

BALCH
& BINGHAM LLP

Robin G. Laurie
(334) 269-3146

December 20, 2011

BY HAND DELIVERY

Mr. Walter Thomas
Secretary
Alabama Public Service Commission
RSA Union Building
8th Floor
100 N. Union Street
Montgomery, Alabama 36104



Re: BellSouth Telecommunications, Incorporated d/b/a AT&T Southeast d/b/a AT&T Alabama v. Life Connex Telecom, LLC, f/k/a Swiftel, LLC Docket No. 31317

BellSouth Telecommunications, Incorporated d/b/a AT&T Southeast d/b/a AT&T Alabama v. Tennessee Telephone Service, LLC d/b/a Freedom Communications, LLC, d/b/a Freedom Communications USA, LLC Docket No. 31318

BellSouth Telecommunications, Incorporated d/b/a AT&T Southeast d/b/a AT&T Alabama v. Affordable Phone Services, Inc. d/b/a High Tech Communications Docket No. 31319

BellSouth Telecommunications, Incorporated d/b/a AT&T Southeast d/b/a AT&T Alabama v. Image Access, Inc. d/b/a New Phone Docket No. 31320

BellSouth Telecommunications, Incorporated d/b/a AT&T Southeast d/b/a AT&T Alabama v. Budget Prepay, Inc. d/b/a Budget Phone Docket No. 31321

BellSouth Telecommunications, Incorporated d/b/a AT&T Southeast d/b/a AT&T Alabama v. BLC Management, LLC d/b/a Angles Communications Solutions Docket No. 31322

BellSouth Telecommunications, Incorporated d/b/a AT&T Southeast d/b/a AT&T Alabama v. dPi Teleconnect, LLC Docket No. 31323

Mr. Walter Thomas
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Dear Mr. Thomas:

BellSouth Telecommunications, Inc. ("AT&T") filed an order from the North Carolina Utilities Commission with a letter claiming that the order will inform on issues to be determined by this Commission. That order should not guide the Commission's determinations here, for several reasons. Moreover, if the Commission is to consider decisions from other commissions, it will want to consider those from states that have not adopted AT&T's position, such as South Carolina (which adopted in-part the Resellers' position) and Louisiana (which remanded the administrative law judge's recommendation to adopt AT&T's positions). In any event, the North Carolina order is ill considered and likely to be reversed on appeal for several reasons, and thus should not guide the Commission's determinations here.

The Public Service Commission of South Carolina issued a Commission Directive November 9, 2011 rejecting AT&T's proposed methodology for calculating the cash back promotional credits due CLEC resellers when the value of the rebate is greater than the first month's charges (which is the case with respect to the cash back promotions at issue in this case). A copy of the South Carolina Commission Directive is attached hereto as Attachment "A."

The South Carolina Commission determined with respect to the calculation of the cash back promotional credits due resellers as follows:

I. Cash Back Offers.... However, since the retail customer gets his rebate after keeping the service for thirty days, this Commission finds that thirty days should be the basis for calculating the rebate. *In the case where the rebate is greater than the first month's charges, discounting the rebate means that the BellSouth retail customer in effect gets a better price than the CLEC. This is definitely not what we believe the Telecommunications Act of 1996 intended. Therefore, in the special cases where the rebate exceeds the first month's cost of service, we find that the retail discount should not be applied to [the] rebate.*¹

In addition, the Louisiana Public Service Commission ("LPSC") remanded to the Administrative Law Judge a proposed decision adopting AT&T's positions. A copy of the LPSC Remand Order is attached hereto as Attachment "C." Also enclosed is a copy of the Resellers' Brief on Remand filed with the LPSC as Attachment "D."

¹ AT&T recently filed with the Commission a copy of its Petition for Rehearing and/or Reconsideration of the South Carolina Commission's Directive. On December 7th, the South Carolina Commission dismissed AT&T's Petition for Rehearing without prejudice or objection by any party as premature because the South Carolina Commission has not yet issued its written order. A copy of the South Carolina Commission Order is attached hereto as Attachment "B."

In any event, should this Commission look for guidance from other state commissions on the issues pending in the above-referenced docket, the North Carolina order should not be followed because it is irretrievably flawed by its violation of federal law and the parties' respective agreements; consequently, it should be overturned on appeal. Furthermore, the North Carolina order bases its decision not on the undisputed *actual* facts, but on *hypothetical* facts which make the North Carolina order unsustainable as precedent and subject to reversal on appeal.

The first tenet of federal law that the North Carolina order violates was made clear by the FCC in the *Local Competition Order*: when calculating wholesale rates, the wholesale rate would be set "***below*** retail rate levels."² The FCC also repeatedly expressed its concern that promotions would be used by ILECs to avoid their resale obligations – namely, the ILECs' obligation to wholesale their services at a rate "below retail rate levels." In fact, in the space of four paragraphs on promotions, the FCC articulates this concern *no less than five times*:

- "We are concerned that conditions that attach to promotions and discounts could be used to avoid the resale obligation to the detriment of competition"³;
- "we are concerned that excluding promotions [from the wholesale obligation] may unreasonably hamper the efforts of new competitors that seek to enter local markets through resale."⁴;
- "***To preclude the potential for abuse of promotional discounts***, any benefit of the promotion must be realized within the time period of the promotion. . . ."⁵;
- "In addition, an incumbent LEC ***may not use promotional offerings to evade the wholesale obligation***, for example by consecutively offering a series of 90 day promotions."⁶;
- Consequently, the FCC found that:

² See *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, First Report and Order, CC Docket No. 96-98, FCC 96-325, 11 FCC Rcd 15499, ¶ 910 (rel. Aug. 8, 1996) ("*Local Competition Order*") (emphasis added).

³ *Id.* at para. 952.

⁴ *Id.* at para. 950

⁵ *Id.* at para. 950 (emphasis added)

⁶ *Id.* (emphasis added).

“...no basis exists for creating a general exemption from the wholesale requirement for all promotional or discount service offerings made by incumbent LECs. **A contrary result would permit incumbent LECs to avoid the statutory resale obligation by shifting their customers to nonstandard offerings, thereby eviscerating the resale provisions of the 1996 Act.**^{7,8}

The North Carolina Utilities Commission’s order strays from federal law because it does not require AT&T to sell its services subject to promotions at a wholesale rate *below* the retail rate.⁹ The North Carolina Utilities Commission’s order also allows AT&T to use promotions to avoid its wholesale obligation in violation of paragraphs 948 and 950 of the FCC’s *Local Competition Order*.

Furthermore, the North Carolina Utilities Commission’s order disregards the parties’ interconnection agreements (“ICAs”), which make clear that AT&T must make its promotions

⁷ *Local Competition Order* ¶ 948.

⁸ The FCC’s concern that ILECs would attempt to use promotions to avoid the wholesale obligation to resell services at a rate below “*below* retail rate levels” has been borne out again and again. For example, for years AT&T sought to avoid extending gift card and cash back promotions altogether, but was made to do so against its will. *See e.g., BellSouth Telecommunications, Inc. v. Sanford*, 494 F.3d 439, 442 (4th Cir. 2007); *In the Matter of dPi Teleconnect, LLC, v. BellSouth Telecommunications, Inc.*, North Carolina Utilities Commission Docket No. P-55, Sub 1744. As another example, in the second half of 2009, AT&T attempted to implement a scheme in which it proposed to credit resellers eligible for cash back promotions not the fixed \$50 cash back that the eligible retail customer received, but an amount drastically reduced by bizarre “retention” and “redemption” “factors.” The net effect had AT&T providing its retail customers a cash back credit in the amount of \$50, but extending resellers a promotion credit of only \$4.20 in Alabama; \$5.54 in Texas; \$3.73 in Georgia; \$3.65 in Tennessee; \$5.92 in Kentucky; \$3.74 in Louisiana; \$4.66 in South Carolina, and so on across all the states. This Retail Promotion Methodology Adjustment model (as it was called by AT&T) was announced in various AT&T Accessible Letters and was to go into effect in September 2009, but was enjoined by the U.S. District Court for the Northern District of Texas. *See Budget Prepay, Inc. et al., v. AT&T Inc., f/k/a SBC Communications, Inc. et al., Cause No. No. 3:09-CV-1494-P in the U.S. District Court, Northern District of Texas, Dallas Division*. Although the Fifth Circuit eventually vacated the injunction, *See Budget Prepay, Inc. v. AT&T Corp.*, 605 F.3d 273, 281 (5th Cir. 2010), it did so solely as a matter of primary jurisdiction, and without review of the facts about AT&T’s conduct the district judge had found so compelling.

AT&T’s latest scheme is no less unlawful. Because AT&T’s method for calculating the wholesale promotional price results in a wholesale price above, rather than below, the retail customer’s price, it hinders competition. As a consequence, AT&T’s method violates not just federal law, but also the parties’ ICAs, and must be repaired or replaced.

⁹ *See, e.g., 47 C.F.R. § 51.607*. “The wholesale rate that an incumbent LEC may charge for a telecommunications service provided for resale to other telecommunications carriers shall equal the rate for the telecommunications service, *less avoided retail costs*, as described in section 51.609.” [Emphasis added.]

available to resellers on terms that are no less favorable than those received by AT&T's retail customers. In fact, the ICAs at issue before the North Carolina Utilities Commission (which also apply in Alabama) show that AT&T must make promotions lasting 90 days or less available for resale at the promotional rate, but must make promotions lasting longer than 90 days available *at the promotional rate further discounted by the avoided cost*. Thus, for the long term promotions at issue in this case, the resale rate must be *below* the promotional rate.

The North Carolina Commission attempted to justify its position by reasoning that over time, the cumulative amount paid by a reseller will drop below the cumulative amount paid by the retail customer. This contravenes the undisputed fact that the promotions are paid in a single lump sum, not over time, and that the customer need not maintain service for longer than 30 days to be entitled to the cash back promotion. (See, e.g., South Carolina PSC Directive – “[S]ince the retail customer get his rebate after keeping the service for thirty days, this Commission finds that thirty days should be the basis for calculating the rebate.”) It also contravenes paragraph 950 of the *Local Competition Order*, which holds that “[t]o preclude the potential for abuse of promotional discounts, any benefit of the promotion must be realized within the time period of the promotion....”)

Despite the fact that federal law clearly expects that wholesale prices will be set *below* retail rates, and expects that this obligation will be honored even when promotions are in play, the North Carolina Utilities Commission's order adopts AT&T's approach which results in the wholesale rate being *ABOVE* the retail rate. (See, South Carolina PSC Directive – “*In the case where the rebate is greater than the first month's charges, discounting the rebate means that the BellSouth retail customer in effect gets a better price than the CLEC. This is definitely not what we believe the Telecommunications Act of 1996 intended.*”)

The North Carolina Utilities Commission suggests that *BellSouth Telecommunications, Inc. v. Sanford*¹⁰ approves AT&T's proposed method of reducing the value of the cash back promotion by the Commission's wholesale discount percentage. This is incorrect. In fact, the principle that wholesale rates should always be *below* retail rates is key to the Fourth Circuit Court of Appeals' decision in *Sanford*, the leading appellate case on promotions. In *Sanford*, the Fourth Circuit held that promotional offers extending for more than 90 days created a “promotional retail rate” to which the avoided cost (wholesale discount) must be applied.¹¹ The Fourth Circuit held that for long-term promotional offerings (such as the ones at bar), the avoided cost or wholesale discount must be subtracted from the *effective* retail rate that results from applying the value of the promotional offering to the retail rate of the underlying service.¹²

¹⁰ *BellSouth Telecommunications, Inc. v. Sanford*, 494 F.3d 439 (4th Cir. 2007).

¹¹ This “promotional retail rate” is referred to herein as the “effective retail rate.”

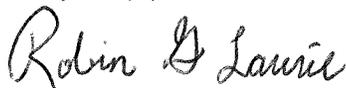
¹² *Sanford* at 442.

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The key lesson from *Sanford* is that wholesale must be less than retail. However, in cases like those at bar, where the promotion amount exceeds the retail price of the service (*e.g.*, a \$25 service combined with a \$50 cash back promotion), AT&T's methodology creates a higher price to resellers (through a smaller bill credit) than the price paid by AT&T's retail customers, which is *exactly* the outcome that *Sanford* and the South Carolina PSC found unreasonable.¹³ In effect, the AT&T formula turns *Sanford* on its head by trying to use the court's reasoning to achieve the very result – a wholesale rate above retail – that offended the *Sanford* court and caused it to reject AT&T's policy of refusing to provide the value of cash back promotions to resellers altogether.

The North Carolina Utilities Commission erred by disregarding the facts. Notwithstanding the clear directive of the law and the ICAs, AT&T admittedly does not charge resellers a price *below* the retail promotional price; it charges resellers *MORE* than the retail promotional price. Therefore, AT&T's method for calculating cash back promotion credits approved by the North Carolina Utilities Commission conflicts with federal and state law and regulations because it violates the key principle that wholesale should be less than retail. The intent of the Act would be better served by adopting the position of the South Carolina Commission or that of Louisiana Public Service Commission Staff, who both rejected AT&T's position and adopted a method which ensures that wholesale will be less than retail when cash back promotions are in effect. The South Carolina Commission has directed that in situations where the promotion exceeds the monthly cost of service, the entire amount of the promotion should be available to resellers. The Louisiana Staff advocates that in such situations, the wholesale price be the wholesale *percentage discount below* the effective retail price.

Very truly yours,



Robin G. Laurie

RGL:dpe
Enclosures
Counsel of Record

¹³ As explained by the *Sanford* court, "Because its position would not account for the promotional rebate check, BellSouth's position would obviously impede competition. The competitive LEC would have to pay BellSouth a wholesale rate of \$96 for the telephone service for which BellSouth's retail customers would pay only \$20." *BellSouth Telecommunications, Inc. v. Sanford*, 494 F.3d 439, 451 (4th Cir. 2007). Although AT&T's method as applied in the case at bar results in a slight less stark example of the wholesale rate being higher than the retail rate, it violates the same core principal from *Sanford* that the wholesale rate *must be* less than the retail rate or competition would be harmed.

ATTACHMENT A

**PUBLIC SERVICE COMMISSION OF SOUTH CAROLINA
COMMISSION DIRECTIVE**

ADMINISTRATIVE MATTER	<input type="checkbox"/>	DATE	<u>November 09, 2011</u>
			<u>2010-14-C/2010-15-C</u>
MOTOR CARRIER MATTER	<input type="checkbox"/>	DOCKET NO.	<u>2010-16-C/2010-17-C</u>
UTILITIES MATTER	<input checked="" type="checkbox"/>	ORDER NO.	<u>2010-18-C/2010-19-C</u>

SUBJECT:

DOCKET NO. 2010-14-C - Complaint and Petition for Relief of BellSouth Telecommunications, LLC d/b/a AT&T Southeast d/b/a AT&T South Carolina v. Affordable Phones Services, Incorporated d/b/a High Tech Communications;

DOCKET NO. 2010-15-C - Complaint and Petition for Relief of BellSouth Telecommunications, LLC d/b/a AT&T Southeast d/b/a AT&T South Carolina v. Dialtone & More, Incorporated;

DOCKET NO. 2010-16-C - Complaint and Petition for Relief of BellSouth Telecommunications, LLC d/b/a AT&T Southeast d/b/a AT&T South Carolina v. Tennessee Telephone Service, LLC d/b/a Freedom Communications USA, LLC;

DOCKET NO. 2010-17-C - Complaint and Petition for Relief of BellSouth Telecommunications, LLC d/b/a AT&T Southeast d/b/a AT&T South Carolina v. OneTone Telecom, Incorporated;

DOCKET NO. 2010-18-C - Complaint and Petition for Relief of BellSouth Telecommunications, LLC d/b/a AT&T Southeast d/b/a AT&T South Carolina v. dPI Teleconnect, LLC;

-and-

DOCKET NO. 2010-19-C - Complaint and Petition for Relief of BellSouth Telecommunications, LLC d/b/a AT&T Southeast d/b/a AT&T South Carolina v. Image Access, Incorporated d/b/a New Phone - Discuss this Matter with the Commission.

COMMISSION ACTION:

My motion addresses the consolidated complaints by BellSouth Telecommunications against various telecommunications service resellers for amounts allegedly owed to BellSouth in connection with certain promotions offered by BellSouth to end users. Federal law requires that former Bell System companies offer these promotions to competitive local exchange carriers (CLECs). Other federal law requires that retail services purchased for resale by CLECs be provided at the same terms and conditions, less an appropriate discount representing avoided costs by the RLEC. Under South Carolina law, that discount has been established at 14.8%.

The disputed amounts relate to three types of offers:

I. Cash Back Offers. These are rebates to the purchasing consumer that require the purchaser to remain on the BellSouth network for thirty days before the rebate check is forwarded to the customer. These rebates could be for more or less than the first month's service. BellSouth claims that the cash back promotions should be the amount provided to the BellSouth customer less the 14.8% resale discount. The CLECs argue that in order to be on the same terms and conditions as sales to BellSouth Customers, the cash back offer should not be

discounted.

This Commission finds that the rebates should be subject to the resale discount. However since the retail customer gets his rebate after keeping the service for thirty days, this Commission finds that thirty days should be the basis for calculating the rebate. If the rebate is less than the first month's charges the discount should apply to the rebate, since this has the effect of keeping that month's charges to the CLEC within the 85.2% ratio of CLEC charges to the retail rates. In the case where the rebate is greater than the first month's charges, discounting the rebate means that the BellSouth retail customer in effect gets a better price than the CLEC. This is definitely not what we believe the Telecommunications Act of 1996 intended. Therefore, in the special cases where the rebate exceeds the first month's cost of service, we find that the retail discount should not be applied to rebate.

II. Line Connection Charge Waivers. In this promotion, BellSouth offers a waiver of the Line Connection charge to the new customer. BellSouth claims that it is meeting the requirements of equal terms and conditions by waiving the Line Connection Charges. The CLECs argue that the same terms and condition clause requires BellSouth to rebate to them the difference between the BellSouth retail charge and the discounted charge that is being waived.

We find that federal law and regulations do not require the full retail amount of the Line Connection Charge to be credited to the reseller.

III. Word of Mouth Promotions. BellSouth also offers current customers a cash payment for referring new customers to BellSouth. BellSouth argues that these payments are sales promotion activities that are already included in the 14.8% discount and are therefore not available for resale. The CLECs argue that the payment is a reduction of price for the retail service and is subject to resale requirements.

We find that Word of Mouth Promotions are indeed a marketing expense included in the resale discount. It is also important that the payment goes to the referrer and not to the new retail customer. Therefore we find that Word of Mouth Promotions are not included in the resale obligation and are not subject to being paid to the reseller.

PRESIDING: Howard

SESSION: Regular

TIME: 1:30 p.m.

	MOTION	YES	NO	OTHER
FLEMING	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
HALL	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
HAMILTON	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
HOWARD	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
MITCHELL	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
WHITFIELD	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
WRIGHT	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	

(SEAL)



RECORDED BY: J. Schmieding

ATTACHMENT B

**PUBLIC SERVICE COMMISSION OF SOUTH CAROLINA
COMMISSION DIRECTIVE**

ADMINISTRATIVE MATTER	<input type="checkbox"/>	DATE	<u>December 07, 2011</u>
			<u>2010-14-C/2010-15-C</u>
			<u>2010-16-C/2010-17-C</u>
MOTOR CARRIER MATTER	<input type="checkbox"/>	DOCKET NO.	<u>2010-18-C/2010-19-C</u>
UTILITIES MATTER	<input checked="" type="checkbox"/>	ORDER NO.	<u>2011-917</u>

THIS DIRECTIVE SHALL SERVE AS THE COMMISSION'S ORDER ON THIS ISSUE.

SUBJECT:

DOCKET NO. 2010-14-C - Complaint and Petition for Relief of BellSouth Telecommunications, LLC d/b/a AT&T Southeast d/b/a AT&T South Carolina v. Affordable Phones Services, Incorporated d/b/a High Tech Communications;

DOCKET NO. 2010-15-C - Complaint and Petition for Relief of BellSouth Telecommunications, LLC d/b/a AT&T Southeast d/b/a AT&T South Carolina v. Dialtone & More, Incorporated;

DOCKET NO. 2010-16-C - Complaint and Petition for Relief of BellSouth Telecommunications, LLC d/b/a AT&T Southeast d/b/a AT&T South Carolina v. Tennessee Telephone Service, LLC d/b/a Freedom Communications USA, LLC;

DOCKET NO. 2010-17-C - Complaint and Petition for Relief of BellSouth Telecommunications, LLC d/b/a AT&T Southeast d/b/a AT&T South Carolina v. OneTone Telecom, Incorporated;

DOCKET NO. 2010-18-C - Complaint and Petition for Relief of BellSouth Telecommunications, LLC d/b/a AT&T Southeast d/b/a AT&T South Carolina v. dPi Teleconnect, LLC;

-and-

DOCKET NO. 2010-19-C - Complaint and Petition for Relief of BellSouth Telecommunications, LLC d/b/a AT&T Southeast d/b/a AT&T South Carolina v. Image Access, Incorporated d/b/a New Phone - Discuss with the Commission AT&T's Petition for Rehearing and/or Reconsideration.

COMMISSION ACTION:

On November 18, 2011, AT&T South Carolina filed a Petition for Rehearing and/or Reconsideration of the decision described in this Commission's November 9, 2011 Directive. AT&T South Carolina acknowledged that the Petition "may be premature given that the Commission has yet to issue a written order memorializing the decision described" in the Directive, and AT&T South Carolina stated that it filed the Petition "in an abundance of caution and to avoid any argument that AT&T South Carolina has failed to satisfy any condition precedent to an appeal" On November 28, 2011, the Resellers responded that they "generally oppose AT&T's Petition, but not the issuance of an order stating that AT&T's Petition is premature." Accordingly, and without objection by any party, I move we dismiss AT&T South Carolina's Petition for Rehearing and/or Reconsideration as untimely. This dismissal is without prejudice to any party's rights to file a petition seeking rehearing, reconsideration, and/or other relief as appropriate upon issuance of the Commission's written order addressing the issues described in the November 9, 2011 Directive.

PRESIDING: Howard

SESSION: Regular

TIME: 10:00 a.m.

	MOTION	YES	NO	OTHER
FLEMING	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
HALL	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
HAMILTON	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
HOWARD	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
MITCHELL	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
WHITFIELD	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	
WRIGHT	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>	

(SEAL)



RECORDED BY: J. Schmieding

ATTACHMENT C

LOUISIANA PUBLIC SERVICE COMMISSION

ORDER NO. U-31364

BELLSOUTH TELECOMMUNICATIONS, INC. D/B/A AT&T SOUTHEAST D/B/A
AT&T LOUISIANA VERSUS IMAGE ACCESS, INC. D/B/A NEW PHONE;

BUDGET PREPAY, INC. D/B/A BUDGET PHONE D/B/A BUDGET PHONE, INC.;

BLC MANAGEMENT, LLC D/B/A ANGLES COMMUNICATIONS SOLUTIONS D/B/A
MEXICALL COMMUNICATIONS;

DPI TELECONNECT, LLC;

AND

TENNESSEE TELEPHONE SERVICE, INC. D/B/A FREEDOM COMMUNICATIONS
USA, LLC

*Docket U-31364 In re: Consolidated Proceeding to Address Certain Issues Common to
Dockets U-31256, U-31257, U-31258, U-31259, and U-31260.*

(Decided at the Commission's September 7, 2011)

REMAND ORDER

BellSouth Telecommunications, Inc. d/b/a AT&T Louisiana ("AT&T") filed collection actions with the Louisiana Public Service Commission ("LPSC") against Image Access, Inc. d/b/a New Phone, Budget Prepay, Inc. d/b/a Budget Phone d/b/a Budget Phone, Inc., BLC Management, LLC d/b/a/ Angles Communications Solutions d/b/a Mexicall Communications, and dPi Teleconnect, LLC (collectively "Resellers"). On May 19, 2010, the collection dockets were consolidated for the limited purpose of addressing and resolving three issues identified in the joint motion, as well as any other common issues subsequently identified and approved for consolidation. The Parties also requested that all other pending motions in the proceedings be held in abeyance while the common issues were addressed.

The Parties, as outlined in the stipulations submitted at the time of the hearing, request a ruling on three basic issues that are to be decided in this consolidated docket, which are: Cashback Offerings, the Line Connection Charge Waiver ("LCCW") and Referral Marketing ("Word-of-Mouth"). A hearing was held on the consolidated issues on November 4 and 5, 2010. A Proposed Recommendation was issued in this matter on June 22, 2011. The Resellers filed Exceptions to the Proposed Recommendation on July 12, 2011. Staff also filed exceptions on July 12, 2011. While Staff agreed with the proposed recommendation concerning the LCCW and the Word-of-Mouth promotion, Staff re-urged that the proper treatment of Cash Back Offerings is that proposed by Staff in its Post-Hearing Brief. AT&T Louisiana filed its Opposition Memorandum to Exceptions of Resellers and Staff on July 25, 2011. AT&T Louisiana supported the Proposed Recommendation, requesting it be issued as the Final

Recommendation. After consideration of those filings, the administrative law judge issued a Final Recommendation on August 18, 2011 adopting AT&T's position on all three issues.

The ALJ's Recommendation was considered by the Commission at its September 7, 2011 Business and Executive Session. Following Oral Argument from Staff, Resellers, and AT&T, Commissioner Holloway made a motion to remand this matter back to the ALJ. Commissioner Boissiere made a substitute motion to accept the ALJ Recommendation, which was seconded by Commissioner Campbell. Commissioners Field, Skrmetta and Holloway objected. Therefore the motion died for a lack of majority. Commissioner Holloway then re-urged his initial motion to remand the matter back to the ALJ for further consideration of the methodology to be applied to cash back promotions, with Commissioners Field, Boissiere and Skrmetta voting yes to remand and Commissioner Campbell voting no.

IT IS THEREFORE ORDERED THAT:

1. This matter shall be remanded to the Administrative Hearings Division for further consideration of the calculation methodology to be applied to cash back promotions.
2. This Order shall be effective immediately.

**BY ORDER OF THE COMMISSION
BATON ROUGE, LOUISIANA**

September 28, 2011

/S/ JAMES M. FIELD
DISTRICT II
CHAIRMAN JAMES M. FIELD

/S/ CLYDE C. HOLLOWAY
DISTRICT IV
VICE CHAIRMAN CLYDE C. HOLLOWAY

/S/ FOSTER L. CAMPBELL (NO)
DISTRICT V
COMMISSIONER FOSTER L. CAMPBELL

/S/ LAMBERT C. BOISSIERE
DISTRICT III
COMMISSIONER LAMBERT C. BOISSIERE, III


EVE KAHAO GONZALEZ
SECRETARY

/S/ ERIC F. SKRMETTA
DISTRICT I
COMMISSIONER ERIC F. SKRMETTA

ATTACHMENT D

PAUL F. GUARISCO
Partner
(225) 376-0285
paul.guarisco@phelps.com

November 18, 2011

230850009
NOV 18 09 30 02
LOUISIANA PUBLIC SERVICE
COMMISSION

Terri Lemoine
Louisiana Public Service Commission
P.O. Box 91154
Baton Rouge, LA 70821-9154

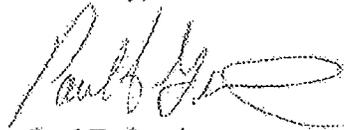
Re: Consolidated Docket No. U-31364
Louisiana Public Service Commission
In Re: BellSouth Telecommunications, Inc. d/b/a AT&T Southeast d/b/a AT&T Louisiana vs Image Access, Inc. D/BA NewPhone, Budget Prepay, Inc. D/B/A Budget Phone F/K/A Budget Phone, Inc., BLC Management, LLC D/B/A Angles Communications Solutions D/B/A Mexicall Communications, dPi Teleconnect, LLC, and Tennessee Telephone Service, Inc. D/B/A Freedom Telecommunications USA, LLC.

Dear Terri:

Enclosed please find an original and three (3) copies of the Resellers' Brief on Remand on Calculation Methodology for Cash Back Promotions to be filed into the record of the above-referenced matter.

Should you have any questions regarding this filing, please contact me.

Sincerely,



Paul F. Guarisco

Enclosures

cc: Jim Dry
Service List

ATTORNEYS AT LAW

LOUISIANA PUBLIC SERVICE COMMISSION
ADMINISTRATIVE HEARINGS DIVISION

CONSOLIDATED DOCKET NO. U-31364

BELLSOUTH TELECOMMUNICATIONS,)
INC. D/B/A AT&T SOUTHEAST D/B/A)
AT&T LOUISIANA VS. IMAGE ACCESS,) Docket No. U-31256
INC. D/B/A NEWPHONE)

BELLSOUTH TELECOMMUNICATIONS,)
INC. D/B/A AT&T SOUTHEAST D/B/A)
AT&T LOUISIANA VS. BUDGET) Docket No. U-31257
PREPAY, INC. D/B/A BUDGET PHONE)
F/K/A BUDGET PHONE, INC.)

BELLSOUTH TELECOMMUNICATIONS,)
INC. D/B/A AT&T SOUTHEAST D/B/A)
AT&T LOUISIANA VS. BLC)
MANAGEMENT, LLC D/B/A ANGLES) Docket No. U-31258
COMMUNICATIONS SOLUTIONS D/B/A)
MEXICALL COMMUNICATIONS)

BELLSOUTH TELECOMMUNICATIONS,)
INC. D/B/A AT&T SOUTHEAST D/B/A)
AT&T LOUISIANA VS. dpi) Docket No. U-31259
TELECONNECT, LLC)

BELLSOUTH TELECOMMUNICATIONS,)
INC. D/B/A AT&T SOUTHEAST D/B/A)
AT&T LOUISIANA VS. TENNESSEE)
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USA, LLC)

RESELLERS' BRIEF ON REMAND
ON CALCULATION METHODOLOGY FOR CASH BACK PROMOTIONS

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RESELLERS' BRIEF ON REMAND
ON CALCULATION METHODOLOGY FOR CASH BACK PROMOTIONS

This Brief on Remand is jointly filed by Image Access, Inc. d/b/a NewPhone, dPi Teleconnect, LLC, BLC Management, LLC d/b/a Angles Communications Solutions d/b/a Mexicall Communications, and Tennessee Telephone Service, Inc. d/b/a Freedom Telecommunications USA, LLC (collectively, the "Resellers"), pursuant to the procedural schedule set forth in the Report of October 26, 2011 Status Conference (Corrected) issued in the above-captioned Consolidated Docket on November 1, 2011.

I. INTRODUCTION

This case is about preserving the viability of wholesale competition for the benefit of Louisiana consumers, and the efficacy of federal pricing requirements. Both are jeopardized by BellSouth Telecommunications, LLC d/b/a AT&T Louisiana's ("AT&T") refusal to provide Resellers with the same amount of credit AT&T provides its own retail customers entitled to cash back promotions. The net result of applying AT&T's method is that AT&T provides services at wholesale at a price ABOVE, rather than BELOW, that which AT&T's retail customers pay. AT&T's method for calculating cash back promotional credits due to the Resellers violates federal law, the terms of the Resellers' Interconnection Agreements with AT&T ("ICAs"), and this Commission's stated policy of promoting competition via resale pursuant to its Local Competition Regulations.

More particularly, the Federal Telecommunications Act of 1996 (the "Act")¹ and federal

¹ 47 U.S.C. § 252(d)(3): Wholesale prices for telecommunications services.

regulations (particularly 47 C.F.R. § 51.607) set the resale rate for telecommunications services that an ILEC may charge at “the [retail] rate for the telecommunications service, less avoided retail costs...”² Because the wholesale price charged to the Resellers is based on AT&T’s retail price – from which one *subtracts* the costs avoided – it is clear from context that federal and state law, as well as the ICAs, necessarily direct that the wholesale price be less than the retail price. AT&T’s method for calculating cash back promotional credits to the Resellers conflicts with federal law and regulations because it violates this key principle that wholesale should be below retail. In fact, AT&T’s formula produces the opposite result: wholesale rates ABOVE retail rates.

On September 7, 2011, the Louisiana Public Service Commission (the “Commission” or “LPSC”) considered and remanded for further consideration the Administrative Law Judge’s (“ALJ”) Final Recommendation recommending the adoption of AT&T’s practice of reducing the amount of cash back credits that AT&T extends to Resellers as compared to the cash back promotional amounts that AT&T offers to its own retail customers.

The ALJ’s Final Recommendation does not correct for the fact that the methodology proposed by AT&T and adopted by the ALJ results (for the particular promotions in question) in the retail price being less than the wholesale price. LPSC Staff recognized that and proposed to

For the purposes of section 251(c)(4) of this title, a State commission shall determine wholesale rates on the basis of retail rates charged to subscribers for the telecommunications service requested, excluding the portion thereof attributable to any marketing, billing, collection, and other costs that will be avoided by the local exchange carrier.

² 47 C.F.R. § 51.607 Wholesale pricing standard.

The wholesale rate that an incumbent LEC may charge for a telecommunications service provided for resale to other telecommunications carries shall equal the rate for the telecommunications service, *less avoided retail costs*, as described in section 51.609.

“Avoided retail costs shall be those costs that reasonably can be avoided when an incumbent LEC provides a telecommunications service for resale at wholesale rates to a requesting carrier.” 47 C.F.R. § 51.609(b).

modify the AT&T formula so that the wholesale rate will always be 20.72% *below*, not above, the retail rate.

The Resellers propose that the ALJ either adopt the LPSC Staff's modified approach or find an alternative way to calculate the cash back amount. An alternative to the methodology in the ALJ's Final Recommendation would be to adopt the formula approved on November 9, 2011, by the South Carolina Public Service Commission (the "SC Commission"). The SC Commission's methodology is similar to LPSC Staff's approach. Both correctly reject AT&T's formula when the resulting wholesale rate is more than the retail rate.

The SC Commission's method simply states that, in situations where the cash back promotion is greater than the retail price, the Resellers should receive the full amount of the cash back promotion. In other words, if the retail price is \$30 and the cash back promotion is \$50, the Reseller should receive the same \$50 rebate that the retail customer receives. Under this approach (assuming a 20% wholesale discount), the retail price is reduced, following the rebate, to (-\$20) while the wholesale price is reduced to (-\$26) after the rebate. Most importantly, the SC Commission approach avoids creating a situation where the retail rate is less than the wholesale rate.³

LPSC Staff also correctly recognizes that AT&T's method results in a higher price or smaller credit to the Resellers (when compared to AT&T's retail customers) in instances where the cash back promotion amount exceeds the retail price for the underlying service and, accordingly, the AT&T method produces a result which is inconsistent with the Act and FCC

³ The SC Commission's approach adopts the logic of Resellers' witnesses Joe Gillan and Dr. Chris Klein, who argued that the Resellers should receive the same rebate amount, without any discount, that AT&T's retail customers receive. The SC Commission did not adopt this approach in all cases, but only in situations where the rebate amount is larger than the retail cost of one month's service. In other words, the SC Commission uses the AT&T methodology except in those cases where the AT&T method results in the retail price being less than the wholesale price. In that situation, the SC Commission adopts the formula recommended by Mr. Gillan and Dr. Klein.

regulations. Staff's method accomplishes this by simply making the wholesale price a percentage less than the "effective retail price" for that service to end-users, by *reducing* the "effective retail rate" by the Commission's avoided cost discount percentage.⁴

II. BRIEF PROCEDURAL HISTORY

After hearing and briefing on the merits, the ALJ issued a Proposed Recommendation in this consolidated proceeding, adopting the approach advocated by AT&T for calculating the amount of cash back promotional credits due Resellers. Over the exceptions to the ALJ's Proposed Recommendation of both the LPSC Staff and the Resellers, the ALJ issued a Final Recommendation to the Commission on August 18, 2011, containing a recommendation on the cash back promotional credits calculation consistent with the ALJ's Proposed Recommendation.

At its September 7, 2011 Open Session Business and Executive Meeting, the ALJ's Final Recommendation came before the Commission, and, after full consideration by the Commission, the Commission voted to remand this consolidated proceeding to the ALJ for reconsideration of the cash back calculation methodology, pursuant to the Commission's Remand Order issued in this docket on September 28, 2011.

⁴ Under the LPSC Staff approach, if the retail price is \$30 and the cash back promotion is \$50, the "effective retail rate" is (-\$20). Assuming a 20% wholesale discount, the "effective retail rate" is *reduced* by the wholesale discount to arrive at a wholesale price of (-\$24).

III. ARGUMENT

AT&T's method for calculating the amount of cash back promotional credits due to the Resellers (the method approved by the ALJ's Final Recommendation) violates the core principle of the Telecommunications Act that wholesale should be priced *below* retail. AT&T's violation of the law cannot be legitimized, and its method must accordingly be rejected.

A. The core principle of the Telecommunications Act regarding resale is that wholesale should be priced below retail.

The overriding principle controlling this proceeding – embodied in federal law and regulations, and recognized by (1) the Federal Communications Commission (“FCC”), (2) the U.S. Fourth Circuit Court of Appeals, (3) the LPSC Staff, and (4) the Public Service Commission of South Carolina (“SC Commission”) – is that the federal Telecommunications Act of 1996 and FCC regulations require that services sold at *wholesale should be priced below retail*. Simply put, AT&T's proposed methodology, and the methodology set forth in the ALJ's Final Recommendation, violate this core principle.

1. Federal statutes and regulations: competition by resale requires that wholesale will be less than retail.

Congress passed the FTCA with the intent of “opening previously monopolistic local telephone markets to competition.”⁵ “[The] provisions of the Telecommunications Act of 1996... were intended to eliminate the monopolies enjoyed by the inheritors of AT&T's local franchises”⁶ and also to promote competition with them.⁷

⁵ See *Southwestern Bell Telephone Co. v. Public Utility Com'n of Texas*, 208 F.3d 475, 477 (5th Cir. 2000)

⁶ See *Verizon Communications, Inc. v. FCC*, 535 U.S. 467, 476 (2002)); see also, *AT&T Communications of Southern States, Inc. v. Bellsouth Telecommunications, Inc.*, 229 F.3d 457, 459 (4th Cir.2000)(The Telecommunications Act of 1996 was intended to break local telephone monopolies.)

⁷ See, e.g., *BellSouth Telecommunications, Inc. v. Sanford*, 494 F.3d 439,441 (4th Cir.2007); *Alenco Communications, Inc. v. F.C.C.*, 201 F.3d 608, 623 (5th Cir.2000); *GTE Northwest Inc. v. Hamilton*, 971 F.Supp. 1350, 1352 (D.Or. 1997); *GTE Northwest, Inc. v. Nelson*, 969 F.Supp. 654, 656 (W.D.Wash. 1997); *GTE South Inc. v. Morrison*, 957 F.Supp. 800, 801 (E.D.Va. 1997); *Western PCS II Corp. v. Extraterritorial Zoning Authority of City and County of Sante Fe*, 957 F.Supp. 1230, 1237 (D.N.M. 1997).

One of the methods by which this goal was to be achieved was by obliging the Incumbent Local Exchange Carriers (“ILECs”), such as AT&T, to make their retail services available for resale at wholesale rates. 47 U.S.C. § 251(c)(4)(A). Competition by resale requires that resellers be allowed to purchase services at a price below retail. The concept that wholesale should be less than retail appears in the text of the Act, the FCC’s rules and orders, and the leading federal appellate case on promotions (the *Sanford* opinion) – all of which require AT&T’s promotional prices to be further discounted for resale. “Discount,” of course, means a reduction – not an increase – in price.⁸

Generally, the Act and federal regulations set the wholesale price as the retail price (or rate) less the costs (such as marketing, billing, collections, etc.) that the ILEC avoids by selling the services in bulk to the competitive Local Exchange Carriers (“CLECs”), such as the Resellers.⁹ Thus, the “wholesale discount” is the avoided cost.

Note that the resale statutes and regulations speak in terms of rates (or prices) and costs. This is most significant. While the amount of the discount is the avoided cost, that cost is subtracted from the retail price – whatever that retail price might be. “Cost” and “price” are two very different concepts: “cost” is the value of the products and services which are necessary to

⁸ “Discount - In a general sense, an allowance or deduction made from a gross sum on any account whatever”. Black’s Law Dictionary. 6th ed. 1990; “Discount - a reduction made from the gross amount or value of something; as a (1): a reduction made from a regular or list price...” Webster’s New Collegiate Dictionary. G. & C. Merriam Co., 1975.

⁹ See, e.g., 47 C.F.R. § 51.607.

47 C.F.R. § 51.607. “The wholesale rate that an incumbent LEC may charge for a telecommunications service provided for resale to other telecommunications carriers shall equal the rate for the telecommunications service, *less avoided retail costs*, as described in section 51.609.” [Emphasis added.]

47 USC 252(d)(3): Wholesale prices for telecommunications services. ... a State commission shall determine wholesale rates on the basis of retail rates charged to subscribers for the telecommunications service requested, excluding the portion thereof attributable to any marketing, billing, collection, and other costs that will be avoided by the local exchange carrier.

Sanford, 494 F. 3d. 439, 445 (4th Cir. 2007): “Thus, the wholesale rate consists of the retail rate, less whatever costs the incumbent LEC will save by selling the services in bulk to the competitive LEC.”

produce a unit of output. “Price” is the value or what a customer has to give up in order to acquire that output. Costs are not necessarily directly related to the price for a service. Simply because a price changes does not necessarily mean that a cost has changed. A price change certainly doesn’t cause a cost to change. There will always be costs associated with providing service, regardless of the level of the sales price – even if the service is given away for free, or even if the customer is given cash to take the service for one of the months that it is offered. It thus is clear from context that the Act and the rules promulgated thereunder expect that the wholesale price should be less than the retail price, because one is required to calculate the wholesale price by subtracting the costs avoided from the effective retail price.

2. **The FCC’s Local Competition Order repeatedly indicates that the wholesale price should be below the retail price, and that promotions cannot be used to circumvent this rule.**

The principle that wholesale prices should always be less than retail prices is repeatedly acknowledged by the FCC in its *Local Competition Order*.¹⁰ In the *Local Competition Order*, the FCC states that when calculating wholesale rates, the wholesale rate must be set “*below* retail rate levels.”¹¹

The FCC spent considerable effort explaining the importance of competition by resale and laying out how wholesale rates should be calculated in its *Local Competition Order*.¹² As mentioned, the FCC made clear that when using percentages to calculate wholesale rates, the

¹⁰ See In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, CC Docket No. 96-98, FCC 96-325, 11 FCC Rcd 15499 (rel. Aug. 8, 1996) (“*Local Competition Order*”).

¹¹ *Id.* at ¶ 910 (emphasis added).

¹² See, e.g., *Local Competition Order* at ¶ 907:

Resale will be an important entry strategy for many new entrants, especially in the short term when they are building their own facilities. Further, in some areas and for some new entrants, we expect that the resale option will remain an important entry strategy over the longer term. Resale will also be an important entry strategy for small businesses that may lack capital to compete in the local exchange market by purchasing unbundled elements or by building their own networks.

wholesale rate would be set by a “percent *below* retail rate levels.”¹³ The FCC also repeatedly expressed its concern that promotions would be used by ILECs, such as AT&T, to avoid their resale obligations – namely, the ILECs’ obligation to wholesale their services at a rate “below retail rate levels.” In fact, in the space of four paragraphs addressing promotions, the FCC articulates this concern no less than *five* times:

We are concerned that conditions that attach to promotions and discounts could be used to avoid the resale obligation to the detriment of competition....¹⁴

We are concerned that excluding promotions [from the wholesale obligation] may unreasonably hamper the efforts of new competitors that seek to enter local markets through resale....¹⁵

To preclude the potential for abuse of promotional discounts, any benefit of the promotion must be realized within the time period of the promotion....¹⁶

In addition, an incumbent LEC *may not use promotional offerings to evade the wholesale obligation*, for example by consecutively offering a series of 90 day promotions....¹⁷

Consequently, the FCC found that:

... [N]o basis exists for creating a general exemption from the wholesale requirement for all promotional or discount service offerings made by incumbent LECs. *A contrary result would permit incumbent LECs to avoid the statutory resale obligation by shifting their customers to nonstandard offerings, thereby eviscerating the resale provisions of the 1996 Act.*¹⁸

The FCC’s concern that ILECs would attempt to use promotions to avoid the wholesale obligation to resell services at a rate below “*below* retail rate levels” has been borne out again and again. For example, for years AT&T sought to avoid extending to resellers altogether gift

¹³ *Local Competition Order* at ¶ 910 (emphasis added).

¹⁴ *Id.* at ¶ 952.

¹⁵ *Id.* at ¶ 950

¹⁶ *Id.* at ¶ 950 (emphasis added)

¹⁷ *Id.* (emphasis added).

¹⁸ *Local Competition Order* at ¶ 948.

card and cash back promotions, but was made to do so.¹⁹ As another example, in the second half of 2009, AT&T attempted to implement a scheme in which it proposed to credit resellers eligible for cash back promotions not the fixed \$50 cash back that the eligible retail customer received, but an amount drastically reduced by bizarre “retention” and “redemption” “factors.” The net effect had AT&T providing its retail customers a cash back credit in the amount of \$50, but extending resellers a promotion credit of only \$3.74 in Louisiana; \$5.54 in Texas; \$3.73 in Georgia; \$3.65 in Tennessee; \$4.20 in Alabama; \$5.92 in Kentucky; \$4.66 in South Carolina, and so on across all the states. This Retail Promotion Methodology Adjustment model (as it was called by AT&T) was announced in various AT&T Accessible Letters and was to go into effect in September 2009, but was enjoined by the U.S. District Court for the Northern District of Texas.²⁰ Although the Fifth Circuit eventually vacated the injunction,²¹ it did so solely as a matter of primary jurisdiction, and without review of the facts about AT&T's conduct the district judge had found so compelling.

AT&T's latest scheme is no less unlawful than prior iterations. Because AT&T's method for calculating the wholesale promotional price results in a wholesale price above, rather than below, the retail customer's price, it is less favorable to the Resellers. As a consequence, AT&T's method and the ALJ's Final Recommendation allows AT&T's “promotional offerings to evade the wholesale obligation” and contravenes the FCC's objective “[t]o preclude the potential for abuse of promotional discounts.”²²

¹⁹ See e.g., *BellSouth Telecommunications, Inc. v. Sanford*, 494 F.3d 439, 442 (4th Cir. 2007); *In the Matter of dPi Teleconnect, LLC, v. BellSouth Telecommunications, Inc.*, North Carolina Utilities Commission Docket No. P-55, Sub 1744.

²⁰ See *Budget Prepay, Inc. et al., v. AT&T Inc., f/k/a SBC Communications, Inc. et al.*, Cause No. No. 3:09-CV-1494-P (N.D. TX).

²¹ See *Budget Prepay, Inc. v. AT&T Corp.*, 605 F.3d 273, 281 (5th Cir. 2010).

²² *Local Competition Order* at ¶ 950.

3. **The Fourth Circuit's *Sanford* decision holds that wholesale rates should be below retail rates, and that promotions cannot be used to circumvent this requirement.**

The principle that wholesale rates should always be *below* retail rates is also key to the U.S. Fourth Circuit Court of Appeals' decision in *Sanford*, the leading appellate case on promotions.²³ In *Sanford*, the Fourth Circuit held that promotional offers extending for more than 90 days created a "promotional retail rate" to which the avoided cost (wholesale discount) must be applied.²⁴ The Fourth Circuit held that for long-term promotional offerings (such as the cash back promotions at issue herein), the avoided cost or wholesale discount must be subtracted from the "effective retail rate" that results from applying the value of the promotional offering to the retail rate of the underlying service.²⁵

The key lesson from *Sanford* is that wholesale must be less than retail. However, in cases like those at bar, where the promotion amount exceeds the retail price of the service (e.g., a \$25 service combined with a \$50 cash back promotion), AT&T's methodology creates a higher price to resellers (through a smaller bill credit) than the price paid by AT&T's retail customers, which is *exactly* the outcome that the Fourth Circuit found unreasonable in *Sanford*.²⁶ In effect, the AT&T formula turns *Sanford* on its head by trying to use the court's reasoning to achieve the very result – a wholesale rate above retail – that offended the *Sanford* court and caused it to reject AT&T's policy of refusing to provide the value of cash back promotions to resellers altogether.

²³ See *BellSouth Telecommunications, Inc. v. Sanford*, 494 F.3d 439 (4th Cir. 2007).

²⁴ This "promotional retail rate" is referred to herein as the "effective retail rate."

²⁵ *Sanford* at 442.

²⁶ As explained by the *Sanford* court, "Because its position would not account for the promotional rebate check, BellSouth's position would obviously impede competition. The competitive LEC would have to pay BellSouth a wholesale rate of \$96 for the telephone service for which BellSouth's retail customers would pay only \$20." *BellSouth Telecommunications, Inc. v. Sanford*, 494 F.3d 439, 451 (4th Cir. 2007). Although AT&T's method as applied in the case at bar results in a slight less stark example of the wholesale rate being higher than the retail rate, it violates the same core principal from *Sanford* that the wholesale rate *must be* less than the retail rate or competition would be harmed.

- B. **AT&T's method for calculating the amount of cash back promotions due to the Resellers (the method set forth in the ALJ's Final Recommendation) violates the core principle of the Telecommunications Act that wholesale should be priced below retail.**

Notwithstanding the clear directive of the law and contract, AT&T admittedly does not charge resellers a price below the retail promotional price during the month the promotion applies - it charges Resellers MORE than the retail promotional price. As an example, when the standard retail price of a service subject to resale is \$25, the discount percentage is 20%, and a cash back promotion of \$50 applies,²⁷ the net credit due to a qualifying retail customer for service during the month the cash back promotion is realized would be \$25 less \$50, or (-\$25). However, for the same service subject to the same cash back promotion sold at wholesale, AT&T *reduces the amount of the cash back credit* by 20% , resulting in a net credit due the reseller of (-\$20) – that is, a net credit ABOVE, rather than BELOW, the net credit extended to the retail customer.

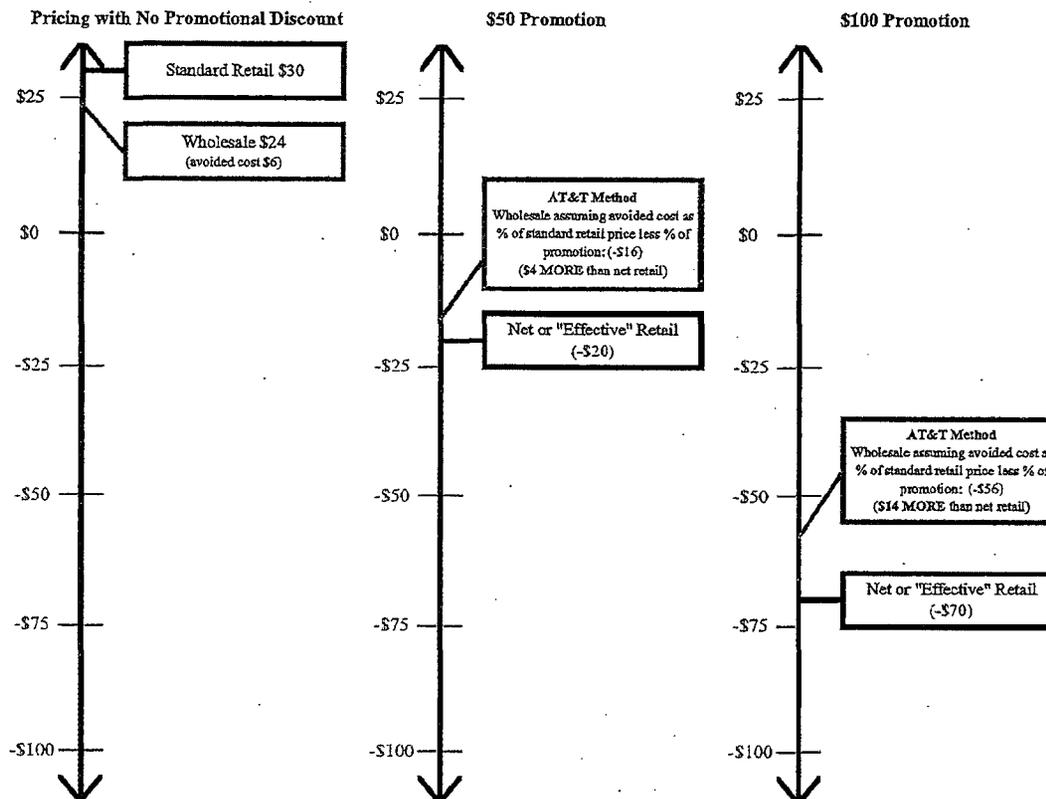
Figure 1, below, charts the results of applying AT&T's method, and shows how the net price to resellers is ABOVE, rather than *below*, the net price to AT&T's retail customers. This approach simply cannot be reconciled with the law.

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²⁷ The standard retail price and discount percentage used for illustrative purposes are round numbers roughly approximating the actual percentage and standard retail price in order to make the math easier.

FIGURE 1: AT&T's METHOD VIOLATES FEDERAL LAW

AT&T provides services at wholesale at a price *HIGHER* than that which AT&T's retail customers pay; therefore, AT&T's method violates federal law and harms competition.



Notes:

1. A hypothetical 20% wholesale discount percentage is used in this chart for demonstration purposes and mathematical simplicity only.
2. Standard Retail Price - Promotional Discount = Net or "Effective" Retail Price
3. AT&T's Method: (Standard Retail Price x Wholesale Discount Percentage) - (Promotional Discount x Wholesale Discount Percentage) = Net Wholesale Price

1. **The Public Service Commission of South Carolina rejects AT&T's method as violating the intent of the Act because it results in wholesale rates ABOVE, rather than BELOW, retail rates.**

On November 9, 2011,²⁸ the SC Commission adopted by unanimous (7-0) vote a Directive rejecting AT&T's proposed methodology for calculating the cash back promotional credits due to resellers when the value of the rebate (i.e., the cash back promotional amount) is greater than the first month's retail charges. A copy of the SC Commission Directive is attached hereto as Exhibit A.

With respect to the calculation of the cash back promotional credits due to resellers, the SC Commission found as follows:

Cash Back Offers. These are rebates to the purchasing consumer that require the purchaser to remain on the BellSouth network for thirty days before the rebate check is forwarded to the customer.

[S]ince the retail customer gets his rebate after keeping the service for thirty days, this Commission finds that thirty days should be the basis for calculating the rebate. *In the case where the rebate is greater than the first month's charges, discounting the rebate means that the BellSouth retail customer in effect gets a better price than the CLEC. This is definitely not what we believe the Telecommunications Act of 1996 intended. Therefore, in the special cases where the rebate exceeds the first month's cost of service, we find that the retail discount should not be applied to [the] rebate.* [emphasis added]

In essence, the SC Commission recognizes (as Resellers have advocated in this proceeding) that: (1) because the cash back promotion is available after maintaining 30 days of telecommunications service, it is improper to presume that it is to be paid out over a period of multiple months; (2) AT&T's method results in AT&T's retail customers receiving a better price than would the CLECs, such as the Resellers, a result which contradicts the intent of the Act; and (3) as a consequence, in situations (such as the one at hand) where the cash back promotion exceeds the monthly charge for telecommunications service, the wholesale rate must be lower

²⁸ See Public Service Commission of South Carolina, Docket Nos. 2010-14-C, 2010-15-C, 2010-16-C, 2010-17-C, 2010-18-C and 2010-19-C, Commission Directive dated November 19, 2011 ("SC Commission Directive") pp. 1-2.

than the retail rate.

The situation highlighted above in the SC Commission Directive is precisely the situation at issue here. All of the cash back promotional offerings at issue in this case are in an amount that exceeds the retail cost of the underlying telecommunications service in the initial month. Applying AT&T's method (which was advocated by the ALJ in the Final Recommendation) to these promotions creates a wholesale price which is *greater than* the retail price to end-users. AT&T's method, and the method set forth in the ALJ's Final Recommendation, allow AT&T to circumvent a core principle of the Act – namely, that wholesale prices should always be less than retail prices. This result, as acknowledged by the SC Commission – “is definitely not what we believe the Telecommunications Act of 1996 intended.”

2. AT&T cannot justify its violation of the law.

According to AT&T, we should disregard the facts, and analyze the situation as though the facts were the opposite of what they actually are. Thus, despite the admitted fact that the cash back promotions are paid in a single lump sum, and despite the fact that one need only maintain service for a single month to receive the cash back promotional credit,²⁹ we should pretend the cash back promotion is pro-rated over a span of months, because if we prorate and then compare the cumulative totals, a quirk of the way math works allows AT&T to argue that the cumulative retail price could be greater than the wholesale price over an extended period of time.

There are a number of problems with AT&T's argument.

First, it impermissibly substitutes hypothetical facts for the actual facts. In other words, AT&T is asking the trier of fact to analyze the facts NOT as they are, but as AT&T wishes they

²⁹ See Stipulations for Consolidated Phase, Attachment A; Taylor Direct Testimony, pp. 13-14; Transcript of Hearing, November 4, 2010, p. 53, lines 19-22.

might be. This is precisely the approach rejected by the SC Commission.³⁰

Second, the hypothesis that AT&T is asking the trier of fact to accept – that the cash back promotional amount is prorated over time – is specifically prohibited by the FCC: “To preclude the potential for abuse of promotional discounts, any benefit of the promotion must be realized within the time period of the promotion....”³¹ Here, the promotion is paid in a lump sum for any person otherwise qualifying and maintaining service for just one month.

Third, the argument that “it is OK to short change Resellers in the short term because we will make it up to Resellers over time” is simply not acceptable and does not conform to reality. Retail and wholesale customers alike are billed for services rendered each month, and each month is billed and collected discretely. For example, CLECs are not expected to realize their wholesale discount by paying the full retail price for four months of service, then getting the fifth month for free – for a “cumulative discount” of 20%. Whatever charges are accrued in a month are subject to the discount on *that month’s bill*.

Fourth, even if we accept AT&T’s hypothesis, it still fails in the first month, where the wholesale rate is still above, rather than below, the retail rate. If a method or formula is to be adopted, it should work in the month at issue - the first month of service – especially because there may be only one month of service.

3. The North Carolina Commission’s decision on this promotion issue should not be followed because it is contrary to federal law.

The North Carolina Utilities Commission recently released an order adopting AT&T’s method for calculating the cash back promotional credit due resellers in that state.³² AT&T is

³⁰ See SC Commission Directive at p. 2: “... since the retail customer gets his rebate after keeping the service for thirty days, this Commission finds that thirty days should be the basis for calculating the rebate.”

³¹ *Local Competition Order* at ¶ 950 (emphasis added).

³² See *BellSouth Telecommunications, Inc. d/b/a AT&T Southeast d/b/a AT&T North Carolina v. dPi Teleconnect, LLC, Image Access, Inc., d/b/a NewPhone, Affordable Phone Services, Inc., BLC Management, LLC, d/b/a Angles*

likely to argue that the North Carolina Commission has issued strong persuasive authority in this case, and that its decision should be followed here. However, the North Carolina Commission order is irretrievably flawed by its violation of federal law, and should be overturned on appeal.

The North Carolina Commission's order strays from federal law³³ because it does not require AT&T to sell its services subject to promotions at a wholesale rate below the retail rate. Consequently, it also violates paragraph 910 of the FCC's Local Competition Order, and allows AT&T to use promotions to avoid its wholesale obligation in violation of paragraphs 948 and 950 of the Local Competition Order. (These provisions are discussed in III A 2, above.) The North Carolina Commission attempts to justify its position by reasoning that given time, the cumulative amount paid by resellers will drop below the cumulative amount paid by AT&T's retail customers. This is arbitrary and capricious, because it contravenes the undisputed fact that the promotions are paid in a single lump sum, not over time, and that the retail customer need not maintain service for longer than 30 days to be entitled to the cash back promotion. It also contravenes paragraph 950 of the Local Competition Order, which holds that "To preclude the potential for abuse of promotional discounts, any benefit of the promotion must be realized within the time period of the promotion...."

Communications Solutions, and LifeConnex Telecom, Inc., f/k/a Swiftel, Dockets No. P-836, Sub 5, P-908, Sub 2, P-1272, Sub 1, P-1415, Sub 2, and P-1439, Sub 2, before the North Carolina Utilities Commission

³³ See, e.g., 47 C.F.R. § 51.607:

The wholesale rate that an incumbent LEC may charge for a telecommunications service provided for resale to other telecommunications carriers shall equal the rate for the telecommunications service, *less avoided retail costs*, as described in section 51.609. [Emphasis added.]

47 USC 252(d)(3):

Wholesale prices for telecommunications services. ... a State commission shall determine wholesale rates on the basis of retail rates charged to subscribers for the telecommunications service requested, excluding the portion thereof attributable to any marketing, billing, collection, and other costs that will be avoided by the local exchange carrier.

Sanford, 494 F. 3d. 439, 445 (4th Cir. 2007): "Thus, the wholesale rate consists of the retail rate, less whatever costs the incumbent LEC will save by selling the services in bulk to the competitive LEC."

In addition, the Resellers' ICAs³⁴ make clear that AT&T must make its promotions available to resellers on terms that are no less favorable than those received by AT&T's retail customers. Under the ICAs, promotions of 90 days duration or less must be made available to resellers at the retail promotional price. For promotions lasting longer than 90 days, AT&T must make those services available at the promotional rate further discounted by the avoided cost. AT&T's proposed method of calculating the cash back promotional credit due Resellers requires the Resellers to buy services subject to promotions at a rate above, rather than below, the retail promotional rate. Consequently, such a method violates the Resellers' ICAs.

C. Because AT&T's method violates the federal law principle that wholesale should be priced below retail, one must choose from the two remaining methods for properly calculating the cash back promotion due to the Resellers.

Because AT&T's method for determining the avoided cost discount (wholesale discount) when promotions are involved has been shown to violate the core principle behind resale (having a wholesale price that is below retail) in instances where the promotion exceeds the normal retail rate, it must be rejected. In the "negative scenario" (where there is a negative "effective retail rate"), *two methods remain*:

- (1) SC Commission Approach: the wholesale discount should be applied to the retail price but *should not* be applied to the cash back promotion, to ensure that wholesale will be less than retail, as found by the SC Commission; and
- (2) LPSC Staff Approach ("AT&T Corrected"): the "effective retail rate" must be properly *reduced* by the wholesale discount; or, stated in algebraic form, the wholesale price must be made equal to the effective retail rate, reduced by the amount arrived at by multiplying the absolute value of the effective retail rate by the wholesale discount percentage:

$$\text{Wholesale} = (\text{retail price} - \text{cash back}) - \% |(\text{retail} - \text{cash back})|$$

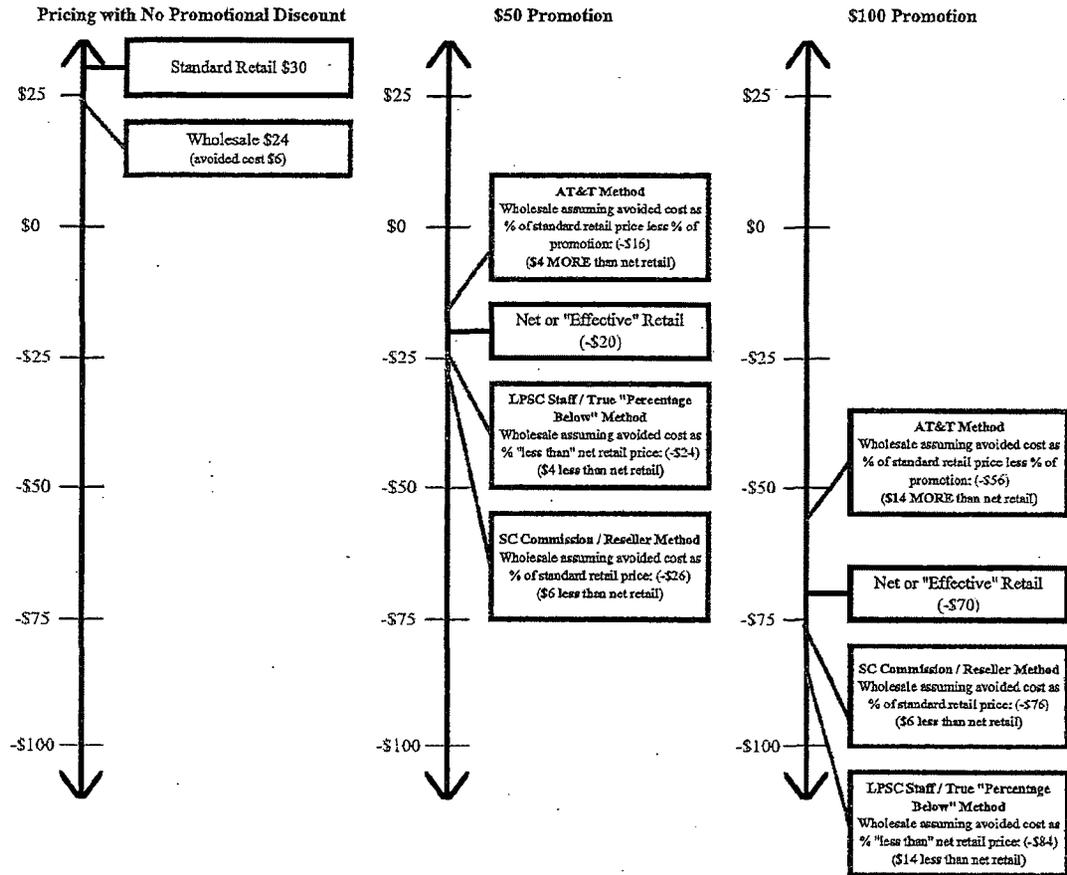
³⁴ See, e.g., Interconnection Agreement by and between AT&T and Image Access, Inc. d/b/a NewPhone dated April 19, 2006, as amended and extended on March 31, 2009, Attachment 1 - Resale, Exhibit A.

This is how one would correctly express mathematically the concept of having the effective retail rate being reduced by the wholesale discount. This approach is advocated by the LPSC Staff.

Figure 2, below, shows a comparison of the results achieved under the three methods.

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**FIGURE 2: COMPARISON OF RESULTS APPLYING AT&T'S METHOD;
SC COMMISSION'S METHOD; AND
LPSC STAFF / TRUE "PERCENTAGE BELOW" METHOD**



Notes:

1. A hypothetical 20% wholesale discount percentage is used in this chart for demonstration purposes and mathematical simplicity only.
2. Standard Retail Price - Promotional Discount = Net or "Effective" Retail Price
3. AT&T's Method: (Standard Retail Price x Wholesale Discount Percentage) - (Promotional Discount x Wholesale Discount Percentage) = Net Wholesale Price
4. SC Commission / Resellers' Method: Standard Retail Price x Wholesale Discount Percentage = Avoided Costs
Standard Retail Price - Promotional Discount - Avoided Costs = Net Wholesale Price
5. LPSC Staff / True "Percentage Below" Method: (Standard Retail Price - Promotional Discount) - (Wholesale Discount Percentage x (Standard Retail Price - Promotional Discount)) = Net Wholesale Price

1. **Replacing AT&T's method with something that works better: the SC Commission directs that Resellers are entitled to the full amount of the cash back promotions/rebates.**

The SC Commission found two fundamental flaws in AT&T's proposed methodology:

(1) the wholesale price ends up being higher than the retail price; and (2) resellers do not get the full benefit of the promotion in the same time period that retail customers get it. As noted above, the SC Commission soundly rejected these flawed outcomes and held that:

[S]ince the retail customer gets his rebate after keeping the service for thirty days, this Commission finds that thirty days should be the basis for calculating the rebate.... *In the case where the rebate is greater than the first month's charges, discounting the rebate means that the BellSouth retail customer in effect gets a better price than the CLEC. This is definitely not what we believe the Telecommunications Act of 1996 intended. Therefore, in the special cases where the rebate exceeds the first month's cost of service, we find that the retail discount should not be applied to [the] rebate.* [emphasis added]

(See Attachment 1 appended hereto).

2. **Repairing AT&T's method: LPSC Staff advocates setting the wholesale price at a consistent percentage discount BELOW the effective retail price.**

Staff correctly recognizes that AT&T's method results in a higher price or smaller credit to the Resellers (when compared to AT&T's retail customers) in instances where the cash back promotion amount exceeds the retail price for the underlying service and, accordingly, the AT&T method produces a result which is inconsistent with the Act and FCC regulations. To comply with the law, the cash back method adopted should produce a net wholesale price below the net retail price to AT&T's end-users even when the "effective retail rate" results in a credit (i.e., is negative). Staff's method accomplishes this by simply making the wholesale price a percentage less than the "effective retail price" for that service to end-users, by *reducing* the "effective retail rate" by the Commission's avoided cost discount percentage.

This approach recognizes that the Resellers are entitled by law to receive services at the effective retail rate (that is, the regular retail rate less the cash back promotion amount), further reduced by the Commission's wholesale discount percentage (i.e., the Commission established estimate of avoided costs). The LPSC Staff uses the following example to illustrate this point:

AT&T's retail service is \$40 a month, and it offers a one-time "cash-back" rebate of \$50. Under this scenario, the effective retail price of the service for the first month is a \$10 credit. Resellers should be entitled to this service, subject to the wholesale discount. Assuming the discount is 20%, the effect would be a discount of \$2.00, i.e. 20% of \$10. *However, since the number is negative, the discount is properly added, thus resulting in a one-time credit of \$12 to the reseller customer*, and preserving the 20% avoided cost on the effective retail price of the service.³⁵

The LPSC Staff's method results in wholesale always being less than retail by the amount of the Commission's established wholesale discount percentage. Or, expressed in algebraic form:

$$\text{Wholesale} = (\text{retail price} - \text{cash back}) - \% |(\text{retail} - \text{cash back})|$$

Using the absolute value function ensures that the "effective retail rate" will always be *reduced* by the Commission's avoided cost discount, resulting in a wholesale rate which is lower than retail.

Additionally, LPSC Staff responded to the ALJ's Proposed Recommendation in this consolidated docket, which is substantively identical to the ALJ's Final Recommendation, by stating:

In the Proposed Recommendation, this Tribunal concluded that the AT&T proposed methodology, that is a discount of the "cash-back" offering by the LPSC's 20.72% avoided cost, subtracted from the retail rate discounted by the LPSC's 20.72% avoided cost, is consistent with the FCC's Local Competition Order and the Orders of this Commission. Staff respectfully disagrees with this conclusion, as the Proposed Recommendation fails to first calculate the "effective retail rate" created by the "cash-back offering" prior to applying the wholesale discount, thus placing the resale customer at a competitive disadvantage to

³⁵ LPSC Staff's Post-Hearing Brief, p. 7 (emphasis added).

AT&T. This is particularly the case when applied in a negative, or credit scenario, as the AT&T methodology results in a greater credit to the retail customer.³⁶

Staff's method correctly applies the *Sanford* rationale – that wholesale should be less than retail – and, more importantly, rejects the clearly erroneous approach taken by AT&T in instances where the “effective retail rate”³⁷ of a telecommunications service results in a credit scenario (i.e., where the promotional value exceeds the retail price).

(*See Attachment 2 appended hereto*).

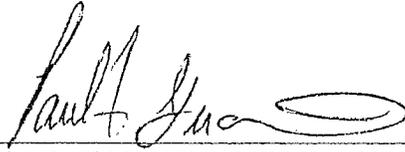
IV. CONCLUSION

At its September 7, 2011 Open Session Business and Executive Meeting, the Commission did not adopt the ALJ's Final Recommendation and instead voted to remand this proceeding to the Administrative Hearings Division “for further consideration of the calculation methodology to be applied to cash back promotions,” pursuant to the Commission's Remand Order dated September 28, 2011. The Commission, therefore, has granted the parties herein an additional opportunity to correct the inherent flaw in the methodology advocated by AT&T and set forth in the ALJ's Final Recommendation, which produces a wholesale rate greater than, not less than, the retail rate to end-users in cases where the cash back promotion exceeds the normal retail price. For the reasons set forth herein, and for the reasons propounded by the FCC, the SC Commission, the U.S. Fourth Circuit Court of Appeals and LPSC Staff, the Resellers respectfully request that the Final Recommendation be amended to adopt a calculation methodology that results in a wholesale rate which is less than retail in each instance.

³⁶ See Staff's Exceptions to Proposed Recommendation/Draft Order, pp. 1-2.

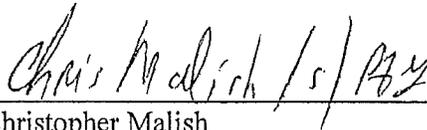
³⁷ The “effective retail rate,” a term used in *Sanford* decision, is the retail rate for a service less the promotion value associated with such service.

Respectfully submitted, this 18th day of November, 2011.



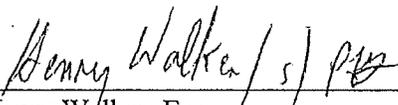
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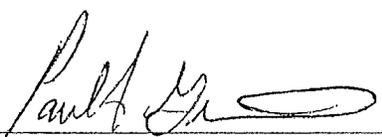
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TELECOMMUNICATIONS USA, LLC

CERTIFICATE OF SERVICE

I hereby certify that a copy of the above and foregoing has this date been served via U.S.

Mail, postage prepaid, or electronic mail to all parties listed on the Official Service List.

This 18th day of November, 2011.



Paul F. Guarisco

ATTACHMENT 1

2011 NOV 18 PM 3:42

LA PUBLIC SERVICE
COMMISSION

Analysis

The parties have no fundamental disagreement in defining a "Cash Back" promotion. Reseller witness Gillan defines a Cash Back promotion as "a category of promotion where a cash payment, gift card, coupon, checks or other similar giveaways are offered as part of a particular promotion." AT&T witness Taylor defines a Cash Back promotion as "an offer that provides a one-time cash or near-cash incentive for customers to subscribe to a service. It often takes the form of a coupon to be mailed back or an online redemption process."

AT&T proposes to (1) bill the Reseller the monthly retail price of the service less the 20.72% resale discount; and (2) provide the Reseller a one-time bill credit in the amount of the retail Cash Back amount less the 20.72% resale discount.

On the other hand, the Resellers and Staff correctly point out that the AT&T approach results in a wholesale price which is greater than, not less than, the retail price when the "effective retail rate" (*i.e.*, the retail price less the cash rebate) is below zero resulting in a credit. Therefore, the Resellers and Staff argue, AT&T's methodology cannot fully comply with the resale provisions of the Telecommunications Act of 1996 (the "Act"), the FCC's *Local Competition Order*¹ and *Sanford*.

Section 252(d)(3) of the Act states:

Wholesale prices for telecommunications services. For the purposes of section 251(c)(4) of this title, a State commission shall determine *wholesale* rates on the basis of *retail* rates charged to subscribers for the telecommunications service requested, *excluding the portion thereof attributable to any marketing, billing, collection, and other costs that will be avoided* by the local exchange carrier. [Emphasis added.]

47 C.F.R. § 51.607 states:

The wholesale rate that an incumbent LEC may charge for a telecommunications service provided for resale to other telecommunications carriers shall equal the rate for the telecommunications service, less avoided retail costs, as described in Section 51.609.

As the Act and FCC rules make clear, the resale rate for telecommunications services that an ILEC may charge is "the rate for the telecommunications service, *less* avoided retail costs, as described in section 51.609."² Second, it is clear from context that the Act and the rules

¹ See In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, CC Docket No. 96-98, FCC 96-325, 11 FCC Rcd 15499 (rel. Aug. 8, 1996) ("*Local Competition Order*").

² "Avoided retail costs shall be those costs that reasonably can be avoided when an incumbent LEC provides a telecommunications service for resale at wholesale rates to a requesting carrier." 47 C.F.R. § 51.609(b). Further, "the amount of avoided retail costs shall be determined on the basis of a cost study...." 47 C.F.R. § 51.609(a).

promulgated thereunder require that the wholesale price should be less than the retail price. In its *Local Competition Order*, the FCC spent considerable effort explaining the importance of competition by resale and laying out how wholesale rates should be calculated.³ The FCC made clear that when using percentages to calculate wholesale rates, the wholesale rate would be set by a “percent *below* retail rate levels.”⁴ The FCC also repeatedly expressed its concern that promotions could be used by ILECs, such as AT&T, to avoid their resale obligations – namely, the ILECs’ obligation to wholesale their services at a rate “below retail rate levels.”⁵ Thus, one cannot comply with the FCC pricing rules by having a wholesale price greater than the retail price.

AT&T’s proposal results in instances where the wholesale rate is actually higher than the retail rate. Accordingly, AT&T’s model cannot be correct. It is not possible to comply with the federal wholesale pricing standard with a wholesale price that is *greater* than the retail price, as AT&T’s proposal produces.

Despite the fact that its method creates a wholesale rate which is greater than the retail rate in the month in which the promotion is realized, AT&T argues that this effect is “corrected” over succeeding months not subject to a cash back promotion. The Commission rejects this argument. In fact, it is undisputed that there is neither a guarantee nor a requirement that service will be maintained for longer than one month. The cash back promotions are offered in the first month of service and are not prorated over a span of months; therefore, the effect of these promotions must be viewed in the first month of service. To “pro-rate” the promotion for Resellers when it is not pro-rated for retail customers discriminates against Resellers, which is prohibited by 47 U.S.C. § 251(c)(4)(B); 47 C.F.R. § 51.603(b); and 47 C.F.R. § 51.613. Last, each month’s service is billed discretely, and Resellers are entitled to the wholesale discount for each month of service to which they subscribe. Because AT&T’s calculation of these promotions create a wholesale rate which is greater than the retail rate in the month to which the promotions are applied, AT&T’s method violates the resale provisions of the Act and FCC rules. Therefore, AT&T’s argument must be rejected.

The parties have provided the Commission with their positions on the effect and import of *BellSouth Telecommunications Incorporated v. Sanford*, 494 F.3d 439 (4th Cir. 2007) (“*Sanford*”). In *Sanford*, the Fourth Circuit Court of Appeals determined that if an ILEC offers a promotion that tends to affect the retail price of a service, it must be offered in turn to CLECs. The Fourth Circuit held that for long-term promotional offerings (such as the cash back promotions at issue herein), the avoided cost or wholesale discount must be deducted from the “effective retail rate” that results from applying the value of the promotional offering to the retail rate of the underlying service.⁶ *Sanford* therefore makes it clear that the wholesale rate must be lower than retail rate to give effect to the Act and federal regulations.

³ See, e.g., *Local Competition Order* at ¶ 907: Resale will be an important entry strategy for many new entrants, especially in the short term when they are building their own facilities. Further, in some areas and for some new entrants, we expect that the resale option will remain an important entry strategy over the longer term. Resale will also be an important entry strategy for small businesses that may lack capital to compete in the local exchange market by purchasing unbundled elements or by building their own networks.

⁴ *Local Competition Order* at ¶ 910 (emphasis added).

⁵ *Id.* at ¶¶ 950 – 952.

⁶ *Sanford* at 442.

This Commission finds that the cash back promotions should be subject to the 20.72% discount in instances where the cash back promotion is less than the retail price for the underlying telecommunications service. In these instances, the "effective retail rate" must be reduced by the Commission's 20.72% discount to arrive at the proper wholesale price to the Resellers. This is the approach contemplated by the *Sanford* court. For example, if the retail price is \$50 and the cash back promotion is \$25, the "effective retail rate" is \$25. This "effective retail rate" is, in effect, the price to AT&T's retail customers. Under AT&T's method (assuming a 20% wholesale discount), the retail price would be discounted to \$40 and the cash back promotion is discounted to \$20, for a net wholesale price to the Resellers of \$20. Since the price to the Resellers of \$20 is less than the price to retail customers of \$25, the wholesale rate is lower than the retail rate and the pricing principles of the Act and FCC rules are preserved.

However, we reject the approach advocated by AT&T when the "effective retail rate" is below zero or results in a credit. If the retail price is \$30 and the cash back promotion is \$50, the "effective retail rate" is a credit of \$20 or (-\$20). Under AT&T's approach (assuming a 20% wholesale discount), the retail price would be discounted to \$24 and the cash back promotion is discounted to \$40, for a net wholesale price to the Resellers of (-\$16) or a credit of \$16. Since the price to the Resellers of (-\$16) is higher than the price to retail customers of (-\$20), the wholesale rate is greater, not lower, than the retail rate. This is definitely not what we believe the Act and FCC rules intend.

In the case where the cash back promotion is greater than the first month's charges, discounting the cash back promotion means that the AT&T retail customer in effect gets a better price than the Resellers. Therefore, in the special cases where the promotion exceeds the first month's cost of service, we find that the retail discount should not be applied to the cash back rebate. Instead, when the cash back promotion exceeds the retail rate of the underlying service, only the retail rate – but not the cash back promotion – should be reduced by the Commission 20.72% wholesale discount. Using the above example – where the retail price is \$30, the cash back promotion is \$50, the "effective retail rate" is (-\$20) and assuming a 20% avoided cost discount – the retail price must be discounted to \$24 and the entire cash back promotion, \$50, must be subtracted to arrive at the wholesale price to Resellers of (-\$26). In this instance, the wholesale rate to the Resellers of (-\$26) is less than the retail rate to AT&T's retail customers of (-\$20), and the pricing principles of the Act and FCC rules are preserved.

ATTACHMENT 2

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LA PUBLIC SERVICES
COMMISSION

Analysis

The parties have no fundamental disagreement in defining a "Cash Back" promotion. Reseller witness Gillan defines a Cash Back promotion as "a category of promotion where a cash payment, gift card, coupon, checks or other similar giveaways are offered as part of a particular promotion." AT&T witness Taylor defines a Cash Back promotion as "an offer that provides a one-time cash or near-cash incentive for customers to subscribe to a service. It often takes the form of a coupon to be mailed back or an online redemption process."

AT&T proposes to (1) bill the Reseller the monthly retail price of the service less the 20.72% resale discount; and (2) provide the Reseller a one-time bill credit in the amount of the retail Cash Back amount less the 20.72% resale discount. The AT&T proposal is demonstrated by the following equation:

$$\text{Wholesale Rate} = [(20.72\% \times (\text{Retail Rate})) - [(20.72\%) \times (\text{Cash-Back})]$$

However, as correctly pointed out by Staff and the Resellers, the AT&T approach results in a wholesale price which is greater than, not less than, the retail price when the "effective retail rate" (*i.e.*, the retail price less the cash rebate) is below zero.

Despite the fact that its method creates a wholesale rate which is greater than the retail rate in the month in which the promotion is realized, AT&T argues that this effect is "corrected" over succeeding months not subject to a cash back promotion. The Commission rejects this argument. In fact, it is undisputed that there is neither a guarantee nor a requirement that service will be maintained for longer than one month. The cash back promotions are offered in the first month of service and are not prorated over a span of months; therefore, the effect of these promotions must be viewed in the first month of service. To "pro-rate" the promotion for Resellers when it is not pro-rated for retail customers discriminates against Resellers, which is prohibited by 47 U.S.C. § 251(c)(4)(B); 47 C.F.R. § 51.603(b); and 47 C.F.R. § 51.613. Last, each month's service is billed discretely, and Resellers are entitled to the wholesale discount for each month of service to which they subscribe. Because AT&T's calculation of these promotions create a wholesale rate which is greater than the retail rate in the month to which the promotions are applied, AT&T's method violates the resale provisions of the Act and FCC rules. Therefore, AT&T's argument must be rejected.

The Resellers and Staff propose that the Commission correct AT&T's method to fully comply with the resale provisions of the Telecommunications Act of 1996 (the "Act"), the FCC's *Local Competition Order*¹ and *Sanford*, by finding that the correct wholesale price is the "effective retail rate" (retail rate less the cash rebate) *reduced by* the wholesale discount, which results in a wholesale price which is always less than the corresponding retail price.

¹ See In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, CC Docket No. 96-98, FCC 96-325, 11 FCC Red 15499 (rel. Aug. 8, 1996) ("*Local Competition Order*").

Section 252(d)(3) of the Act states:

Wholesale prices for telecommunications services. For the purposes of section 251(c)(4) of this title, a State commission shall determine *wholesale* rates on the basis of *retail* rates charged to subscribers for the telecommunications service requested, *excluding the portion thereof attributable to any marketing, billing, collection, and other costs that will be avoided* by the local exchange carrier. [Emphasis added.]

47 C.F.R. § 51.607 states:

The wholesale rate that an incumbent LEC may charge for a telecommunications service provided for resale to other telecommunications carriers shall equal the rate for the telecommunications service, less avoided retail costs, as described in Section 51.609.

As the Act and FCC rules make clear, the resale rate for telecommunications services that an ILEC may charge is “the rate for the telecommunications service, *less* avoided retail costs, as described in section 51.609.”² Second, it is clear from context that the Act and the rules promulgated thereunder expect that the wholesale price should be less than the retail price. In its *Local Competition Order*, the FCC spent considerable effort explaining the importance of competition by resale and laying out how wholesale rates should be calculated.³ The FCC made clear that when using percentages to calculate wholesale rates, the wholesale rate would be set by a “percent *below* retail rate levels.”⁴ The FCC also repeatedly expressed its concern that promotions could be used by ILECs, such as AT&T, to avoid their resale obligations – namely, the ILECs’ obligation to wholesale their services at a rate “below retail rate levels.”⁵ Thus, one cannot comply with the FCC pricing rules by having a wholesale price greater than the retail price.

AT&T’s proposal results in instances where the wholesale rate is actually higher than the retail rate. Accordingly, AT&T’s model cannot be correct. It is not possible to comply with the federal wholesale pricing standard with a wholesale rate that is *greater* than the retail rate, as AT&T’s proposal suggests.

The parties have provided the Commission with their positions on the effect and import of *BellSouth Telecommunications Incorporated v. Sanford*, 494 F.3d 439 (4th Cir. 2007) (“*Sanford*”). In *Sanford*, the Fourth Circuit Court of Appeals determined that if an ILEC offers a promotion that tends to affect the retail price of a service, it must be offered in turn to CLECs.

² “Avoided retail costs shall be those costs that reasonably can be avoided when an incumbent LEC provides a telecommunications service for resale at wholesale rates to a requesting carrier.” 47 C.F.R. § 51.609(b). Further, “the amount of avoided retail costs shall be determined on the basis of a cost study....” 47 C.F.R. § 51.609(a).

³ See, e.g., *Local Competition Order* at ¶ 907; Resale will be an important entry strategy for many new entrants, especially in the short term when they are building their own facilities. Further, in some areas and for some new entrants, we expect that the resale option will remain an important entry strategy over the longer term. Resale will also be an important entry strategy for small businesses that may lack capital to compete in the local exchange market by purchasing unbundled elements or by building their own networks.

⁴ *Local Competition Order* at ¶ 910 (emphasis added).

⁵ *Id.* at ¶¶ 950 – 952.

The Fourth Circuit held that for long-term promotional offerings (such as the cash back promotions at issue herein), the avoided cost or wholesale discount must be deducted from the "effective retail rate" that results from applying the value of the promotional offering to the retail rate of the underlying service.⁶ *Sanford* therefore makes it clear that the wholesale rate must be lower than retail rate to give effect to the Act and federal regulations.

This Commission finds that the proper calculation of the wholesale rate is to reduce the "effective retail rate" by the 20.72% discount, as contemplated by the *Sanford* Court. For example, if the retail price is \$50 and the cash back promotion is \$25, the "effective retail rate" is \$25. This "effective retail rate" is, in effect, the price to AT&T's retail customers. Under AT&T's method (assuming a 20% wholesale discount), the retail price would be discounted to \$40 and the cash back promotion is discounted to \$20, for a net wholesale price to the Resellers of \$20. Since the price to the Resellers of \$20 is less than the price to retail customers of \$25, the wholesale rate is lower than the retail rate and the pricing principles of the Act and FCC rules are preserved.

The Commission finds that these same principles should be followed when the "effective retail rate" is less than zero or results in a retail credit. We therefore reject the approach advocated by AT&T when the "effective retail rate" is less than zero or results in a credit. If the retail price is \$30 and the cash back promotion is \$50, the "effective retail rate" is a credit of \$20 or (-\$20). Under AT&T's approach (assuming a 20% wholesale discount), the retail price would be discounted to \$24 and the cash back promotion is discounted to \$40, for a net wholesale price to the Resellers of (-\$16) or a credit of \$16. Since the price or credit to the Resellers of (-\$16) is higher than the price or credit to retail customers of (-\$20), the wholesale rate is greater, not lower, than the retail rate. This is not what we believe the Act and FCC rules intend.

In the above example, the correct approach, and the approach adopted by this Commission, is to *reduce* the "effective retail rate" by the avoided retail costs. In the above example, and assuming a 20% wholesale discount, the discount should reduce the "effective retail rate" or credit of (-\$20) to arrive at a wholesale rate or credit to the Resellers of (-\$24), which is less than the "effective retail rate" to retail customers. By so correcting AT&T's formula, this Commission's decision is in line with the concept that the wholesale rate must be less than the effective retail rate as set out in the *Local Competition Order* and the *Sanford* decision.

⁶ *Sanford* at 442.