

determined to be TELRIC-compliant; and (3) interim rates imported from Texas that neither the MPSC nor this Commission has found to comply with TELRIC principles.

4. SWBT's Missouri Rates Are Inflated By Its Use Of Outdated Cost Data.

In all events, even assuming (contrary to fact) that the arbitrary discounts offered by SWBT could offset the rate inflation caused its non-TELRIC-compliant cost studies (and its use of numerous non-TELRIC-compliant interim rates), that would only mean that SWBT's flawed cost studies combined with the rate discounts could produce TELRIC-compliant rates for the pre-1997 data on which its cost studies relied. Section 271 is framed in the present tense and requires a showing that the BOC's rates comply with the checklist today.²⁴ As explained by MPSC Commissioner Gaw, the MPSC "has heard no evidence as to the appropriateness of these [SWBT's Missouri] rates as of the date of this order."²⁵ And it is beyond serious dispute that the costs of the facilities used to provide UNEs have declined dramatically during the past several years.

For example, SWBT's Missouri cable and wire investment declined by 31 percent between 1996 and 2001, which strongly indicates that SWBT's loop costs have significantly declined since 1996. *See* Lieberman AR/MO Decl. ¶ 24 & Exhibit 12. Likewise, SWBT's Missouri switching costs have plummeted since 1996. This Commission has already explicitly recognized that fact.²⁶ And a simple analysis of SWBT's Missouri net switch investments and its dial equipment minutes ("DEMs") reveals that net switch investments have been declining on a

²⁴ *See* 47 U.S.C. § 271(c)(2)(A) ("such company *is* providing access and interconnection . . . [that] meets the" checklist requirements) (emphasis added).

²⁵ *Gaw Concurrence* at 1-2.

²⁶ *See, e.g., Order on Remand and Report and Order, Implementation of the Local Competition Provisions in the Telecommunications Act of 1996 and Intercarrier Compensation for ISP-Bound Traffic*, CC Dockets No. 96-98 and 99-68, FCC 01-131, at 84, n. 157, 93 (April 27, 2001) ("*Intercarrier Compensation Order*").

per-minute-of-use basis since 1996. *See id.* ¶ 27 & Exhibits 12-13. Between 1996 and 2000 net switch investment has grown much slower than DEMs. *See id.* Combining that slow growing net switch investment with the explosive increase in minutes, results in a 20 percent decline in switching investment per DEM between 1996 and 2000. *See id.*

The MPSC cannot be relied upon to address these cost declines are fix SWBT's TELRIC violations at any time in the near future. As noted above, the MPSC had an opportunity to address these issues earlier this year, but still chose to retain SWBT's inflated M2A rates. *June 7 Arbitration Order* at 13-15. Thus, the Commission cannot reasonably approve SWBT's application with the expectation that the MPSC will soon address the fundamental flaws in SWBT's M2A rates.

5. SWBT'S UNE Rates Fall Far Outside Any Reasonable TELRIC Range.

Given all of the TELRIC errors discussed above, it is not surprising that SWBT's original section 271 Application were "outside the range that the reasonable application of TELRIC principles would produce." DOJ MO Eval. at 2. As demonstrated by the expert analyses submitted by commenters²⁷ and by SWBT itself,²⁸ SWBT's UNE "[p]rices in Missouri are higher than those in neighboring states which the Commission has found to be compliant with TELRIC, and this disparity does not appear to be accounted for by cost differences between states." DOJ MO Eval. at 2. The minor arbitrary rate discounts implemented by SWBT in its most recent Missouri 271 Application do not change these findings.

The most appropriate comparison states, for purposes of analyzing Missouri's UNE rates, are Kansas and Arkansas (because SWBT imported its Kansas rates into Arkansas).

²⁷ *See, e.g.*, WorldCom MO Comments at 4 & Frentrup Decl. at ¶¶ 7-11.

²⁸ *See* Letter from Geoffrey M. Klineberg to Magalie Roman Salas, Secretary, *Application by Southwestern Bell for Provision of In-Region, InterLATA Service in Missouri*, CC Docket No. 01-88 (May 4, 2001).

See DOJ MO Eval. 12 & nn. 42, 43. This is true, in part, because (as DOJ observes) “these are adjacent states with nearly identical costs, according to the USF model.” But Kansas and Arkansas are the appropriate benchmarks here for even more fundamental reasons. Although now somewhat dated, the Kansas Commission’s application of TELRIC methodology in setting recurring UNE rates was, by all accounts, rigorous and independent. Its analysis was accepted as implementing TELRIC for recurring rates by all affected parties, even in a circumstance where its conceded failure to adhere to TELRIC principles with respect to non-recurring rates was roundly criticized. Indeed, SWBT itself has effectively endorsed the Kansas recurring UNE rates as TELRIC-based by relying on those rates in its contemporaneous Arkansas 271 Application.

Texas, by contrast, is a poor benchmark. As an initial matter, SWBT’s Texas rates were never litigated before this Commission and, therefore, cannot be properly relied upon to justify other states’ rates.²⁹ Furthermore, even if Texas rates had been properly set in 1997 (and it has been clear that they were not), the forward-looking cost of providing UNEs has declined substantially over the past several years. See Lieberman AR/MO Decl. ¶¶ 22-27. For example, SWBT’s Texas cable and wire investment declined by 36 percent between 1996 and 2001, which strongly indicates that SWBT’s Texas loop rates – which are based on pre-1997 data – are not TELRIC compliant. See Lieberman AR/MO Decl., Exhibit 12. Likewise, SWBT’s switching costs have fallen dramatically – a fact that this Commission has already recognized. See *Intercarrier Compensation Order* at ¶ 84, n. 157, ¶ 93. A straightforward

²⁹ Allowing SWBT to rely on rates in a state that were never litigated would create perverse incentives that would greatly increase the scope and frequency of rate litigation in 271 proceedings. Even a state where UNE rate levels, were, on the whole, reasonably close to TELRIC levels, for example, competing carriers would be encouraged – indeed, required – to litigate the individual rate elements that strayed furthest from TELRIC for fear that those rate elements would later be used to justify rates for those elements in another state in which UNE rates were, on the whole, excessive.

analysis of SWBT’s Texas net switch investments and its dial equipment minutes (“DEMs”) confirms that between 1996 and 2000 net switch investment has grown much slower than DEMs, *see id.*, while there has been an explosive increase in minutes. *See id.* As a result, there has been a 28 percent decline in switching investment per DEM during that time. *See id.* It is not surprising, therefore, that CLECs have recently filed a petition with the TPUC seeking, among other things, to have TPUC address “the rate level and rate structure of UNE inputs [that are] critical to the provision of UNE Platform-based services”³⁰ in Texas.³¹

Comparing SWBT’s Missouri rates to those in Kansas and Arkansas shows that SWBT’s rates are outside the range that any reasonable application of TELRIC principles would have produced. As noted by Commissioner Gaw, it is “striking . . . [that] Missouri’s rates are higher than the rates just volunteered by SWBT to Arkansas – a state that is more rural and with more difficult terrain than Missouri.”³² Commissioner Gaw’s observations are accurate. SWBT’s Missouri UNE loop rates exceed those in Kansas and Arkansas by 11 and 7 percent, respectively. *See* Lieberman AR/MO Decl. ¶ 21 & Exhibit 11. These rate differences are striking because the Commission’s Synthesis Model predicts that the costs of providing loops in Missouri are about the same as those in Kansas, and are significantly lower than those in Arkansas. *See id.*

Given SWBT’s extravagant Missouri rates, it is not surprising that competitors are foreclosed from profitable UNE-based entry. In two of the four UNE rate zones, a new

³⁰ Petition for Expedited Resolution of UNE-P Competition Issues, And Motion to Consolidate with Docket No. 24542 by the Texas UNE Platform Coalition, AT&T Communications of Texas, LP and McLeod USA Telecommunications Services, Inc., *Petition for Expedited Resolution of Disputed Issues Regarding UNE-P Competition in Texas*, Docket No. [unassigned] (September 7, 2001).

³¹ To hold Oklahoma out as the TELRIC “standard” would truly make a mockery of the Commission’s Section 271 authority, given the sheer arbitrariness of the process used to establish those rates and the reality that there is *no* significant UNE-based residential competition in Oklahoma.

³² *Gaw Concurrence* at 1-2

competitor would lose money on each residential line it serves. Lieberman AR/MO Decl. ¶¶ 18-20. And although state-wide margins for Missouri are slightly positive, those margins are not remotely sufficient to cover a competitor's internal costs of entry, including marketing, customer service, billing, order processing, and other operating activities. *See id.*

For all of these reasons, SWBT's Missouri rates plainly fall well outside the range of rates that any reasonable application of TELRIC principles would have produced.

6. Contrary to SWBT's Claims, The Courts Have Never Even Reviewed Its Missouri UNE Rates for Compliance With the Commission's TELRIC Rules, Much Less Held Them to be TELRIC Compliant.

SWBT makes almost no effort at all to carry its burden of establishing that its UNE rates for Missouri comport with TELRIC except to refer selectively to particular findings of the MPSC and to cite to certain statements – out of context – made by a district court and the United States Court of Appeals, for the Eighth Circuit. SWBT first asserts that the MPSC Staff “found that SWBT cost studies fully complied with TELRIC principles.” SWBT AR/MO Br., at 26-30. This assertion is directly contradicted by the MPSC Staff report. As described above and in the declaration of AT&T witness Michael Baranowski, the MPSC Staff identified numerous aspects of SWBT's cost models, as adopted by the MPSC, that continue to violate core TELRIC principles. *See, e.g.,* Baranowski AR/MO Decl. ¶¶ 10-70. Moreover, it is obvious from the MPSC's express endorsement of SWBT's reproduction cost approach, that it clearly misunderstood the requirements of TELRIC.

SWBT next claims that the U.S. District Court, W.D. Missouri, Western Division concluded that SWBT's cost studies as adopted by the MPSC Staff complied with TELRIC principles.³³ This claim is spurious. In recommending permanent rates to the MPSC, SWBT

³³ *See AT&T Communications Corp. of the Southwest v. Southwestern Bell Telephone Company*, 86 F.Supp.2d 932 (W.D.Mo. 1999).

chose to submit its purportedly forward-looking cost studies, which it labeled TELRIC studies, rather than its preferred historical cost studies. After the Eighth Circuit invalidated the FCC's TELRIC methodology, however, SWBT argued that the MPSC erred by failing to base rates on a historical cost approach. The District Court was never called upon to look behind the TELRIC label SWBT affixed to its cost studies (which, as demonstrate above, were not remotely TELRIC-compliant), and the District Court did not do so. Rather, the District Court considered SWBT's due process and historical cost challenges, stating with respect to the latter that "the staff considered only competing TELRIC models, even though SWBT had argued that historical costs should be used to set rates." *AT&T Communications*, 86 F. Supp. 2d at 942. SWBT's claim that this statement constitutes a "conclusion" by the District Court that SWBT's cost studies are TELRIC-compliant is, therefore, clearly erroneous.³⁴

SWBT also claims that AT&T defended the permanent UNE rates adopted by the MPSC as TELRIC-compliant. To the contrary, AT&T defended only against SWBT's challenges – that the MPSC violated SWBT's due process through its rate-setting procedures and that the MPSC was required to use historical costs. In defending against those baseless claims, AT&T in no way endorsed the levels of the rates as TELRIC-compliant or opined that SWBT and the MPSC had fully implemented the TELRIC rules. And, as explained above, they most certainly did not.

SWBT continues its assault on reality when it claims that the "Eighth Circuit reversed and remanded the case back to the Missouri PSC precisely *because* TELRIC had been applied [by SWBT's cost studies]." SWBT AR/MO Br. at 29 (emphasis in original) (citing

³⁴ Likewise, SWBT's citation to the District Court's opinion for the proposition that "[t]he PSC did apply TELRIC methodology when making its pricing decisions," SWBT AR/MO Br. at 29, is taken out of context. In that portion of the district court's opinion, the district court was simply referring to the MPSC's contention that it attempted to
(continued)

Southwestern Bell Telephone Company v. Missouri Public Service Commission, 236 F.3d 922 (8th Cir. 2001). In reality, the Eighth Circuit never even looked at any of SWBT's cost models or its UNE rates for Missouri. That is not surprising given that the court did not find it necessary to determine whether SWBT's UNE rates for Missouri comply with TELRIC principles. *Id.* at 924-925. Rather, the Eighth Circuit simply held that because the MPSC admits that it *tried* to apply TELRIC principles, Missouri's arbitration proceeding violated the Eighth Circuit's recent (and currently stayed) decision that this Commission's TELRIC principles violate the 1996 Act. *Id.*

In sum, the record compels the conclusion that SWBT has failed to meet its burden of proving that its Missouri UNE rates comply with Checklist Item 2.

B. ARKANSAS.

The Arkansas Public Service Commission ("APSC") adopted SWBT's Kansas rates for Arkansas with *no independent review*, relying solely on the Commission's recent statements that it might be appropriate for a state to import the rates of another state with similar costs that has already obtained section 271 approval. *See* Second Consultation Report of the Arkansas Public Service Commission to the Federal Communications Commission Pursuant to Section 271(d)(2)(B), Docket No. 00-211-U, at 2-3 (May 21, 2001) ("*Second Consultation Report*").³⁵ As a result of its blind adoption of SWBT's Kansas NRCs, the APSC overlooked the fact that SWBT's Kansas NRCs are not TELRIC compliant, and far exceed the NRCs of all other section 271 approved states, including Texas. This failure is significant.

apply TELRIC standards. The district court did not reach any conclusions about whether SWBT's cost studies were TELRIC-compliant. Indeed, none of the issues before the district court required it to address that issue.

³⁵ One reason that the APSC did not review SWBT's proposed Arkansas rates is that the APSC views itself as lacking authority in setting UNE prices. *See* Consultation Report of the Arkansas Public Service Commission to the Federal Communications Commission Pursuant to Section 271(d)(2)(B), Docket No. 00-211-U, at 11 (December 21, 2000) ("*Consultation Report*").

This Commission has long recognized that regardless of how closely an incumbent LEC's recurring charges are held to efficient forward-looking costs, an incumbent LEC can and will evade competition if it is allowed to increase potential competitor's costs significantly through non-recurring charges. *See, e.g., AT&T Communications*, 103 FCC 2d 277, ¶ 37 (1985) ("It is evident that nonrecurring charges can be used as an anticompetitive weapon to . . . discourage competitors"); *Second Memorandum Opinion and Order on Reconsideration, Expanded Interconnection with Local Telephone Company Facilities*, 8 FCC Rcd. 7341, ¶ 43 (1993) ("absent even-handed treatment, nonrecurring reconfiguration charges could constitute a serious barrier to competitive entry"). *See also* 47 C.F.R. § 51.507(e) ("[n]onrecurring charges . . . shall not permit an incumbent LEC to recover more than the total forward-looking economic cost of providing the applicable element").

In its order establishing non-recurring rates, the Kansas Corporation Commission ("KCC") recognized that SWBT's Kansas nonrecurring rates – which, among other things assumed manual processing 100 percent of the time, thereby inflating costs by twenty times or more – flatly violated basic forward-looking principles, and it ordered SWBT to modify its studies in a number of very specific ways to correct for the most obvious errors. In particular, the KCC ordered SWBT to "rerun NRC studies" and to "use a fall out rate of 5%," to "assume electronic processing," and to "assume a 100% dedicated Inside Plant ("DIP") and an 80% Dedicated Outside Plant ("DOP") factor." *KCC Recon. Order* at 27. *See also id.* (noting that "both SWBT and AT&T seem to acknowledge" that a "1-2% fall out rate" is achievable in the long run); *id.* at 28 ("Staff and AT&T have persuasively argued that charges for NRCs should not be based on inefficient manual processing systems"); *id.* at 26-28 ("electronic processing is a reasonable assumption for calculation of nonrecurring costs, which is consistent and arguably

required under the TELRIC costing principles which this Commission and the FCC have adopted”). Indeed, SWBT has claimed that its OSS achieve these levels of electronic processing.

SWBT never complied with these orders, leaving its Kansas nonrecurring rates in plain violation of TELRIC principles. SWBT simply refiled its NRC studies with most of the very same errors, including, for many NRCs, the same erroneous 100 percent manual processing assumption. *See KC NRC Order* at 13 (“Staff notes that in spite of direct language in Commission orders, SWBT submitted a cost study based on fully manual processes; *id.* at 27 (“The Commission specifically directed SWBT to use a fall out rate of 5 percent”). Despite the KCC’s Reconsideration Order finding that the resubmission of cost studies was necessary because SWBT’s original proposals were “overstated,” the prices set forth “in SWBT’s resubmitted cost study are significantly higher than the prices submitted in SWBT’s original studies.” *Id.* at 41 (emphasis added). *See also id.* at 41-42 (“No explanation has been provided explaining why a re-submitted cost study could have caused a doubling, tripling or even quadrupling of the UNE prices”).

Although the KCC acknowledged that SWBT’s refusal to comply with the KCC’s orders (and TELRIC principles) with regard to non-recurring charges, it nevertheless claimed to be bound by its “agree[ment] to support SWBT’s [section 271] application” *KCC NRC Order* at 24. In an eleventh hour attempt to minimize the impact of SWBT’s grossly overstated nonrecurring charges, the KCC applied an entirely arbitrary one-third/two-thirds weighting of the SWBT and AT&T NRCs. But the resulting NRCs still far exceeded (and continue to exceed) forward-looking costs. Because of SWBT’s clearly erroneous manual processing, fallout and DIP/DOP assumptions, SWBT’s rate proposals were many times higher than AT&T’s TELRIC-

based proposals, and thus even weighting SWBT's study at 1/3 had the effect of more than doubling the resulting rates above cost-based levels. *See* Baranowski AR/MO Decl. ¶¶ 79-89.

SWBT itself apparently recognized that its NRCs were clearly excessive and volunteered an insufficient "25 percent discount" to those rates, which are SWBT's current Kansas rates that were imported into Arkansas.³⁶ But that 25 percent discount to rates that are already as much as 100 percent above cost-based levels was clearly insufficient to bring SWBT's Kansas NRCs – and now Arkansas NRCs – within the realm of TELRIC compliance. As explained above, there can be no non-arbitrary finding that an across the board haircut off of excess rates produces cost-based rates.

The excessive nature of SWBT's Kansas NRCs – which SWBT has imported into Arkansas – is obvious when those NRCs are compared to SWBT's Texas NRCs. For instance, SWBT's UNE-P NRC for Analog to Switch Port Cross-Connect is more than five times higher than that in Texas. *See* Baranowski AR/MO Decl. ¶ 82. Likewise, SWBT's Kansas individual UNE NRCs DS1 Trunk Port, Dedicated Cross Connect Voice Grade 2w, STP Port, White Page Information Zone 3, and Feature Activation Charges are from two-thirds to fifty times than those in Texas. *See id.*

These intrastate NRC disparities are significant and telling. As correctly pointed out by the KCC, "NRCs should not be expected to vary significantly across SWBT's jurisdictions because the activities associated with the NRCs are expected to be very similar across these jurisdictions." *KCC Recon. Order* at 26. *See also KCC Final Order* at 32 ("variances between Kansas [NRC] prices and other states should be limited"). Thus, the fact that SWBT's Kansas NRCs (and now Arkansas NRCs) significantly exceed those of Texas

³⁶ *See Ex Parte* Presentation, Letter to Magalie Roman Salas, Secretary, from Goeffrey M. Klineberg (filed December 28, 2000) ("Dec. 28 *ex parte*").

strongly suggests that SWBT's Kansas and Arkansas NRCs are well outside the bounds of TELRIC compatibility.

SWBT has argued that the massive differences in NRCs in Kansas and Texas can be explained by differences in opinion among the Kansas and Texas commissions. *See* Lundy AR/MO Decl. ¶¶ 27-29. For example, SWBT claims that the rate disparities between Kansas and Texas reflect a difference in opinion between the two commissions as to whether to allow a "trip charge." *See id.* That is clearly wrong. First, there was no trip charge proposed in Kansas or approved by the KCC. Nor could a trip charge have been justified as TELRIC compliant. The Texas Public Utility Commission ("TPUC") squarely rejected the inclusion of such charges in SWBT's Texas NRCs. *See* Baranowski AR/MO Decl. ¶ 84. That finding was proper because, as AT&T's testimonials established, SWBT's proposed Texas "trip charges" reflected phantom "trips" that an efficient operator would never make.³⁷

SWBT's inflated Arkansas NRCs will have an especially adverse impact on CLECs' ability to successfully compete for new customers. As this Commission has recognized, "a substantial percentage of the customers that purchase CLEC local services are [classified as] 'new service' customers" (*Kansas/Oklahoma 271 Order* ¶ 61 n.168) for which SBC NRC rates are 48 percent higher. *See* Flappan/Browne KS Decl. ¶ 8 (attached to Baranowski AR/MO Decl.). As a result, SWBT's inflated NRCs ensure that its competitors incur average costs that are much higher than SWBT's own costs. That is precisely what Checklist Item 2 is designed to prevent.

³⁷ *See Ex Parte* Letter from Dina Mack, AT&T, to Magalie Roman Salas, FCC Secretary, *Joint Application of SBC et. al. for Provision of In-Region InterLATA Service in Kansas and Oklahoma*, CC Docket No. 00-217 (filed January 17, 2001).

The bottom line is that the SWBT's massively inflated Kansas NRCs are not TELRIC-compatible and are discriminatory. Thus, APSC's blind adoption of those NRCs results in equally non-TELRIC compatible and discriminatory rates for Arkansas, in direct violation of Checklist Item Two.

II. SWBT HAS FAILED TO COMPLY WITH ITS PERFORMANCE REMEDY PLAN

There is no factual basis for SWBT's claims that its performance reporting and monitoring plans in Arkansas and Missouri “constitute probative evidence that the BOC will continue to meet its Section 271 obligations and that its entry would be consistent with the public interest.”³⁸ In its prior Section 271 decisions, the Commission has recognized that performance monitoring and enforcement mechanisms, could “constitute probative evidence that the BOC will continue to meet its Section 271 obligations and that its entry would be consistent with the public interest.”³⁹ The Commission has also made clear that, when an applicant, such as SWBT here, relies on a performance monitoring and enforcement plan to support its application, it will review the contours of that plan to assess whether it provides sufficient incentives for compliance with Section 271, stating:

Where, as here, a BOC relies on performance monitoring and enforcement mechanisms to provide assurance that it will continue to maintain market-opening performance after receiving section 271 authorization, *we will review the mechanisms involved to ensure that they are likely to perform as promised.* While the details of such mechanisms developed at the state level may vary widely, *we believe that we should examine certain key aspects of these plans to determine whether they fall within a zone of*

³⁸ SWBT AR/MO Br. at 156 (citing *Kansas/Oklahoma 271 Order* ¶ 269).

³⁹ *New York 271 Order* ¶ 429. See also *Massachusetts 271 Order* ¶ 236; *Kansas/Oklahoma 271 Order* ¶ 269.

*reasonableness, and are likely to provide incentives that are sufficient to foster post-entry checklist compliance.*⁴⁰

Moreover, the FCC has identified certain key elements in a performance monitoring and enforcement plan that will buttress a showing “that markets will remain open after grant of the application.”⁴¹ For example, in the *New York 271 Order*, the FCC found that the New York performance assurance plan would serve as an effective mechanism for ensuring future Section 271 compliance because it, contained, *inter alia*, “meaningful and significant incentive[s]” that would assure compliance with performance standards, as well as “a self-executing mechanism that does not leave the door open unreasonably to litigation and appeal.”⁴²

In its Joint Application, SWBT asserts that its performance remedy “plans in Arkansas and Missouri – involving self-executing payments to the Arkansas and Missouri State treasuries, as well as to CLECs – are practically ‘mirror images’ of” its Texas remedy plan that this Commission previously approved.⁴³ Emphasizing the striking similarities of the key components in its remedy plans, SWBT maintains that the Commission’s evaluation of its Missouri and Arkansas remedy plans under the public interest standard should be relatively simple. In this regard, SWBT contends that, because the major components in its Texas plan are identical to the provisions in its Arkansas and Missouri remedy plans, “it necessarily follows that SWBT’s performance incentive plans in Arkansas and Missouri, ‘include[] appropriate, self-executing enforcement mechanisms that are sufficient to ensure compliance with the established performance standards.’”⁴⁴ Accordingly, on the strength of this Commission’s prior approval of

⁴⁰ *New York 271 Order* ¶ 433 (emphasis added). See also *Texas 271 Order* ¶ 423; *Kansas/Oklahoma 271 Order* ¶ 273.

⁴¹ *New York 271 Order* ¶ 423.

⁴² *Id.* ¶ 433.

⁴³ SWBT AR/MO Br. at 159.

⁴⁴ SWBT AR/MO Br. at 160 (citations omitted).

its Texas remedy plan, SWBT entreats this Commission to bless its Missouri and Arkansas performance remedy plans as well. The Commission should not and must not rise to the bait.

SWBT's recent conduct reveals that, under the Texas remedy plan, SWBT has skillfully avoided paying liquidated damages to which AT&T is entitled, flouted the authority of the TPUC to compel SWBT to implement revisions to performance measures and remedies, cavalierly ignored or unilaterally modified the language of the plan to suit its purposes, and mired or threatened to mire the CLECs in litigation that undermines the Commission's stated goal of having "self-executing enforcement mechanisms that are automatically triggered by noncompliance in the applicable performance standard without resort to lengthy regulatory or judicial intervention."⁴⁵ Because the Missouri and Arkansas remedy plans are, by SWBT's own admission, "mirror images" of the Texas remedy plan -- a plan that has not operated in the self-executing manner envisioned by the Commission when it approved SWBT's Texas 271 application -- the performance and monitoring mechanisms in Arkansas and Missouri cannot and will not provide the necessary incentives that will foster post-entry statutory compliance.⁴⁶

A. SWBT's Recent Conduct in Texas Confirms That Its Remedy Plans Are Not Self-Executing.

When SWBT urged the Commission to approve its Texas Section 271 application, SWBT represented that its Texas remedy plan satisfied all of the key criteria of an effective performance plan identified by the Commission with its *New York 271 Order*.⁴⁷ Thus, for example, SWBT contended that its Texas remedy plan was "self-executing without any opportunities for appeal that would conceivably affect SWBT's incentives to comply" with its

⁴⁵ *Michigan 271 Order* ¶ 394; *Second BellSouth Louisiana Order* ¶ 369.

⁴⁶ See DeYoung Decl. ¶¶6-9.

⁴⁷ See *id.* ¶ 13.

obligations thereunder.⁴⁸ Additionally, SWBT heralded the comprehensiveness of its performance measures and standards and asserted that the six-month review procedure before the TPUC would assure the continuing refinement of performance measures whenever market experience dictates that such modifications are necessary.⁴⁹

In opposing SWBT's Texas 271 application, the CLECs argued that the Texas remedy plan did not contain sufficient incentives to deter SWBT from engaging in discriminatory conduct after Section 271 entry.⁵⁰ Thus, for example, AT&T pointed out that SWBT had demonstrated a penchant for inappropriately ascribing its performance failures to external factors, and that it would undoubtedly abuse the waiver provisions in the remedy plan to avoid making liquidated damages payments to which CLECs were entitled.⁵¹

Relying on, *inter alia*, the representations of SWBT and the TPUC regarding the efficacy of the enforcement mechanisms in the Texas remedy plan, the Commission found that SWBT's Texas "performance remedy plan provides additional assurance that the local market will remain open after SWBT receives Section 271 authorization."⁵² In this regard, the Commission expressed confidence that the Texas remedy plan would trigger self-executing remedy payments, and that the TPUC would "take appropriate action" to assure that SWBT could not delay or otherwise avoid its obligations by "abusing the dispute-resolution procedures provided in the Plan."⁵³ The Commission was also convinced that the six month review process in the Texas remedy plan would spawn the continuing development of measures that would

⁴⁸ SWBT Brief in Support of Application for Provision of In-Region InterLATA Services in Texas ("Texas Application") at 22. *See also* DeYoung Decl. ¶ 13.

⁴⁹ *See* Dysart Tex. Aff. ¶ 45 at 21; DeYoung Decl. ¶ 14.

⁵⁰ DeYoung Decl. ¶ 15.

⁵¹ *Id.*

⁵² *Texas 271 Order* ¶ 420.

reflect the dynamic changes in the telecommunications industry, including new measures for “DSL-related services.”⁵⁴ Indeed, the Commission emphasized that the six-month review process “is an important feature because it allows the Plan to reflect changes in the telecommunications industry and in the Texas market.”⁵⁵ Unfortunately, actual market experience has demonstrated that the Texas remedy plan has not lived up to the Commission’s expectations.⁵⁶

The Texas remedy plan has not generated penalty payments “that are automatically triggered by noncompliance with the applicable performance standards.”⁵⁷ In that connection, SWBT’s own performance results confirmed that SWBT consistently failed the parity standard for Performance Measure 27 that measures the average installation interval for non-dispatch UNE-P orders. However, instead of paying AT&T the liquidated damages to which it is entitled, SWBT seized upon the waiver provisions in the Texas remedy plan and advised the TPUC by letter that it was withholding AT&T’s penalty payments.⁵⁸ SWBT’s decision to withhold these payments was and is wholly improper.

Under the Texas remedy plan, SWBT is not permitted to withhold payments below the procedural cap unless it has instituted an expedited dispute resolution proceeding on or before the penalty due date, and the TPUC has issued a finding confirming that SWBT’s performance failures were attributable to an act of a CLEC in “bad faith.”⁵⁹ When SWBT

⁵³ *Id.* ¶ 427.

⁵⁴ *Id.* ¶ 425.

⁵⁵ *Id.* ¶ 425 (footnote omitted).

⁵⁶ DeYoung Decl. ¶¶ 16-36.

⁵⁷ *Michigan 271 Order* ¶ 394.

⁵⁸ DeYoung Decl. ¶ 20.

⁵⁹ *Id.* ¶¶ 22-23.

advised the TPUC that it was withholding AT&T's liquidated damages payments, SWBT did not explicitly allege -- nor could it -- that its performance failures were somehow due to AT&T's bad faith. *Id.* ¶¶ 20-23. And, importantly, in clear violation of the plan, SWBT withheld AT&T's penalty payments without instituting the required expedited dispute resolution proceeding or obtaining the TPUC's prior approval. Relatedly, in construing similar provisions in Ameritech's performance remedy plan, SBC's witness during hearings conducted before the Illinois Commerce Commission confirmed that, unless Ameritech "initiate[s] an expedited procedure before the remedy payments are due, the penalty payments must be paid to the CLECs."⁶⁰

Because SWBT improperly withheld liquidated damages to which AT&T is entitled, AT&T was forced to file a complaint that is currently pending before the TPUC. *See id.* ¶¶ 18-24. These most recent events demonstrate that the Commission should not and must not accept any representations that SWBT makes in this proceeding regarding the efficacy of the self-executing remedial mechanisms in its Texas remedy plan – the same provisions which are incorporated in its Missouri and Arkansas remedy plans. Recent history confirms that the enforcement mechanisms under the Texas remedy plan are not self-executing, and that SWBT believes that it can avoid making liquidated damages payments whenever it suits its purposes, thereby shifting to CLECs the burden of instituting litigation to collect the purported automatic payments that should have been triggered by the self-executing mechanisms under the Texas remedy plan.⁶¹

⁶⁰ DeYoung Decl. ¶ 25. *In the Matter of Petition for Resolution of Disputed Issues Pursuant to Condition (30) of the SBC/Ameritech Merger Order*, No. 01-0120 (Illinois Commerce Commission) Tr. 275 (Levy) (Aug. 31, 2001) (Ex. 7).

⁶¹ DeYoung Decl. ¶ 26.

B. SWBT's Recent Conduct in Texas Confirms That It Has Not Implemented and Will Not Implement Changes to Measures and Remedies.

In its *New York 271 Order* and subsequent orders, the Commission has emphasized the importance of performance monitoring mechanisms that reflect the ever-evolving changes in the telecommunications industry. Thus, for example, in its *New York 271 Order*, the Commission “applaud[ed] the role played by the New York Commission in providing a forum for ongoing modification and improvement of the performance metrics.”⁶² Additionally, in approving SWBT’s Texas Section 271 application, the Commission observed that the six-month review process in the Texas remedy plan “is an important feature because it allows the Plan to reflect changes in the telecommunications industry and in the Texas market.”⁶³

In its application and when it has otherwise suited its purposes, SWBT has hailed the six month review proceeding as the appropriate and ultimate forum within which to resolve all issues relating to its performance measures and to assure ongoing refinements to its remedy plan that are dictated by market experience. *See* DeYoung Decl. ¶¶ 19-20, 28. Thus, for example, in its initial Missouri 271 application, SWBT stated that the six-month review process spawned important changes to its measures and was such “an important feature” that “the FCC has twice lauded the SWBT Performance Measurements Plan’s ability to evolve”.⁶⁴

Similarly, in its current application, SWBT asserts that it is fully committed to ensuring that its performance remedy plans continue “to evolve” to reflect the dynamic changes in the telecommunications market.⁶⁵ As evidence of that commitment, SWBT represents that it has “implement[ed] all changes that were ordered by the Texas PUC in its six-month review

⁶² *New York 271 Order* ¶ 438.

⁶³ *Texas 271 Order* ¶ 425.

⁶⁴ *Dysart MO Aff.* ¶ 16 (April 2, 2001).

⁶⁵ SWBT AR/MO Br. at 156.

process.” *Id.* However, SWBT’s representation is belied by its public filings before the TPUC confirming that SWBT has not implemented all changes to measures and remedies ordered by the TPUC, and that it has absolutely no intention of complying with any order arising out of the six-month review process, absent its consent or separate arbitration proceedings subject to appeal. *See* DeYoung Decl. ¶¶ 29-35.

Thus, for example, when this Commission approved SWBT’s Texas 271 application, it fully expected that new “performance measurements for provision of DSL-related services” would be developed.⁶⁶ However, in rejecting a recent request by the TPUC Staff for proposed measures that would improve SWBT’s performance with respect to DSL-related service, SWBT stated that “the Performance Remedy Plan cannot be changed without the mutual consent of the parties . . . [and that it] is not amenable to changes in the plan based on its current high level of performance.”⁶⁷

Similarly, after the second six month review proceeding which culminated in an order from the TPUC directing SWBT to implement modifications to performance measures and pay liquidated damages, SWBT filed a petition for reconsideration challenging the very authority of the TPUC to compel it to comply with any order arising out of the six-month review process.⁶⁸ Noting that certain aspects of the TPUC’s order were “regrettably unacceptable,”⁶⁹ SWBT argued that the changes to the measures and remedies ordered by the TPUC were of “no benefit to CLECs or to the public.” *Id.* Notably, among the directives that SWBT found “unacceptable”

⁶⁶ *Texas 271 Order* ¶ 425.

⁶⁷ DeYoung Decl. ¶ 34, Southwestern Bell Telephone Company’s Proposal with Regard to the Performance Remedy Plan, Project No. 20400 (Tex. PUC) (Aug. 15, 2001) at 1 (Ex. 11).

⁶⁸ DeYoung Decl. ¶ 30-32.

⁶⁹ DeYoung Decl. ¶ 31, Southwestern Bell Telephone Company’s Motion for Rehearing and Clarification, Project 20400 (Tex. PUC) (July 2, 2001) at 3 (Ex. 9).

and of “no benefit to CLECs” were requirements that SWBT implement new special access performance measures, institute a sampling methodology regarding the accuracy of its loop qualification database, and pay liquidated damages for failing to comply with business rules and violating performance standards for its flow-through measure. *Id.*

In its petition for reconsideration, SWBT advised the TPUC that it could *not* compel it to make liquidated damages payments:

[T]he Performance Remedy Plan is a form of liquidated damages to which both parties must voluntarily agree in order for the penalty to be lawful and binding, as was done in the T2A. SWBT does not agree to liquidated damages for these identified PMs and any attempt to compel a negotiated agreement would constitute a violation of SWBT’s constitutional rights to due process.⁷⁰

Furthermore, SWBT announced that it had *no* obligation to comply with any order resulting from the six month review unless SWBT concurred or a separate arbitration proceeding was conducted subject to rights of appeal:

SWBT’s Filing on July 2, 2001 was intended to advise the Commission and the parties of its disagreement with certain aspects of Order No. 33. Absent consent by SWBT to implement all of the directives arising out of this PM collaborative proceeding, the Commission cannot require implementation without mutual agreement of the parties or, with respect to new measures, unless and until an arbitration on the record subject to appellate rights is conducted.⁷¹

SWBT’s position is wholly untenable. Section 6.4 of the Texas remedy plan provides that, during the six-month review procedure, “[a]ny changes to existing performance measures and this remedy plan should be by mutual agreement and, if necessary, with respect to new measures and their appropriate classification, by arbitration.” Although the term

⁷⁰ DeYoung Decl. ¶ 33, Southwestern Bell Telephone Company’s Motion for Rehearing and Clarification, Project No. 20400 (Tex. PUC) (July 2, 2001) at 4 n. 3 (Ex. 9).

⁷¹ DeYoung Decl. ¶ 32, Reply of Southwestern Bell Telephone Company, Project No. 20400 (Tex. PUC) (July 13, 2001) at 2 (Ex. 10).

“arbitration” is not specifically defined in the remedy plan, the process followed by the parties and the TPUC during the six-month review process – which included extensive off-the-record negotiations at the direction of the TPUC, the exchange of written statements outlining areas of dispute, and full-blown evidentiary hearings culminating in the issuance of an order on all unresolved issues⁷² – clearly constituted the “arbitration” that Section 6.4 contemplated. The TPUC has not yet ruled upon SWBT’s petition for reconsideration.

In all events, six-month review proceedings with full-blown hearings culminating in orders that SWBT is free to disregard – coupled with motions for reconsideration and followed by separate arbitration and appeals proceedings – cannot possibly satisfy the Commission’s vision of an “evolv[ing]” plan that would reflect changes in the industry and the marketplace that the Commission deemed an “important feature” of SWBT’s plan when it approved SWBT’s Section 271 application in Texas.⁷³ More fundamentally, SWBT’s current stance threatens to undermine the Section 271 compliance monitoring process in Texas. Because SWBT considers any order arising out of the six-month review process as a mere non-binding recommendation that it can ignore, resource-constrained CLECs must now seriously reassess whether they should even participate in these proceedings.⁷⁴ Additionally, if SWBT can disregard the outcome of the six-month review process and compel separate arbitration proceedings subject to appeal, SWBT will be able to delay experiencing financial consequences for plainly discriminatory conduct. Further, if SWBT can successfully avoid complying with orders issued by the TPUC arising out of the six month review process absent its consent, it

⁷² DeYoung Decl. ¶ 30.

⁷³ *Texas 271 Order* ¶ 425

⁷⁴ DeYoung Decl. ¶ 38.

clearly has no incentive to reach any agreements on issues that can facilitate competitive entry.⁷⁵ And it will be impossible for performance measures and remedies to evolve in a timely manner that will capture the dynamics in the telecommunications market.⁷⁶

Against this backdrop, SWBT's actions in Texas have made a mockery of the basis upon which this Commission approved its Texas remedy plan. SWBT's refusal to pay liquidated damages, its defiance of the authority of the TPUC, its unilateral manipulation of the express provisions in the Texas remedy plan, and its attempt to force the CLECs to collect damages and enforce performance standards through costly and lengthy proceedings illustrate that SWBT's assertions here regarding the efficacy of the self-executing mechanisms in its Texas remedy simply cannot be credited. Accordingly, this Commission should and must decline SWBT's invitation to bless its Missouri and Arkansas performance remedy plans on the strength of this Commission's prior approval of the Texas remedy plan. The CLECs' recent experiences in Texas confirm that the Texas remedy plan has been anything but self-executing, and that SWBT has not implemented and cannot be trusted to implement in the future its market-opening obligations under the Act.

III. SWBT HAS NOT FULLY IMPLEMENTED ITS CHECKLIST OBLIGATIONS WITH RESPECT TO ADVANCED SERVICES.

SWBT has failed to fully implement its checklist obligations with respect to advanced services in two important respects. First, SWBT is not providing CLECs with full, nondiscriminatory access to the resale of DSL services at an appropriate avoided-cost discount. Second, SWBT is not providing CLECs with full, nondiscriminatory access to line-sharing for fiber-fed loops. Each of these violations justifies rejection of SWBT's application.

⁷⁵ *Id.* ¶ 39.

⁷⁶ See e.g. *Texas 271 Order* ¶ 425 n. 1243 (noting the importance of the six-month review process that will ensure continuing refinements to the remedy plan).

A. SWBT Unlawfully Denies Competitors Resold DSL

SWBT's application should be denied because it fails to resell DSL service at a wholesale discount, in violation of Sections 251(c)(4) and 271(c)(2)(B)(xiv) of the Act. *First*, by its own admission, SWBT still engages in split billing with unaffiliated ISPs. That is, SWBT admits that it continues to bill individual consumers for DSL transport as it previously has done. Thus, although SWBT contends that it no longer accepts new orders from ISPs requesting split billing and "is working with the ISPs to convert existing split-billed accounts to consolidated billing" (SWBT AR/MO Br. at 57), the fact remains that SWBT is currently billing end-users directly for DSL as a stand-alone service. That fact is further confirmed by the web site of one of the unaffiliated "ISP partners" of SWBT, which states that its customers purchase their service from SWBT, but their Internet service from the ISP. Finney Decl. ¶¶ 19-20.

Because SWBT today continues separately to provide and bill individual customers for DSL transport at retail, SWBT today remains obligated, under the Commission's *Second Advanced Services Order*, to offer stand-alone DSL Transport to competitors for resale at a wholesale discount.⁷⁷ SWBT's failure to do so is a stark checklist violation and alone requires that its joint application be denied.

It is no answer to maintain, as SWBT does, that the business plan of its subsidiary, ASI, "simply does not include retail DSL Transport services." SWBT AR/MO Br. at 52. As the D.C. Circuit has held, and this Commission has since confirmed, neither SBC nor SWBT may avoid its checklist obligations for advanced services "by setting up a wholly owned

⁷⁷ See *Second Advanced Services Order*, ¶ 3 ("advanced services sold at retail by incumbent LECs to residential and business end-users are subject to the section 251(c)(4) discounted resale obligation, without regard to their classification as telephone exchange service or exchange access service").

*affiliate to provide those services.”*⁷⁸ See *Connecticut 271 Order* ¶ 32. (“to the extent Verizon’s attempt to justify a restriction on resale of DSL turns on the existence of VADI as a separate corporate entity (or even a separate division), it is not consistent with the *ASCENT* decision”). SBC’s (and SWBT’s) business plan has plainly included selling DSL Transport services on a mass-market basis. Indeed, in its “Investor Briefing” on its 2nd quarter 2001 results, SBC stated that it “[i]ncreased its DSL in-service base to more than 1 million,” and that it “views DSL as a strategic growth driver for the future – capable of delivering to business and residential end-users a host” of services, “as well as high-speed Internet access.”⁷⁹ Because SWBT has not shown that it is making DSL services available for resale at a wholesale discount, it has not met the requirements of the checklist.⁸⁰

Second, SBC’s recent efforts to evade its resale obligation only compound its unlawful discrimination against competitors. As recently as April 23, 2001, SWBT was actively marketing DSL transport directly to customers, featuring a website that advertised “DSL Transport only” and invited the end-user to “Order *just the DSL feature* and use your current Internet Service Provider (ISP) or an ISP from our ISP Partners Program.” Finney Decl. ¶ 12 (emphasis added). SWBT then dropped that offer in response to AT&T’s claim that it created an obligation to resell that DSL transport service. When AT&T pointed out that SWBT was accomplishing the same result by providing split billing with ISPs, SWBT again revised its web page to eliminate split billing. See *id.* ¶¶ 14-16; *Habeeb Aff.* ¶ 38 & Att. D. In each case, SWBT eliminated products from the market that it previously provided and that customers desired solely

⁷⁸ *Association of Communications Enterprises v. FCC*, 235 F.3d 662, 668 (D.C. Cir. 2001) (“*ASCENT I*”) (emphasis added).

⁷⁹ SBC Investor Briefing, “SBC’s Second-Quarter Diluted Earnings Per Share Increases 8.9% With Focus on Disciplined Financial Management, Growth Drivers,” dated July 25, 2001, at 5 (located at http://www.sbc.com/Inestor/Financial/Earning_Info/docs/2Q_1B_FINAL_Color.pdf); Finney Decl. ¶ 21 & Att. 4.

and concededly in order to deny competitors access to DSL transport at a wholesale discount. *E.g.*, *Habeeb Aff.* ¶ 38; *see also* *SWBT AR/MO Br.* at 57-58.⁸¹

This bald effort to deny competitors the ability to resell DSL, while at the same time exploiting its own ability, through creation of an affiliated ISP subsidiary, to jointly market local voice and DSL service, is precisely the sort of leveraging of the local monopoly that the Communications Act in general and sections 201, 202, 251, and 271 in particular forbid and are intended to prevent.⁸² SWBT's actions are intended to and will have the effect of blocking CLECs from competing in the market for local exchange service and advanced services. In its recent *Connecticut 271 Order*, the Commission recognized that Verizon's policy of limiting resale of DSL to situations where Verizon remained the voice carrier "severely hinders the ability of other carriers to compete," because it "prevents competitive resellers from providing both DSL and voice service to their new customers, while Verizon is able to offer both together to its customers." Such a result, the Commission concluded, would be "clearly contrary to the pro-competitive Congressional intent underlying section 251(c)(4)."⁸³

⁸⁰ *See, e.g., Second Advanced Services Order*, ¶¶ 17-18.

⁸¹ *See* *SWBT AR/MO Br.* at 57 ("SBC has modified the web sites that had been identified in the initial Missouri proceedings to make unmistakably clear that SBC does not currently offer DSL transport services directly to end-user customers at retail but rather offers such services exclusively to ISPs"); *Habeeb Aff.* ¶ 38 (SWBT's web site and other published materials "that became the subject of comments in the initial Missouri 271 proceeding have been reviewed and revised to eliminate any suggestion that DSL Transport is a retail product").

⁸² SWBT's deletion of its "DSL Transport only" offering is also unlawful because it constitutes a discontinuance of common carrier service without filing an application for, and having previously received, Commission approval. That practice is clearly contrary to the Commission's recent admonition that common carriers are required to follow the procedures set forth in Part 63 of its rules, and to obtain Commission authorization, "before discontinuing, reducing, or impairing common carrier services." *See* DA 01-1173, *Reminder To Common Carriers Regarding Discontinuance of Domestic Service Under Section 234 of the Communications Act* (released May 8, 2001). *See also* *SWBT AR/MO Br.* at 56 n.46 (acknowledging that "DSL transport services are telecommunications services subject to the resale requirements of section 251(b)(1)").

⁸³ *Connecticut 271 Order* ¶ 32.