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February 13, 2012

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Jeff DeRouen
Executive Director
Kentucky Public Service Commission
211 Sower Boulevard
Frankfort, KY 40601

**Re: DPI Teleconnect, LLC v. BellSouth Telecommunications, Inc. d/b/a
AT&T Kentucky
Case No. 2009-00127**

Dear Mr. DeRouen:

Enclosed please find an original and ten copies of dPi Teleconnect, LLC's ("dPi") Motion for Reconsideration in the above-referenced case.

Please confirm your receipt of this filing by placing the stamp of your Office with the date received on the enclosed additional copy of the filing and return to me via our runner.

Sincerely yours,

Douglas F. Brent

DFB:jms
Enclosure
cc: Parties of Record

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COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of)
))
DPI TELECONNECT, L.L.C.)
))
COMPLAINANT)
))
v.)
))
BELLSOUTH TELECOMMUNICATIONS, INC.)
D/B/A AT&T KENTUCKY)
))
DEFENDANT)
))
DISPUTE OVER INTERPRETATION OF THE)
PARTIES' INTERCONNECTION AGREEMENT)
REGARDING AT&T KENTUCKY'S FAILURE TO)
EXTEND CASH-BACK PROMOTIONS TO DPI)

CASE NO.
2009-00127

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COMMISSION

dPi TELECONNECT, L.L.C.'s MOTION FOR RECONSIDERATION
ON HOW TO CALCULATE WHOLESALE PRICE FOR SERVICES
SUBJECT TO CASH BACK PROMOTIONS

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**dPi TELECONNECT, L.L.C.’s MOTION FOR RECONSIDERATION
ON HOW TO CALCULATE WHOLESALE PRICE FOR SERVICES
SUBJECT TO CASH BACK PROMOTIONS**

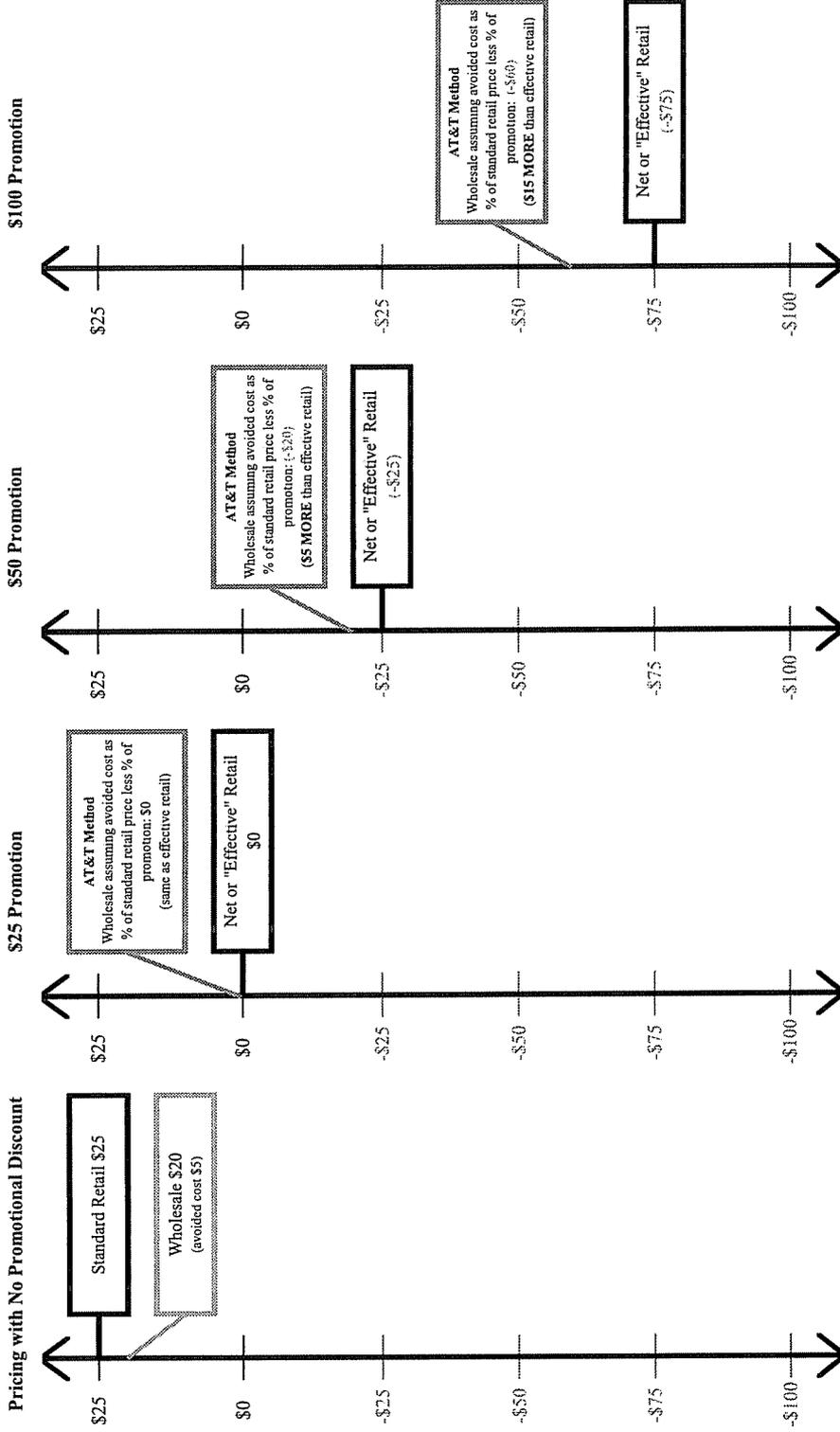
I. INTRODUCTION

Pursuant to KRS 278.400, dPi Teleconnect, L.L.C. (“dPi”) urges the Kentucky Public Service Commission (“Commission”) to reconsider that portion of its Final Order adopting BellSouth Telecommunications, LLC d/b/a AT&T Kentucky (“AT&T”)’s hypothetical method that understates the amount of credit due resellers who obtain AT&T services that are subject to cash back promotions. While the Commission ruled largely in favor of dPi, the Commission’s Order includes an error. Its adoption of AT&T’s method for calculating cash back promotional credits due to resellers violates federal law because 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. As the South Carolina Commission’s directive—issued shortly after oral argument in Kentucky—put it, “[t]his is definitely not what we believe the Telecommunications Act of 1996 intended.” This is graphically illustrated in Figure 1, below:

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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

The Order refused to adopt dPi's position, stating that it would "put AT&T Kentucky in the position of paying its competitors to "purchase" AT&T Kentucky's service." Respectfully, that concern is misplaced. dPi never insisted that AT&T dream up the promotions that led to this complaint. But AT&T must adhere to the law, and should not be rewarded for trying to avoid it. Allowing AT&T to avoid selling its services at a wholesale price less than what it charges its own retail customers – which is what happens when AT&T provides resellers with less credit than AT&T provides its own retail customers entitled to cash back promotions – allows AT&T to structure promotions in a way that undermines core principles that underlie resale requirements of federal law, jeopardizing the viability of wholesale competition altogether. It is neither "absurd" nor "anti-competitive" to apply resale principles strictly to AT&T.

Accordingly, in this motion for reconsideration, dPi will:

1. show that federal law and supporting authorities *require* resale to be lower than retail pricing, particularly including promotions;
2. demonstrate how AT&T's method, accepted by the Commission, *violates* federal law because it results in wholesale rates higher than retail rates, and thus must be replaced or repaired; and
3. suggest other methods for adoption that *are* consistent with federal law and authorities.¹

While the Commission is not obligated to adopt dPi's preferred method, the method it does choose must nevertheless comply with the law.

II. STANDARD FOR REHEARING

KRS 278.400 allows any party to apply for rehearing with respect to "any of the matters"

¹ The Commission's Final Order misapprehended dPi's position and subsequently miscalculated the net wholesale price in its example provided in the Final Order. *See* Final Order, pages 12-13.

determined by the Commission. Among other things, rehearing is the means for the Commission to reconsider an order in light of alleged errors and omissions.² The Commission should reconsider an order when a party identifies material evidence adduced in a proceeding that was overlooked in the Commission's order. If the Commission agrees that the existing record supports a different result not fully considered or explained by its original decision, it should amend its order.

III. ARGUMENT

AT&T's method for calculating the amount of cash back promotional credits due to resellers (the method approved by the Commission's Final Order) *conflicts with federal law and regulations because it violates* the core principle of the Telecommunications Act *that wholesale pricing should always reflect a price below retail*. In fact, AT&T's distorted formula produces the opposite result: wholesale rates ABOVE retail rates. 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 issue – 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 Public Service Commission of South Carolina (“PSCSC”), and (4) the Louisiana Public Service Commission (“LPSC”) Staff – is that the Federal Telecommunications Act of 1996³ (“FTA” or “Act”) and FCC regulations require that services sold at *wholesale should be priced below retail*. Simply put, AT&T's proposed methodology, which has been adopted by the Order, violates this core principle.

² See, e.g., *Kentucky-American Water Co.*, Case No. 2000-00120, Order at 2-4 (February 29, 2001).

³ Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (codified at 47 U.S.C. §§ 151 *et seq.*).

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

Congress passed the FTA with the intent of “opening previously monopolistic local telephone markets to competition.”⁴ “[The] provisions of the Telecommunications Act of 1996 . . . were intended to eliminate the monopolies enjoyed by the inheritors of AT&T’s local franchises”⁵ and also to promote competition with them.⁶ As an aside, it worth noting here that the Act was not designed or intended to foster Incumbent Local Exchange Carriers (“ILECs”) ILECs or regional Bell operating companies like AT&T with other carriers; in fact, the **opposite** is true. Thus, concerns that a decision by this Commission might harm AT&T’s ability to compete (*see, e.g.*, Order at p. 12) are entirely misplaced; that which must be fostered is the ability of resellers like dPi to compete with AT&T.

One of the methods by which this goal of eliminating monopolies and promoting competition with AT&T’s local franchises was to be achieved was by obliging the ILECs, such as AT&T, to make their retail services available for resale at wholesale rates.⁷ 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

⁴ See *Southwestern Bell Telephone Co. v. Public Utility Comm’n of Texas*, 208 F.3d 475, 477 (5th Cir. 2000).

⁵ See *Verizon Communications, Inc. v. F.C.C.*, 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.)

⁶ 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 Santa Fe*, 957 F. Supp. 1230, 1237 (D.N.M. 1997).

⁷ 47 U.S.C. § 251(c)(4)(A).

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 dPi.⁹ Thus, the "wholesale discount" is the avoided cost. Because the wholesale price charged to 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 interconnection agreements, necessarily direct that the wholesale price be less than the retail price.

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*. Remember, "cost" and "price" are two very different concepts: "cost" is the value of the products and services which are necessary to produce a unit of output. But "price" is the value or what a customer has to give up in order to acquire that output: a seller's *costs* are not necessarily directly related to the *price* the seller charges for a service. Moreover, a price change does not necessarily mean that a cost has

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."

changed – and, more importantly, a seller’s price change certainly does not *cause the seller’s 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 wholesale rate would be set by a “percent *below* retail rate levels.”¹³ The FCC also repeatedly

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.

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

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

¹⁴ *Id.* at ¶ 952 (emphasis added).

¹⁵ *Id.* at ¶ 950 (emphasis added).

¹⁶ *Id.* at ¶ 950 (emphasis added).

¹⁷ *Id.* (emphasis added).

¹⁸ *Local Competition Order* at ¶ 948 (emphasis added).

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. In any event, AT&T abandoned its RPMA scheme before the Fifth Circuit rendered its opinion.

AT&T’s current scheme is no less unlawful than other 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 appears intended to undermine resale competition. As a consequence, AT&T’s method and the Commission’s Final Order allows AT&T’s “promotional offerings to evade the wholesale obligation” and contravenes the FCC’s objective

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. 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).

“[t]o preclude the potential for abuse of promotional discounts.”²²

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 According to the *Sanford* Court, “Bellsouth’s position [in which its retail customers pay less than its wholesale customers] would obviously impede competition.”²⁶

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*.²⁷ In effect, the

²² *Local Competition Order* at ¶ 950.

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 *Id.* at 451.

²⁷ 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

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.

B. AT&T's method inexcusably violates state and federal law and the contract because it results in the wholesale price being GREATER than the effective retail price – thereby making wholesale less favorable than retail.

1. AT&T's method results in the wholesale price being GREATER than the effective retail price, violating state and federal law, and the terms of the contract.

As just shown, the overriding principle controlling this proceeding is that the Act, the FCC regulations and the *Sanford* decision require that *wholesale prices should always be less than retail prices*.

However, the AT&T formula for determining the wholesale price when cash back promotions are in play results in situations where the wholesale rate is **GREATER**, not less than, the effective rate charged to AT&T's retail customers.

In fact, what *Sanford* calls for –subtracting the promotion amount from the retail price and then further reducing that sum by the avoided cost discount – *is not what AT&T's formula does*: AT&T's formula (1) reduces the retail rate by the discount percentage and then (2) reduces the amount of the promotion credit by the discount percentage as well.²⁸

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.

²⁸ Note that if one were really attempting to ensure the wholesale price is a percentage *less than* the promotional rate, one would say (properly stated algebraically) that the wholesale price is the effective retail rate *reduced by* the amount arrived at by multiplying the *absolute value* of the effective retail rate by the discount percentage rate:

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

In instances such as all of the promotions in this case, where the cash back amount exceeds the normal retail rate of the underlying telecommunications service, the “effective retail rate” is negative. For example, where the retail price is \$25 and the cash back rebate is \$50, the “effective retail rate” is (-\$25). Under the rule in *Sanford*, that amount is to be further reduced by the avoided retail costs. In this example, the avoided costs are \$5 (assuming a 20% discount to make the math easier), which amount is deducted from the effective retail rate to produce a wholesale price of (-\$30). In other words, the dollars “avoided” must be deducted from the retail price to arrive at the correct wholesale price. Under AT&T’s formula, however, using the numbers from this example, AT&T would resell the service at (-\$20), which is 20% *more* than the promotional rate.

The practical effects of applying AT&T’s formula using examples more in line with real life are again illustrated in Figure 1 (which appears at the beginning of this brief), and clearly show that in practice, AT&T’s method produces wholesale rates that are not the wholesale percentage *less than* the promotional rate, but *more* than the promotional rate.

Interestingly, in other states, AT&T continues to claim that AT&T’s formula *does* reduce the effective retail price by the discount percentage. The problem is that all of the illustrations typically employed to show that its formula for calculating the wholesale price results in a wholesale rate less than the retail rate *work only because the promotion amount is less than the monthly retail rate of the service* (e.g., situations where the monthly rate is assumed to be \$75 and the promotion amount assumed to be \$50, resulting in a net effective, or promotional, rate of \$25). Using such examples to “prove” that AT&T’s formula always results in wholesale prices lower than retail is grossly misleading, because in fact, and in the case of every promotion at issue in this case, the monthly rate is typically closer to \$25 – not \$75 – so that with a \$50 dollar

promotion, the net effective retail (or promotional) rate is *negative*. Applying AT&T's formula in such instances RAISES the rate to resellers by the percentage, rather than reducing that rate.

Because AT&T's formula results in instances where the wholesale rate is actually higher than the retail rate, AT&T's model cannot be correct, and is not consistent with any legal authority. It is not possible to comply with the federal wholesale pricing standard with a wholesale price that is greater than the retail rate.

2. AT&T's violation of law and contract by imposing a method that results in the wholesale price being GREATER than the effective retail price is not excused.

Once forced to admit that its formula produces a results contrary to the law and contract, AT&T attempts to excuse the illegal effects of applying its formula by claiming (1) that its method is in fact sanctioned by the *Sanford* case and the results are "mathematically the same" as the percent less than method and (2) "in the long run, the total paid at wholesale will be less than the total paid at retail." All are without merit.

a. *Sanford* disapproves, not justifies AT&T's method, because under *Sanford*, wholesale must be less than retail.

AT&T has claimed that *Sanford* approves its proposed method of reducing the value of the cash back promotion by the Commission's wholesale discount percentage and that the results of applying its method "mathematically the same" as the percent less than method. Nothing could be further from the truth.

As noted above, the *Sanford* court held that for these long-term promotional offerings, the avoided cost or wholesale discount must be applied to the actual, or effective, retail rate created by applying the value of the promotional offering to the retail rate of the underlying service.²⁹ AT&T has applauded this method and purported to follow it – but then substitutes

²⁹ *Sanford* at 442.

something different: AT&T's formula (applying the percentage first to the standard rate, then to the promotion), which gives very different results when the promotion is greater than the standard retail rate.

Of course, AT&T's method is not the same as the "percent less than the promotional rate" discussed in *Sanford*; as already shown, AT&T's method results in the wholesale price being *more* than the retail price where the promotion is greater than the retail price in the first month of service, not less than the retail price

Moreover, the key lesson from *Sanford* is that wholesale must be less than retail.³⁰ 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* found unreasonable.³¹ 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

³⁰ Note that *Sanford* was not primarily involved with setting what the avoided cost discount should be, but rather was deciding the concept of whether promotions *in general* should be made available to resellers. The court concluded that promotions should be available to resellers, because otherwise resale would be pointless, as the wholesale rate would be higher than the net retail rate.

The example from *Sanford* that AT&T attempts to exploit is a hypothetical where the *Sanford* court attempts to show how an ILEC could use promotions to undermine the resale provisions of the Act – a hypothetical where the "normal" rate is \$20, then through a series of machinations is raised to \$120 per month each month but offset by a \$100 monthly retail discount. In other words, the "real" rate for the service in such a hypothetical is still \$20 per month. In such an outlandish situation it would be correct to assume the "real" monthly rate to be \$20 and base the avoided cost calculation off that number.

³¹ 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 slightly 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.

reject AT&T's policy of refusing to provide the value of cash back promotions to resellers altogether.

b. AT&T's method cannot be excused under the theory that "if the customer stays long enough, the effects will be diluted on average."

AT&T also dismisses out of hand the fact that AT&T's method results in a higher wholesale rate in the month the promotion is applied by claiming that over time, the *total* amount paid at wholesale will be less than total amount paid at retail.

This is irrelevant: resellers are entitled to purchase services less the costs avoided discount in each and every month they take service. Furthermore, *the promotions at issue are not paid out over a series of months, but in a single month in a lump sum*; therefore, it is irrelevant whether the effects of AT&T's unlawful charges to the resellers are diluted over a period of months or years. *The fact remains that AT&T's method violates the Act and FCC rules in the month in which the promotion is applied.*

Furthermore, there is no guarantee that the reseller will be able to keep the customer for the period of time necessary to result in the total paid at wholesale to drop below the total amount a retail customer would pay.

In any event, note that if AT&T is allowed to so overcharge in the first month, even though the net effect of that overcharge will be increasingly diluted over time, the amount overpaid by the reseller will NEVER be recouped.

c. 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, the PSCSC adopted by unanimous (7-0) vote a Directive³²

³² 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 ("PSCSC Commission Directive") pp. 1-2.

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 PSCSC's Directive is attached hereto as Exhibit A.

With respect to the calculation of the cash back promotional credits due to resellers, the PSCSC 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 PSCSC recognizes (as dPi has 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, 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 than the retail rate.

The situation highlighted above in the PSCSC Directive is precisely the situation at issue here. Unlike the hypothetical used in the Order (see p. 12-13), 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 to these promotions

creates a wholesale price which is *greater than* the retail price to end-users. AT&T's method allows 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 PSCSC, “is definitely not what we believe the Telecommunications Act of 1996 intended.”

In similar proceedings in Louisiana,³³ the LPSC Staff also rejected AT&T's methodology.³⁴ A copy of LPSC Staff's Brief on Remand is attached hereto as Exhibit B.

C. Because AT&T's formula results in wholesale rates higher than retail rates, it cannot be correct, and another method must be adopted.

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 *less than* retail), it must be rejected. Two methods remain:

- (1) Replacing AT&T's formula with one that calculates the wholesale (cost avoided) discount associated with a service from the standard/tariffed cost avoided for that service (this is the method advocated by dPi); and
- (2) Repairing AT&T's method so that it correctly calculates the wholesale (cost avoided) discount associated with a service as a percentage *less than* the net retail price for that service; or, stated in algebraic form, the wholesale price is 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 discount percentage rate:

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

³³ See *BellSouth Telecommunications, Inc. d/b/a AT&T Southeast d/b/a AT&T Louisiana v. 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*; in Docket No. U-31364 before the Louisiana Public Service Commission.

³⁴ In its Brief on Remand, LPSC Staff stated:

In no uncertain terms, AT&T's methodology for calculating the cash-back credit provided to a reseller when the amount of the cash-back exceeds the price of the service, results in the reseller receive less of a benefit than the retail customer in the month that credit is applied. **Such a result cannot be logical**, particularly when its justification is that the “wholesale discount is applied” resulting in the 20% reduction in the discount. . . . Thus, as Staff has argued throughout this proceeding, while mathematically correct, **the formula defies logic**. One need not be an economist, mathematician, or even an attorney, to reach such a conclusion.

LPSC Staff's Brief on Remand at 4 (emphasis added).

This is how one would correctly express mathematically the concept of having the effective retail rate being *reduced by* a particular percentage.³⁵

1. Preferred method for calculating the avoided costs: subtracting the known avoided costs from the net retail rate.

dPi' preferred method for calculating the avoided costs associated with services subject to special sales or promotions is to base the avoided costs on the standard or tariffed rate, and subtract the avoided costs from the promotional price of the service – because this method recognizes that the avoided costs associated with a service do not change simply because some customers taking the service have a coupon or are otherwise eligible for a temporary price reduction through a promotion.

It is undisputed that the costs of providing a particular service do not change, even if purchasers of that service may be able to purchase the service at a special sale, or promotional, prices. In other words, the avoided cost is the same for both a service sold at the standard retail rate, and the same service sold pursuant to a special sale, or promotional rate. This is because the *costs* associated with the service are the same, even if the *price* is temporarily changed (for a single month) for a particular customer pursuant to a special sale or promotion. Just as this

³⁵ The Commission's Final Order misapprehended dPi's position and subsequently miscalculated the net wholesale price in its example provided in the Final Order. See Order, pages 12-13. In the Commission's illustration, the mathematical representations are *not* what dPi has advocated. In actuality, if the avoided cost discount was applied to the standard retail price, the math would be:

$$\text{Standard Retail Price} \times \text{Wholesale Discount Percentage} = \text{Avoided Costs}$$

$$\text{Standard Retail Price} - \text{Promotional Discount} - [\text{Avoided Costs}] = \text{Net Wholesale Price}$$

In other words: $\$120 - \$100 - [\$120 \times 20\%] = \text{Net Wholesale Price}$, thus

$$\$20 - \$24 = -\$4.$$

If the "percentage less than" method were properly applied, the math would be:

$$\text{Standard Retail Price} - \text{Promotional Discount} = \text{Net Retail Price and}$$

$$\text{Net Retail Price} - 20\%[\text{Net Retail Price}] = \text{Net Wholesale Price}$$

In other words: $(\$120 - \$100) - 20\%(\$120 - \$100) = \text{Net Wholesale Price}$, thus

$$\$20 - \$4 = \$16.$$

estimate is correct for every other month for the service – and for every other customer, including those that are not eligible for the promotion – the estimate remains appropriate to the single month that the promotional credit is processed.

As we know from the statutes, the wholesale discount is supposed to be the net retail price less the avoided costs involved with providing the services in bulk to resellers. However, the Commission has already determined how to calculate the avoided costs associated with these services: to properly determine the avoided cost, one multiplies the resale discount factor times the pre-promotion, standard/tariffed price.³⁶ This gives one the base amount of the avoided cost associated with the service, and thus the amount by which the wholesale amount should be less than the effective retail price.

Thus, the *price* to which the avoided cost is applied is the lower of the tariffed standard price, or, if any, the promotional price in effect for the services in question. Stated another way, the three steps to finding the wholesale price are:

- STEP 1: Find the pre-promotion standard/tariffed retail price.
- STEP 2: Find the avoided cost: multiply the standard/tariffed retail price by the wholesale discount factor.
- STEP 3: Subtract the avoided cost from the effective retail sales price, which is the standard tariffed price, or, if a promotion applies, the price after applying the promotion.

By applying this method, the wholesale price is always the same amount less than the retail price, which is a better reflection of the fact that the cost to provide the services is constant

³⁶ At the time this Commission established its wholesale discount rate at a percent of the retail rate of telecommunications services, it focused on the standard (that is, non-promotion) tariffed retail rate of services provided to calculate a wholesale discount percentage. This method need not change just because BellSouth/AT&T has offered a promotion – the best estimate of a product’s avoided retail cost is still best estimated by applying the discount to its pre-promotion retail price. Such an approach also ensures that resellers are entitled to the full, dollar-for-dollar value of an ILEC’s promotional offerings to the same extent as retail, end-use customers.

regardless of temporary fluctuations in the sales price caused by non-standard special sales.

Table 1, below, shows how this works.

Table 1. Results of applying avoided cost discount based on standard/tariff retail price.				
Standard Retail Price	Standard Wholesale Discount Percentage	Promotion Amount	Net Retail Price¹	Net Wholesale Price² assuming avoided cost calculated as % of standard retail price
\$25	20%	–	\$25	\$20 (\$5 less than net retail)
\$25	20%	\$25	\$0	-\$5 (\$5 less than net retail)
\$25	20%	\$50	-\$25	-\$30 (\$5 less than net retail)
\$25	20%	\$100	-\$75	-\$80 (\$5 less than net retail)

1. Standard Retail Price - Promotional Discount = Net Retail Price
2. Standard Retail Price x Wholesale Discount Percentage = Avoided Costs
Standard Retail Price - Promotional Discount - [Avoided Costs] = Net Wholesale Price

Note that calculating the wholesale discount – that is, the avoided cost discount – from the standard or tariffed rates in this manner conforms to the principle that wholesale price should *always be less than retail price.*

Another reason for adopting the method above is that the Act and FCC regulations require AT&T to offer certain promotions for resale “subject to the same terms and conditions” as offered to retail customers. Thus, CLECs are entitled to the full value of AT&T’s cash back promotions. According to the Act and pertinent FCC regulations, AT&T is required to offer its services for resale “subject to the same conditions” that AT&T offers its own end-users and at “the rate for the telecommunications service less avoided retail costs.”³⁷ For example, when

³⁷ 47 C.F.R. § 51.603(b) and 47 C.F.R. § 51.607.

Furthermore, other than in limited circumstances not applicable here, BellSouth/AT&T cannot impose any restrictions on the resale of its services unless BellSouth/AT&T “proves to the state commission that the restriction is reasonable and non-discriminatory.” 47 C.F.R. §51.613.

AT&T offers retail telephone service in conjunction with a “\$50 cash back” rebate to new customers, AT&T must make that offer available to CLECs “under the same conditions,” that is, with a \$50 cash rebate, and “at the rate for such telecommunications services less the avoided retail costs,” that is, at the tariffed retail price less the wholesale discount. FCC rules unambiguously place the reseller in the shoes of the retail customer when it acquires a service for resale. The FCC rules make clear that no additional conditions can be placed on the reseller, particularly any condition that would have the effect of imposing some restriction on the reseller that does not apply to AT&T retail customers. Accordingly, resellers are fully entitled to the cash-back payment as an end-user. To provide any less – or to impose any other qualifying requirements – violates the Act and FCC rules prohibiting any additional conditions or restrictions on the reseller.

Note that this method does apply the Commission’s discount percentage to calculate the avoided costs – it just applies that discount to the standard retail rate for the service in order to arrive at the costs avoided associated with a particular service, then subtracts the result from the promotional price. AT&T may suggest this method conflicts with the authorities, including the FCC, *Sanford*, and the North Carolina Commission, as allegedly requiring application of a *percentage* to the net retail rate. *See e.g.*, Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98, First Report and Order, 11 FCC Rcd. 15499 (1996) (“*Local Competition Order*”). However, neither the FCC nor the other authorities cited expressly address the calculation of the discount as requiring a percentage discount.

The FCC’s *Local Competition Order* addressed the question of whether ILECs’ promotional practices (like the cash back promotion at issue here) were subject to the resale

provisions of the Act. However, the *Local Competition Order* did not specifically address the calculation of avoided costs, if any, associated with the resale of promotions to CLECs such as the Resellers. Nowhere in the *Local Competition Order* does the FCC announce that a promotional cash back payment should be reduced by any kind of percentage. As noted earlier, the law does not define the wholesale discount in terms of a “percentage” reduction, but as a subtraction problem: the wholesale discount is determined by subtracting the avoided costs from the retail rate. See 47 C.F.R. § 51.607: “The wholesale rate . . . shall equal the rate for the telecommunications service, less avoided retail costs. . . .”

In any event, if the authorities require that the promotional price be reduced by the percentage discount, that is not what AT&T’s formula accomplishes.

2. Correcting AT&T’s method to ensure that wholesale price actually is a fixed percentage less than the net retail price.

While the Commission may not be obligated to adopt dPi’ preferred method, the method it chooses comply with the law. If wishes to use AT&T’s formula as a baseline, it must correct AT&T’s formula to conform to its stated intent (and the law’s requirement) of producing a result in which the reseller pays less for the service than the retail customer. There is no reduction from the effective retail rate when AT&T’s *uncorrected* formula is used; instead, there is an *increase* from the effective retail rate. For example, the wholesale price that is 20% *less than* the retail rate of -\$25 is -\$30, not the -\$20 AT&T would charge. It is not possible to comply with the federal wholesale pricing standard with a wholesale price that is greater than the retail rate.

If the intent is truly to make the wholesale price less than the retail price by *reducing the retail price* by a particular percentage, the correct method for calculating the wholesale (cost avoided) discount associated with a service is to simply make the wholesale price a percentage

less than the net retail price for that service. Again, stated in algebraic form, the wholesale price is 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 discount percentage rate:

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

This formula more correctly captures the intent of having the wholesale rate being a fixed percentage *less than* the effective retail rate. This method is very similar to the rule expressed in *Sanford*,³⁸ although *Sanford* does not specify that the discount be a percentage discount.

Table 2 shows how this works under various scenarios.

Table 2. Results of applying “percentage less” calculation to effective retail rate.				
Standard Retail Price	Standard Wholesale Discount Percentage	Promotion Amount	Net Retail Price¹	Net Wholesale Price² assuming avoided cost calculated as % “less than” net retail price
\$25	20%	–	\$25	\$20 (\$5 less than net retail)
\$25	20%	\$25	\$0	\$0 (same as net retail)
\$25	20%	\$50	-\$25	-\$30 (\$5 less than net retail)
\$25	20%	\$100	-\$75	-\$90 (\$15 less than net retail)

1. Standard Retail Price – Promotional Discount = Net Retail Price
2. Wholesale Discount Percentage “Less Than” Net Retail Price = Net Wholesale Price; that is, Wholesale = (retail price – cash back) – % |(retail – cash back)|

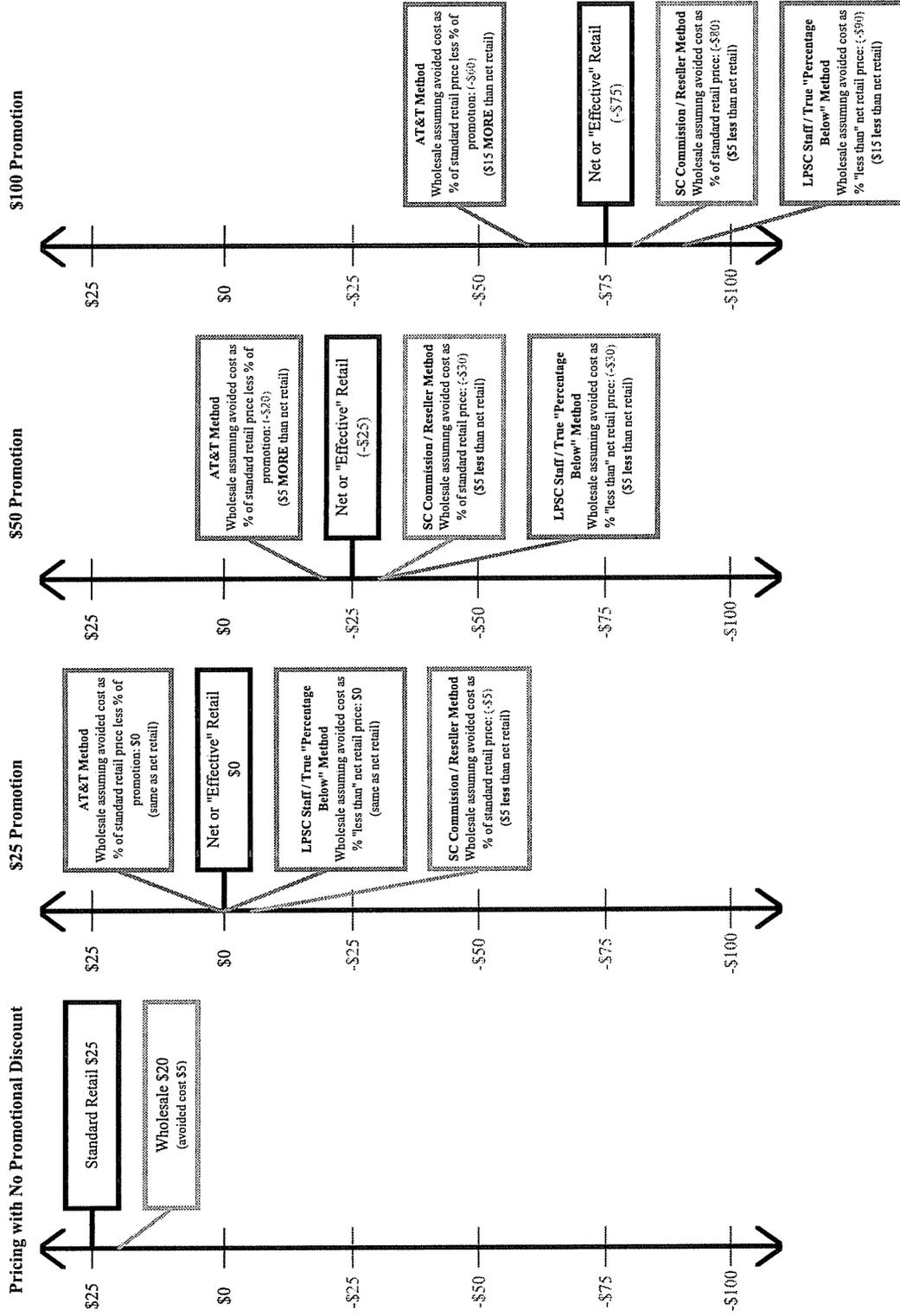
This method is also mostly consistent with the principle that wholesale rates should always be lower than retail rates and the rationale set forth by the Fourth Circuit Court of Appeals in *Sanford*, which indicates that the wholesale discount should be employed to create a

³⁸ *BellSouth Telecommunications, Inc. v. Sanford*, 494 F.3d 439, 442 (4th Cir. 2007). The *Sanford* court held that for these long-term promotional offerings, the avoided cost or wholesale discount must be applied to the actual, or effective, retail rate created by applying the value of the promotional offering to the retail rate of the underlying service.

lower charge to a reseller when compared to a retail customer. The only potential problem with this method is that when the net effective retail rate approaches zero, so does the avoided cost discount – even though we know that certain costs are always avoided in resale, and an avoided cost discount of zero would thus not be appropriate.

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

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

IV. CONCLUSION AND PRAYER

AT&T's method for calculating cash back promotion credits conflicts with federal and state law and regulations because it violates the key principle that wholesale should be less than retail. In fact, AT&T's formula produces the opposite result: wholesale rates GREATER than retail rates. This outcome also means that resellers are treated less favorably than AT&T's retail customers. It is a perversion of this purpose of the Act to hold that AT&T can reduce the effective retail rate of its services for its retail customers and not correspondingly decrease the rate for its wholesale customers. Widening the price point between AT&T's pricing and CLECs' pricing makes already difficult competition that much more difficult. Allowing this outcome would enable AT&T to further gain market share and reduce competition, the antithesis of what the Act is designed to do. Accordingly, AT&T's method must be either repaired or replaced.

Of the three methods for calculating cash back promotion credits advanced in this case, dPi' most closely conforms to the key principles underlying the Act, because it uniformly produces a wholesale price that is lower than the retail rates. In the alternative, if the intent is truly to reduce the effective rate by a given percentage, the mathematically correct way to do so is to apply AT&T's method as correct – the true percentage “less than” method.

Respectfully submitted,



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Attorneys for dPi Teleconnect, L.L.C.

CERTIFICATE OF SERVICE

I hereby certify that I have on this 13th day of February, 2012, served a true and correct copy of the foregoing to the following via U.S. First Class Mail and/or electronic mail:

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Douglas F. Brent

EXHIBIT A

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

ADMINISTRATIVE MATTER	┌	DATE	November 09, 2011
			2010-14-C/2010-15-C
MOTOR CARRIER MATTER	┌	DOCKET NO.	2010-16-C/2010-17-C
UTILITIES MATTER	└	ORDER NO.	2010-18-C/2010-19-C

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



EXHIBIT B



Louisiana Public Service Commission

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COMMISSIONERS

- Jimmy Field, Chairman
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- Clyde C. Holloway, Vice Chairman
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- Lambert C. Boissiere III
District III
- Eric F. Skrmetta
District I

EVE KAHAO GONZALEZ
Executive Secretary

DENNIS WEBER
Executive Counsel

JOHNNY E. SNELLGROVE, JR.
Deputy Undersecretary

July 12, 2011

2011 NOV 18 PM 4:13
LA PUBLIC SERVICE
COMMISSION

Ms. Terri Lemoine
Louisiana Public Service Commission
Docketing Division
P. O. Box 91154
Baton Rouge, LA 70821

Docket No. U-31364- In re: Consolidated Proceeding to Address Certain Issues Common to Dockets U-31256, U-31257, U-31258, U-31259, and U-31260.

Dear Ms. Lemoine:

Please find attached hereto an original and two copies of Staff's Brief on Remand on behalf of the Louisiana Public Service Commission for the above referenced docket. Parties are being served via e-mail and U.S. mail. Should you have any questions regarding this filing, please contact me.

Please return me a date stamped copy.

Very truly yours,

Brandon M. Frey
LPSC Deputy General Counsel

BMF/khb

BEFORE THE
LOUISIANA PUBLIC SERVICE COMMISSION

2011 NOV 18 PM 4:13

DOCKET NO. U-31364

L.A. PUBLIC SERVICE
COMMISSION

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

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

STAFF'S BRIEF ON REMAND

The Staff of the Louisiana Public Service Commission ("Staff") respectfully submits this Brief on Remand in accordance with the procedural schedule established by this Tribunal. For the reasons set forth herein, Staff re-urges its position advocated in Staff's Post-Hearing brief filed February 9, 2011 and in the exceptions to this Tribunal's recommendation filed by Staff on July 12, 2011. In the alternative, Staff urges this tribunal to adopt a compromise position, as addressed herein, that insures a reseller receives no less of a benefit than an AT&T retail customer.

I. The Scope of this Remand is Dictated by Order U-31364

As set forth in Order U-31364, adopted by the Commission, this matter "shall be remanded to the Administrative Hearings Division for further consideration of the calculation

methodology to be applied to cash back promotions.”¹ Thus the Commission, after reviewing the prior filings of the parties, this Tribunal’s recommendation on all pending issues, and listening to oral argument, determined that the cash back promotion methodology necessitated further consideration.

While the Order does not specify what further consideration was anticipated, it is clear that, based on the information before it, the majority of the Commission was not comfortable in reaching a vote on the merits. A review of the prior filings, as well as the transcripts, leads Staff to conclude that this discomfort is a direct result of the issue before the Commission being muddled by the spurious arguments that have been made. Rather than rehash Staff’s prior arguments, and those of AT&T and the resellers, Staff will attempt to focus on what it believes is the core problem with AT&T’s methodology and why it should be rejected when the cash-back amount results in a “negative price”.

A. What is at issue is the “negative effective price” that exists when the cash-back offering exceeds the price of the service. AT&T’s “red herrings” should be ignored.

While it should be clear that the focus of this issue is how to properly allocate a cash-back credit to a reseller when the amount of the credit exceeds the price of the service, Staff believes that issue has been confused by AT&T arguing that a) resellers aren’t harmed because they fail to pass these credits on to their customers, b) resellers work with affiliates to churn customers to take advantage of the system c) Staff’s position, if adopted, would “improperly pad the pockets of resellers without providing any benefit to Louisiana customers,” and d) the effect of the cash-back credit must be considered in the aggregate over time.²

¹ Order U-31364, Ordering paragraph 1.

² See AT&T’s reply brief dated March 1, 2011.

What AT&T fails to mention from its statements is that a) there is absolutely no requirement that resellers pass on any credits to their customers, b) there is no evidence in this proceeding that the resellers in this proceeding are engaging in such activity, c) Staff's position would ensure resellers receive no less of a benefit than retail customers and d) the fallacy of considering the effect in the aggregate over time is the lack of a requirement to keep the service over time.

Staff also reminds this Tribunal that AT&T used Staff's failed attempt at humor in characterizing counsel's inability to perform mathematical equations as "dangerous", into an attempt to discredit Staff, using the phrase "dangerous legal mathematics" in a pejorative sense no less than four times in its reply brief. Finally, Staff would also remind this Tribunal that AT&T vehemently argued throughout its reply brief that Staff's methodology was "new" and "unprecedented", despite the fact that the same method was, as properly pointed out the resellers, discussed by Mr. Gillan, and thus not a novel approach.

But why is it important to address these prior arguments again? In simple terms, AT&T's methodology, when applied in a "negative effective price" scenario, produces results that are illogical, a conclusion that cannot be ignored. Any attempt to shift the focus from this illogical conclusion should be rejected.

B. Staff's proposed methodology, rejected by AT&T and this Tribunal, provides the same wholesale price when the credit does not exceed the retail price.

Somewhat glossed over in this proceeding is that Staff's proposed methodology, (despite its warts discussed above), when applied to a scenario wherein the amount of the credit is less than the price of the service, **produces the exact same result as AT&T's methodology.** This occurs even though a different formula is applied. The following example illustrates the above conclusion:

STAFF Methodology:

If AT&T's retail service is \$30 a month, and if it offers a cash back amount of \$20 to sign up for that service, in the first month, the \$20 cash back has the effect of changing the retail rate for that month to \$10. Under Staff's proposal, the 20% avoided cost discount is applied to that \$10, resulting in an avoided cost in month one of \$2. **The wholesale customer thus gets the service for \$8.**

AT&T Methodology:

AT&T argues that the 20% discount must be applied to both the \$30 monthly fee ($\$30 \times 20\%$) and the cash back offering ($\$20 \times 20\%$). Under this scenario, the monthly fee for month one is \$24, the credit is \$16, **the result is the same \$8 charge to the wholesale customer.**

C. AT&T's methodology, however, results in a greater benefit being provided to its retail customers than is provided to wholesaled customers when the effective price is negative.

In no uncertain terms, AT&T's methodology for calculating the cash-back credit provided to a reseller when the amount of the cash-back exceeds the price of the service, results in the reseller receiving less of a benefit than the retail customer in the month that credit is applied. Such a result cannot be logical, particularly when its justification is that the "wholesale discount is applied" resulting in the 20% reduction in the discount. AT&T, through what it has called an appropriately applied avoided cost discount, has devised a method by which it ensures its reseller customers will receive a net benefit of 20% less than its retail customers.³ Thus, as Staff has argued throughout this proceeding, while mathematically correct, the formula defies logic. One need not be an economist, mathematician, or even an attorney, to reach such a conclusion.

³ See Attachment G to AT&T's Reply Brief wherein the \$8.00 credit is characterized as 20% different from net retail.

AT&T will no doubt respond, as it has throughout this proceeding, that it is improper to look at the credit on a one month basis. This argument fails, however, on the fundamental grounds that the cash-back promotion that is the subject of this proceeding requires the customer to remain with AT&T for ONE month only. Regardless of what the average length of time is the customer stays with the company, AT&T still places no obligation the customer remain for that time. As a result, it is only the month in which the credit is applied, that its impact should be addressed.⁴

What hasn't been briefed previously is the absurd consequences that could result from applying AT&T's methodology and formula. If, for example, AT&T decided to offer a \$500 cash-back promotion, under the same terms as the current promotion, and the retail price was \$30, the AT&T retail customer would get a credit of \$470 the first month. Under the AT&T formula, the reseller customer's credit, "reduced" by the avoided cost discount, would result in credit of \$376 dollars. The difference between the \$470 credit and the \$376 credit - 20%. Clearly this cannot be what was contemplated by the Telecommunications Act. While it is unlikely that AT&T would make such a promotional offering, looking at the absurd consequences of AT&T's methodology under such a scenario illustrates how it logically fails.

II. Staff's Logical, Mathematic-Free, Compromise Approach

As shown above, AT&T's methodology could result in a situation resellers are greatly harmed by its application. While Staff is aware that a solution to address such absurd consequences is being considered by the South Carolina Commission⁵, and solution that may have some merit, Staff believes a more simple solution could apply, that would address the

⁴ Staff is aware that the North Carolina Commission has adopted AT&T's argument, and looked at the aggregate impact of the credit over time. Staff respectfully disagrees with this application.

⁵ The South Carolina Commission order, as of the date of this filing, has not been issued to the best of Staff's knowledge. Staff only references this potential decision to the extent it is rendered prior to the briefing schedule in this matter being concluded.

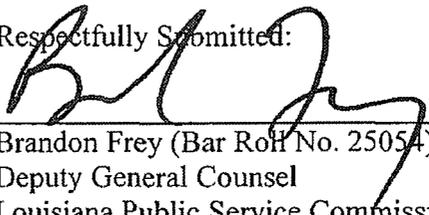
concerns. In simple terms, AT&T should provide the same credit amount to a reseller than it provides to its retail customers, if the cash-back amount is greater than the price of the service.

Under this scenario, the reseller customer would receive precisely the same credit as the retail customer in month one. In simple terms, if the retail price is \$30, and the cash-back amount is \$40, both customers should receive a credit of \$10 in the first month. In each subsequent month the customer maintains service, that month's service is reduced by the avoided cost, as would be the case absent the cash-back offering. Staff fully anticipates AT&T will argue this compromise position has not been argued before this Tribunal and thus should not be considered. However, failing to consider a position that, at the very least, ensures the reseller receives at least the same benefit retail customer, would continue to defy logic.

III. Conclusion

For the reasons stated herein, and in Staff's prior filings, Staff respectfully requests that this Tribunal adopt on remand the position advanced by Staff with respect to the correct treatment of "cash-back" promotions. In the alternative, Staff respectfully requests this tribunal consider Staff's alternative compromise that ensures resellers receive equal benefits as retail customers.

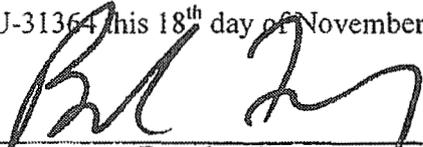
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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing was sent via email to the service lists for docket U-31364 this 18th day of November 2011.



Brandon Frey

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