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January 30, 2003

EX PARTE – Via Electronic Filing

Ms. Marlene Dortch
Secretary
Federal Communications Commission
The Portals
445 12th Street, S.W.
Washington, DC 20554

Re: CC Docket Nos. 01-338, 96-98, and 98-147

Dear Ms. Dortch:

Attached for inclusion in the record of this proceeding is a letter to Chairman Powell and the commissioners addressing a January 21, 2003 submission by SBC Communications, Inc., BellSouth Corporation, and Qwest Communications International, Inc., that argued that the Commission has the authority to override change-of-law provisions in existing interconnection agreements. The attached letter refutes that contention.

In accordance with FCC rule 1.49(f), this *ex parte* letter and attachment are being filed electronically pursuant to FCC Rule 1.1206(b)(1).

Sincerely,

/s/

Christopher J. Wright
Counsel Z-Tel Communications, Inc.

cc:

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January 30, 2003

Ex Parte

Honorable Michael K. Powell
Chairman
Honorable Kathleen Q. Abernathy
Honorable Michael J. Copps
Honorable Kevin J. Martin
Honorable Jonathan S. Adelstein
Commissioners
Federal Communications Commission
445 12th Street, S.W., Room 8-B201
Washington, DC 20554

Re: Commission override of change-of-law provisions in existing interconnection agreements, CC Docket Nos. 01-338, 96-98, and 98-147

Dear Chairman Powell and Commissioners:

On behalf of Z-Tel Communications, this filing further addresses the legal effect of the change-of-law provisions in existing arbitration agreements between ILECs and competitive carriers. Z-Tel recently submitted an ex parte letter explaining that, as a practical matter, little would change if the Commission were to delay issuance of a Triennial Review decision beyond February 20, because arbitration agreements' change-of-law provisions typically require notice and good-faith negotiation, followed by specified dispute resolution procedures.[1] On January 21, 2003, SBC Communications, BellSouth Corporation, and Qwest Communications International, Inc. (the "BOCs"), submitted a letter making the surprising claims that those provisions do not mean what they say and, in any event, that this Commission has authority simply to override them.[2] As further set forth below, those arguments proceed from a fundamentally mistaken view of the 1996 Act, as well as of court decisions interpreting it.

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[1] *See* Letter of January 23, 2003 from Christopher J. Wright, on behalf of Z-Tel Communications, to Chairman Michael K. Powell.

[2] *See* Letter of January 21, 2003 from Michael K. Kellogg to Marlene H. Dortch ("*1/21/03 BOC Letter*").

1. *The D.C. Circuit's* USTA *decision remanded the Commission's unbundling rules, but did not "vacate" them*: As the Commission recently explained in its motion to the D.C. Circuit to extend the partial stay of the mandate, the *USTA* court did not expressly indicate any intent to vacate the *UNE Remand Order*.[3] To the contrary, while the body of the court's opinion stated that the *Line Sharing Order* "must be vacated and remanded," *see* 290 F.3d at 429, the decision makes no similar statement about the *UNE Remand Order*. And "the *USTA* decision did not even *address* directly the specific network elements identified" in the *UNE Remand Order*[4] – let alone suggest that any or all of the Commission's unbundling requirements could not be justified by an appropriate impairment analysis. Under these circumstances, it strains credulity to suggest that the *USTA* court intended to cast a shadow of uncertainty over the competitive industry by vacating the *UNE Remand Order*.

2. *Regardless of the intent of the* USTA *decision, the requirement that BOCs unbundle loops, transport, switching and signaling at cost-based rates is a* statutory *obligation that cannot be "vacated"*: More fundamental than the BOCs' misinterpretation of the *USTA* decision, however, is their mistaken view that the issue of "vacatur" has much significance as to them. It does not. As Z-Tel has explained in detail elsewhere, section 271 plainly requires the BOCs to unbundle loops, transport, switching, and signaling for "the reasonably foreseeable future,"[5] regardless of whatever additional unbundling the Commission may require under section 251(d)(2).[6] In the *UNE Remand Order*, the Commission expressly reaffirmed that section 271 requires the BOCs to provide unbundled access to items on the checklist,[7] and Verizon's filing of its pending Forbearance Petition implicitly recognizes that fact.[8]

Section 271 was not at issue in *USTA* and could not, of course, have been "vacated" by the D.C. Circuit even if it had been. The statute's unbundling obligations constitute unequivocal congressional

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[3] *Emergency Consent Motion of the Federal Communications Commission to Extend Partial Stays of Mandates, United States Telecom Association v. FCC*, Nos. 00-1012, *et al.* & 00-1015, *et al.* (Dec. 4, 2002).

[4] *Id.* at 6.

[5] 141 Cong. Rec. S8,469 (daily ed. June 15, 1995) (statement of Senator Pressler); *see generally* Opposition of Z-Tel Communications, Inc. to Petition for Forbearance of Verizon (filed Sept. 3, 2002) (explaining in detail that the BOCs must continue to unbundle the section 271 UNEs until the forebearance standards of section 10 have been satisfied and, by that standard, that Verizon's Petition for Forbearance is grossly premature).

[6] Of course, as to UNEs that do not appear on the section 271 checklist, the *USTA* decision may have some limited effect on BOC unbundling.

[7] *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996* ("*UNE Remand Order*"), 15 FCC Rcd 3696 (1999), ¶ 468 ("[P]roviding access and interconnection to [the elements on the section 271 checklist] remains an obligation for BOCs seeking long distance approval.").

[8] *See* Petition for Forbearance of Verizon (filed July 29, 2002).

commands that remain in force regardless of the legal status of the Commission's "impairment" analysis under section 251(d)(2). Accordingly, as to the BOCs, the only effect of "vacatur" of the Commission's rules implementing section 251(d)(2) – even had it occurred – would be to raise the question of how items on the section 271 checklist should be priced. But as Z-Tel has also argued in this proceeding,[9] the statute itself answers that question. In 1996, Congress adopted a new model of federal/state cooperation to govern the resolution of disputes between carriers concerning network elements. Under section 252, if an incumbent local exchange carrier and a new entrant cannot agree on the rates for network elements to be leased, the state commissions are explicitly authorized to arbitrate the dispute. Specifically, section 252(a)(1) provides that all interconnection agreements must "include a detailed schedule of itemized charges for . . . network elements included in the agreement." Section 252(c)(2), in turn, directs state commissions arbitrating interconnection agreements to "establish any rates for . . . network elements according to subsection (d)." Section 252(d)(1)(A), of course, provides that rates for unbundled network elements must be cost-based; that provision was construed by the Commission to call for TELRIC pricing, and that determination was upheld by the Supreme Court over the BOC's jurisdictional and substantive objections.[10]

This basic statutory scheme has not been affected by the *USTA* decision, whatever the court may have intended on the question of "vacatur." Section 271 continues to mandate that BOCs unbundle the checklist UNEs; section 252(c)(2) continues to authorize state commissions to set rates through arbitration when the parties cannot agree; and section 252(d)(1)(A) continues to require state commission to set cost-based rates. The BOCs' one-sided focus on the *USTA* decision and section 251(d)(2) unbundling misses this fundamental point.

3. *As to the BOCs, there has been no significant change of law, and even if there were, the Commission would have no authority to override the change-of-law provisions in existing interconnection agreements*: The BOCs' recent letter devotes considerable energy to arguing that the "D.C. Circuit vacatur . . . creates the change of law." That assertion is wrong on several levels. First, as briefly set forth in Part 1 of this letter, there has been no "vacatur." Second, as discussed directly above, even if there had been a "vacatur," there would be little "change of law" relevant to the BOCs.[11] Prior to the *USTA* decision, the BOCs were required to unbundle loops, transport, switching, and signaling at cost-based rates (under section 251(d)(2)), and since the *USTA* decision the BOCs are still required to unbundle loops, transport, switching, and signaling at cost-based rates (under section 271). The thrust of the "law," at least as to the BOCs, has not "changed."

The BOCs' argument is also inconsistent with clear intent of the parties in the interconnection agreements themselves. As discussed by Z-Tel in its January 23, 2003 letter, interconnection agreements – usually at the proposal of the BOC – generally address with specificity the impact of

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[9] *See, e.g.,* Letter of December 20, 2002, to Chairman Powell from Robert A. Curtis and Thomas M. Koutsky, Z-Tel Communications, Inc., at 2-5 ("*12/20/02 Letter*").

[10] *AT&T Corp. v. FCC*, 525 U.S. 366 (1999) (rejecting the BOCs' jurisdictional arguments); *Verizon Communications Inc. v. FCC*, 122 S. Ct. 1646 (2002) (rejecting the BOCs' substantive arguments).

[11] As set forth in note 6, there might be minor changes in the law regarding elements that do not appear on the section 271 checklist.

possible legal and regulatory changes on the legal rights of the parties. The amount of litigation that the Telecommunications Act of 1996 has spawned is no secret and the BOCs were thus fully aware of the possibility of changes in law when they entered into these interconnection agreements. That is why the BOCs agreed to the clear, contractual change-of-law provisions that – with their January 21 letter – they now ask this Commission to overturn due to some form of "buyer's remorse." Z-Tel urges this Commission, however, that it is not the FCC's job to protect the BOCs from the consequences of contractual language that they agreed to (and, again, often even proposed).

Furthermore, under many of these change-in-law clauses, even if the *USTA* case were to have substantial implications for BOC unbundling – which it does not – there would be no "change of law" until appeals in the case have run their course.[12] Similarly, in the event that the upcoming Triennial Review decision changes the BOCs unbundling obligations – an unlikely result in light of the requirements of section 271, which are not at issue in the Triennial Review proceeding – there will be no "change of law" until that order is effective and all appeals of the order have concluded.

There is good reason for interconnection agreements to have change-in-law provisions that operate in this manner. The parties to the transactions (especially, although not they alone) underlying these agreements desire certainty to allow them to execute their business plans. Entering the local telecommunications market in a state can take years of effort and require the expenditure of significant sunk costs and those efforts and expenditures cannot reasonably be made in the absence of certainty. Moreover, it is not only the CLECs that rely on predictable, enforceable agreements – CLECs, of course, provide service to *customers* pursuant to the representations and commitments made by ILECs in these interconnection agreements. This Commission should recognize that, particularly in a period of widespread legal uncertainty, it simply makes good sense *not* to disconnect or disrupt service to customers until all of the litigation surrounding the availability, terms, or conditions of these ILEC commitments has fully played out. Cutting off customers while litigation and appeals are pending is the antithesis of the public interest.

The BOCs suggest that, regardless of what these negotiated, contractual change-of-law provisions say, this Commission has authority simply to "override" them.[13] Aside from being utterly cavalier, that assertion stems from a fundamentally mistaken view of the Act's division of authority between federal and state regulatory agencies. As set forth in Part 2, *supra*, in 1996 Congress established a regime in which *Congress itself* mandated that the BOCs must unbundle certain UNEs for the "foreseeable future" under section 271; *this Commission* was directed both to determine what additional elements should be made available on a nation-wide basis and by non-BOC ILECs, and to issue pricing rules to govern pricing of UNEs; and *the state commissions* were given authority to arbitrate interconnection agreements, including establishing prices for UNEs through the application of FCC pricing rules. Within that framework, it makes no sense to suggest that this_Commission can override provisions of interconnection agreements *over which Congress gave authority to the state commissions*.

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[12] A petition for certiorari review of *USTA* remains pending before the Supreme Court. Briefs in opposition to certiorari are due on February 5.

[13] *See 1/21/03 BOC Letter* at 3-5.

The Supreme Court's opinion in *AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 381 (1999) does not – despite the frequency and fervor with which it is cited by the BOCs – imply otherwise. That case indisputably did uphold (over the BOCs' objections) this Commission's regulatory jurisdiction to issue pricing rules to be applied in establishing the rates for network elements. But the *Iowa Utilities* case did nothing (and, indeed, could do nothing) to disturb Congress's judgment that the state regulatory authorities – with their greater proximity to the facts and the parties – are the appropriate entities to arbitrate interconnection agreements and to apply this Commission's pricing rules to set rates for individual UNEs in specific markets.

When viewed in this context of shared federal/state authority, the BOCs repeated citations to the Supreme Court's *Mobile-Sierra* doctrine are obviously inapposite.[14] The *Mobile-Sierra* doctrine sensibly gives the Commission limited authority to order a change in rates over which *it* has authority when necessary. As stated by the D.C. Circuit: "For all contracts *filed with the FCC*, it is well-established that the Commission has the power to prescribe a change in rates when it finds them to be unlawful [or] . . . when necessary to serve the public interest." *Cable & Wireless, P.L.C. v. FCC*, 166 F.3d 1224, 1231-32 (D.C. Cir. 1999) (internal quotation marks and citations omitted; emphasis added). But the change-in-law provisions here are clearly *not* rates or contract terms "filed with the FCC" but rather are integral terms of contracts over which Congress expressly gave *state commissions* authority. The BOCs would thus expand *Mobile-Sierra* from a doctrine allowing the FCC to prescribe rate adjustments in limited circumstances to one that would allow the FCC to "override" any term in any contract involving telecommunications, regardless of whether the FCC has authority over that contract. This Commission should not expand the *Mobile-Sierra* doctrine in such dramatic fashion.

A brief examination of the *Mobile* and *Sierra* cases themselves helps to illustrate the limited nature of the doctrine. Both cases posed the question whether a utility company could supercede a contract rate between it and a customer through the simple expedient of unilaterally filing a new rate with the Federal Power Commission. Not surprisingly, in both cases the Supreme Court held that a utility could not change its rates in this manner, regardless of whether the commission approved the newly filed rate.[15] The Court went on to observe, however, that under the relevant statute the agency had "undoubted power" to prescribe a new rate upon a finding that a contractual rate was unlawful or inconsistent with the public interest.[16] Clearly, however, this *Mobile-Sierra* principle that an agency with the power to prescribe rates may supercede a contractual rate upon a finding that the rate is unlawful has no application here. As discussed above, this Commission does *not* have any power to prescribe the terms of interconnection agreements – those agreements are, by statute, the domain of state commissions, and those same state commissions are explicitly charged with setting the rates for unbundled network elements.

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[14] *See Federal Power Comm'n v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956); *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332 (1956).

[15] *See Sierra*, 350 U.S. at 353.

[16] *Id.*

The BOCs' argument would turn the *Mobile-Sierra* doctrine on its head. As discussed above, the doctrine was originally developed to *protect* the private right of contract from undue governmental intrusion (*e.g*, by allowing a newly filed tariff to eviscerate a pre-existing private contract rate) except in cases where the government shows that the "public interest" is otherwise served. That public interest standard, one court observed, is "practically insurmountable." *See Papago Tribal Utility Authority v. FERC*, 723 F.3d 950, 954 (D.C. Cir. 1983). As a result – as discussed above – the Supreme Court's *Mobile- Sierra* doctrine places strong limitations upon a federal regulatory authority's ability to override private contractual terms.

The appellate court cases cited by the BOCs also do not remotely suggest that the *Mobile-Sierra* doctrine extends to FCC abrogation of agreements arbitrated by state commissions under section 252. To the contrary, those cases involved federal agencies regulation of rates over which the federal agencies themselves had express statutory authority. *Cable & Wireless, P.L.C. v. FCC*, 166 F.3d 1224 (D.C. Cir. 1999), for example, posed the question whether the FCC could prohibit U.S. companies from paying more than specified "settlement rates" for services relating to the completion of international calls. The court emphasized that "[a]t least three provisions of the Communications Act authorize the FCC to regulate the settlement rates that U.S. carriers pay to foreign carriers." And "[g]iven the [Commission's] expansive powers" over those rates under the statute, the court held, there could be no doubt that the Commission had authority to "regulate such prices directly." Again, however, that is not the case here – the statute, far from giving the FCC the authority over the terms of interconnection agreements, expressly delegates that responsibility to the state commissions.

Western Union Tel Co. v. FCC, 815 F.2d 1495 (D.C. Cir. 1987), also cited by the BOCs, directly supports Z-Tel's position that the change-of-law provisions may not be "overridden" by this Commission. *Western Union* involved a settlement agreement entered into between a number of long distance carriers and AT&T-owned local operating companies, setting forth rates for the leasing of special access facilities and providing that new rates could not become effective on less than six months notice. Years later – after what the court aptly characterized as a "tortuous history" – the FCC found the settlement agreement rates to be unlawfully low and purported to abrogate the agreement (including the six months notice period) and order an immediate 20% increase in rates. *Id.* at 1500-01. The D. C. Circuit reversed and remanded, protecting the private right of contract in that case, and preventing the Commission from simply "jettisoning" the notice provision of the agreement. That provision was an "integral part of the original settlement agreement, which the Commission approved," and was "understandably thought to ensure appropriate and full consideration of any proposed rate increases before they would become effective." *Id.* at 1502. There was, the court held, "no reason to think that the[] clause[] did not continue to serve those useful purposes." *Id.*

Much the same is, of course, true here. The change-of law provisions now attacked by the BOCs are "integral parts" of existing interconnection agreements, properly approved by the state commissions pursuant to the Act. As discussed above, these clauses have a legitimate purpose and were generally voluntarily-negotiated between ILECs and CLECs. In particular, these clauses were understandably intended by the parties to ensure both continuity of service to customers pending litigation and the use of predictable and mutually acceptable procedures in negotiating any amendments to the agreements necessitated by changes in the law. As the court in *Western Union* held, there is no reason to think that the provisions do not continue to serve those useful purposes, and certainly there is no warrant or authority for the FCC to "override" them. Indeed, that is particularly true in the present circumstances because – unlike in *Western Union* – the agreements at issue were not even initially subject to FCC approval. Rather, as noted above, they were approved (pursuant to the Act) by the state commissions. Those commissions are therefore the proper forums for renegotiations or other alterations.

Moreover, if the FCC were to act as the BOCs suggest, it would directly reverse a long-standing policy without providing notice. Such action would violate the Administrative Procedure Act. As the BOCs concede, the FCC has specifically *declined* to apply the *Mobile-Sierra* doctrine to interconnection agreements: "[T]he *Mobile-Sierra* doctrine does not apply to interconnection agreements under sections 251 and 252 of the Act, because the Act itself provides the standard of review of such agreements."[17] Significantly, in making the determination that the Act itself, not *Mobile-Sierra*, governs alterations of interconnection agreements, the Commission cited 47 U.S.C. § 252(e)(2), the provision that sets forth the grounds for State commission rejection of interconnection agreements. Section 252 as a whole (entitled "Approval by State Commissions") delegates authority over interconnection agreements to the state commissions; the specific subsection cited by the Commission (entitled "Grounds for Rejection") authorizes *state commission* to "reject" an interconnection "agreement (or any portion thereof)" on certain narrow, specified grounds. Clearly, then, as this Commission has previously held, parties wishing to amend existing interconnection agreements are directed by the statute itself to the state commissions, which are the entities with statutory authority over those agreements. That rule is clearly the announced policy of the agency; if the Commission wishes to change it, it must allow parties an opportunity for notice and comment consistent with the requirements of the APA. *See Sprint Corp. v. FCC*, 2003 U.S. App. LEXIS 910, *10-11.

The BOCs suggest that in the 1996 *Local Competition Order* the FCC "applied *Mobile-Sierra*" in circumstances analogous to those presented here.[18] It did not. Notably, the CMRS contracts affected by that FCC decision *were not* interconnection agreements negotiated pursuant to sections 251 and 252 of the 1996 Act. Those CMRS contracts instead were subject to the Commission's explicitly preemptive Title III authority over CMRS, 47 U.S.C. 332. In addition, in that case, the Commission merely held that CMRS providers who had been strong-armed by ILECs into contracts that did not – in clear violation of section 20.11 of the Commission's rules, which predated enactment of the 1996 Act – provide for mutual compensation for transport and termination of the other carrier's calls were to be allowed to renegotiate those agreements.[19] There is, of course, nothing surprising in the Commission's 1996 determination that companies upon which the ILECs had "imposed" illegal agreements should be allowed to renegotiate them, particularly given that those CMRS contracts explicitly fell within the FCC's Title III authority. Nothing similar is at issue with regard to section 251-252 interconnection agreements – those interconnection agreements were voluntarily negotiated or arbitrated, then filed with state commissions, and then approved by those same state commissions. There can be no serious suggestion that the change-of-law provisions arrived at through that process violate either the

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[17] *IDB Mobile Communications, Inc. v. COMSAT Corp.*, Memorandum Opinion and Order, 16 FCC Rcd 11474, ¶ 16 n. 50 (2001).

[18] *See* 1/21/03 *BOC Letter* at 3.

[19] *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, First Report and Order, 11 FCC Rcd 15499, ¶ 1095 (1996).

Commission's rules or any other provision of law. Moreover, even if that decision in 1996 could be interpreted as an application of the *Mobile-Sierra* doctrine to interconnection agreements, that policy has been subsequently overridden by the Commission's clear statement in 2001 in the *IDB Mobile Communications* case that *Mobile-Sierra* does not apply to section 251-252 interconnection agreements.

Finally, the BOCs' argument that the Commission should at least "clarify" that changes to interconnection agreements negotiated pursuant to existing change-of-law provisions "must become effective within the time frame established by the Commission for its new rules" is merely a variation on its failed *Mobile-Sierra* argument.[20] Essentially, the BOCs claim that even if the Commission lacks authority to "override" the change-of-law provisions, it may still "blue pencil" them from afar. Again, in the context of the federal/state division of authority established by the 1996 Act, this argument makes no sense. Interconnection agreements are creatures of state law,[21] and changes to those agreements should therefore be made under the auspices of the state authorities as section 252 plainly provides. Of course, state commissions remain bound by the Act – including this Commissions' regulations implementing the Act (*e.g.*, state commissions must apply TELRIC in setting UNE rates) – and that obligation will extend to this Commissions' eventual decision in the Triennial Review. Clearly, however, the proper forums in which to determine the effects of that forthcoming decision on state-arbitrated interconnection agreements are the state commissions.

* * * * *

In sum, as Z-Tel has previously argued, it is far more important that this Commission issue a <u>correct</u> decision in the Triennial Review than that it issue a decision by February 20 – although Z-Tel certainly desires a decision sooner rather than later. As a practical matter, however, little will change on February 21; existing arbitration agreements' change-of-law provisions will apply. The unbundling requirements of sections 251(c)(3) and 271(c)(2)(B) will remain the law of the land. Unbundling under those provisions pre-dated the FCC's 1996 *Local Competition* rules; unbundling continued even though the Eight Circuit stayed many aspects of those rules in 1997; unbundling remained after the Supreme Court vacated those rules in 1998; and unbundling will (by statute) remain on February 21. And even if the law were somehow to change, existing interconnection agreements would remain binding on both CLECs and ILECs pursuant to their own change-of-law provisions. Those provisions set forth the legally binding processes by which any amendments to interconnection agreements necessitated by changes in the law may be made. This Commission lacks authority to ignore or override them.

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[20] 1/21/03 *BOC Letter* at 6-7.

[21] *See, e.g., Southwestern Bell Telephone Co. v. Public Service Commission of Texas*, 208 F.3d 475 (5th Cir. 2000); *Illinois Bell Telephone Co. v. Worldcom Technologies, Inc.*, 179 F.3d 566 (7th Cir. 1999); *Southwestern Bell Telephone Co. v. Brooks Fiber Communications*, 235 F.3d 493 (10th Cir. 2000) (all holding that interpreting the provisions of an interconnection agreement is a matter of state law).

Sincerely,

/s/

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Thomas M. Koutsky
Vice President, Law and Public Policy