COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

THE INTERCONNECTION AGREEMENT NEGOTIATIONS BETWEEN AT&T COMMUNICATIONS OF THE SOUTH CENTRAL STATES, INC. AND BELLSOUTH TELECOMMUNICATIONS, INC. PURSUANT TO 47 U.S.C	))))))	CASE NO. 96-482

O R D E R

On February 6, 1997, the Commission entered its final Order deciding the arbitrated interconnection issues between AT&T Communications of the South Central States, Inc. ("AT&T") and BellSouth Telecommunications, Inc. ("BellSouth"). On February 26, 1997, BellSouth filed with the Commission its Motion for Reconsideration and/or Rehearing ("Motion") and on March 7, 1997, AT&T filed its response to BellSouth's Motion, which includes a request that the Commission deny BellSouth's Motion as inappropriate. AT&T states that BellSouth's Motion is "an effort to reargue issues that were litigated fully in the arbitration hearing held January 6-7, 1997." The Commission's decisions regarding the parties' requests follow.

I. RECONSTITUTION OF UNBUNDLED NETWORK ELEMENTS

BellSouth requests rehearing on the issue of recombination of unbundled network elements. It argues that the Commission's decision permits AT&T to circumvent the resale pricing provisions of the Telecommunications Act of 1996 (the "Act") by "engaging in 'sham unbundling,' -- i.e., engaging in the wholly imaginary process of purchasing allegedly unbundled network elements and then 'rebundling or recombining' them in a way that makes them virtually the same in all relevant ways to complete retail offerings."

As support for its argument, BellSouth incorporates by reference the brief and motion for reconsideration that it filed with the Commission in Case No. 96-431.[1] Referencing detailed information contained in that case, BellSouth reiterates that commissions in Georgia, North Carolina,[2] Tennessee,[3] and Louisiana[4] have found that "sham unbundling" is in fact resale. To this list of commissions, BellSouth now adds the commission in

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1 Case No. 96-431, Petition by MCI for Arbitration of Certain Terms and Conditions of a Proposed Agreement with BellSouth Telecommunications, Inc. Concerning Interconnection and Resale Under the Telecommunications Act of 1996.

2 The Commission notes that the North Carolina commission concluded that AT&T should be allowed to combine unbundled elements in any manner it chooses. However, that commission left open the issue of how its decision should be implemented. Further consideration is expected after receipt of additional information. Docket No. P-140 Sub. 50 at 31-32, December 23, 1996.

3 The Commission notes that the Tennessee commission ordered that AT&T and MCI could purchase unbundled elements but could not combine them in any manner they choose. The recombined network elements must provide a new or different service from that being provided by BellSouth. However, this restriction on unbundling is only in effect until the completion of the Federal Communications Commission's ("FCC") universal service and access charges proceedings or until BellSouth has entered the interLATA market, whichever occurs first. Docket No. 96-01152, January 23, 1997 at 42.

4 The Commission notes that in Louisiana, two different arbitrators decided the issue in two different ways. It is expected that the Louisiana commission will enter other rulings to make these decisions consistent.

South Carolina. It anticipates adding the commissions in Alabama,[5] Florida,[6] and Mississippi.[7]

BellSouth contends that the Commission's interpretation of the Act gives a new entrant an unfair competitive advantage. It therefore requests that the Commission reconsider its decision on this issue and find that "sham unbundling" is in fact resale. Accordingly, it seeks reconsideration of the pricing rules for recombined network elements that duplicate BellSouth retail service.

In its response, AT&T states that "[o]ther than alleging that the requirements of the Act, the FCC Order and this Commission's orders in this case and three others are perpetrating a 'sham,' BellSouth offers nothing new in support of its argument that combinations of unbundled network elements should be priced as if they were services offered for resale." It contends that requiring new entrants to pay wholesale prices for the elements would violate the Act. It further contends that "permitting BellSouth to price

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5 The Commission notes that the Alabama commission, in its AT&T-BellSouth arbitration case, ordered that the recombined elements be priced at resale. In its more recent arbitration case between AT&T and GTE, however, the Alabama commission ordered that the recombined elements be priced at TELRIC. Both decisions are under reconsideration.

6 The Commission notes that the Florida commission permitted AT&T and MCI to combine unbundled network elements in any manner they choose and followed the FCC's standards for such recombinations. That commission noted its concern, however, and stated that it would notify the FCC of them and revisit its order if the FCC's interpretation changed. Order No. PFC-96-1579-FOF-TP, December 31, 1996 at 37-38.

7 The Commission notes that in Mississippi, an arbitrator has recommended to the Mississippi commission that the recombined elements be priced at the wholesale discount rates. Docket No. 96-AD-0559 at 24. That commission's decision is expected in mid-April.

combinations of unbundled network elements as if they were wholesale services at resale rates would violate a section of the FCC Order which has not been stayed." Furthermore, AT&T correctly states that this Commission has decided this same issue no less than five times.

AT&T contends that permitting it to purchase unbundled network elements and combine them into a platform does not result in "sham unbundling." The platform configuration, AT&T argues, is not identical to a basic service available for resale; it differs from service resale in structure, pricing, risk and flexibility.

The Commission finds that BellSouth has fully litigated this issue at hearing. BellSouth's motion for rehearing on the issue is therefore denied. The Commission's previous decision that BellSouth may not restrict its provision of unbundled network elements on the basis it suggests is affirmed.

The interpretation of the Act and the FCC's First Report and Order (Docket No. 96-325) has been the subject of considerable debate and a major issue in arbitration proceedings before state commissions. Generally, the debate is whether the language in the Act and the FCC Order is plain on its face. The decision of this Commission, and a majority of others that have considered the issue, has been and is in the affirmative.[8]

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[8] The Commission notes that 32 state commissions and the District of Columbia have issued orders that do not support BellSouth's position. The states involved are: Kentucky, Florida, Alabama, Connecticut, Maine, Massachusetts, New Hampshire, New York, Rhode Island, Vermont, Indiana, Michigan, Ohio, Wisconsin, Colorado, Iowa, Minnesota, Nebraska, Oregon, Maryland, Pennsylvania, Illinois, Hawaii, Missouri, Oklahoma, Texas, Virginia, Washington, North Carolina, Arizona, California, Utah, and Washington, D.C.

The Illinois Commission states that it is "required to follow the FCC's Order and

Reiterating, the Act provides pricing standards for the sale of unbundled elements that differ from the pricing standards for the sale of "service" to another carrier. Furthermore, the Act, at Section 251(c)(3) clearly states that a requesting carrier must be provided with "nondiscriminatory access to network elements on an unbundled basis" and that the incumbent must provide the elements "in a manner that allows requesting

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will therefore impose no restrictions or limitations on the sale or use of unbundled network elements." Order 96-AB-005, December 3, 1996, at 45.

The Missouri Commission finds that "GTE's attempt to restrict AT&T's ability to combine unbundled network elements in order to bypass resale offerings is in direct conflict with the Act, § 251(c) (3), which requires an incumbent to 'provide such unbundled network elements in a manner that allows requesting carriers to combine such elements in order to provide such telecommunications service.' A CLEC should be able to provide services either through resale or through any technically feasible combination of unbundled network elements. The Commission finds that the terms and conditions of the interconnection agreement should not unreasonably restrict AT&T's ability to combine network elements. AT&T should not be prevented from combining purchased network elements to bypass resale offering." Case No. TO-97-63, December 10, 1996 at 35.

The Pennsylvania Commission noted that Section 251(c)(3) permits what AT&T is seeking and found that the Act does not contain any exception or limitation on unbundling. Order A-310125, F0002, December 5, 1996 at 59.

The Arbitration Panel in Alabama regarding AT&T and GTE found that the Act requires GTE to "provide such unbundled network elements in a manner that allows requesting carriers to combine such elements in order to provide such telecommunications service." 47 U.S.C. Section 251(c)(3). The Panel also noted that "the Act also specifically requires that combinations of network elements be priced at unbundled network element rates." 47 U.S.C. Section 252(d)(1). The FCC Order states that an entrant may purchase and combine unbundled network elements in any way it chooses, including the recreation of existing services. 47 C.F.R. §§ 51.309(a), and 51.315(c); FCC Order No. 96-325, Paragraphs 292, 296. The Panel further recommended that GTE be prohibited from restricting or limiting AT&T in any way from combining unbundled network elements and AT&T should be allowed to purchase combinations of unbundled network elements at unbundled network element rates. Docket 25704, issued February 12, 1997, at 30 - 31.

carriers to combine such elements in order to provide such telecommunications service." Thus, the Act confers upon AT&T the authority to combine unbundled network elements to provide any service it chooses.

BellSouth incorrectly states that "the Commission recognized in its Order on Rehearing in the MCI arbitration . . . that its literal interpretation of Section 251(c)(3) will permit new entrants to engage in a substantial arbitrage of BellSouth business rates," which it claims cannot be sufficiently remedied by rate rebalancing alone. In that Order, the Commission recognized that the issue was a critical one and it stated, that BellSouth's insistence that the Commission's Order subjects it to injustice is apparently based upon the false premise that it will be unable to compete when its tariffed rate is substantially higher than the price at which a competitor can buy unbundled elements to provide service. The Commission adopts its finding in Case No. 96-431 that there are alternatives available to BellSouth other than attempting to convince this Commission to distort the statute.

Finally, as the parties correctly state, the Commission has concluded that viable competition is likely to grow if competitors are able to purchase BellSouth's unbundled network elements at cost. BellSouth, relying on the announcement of American Communication Services, Inc. that it has begun to compete with BellSouth for local service in Louisville over its 47 mile fiber network, challenges the Commission's statement in its Order on Rehearing in Case No. 96-431 that: "[I]f competitors are not able to use BellSouth's network elements at cost to provide service, viable competition

is unlikely to grow."[9] The Commission finds that the entry of a single competitor operating on a limited basis does not contradict the Commission's conclusion.

II. VERTICAL SERVICES AND THE LOCAL SWITCHING ELEMENT

BellSouth argues that the Commission's decision allows AT&T to evade the Act's resale pricing provisions by improperly treating vertical services as network elements. Simply purchasing a loop, a port and local switching, BellSouth contends, will not result in obtaining these retail services. BellSouth argues that because retail services are to be offered for resale at a wholesale discount, each of the features, whether activated from within the switch or provided external to the switch, should be treated identically.

As support for its argument, BellSouth states that the switching capabilities involved in the provision of vertical services are similar to those involved in the provision of switched access Feature Group A, where carriers receive the fundamental switching capability only when they purchase that service. In both instances, BellSouth contends, the services involved are retail services and should be treated identically. Stating that it properly omitted the costs of vertical services from the TELRIC study it filed with the Commission, BellSouth requests that the Commission order that the activation of vertical services be at retail rates.[10]

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9 See Order on Rehearing in Case No. 96-431 at 2.

10 On March 11, 1997, BellSouth filed, as an addendum to its Motion, the March 10, 1997 Order of the South Carolina Public Service Commission in the AT&T arbitration in that state, which, inter alia, requires vertical services to be priced at the resale discount. See South Carolina Order at 11.

AT&T argues that the Commission should not reconsider its decisions as a result of BellSouth's "deliberate omission of information in the hearing." Noting BellSouth's admission that it did not include the costs of vertical services in its TELRIC cost studies, AT&T argues that "the cost information clearly could have been developed and provided to the Commission at the original hearing."

AT&T further argues that, pursuant to the Act, BellSouth is required to provide all of the features and functions that are resident in the local switch when AT&T purchases local switching as an unbundled network element. These features, AT&T contends, must be priced as part of the switch at unbundled network element rates.

The Commission agrees with AT&T. Pursuant to 47 U.S.C.A. § 153(45) and 47 C.F.R. § 51.319(c)(1)(C), network elements include all features, functions, and capabilities. BellSouth's Motion is therefore denied.

III. BELLSOUTH'S PRODUCTION OF ADDITIONAL COST STUDIES

BellSouth requests that the Commission resolve an alleged inconsistency between the Commission's Orders requiring it to file additional cost studies. It also requests an Order from the Commission requiring the additional studies to be filed by March 31, 1997. As support for its request, BellSouth states that arbitrations in nine states have placed inordinate demands on its staff.

While AT&T does not raise any objections to BellSouth's request, it does seek, for itself and other parties, an opportunity to provide comments and/or to be heard in an evidentiary proceeding, as appropriate, before the Commission sets final rates.

The Commission finds that its Orders do not contain the inconsistency BellSouth alleges. It also finds that BellSouth's request should be granted, under the circumstances. The additional studies required in this proceeding and in Case No. 96-431 are, therefore, required to be filed with the Commission by no later than March 31, 1997. AT&T and other parties may provide comments, as appropriate, before the Commission sets final rates.

IV. MEDIATED ACCESS TO ADVANCED INTELLIGENT NETWORK ("AIN") ELEMENTS

First, BellSouth requests that the Commission order interested parties to use the "Industry Forum process" to develop interconnection specifics to ensure that the mediation mechanisms which must be developed meet the needs of all parties. BellSouth asserts that, due to the complexities of SS7 interconnection and the potential for impacts on network performance, "several public service commissions have asked involved parties to use the Industry Forum process to drive interconnection in this area." BellSouth contends that such deferral of specifics to cross industry "experts" is a logical approach to resolving the potential problems associated with AIN interconnection.

Pointing out BellSouth's statement in Exhibit 2 to its Motion that discussions on this topic have been ongoing for three years, AT&T states that "[n]ow BellSouth asks the Commission to wait an unspecified length of time while discussions continue." AT&T also states that "during a recent conference call among members of the industry group addressing this issue on December 12, 1996, members determined that they should work to accomplish the initial phase of a six phase program to develop AIN mediation

mechanisms by the end of 1997." AT&T contends that no dates have been set for completing the remaining work.

The Commission finds that BellSouth has not offered any new evidence to support its argument. BellSouth's Motion is therefore denied with the following clarifications. The Commission agrees that all interested parties should have the opportunity and be encouraged to participate in industry forums addressing interconnection issues. However, this Commission has rendered its decision on the use of mediation and until such industry forums recommend otherwise, BellSouth should comply with this Commission's determination.

Second, BellSouth requests rehearing on the issue of mediated access to BellSouth's AIN, citing it as "one of the more important matters to be arbitrated." BellSouth states that "the Commission's decision to require the testing of BellSouth's mediation mechanism for 90 days will not serve the Commission's intended purpose of assuring network reliability." It contends that mediation on a trial basis is not appropriate because: (1) software defects may exist in an interconnector's on-line databases that would not be revealed within the 90-day trial period, (2) it is highly unlikely that any party will agree to develop and implement mediation mechanisms if their useful lifetime may be only 90 days, (3) an inference may be made during such a short trial that mediation mechanisms are not required if no disruption occurs,[11] and (4) in the absence of ongoing use of appropriate mediation mechanisms, BellSouth could be placed in the position of

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[11] BellSouth states that for real-time call processing via SS7 interfaces, the need for a properly functioning mediation mechanism is demonstrated when disruptions do not occur.

assuming liability for service disruption or network outages that are outside its control. For these reasons, BellSouth requests that the Commission order the permanent use of mediation mechanisms for AIN interconnection. It also requests that the Commission clarify that BellSouth is entitled to recover some or all of the costs it will incur to design, develop, test, implement, and maintain the mediation mechanisms.

AT&T states that the Commission should reject BellSouth's attempt to reargue this issue. The Commission finds that this issue has been fully litigated at hearing. BellSouth's Motion to reconsider the Commission's findings or recommendations with respect to requiring the use of mediation mechanisms for a 90-day period is therefore denied.

The Commission maintains that the use of permanent mediation mechanisms may result in less than equal access to competitors. Furthermore, the Commission has insufficient evidence to conclude that unmediated access will necessarily jeopardize the integrity of BellSouth's network. Therefore, the Commission reaffirms its prior decision to allow a 90-day trial period for mediation with the costs to be borne jointly by BellSouth and AT&T. As always, BellSouth retains the right and obligation to ensure, through reasonable means, the performance and reliability of its network. Any specific disputes may be resolved through the Commission's complaint process.

The Commission, having considered BellSouth's Motion and the response thereto, and having been otherwise sufficiently advised, HEREBY ORDERS that:

1. The Commission's February 6, 1997 Order is affirmed in all respects except as modified herein.

2. The additional studies required in this proceeding and in Case No. 96-431 shall be filed by no later than March 31, 1997.

Done at Frankfort, Kentucky, this 18th day of March, 1997.

PUBLIC SERVICE COMMISSION

Vice Chairman

Commissioner

DISSENT OF CHAIRMAN LINDA K. BREATHITT

I dissent only from the majority opinion on the issue of recombination of unbundled elements.

Section 251(c)(3) states that an incumbent local exchange carrier shall provide such unbundled network elements in a manner that allows requesting carriers to combine such elements in order to provide such telecommunications service. On its face, this would logically lead to the conclusion that recombination of the unbundled elements in any manner was contemplated by Congress.

However when taken in context with other sections of the Act, this conclusion fails. In particular if recombinations were contemplated, there would have been no reason for Congress to establish two distinct pricing programs - one for resale and one for network element pricing. The establishment of two pricing arrangements is inconsistent with the idea of recombination of all the elements.

Secondly, the joint marketing prohibition in Section 271(e)(1) states that a telecommunications carrier that serves more that 5 percent of the nation's presubscribed access lines is restricted from jointly marketing its interLATA toll services with services obtained from the BOC via resale. This restriction is lifted when a new entrant purchases unbundled network elements.

It seems to me a loophole in the Act has been exposed. Commissions in Alabama, Georgia, Louisiana, Mississippi, North Carolina, South Carolina and Tennessee have also recognized this.[1]

The Act requires the elimination of implicit subsidies, which is a good thing in a competitive world. BellSouth's business rates need to come down. However, this Commission has long encouraged telephone price subsidies because they keep urban and especially rural residential rates lower. The Commission affirmed this policy again in Case No. 94-121 by freezing residential rates for a period of three years or until there is a universal service fund in place. The elimination of these subsidies should occur, but my concern is that it may occur too swiftly if competitors are permitted to recombine certain network elements. That leaves residential customers scratching their heads and trying to make sense of competition as their bills increase.

I do not have a crystal ball, nor would I be accomplished in its use if I did have one. I do not know BellSouth's plans on rate rebalancing; nor do I know how all this will ultimately shake out. The Commission has opened a docket on universal service with

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[1] The Commissions in Alabama, Mississippi and South Carolina have recognized this loophole in the Act since my original dissent in Case No. 96-431, Petition by MCI for Arbitration of Certain Terms and Conditions of a Proposed Agreement With BellSouth Telecommunications, Inc. Concerning Interconnection and Resale Under the Telecommuications Act of 1996, dated January 29, 1997.

the intent of providing a safety net where necessary subsidies in rates have been removed by competitive pricing; but will universal service come to the rescue of rural customers in time? I fear it may not. I respectfully dissent.

Linda K. Breathitt
Chairman

ATTEST:

Executive Director