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May 6, 2011

The Honorable Jocelyn Boyd
Chief Clerk of the Commission
Public Service Commission of South Carolina
Post Office Drawer 11649
Columbia, South Carolina 29211

Re: Complaint and Petition for Relief of BellSouth Telecommunications, Inc. d/b/a AT&T Southeast d/b/a AT&T South Carolina v. Affordable Phone Services, Inc. d/b/a High Tech Communications, Dialtone & More, Inc., Tennessee Telephone Service, LLC d/b/a Freedom Communications USA, LLC, OneTone Telecom, Inc., dPi Teleconnect, LLC and Image Access, Inc., d/b/a New Phone
Docket No. 2010-14-C, Docket No. 2010-15-C, Docket No. 2010-16-C,
Docket No. 2010-17-C, Docket No. 2010-18-C, & Docket No. 2010-19-C

Dear Ms. Boyd:

Enclosed for filing is AT&T South Carolina's Notice of Subsequent Development in the above-referenced matters.

By copy of this letter, I am serving all parties of record with a copy of these pleadings as indicated on the attached Certificate of Service.

Sincerely,

Patrick Turner

Patrick W. Turner

PWT/nml
Enclosure
cc: All Parties of Record
923033

BEFORE THE
PUBLIC SERVICE COMMISSION
OF SOUTH CAROLINA

In Re: BellSouth Telecommunications, Incorporated d/b/a AT&T Southeast d/b/a AT&T South Carolina v. Affordable Phone Services, Incorporated d/b/a High Tech Communications
Docket No. 2010-14-C

BellSouth Telecommunications, Incorporated d/b/a AT&T Southeast d/b/a AT&T South Carolina v. Dialtone & More Incorporated
Docket No. 2010-15-C

BellSouth Telecommunications, Incorporated 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. 2010-16-C

BellSouth Telecommunications, Incorporated d/b/a AT&T Southeast d/b/a AT&T South Carolina v. OneTone Telecom, Incorporated
Docket No. 2010-17-C

BellSouth Telecommunications, Incorporated d/b/a AT&T Southeast d/b/a AT&T South Carolina v. dPi Teleconnect, LLC
Docket No. 2010-18-C

BellSouth Telecommunications, Incorporated d/b/a AT&T Southeast d/b/a AT&T South Carolina v. Image Access, Incorporated d/b/a New Phone
Docket No. 2010-19-C

AT&T SOUTH CAROLINA'S NOTICE OF SUBSEQUENT DEVELOPMENT

BellSouth Telecommunications, Inc. d/b/a AT&T South Carolina ("AT&T South Carolina") respectfully submits the attached documents to inform the Public Service Commission of South Carolina ("the Commission") of a development in similar proceedings in North Carolina that took place after the parties filed their Briefs and Proposed Orders on March 21, 2011.

AT&T South Carolina's Post-Hearing Brief addresses the North Carolina Commission's Order in favor of AT&T North Carolina in a cashback complaint proceeding dPi brought against

AT&T in that state. *See* AT&T South Carolina's Post-Hearing Brief filed March 21, 2011 at 12-13. dPi appealed that North Carolina Commission Order, and dPi's brief in that proceeding presents the same arguments the Resellers present in their South Carolina brief in this Consolidated Phase. Among the headings of the North Carolina Commission's Response Brief, filed April 21, 2011, are:

> The Method that the [North Carolina Commission] Directed Parties to Use to Calculate Promotional Credits Mirrors the Method Described in *Sanford* by the Fourth Circuit. *See* North Carolina Commission Brief (attached) at 16.
>
> Contrary to dPi's Argument, Federal Provisions Allow Temporary Retail Price Reductions That Drop Below Wholesale Prices and Do Not Require Revisions to the Wholesale Discount in Order to Ensure that Wholesale Prices Are Always Lower than Retail Prices. *Id.* at 17.
>
> Contrary to dPi's Argument, Federal Requirements Do Not Allow Changes to the Discount Percentage for Cashback Promotions. *Id.* at 20.

The North Carolina Commission's discussion associated with these headings squarely addresses and refutes each of dPi's erroneous arguments (which are the same as the arguments the Resellers present in this Consolidated Phase).

Attached for the Commission's convenience is a Reply Brief AT&T recently filed with the Alabama Commission that more fully explains how the North Carolina Commission's Response Brief fully supports AT&T South Carolina's positions in this Consolidate Phase and fully refutes the Resellers' positions. Attachment A to that Reply Brief is dPi's appellate brief in North Carolina (which presents the same arguments the Resellers present in their Brief in this proceeding), and Attachment D to that Reply Brief is the North Carolina Commission's Response Brief discussed above.

In light of the overwhelming authority supporting AT&T South Carolina's position on the issues in this Consolidated Phase, AT&T South Carolina respectfully requests that the

Commission deny the Reseller's request for oral argument and enter an order adopting AT&T South Carolina' position on each issue in this proceeding as quickly as possible.

Respectfully submitted on this the 6th day of May, 2011.

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STATE OF TENNESSEE)
) CERTIFICATE OF SERVICE
COUNTY OF DAVIDSON)

The undersigned, Carolyn Hanesworth, hereby certifies that she is employed by the Legal Department for BellSouth Telecommunications, Inc. d/b/a AT&T South Carolina ("AT&T") and that she has caused AT&T South Carolina's Letter dated April 12, 2011 in Docket Nos. 2010-14-C, 2010-15-C, 2010-16-C, 2010-17-C, 2010-18-C and 2010-19-C to be served upon the following on April 12, 2011:

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April 29, 2011

SECRETARY
Filed
Apr 29, 2011
APSC

Via Electronic Filing and Overnight Mail

Walter Thomas, Secretary
ALABAMA PUBLIC SERVICE COMMISSION
RSA Union Building, Suite 850
100 N. Union Street
Montgomery, AL 36104

Re: BellSouth Telecommunications, Inc., d/b/a AT&T Alabama or AT&T Southeast vs. LifeConnex Telecom, LLC f/k/a Swiftel, LLC Docket No. 31317

BellSouth Telecommunications, Inc., d/b/a AT&T Alabama or AT&T Southeast vs. Tennessee Telephone Service, Inc., d/b/a Freedom Communications, USA, LLC - Docket No. 31318

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

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

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

BellSouth Telecommunications, Inc., d/b/a AT&T Alabama or AT&T Southeast vs. BLC Management, LLC d/b/a Angles Communications Solutions – Docket No. 31322

BellSouth Telecommunications, Inc., d/b/a AT&T Alabama or AT&T Southeast vs. dPi Teleconnect, LLC - Docket No. 31323

Dear Mr. Thomas:

Enclosed for electronic filing today in connection with the above referenced dockets is *AT&T Alabama's Reply Brief*. The original and ten (10) paper copies will be forwarded to the Commission today via overnight mail. Please distribute as needed.

Proud Sponsor of the U.S. Olympic Team

Thank you for your assistance in this matter.

Sincerely yours,

Francis B. Semmes
General Attorney – AT&T Alabama

FBS/mhs
Enclosures

cc: Honorable John Garner, Exec. Director and Chief ALJ
Darrell Baker, Director, Telecommunications Div. (via email)
Parties of Record (via email and U.S. Mail)

BEFORE THE
ALABAMA PUBLIC SERVICE COMMISSION

Re: BellSouth Telecommunications, Inc., d/b/a AT&T Alabama or AT&T Southeast vs. LifeConnex Telecom, LLC f/k/a Swiftel, LLC
Docket No. 31317

BellSouth Telecommunications, Inc., d/b/a AT&T Alabama or AT&T Southeast vs. Tennessee Telephone Service, Inc., d/b/a Freedom Communications, USA, LLC - Docket No. 31318

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

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

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

BellSouth Telecommunications, Inc., d/b/a AT&T Alabama or AT&T Southeast vs. BLC Management, LLC d/b/a Angles Communications Solutions – Docket No. 31322

BellSouth Telecommunications, Inc., d/b/a AT&T Alabama or AT&T Southeast vs. dPi Teleconnect, LLC - Docket No. 31323

AT&T ALABAMA'S REPLY BRIEF

In accordance with the April 13, 2011 Procedural Ruling Granting Joint Motion for Extension of Due Date for Reply Briefs, BellSouth Telecommunications, Inc. d/b/a AT&T Southeast d/b/a AT&T Alabama ("AT&T Alabama") respectfully submits its Reply Brief in this Consolidated Phase proceeding.

AT&T Alabama believes the arguments in the Brief it submitted on April 1, 2011 fully address and refute the arguments presented in the Brief that the Resellers submitted on the same date. AT&T Alabama, therefore, will not restate those arguments here. Instead, this Reply Brief addresses: (1) the Louisiana Staff proposal discussed (but only in part) at pages 22 through 23 of

the Resellers' Brief; (2) the recommendation the South Carolina Office of Regulatory Staff[1] filed on April 6, 2011 in the companion Consolidated Phase proceedings in South Carolina ("South Carolina ORS Recommendation"); and (3) the Brief the North Carolina Commission filed on April 21, 2011 in dPi's appeal of that Commission's Recommended Order that is discussed at page 11 of AT&T Alabama's Brief ("North Carolina Commission's Brief").[2]

I. LINE CONNECTION CHARGE WAIVER ("LCCW") PROMOTIONS

The Resellers argue that when AT&T Alabama waives a $40 line connection charge for a retail customer, instead of giving a Reseller a $33.48 credit to net out the $33.48 wholesale price the Reseller paid for the line connection,[3] AT&T Alabama must actually pay the Resellers a net of $6.52. *See* AT&T's Brief at 36-37. AT&T Alabama, the Louisiana Staff, and the South Carolina ORS disagree.[4] The Louisiana Staff noted that "the application espoused by the Resellers can result in a situation where the Reseller is actually paid for the [line connection]," and it "believes that the proper method for applying the waiver of the line connection charge is to provide a credit to the previously charged amount to the Reseller." *See* Attachment B at 8. Similarly, the South Carolina ORS's Recommendation states that "the [LCCW] waiver should be in the amount of a credit to zero out the amount previously charged to the Reseller" so that "the

---

[1] The Office of Regulatory Staff is state agency, independent of the South Carolina Commission, that "must represent the public interest of South Carolina before the [South Carolina] Commission." *See* S.C. Code Ann. §58-4-10(B).

[2] Although none of the other Resellers were parties to the dPi cashback complaint proceeding in North Carolina, dPi's Brief to which the North Carolina Commission's Brief responds presents that same "cashback" arguments as the Resellers present in the Brief they filed in this Consolidated Phase. *See* Attachment A (copy of dPi's Brief to the federal district court in North Carolina).

[3] This $33.48 amount is the $40 retail price for the line connection discounted by the Commission-established 16.3% resale discount.

[4] The North Carolina Commission's Brief does not address this issue because dPi's complaint in that proceeding did not address LCCW promotions.

Reseller is not paid for the Line Connection Charge." Attachment C at 4. To date, no state Commission or Staff has recommended adopting the Resellers' position on the LCCW issue.

II. WORD-OF-MOUTH PROMOTIONS

The Resellers argue that they are entitled to resell referral marketing programs like the word-of-mouth promotion. AT&T Alabama, the Louisiana Staff, and the South Carolina ORS disagree.[5] The Louisiana Staff summarily rejected this argument, stating "Staff agrees with AT&T that the word-of-mouth promotions should not be subject to resale." *See* Attachment B at 8. The South Carolina ORS "submits that resale obligations apply only to 'telecommunications services' the ILEC provides at retail, and a marketing referral program like 'word-of-mouth' should not be subject to resale." Attachment C at 3. To date, no state Commission or Staff has recommended adopting the Resellers' position on the word-of-mouth issue.

III. CASHBACK PROMOTIONS

The Resellers argue that the Commission-approved 16.3% resale discount should be applied to the full standard price of the service to which the promotion applies and not to the lower promotional price of the service (that is, the standard price less the cashback benefit). As explained below, the South Carolina ORS and the North Carolina Commission disagree and appropriately find that the resale discount should be applied to the promotional price of the service as advocated by AT&T North Carolina.

The Louisiana Staff also disagrees with the Resellers when the cashback benefit is less than the monthly price of the service, but as the Resellers note at pages 22-23 of their Brief, the Louisiana Staff proposes an unprecedented alternative methodology when the cashback benefit is

[5] The North Carolina Commission's Brief does not address this issue because dPi's complaint in that proceeding did not address referral marketing programs like the word-of-mouth promotion.

greater than the monthly price of the service. The Louisiana Staff's alternative methodology (which is substantively identical to Resellers' Method 2), however, is inconsistent with a Proposed Recommendation issued by an Administrative Law Judge in Louisiana, and it is flawed for all of the reasons set forth at pages 16 through 36 of AT&T Alabama's Brief. As explained below, the Louisiana Staff's proposal also is inconsistent with the more recent (and more well-reasoned) South Carolina ORS Recommendation and North Carolina Commission's Brief.

A. Promotions with a cashback benefit that is less than the monthly price of the applicable service(s).

The Louisiana Staff, the South Carolina ORS, and the North Carolina Commission all agree with AT&T Alabama that the Commission-established resale discount should be applied to the promotional price of the service when the cashback amount is less than the retail price of the applicable service. The Louisiana Staff's proposal, for example, yields the same results as AT&T Alabama's methodology when the cashback amount is less than the price of the service. *See* Attachment B at 7-8 (applying Louisiana Staff's proposal to a one-time cashback benefit of $50 and a service with a monthly price of $60). Similarly, "[f]or cash-back promotions where the cash-back amount is less than the standard retail price of the service, the [South Carolina] ORS recommends that the [South Carolina] Commission adopt AT&T's position that the wholesale discount . . . be applied to the promotional price and not to the standard retail price of the services that are subject to the promotional offerings." Attachment C at 2. And the North Carolina Commission's Brief supports that Commission's prior determination that the resale discount is to be applied to the promotional price of the service, explaining that "the dPi approach is simply incorrect mathematically" and "ignores the formula that is inherent in the FCC regulation . . . ." Attachment D at 10.

B. Promotions with a cashback benefit that is greater than the monthly price of the applicable service(s).

As anticipated at pages 15-29 of AT&T Alabama's Brief, the Resellers erroneously argue that AT&T Alabama's method creates an impermissible "wholesale is greater than retail" situation when the cashback amount is greater than the retail price of the associated services. Distracted by this argument (which is thoroughly refuted at pages 16-36 of AT&T Alabama's Brief), the Louisiana Staff proposed an unprecedented alternative methodology to address these situations.[6] The Louisiana Staff's proposal, however, is inconsistent with a Proposed Recommended Decision of an Administrative Law Judge in a separate proceeding in Louisiana, *see* AT&T Alabama's Brief at 11-12, and the Administrative Law Judge presiding over the Consolidated Phase proceeding has yet to issue a recommended decision addressing the Louisiana Staff's proposal. The Louisiana Staff's proposal also is inconsistent with the more recent (and more well-reasoned) South Carolina ORS Recommendation and North Carolina Commission's Brief, both of which consider and expressly reject the Reseller's "wholesale is greater than resale" argument.

The South Carolina ORS, for instance, rejects the Resellers' argument that only the month in which the cash benefit is received should be considered, explaining instead that "cash-back promotions where the cash-back amount is higher than the standard retail price of the services" should be "evaluated over a reasonable period of time." Attachment C at 3. The ORS, however, also expressed a theoretical concern that AT&T's position "could impede a Reseller's ability to compete" if what the Resellers characterize as a "negative price" situation persists over a long period of time. In order to "balance these concerns," the ORS recommended that the South Carolina Commission:

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[6] The Louisiana Staff's proposal is substantively identical to the Resellers' Method 2, which is described at pages 17-18 of AT&T's Brief.

> find that ATT's method is appropriate when the net amount paid by a Reseller in the aggregate is greater than the net amount paid by a retail customer in the aggregate over a period of three months or less, but where the net amount paid by a Reseller in the aggregate is greater than the net amount paid by a retail customer in the aggregate over a period of four or more months, Resellers can challenge AT&T's methodology before this Commission in light of the specific facts of the situation. ORS respectfully submits that this is consistent with the reasoning that led the Federal Communications Commission to exempt promotions lasting ninety (90) days or less from the resale obligations of the Telecommunications Act of 1996.

Attachment C at 3. While AT&T Alabama acknowledges that the ORS's recommendation is much more reasonable (and much more consistent with controlling law) than the proposals suggested by the Resellers, it believes that the disciplines imposed by the competitive marketplace render the "greater than four months" aspect of the ORS's recommendation unnecessary. It is clear from the North Carolina Commission's Brief that it too believes this aspect of the recommendation is unnecessary.

The North Carolina Commission's Brief states that dPi's argument "that its method for calculating promotional credits must be used in order to ensure that wholesale prices are *always* lower than retail prices . . . is flawed for several reasons."[7] Attachment D at 17. The North Carolina Commission's Brief notes (as does AT&T Alabama at pages 22-23 of its Brief) that as a result of the FCC's rule exempting short-term promotional offerings from the resale provisions of federal law, "the price that retail customers pay may temporarily fall below the wholesale price." *Id.* at 18. Accordingly, the North Carolina Commission's Brief states that "the argument is not compelling that the difference between the retail price and the wholesale price in a particular month is problematic," *id.* at 19, and it concludes that "dPi's argument that the full value method must be used to calculate promotional credits in order to keep wholesale prices less than net retail prices in a particular month is flawed." *Id.* at 20.

---

[7] This argument in dPi's North Carolina brief is substantively identical to the "wholesale is higher than retail" arguments the Resellers make in this proceeding.

The North Carolina Commission's Brief further states that dPi's example of a cashback amount that is four times greater than the retail price of the underlying service is "exaggerated" in light of the evidence in that proceeding. *See* Attachment D at 20. Similarly, on cross-examination in this Consolidated Phase proceeding, Reseller witness Dr. Klein conceded that there is no evidence of a cashback amount that exceeds the monthly price of a service by a factor of four. (Tr. at 258-259). This is why AT&T Alabama respectfully submits that the disciplines imposed by the competitive marketplace render the "greater than four months" aspect of the South Carolina ORS's recommendation unnecessary.

The North Carolina Commission's Brief goes on to note that both methods proposed by dPi (which, again, are identical to the methods proposed by the Resellers in these proceedings) result in discounts from the promotional retail price that exceed the resale discount rate established by the North Carolina Commission. Consistent with AT&T Alabama's arguments at pages 26-30 of its Brief, the North Carolina Commission's Brief explains that "[w]ithout performing a cost study, it is not appropriate for the [North Carolina Commission] to abandon the 21.5% percentage discount established for AT&T." Attachment D at 20. *See also Id.* at 21 ("dPi's position that the formula should be altered in this case would result in a change in the percentage discount without analysis, contrary to federal regulatory requirements.").

Finally, the North Carolina Commission's Brief effectively addresses (and refutes) the Resellers' "rebate" argument, stating that "dPi also appears to argue that the full value of the cashback offers should be credited . . . so that the same terms and conditions offered to retail customers are offered to resellers." *Id.* at 22. Consistent with AT&T Alabama's position set forth at pages 31-33 of its Brief, the North Carolina Commission's Brief rejects this argument, explaining that "the obligation relating to promotional offers is to provide the *benefit* of the

promotional offer through the wholesale price charged the reseller, not to provide the promotional item (such as a gift or cash) itself." Attachment D at 22. In other words, the 1996 Act may require AT&T Alabama to pass certain aspects of a service along to the Resellers in the same manner as that are provided to retail customers, but price is not one of them. *See* AT&T Alabama's Brief at 31.

CONCLUSION

For all the reasons set forth above and in AT&T Alabama's Brief, AT&T Alabama respectfully requests that the Commission enter an Order finding that:

> It is appropriate for AT&T Alabama to make cashback promotional offerings available for resale by a two-step process whereby: (1) the reseller orders the requested service and is billed the standard retail price of the service discounted by the 16.3% resale discount rate established by the Commission; and (2) the reseller requests a cashback promotional credit which, if verified as valid by AT&T Alabama, results in the reseller receiving a bill credit in the amount of the face value of the retail cashback benefit discounted by the 16.3% resale discount rate established by the Commission.
>
> It is appropriate for AT&T Alabama to make LCCW promotional offerings available for resale by a two-step process whereby: (1) the reseller is initially billed the standard retail price for the line connection discounted by the 16.3% resale discount rate established by the Commission; and (2) the reseller requests a LCCW promotional credit which, if verified as valid by AT&T Alabama, results in the reseller receiving a bill credit in the amount of the standard retail price for the line connection discounted by the 16.3% resale discount rate established by the Commission
>
> AT&T Alabama is not required to make marketing referral promotions like the "word-of-mouth" offering available for resale.

Respectfully submitted on this the 29th day of April, 2011.

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ATTORNEYS FOR
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d/b/a AT&T ALABAMA

920597

CERTIFICATE OF SERVICE

I hereby certify that I have served a copy of *AT&T Alabama's Reply Brief* on all parties of record by electronic mail this **29th** day of **April**, 2011, and by placing a copy of same in the United States Mail, properly addressed and postage prepaid.

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FRANCIS B. SEMMES

ATTACHMENT A

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NORTH CAROLINA
WESTERN (RALEIGH) DIVISION

Case No.: 5:10-CV-466-BO

dPi TELECONNECT, L.L.C. Plaintiff. v. Edward S. Finley, Jr. *et al.*, Defendants.	§ § § § § § § § §	dPi's MOTION FOR SUMMARY JUDGMENT/BRIEF ON THE MERITS

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B. An ILEC may not restrict resale of these presumptively unreasonable and discriminatory promotions that are offered in excess of 90 days without securing pre-approval from this Commission to do so.. 21

1. The Recommended Order contradicts a plain reading of the FCC rule, the only known federal case to specifically address the issue, and the Commission's own precedent – all of which show that ILECs must secure Commission approval prior to imposing restrictions on a CLEC's acceptance of promotional offers. 22

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IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NORTH CAROLINA
WESTERN (RALEIGH) DIVISION

Case No.: 5:10-CV-466-BO

dPi TELECONNECT, L.L.C.	§	
	§	
Plaintiff.	§	
	§	**dPi's MOTION FOR SUMMARY**
v.	§	**JUDGMENT/BRIEF ON THE**
	§	**MERITS**
Edward S. Finley, Jr. *et al.*,	§	
Defendants.	§	

I. INTRODUCTION

1. This dispute centers around BellSouth Telecommunications, Inc. d/b/a AT&T North Carolina ("AT&T")'s failure to comply with its obligations under 47 U.S.C. 251(c)(4)(A), 47 U.S.C. 252(d)(3), and 47 C.F.R. § 51.607, to sell services to dPi Teleconnect, L.L.C. ("dPi") at AT&T's effective retail price for those services less AT&T's avoided costs. More specifically the issue is whether AT&T must extend to dPi the full amount of promotional credits or rebates on services when dPi is otherwise eligible for the promotion.

2. This appeal arises under § 252(e)(6), and §§ 251(c)(4) and 252(d)(3) of the Federal Telecommunications Act of 1996 (the "FTA" or "Act"), which is the source of the Court's jurisdiction in this matter. It is essentially an appeal of a state commission's decision of a dispute arising under the FTA, because the North Carolina Commission did not compel AT&T to meet its statutory obligations arising from the Act and the regulations promulgated thereunder.

II. FACTS

A. Regulatory Background

3. The FTA opens up the local telephone service market by, among other things, requiring the incumbent local exchange carriers ("ILECs"), such as AT&T, to offer their retail services at wholesale rates to competitive local exchange carriers ("CLECs"), such as dPi. 47 USC § 251(c)(4).

4. The wholesale rate is calculated by subtracting from AT&T's retail price the costs AT&T avoids, or saves, by providing the service at wholesale rather than retail. 47 USC § 252(d)(3); 47 C.F.R. § 51.607.

5. Among other things, the ILECs' resale obligations require that when ILECs make special or promotional offers to their retail customers over periods of 90 days or more, ILECs must extend those offers to CLECs, like dPi, as well. 47 C.F.R. § 51.605; 47 C.F.R. § 51.613.

B. Procedural background and generic facts of the case

6. dPi Teleconnect resells AT&T's retail residential telephone services. dPi's dispute centers on credits which are due from AT&T to dPi Teleconnect as a result of dPi Teleconnect's reselling of services subject to AT&T promotional discounts.

7. AT&T has over the past months and years sold its retail services at a discount to its end users under various promotions that have lasted for more than 90 days. dPi is entitled to purchase and resell those same services at the promotional rate, less the wholesale – that is, costs avoided – discount.

8. As a practical matter, dPi Teleconnect has bought these services at the regular retail rate less the resale discount, then been credited the difference between that rate and the

promotional rate pursuant to "promotion credit requests."

9. Of concern in this particular case, AT&T has provided a number of "cash back" promotions going back to late 2003.[1] Although dPi met the same qualifications as AT&T's retail end users, and applied for these promotional credits, it was not paid the credits requested for the periods ending June 8, 2007. AT&T has, however, paid the credits requested for service rendered after June 2007. The timing appears to coincide with the 4th Circuit's decision in *BellSouth Telecommunications Inc. v. Sanford et al.*, 494 F3d 439 (C.A. 4 – N.C., 2007), in which the 4th Circuit upheld the North Carolina Commission's decision that promotions that tend to reduce the retail price paid by retail customers must be made available to CLECs.

10. dPi initiated a case against AT&T on its refusal to extend the promotions to dPi before the North Carolina Commission on April 11, 2008. The case was styled *In the Matter of the Complaint of dPi Teleconnect, L.L.C. Against BellSouth Telecommunications, Inc.*, Docket No. P-55, SUB 1744, before the State of North Carolina Utilities Commission. In this docket, dPi sought a decision that dPi was (1) entitled to the cash back promotions, because they reduced the effective retail rate of underlying service; and (2) that the costs avoided by AT&T in providing a service subject to a cash back promotion does not change, and should be based on the standard or tariffed rate.

11. The Commission heard the case and entered a recommended decision in part favorable to dPi on May 7, 2010: the Commission held that dPi was entitled to the benefit of the cash back promotion, but allowed AT&T to discount the amount of cash back that it

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[1] The three promotions involved through July 2007 are designated by AT&T as Cash Back $100 Two Features - C2TF; Cash Back $100 Discount Complete Choice $100; and Cash Back $50 2 Pack Plan (PAMA6) - CBP6

extended dPi. Both AT&T and dPi filed exceptions to the proposed order. On October 1, 2010, the Commission entered denying the parties' exceptions and adopting and providing further support for the May 7, 2010, recommended order.

C. Key facts and law relevant to this appeal

12. The FTA[2] and federal regulations (particularly 47 C.F.R. § 51.607) set the resale rate for telecommunications services that an ILEC may charge at "the [retail] rate for the telecommunications service, less avoided retail costs..."[3] Thus, the "wholesale discount" must by law be calculated as the avoided cost.

13. Note that while the amount of the discount is the avoided cost, that *cost* is subtracted from the retail ***price*** – whatever that retail price might be. Costs are not necessarily directly related to the price for a service. "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.
- "Price" is the value or what a customer has to give up in order to acquire that.
- Simply because a price changes does not necessarily mean that a cost has

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[2] 47 U.S.C. § 252(d)(3): Wholesale prices for telecommunications services

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

[3] **47 C.F.R. § 51.607 Wholesale pricing standard.**

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

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

changed. It certainly doesn't cause a cost to change.

14. 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.

15. The Commission has set BellSouth/AT&T's avoided costs in the wholesale context at a percentage of the standard retail price of the respective telecommunications service. When originally determined by the Commission, the avoided cost was based on, and calculated from, BellSouth/AT&T's pre-promotion (or standard/tariffed) retail rate. This is considered a fair approximation by all parties.

16. Since the wholesale price is based on the retail price (whether positive or negative), from which one ***subtracts*** the costs avoided, is clear from context that the FTA and the rules promulgated thereunder expect that the wholesale price should necessarily always be less than the retail price.

17. The costs of providing a particular service do not change, even if some purchasers of that service may have a coupon or similar promotional mechanism which allows those purchasers to secure the service at 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 that same service sold pursuant to a special sale, or promotional rate.

18. A cash back promotion, if available to a qualifying order, applies a single time and is paid in a single lump sum. It is not paid out over time; for example, a $50 cash back promotion is paid by a single check for $50, not a $5 payment each month for 10 months.

19. An end user need not stay on the platform for more than 30 days in order to qualify for a cash back promotion.

20. In all other months in which no promotion is in effect it is agreed that the avoided costs are calculated by applying the discount percentage to the standard/non-promotional rate.

21. One of the questions before the Commission was how to determine the amount a reseller is entitled to when reselling services subject to cash back promotions for the single month when the promotion is processed. (No other months are in dispute.)

22. Three methodologies have been identified for determining the avoided cost discount (wholesale discount) when promotions are involved:

(1) calculating 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;

(2) calculating the calculating the wholesale (cost avoided) discount associated with a service as a percentage of the standard/tariffed price less a percentage of the cash back promotion amount. This is the method advocated by AT&T under the theory that it resulted in reducing the net retail price by the wholesale discount (*see e.g.* Document 17, AT&T's Brief in Support of Proposed Order at 26-27). This is the method sanctioned by the Commission after briefing; and

(3) calculating 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:

Wholesale = (retail price – cash back) – % *ABS(retail – cash back)

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

23. A comparison of the results from applying these three methodologies to illustrative price points and promotion amounts is produced in Table 4, below.

Table 4. Comparison of results using various methods.						
Standard Retail Price	**Standard Wholesale Discount Percentage**	**Promotion Amount**	**Net Retail Price**[1]	**Method 1: dPi: Net Wholesale Price assuming avoided cost calculated as % of standard retail price**[2]	**Method 2: AT&T 'less than': Net Wholesale Price assuming avoided cost calculated as % of standard retail price less % of promotion**[3]	**Method 3: True 'less than:' Net Wholesale Price assuming avoided cost calculated as % "less than" net retail price**[4]
$25	20%	–	$25	$20 ($5 less than net retail)	$20 ($5 less than net retail)	$20 ($5 less than net retail)
$25	20%	$25	$0	-$5 ($5 less than net retail)	$0 (**same** as net retail)	$0 (**same** as net retail)
$25	20%	$50	-$25	-$30 ($5 less than net retail)	-$20 ($5 **MORE** than net retail)	-$30 ($5 less than net retail)
$25	20%	$100	-$75	-$80 ($5 less than net retail)	-$60 ($15 **MORE** than net retail)	-$90 ($15 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

3. (Standard Retail Price x Wholesale Discount Percentage) -
(Promotional Discount x Wholesale Discount Percentage) = Avoided Costs

4. Wholesale Discount Percentage "Less Than" Net Retail Price = Net Wholesale Price; that is,
Wholesale = (retail price – cash back) – % *ABS(retail – cash back)

24. The first method uniformly produces a wholesale price that is lower than the retail rates by the fixed amount determined by applying the discount percentage to the standard/non-promotional retail rate.

25. The second method, which ***purports*** to reduce the retail price by a percentage, actually results in situations (such as when the standard retail rate of the service is $25, and

the promotion amount is equal to, or greater than, $25) where the wholesale rate is higher than the retail rate, and the costs avoided in providing the service are not subtracted from the net retail rate.

26. The third method (which is essentially the second method corrected to the mathematical expression of how to ensure that one is ***reducing*** the retail price by a particular percentage), produces a wholesale price that tends to be lower than the retail rates by an amount that varies with the amount of the promotion (and thus the net effective retail rate). However, as the net effective retail rate approaches zero, so too does the amount calculated as the avoided cost. Thus, when the net retail rate ends up at zero, there is no reduction for costs avoided at wholesale – even though there are costs avoided when the service is sold at an effective retail rate of zero.

III. ANALYSIS

27. The FTA[1] and federal regulations (particularly 47 C.F.R. § 51.607) set the resale rate for telecommunications services that an ILEC may charge at "the [retail] rate for the telecommunications service, less avoided retail costs..."[2] Thus, the "wholesale discount"

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

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

[2] **47 C.F.R. § 51.607 Wholesale pricing standard.**

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

"Avoided retail costs shall be those costs that reasonably can be avoided when an incumbent LEC provides a telecommunications service for resale at wholesale rates to a requesting carrier."

must by law be calculated as the avoided cost. Moreover, since the wholesale price is based on the retail price (whether positive or negative), from which one ***subtracts*** the costs avoided, is clear from context that the FTA and the rules promulgated thereunder expect that the wholesale price should necessarily always be less than the retail price. Intuitively, this must be correct: 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.

28. However, the Commission's decision conflicts with federal law and regulation because it adopts a methodology which violates the key principle that wholesale should be less than retail.

A. How to correctly calculate the avoided costs: subtracting the known avoided costs from the net retail rate.

29. The question before the Commission was how to determine the amount dPi is entitled to when reselling services subject to cash back promotions for that single month when the promotion is processed. No other months are in dispute. In making this determination, the Commission failed to keep two keep principles in mind.

30. First, the FTA[3] and federal regulations (particularly 47 C.F.R. § 51.607) set the resale rate for telecommunications services that an ILEC may charge at "the rate for the

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47 C.F.R. § 51.609(b). Further, "the amount of avoided retail costs shall be determined on the basis of a cost study...." 47 C.F.R. § 51.609(a).

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

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

telecommunications service, less avoided retail costs, as described in section 51.609."[4] Thus, ***the "wholesale discount" must by law be calculated as the avoided cost.***

31. Second, it is clear from context that the FTA and the rules promulgated thereunder expect that the ***wholesale price should be less than the retail price.***

32. When considering the wholesale – that is, cost avoided – discount, keep in mind that while the statute bases the wholesale discount on certain costs avoided, costs are not necessarily directly related to the price for the service. 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.
- "Price" is the value or what a customer has to give up in order to acquire that.
- Simply because a price changes does not necessarily mean that a cost has changed. It certainly doesn't cause a cost to change.

Obviously, 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, of if the customer is given cash to take the service for one of the months that it is offered. Moreover, the costs of providing a particular service do not change, even if some 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 that same service sold pursuant to a special sale, or promotional rate.

33. The principle that wholesale rates should always be lower than retail rates is noted

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

by the Fourth Circuit Court of Appeals in *BellSouth Telecommunications, Inc. v. Sanford*,[5] which indicates that the wholesale discount should be employed to create a lower charge to a reseller when compared to a retail customer. In *Sanford*, the Fourth Circuit reversed a federal district court ruling and restored a North Carolina Utilities Commission order which held that promotional offers extending for more than 90 days created a "promotional retail rate" to which the avoided cost discount must be applied.[6] The Fourth Circuit 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.[7] The *Sanford* decision, therefore, makes it clear that ILECs cannot use long-term promotional offerings to price resellers out of the market; these promotional offerings must be made available to resellers as well, subject to the costs avoided wholesale discount set by each state Commission. The Fourth Circuit recognized that in order for resellers to be able to compete in the telecommunications market, resellers must be subject to a lower, wholesale charge as compared to retail customers.

34. So what is the avoided cost associated with providing a service? The Commission set BellSouth/AT&T's avoided costs in the wholesale context at a percentage of the retail price of the respective telecommunications service. When originally determined by this Commission, the avoided cost was based on, and calculated from, BellSouth/AT&T's pre-promotion (or standard/tariffed) retail rate, because that is the calculation most consistent

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

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

7 *Sanford* at 442.

with the Commission's avoided cost methodology.

35. Three methodologies have been identified for determining the avoided cost discount (wholesale discount) when promotions are involved:

(1) calculating 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;

(2) calculating the calculating the wholesale (cost avoided) discount associated with a service as a percentage of the standard/tariffed price less a percentage of the cash back promotion amount. This is the method advocated by AT&T under the theory that it resulted in reducing the net retail price by the wholesale discount (*see e.g.* Document 17, AT&T's Brief in Support of Proposed Order at 26-27). This is the method sanctioned by the Commission after briefing; and

(3) calculating 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:

Wholesale = (retail price – cash back) – % *ABS(retail – cash back)

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

36. Of these methods advanced, the first (dPi's) most closely conforms to the key principles underlying the Act, because it uniformly produces a wholesale price that is lower than the retail rates. The second method (advanced by AT&T as reducing the effective retail rate by a fixed percentage, and endorsed by the Commission) cannot be correct because it results in situations where the wholesale rate is higher than the retail rate, and the costs avoided in providing the service are not subtracted from the net retail rate. If the intent is truly to reduce the effective rate by a given percentage, the mathematically correct way to do so is to apply the third method.

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

37. 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 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.**

38. **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 service. 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.**[1] **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.**

39. **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**

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[1] At the time this Commission established its wholesale discount rate at a percent of the retail rate of telecommunications services, it focused on the tariffed, retail rate of services provided to calculate a wholesale discount percentage based on the methodology that the avoided costs for each products is proportional to its price. This methodology 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.

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 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 Price[1]	Net Wholesale Price[2] 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

40. 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.*** As will be shown, other methods of determining the cost avoided discount do not produce such results, and in fact

BellSouth/AT&T's proposed method actually results in a situation ***where the wholesale rates are higher than retail.***

41. Another reason for adopting the method above is that the Act and FCC regulations require BellSouth/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 BellSouth/AT&T's cash back promotions. According to the Act and pertinent FCC regulations, BellSouth/AT&T is required to offer its services for resale "subject to the same conditions" that BellSouth/AT&T offers its own end-users and at "the rate for the telecommunications service less avoided retail costs."[2] For example, when BellSouth/AT&T offers retail telephone service in conjunction with a "$50 cash back" rebate to new customers, BellSouth/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 BellSouth/AT&T retail customers. As such, 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.

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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.

42. An important factor in the Commission's decision not to adopt dPi's method was the mistaken concern that adopting dPi's method would result in resellers receiving "a greater benefit" than dPi would receive had AT&T merely reduced the service's rate. But of course, the point here is that AT&T ***does not*** reduce its monthly rate. A cash back promotion is a price gimmick – a one-time deal designed to win business from competitors – that does ***not*** change the standard monthly rate and thus does ***not*** indicate a change in avoided costs. Thus, applying dPi's method does nothing more than preserve the cost avoided dollar difference between wholesale and retail – whether a service is offered with or without a promotion that might affect its effective retail rate.

2. Improper Method for Determining Avoided Cost: Reducing the Cash Back Amount by the Wholesale Discount.

43. BellSouth/AT&T persuaded the NCUC that if AT&T is required to extend cash back promotions to CLECs at all, then it should not be required to extend to CLECs the entire amount of the promotion, but rather a lesser amount derived by reducing the promotional amount by the resale discount. AT&T claimed that its formula correctly resulted in reducing the effective retail rate by the fixed percentage.

44. In fact, AT&T's formula does ***not*** uniformly result in ***reducing*** the effective retail rate for resellers: in the situations at hand, this methodology results in a situation where its calculation of the wholesale price produces ***a wholesale price greater than the retail price***. This flaw is dramatically illustrated by the promotions in question as shown in Table 2, below:

Table 2. **Results of applying BellSouth/AT&T's proposed method for calculating promotion amount due resellers (applying hypothetical 20% wholesale discount to both standard/tariff price and to promotional price).**				
Standard Retail Price	**Standard Wholesale Discount Percentage**	**Promotion Amount**	**Net Retail Price[1]**	**Net Wholesale Price[2] assuming avoided cost calculated as % of standard retail price less % of promotion**
$25	20%	–	$25	$20 ($5 less than Net Retail)
$25	20%	$25	$0	$0 (**same** as Net Retail)
$25	20%	$50	-$25	-$20 ($5 **MORE** than Net Retail)
$25	20%	$100	-$75	-$60 ($15 **MORE** than Net Retail)

1. Standard Retail Price - Promotional Discount = Net Retail Price

2. (Standard Retail Price x Wholesale Discount Percentage) - (Promotional Discount x Wholesale Discount Percentage) = Net Wholesale Price

45. This disparity is even more glaring when portrayed on number graphs, as shown on the next page.

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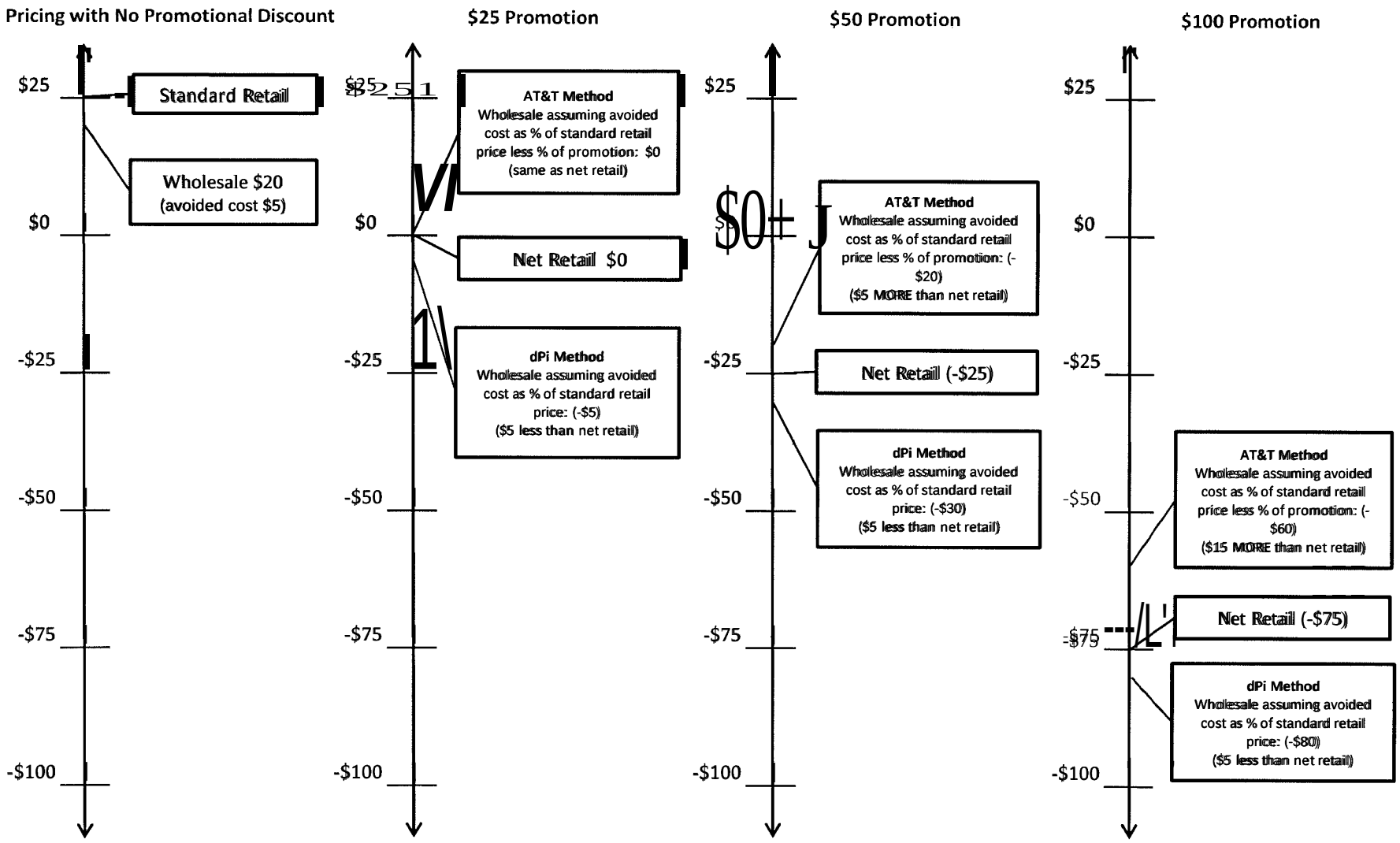
Pricing with No Promotional Discount
$25
$0
-$25
-$50
-$75
-$100
Standard Retail
Wholesale $20
(avoided cost $5)
$25 Promotion
AT&T Method
Wholesale assuming avoided cost as % of standard retail price less % of promotion: $0
(same as net retail)
Net Retail $0
dPi Method
Wholesale assuming avoided cost as % of standard retail price: (-$5)
($5 less than net retail)
$50 Promotion
AT&T Method
Wholesale assuming avoided cost as % of standard retail price less % of promotion: (-$20)
($5 MORE than net retail)
Net Retail (-$25)
dPi Method
Wholesale assuming avoided cost as % of standard retail price: (-$30)
($5 less than net retail)
$100 Promotion
AT&T Method
Wholesale assuming avoided cost as % of standard retail price less % of promotion: (-$60)
($15 MORE than net retail)
Net Retail (-$75)
dPi Method
Wholesale assuming avoided cost as % of standard retail price: (-$80)
($5 less than net retail)

46. A comparison of the results from using the various methodologies is produced in Table 4, below.

Table 4.

Comparison of results using various methods.

Standard Retail Price	Standard Wholesale Discount Percentage	Promotion Amount	Net Retail Price[1]	Method 1: dPi: Net Wholesale Price assuming avoided cost calculated as % of standard retail price[2]	Method 2: AT&T 'less than': Net Wholesale Price assuming avoided cost calculated as % of standard retail price less % of promotion[3]	Method 3: TRUE 'less than:' Net Wholesale Price assuming avoided cost calculated as % "less than" net retail price[4]
$25	20%	–	$25	$20 ($5 less than net retail)	$20 ($5 less than net retail)	$20 ($5 less than net retail)
$25	20%	$25	$0	-$5 ($5 less than net retail)	$0 (same as net retail)	$0 (same as net retail)
$25	20%	$50	-$25	-$30 ($5 less than net retail)	-$20 ($5 MORE than net retail)	-$30 ($5 less than net retail)
$25	20%	$100	-$75	-$80 ($5 less than net retail)	-$60 ($15 MORE than net retail)	-$90 ($15 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

3. (Standard Retail Price x Wholesale Discount Percentage)-
(Promotional Discount x Wholesale Discount Percentage) = Avoided Costs

4. Wholesale Discount Percentage "Less Than" Net Retail Price = Net Wholesale Price; that is,
Wholesale = (retail price – cash back) – % *ABS(retail – cash back)

Table 4 clearly shows that the BellSouth/AT&T method results in a higher charge (through a lower credit) to resellers when compared to the retail rate paid by end-use customers. Obviously, adopting a model which results in a wholesale price that is greater than the retail price guts the purpose of the FTA, violates federal (and Commission) pricing rules, and

dooms competition. The BellSouth/AT&T methodology produces an absurd result – a wholesale price that is higher than the retail price. Accordingly, BellSouth/AT&T's model cannot be correct. It is not possible to comply with the federal wholesale pricing standard with a wholesale price that is ***greater*** than the retail rate as proposed by BellSouth/AT&T. The only way that the wholesale pricing standard could be satisfied by a wholesale rate greater than the retail rate is if there are negative avoided costs that when subtracted from the retail rate, produce a higher number. However, there are no "negative" avoided costs; avoided costs are ***always*** positive.

47. Note that by "discounting" the promotions- and thereby effectively reducing the amount of the wholesale discount – BellSouth/AT&T turns the key holding from *Sanford* on its head. In nearly all instances involving the cash back promotional offering at issue in this proceeding, BellSouth/AT&T has used the Commission's wholesale discount to subject resellers to a *higher* price for the underlying telecommunications service when compared to the effective retail rate to end-use customers, as shown in Table 4, above. If the retail rate of an BellSouth/AT&T telecommunications service is $25, and BellSouth/AT&T offers a $50 cash back promotion in the first month to customers who order that service, a BellSouth/AT&T retail customer would receive a credit of $25 as a result of the promotion at the normal retail rate ($25 service less the $50 cash back, resulting in a -$25 effective retail rate). In the resale context, however, BellSouth/AT&T has been *increasing* the -$25 received by its customers by the 20% discount factor normally applied to the standard rates to arrive at a price of -$20 (-$25 *increased* by 20%), or a credit of $20 to resellers. The effect of BellSouth/AT&T's methodology is to increase the cost to CLECs, through a smaller promotion credit, as compared to the same service purchased by an BellSouth/AT&T

customer. Thus, the BellSouth/AT&T method is contrary to the purpose underlying the Commission's wholesale discount and the rationale of *Sanford*. By applying the "discount" to a negative price (*i.e.*, the cash-back component), the "discount" becomes a benefit to BellSouth/AT&T (not the reseller).

48. Under the Commission's method, there would be no benefit (in fact, there would be a deterrent) for a reseller to purchase at wholesale any telecommunications service which is accompanied by a promotional offering with a value that exceeds the cost for the underlying service; it would be more beneficial in such situations to pay the full retail price. If the Commission's method is sustained, BellSouth/AT&T (and similarly situated ILECs) could effectively price resellers such as dPi out of the market by offering similar promotions for all of the ILEC's telecommunications services and charging the resellers more (by providing them with a smaller credit) for the services and accompanying promotions. This form of regulatory arbitrage is both anti-competitive and unlawfully discriminatory.

3. Third method for calculating the avoided costs: correcting AT&T and the Commission's method to ensure that wholesale price actually is a fixed percentage *less than* the net retail price.

49. If the intent is truly to make the wholesale price ***reduced*** 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. Table 3 shows how this works under various scenarios.

Table 3. Results of applying "percentage less" calculation to effective retail rate.				
Standard Retail Price	**Standard Wholesale Discount Percentage**	**Promotional Discount**	**Net Retail Price**[1]	**Net Wholesale Price**[2] (assuming avoided cost calculated as % "less than" net retail price)
$25	20%	–	$25	$20 ($5 less than net retail)
$25	20%	$25	$0	$25 (same as net retail)
$25	20%	$50	-$25	$25 ($5 less than net retail)
$25	20%	$100	-$75	$25 ($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) – % *ABS(retail – cash back)

50. This method is otherwise 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 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.

B. An ILEC may not restrict resale of these presumptively unreasonable and discriminatory promotions that are offered in excess of 90 days without securing pre-approval from this Commission to do so.

51. In "Evidence and Conclusions for Findings of Fact Nos. 14, 15, 16, 17, 18, 19, 20, 21, 22, 23, 24, and 25", the Recommended Order states that "an ILEC may restrict resale of these presumptively unreasonable and discriminatory promotions that are offered in excess of 90 days without securing pre-approval from this Commission to do so." This holding is

in direct contravention of 47 C.F.R. § 51.613(b); the only known federal case on this issue; and even the Commission's own precedent, including the Orders in Docket No. P-100, Sub. 72(b). Moreover, following the FCC rules and precedent will neither unduly tax the Commission's resources (since only rarely should ILECs be seeking to impose restrictions on CLECs accepting promotional offers given that all restrictions are presumed to illegal), nor should it chill ILECs from offering promotions, since pre-approval is not necessary for instituting promotions, but only from blocking access to those promotions.

1. The Recommended Order contradicts a plain reading of the FCC rule, the only known federal case to specifically address the issue, and the Commission's own precedent – all of which show that ILECs must secure Commission approval prior to imposing restrictions on a CLEC's acceptance of promotional offers.

52. The Commission's Recommended Order's "Evidence and Conclusions for Findings of Fact Nos. 14, 15, 16, 17, 18, 19, 20, 21, 22, 23, 24, and 25" states that "an ILEC may restrict resale of these presumptively unreasonable and discriminatory promotions that are offered in excess of 90 days without securing pre-approval from this Commission to do so." This determination directly contravenes 47 C.F.R. § 51.613(b); the only know federal case on this issue; and Commission precedent, including the Commission's *Restriction on Resale Order*.

a. Federal law requires pre-approval of restrictions on resale, including promotions

53. In selling telecommunication services to CLECs like dPi, an ILEC has a duty "not to prohibit, and not to impose unreasonable or discriminatory conditions or limitations on, the resale of such telecommunication service." 47 U.S.C. § 251(c)(4)(B). This rule is refined and reinforced by FCC regulations, which provide, with very limited exceptions, that the "incumbent LEC shall not impose restrictions on the resale by [a competitive LEC] of

telecommunication services offered by the incumbent LEC." 47 C.F.R. 51.605(e).

54. If an ILEC wishes to impose any restriction on resale, it may do so, but "only if it proves to the state commission that the restriction is reasonable and nondiscriminatory." 47 C.F.R. § 51.613(b). Even then, the FCC has imposed a negative presumption on the validity of any resale restriction or condition that must be overcome. As the FCC ruled in its *Local Local Competition Order,*[3] "we, as well as state commissions, are unable to predict every potential restriction or limitation an incumbent LEC may seek to impose on a reseller. Given the probability that restrictions and conditions may have anticompetitive results, we... *presume* resale restrictions and conditions to be ... in violation of *section 251(c)(4)*." Therefore, ILECs have a heavy burden to overcome *prior* to being permitted to impose a restriction or limitation on resale. The rationale for establishing the presumption is to eliminate litigation burdens on *resellers* – "This presumption **should reduce unnecessary burdens on resellers** seeking to enter local exchange markets, which may include small entities, **by reducing the *time and expense of proving affirmatively* that such restrictions are unreasonable**." *Id.* [emphasis added].

55. The Commission's Recommended Order would reverse this federal presumption that resale restrictions are unreasonable and discriminatory by essentially allowing restrictions unless challenged; and instead of requiring an ILEC to follow the federal directive to obtain Commission approval before restricting resale, the Recommended Order incorrectly places the burden on the CLEC to challenge each restriction on resale. This is diametrically opposed to the federal scheme outlined by the FCC in its rules and orders, and the only

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[3] *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, First Report and Order, 11 FCC Rcd 15954, ¶939 **(rel. Aug. 8, 1996) ("Local Competition Order").**

known federal case on this issue.

b. Federal precedent requires pre-approval of restrictions on resale, including promotions.

56. This issue about whether an ILEC must secure state commission approval prior to imposing restrictions on the resale of promotions came up in federal court in 2009 in *Budget Prepay, Inc. et al., v. AT&T Inc., f/k/a SBC Communications, Inc. et al.*, Cause No. No. 3:09-CV-1494-P in the US District Court, Northern District of Texas, Dallas Division (reversed on other grounds.) In that case, AT&T was attempting to impose its "RPMA" restrictions on the cash back promotions, a situation which would have resulted in AT&T providing only ~$3.00 - ~$7.00 on each $50 promotion involved (depending on the state involved.) The U.S. District Court enjoined AT&T from imposing such restrictions until it had secured state commission approval to do so. In its November 30, 2009, Order (attached as Appendix A), the court noted that:

> "... it would be bad policy to require Plaintiffs in this specific case to [first challenge the ILEC's restrictions at the state commissions] because it would allow Defendants to shift to Plaintiffs the duties imposed upon ILECs by the Act. The Act imposes on ILECs a duty to obtain state commission approval before placing restrictions on resale. 47 C.F.R. § 51.613(b). When an ILEC imposes a restriction on resale that is not permitted under 47 C.F.R. § 51.613(a), subsection (b) requires an ILEC "to prove to the state commission that the restriction is reasonable and nondiscriminatory" before imposing the restriction. Despite the regulation placing the duty of going to the state commission on ILECs, Defendants have asked the Court to require the Plaintiffs, CLECs, to go to the state commission before bringing a claim in federal court. Were the Court to oblige Defendants request it would allow them to contravene the requirements and intent of the Act." p. 13-14
>
> "... Congress passed the FTCA with the intent of "opening previously monopolistic local telephone markets to competition." *SWBT*, 208 F.3d at 477. Congress entrusted the FCC with the duty of promulgating regulations that would ensure the Act's purpose would be met, including regulations that prevented ILECs from placing restrictions on resale that are unreasonable or discriminatory. 47 U.S.C. § 251(c)(4)(B). To that end, 47 C.F.R. § 51.613(b) requires ILECs to prove that restrictions on resale are reasonable and nondiscriminatory before imposing such

restrictions. Requiring ILECs to obtain state commission approval prior to placing restrictions on resale demonstrates a recognition that resale restrictions can have a devastating effect on a CLEC's ability to remain competitive. More importantly, it clearly places the duty to gain state commission approval on ILECs - not CLECs.... Defendants ignored their own duty to gain state commission approval before placing restrictions on resale." p. 14.

c. Commission precedent requires pre-approval of restrictions on resale, including promotions.

57. The Commission itself has looked long and hard at promotional issues in Docket No. P-100, Sub72b, *In the Matter of Implementation of Session Law 2003-91, Senate Bill 814 Titled "An Act to Clarify the Law Regarding Competitive and Deregulated Offerings of Telecommunications Services."* In that docket, the Commission repeatedly recognized that an ILEC must first secure approval from the Commission before imposing restrictions on the resale of promotions. For example, in its December 22, 2004, *Order Ruling on Motion Regarding Promotions ("Restriction on Resale Order,")*, after finding that anything of economic value paid, given, or offered to a customer to induce the purchase of services are promotional discounts, the Commission found that:

> "... *upon proof* that it is reasonable and nondiscriminatory not to offer the benefit of a promotion offered for more than 90 days to resellers, ILECs will not be required to provide such benefit to resellers in addition to the established reseller wholesale discount. However, ILECs should be mindful that resale restrictions on unreasonably long, unlimited or permanent promotions that compete with and undercut the tariffed retail price for services would gut the resale obligation of TA96 and will be held unreasonable." p. 13

58. Moreover, in its *Order Clarifying Ruling on Promotions and Denying Motions for Reconsideration and Stay ("Restriction on Resale Order II,")*[4], the Commission clearly imposes the above noted requirement from 47 C.F.R § 51.613(b), stating:

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[4] Docket No. P-100, Sub. 72(b), June 3, 2005

> ...the Commission...recognize[s] that FCC rules do permit and ILEC to restrict resale of a promotion offered at retail for more than 90 days, upon *proving* that the restriction is reasonable and nondiscriminatory
>
> ***
>
> In order to withhold the benefit of a long-term (90-day-plus) promotional rate from resellers, an ILEC is ***first*** required to "[prove] to the [Commission] that the restriction is reasonable and nondiscriminatory.... The Commission will consider all arguments and admissible evidence presented and decide on a promotion-by-promotion basis...whether an ILEC has proved that a restriction on resale is permissible pursuant to 47 C.F.R. 51.613(b). ***The Commission cannot authorize a restriction on resale of a long-term promotion in the absence of such proof.*** [5]

59. The Recommended Order in this instance is thus directly opposite of the Commission's prior rulings.

2. Following the FCC rules, Commission precedent, federal precedent will neither unduly tax the resources of the Commission, nor stifle ILEC promotional offers.

60. The Recommended Order advances two reasons for refusing to mandate an ILEC's seeking prior approval for imposing restrictions on resale. The first is that "imposing a mandated pre-approval process would unnecessarily burden the Commission's resources because it would have to convene a proceeding to address *all* such offerings instead of only addressing those to which affected parties actually object." The second reason advanced is that requiring an ILEC to seek approval prior to imposing restrictions on the resale of its promotions "would also have a chilling effect on the competitive offerings available to consumers" because other carriers would have advanced notice of such offerings.[6] Both concerns are misplaced.

61. First, it is unlikely that a mandate requiring an ILEC to secure pre-approval prior

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[5] *Restriction on Resale Order II,* at p. 3 (emphasis added).

[6] Recommended Order at p. 10.

would create an undue strain on Commission resources, because these proceedings should be few and infrequent, and uncontroversial restrictions would be unopposed. Remember, prior approval is necessary only where AT&T seeks to ***restrict*** its resale obligations – an occurrence which should be expected to be infrequent, since such restrictions are presumptively unreasonable and discriminatory.

62. In any event, the pre-approval process need not be unduly burdensome even in those few instances in which it would be invoked. As in the tariff change filing process, the pre-approval process could be structured such that once the request for approval of a restriction is filed, there is time for objections, and, if none are made, the restrictions can be implemented.

63. Second, following the law by requiring ILECs to secure approval prior to imposing restrictions on the resale of promotional offerings will not produce a chilling effect on competition as a consequence of having to secure advance approval. This is because the law does not prevent the ILEC from instituting the promotion without notice; 47 C.F.R. § 51.613(b) and the *Restriction on Resale Order,* provide only that ***restrictions*** on resale of promotions lasting over 90 days are subject to prior Commission approval In other words, AT&T would have no need to seek Commission approval if AT&T were to offer its long-term promotions to resellers "subject to the same conditions" as AT&T offers these promotions to retail end-users.[7] The Recommeded Order cites to footnote 12 on p. 13 of the *Restriction on Resale Order,* for the proposition that ***not*** requiring pre-approval for imposing restrictions on the resale of promotions is consistent with prior Commission thought on the matter. Careful reading shows this analysis to be incorrect: the footnote referenced is ***not***

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[7] *See* 47 CFR § 51.603(b)

concerned with the ILEC's obligation to secure prior Commission approval prior to restricting CLECs from reselling promotional offerings without ; footnote 12 is concerned with the ILEC's right to ***offer the promotion to the public*** without obtaining advance Commission's approval.

IV. CONCLUSION AND PRAYER

64. The Commission failed to compel AT&T to comply with its obligations under 47 U.S.C. 251(c)(4)(A), 47 U.S.C. 252(d)(3), and 47 C.F.R. § 51.607, to sell services to dPi Teleconnect, L.L.C. ("dPi") at AT&T's effective retail price for those services less AT&T's avoided costs by failing to require AT&T to extend to dPi the full amount of promotional credits or rebates on services when dPi is otherwise eligible for the promotion. The Commission's Recommended Order's holding – that an ILEC may restrict resale of these presumptively unreasonable and discriminatory promotions that are offered in excess of 90 days without securing pre-approval from this Commission to do so -- **directly contravenes 47 C.F.R. § 51.613(b) and the only know federal case on this issue.**

65. **Consequently, dPi respectfully requests that judgment be entered for dPi granting the following relief:**

> **a declaration that the Commission's order is contrary to the FTA of 1996 and/or arbitrary and capricious and that that dPi is entitled to the full amount of the promotion credits, with a reversal or remand of this case to the PUC with the instruction that the PUC issue a new order not inconsistent with the Court's ruling in this case; and**
>
> **such other and further relief to which the Plaintiff may be entitled at law or in equity.**

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on the 16th day of March, 2011, a true and correct copy of the forgoing was filed with the CM/ECF electronic filing system, which constitutes electronic service upon the following parties of record in this action:

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ATTACHMENT B

BEFORE THE
LOUISIANA PUBLIC SERVICE COMMISSION

DOCKET NO. U-31364

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

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

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

DPI TELECONNECT, LLC;
AND
TENNESSEE TELEPHONE SERVICE, INC. D/B/A FREEDOM COMMUNICATIONS USA, LLC

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

STAFF'S POST-HEARING BRIEF

The Staff of the Louisiana Public Service Commission ("Staff") respectfully submits this post-hearing brief in the above captioned consolidated proceeding. For the reasons set for herein, Staff concludes that 1) the proper wholesale rate applicable when a "cash-back" promotion is offered is the "effective retail price" of the telecommunications service multiplied by the LPSC's 20.72% avoided cost; 2) that credits to resellers for "waiver of line connection charge" promotion ("WLCC") should be equal to the amount the reseller was charged the service; and 3) that word-of-mouth promotions should not be available for resale.

I. Background and Procedural History

The parties to this proceeding, BellSouth Telecommunications Inc. D/B/A AT&T Southeast D/B/A AT&T Louisiana ("AT&T") and the collective "Resellers[1]" have done an

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[1] Image Access, Inc. D/B/A New Phone, Budget Prepay, Inc. D/B/A Budget Phone, BLC Management D/B/A Angles Communications Solutions D/B/A Mexicall Communications, dPi Teleconnect, LLC and Tennessee

admirable job of providing this Tribunal with the background and procedural history regarding how this matter ultimately came before the Commission. In simple terms, the issues that remain at dispute are the appropriate treatment for resale purposes of "cash-back promotions" offered by AT&T to its retail customers; the appropriate treatment for resale purposes of WLCC promotions offered by AT&T to its retail customers; and the availability of word-of-mouth promotions offered to AT&T retail customers as a resale offering. Rather than further restating the background and procedural summaries previously stated in the post-hearing briefs filed by AT&T and the Resellers, Staff's brief will focus on the controlling law and its application to the current dispute.

II. Applicable Law

Pursuant to the 47 USC § 251(c)(4)(A), Incumbent Local Exchange Carriers ("ILECs") have a duty,

> to offer for resale at wholesale rates any ***telecommunications service*** that the carrier provides at retail to subscribers who are not telecommunications carriers. (emphasis added)

Interestingly, neither AT&T, nor the Resellers have provided a citation to what is defined to be "telecommunications service" as contained above. The Telecommunication Act provides us guidance in 47 USC § 153(43), wherein it defines telecommunications as follows:

> The term "telecommunications" means the transmission, between or among points specified by the user, of information of the user's choosing, without change in for or content of the information as sent and received.

Further, 47 USC § 153(46) defines "telecommunications service" as follows:

> The term "telecommunications service" means the offering of telecommunications for a fee directly to the public, or to such classes of

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Telephone Service, Inc. D/B/A Freedom Telecommunications USA, LLC. are collectively referred to herein as "Resellers".

> users as to be effectively available directly to the public, regardless of the facilities used.

In addition to the requirement to offer telecommunications services for resale, an ILEC has a further duty, as stated by 47 USC § 251(c)(4)(B)

> not to prohibit, and not to impose unreasonable or discriminatory conditions or limitations on, the resale of such telecommunications service.

Congress provided some guidance on how such wholesale rates should be established in 47 USC § 252(d)(3), stating

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

In simple terms, the wholesale rate an ILEC is authorized to charge a reseller of its telecommunications service are the "avoided costs" to provide that service. LPSC Order Number U-22020, consistent with Section 252(d)(3), determined the applicable wholesale discount (i.e. avoided cost) to be applied to BellSouth's retail telecommunications services in Louisiana as 20.72%

The FCC, in adopting rules to implement the Telecommunications Act, provided some additional guidance regarding the resale obligations of ILECs. While the majority of these rules focus on pricing, 47 C.F.R. §51.613 does provide some insight on how promotions are to be viewed. In pertinent part, §51.613(a)(2) provides as follows:

> (2) Short term promotions. An incumbent LEC shall apply the wholesale discount to the ordinary rate for a retail service rather than a ***special promotional rate*** only if:
>
> (i) Such ***promotions involve rates*** that will be in effect for no more than 90 days; and

> (ii) The incumbent LEC does not use such promotional offerings to evade the wholesale rate obligation, for example by making available a sequential series of 90-day ***promotional rates***. (emphasis added)

The LPSC, in Section 1101 B 5 of the Commission's Regulations for Competition in the Local Telecommunications Market, essentially mirrors the above Rule, stating:

> Short-term promotions, which are offered for 90 days of less, are not subject to mandatory resale. Promotions that are offered for more than ninety (90) days must be made available for resale, at the Commission established discount, with the express restriction that TSPs shall only offer ***a promotional rate obtained from the ILEC for resale*** to those customers who would qualify for the promotion if they received it directly from the ILEC. (Emphasis added)

III. Staff's Analysis of the Controlling Law

In his pre-filed testimony, Reseller witness Mr. Gillan states that the law is clear on the issue of how "cash-back" rebates should be treated, consistent with the Resellers' position[2]. Not surprisingly, AT&T's witness Dr. Taylor provides testimony concluding the law supports AT&T's methodology as the correct one. Yet, despite this perceived clarity in the rules, the LPSC finds itself with the task of deciphering the meaning of the FCC's rules and regulations.

What we do know unequivocally under the above-cited law is that AT&T has an obligation to provide, at a wholesale discount, and free from any unreasonable and discriminatory conditions, telecommunications services to the Resellers. That wholesale price at which these services are to be provided in simple terms can also be referred to as the "avoided cost", a term used throughout the testimony of the witnesses for both AT&T and the Resellers[3]. We also know that the LPSC has established that avoided cost at 20.72%, a wholesale rate that has not been modified since its adoption by Order U-22020, and has been continuously applied.

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[2] Gillan direct page 4, lines 7-11, page 6 lines 10-13.
[3] For example, Taylor Direct page 7, lines 11-16; Gillan direct, page 5, line 23.

Finally, While the above-cited rules discuss "promotions", they make no mention of "cash-back" offers or rebates, waivers of line connection charges or word-of-mouth promotional offers.

A. FCC's Treatment of "Promotions"

The above-cited law, and the LPSC's rules provide that when "promotions" are offered by an ILEC to its retail customers for greater than 90 days, the "***promotional rates***" shall be available for resale at the wholesale discount. Thus, the only discussion of "promotions" contained in the federal rules clearly contemplates the application of the wholesale discount to the "***promotional rates***". From the language contained in §51.613(a)(2), it is apparent to Staff that the "promotions" contemplated by the FCC in the rules were those that lowered the rate for a particular service. A simple example would be as follows:

> AT&T's monthly retail service is $25 dollars, but it offers a promotion (for greater than 90 days) that if a customer signs up for the service, the rate will be discounted to $15 for the first three months of service. Under such a scenario, it should be undisputed that the promotional rate, $15 is reduced by the Commission's 20.72% avoided cost to determine the appropriate wholesale rate.

Staff's scenario described above closely mirrors the scenario discussed during the cross-examination of Mr. Gillan by Mr. Turner.[4]

B. BellSouth Telecommunications Incorporated v. Sanford[5]

What is not explicitly contemplated in the Act or the rules is the situation where a "cash-back" reward/offering[6] is made to a new customer. This very issue was the subject of the Fourth Circuit's decision in *Sanford*. The case stems from a North Carolina Utilities Commission ("NCUC") decision that determined an incumbent provider's "incentive offers", such as gift

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[4] See transcript day 2, pages 17, line 19, through page 21.
[5] *BellSouth Telecommunications Incorporated v. Sanford*, 494 F.3d 439 (4th Cir. 2007).
[6] Or WLCC promotion or word-of-mouth promotion.

cards and cash rebates, when extended to subscribers for more than 90 days, created a promotional retail rate that must be offered to competitors, less a wholesale discount."[7] The court concluded that, while gift cards, coupons and gifts are not "telecommunications services" these incentives result in the reduction of the price or fee for telecommunication services and thus ultimately reduce the rate that should be subject to the wholesale discount.[8] Sanford ultimately concluded that that the NCUC was correct in determining that such incentive offers have the effect of changing the actual retail rate, to which the wholesale discount must be applied.[9]

Staff agrees with the Sanford conclusion in determining that incentives such as "cash-back" offerings, while not necessarily "telecommunications services", can have the effect of reducing the retail rate offered to an ILEC's customers. Accordingly, they are required to be subject to resale in the sense that they lower the retail rate to which the wholesale discount must be applied. Staff disagrees with the position advocated by the Resellers that relies upon the concurring opinion in *Sanford* in distinguishing between a rebate and discount, and reminds this Tribunal that the majority in *Sanford* agreed with NCUC methodology.

1. Applying Sanford methodology to the "cash-back" scenario.

Staff must compliment witnesses for both AT&T and the Resellers in describing the mathematical formulas in a method that even an attorney can understand. For purposes of discussing how Staff's approach would apply to the "cash-back" offering, Staff will refer this Tribunal to Mr. Gillan's equations outlining the alternative positions[10]. They are as follows:

<u>Reseller Proposal</u>

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[7] Sanford at page 442.
[8] Id at 449.
[9] Id at 443.
[10] See Gillan Rebuttal testimony, page 3, lines 4-14.

Wholesale Rate = (Discount) x (Retail Rate)- (Cash-Back)

AT&T Proposal

Wholesale Rate = (Discount) x (Cash Back) – (Retail Rate) x (Cash-Back)[11]

Staff concludes that the proper method for determining what is available to a reseller is not the method adopted by AT&T, nor is it the method adopted by the resellers, but rather a third option that is consistent with both the Rules and *Stanford*. Applying "legal mathematics", certainly a dangerous proposition, to Staff's position on this issue results in the following formula:

Staff's Position- (Effective Retail Rate)

Wholesale Rate = (Retail Rate) – (Cash-Back)[12] x (Discount)

Under this formula, the wholesale rate is determined by applying the avoided discount to what has become the "effective retail rate." In this respect, the "effective retail rate" is no different that the "promotional rate" contemplated in both §51.613(a)(2) and Section 1101 B 5. Staff's proposed formula would apply as follows:

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

The formula works as well when the "cash-back" does not reduce the effective retail price to a negative number.

> AT&T's retail service is regularly priced at $60. A one-time cash-back rebate of $50 is offered, thus reducing the "effective retail rate" of the service to $10. To

[11] In a similar exercise, Dr. Taylor refers to the proposals as Full Cash-Back (Reseller) and Discount Cash-Back (AT&T)- see Taylor Rebuttal, page 5, lines 1-2.
[12] "Effective" Retail rate of the service.

that amount the wholesale discount is then applied, resulting in a wholesale value of $8, once again consistent with the 20% adjustment.

Under the Staff's proposal, the avoided cost between the effective retail rate and the wholesale discount is preserved. Staff's proposal also addresses the concerns raised by the resellers wherein AT&T's "Discounted Cash Back" proposal results in a greater credit for its retail customers. In conclusion, Staff believes this position is consistent with the Act and Federal rules, the LPSC's rules and the limited jurisprudence on this topic and thus should be adopted.

C. Waiver of Line Connection Charge and Word-of-Mouth Promotions

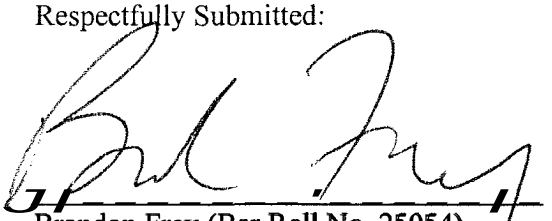
Staff believes that AT&T and the Resellers have clearly presented this issue to the Commission. Currently, AT&T offers promotions whereby the Line Connection Charge is waived to its retail customers. As pointed out in the testimony, the retail customer normally would incur a charge of $40 for the Line Connection, and as a result of the waiver is charged nothing. The Resellers, however, are first charged the LCC, at the applicable wholesale discount, and they credited back the amount assuming they qualify for the promotion. Under the Reseller's proposal, however, it is argued that the waiver amounts to a rebate and thus the full amount (prior to application of the wholesale discount) must be credited to the Reseller.

As AT&T points out in its testimony and post-hearing brief, the application espoused by the Reseller can result in a situation where the Reseller is actually paid for the LCC. Staff agrees with AT&T's position, and for the reasons provided by AT&T, believes that the proper method for applying the waiver of the line connection charge is to provide a credit to the previously charged amount to the Reseller. Finally, Staff agrees with AT&T that the word-of-mouth promotions should not be subject to resale.

IV. Conclusion

For the reasons stated herein, Staff respectfully requests that this Tribunal adopted the position advance by Staff with respect to the correct treatment of "cash-back" promotions, and adopt the position of AT&T with respect to the Waiver of Line Connection Charge promotion and Word-of-Mouth promotion.

Respectfully Submitted:



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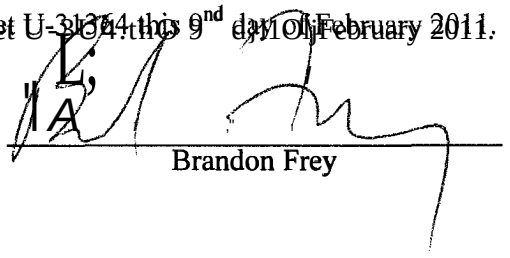
CERTIFICATE OF SERVICE

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 9nd day of February 2011.



Brandon Frey

Service List for U-31364
as of 2/9/2011

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Eric Skrmetta, Commissioner
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April 6, 2011

VIA ELECTRONIC FILING

The Honorable Jocelyn Boyd
Chief Clerk and Administrator
Public Service Commission of South Carolina
101 Executive Center Dr., Suite 100
Columbia, SC 29210

Re: Complaint and Petition for Relief of BellSouth Telecommunications, Incorporated d/b/a AT&T Southeast d/b/a AT&T South Carolina v. Affordable Phone Services, Incorporated d/b/a High Tech Communications
Docket No. 2010-14-C

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

Complaint and Petition for Relief of BellSouth Telecommunications, Incorporated 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. 2010-16-C

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

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

Complaint and Petition for Relief of BellSouth Telecommunications, Incorporated d/b/a AT&T Southeast d/b/a AT&T South Carolina v. Image Access, Incorporated d/b/a NewPhone
Docket No. 2010-19-C

Dear Ms. Boyd:

Although the South Carolina Office of Regulatory Staff ("ORS") did not present testimony or file proposed orders and briefs in the above referenced dockets, attorneys for both complainant and defendants have asked ORS to review the issues raised in this matter.

In considering the briefs submitted by the parties, ORS submits the following recommendations for the Commission's consideration in deciding the issues before the Commission in this proceeding. The three issues before the Commission are as follows:

I. The methodology for computing cash back credits to Resellers of AT&T South Carolina's ("AT&T") retail promotions
II. Whether word-of-mouth promotions are available for resale and if so the methodology for computing credits to Resellers
III. The calculation of credits to Resellers for waiver of the line connection charge

I. Cash-Back Promotions

The Federal Communications Commission's *Local Competition Order*[1] provides that promotions lasting longer than ninety (90) days are subject to resale. An Incumbent Local Exchange Carrier ("ILEC") must offer for resale at wholesale rates any telecommunications service that the carrier provides at retail to subscribers who are not telecommunications carriers.[2] Furthermore, an ILEC cannot impose unreasonable or discriminatory conditions or limitations on, the resale of such telecommunications service. Consistent with the Telecommunications Act, the South Carolina Public Service Commission established a wholesale discount of 14.8% to be applied to BellSouth Telecommunications, Inc.'s retail telecommunications services in Order No. 97-189.

For cash-back promotions where the cash-back amount is less than the standard retail price of the service, ORS recommends that the Commission adopt AT&T's position that the wholesale discount of 14.8% be applied to the promotional price and not to the standard retail price of the services that are subject to the promotional offerings. For example, assuming a monthly retail amount of $30.00 with a cash-back promotion of $25.00 using AT&T's methodology maintains an avoided cost percentage of 14.8%.

AT&T's Method						
Total Paid	$ 25.56	$ 51.12	$ 76.68	$ 102.24	$ 127.80	$ 153.36
Total Cashback	$ (21.30)	$ (21.30)	$ (21.30)	$ (21.30)	$ (21.30)	$ (21.30)
Net Amount Paid	$ 4.26	$ 29.82	$ 55.38	$ 80.94	$ 106.50	$ 132.06
% Difference from Net Retail	14.8%	14.8%	14.8%	14.8%	14.8%	14.8%

[1] *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98, First Report and Order, 11 FCC Red 15499, (1996)(*Local Competition Order*), *subsequent history omitted.*
[2] 47 USC § 251(c) (4)(A)

However, for cash-back promotions where the cash-back amount is higher than the standard retail price of the services, ORS recommends a different approach. While we believe that it is not appropriate to consider only the month in which the cash-back is received, ORS believes that these types of promotion should be evaluated over a reasonable period of time. ORS can foresee circumstances in which AT&T's methodology could impede a Reseller's ability to compete. For example, if AT&T offered $200 cash-back on a service with a monthly price of $20.00, under AT&T's method it would be many months before the aggregate amount a retail customer pays for the service exceeds the aggregate amount a Reseller pays for the service:

AT&T's Method						
Total Paid	$ 17.04	$ 34.08	$ 51.12	$ 68.16	$ 85.20	$ 102.24
Total Cashback	$ (170.40)	$ (170.40)	$ (170.40)	$ (170.40)	$ (170.40)	$ (170.40)
Net Amount Paid	$ (153.36)	$ (136.32)	$ (119.28)	$ (102.24)	$ (85.20)	$ (68.16)
% Difference from Net Retail	**14.8%**	**14.8%**	**14.8%**	**14.8%**	**14.8%**	**14.8%**

To balance these concerns, ORS recommends that the Commission find that AT&T's method is appropriate when the net amount paid by a Reseller in the aggregate is greater than the net amount paid by a retail customer in the aggregate over a period of three months or less, but where the net amount paid by a Reseller in the aggregate is greater than the net amount paid by a retail customer in the aggregate over a period of four or more months, Resellers can challenge AT&T's methodology before this Commission in light of the specific facts of the situation. ORS respectfully submits that this is consistent with the reasoning that led the Federal Communications Commission to exempt promotions lasting ninety (90) days or less from the resale obligations of the Telecommunications Act of 1996.

II. Word-of-Mouth Promotions

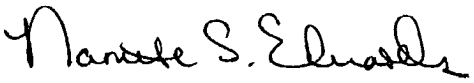
AT&T states that qualifying AT&T South Carolina retail customers can receive promotional benefits such as gift cards under these offerings if they convince friends and family members who are not AT&T retail customers to purchase particular AT&T services (i.e. word-of-mouth promotion). The Resellers in their brief state that the Word-of-Mouth promotion allows an AT&T customer to receive a $50 rebate for referring a new customer to AT&T. ORS submits that resale obligations apply only to "telecommunications services" the ILEC provides at retail, and a marketing referral program like "word-of-mouth" should not be subject to resale. Therefore, ORS recommends that the Commission adopt AT&T's position on this issue.

III. Waiver of Line Connection Charge Promotions

AT&T also offers a line connection charge waiver ("LCCW") promotion to its end-users. The retail customer would normally incur a charge for the line connection, and as a result of the waiver is charged nothing. The Resellers are first charged the Line Connection Charge at the applicable wholesale discount and then are credited back the amount assuming they qualify for the promotion.

The Resellers seek a credit of the entire amount (prior to application of the wholesale discount). ORS's position is that the waiver should be in the amount of a credit to zero out the amount previously charged to the Reseller. In this manner, the Reseller is not paid for the Line Connection Charge. Thus, ORS recommends that the Commission adopt AT&T's position on this issue.

Respectfully submitted,



Nanette S. Edwards

cc: Patrick W. Turner, Esquire
Henry Walker, Esquire
John J. Pringle, Jr., Esquire
Anton Christopher Malish, Esquire
Paul Francis Guarisco, Esquire

ATTACHMENT D

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NORTH CAROLINA
WESTERN (RALEIGH) DIVISION

Civil Action 5:10-cv-00466-BO

dPi TELECONNECT, L.L.C., Plaintiff, v. Chairman Edward S. Finley, Jr., Commissioner William T. Culpepper, III, Commissioner Lorinzo L. Joyner, Commissioner Bryan E. Beatty, Commissioner Susan W. Rabon, Commissioner ToNola D. Brown-Bland, and Commissioner Lucy T. Allen (in their official capacities as Commissioners of the North Carolina Utilities Commission); and BellSouth Telecommunications, Inc. d/b/a/ AT&T North Carolina Defendants.	)	**DEFENDANT COMMISSIONERS' RESPONSE BRIEF IN SUPPORT OF AN ORDER DENYING RELIEF SOUGHT BY PLAINTIFF AND AFFIRMING ORDERS OF THE NORTH CAROLINA UTILITIES COMMISSION**

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IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NORTH CAROLINA
WESTERN (RALEIGH) DIVISION

Civil Action 5:10-cv-00466-BO

dPi TELECONNECT, L.L.C., Plaintiff, v. Chairman Edward S. Finley, Jr., Commissioner William T. Culpepper, III, Commissioner Lorinzo L. Joyner, Commissioner Bryan E. Beatty, Commissioner Susan W. Rabon, Commissioner ToNola D. Brown-Bland, and Commissioner Lucy T. Allen (in their official capacities as Commissioners of the North Carolina Utilities Commission); and BellSouth Telecommunications, Inc. d/b/a/ AT&T North Carolina Defendants.	)	**DEFENDANT COMMISSIONERS' RESPONSE BRIEF IN SUPPORT OF AN ORDER DENYING RELIEF SOUGHT BY PLAINTIFF AND AFFIRMING ORDERS OF THE NORTH CAROLINA UTILITIES COMMISSION**

Defendants Edward S. Finley, Jr., in his capacity as Chairman of the North Carolina Utilities Commission, and William T. Culpepper, III, Lorinzo L. Joyner, Bryan E. Beatty, Susan W. Rabon, ToNola D. Brown-Bland, and Lucy T. Allen, in their official capacities as Commissioners of the North Carolina Utilities Commission (together, "the Defendant Commissioners"), by and through their undersigned counsel, file this responsive brief in support of an order that denies the relief sought by Plaintiff dPi Teleconnect, L.L.C. ("dPi") and affirms the orders of the North Carolina Utilities Commission ("NCUC" or "Commission").

SUMMARY OF THE NATURE OF THE CASE

This action for declaratory judgment is in the nature of an administrative appeal from orders of the NCUC in a complaint proceeding, and concerns how promotional credits should be calculated for "resale" services that defendant BellSouth Telecommunications, Inc., d/b/a AT&T North Carolina ("AT&T") sold to dPi pursuant to requirements of the Telecommunications Act of 1996 ("the Telecom Act" or "the Act."). *See* 47 U.S.C., §§ 251(c)(4); 252(d)(3). dPi filed a complaint with the NCUC seeking a determination that it is entitled to recovery of promotional credits from AT&T pursuant to the parties' interconnection agreements for the period beginning late 2003 through July 2007. (Doc 38-1) Following an evidentiary hearing and oral arguments, the NCUC issued a Recommended Order that allowed dPi's complaint and ordered AT&T to pay dPi's claims subject to validation of the amounts. *See Recommended Order* issued 7 May 2010 in *In the Matter of dPi Teleconnect, LLC v. BellSouth Telecommunications, Inc., d/b/a/ AT&T North Carolina*, Docket No. P-55, Sub 1744 (*"RO"*). (Doc 39-10) However, the NCUC did not find that the credits should be calculated using the method advocated by dPi. *RO* 6, 20-22. (Doc 39-10 pp 7, 21-23) Under dPi's method, the full value of promotional cashback offers (e.g. $100) would be credited to dPi, but the NCUC found that the promotional credits must reflect an adjustment of both the retail rate and the corresponding wholesale discount that applies for services sold to resellers. *Id.* The parties filed exceptions to the *RO* and, following oral arguments, the NCUC affirmed the decision in the *RO* in the *Order Denying Exceptions and Affirming the Recommended Order* issued 1 October 2010. (Doc 39-16) dPi filed this action seeking a declaration that the method of calculation adopted by the NCUC is not consistent with federal law and policies

under the Telecommunications Act, and that dPi's method must be used. (Doc 1)

The matter is now before this Court to address dPi's complaint for declaratory relief from the NCUC decision, and will be decided based on the record before the NCUC and the briefs filed by the parties with this Court. *See* Scheduling Order (Doc 37); Report of Rule 26(f) Conference and Joint Motion for Scheduling Order (Doc 36).

dPi's brief is denominated a "Motion for Summary Judgment/Brief on the Merits." (Doc 41) If the Court treats the briefs as motions and memoranda supporting summary judgment, then Defendant Commissioners ask that this Response be considered as the Defendant Commissioners' memorandum of law in support of their response to dPi and in support of a cross motion for summary judgment for defendant Commissioners.

dPi's brief makes two arguments: first, that the NCUC decided the method of calculation of promotional credits incorrectly under federal requirements; and second, that federal law requires AT&T to obtain pre-approval from the NCUC for promotions that are offered in excess of 90 days. The second argument raises an issue that is not presented in or pertinent to dPi's Complaint filed with this Court.

STATEMENT OF THE FACTS

Background about the Telecom Act is helpful to an understanding of the facts.

The Act restructured the local telecommunications industry in order to introduce competitive markets where previously the industry had consisted primarily of state-regulated monopolies. The Act regulates incumbent (i.e., historical) local exchange companies ("incumbent LECs") and competing local exchange companies ("CLECs") to facilitate competition and reduce monopoly control of local markets. *See DPI Teleconnect LLC v.*

Owens, 2011 U.S. App. LEXIS 2233 at *2 (4th Cir. 2011) (citations omitted)(unpublished).

To that end, the Act imposes a number of duties on incumbent LECs, including in pertinent part, the duty to offer telecommunications services to resellers (e.g., CLECs) for resale by CLECs to end users. 47 U.S.C. § 251(c)(4) (Each incumbent LEC has the duty "to offer for resale at wholesale rates any telecommunications service that the carrier provides at retail to subscribers who are not telecommunications carriers."). Resale services must be sold at wholesale prices established by state commissions based on the retail rate less avoided costs. 47 U.S.C. § 252(d)(3). The duty to sell services to resellers at wholesale prices applies to promotional offerings of telecommunications services as well as to standard tariff offerings, except if the promotion is provided short term (i.e., rates that are in effect for no more than 90 days and that are not used to evade the wholesale rate obligation). 47 C.F.R. § 51.613(a)(2); *See BellSouth Telecommunications, Inc. v. Sanford*, 494 F.3d 439 (4th Cir. 2007)("*Sanford*"). The NCUC has concluded, in decisions affirmed by the Fourth Circuit Court of Appeals in *Sanford*, that promotional offerings that exceed 90 days "have the effect of changing the actual retail rate to which a wholesale requirement or discount must be applied." *Sanford*, 494 F.3d at 442 (*affirming "Restriction on Resale Order I"* issued December 22, 2004 and *"Restriction on Resale Order II"* issued June 3, 2005, in Docket No. P-100, Sub 72(b)). Thus, the

> "benefit of a ... promotion offered for more than 90 days must be made available to resellers such that resellers are permitted to purchase the regulated service(s) associated with the promotion at the promotional rate minus the wholesale discount, unless the [incumbent LEC] proves to the Commission (per 47 C.F.R. [§] 51.613(b)) that not applying the wholesale discount to the promotional offering is a reasonable and nondiscriminatory restriction on the [incumbent LEC's] resale obligation."

RO 10 (quoting *Restriction on Resale Order I)*. (Doc 39-10 p 11)

The complaint to the NCUC involved a dispute about the wholesale price applicable to purchases made by reseller dPi from incumbent LEC AT&T[1] during the period beginning in late 2003 through July 2007. AT&T offered three cashback promotions to its retail customers that were not made available for resale. Under the promotions, end users who agreed to subscribe to a particular service or bundle of services for a particular period of time were offered coupons that could be applied for and redeemed for cash. *RO* 4. (Doc 39-10 p 5)

Promotion #1, referred to as the "$100 Cashback for IFR + 2 Custom Calling or TouchStar Features" promotion, was available for new residential local service subscribers who purchased at least two qualifying features in addition to basic residential service from August 25, 2003 to January 31, 2005. *RO* 6 (Doc 39-10 p 7) AT&T mailed a $100 Cashback coupon to qualified users and the coupon could be redeemed within 90 days for a $100 check. *Id.* Promotion #2, referred to as the "$100 Cashback for Complete Choice, Area Plus with Complete Choice and Preferred Pack" promotion, was available for returning AT&T local service users who purchased one of the qualifying plans from June 1, 2003 through the rest of the period addressed in the complaint. *Id.* AT&T mailed a $100 Cashback coupon to qualified users and the completed coupon could be redeemed for a $100 check by mailing the coupon along with the first month's bill showing the purchase of eligible services. *Id.* Promotion #3, referred to as the "$50 Cashback 2-Pack Bundle Plan" promotion, was available for reacquisition end users from December 15, 2005 to April 30, 2007. From May 1, 2007 through the rest of the period addressed in the complaint the Cashback reward was reduced to

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[1] AT&T, Inc. and BellSouth Corporation merged effective December 29, 2006 and for purposes of this matter are referred to together as AT&T.

$25. AT&T mailed a Cashback coupon to qualifying users that could be redeemed for a check. *RO* 7. (Doc 39-10 p 6)

AT&T adopted the official position that these cashback promotions were not available for resale. *RO* 4, 7. (Doc 39-10 pp 5,8) However, in July 2007 AT&T changed its position following the *Sanford* decision, 484 F.3d 439, and began making cashback promotions available for resale prospectively. *RO* 4-5. (Doc 39-10 pp 5-6) Despite the change in position, AT&T continued to deny claims made by dPi for credits related to promotions that had occurred from 2003 through 2007. *Id.*

The NCUC heard dPi's complaint seeking credits for the cashback promotions offered during 2003-2007, and found that dPi had complied with the applicable terms of its interconnection agreements with AT&T. *RO* 6 (Doc 39-10 p 7) Further, the NCUC found that AT&T failed to show that the refusal to allow resale of the promotions was reasonable and nondiscriminatory or that the credits should be barred on other grounds. *Id.* Therefore the NCUC determined that dPi is entitled to receive credits relating to the promotions. *Id.*

AT&T has not challenged the NCUC's decision, and there is not a dispute before this Court that dPi should receive credits relating to the promotions from 2003 through mid 2007. Rather, the dispute concerns how the credits should be calculated. (Doc 1 p 6)

The method advocated by dPi would credit the full face value of the promotional offering. (Doc 1 p 5) Hence, dPi would credit $100 or $50 or $25 depending on the promotion that the credit relates to. AT&T proposed a method that would calculate the credit based on the value of the promotional offering reduced by the wholesale discount. *RO* 20 (Doc 39-10 p 21) Hence, under AT&T's method, dPi would be credited based on the face value of

the promotion ($100 or $50 or $25) reduced by the 21.5% wholesale discount. Based on the evidence, the NCUC adopted AT&T's method, finding "AT&T should calculate the value of the promotional discount by deducting the wholesale discount from the retail value of the promotion." *RO* 6, 20-22. (Doc 39-10 pp 7, 21-23)

Other facts in the case are provided in conjunction with arguments that follow.

ARGUMENT

I. THE DETERMINATION OF HOW A CREDIT TO DPI SHOULD BE CALCULATED WAS PRIMARILY A FACTUAL MATTER TO WHICH THE COURT APPLIES A SUBSTANTIAL EVIDENCE STANDARD OF REVIEW; AND AS TO LEGAL CONCERNS, THE STANDARD OF REVIEW IS *DE NOVO* BUT THE NCUC DECISION SHOULD BE ACCORDED RESPECT GIVEN THE CARE AND EXPERTISE EXERCISED IN THE MATTER.

The determination that dPi challenges in this case – the correct way to calculate the amount of promotional credits – is predominantly a factual issue. DPi paid too much for telecommunications services during the period 2003-2007 because the value of cashback promotions was not reflected in the wholesale prices that dPi paid. The issue is whether the method that was approved by the NCUC for calculating promotional credits in order to correct the amounts dPi overpaid was - or was not - appropriate. As to findings of fact, the "substantial evidence" standard is applied. *See GTE South v. Morrison*, 199 F.3d 733, 745 n.5 (4th Cir. 1999) (holding 'substantial evidence' is the appropriate standard, but noting that "some other courts" have applied the 'arbitrary and capricious' standard, and observing that "[w]ith respect to review of factfindings, there is no meaningful difference"). On review of a state commission determination under the Act, the court does not "sit as a super public utilities commission," *id* at 745, and is "not free to substitute its judgment for the agency's." *Id* at

746. Instead, the court "must uphold a decision that has substantial support in the record as a whole even if [the court] might have decided differently as an original matter." *Id* at 746; *see also DPI Teleconnect v. Owens*, 2011 U.S. App. LEXIS at *8.

dPi makes legal or policy arguments for using dPi's preferred method to determine the credits. As to questions of law that are raised by dPi's claims, the review is *de novo*. However, NCUC decisions are accorded respect and consideration and should not be taken lightly even under *de novo* review given the NCUC's longtime experience and the important role that state commissions play under the regulatory scheme established in the Telecommunications Act. *Sanford*, 494 F.3d at 447-48 (citing *United States v. Mead Corp.*, 533 U.S. 218, 226-27 (2001) and *Skidmore v. Swift* & Co., 323 U.S. 134, 139-40 (1944)). While the decision in *Sanford* confirmed that state commission orders construing the Act fall outside "*Chevron*'s domain and its mandate of deference to reasonable interpretations of ambiguous statutes," 494 F.3d at 447, it found nonetheless that state commissions may deserve "the respect that flows from the longstanding principle that 'the well-reasoned views of the agencies implementing a statute' constitute a body of experience and informed judgment to which courts and litigants may properly resort for guidance.'" 494 F.3d at 448 (quoting *Skidmore*, 323 U.S. at 139-40). In particular cases, the court found that the "amount of respect afforded to a state commission will vary in accordance with 'the degree of the agency's care, its consistency, formality, and relative expertness,' as well as 'the persuasiveness of the agency's position.'" *Sanford*, 494 F.3d at 448 (quoting *Mead*, 533 U.S. at 228).

Here, the NCUC proceedings involved initial pleadings, discovery, pre-filed testimony, evidentiary hearings, and the submission of written briefs and proposed orders.(Doc 38-5)

Following the issuance of the *Recommended Arbitration Order*, parties filed exceptions and participated in oral argument, and the full Commission reviewed the case. The final order denied exceptions and affirmed the *RO*, providing additional explanation for the decision. (Doc 39-16) The Commission's orders provide extensive consideration of the issues raised by the parties and the reasoning for the determinations made. (Docs 39-10, 39-16)) These factors support a high level of respect for the NCUC decision in this case as to matters of law.

II. THE NCUC CORRECTLY DETERMINED THE METHOD FOR CALCULATING THE PROMOTIONAL CREDITS.

The NCUC accurately decided how promotional credits should be calculated in order to correct the amount that dPi paid for services from 2003-2007 to reflect the effect of the cashback promotions on the wholesale price. The method adopted by the NCUC was supported by on substantial evidence and used the same method for calculating the wholesale price for a promotional telecommunications service as was used in a hypothetical described in the *Sanford* decision. The method advocated by dPi, on the other hand, is not mathematically accurate - i.e., not an accurate way to calculate the promotional rate or the credit in order to correct the amount overpaid. The legal arguments posited by dPi are not well founded and do not support the use of an incorrect calculation method.

As computed by the NCUC, the promotional credits reflect the difference between what dPi originally paid for services during 2003-2007– *i.e., the standard retail rate less the wholesale discount* – and what dPi would have paid taking into account the cashback promotions - i.e., *the promotional retail rate less the wholesale discount.* The promotional rate is the standard retail rate adjusted for the cashback amount. The NCUC's method of

calculating the credits correctly makes adjustments to all components of the formula relating to the change in the retail rate, whereas the approach that dPi advocates would adjust the retail rate to reflect the value of the cashback promotion, but would not make any corresponding adjustment to the amount of the wholesale discount. Thus, the dPi approach is simply incorrect mathematically. In fact, as will be shown below, dPi's discussion about how the credits should be calculated ignores the formula that is inherent in the FCC regulation, disregards the evidence of how the formula applies shown during cross examination of dPi's witness, and conflicts with the statements provided in prepared testimony presented by dPi's own witness.

A. Federal and State Provisions Establish the Formula for Determining the Wholesale Price Available to Resellers

The formula used by the NCUC to determine the wholesale price applicable to resellers is based on federal requirements. Under the Telecommunications Act, incumbent LECs are obliged to offer telecommunications services for resale to competing providers, 47 U.S.C. § 251(c)(4), and the wholesale price for services sold to resellers is a matter that is determined by a State commission "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." 47 U.S.C. § 252(d)(3). The *wholesale price* that an incumbent LEC may charge for a particular telecommunications service provided for resale must equal the retail rate for that service less "avoided retail costs." 47 C.F.R. § 51.607. Pursuant to 47 C.F.R. § 51.609, the amount of the avoided retail costs shall be determined by State commissions on the basis of a

cost study that meets particular requirements. 47 C.F.R. § 51.609(a); *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996,* 11 F.C.C.R. 15499 (*"Local Competition Order"*) ¶ 909. The criteria in the regulation are designed to apply consistent interpretations of the Act in setting wholesale rates based on avoided cost studies in order to facilitate swift entry by resellers. *Id.* Nonetheless, the criteria "are intended to leave the state commissions broad latitude in selecting costing methodologies that comport with their own ratemaking practices for retail services." *Id.* The FCC specifically recognizes that state commissions may use a single uniform discount rate for determining wholesale prices. *Local Competition Order* ¶ 916; In other words, the FCC regulations recognize and anticipate that an evaluation of particular avoided costs for each service would be cumbersome and instead allow the application of a uniform percentage discount. *Id.* The FCC recognized that the adoption of a uniform rate "is simple to apply, and avoids the need to allocate costs among services." *Id.*

The discount rate for AT&T (i.e., the "BellSouth") was determined by the NCUC in the *Recommended Arbitration Order* issued 23 December 1996 in *In the matter of Petition of AT&T Communications of the Southern States, Inc. For Arbitration of Interconnection with BellSouth Telecommunications, Inc.,* Docket No. P-140, Sub 50.(*"AT&T RAO 1996"*)[2] The NCUC adopted a wholesale discount rate of 21.5% for residential services and 17.6% for business services. *Id* p 43. The parties have not challenged the accuracy of the percentage or supplied new cost studies for the purpose of establishing additional classes of service to which

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[2] dPi agrees that the discount percentage was established in the *AT&T RAO 1996. See dPi's Reply to Staff's Proposed Findings and Conclusions.* (Doc 39-7 p 7, note 2)

a different discount rate should apply.

B. Examples Illustrate How the Wholesale Price Is Calculated and Demonstrate that the NCUC Ordered the Accurate Method to Calculate Corrections to the Wholesale Price Charged from 2003-2007.

The wholesale price for a particular service is equal to the retail rate for the service reduced by the wholesale discount. 47 C.F.R. § 51.607(a); *Local Competition Order* ¶ 916. For example, if the retail rate for a residential service is $75, the corresponding 21.5% wholesale discount is $16.12 and the wholesale price is equal to $58.88:

Example 1: $75 - 21.5% of $75 = $58.88

Since the wholesale discount amount is equal to a percentage of the retail rate, a larger retail rate corresponds to a larger discount amount. For example, if the retail rate is reduced by $25 from $75 to $50, then the corresponding wholesale discount is reduced from $16.12 to $10.75 and the reduced wholesale price is equal to $39.25:

Example 2: $50 - 21.5% of $50 = $39.25

Reviewing the math, when the retail rate was reduced by $25 in Example 2, the reduction in the retail rate prompted a corresponding reduction in the amount of the wholesale discount.

Example 1: Wholesale discount for $75 = $16.12

Example 2: Wholesale discount for $50 = $10.75

The difference between the wholesale price for a retail service offered at $75 (Example 1) and a retail service offered at $50 (Example 2) equals $19.63:

$58.88 - $39.25 = $19.63

Another way that the difference in the wholesale price can be measured is by applying

the discount to the amount of the reduction:

$75-$50 = $25 - 21.5% of $25 = $19.63

During cross examination of dPi's CEO Tom O'Roark (who adopted pre-filed testimony of Mr. Brian Bolinger), AT&T questioned the witness about the way the wholesale price would be calculated using similar examples illustrated in O'Roark Cross-Examination Exhibit No. 4, and Mr. O'Roark agreed with the math. (Doc 39-1 pp 87-90) Pages from testimony relating to these calculations are attached in Commissioner's Response Exhibit A and the cross examination exhibit is attached in Commissioner's Response Exhibit B.

When the NCUC considered the issue about what method is appropriate for calculating the impact of cashback promotions on the wholesale price that dPi should have paid between 2003 through 2007, dPi had already paid for the services.(Doc 39-1 pp 50-51) The wholesale price dPi had paid was based on AT&T's *standard* retail rate unadjusted for the reductions caused by the cash-back promotions. *Id.* Therefore the NCUC calculated what *correction* should be made to credit dPi for the difference between the wholesale price applicable to the standard retail rate and the wholesale price applicable to the promotional retail rate. It found that what is required is "that the price lowering impact of any such 90-day-plus promotions on the real tariff or retail list price be determined and that the benefit of such a reduction be passed on to resellers by applying the wholesale discount to the lower actual retail price." *RO* p 21 (Doc 39-10 p 22)(quoting *Restriction on Resale Order II* p 6)

AT&T argued that the proper method to correct the amount paid during 2003-2007 would be to credit dPi for the promotional amount less the amount of the corresponding correction to the wholesale discount. *RO* 20 (Doc 29-10 p 21) So, for a promotion offering

$25 cash back, AT&T argued dPi should be given a promotional credit of $25 - 21.5% of $25 = $19.63. (Doc 39-1 p 90) AT&T's method correctly reflects the fact, demonstrated in Examples 1 and 2 above, that when the retail rate is reduced, there is a corresponding reduction in the amount of the wholesale discount. Therefore, a correction to the amount paid by a reseller must reflect both the change in the retail rate and the corresponding change to the discount amount.

dPi argued that the proper method to correct the amount it paid during 2003-2007 would be to credit dPi for the *full amount* of the cash back dollars offered in promotions. *RO* 21 (Doc 39-10 p 22) So for a promotion offering $25 cash back, dPi argued it should be given a promotional credit of $25.

dPi's method of calculating the amount of the correction was not consistent with some of dPi's own testimony, however. dPi's witness argued in his pre-filed testimony that, "the practical effect of these promotions is to reduce the effective retail rate qualifying customers pay for telephone service." (Doc 39-1 p 51) dPi discussed AT&T's failure to make the promotional rate available to dPi and described the way the wholesale price should have been determined:

> This dispute arises because BellSouth has over the past months and years sold its retail services at a discount to its end users under various promotions that have lasted for more than 90 days. DPi Teleconnect is entitled to purchase and resell those same services *at the promotional rate, less the wholesale discount.*

(Doc 39-1 p 50) Thus dPi's witness conceded that the wholesale discount applies to the *promotional rate*, a position that is not consistent with the position taken later in arguments that the wholesale discount applies to the standard rate, and then the full value of the

promotion is subtracted. *See* dPi's Brief 14 (Doc 41 p 16) and *compare* (Doc 39-1 p 50).

Furthermore, other testimony presented by dPi indicates that dPi's witness was not strongly wedded to the "full value" approach now advocated by dPi. In pre-filed rebuttal testimony dPi's witness was asked, "What about BellSouth's contention that some of the cashback amounts requested by dPi are too high?" He answered,

> There may be some merit in this concern. This has to do with when the retail price is calculated, and ... when the corresponding wholesale discount is applied. *Thus, if the discount is applied before the promotion is taken, the promotion should also be discounted.* The converse is also true. The parties should be able to reach agreement on the true numbers at issue.

(Doc 39-1 p 56) (Emphasis added.)

Although the NCUC agreed with dPi's witness that the promotional rate should have been used to determine the wholesale price, and required AT&T to credit dPi for the corrected amount, the NCUC agreed with AT&T about how the promotional credits should be calculated in order to make the correction.

Therefore, the NCUC directed AT&T to "calculate the value of the promotional discount by deducting the wholesale discount from the retail value of the promotion." *RO* 6 (Doc 39-10 p 7) In other words, the calculation should factor in the effect of the retail rate reduction on the discount.

The NCUC explained its reasoning first by summarizing the examples used in cross examination of Mr. O'Roark and in O'Roark Cross-Examination Exhibit No. 4. *RO* 20 (Doc 39-10 p 21) The NCUC observed that, if the amount of the promotional offering were not reduced by the wholesale discount, then dPi "would receive a greater benefit than it otherwise would be entitled to receive had AT&T merely reduced the telecommunications service's

rate." *RO* 21 (Doc 39-10 p 22) Without an adjustment to the discount amount, the promotional credit would not correct for the difference between what dPi paid as a wholesale price during the 2003-2007 period – based on the *standard rate less the wholesale discount* and what dPi should have paid – based on the *promotional rate less the wholesale discount.*

In sum, the testimony presented to the NCUC provided substantial evidence in support of the method that the NCUC adopted for purposes of calculating promotional credits to correct the overpayments that occurred from 2003-2007.

C. The Method that the NCUC Directed Parties to Use to Calculate Promotional Credits Mirrors the Method Described in *Sanford* by the Fourth Circuit

There is a hypothetical described in the *Sanford* decision that illustrates the impact of a promotion on the retail rate and wholesale price, and the hypothetical applies the same calculation method that was adopted by the NCUC in this case. 494 F.3d at 450-51. The hypothetical was discussed during cross examination of dPi's witness. (Doc 39-1 pp 93-97)

In the hypothetical developed by the Court, the standard rate for telephone service is $120/month, but the customer is sent a monthly rebate check for $100/month. 494 F.3d at 450-51. The Court found that the NCUC was correct in finding that the rebate check must be considered in determining the wholesale price. *Id.* Therefore, the Court observed that, under the NCUC's determination, the appropriate wholesale rate would be "$16, because that is the *net* price paid by the retail customer ($20), less the wholesale discount (20%)" *Id.* (The 20% discount was hypothetical). The formula developed by the Court applied the discount to the *promotional rate* (the method advocated by AT&T in this case and adopted by the NCUC). It did not subtract the *full value* of the $100 rebate check and apply the discount only to the

standard rate (as dPi's method would do). If the Court had applied dPi's method in the hypothetical in *Sanford*, then instead of $16, the wholesale price would have been negative $4. I.e., the standard rate ($120), less the wholesale discount (20% of $120 or $24), less the full $100 rebate:

$120 (the standard rate) - 20% of $120 - $100 = -$4

AT&T questioned Mr. O'Roark about what would be done to correct an overcharge using the hypothetical from *Sanford.*(Doc 39-1 pp 93-94) Through the questioning, AT&T showed that, if the reseller had originally paid a wholesale price of $96 based on the standard $120/month rate ($120 less 20% of $120), then the correction for the promotion would be calculated by applying the discount (20%) to the $100 rebate amount and the reseller would be due a credit of $80. Thus the original $96 rate corrected by the $80 credit would come back to the appropriate retail rate of $16. (Doc 39-1 pp 93-94)

Thus, as was shown in evidence presented to the NCUC, the method of calculating the promotional credits advocated by AT&T is consistent with the method approved in *Sanford.* 494 F.3d at 450-51.

D. Contrary to dPi's argument, Federal Provisions Allow Temporary Retail Price Reductions That Drop Below Wholesale Prices and Do Not Require Revisions to the Wholesale Discount in Order to Ensure that Wholesale Prices Are Always Lower than Retail Prices.

dPi argues that its method for calculating promotional credits must be used in order to ensure that wholesale prices are *always* lower than retail prices. *See* dPi's Brief p 9 ("the Commission's decision ... adopts a methodology which violates the key principle that wholesale should be less than retail.") dPi's argument is flawed for several reasons.

First, although retail rates are reduced by avoided costs to determine wholesale rates, what constitutes the "retail rate" is not specifically defined and the FCC has not found that retail prices must at all times be lower than wholesale prices. *Local Competition Order* ¶949. FCC regulations allow incumbent LECs to offer short term (i.e., up to 90 day) promotions that result in temporary price reductions without making such promotions available for resale. *See* 47 C.F.R. § 51.613(a)(2);*Local Competition Order* ¶949. The effect of such short term promotions is not considered in the retail rate of the underlying services when the discounted wholesale price is determined. *Id.*[3] As a result, the price that retail customers pay may temporarily fall below the wholesale price. The FCC found that when promotions are limited in length they may serve pro-competitive ends. *Local Competition Order* ¶949. Hence, dPi's contention that wholesale prices are *always* lower than retail prices is an overstatement. The price may vary temporarily, and the effect on the rate is not necessarily limited to the single month.

In this case, dPi's complaint that the wholesale price is temporarily higher than the retail price is based on the fact that the promotional credit relates to a lump sum amount that shows up in a single month, but the effect on rates is not felt in a single month. In fact, the cashback offer is not paid until a cashback coupon is mailed out to retail customers and returned by them. *RO* 6 (Doc 39-10 p 7) The record does not indicate how much time passes during which retail customers pay the standard rate before they receive the cashback amount. Similarly, the promotional credits to dPi do not match up with a particular month of wholesale

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[3] In this case, the promotions do not qualify as "short term" because they are available as offers for longer than 90 days, thereby affecting the retail rate. *Id; Sanford*, 494 F.3d 439.

service. In fact, the credits are corrections to the wholesale price for services that AT&T sold to dPi between 2003 and 2007. Thus, although the corrections are reflected as promotional credits that apply in one month, the corrections relate to services that dPi purchased for resale at least four years ago. Accordingly, the argument is not compelling that the difference between the retail price and wholesale price in a particular month is problematic and the problem would be corrected if dPi's calculation method were used instead of the method adopted by the Commission.

Moreover, dPi uses an illustration in Table 4 of its Brief based on hypothetical rates and a hypothetical discount percentage that may exaggerate the effect of promotions on net retail prices and corresponding wholesale prices. dPi Brief p 7. The Table compares results of applying the NCUC's adopted approach versus dPi's full value approach to measure the retail versus wholesale prices under several scenarios.[4] The hypothetical assumes a discount rate of 20%, whereas the rate is 21.5% in North Carolina. *Id.* Further, the "standard retail price" in the Table is assumed to be $25 for all cases while the cashback promotion amount changes in the cases from zero, to $25, to $50, and to $100. *Id.* dPi's assumption that the standard retail price stays $25 in all cases is not supported by evidence of the actual price, and does not take into account the fact that the $100 cashback promotions were offered in connection with services that have enhanced features or expanded calling areas that would tend

[4] The table reflects the approved method and dPi's "full value" approach for calculating the wholesale price change. It also reflects a third method discussed by dPi that calculates the wholesale price using an "absolute value" formula. The third method ignores that the promotional credit is a *correction* to amounts previously overpaid by dPi, and accordingly the reduction to retail rate corresponds to a reduction in the amount of the discount. The "absolute value" approach appears to add to, rather than correct, the impact of the rate change on the discount.

to increase the standard retail price. The amount of the cashback offer compared to the standard retail rate makes a difference in the results shown. The results depicted in dPi's Table are exaggerated because of the assumptions that were used in the illustration.

For these reasons, dPi's argument that the full value method must be used to calculate promotional credits in order to keep wholesale prices less than net retail prices in a particular month is flawed. The argument does not justify the use of a calculation method that would compute credits that over-correct for past overpayments.

E. Contrary to dPi's Argument, Federal Requirements Do Not Allow Changes to the Discount Percentage For Cashback Promotions.

dPi appears to argue that the wholesale discount ought not be applied to the cashback amount in calculating the promotional credits dPi is owed because the avoided costs of providing particular services to resellers do not change when offered at promotional rates. However, the formula for determining wholesale prices applies a percentage discount to the retail rate for any service in order to set the wholesale price. 47 C.F.R. §§ 51.607, 51.609; *Local Competition Order* ¶¶ 909, 916; ***AT&T RAO 1996*** **p 43. Accordingly, the amount of the retail rate affects the calculation of amount of the discount. If an adjustment is not made to the amount of the wholesale discount for a change in the retail rate, then under the mathematical formula, there is a change in the percentage that has been discounted. Without performing a cost study, it is not appropriate for the NCUC to abandon the 21.5% percentage discount established for AT&T. 47 C.F.R. §§ 51.609(a).**

It is unlikely that dPi would obtain an advantage if the NCUC were to engage in a recalculation of the percentage rate for particular promotions or for other types of new

services as they are offered. Although the percentage approach that applies uniformly to residential services is not an exact measure of avoided costs, it would be administratively impractical to identify such costs on a case by case basis.

In this case, there is no evidence to support dPi's contention that a change in the effective retail rate effected by cashback promotions did not have an impact on the amount of avoided costs that would be calculated if a cost study were performed. dPi's position that the formula should be altered in this case would result in a change in the percentage discount without analysis, contrary to federal regulatory requirements.

The NCUC accurately decided that the cash back promotion modifies the retail rate, and, under the wholesale pricing formula, the change in the retail rate prompts a corresponding change in the amount of the discount. As discussed earlier, dPi's witness conceded this point when he explained that "DPi Teleconnect is entitled to purchase and resell [the] same services *at the promotional rate, less the wholesale discount.*" (Doc 39-1 p 50)

F. Contrary to dPi's Argument, Promotional Credits Are Corrections to Amounts Paid by dPi in Prior Periods, and the Corrections Must Reverse the Original Discount Amount to the Extent it Was Based on an Overstated Retail Rate.

Another argument dPi makes for using dPi's method to calculate the promotional credits is that the statute requires that the avoided cost (i.e., the discount percentage) be <u>subtracted</u> from the retail price in order to compute the wholesale price. Apparently, dPi finds it hard to reconcile this principle with the calculation method adopted by the NCUC. However, dPi's argument fails to recognize that the purpose of the promotional credits is to make corrections to the wholesale prices that were charged from 2003 through 2007. The

original retail rates were overstated since they did not reflect the value of the cashback promotions, *and* the corresponding discount amounts were overstated since the discounts were based on the standard retail rates. The corrections adjust the retail rates *and* the discounts for the value of the promotions. As was demonstrated earlier in Examples 1 and 2, a reduction to the retail rate prompts a corresponding reduction in the amount of the wholesale discount. Therefore, the correction in the discount offsets the reduction in the retail rate somewhat when the promotional credit is calculated.

dPi also appears to argue that the full value of the cashback offers should be credited (e.g., the full $100 amount) so that the same terms and conditions offered to retail customers are offered to resellers. As the NCUC stated in the *RO* and in previous determinations, the obligation relating to promotional offers is to provide the *benefit* of the promotional offer through the wholesale price charged the reseller, not to provide the promotional item (such as a gift or cash) itself. *RO* 21 (Doc 39-10 p 22) The face value of the promotion is not required to be passed through to a reseller. Instead, "the price lowering impact of any such 90-day-plus promotions on the real tariff or retail list price [must] be determined and ... the benefit of such a reduction [must] be passed on to resellers by applying the wholesale discount to the lower actual retail price." *RO* 21 (Doc 39-10 p 22), *quoting Restriction on Resale Order II*, issued 3 June 2005 in Docket No. P-100, Sub 72(b), *affirmed* in *Sanford*, 494 F.3d 439) The formula approved by the NCUC for determining promotional credits accomplishes the purpose of correcting the wholesale price that dPi paid from 2003 through 2007 to reflect the price lowering impact of the cashback promotions on the standard retail rate.

III. DPI'S ARGUMENT CONCERNING PREAPPROVAL SHOULD NOT BE REVIEWED BECAUSE IT WAS NOT RAISED IN THE PLEADINGS AND IS NOT PERTINENT TO THE DETERMINATION OF THE ISSUE THAT *WAS* RAISED, DPI IS NOT AGGRIEVED BY THE NCUC'S STATEMENT CONCERNING PREAPPROVAL, AND, IF REVIEWED, THE NCUC'S STATEMENT DESCRIBED A PRACTICE THAT IS NOT CONTRARY TO FEDERAL LAW.

Next, dPi argues that AT&T must obtain preapproval from the NCUC in order to impose restrictions on resale of promotions that are offered in excess of 90 days, and the NCUC incorrectly stated that preapproval is not required. dPi does not specify what relief is sought from the NCUC's statement but apparently seeks a declaratory judgment that preapproval is required. This argument does not concern a factual or legal matter that is raised in the complaint dPi filed in this Court, (Doc 1) and indeed, although the NCUC commented on the issue in the *RO*, *RO* 10-11 (Doc 39-10 pp 11-12), dPi's complaint to the NCUC did not raise the issue for consideration either. (Doc 39-1) The NCUC's statement about the lack of a preapproval requirement did not affect the outcome of dPi's complaint, obviously, because the NCUC resolved that dPi is entitled to promotional credits. Thus, dPi is not aggrieved by the statement since it had no effect on the outcome. *See* 47 U.S.C. § 252(e(6); Complaint (Doc 1 p 2). Again, here, the resolution of the preapproval issue is not pertinent to the issue that is raised for determination by this Court, i.e., whether the method adopted for calculating promotional credits for telecommunications services purchased from 2003 to 2007 is proper. The discussion about preapproval does not concern a matter in dispute and Defendant Commissioners ask the Court to decline to issue a declaratory judgment addressing the matter.

If the Court determines that a ruling on the pre-approval question is appropriate, then Commissioners submit the following arguments in support of the NCUC's statement that pre-approval is not required.

dPi's argument about preapproval asserts that, when an incumbent LEC offers a promotion for more than 90 days and does not make the benefit of the promotional offering available for resale, there is a presumption that the restriction on resale is unreasonable and discriminatory and therefore that pre-approval from the NCUC is required before the promotion is offered. The NCUC has found that the benefit of a promotion offered for more than 90 days must be made available to resellers such that resellers are permitted to purchase the telecommunications services at the promotional rate minus the wholesale discount, "unless the [incumbent] LEC proves to the Commission [per 47 C.F.R. 51.613(b)] that not applying the wholesale discount to the promotional offering is a reasonable and nondiscriminatory restriction on the [incumbent] LEC's resale obligation." *RO* 10 (*quoting Restriction on Resale Order I, aff'd, Restriction on Resale Order II* , *aff'd Sanford*, 494 F.3d 439). (Doc 39-10 p 11) However, in reaching this decision, the NCUC has refused to establish a bright line rule that promotions exceeding 90 days must be offered to resellers, and instead has adopted a case by case approach allowing incumbent LECs to prove that a 90+ day promotion is reasonable and nondiscriminatory and thus not harmful to competition, though not offered for resale. *Id.*

In this case, the NCUC disagreed with dPi's contention that FCC regulations require an incumbent LEC to obtain pre-approval of promotions containing restrictions on resale that are intended to last more than 90 days, before implementing such restrictions. *Id.* The NCUC found that such a requirement "would unnecessarily burden the Commission's resources

because it would have to convene a proceeding to address *all* such offerings instead of only addressing those to which affected parties actually object." *Id.* dPi doubts that the NCUC would be burdened by a pre-approval requirement, but the NCUC is better situated than dPi or this Court to evaluate the potentially burdensome effect of a pre-approval requirement.

The NCUC's position on preapproval is consistent with federal law. The FCC does not specify that pre-approval is required. Indeed, the FCC has observed that it is not necessarily possible to predict the potential that resale provisions will unreasonably restrict or limit resale. The FCC observed, "we, as well as state commissions, are unable to predict every potential restriction or limitation on resale." *Local Competition Order* ¶ 939. As is alluded to in the FCC's comment, the NCUC may not foresee the problematic nature of a restriction or limitation on resale in a pre-approval process.

Furthermore, the NCUC has expressed concern that a preapproval requirement would have a chilling effect on competitive offerings because incumbent LECs would be reluctant to provide their wireline, wireless, cable, and VoIP competitors such advanced notice of upcoming offerings. *RO* 10 (Doc 39-10 p 11)

In sum, dPi's arguments concerning the need for a preapproval process are not pertinent to the matter raised in dPi's complaint, and the arguments lack merit.

CONCLUSION

For the foregoing reasons, Defendant Commissioners ask the Court to deny the relief sought by Plaintiff dPi and to affirm the orders of the North Carolina Utilities Commission.

Respectfully submitted, this the 21st day of April, 2011.

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Attorney General

/s/ Margaret A. Force
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CERTIFICATE OF SERVICE

I hereby certify that on this day, the 21st day of April, 2011, I electronically filed the foregoing with the Clerk of the Court using the CM/ECF system which will send notification of such filing to the following counsel: David S. Wisz, Dennis G. Friedman, Jeffrey M. Strauss, Mary Kathryn Mandeville, Patrick W. Turner and I hereby certify that I have mailed the document to the following non CM/ECF participants: none.

Respectfully submitted,

/s/ Margaret A. Force
Assistant Attorney General

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COMMISSIONER'S RESPONSE EXHIBIT A

OFFICIAL COPY

1 PLACE: Dobbs Building, Raleigh, North Carolina

2 DATE: Thursday, November 12, 2009

3 DOCKET NO.: P-55, Sub 1744

4 TIME IN SESSION: 10:03 A.M. - 4:37 P.M.

5 BEFORE: Commissioner William T. Culpepper, III, Presiding
Chairman Edward S. Finley, Jr.
6 Commissioner Bryan E. Beatty

7

8 IN THE MATTER OF:

9 BellSouth Telecommunications, Inc.: Complaint of dPi
Telecommect, LLC

10

11

12 A P P E A R A N C E S:

13 FOR AT&T NORTH CAROLINA:

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1 AT&T was not providing cash back credits to dPi, the
2 number of customers in North Carolina increased from 2,896
3 to 5,139, right?
4 A. Right.
5 Q. And from the time that AT&T began giving these
6 credit requests to dPi in North Carolina, your number of
7 customers in North Carolina dropped from 5,139 to 3,966 in
8 June of 2009, correct?
9 A. Correct.
10 Q. Now, let's talk about the amounts that dPi is
11 seeking in this docket. I want you to assume that AT&T's
12 promotion provided its retail customer a coupon that could
13 be redeemed for a $50 cash back check, okay?
14 A. Okay.
15 Q. If that is the request at issue in this docket, is
16 dPi asking the Commission to order BellSouth or AT&T to
17 pay $50 in credits or $50 less the promotional discount
18 and credits?
19 A. I believe that we've asked for $50, right?
20 Q. I'm asking you, sir.
21 A. I'd have to go back and revisit the calculation,
22 but I believe it's based on $50.
23 MR. TURNER: Mr. Chairman, I have a four-page
24 exhibit that I'd like to walk through in hypothetical form

1 with the witness. And I'd like that -- to ask that it be
2 marked as O'Roark Cross-Examination Exhibit No. 4.
3 COMMISSIONER CULPEPPER: All right. Let the
4 document be so identified.
5 (Whereupon, O'Roark Cross-Examination Exhibit
6 No. 4 was marked for identification.)
7 Would you tell us again what this document is?
8 MR. TURNER: Yes, sir. The first page is titled
9 "Telecommunications Service A Retail Price of $75."
10 Mr. Chairman, what I intend to do is walk through the
11 document and compare a price reduction to a cash back and
12 see the dollar amounts that would be at issue there.
13 COMMISSIONER CULPEPPER: All right. Well, let's
14 let the exhibit be identified as O'Roark Cross-Examination
15 Exhibit No. 4.
16 Q. Tell me when you've had a chance to look through
17 that, Mr. O'Roark, and are ready for me to ask you
18 questions.
19 A. I've looked at it.
20 Q. In order to explore dPi's position that it's
21 entitled to a credit for the full face value of a
22 promotional offering, I want you to assume, as depicted on
23 page 1 here, that AT&T has a retail telecommunications
24 service A that has a retail price of $75. I also want you

to assume that the residential resale discount in North Carolina is 21.5 percent. Will you assume that with me?

A. Sure.

Q. Now, if A -- if dPi purchases service A for resale, we can agree, can't we, that dPi would pay AT&T the $58.88 price that's set out on the last line of page 1 of Exhibit 4?

A. Hypothetically, yes.

Q. That's simply the $75 retail price less 21-and-a-half percent resale discount, right?

A. Right.

Q. Now, you've testified that the net effect of a cash back promotion is to reduce the retail price that AT&T's customers are paying for telephone service, right? And if you want to look at your rebuttal, page 3, lines 1 through 2, it could refresh your memory.

A. You giving $50 to your customer reduces the price that your customer pays, is that your question?

Q. My --

A. Yes, it does. Yes, it does.

Q. So let's assume that -- I said 50. I want you to do 25. Let's assume that there's a $25 price reduction. And let's assume that instead of taking the form of a cash back offer, AT&T simply decides to reduce its price for

1 Telecommunication Service, here A, by $25. Will you make
2 that assumption with me?
3 A. Okay.
4 Q. Go to page 2 of Exhibit 4. We see a retail price
5 of $50 there, right?
6 A. Uh-huh.
7 Q. That's a yes?
8 A. Yes.
9 Q. And that is $25 less than the price on page 1,
10 right?
11 A. Right.
12 Q. If dPi purchased this service now with a $50
13 retail price, it would pay the 39.25 depicted at the
14 bottom of Exhibit 2, right?
15 A. Right.
16 Q. Now, flip to page 3. When the price of the
17 service was $75 dPi paid to resell the service, it paid
18 58.88, right?
19 A. Correct.
20 Q. And after the $25 reduction of the face value of
21 the price, dPi paid 39.25, right?
22 A. That's right.
23 Q. That's a difference of 19.63, right?
24 A. That's right.

1 Q. So a retail price reduction of $25 resulted in a
2 price reduction for dPi of 19.63, correct?
3 A. Correct.
4 Q. And you agree that if that's the way that this was
5 laid out, the 19.63 would be the difference that dPi was
6 entitled to, correct?
7 A. Do I agree that the difference between 58.88 and
8 39.25 is 19.63, yes, I agree.
9 Q. That's not quite what I asked. I'll clarify.
10 A. Okay.
11 Q. Do you agree that if AT&T reduced its retail price
12 from $75 to $50, that would inure to a benefit of $19.63
13 to dpi? It's not a $25 price reduction for dPi, it's a
14 19.63 price reduction, isn't it?
15 A. Yes. Yes.
16 Q. Let me ask you --
17 A. If you reduce the retail price, yes, that's
18 correct.
19 Q. If when we reduce our resale price by $25 you're
20 only entitled to 19.63, how is it that you claim to be
21 entitled to more than that when the reduction takes the
22 form of a cash back offer as opposed to a retail price
23 reduction?
24 A. Well, my understanding is that the law is and that

1 our interconnection agreement is that any promotion you
2 make available to your customer you have to make available
3 to my -- to my customer. And that if a customer comes to
4 you through the CLEC sales channel, you can't treat that
5 customer different than you treat a customer who comes to
6 you through your direct sales channel. So that when -- if
7 you give $25 to a customer that comes to you through your
8 direct channel, that you're obligated by contract and by
9 law to give that same $25 to the customer that comes to
10 you through the CLEC sales channel.
11 So, you know, that's my understanding of it. If
12 I'm -- I guess the Commission will decide what the actual
13 rule is, but, you know, we've -- we've asserted what we
14 believe to be the law and what we believe to be your
15 contractual obligation, that any promotion you make
16 available to your customer, you're obligated to make
17 available to my customer. If you give your customer $25,
18 you're obligated to give that same $25 to my customer.
19 You know, it's -- they're -- they're both
20 BellSouth customers. They just come through different
21 sales channels. They're still both BellSouth customers.
22 So we understood that the rule was that any promotion you
23 made available to your customer you had to make available
24 to my customer. You couldn't treat the two customers

1 differently just because one came through the CLEC sales
2 channel and one came through your direct sales channel,
3 that you had to treat them both the same; and that if you
4 didn't do that, that was -- that was unfair and that that
5 wasn't the rule. So that's part of what, I guess, is
6 going to be decided.
7 Q. Yes, your understanding of the law. I take it
8 that you rely in part on the Samford decision in
9 determining whether it complies with the law or not?
10 A. I think the Samford decision -- in my mind the
11 only -- the significance of the Samford decision was that
12 it says that any promotion that tends to reduce the retail
13 price paid had to be passed through, had to be made
14 available to the CLEC. That didn't deal -- my
15 understanding was -- and I'm not a lawyer, but my
16 understanding was it didn't deal with this specific cash
17 back, but it just dealt with general principle that if a
18 retail promotion had the effect of -- tended to have the
19 effect of reducing the price that a customer paid, that
20 that retail promotion had to be made available to the
21 CLEC.
22 And the only other significance was that for some
23 reason you began issuing credits to CLECs about the same
24 time that that ruling came down. So -- but you never went

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1 back and corrected the prior, so...

2 MR. TURNER: Mr. Chairman, I would like to

3 explore that a bit. And what I'd like to propose is that

4 I use the blackboard and ask my colleague, Ms. Phillips,

5 to copy what I'm putting on that blackboard. We'll

6 probably make it a -- move to make it a hearing exhibit at

7 the end so that the transcript can reflect what's on that

8 board.

9 COMMISSIONER CULPEPPER: That will be fine. Go

10 right ahead.

11 Q. See if we can make the hypothetical jibe with the

12 Sanford decision. Let's assume that the retail price is

13 $120. Assume that the coupon involved is $100. And to

14 make the math the same as the Fourth Circuit made it,

15 let's assume that the discount, resale discount, is

16 20 percent, right? If you take the service of 120, you'll

17 agree with me that 20 percent of 120 is 24, right?

18 A. Uh-huh.

19 Q. And that leaves -- if the CLEC bought the $120

20 service at a 20 percent discount, it would pay $96 for the

21 service, correct?

22 A. Uh-huh.

23 Q. Take the coupon. Coupon has a face value of $100,

24 right? You've got to say yes or --

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A. Oh, I'm sorry. Yes. Sorry.

Q. That's all right. And if you take 20 percent discount off the coupon, you come up with 80, right?

A. Uh-huh.

Q. Well -- so if AT&T charged dPi $96 for the service, then credited it $80, how much does dPi end up paying for the service?

A. 16, right.

Q. Do you have a copy of the Sanford decision in front of you?

A. No.

COMMISSIONER CULPEPPER: He doesn't have a copy of it, Mr. Turner.

MR. TURNER: Oh, I'm sorry. I didn't hear him. I'm trying to think of the least painful way to do this.

COMMISSIONER CULPEPPER: That's all right.

MR. TURNER: Mr. Chairman -- and I'm going to ask counsel to agree to this so we can speed the process up -- what I would like to do is to read into the record a paragraph from the Sanford decision to show how it applies to this.

COMMISSIONER CULPEPPER: Do you have a copy of the Sanford excision -- decision that you want to present to the witness?

MR. TURNER: I don't have it -- I have one copy, Your Honor, and that's the problem.

COMMISSIONER CULPEPPER: You have one copy of it, okay. Well --

MR. MALISH: I don't have -- I don't have an objection to him reading it into the record. I don't have an objection to him putting a copy in and he'll just add it -- you know, actually give the court reporter --

COMMISSIONER CULPEPPER: Well, I --

MR. MALISH: -- a hard copy later. I mean, this decision -- excuse me, the decision speaks for itself.

COMMISSIONER CULPEPPER: I understand that, Mr. Malish. I understand that. So I tell you what, let's -- let's do it this way. Mr. Turner, you hand Mr. O'Roark a copy of the Samford decision and you ask him to read into the record whatever part of that decision you would like for him to do so.

MR. TURNER: Yes, sir.

Q. Mr. O'Roark, just to save time, I would like you to read from "suppose" down to this 20 percent number here.

A. Subbose -- "Suppose BellSouth offers its subscribers residential telephone service for $20 a month. Assuming a 20 percent discount for avoided cost, see Local

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1 Competition Order PP [sic] 931-33. BellSouth must resell
2 this service to competitive LECs for $16 per month,
3 enabling the competitive LEC to compete with BellSouth's
4 $20 retail fee. Now suppose that BellSouth offers its
5 subscribers telephone service for 120 a month, but sends
6 the customer a coupon for a monthly rebate for $100.
7 According to the North Carolina Commission's orders, the
8 appropriate wholesale rate is still $16, because that is
9 the net price paid by the retail customer ($20) less the
10 wholesale discount. According to BellSouth's position,
11 however, the appropriate resale rate" --
12 Q. That's fine.
13 A. -- "the appropriate wholesale rate would be $96,
14 the nominal rate of 120, less the 20 percent discount for
15 *451 avoided cost."
16 COMMISSIONER CULPEPPER: All right. Stop right
17 there, Mr. O'Roark. Do you wish him to read any more of
18 the --
19 MR. TURNER: No.
20 COMMISSIONER CULPEPPER: -- of the decision?
21 All right. Thank you, Mr. O'Roark.
22 Q. Mr. O'Roark --
23 COMMISSIONER CULPEPPER: Ask him another
24 question now.

1 MR. TURNER: Yes, sir.
2 Q. Mr. O'Roark, we can agree that in that passage the
3 Fourth Circuit said that if you had a $120 retail price
4 and a $100 coupon, the appropriate price that a reseller
5 should pay is 16, correct?
6 A. According to the North Carolina Commission orders,
7 the appropriate rate is still $16, yes, that's what it
8 says.
9 Q. In our hypothetical here when we took the coupon
10 and discounted it by the percentage that is there in that
11 order, we came to $16, didn't we?
12 A. Yes.
13 Q. If we gave the full value of the coupon, we'd come
14 up with a negative four, wouldn't we?
15 A. Right.
16 Q. And that's not the number that's in that Sanford
17 decision --
18 A. No, it's not.
19 Q. -- is it?
20 Could I have the decision back, please?
21 A. Yes.
22 MR. TURNER: Mr. Chairman, may I give a copy of
23 Ms. Phillips' notes on the board to opposing counsel so he
24 can agree that it's an accurate depiction of what was on

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COMMISSIONER'S RESPONSE EXHIBIT B

O'Roark Cross-Examination Exhibit No. 1.4
I & A
CCC

Telecommunications Service A
Retail Price of $75.00

Price Retail Customer Pays	**$75.00**
Less 21.5% Resale Discount	**($16.13)**
Price Reseller Pays AT&T	**$58.88**

Telecommunications Service A
Retail Price Reduced by $25

Price Retail Customer Pays	$50.00
Less 21.5% Residential Discount	($10.75)
Price Reseller Pays AT&T	$39.25

Effect of $25 Retail Price Reduction on Price Reseller Pays AT&T

Price Reseller Paid AT&T Before $25 Retail Price Reduction	$58.88
Price Reseller Paid AT&T After $25 Retail Price Reduction	$39.25
Price Reduction for CLEC	$19.63

Reducing the Face Value of the Reduction by the Resale Discount

Retail Price Reduction	**$25.00**
Less 21.5% Residential Discount	**($5.38)**
	$19.63