telecommunications carriers may seek access to unbundled network element to provide a

¹ In Texas, the Public Utility Commission has ordered SBC to provide competitors with the ability to utilize UNEs to provide intraLATA toll service.

² 47 U.S.C. § 251(c)(3).

Adam McKinney
December 5, 2000

'telecommunications service,' and exchange access and interexchange services [including intraLATA toll services] are telecommunications services."³ Indeed, the FCC has found that this "interpretation of section 251(c)(3) is compelled by the plain language of the 1996 Act."⁴

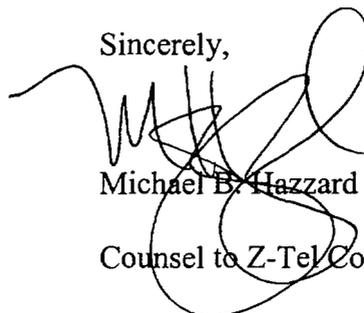
The Commission's implementing rules follow from the Act's mandate that a telecommunications carrier may use UNEs to provide any telecommunications service, including intraLATA toll service. Section 51.309 of the FCC's rules, in relevant part, provides:

An incumbent LEC shall not impose limitations, restrictions, or requirements on requests for, or the use of, unbundled network elements that would impair the ability of a requesting carrier to offer a telecommunications service in the manner that the requesting telecommunications carrier intends.⁵

IntraLATA toll service without question is a telecommunications service, and the FCC's implementing rules make clear that competitors, and not incumbents, have the discretion to determine the telecommunications services that are provided over UNEs.

At bottom, "[t]he only limitation that the statute imposes on the definition of a network element is that it must be 'used in the provision of a telecommunications service.'"⁶ Neither the Act nor the FCC's rules permit any other use restriction. For all of these reasons, Z-Tel respectfully requests that SBC reconsider its unilateral and unlawful restriction on the use of UNEs by competitors to provide intraLATA toll service. If you have any questions or need additional information, please contact me on (202) 887-1209. I look forward to your prompt response.

Sincerely,



Michael B. Hazzard

Counsel to Z-Tel Communications, Inc.

cc: Ron Walters

³ *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-98, First Report and Order, 11 FCC Rcd 15499, ¶ 356 (1996) ("First Report and Order").

⁴ *Id.*

⁵ 47 C.F.R. § 51.309.

⁶ First Report and Order, ¶ 261.

CERTIFICATE OF SERVICE

I, Charles M. Hines III, hereby certify that a true and correct copy of the foregoing "**Comments of Z-Tel Communications, Inc.; CC Docket No. 00-217**" was delivered by courier service this 11th day of December, 2000 to the individuals on the following list:

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