

preemption is warranted under the Supremacy Clause and under Section 253(a) of the Act because (1) the Board's Generic Proceeding rates were set without having a forward looking economic cost study or a generic cost model approved by the FCC; (2) such rates can not be "permanent rates" nor can they be interim rates due to non compliance with Section 51.513(a); (3) the Board's actions are inconsistent with and conflict with the Act, the *Local Competition Order* and FCC regulations; and (4) the Board's Generic Proceeding rates violate Section 51.505(d)(1) of the FCC's Rules.

Comments and reply comments have been filed in the proceeding by interested parties and the matter is awaiting decision by the FCC. To date, the FCC has not issued a decision in this matter.

STANDARD OF REVIEW

The issues on appeal concern questions of law subject to *de novo* review by this Court. The issues involve matters of statutory interpretation and federal preemption for which this Court owes no deference to the district court or to the New Jersey Board of Public Utilities. See *GTE South, Inc. v. Morrison*, 199 F.3d 733 (4th Cir. 1999) (applying a *de novo* standard of review to a district court's affirmance of a state agency's interpretation of 47 U.S.C. § 251 et seq.) See also *Orthopaedic Hosp. v. Belshe*, 103 F.3d 1491, 1495-96 (9th Cir. 1997) (holding that a "state agency's interpretation of federal statutes is not entitled to the deference afforded a federal agency's interpretation of its own statutes under Chevron") (citation omitted). Review is plenary. See

Omnipoint Communications Enterprises v. Newton Township, 219 F.3d 240 (3rd Cir. 2000).

SUMMARY OF ARGUMENT

As a matter of law, the District Court erred in ruling that the Board had authority to supplant the rates developed in the extensive arbitration proceeding mandated by Section 252 of the Act with uniform rates resulting from a generic rate proceeding. Section 252 only permits the Board to accept or reject arbitrated rates; it does not otherwise authorize the Board to modify, alter or replace the rates developed through arbitration between the parties. Moreover, contrary to the District Court's order, Section 261 of the Act -- which allows the states to impose "additional requirements necessary to further competition" and "not inconsistent" with the Act in reviewing arbitration agreements -- does not confer to the Board authority to substitute rates. Because a state commission's substitution of rates flatly breaches the "approve or reject" mandate of Section 252 and because it is inconsistent with both the terms, structure and underlying policy of the Act, the narrow exception for adding requirements provided by Section 261 does not apply.

Further, the District Court confused the provisions of Section 252 when it discussed the state's "broad authority" to substitute rates. State commissions may have "broad authority" while arbitrating unresolved issues in arbitration, but that authority is significantly limited once arbitration has concluded and all that remains is for the state to approve or reject the arbitrated

outcome.

The District Court's interpretation of the Telecommunications Act not only violates the direct terms of the Act but also fails conform to traditional canons of statutory construction. The interpretation runs counter to the policy, the assumptions, and the structure of the Act. Several provisions of the Act would be rendered meaningless under the District Court's interpretation. Moreover, the lower court's approval of the Board's rate substitution authority -- which reflected the Board's desire to promote consistency in rates -- runs afoul of the underlying intent of the Act to promote diversity and competition in the telecommunications industry.

Finally, regardless of whether the Act itself prohibits substitution, the FCC's regulations do not allow state regulators to substitute standard rates for arbitrated under Section 252 of the Act. The FCC has preempted provisions of state regulation such as the regulation present here, where the state's policy of substitution adversely effects a telecommunications carrier's ability to negotiate and arbitrate terms more favorable than the terms set by the state regulation.

Thus, while the District Court correctly ruled that the Board's generic rates themselves are not the product of reasoned decision making and therefore are "arbitrary and capricious," this Court must reverse the District Court's holding that the Board has authority under the Act to substitute its own rates for rates reached in an agreement arbitrated under Section 252.

ARGUMENT

I. The Telecommunications Act of 1996 Precludes the Board from Substituting Uniform Rates for Arbitrated Rates.

A. The Board's Authority Under the Plain Language of Section 252 is Limited to Acceptance or Rejection of the Arbitrated Rates.

Section 252(e) states that upon submission of an arbitrated agreement, state commissions "shall approve or reject the agreement, with written findings as to any deficiencies." State commissions "may only reject" an arbitrated agreement upon specific findings of violations of Section 252(d) or Section 251. The Supreme Court has consistently held that where a statute is clear on its face, that is the end of the matter.⁶ The implications of this express language makes clear several things.

First and most significantly, the plain words of the subsection permit only rejection or approval. The text -- stating that the state commission "shall approve or reject" the agreement -- is unambiguous. It does not permit the state commission to modify, subject approval to conditions, or to substitute the terms of an agreement submitted for approval with terms it thinks are better. The text does not leave room for the exercise of discretion in determining how to handle submitted agreements; the term "shall" commands approval or rejection. Moreover, the

⁶ See *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 843 (1984), that "[if the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress."

subsection presumes the validity of arbitrated and negotiated agreements by precluding states from rejecting agreements unless they make the specific written findings required under paragraphs (2)(A) and (2)(B) of Section 252(e).⁷

Second, the detail in the language of Section 252(e) suggests that Congress did not casually or accidentally omit authority for state commissions to modify or condition arbitrated agreements. Like the rest of Section 252, Section 252(e) is quite specific. It states that states "shall approve or reject" agreements submitted for review, it limits the scope of their review (agreements "may only" be rejected on the basis of specified criteria), and it requires state commissions to make "written findings as to any deficiencies." Further, Section 252(e) treats negotiated and arbitrated agreements differently in terms of the required findings a state must make in order to reject the agreement. Congress' effort to delineate clear parameters for what state commissions can and cannot do is unambiguous and apparent from a facial reading of Section 252(e). Had Congress wanted to confer additional authorities to state commissions in their review it clearly would have done so. The Act was a clear roadman for achieving competition in all telecommunications markets.

Third, Congress' intent not to include language authorizing states to modify or condition arbitrated agreements submitted for

The presumption is created by the limiting language of subsection (e)(1) declaring that the state commission "may only reject" a negotiated or arbitrated agreement if it makes certain findings.

their review under Section 252(e) review is evidenced by its inclusion of such language in Section 252(c), which covers arbitration. In Section 252(c), Congress gave state commissions, in their role as arbitrators, the authority to "impose] appropriate conditions" and "establish rates" in resolving issues submitted for arbitration. Section 252(c) demonstrates that Congress was well aware of the need for language authorizing conditions and ratesetting authority and that it was capable of drafting such language. Had Congress wanted to give state commissions authority to modify or substitute terms of arbitrated agreements during the review, it would have included in Section 252(e) language similar to that in Section 252(c).⁸ Congress choose not to include such language, however. Consistency therefore requires this Court to conclude that Congress intentionally omitted from Section 252(e) language authorizing states to impose conditions.

Fourth, there are well-founded, practical reasons for why Congress chose not to give states broad authority to substitute terms or otherwise condition approval of agreements submitted for state commission approval. Arbitrated agreements are private contracts, here between two competing carriers seeking to provide telecommunications services, resulting from private deliberations with the assistance of state arbitrators. "The structure of the Act reveals the Congress's preference for voluntarily negotiated

⁸ Consistent with its intent to give state commission authority only to reject or approve arbitrated agreements, a finding regarding Section 252(c) would have no bearing on a state commission's ability to reject or approve an arbitrated agreement.

interconnection agreements between incumbent LECs and their competitors over arbitrated agreements." *Iowa Utilities Board v. FCC, et al.*, 120 F.3d 753 at 801 (8th Cir. 1997) Congress did not want state commissions to upset the balance accomplished by the give and take involved in reaching an agreement. Allowing state commissions in the review process to substitute terms of the contract or otherwise condition approval would upset this balance, by upsetting the core expectations of the parties. Rather, Congress created a presumption in favor of approval, while seeking to ensure that agreements met the basic criteria of Section 252(d) and Section 251. The requirement for approval or rejection enables the parties themselves to resolve the issues upon which rejection was based or to seek judicial review of a state commission's rejection. The District Court's holding in this case obliterates Congress' regime of private negotiation and arbitration by permitting state-imposed terms to private agreements.

Fifth, Section 252(d) unambiguously anticipates multiple determinations of prices, not one determination of a standard rate. A former monopoly marketplace was being transformed into a competitive marketplace requiring proper economic incentives for each new entrant. Section 252(d), which establishes standards by which states are to assess the rates of arbitrated agreements, begins by stating, "Determinations by a State commission of the just and reasonable rate...." (emphasis added). Congress' use of the plural form of "determination" in the Section 252(d)(1) phrase indicates that Congress did not envision a state to make a single

determination of a standard rate; rather it anticipated multiple "determinations." The District Court's holding, however, would allow states to conduct only one determination of a just and reasonable rate. The holding is thus contrary to the statute and the goals of the Act to provide incentives for competitors to enter the marketplace.

B. The District Court Erred in Interpreting Section 261 as Providing States Authority to Impose Standard Rates as an "Additional Requirement" of State Review of Arbitrated Agreements.

The District Court ruled that the Act provides state commissions the authority "to substitute generic rates for arbitrated rates." (14a) The District Court dedicated just one sentence to its discussion of the Board's rate substitution authority.⁹ That sentence states that "[t]he Board has independent authority to impose additional requirements not inconsistent with the Act under § 261(c)...." (14a)

The District Court's interpretation of Section 261(c) is erroneous. Section 261(c) is a general provision saving from federal preemption "additional state requirements" that "are necessary to further competition...as long as [they] are not inconsistent" with the Act or the FCC's regulations under the Act. Put simply, Section 261(c) fails to provide authority for the Board to substitute arbitrated rates with generic rates because

⁹ The remainder of the Court's discussion concerns only the undisputed authority of a state commission to reject an agreement for its failure to comply with section 251 and subsection (d) of Section 252.

substitution is totally inconsistent with specific provisions of the Act. Specifically, rate substitution is inconsistent for at least three reasons:

1. As explained above, the plain language of Section 252(e) limits state commission action to approval or rejection with written findings. See Part I.A., *supra*. Further, Section 252(e) does not simply list standards for state commission review to which courts may add or impose "additional requirements"; rather, the language expressly negates the ability of states to take into consideration any additional terms by providing that states "may only" reject a submitted agreement upon making the identified findings. Thus, any "additional requirements" for consideration by a state commission reviewing an arbitrated agreement -- such as a requirement that the agreement include generic rates -- are inconsistent with Section 252(e).
2. The statute is designed to promote competition through negotiated and arbitrated agreements. The Board's substitution of generic rates for negotiated and arbitrated rates would undermine the statute because it would remove one of the key elements of negotiation and arbitration -- price -- from consideration completely. See Part I.E., *infra*. Economic competition, by definition, requires the ability of the carrier to offer competing prices. Thus, substitution of generic rates is inconsistent with the Act and Section 261 provides no relief.
3. Substitution of generic for arbitrated rates conflicts with the FCC's regulations and rulings implementing the Act. The FCC has declared that any state law requirements that preclude parties from negotiating or arbitrating more favorable terms than those required under the state law are preempted, see Part II, *infra*., which is exactly what the Board did here - imposed one price which precluded negotiation for more favorable terms. Inconsistency with FCC rules is sufficient to invalidate any additional state requirements that might otherwise be valid under Section 261.

As we explain in Part I.E., *infra*, the substitution of generic rates not just fails to further competition, it undermines

competition, the stated goal of the Act, which is "to promote competition and reduce regulation in order to secure lower prices and higher quality services for American telecommunications consumers and encourage the rapid deployment of new telecommunications technologies." *Iowa Utilities Board v. FCC, et al.*, 120 F.3d 753 at 792 (8th Cir. 1997).

In sum, the District Court erred in relying on Section 261(c) to hold that a state commission may superimpose standard rate requirements on arbitrated agreements. Mandatory substitution of generic rates for arbitrated rates is inconsistent with the Act and FCC regulation, and it is contrary to the objective of effective competition.

C. The District Court Confused the State Commission Role During Arbitration with the State Commission Role in Reviewing Agreements.

Although its specific discussion of the authority of state commissions to substitute standard rates for arbitrated rates is quite brief, the District Court apparently relied in part on what it called the "broad authority" given state commissions over "every aspect of an interconnection agreement" to hold that the Board has authority to substitute generic rates for arbitrated rates. (14a) The court erred, however, by failing to distinguish the scope of state commission authority during arbitration from the scope of state authority in the review of a consummated arbitrated agreement.

Section 252(c) and Section 252(e) apply at different points in

the process of establishing an interconnection agreement. Section 252(c), entitled "Standards for Arbitration," provides state commissions broad authority to resolve open issues during arbitration. The subsection applies when the state commission is "resolving by arbitration under subsection (b) any open issues...." Section 252(c)(2) permits states to determine interconnection rates if such rates have been identified as an unresolved issue in a petition for arbitration. No other language in Section 252 provides such ratesetting authority to states. In this case, Section 252(c) applies to the arbitration proceedings of Judge Thompson.

Section 252(e), on the other hand, applies only after arbitration -- and the state commission's role as arbitrator -- has been completed. The subsection applies when an interconnection agreement has been "submitted for approval to the State commission." Thus, after arbitration, when the state commission is acting in its quasi-judicial role to review the agreement pursuant to the statutory standard set forth in the Act, the state commission no longer has the ability to impose conditions or establish rates; it is limited to acceptance or rejection under Section 252(e).

The District Court confused the important distinctions between these two subsections. Its confusion is reflected in its incorporation of Section 252(c) into its discussion of the Board's review of a completed arbitration agreement under Section 252(e). See p. 9 of the District Court's opinion. (14a)

It is clear, however, that contrary to the District Court's ruling, Congress only provided states the ability to establish rates during the arbitration between a competitive carrier and an ILEC. In this case, Judge Thompson imposed rates according to the arbitration provisions of the Act. Once the arbitration was completed, state authority to establish rates ended. The Board had no authority to establish rates another time during the approval process set forth in Section 252(e). Assuming the arbitrator failed to establish rates in compliance with Section 251 or subsection (d), the Board's only recourse was to reject the agreement with a written explanation in accordance with Section 252(e).

D. The District Court's Reading of the Act Violates Several Canons of Statutory Construction.

The District Court's reading of the Act to allow state commissions to replace arbitrated rates with uniform or "generic" rates violates several tenets of statutory interpretation. We highlight five of them.

1. The District Court's Decision Would Render Superfluous Several Provisions of the Telecommunications Act of 1996.

Statutes should not be interpreted so as to render other provisions of the same act superfluous. *Coluatti v. Franklin*, 439 U.S. 379, 392 (1979) (observing that it is an "elementary canon of construction that a statute should be interpreted so as not to render one part inoperative"). The District Court's holding allowing the imposition of generic rates renders useless, for most

practical purposes, the negotiation and arbitration provisions of Section 252(a) and Section 252(b). See Part I.E, *infra*. Likewise, the imposition of generic rates effectively precludes a competitive carrier from exercising its rights to pick and choose terms from other agreements for its own agreement under Section 252(i).⁴³ Since all rates will be the same, there will be nothing to "pick and choose." The District Court's holding thus renders Section 252(i) superfluous and inoperative.

2. The District Court's Interpretation is Inconsistent with the Basic Structure of the Act.

Courts should avoid interpreting statutes in ways that are inconsistent with the structure of the Act from which they are derived. See *Eli Lilly & Co. v. Medtronic, Inc.*, 496 U.S. 661 (1990). Congress devoted an entire statutory section to "Procedures for Negotiation, Arbitration, and Approval of Agreements," as Section 252 is titled. Subsections (a) through (j) of Section 252, with their numerous subparagraphs, are all designed to make negotiation and arbitration successful and in the public interest. Yet the District Court's interpretation that state commissions have the power to substitute uniform rates for arbitrated rates is based on Section 261, a general section removed from the context of

⁴³ Section 252(i) require ILECs to "make available any interconnection, service, or network element provided under an agreement ... to which it is a party to any other requesting telecommunications carrier upon the same terms and conditions as those provided in the agreement." The Supreme Court has held that this provision permits carriers to pick and choose terms from different agreements between ILECs and carriers for its own interconnection agreement. *AT&T Corp. v. Iowa Util. Board*, 119 S.Ct. 721 (1999).

Section 252's negotiation and arbitration provisions.

3. The District Court's Interpretation is Inconsistent with Necessary Assumptions of the Act.

The Supreme Court also has admonished courts not to interpret statutes in ways inconsistent with the necessary assumptions of the Act. See *Gade v. National Solid Wastes Management Ass'n.*, 505 U.S. 88, 101 (1992). In this case, one may reasonably assume that Congress, in seeking to promote local telephone competition through negotiated and arbitrated agreements, intended those negotiations and arbitration to have practical value. Eliminating price completely from any consideration in negotiation and arbitration through the establishment of uniform rates undermines the necessary assumption that Congress wanted negotiation and arbitration to foster competition. See *Local Competition Order* at ¶¶ 13 and 41.

4. The District Court's Interpretation is Inconsistent with the Policies Sought to Be Furthered by the Act.

Courts should avoid interpreting statutes in ways that are contrary to the policies of the statute. See *United Savings Ass'n of Texas v. Timbers of Inwood Forest Assoc., Ltd.*, 484 U.S. 365 (1988). In this case, the District Court's holding allowing the substitution of standard rates for arbitrated rates is inconsistent with Congress' policy of promoting individualized agreements between carriers and ILECs, rather than uniformity under standard rates like those which had existed in the monopoly marketplace - one carrier offering local service at state commission established rates. See, e.g., Section 252(i) (allowing carriers to pick and

choose terms from different agreements for their own; see also Part I.E., *infra*. Congress hoped that carriers would have a diversity of options for agreements with ILECs, but the Board's decision, which was erroneously affirmed by the District Court's holding, would leave only one price option.

5. The District Court Interpreted the Act Broadly, When Congress Provided for the Broader Policy in Specific Provisions.

Courts should avoid broad interpretations of statutory provisions where Congress addressed the broader policy in specific provisions elsewhere in the statute. See *West Virginia University Hospitals v. Casey*, 499 U.S. 83 (1991). The District Court interpreted state commission authority under the Act broadly -- specifically, by invoking the general savings provision of Section 261(c) -- to give the Board authority to substitute generic rates for arbitrated rates in every case. Congress, however, specifically provided for the scope of state authority in more specific language throughout Section 252. See Part I.A., *supra*. The District Court therefore erred by holding that a broad statutory provision overrides a specific provision governing the very issue in dispute.

E. Substitution of Standard Rates for Arbitrated Rates is Inconsistent with Congress's Intent Through Arbitration and Negotiation to Promote Diversity and Competition, Not Uniformity and Regulation.

1. In Choosing Competition over Regulation, Congress Precluded State Commissions From Promoting Uniformity or Consistency by Setting Uniform Rates.

The Board's unlawful act of substituting its generic rates for

arbitrated rates arises out of its desire that there be uniform rates for interconnection with the ILEC throughout New Jersey. This desire for uniform rates throughout the state is representative of the Board's unwillingness to step out of the old regime of monopoly regulation and into the new regime of competition sought by Congress. Congress preempted the old regime of uniform rates when it choose competition over regulation in enacting the Telecommunications Act of 1996 "which was designed, in part, to erode the monopolistic nature of the local telephone service industry by obligating the current providers of local phone service...to facilitate the entry of competing companies into local telephone service markets across the country." *Iowa Utilities Board v. FCC, et al.*, 120 F.3d 753, 791 (8th Cir. 1997).

The Board's apparent obsession with consistency among arbitrated rates in New Jersey is evident throughout its discussion of the effect of its generic rates on arbitrated rates in the Generic Proceeding order, where it concluded that the generic rates should substitute for the arbitrated rates in the BA-NJ/AT&T agreement. (114a-157a) The Board stated, for example, that "of great importance to the Board is the fact that this generic proceeding has allowed the Board to establish rate, terms, and conditions for interconnection...which are consistent statewide." Generic Proceeding order at p. 245 (emphasis added). (146a) With respect to AT&T's arbitrated rates, the Board emphasized that AT&T should have known that it might substitute generic rates for arbitrated rates, "particularly ... where such results were

inconsistent with other arbitration decisions." (153a)

The Board's ability to legally effectuate its desire for consistency and uniformity, however, was preempted by Congress in the Telecommunications Act. In Section 252(e)(2)(B) of the Act, Congress limited the criteria upon which a state may reject arbitrated interconnection agreements to compliance with Section 251 and with the pricing rules of Section 252(d). See Part I.A., *supra*. The lack of consistency or uniformity in pricing is not a legally permissible criterion for rejection in Section 252(d) or Section 251.

Although Congress anticipated that individualized -- and therefore inconsistent -- agreements would arise out of its enactment of the negotiation and arbitration provisions of Section 252, it did allow for some measure of consistency to develop among interconnection agreements. Congress imposed nondiscrimination requirements on ILECs, and, through Section 252(i), it enabled carriers to pick and choose from particular terms of different interconnection agreements.

The Board, however, believed Congress' policy in Section 252(i) to be insufficient. The Board disagreed with Congress when it stated in the generic proceeding that it "doubts that the operation of Section 252(i) alone will lead to the consistency in interconnection rates, terms and conditions which is necessary to achieve fair competition in the local exchange marketplace." (150a) While the Board may be free to "doubt" the policies adopted by Congress, it is legally barred under the Supremacy Clause of the

Constitution from modifying the legal standards set forth in valid federal law. Had Congress believed, like the Board, that uniform rates were "necessary" for competition, it had several avenues for requiring that uniform rates be established, as described in Part I.A. Congress instead believed individual agreements would better promote competition. The Board is therefore not free to act inconsistently with the clear intent of Congress to limit the Board to approval or rejection of arbitrated rates.

2. The District Court's Holding Will Leave Competitive Carriers One Option -- Standardized or Generic Rates -- When the Statute Envisioned Multiple Options to Facilitate Competition.

Aside from violating Congress' clear limitations over state review of arbitrated agreements under Section 252(e), the Board's desire for consistent interconnection rates flies in the face of the goals of competition. Congress anticipated that each carrier would have the opportunity to negotiate an agreement with the monopoly carrier based on its own particular goals for entering the competitive marketplace. Congress thus geared Section 252 toward one result -- individualized interconnection agreements. Congress provided only a limited role for state commissions in the agreement process -- to overcome deadlocks in negotiations through arbitration over particular issues. When a deadlock occurs over interconnection rates, state commissions - in their role as arbitrators - may establish prices for the agreement. After an agreement has been reached, however, the role of the state commission is even more limited - approval or rejection of the

agreement. See 252(e)(1). Nowhere does the Act give state commissions the authority to negate the practical value of negotiation by requiring that all agreements have the same rate.

Ultimately, the Board's decision to substitute generic rates for arbitrated rates undermines a central goal of Section 252 of the Telecommunications Act: to foster the emergence of a competitive telecommunications marketplace through negotiation of individualized agreements between telecommunications carriers and incumbents. Where the Board can substitute a previously established generic rate for any arbitrated interconnection rate, ILECs have no incentive to negotiate over rates at all, knowing they would receive a higher rate upon advancing to arbitration which serves as an impediment to competition. The Supreme Court has explicitly held that "[s]tates may no longer enforce laws that impede competition, and incumbent LECs are subject to a host of duties intended to facilitate market entry." *AT&T v. Iowa Utils. Bd.*, 525 U.S. 366 at (1999). In other words, allowing the Board to substitute its generic rates for the arbitrated rates makes negotiation futile because arbitration results in the Board established generic rates -- every time. By contrast, in the absence of a "guaranteed generic rate, the uncertainty of the outcome of an arbitrated proceeding pressures all participants to reach a negotiated and mutually agreeable result which fits their respective market strategies, financial structures and customer bases -- as was intended by the Act.

In fact, the Board's effort has made negotiation and

arbitration in New Jersey an exercise in futility. All interconnection agreements and resale agreements approved by the Board to date contain the permanent rates established by the Board. No telecommunications carrier in New Jersey has been able to negotiate or arbitrate with ILECs for rates that differ from the Board's permanent rates.

In sum, by permitting states to require complete uniformity, the District Court's holding in this case completely undermines Congress' desire to promote individualized resolution of interconnection issues. Thus, left intact, the District Court's holding would allow state regulation to entirely supplant Congress' desire to foster competition and choice for consumers in an open marketplace through individualized agreements.

II. Regardless of Whether the Act Itself Precludes Substitution, the FCC Has Preempted State Regulators from Substituting Standard Rates for Arbitrated Rates Through the Valid Exercise of its Authority.

Section 261 of the Act, relied upon by the lower court to uphold the Board's power to require generic rates, allows states to impose requirements on carriers only if they are necessary to competition, consistent with the Act, and consistent with FCC regulation under the Act. Assuming, *arguendo*, that the Board's substitution of generic rates for arbitrated rates complies with the Act, the court still must consider whether substitution is consistent with FCC regulation. In the next two subparts, we explain why the Board's action of substituting rates is inconsistent with (a) FCC orders regarding preemption of state

requirements affecting negotiation and arbitration and FCC regulations regarding price.

A. FCC Regulation Preempts Inconsistent State Regulation.

The FCC recently described the legal framework for preemption by a federal agency under the Supremacy Clause:

A federal statute preempts a state statute under the Supremacy Clause when the state statute conflicts with the federal statute or stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress. Such conflict preemption may result not only from action taken by Congress. It may also result from action taken by a federal agency, but only when the agency acts within the scope of its congressionally delegated authority. Pursuant to this conflict preemption doctrine, the Commission has on numerous occasions preempted state law that conflicted with federal law or stood as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.¹¹

Two recent FCC orders bear on the District Court's holding at issue on this appeal, wherein the FCC ruled on the scope of its preemption under the Telecommunications Act.

1. Texas Preemption Order.

In its 1997 *Memorandum Opinion and Order*,¹² the FCC applied

¹¹ I/M/O *American Communications Services, Inc.; MCI Telecommunications Corp.; Petitions for Expedited Declaratory Ruling Preempting Arkansas Telecommunications Regulatory Reform Act of 1997 Pursuant to Sections 251, 252, and 253 of the Communications Act of 1934, as amended*, Memorandum Opinion and Order, CC Docket No. 97-100, 14 FCC Rcd 21579, FCC 99-386, (released December 23, 1999) (*Arkansas Preemption Order*), at 13 (internal quotations and footnotes omitted).

¹² I/M/O *the Public Utility Commission of Texas; The Competition Policy Institute, IntelCom Group (USA), Inc. And ICG Telecom Group, Inc., AT&T Corp., MCI Telecommunications Corporation. And MFS Communications Company, Inc.; Teleport*

preemption analysis to several Texas statutes and regulations, including a "continuous property" rule which limited the resale of centrex service.¹³

The FCC determined that several provisions of Texas law, as applied and interpreted, affected rights under Sections 251 and 252 of the Act. The FCC ruled that several of these provisions were not preempted because the Texas PUC represented that they would not preclude parties under Sections 251 and 252 from negotiating or arbitrating more favorable terms and conditions.¹⁴ However, the FCC preempted the continuous property restriction because of its effect on negotiation and arbitration:

By virtue of the Texas Commission decisions [regarding the continuous property restriction], carriers wishing to provide competing centrex service through resale are effectively precluded from invoking the section 252 negotiation and arbitration procedures in order to obtain centrex for resale on terms more favorable than those

Communications Group, Inc.; City of Abilene, Texas; Petitions for Declaratory Ruling and/or preemption of Certain Provisions of the Texas Public Utility Regulatory, Memorandum Opinion and Order, FCC 97-346, 13 FCC Rcd. 3460 (released October 1, 1997.), petition for recon. pending, petition for review, denied, City of Abilene, Texas v. FCC, 164 F.3d 49 (5th Cir. 1999).

¹³ "Centrex" is the generic name for central office-based private branch exchange (PBX)-type services such as intercom, access line pooling, call transfer, conference calling, etc. The Texas Commission had approved a tariff which prohibited resale of centrex by competing carriers to customers, if any of the centrex lines terminated in facilities which were not situated on a continuous property area and that at least 30 business lines per customer premise. See *Memorandum Opinion and Order* at footnotes 490-492.

¹⁴ See 15, 92, 102-108, 119, 138-141, 151, 155, 159-160, 165, 171, 194, 197, 206-210, 220-223, and 218-226 of the FCC's *Memorandum Opinion and Order*.

provided under SWBT's centrex resale tariff,
containing the continuous property restriction.¹⁵

The Ratepayer Advocate submits that the District Court decision affirming the Board's authority to supersede arbitrated provisions failed to consider the doctrine of preemption as announced and interpreted by the FCC. First, if the decision below stands, it precludes a party seeking to enter the telecommunications marketplace as a competitor from using negotiation and arbitration to obtain more favorable rates; and second, it renders Section 252(i) of the Act meaningless. Left in place, this decision creates but one option for telecommunications carriers. It is clear that Congress envisioned multiple options for telecommunications carriers, based upon their individual market entry strategies, financial structures, and choice of service(s) they intend to provide. Thus, the FCC will preempt a state regulation that has an adverse effect on carriers' ability to negotiate and arbitrate terms more favorable than the terms set by regulation.

2. Arkansas Preemption Order.¹⁶

In its *Arkansas Preemption Order*, the FCC preempted the enforcement of an Arkansas statute that imposed a different standard for state commission review of negotiated agreements than

¹⁵ *Id.* at para. 219 (emphasis added).

¹⁶ The Ratepayer Advocate acknowledges that the District Court did not have available to it the *Arkansas Preemption Order* since it came out after briefing and oral argument. However, this FCC order now compels reversal of the District Court's affirmance of the Board's actions below.

the standard contained in Section 252(e)(2)(A) of the Act."

The Arkansas statute ("Arkansas Section 9(i)") provided that

"the [Arkansas] Commission shall approve any negotiated interconnection agreement ... filed pursuant to the Federal Act unless it is shown by clear and convincing evidence that the agreement or statement does not meet the minimum requirements of Section 251 of the Federal Act...." (emphasis added).

The FCC preempted the Arkansas statute because it altered the criteria and burden of proof for state commission review of negotiated agreements:

Comparing the language of [Arkansas] section 9(i), however, with the relevant sections of the Communications Act, reveals that [Arkansas] section 9(i) provides the wrong standard of review.... As we have seen, the Communications Act requires state commissions to approve negotiated agreements unless they harm a non-party carrier or are inconsistent with the public interest. Section 9(i), however, is silent as to these points. Instead, [Arkansas] section 9(i) requires that negotiated agreements satisfy the Communication Act's section 251. Thus, section 9(i) omits two statutory requirements for the approval of negotiated agreements (those touching on third parties and the public interest) while introducing a new hurdle (conformity with section 251) that is nowhere to be found in Communication Act's standard for review of negotiated agreements. The [Arkansas] section 9(i) standard is therefore entirely different from, and in conflict with, the federal standard for review of negotiated agreements set forth in section 252(e)(2)(A).¹⁸

¹⁷ Section 252(e)(2)(A) provides that a state commission may reject a negotiated interconnection agreement only if the agreement discriminates against a non-party telecommunications carrier or conflicts with the public interest.

¹⁸ *Id.* at ¶ 74 (footnotes omitted) (emphasis added).

B. The Board's Requirement of Rate Substitution is Inconsistent with FCC Regulation.

The Board in this case established a single rate which is both a minimum and maximum for unbundled network elements. This one-rate requirement violates the FCC's preemption orders, because the setting of a single rate precludes telecommunications carriers from negotiating and arbitrating more favorable provisions under Sections 251 and 252 of the Act.

A state commission's generic rates are permissible only if they do not affect a carrier's ability to obtain a more favorable rate through negotiation or arbitration. Consider the similarities between the Board's action in this case and the state requirements invalidated in the *Arkansas Preemption Order* and the *Texas Preemption Order*:

1. In the *Arkansas Preemption Order*, the FCC addressed a state law requirement that altered the standard of state review under § 252(e)(2)(A). This case involves the correlating standard of review under § 252(e)(2)(B) for arbitrated agreements. The Board's order requiring substitution of generic rates for arbitrated rates has the same effect on § 252(e)(2)(B) as the effect of the Arkansas statute at issue in the *Arkansas Preemption Order*. As in the Arkansas case, the Board's action in this case "introduc[es] a new hurdle [conformity with the Board's generic rates] that is *nowhere to be found* in Communication Act's standard for review of negotiated agreements."
2. The Board's policy of generic rate substitution also is analogous to the Texas regulation invalidated in the *Texas Preemption Order*. The Texas PUC's "continuous property" rule effectively precluded carriers from negotiating or arbitrating more favorable terms than the ILEC's resale tariff. Like the Texas regulation, under the Board's rate substitution requirement, "carriers ... are