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October 21, 2002

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Missouri Public Service Commission

Dale Hardy Roberts
Secretary of the Commission
Missouri Public Service Commission
PO Box 360
Jefferson City, MO 65101

Dear Mr. Secretary:

Attached for filing with the Commission, please find the original and eight copies of the initial brief of AT&T Communications of the Southwest.

I thank you in advance for your cooperation in bringing this to the attention of the Commission.

Very truly yours,

Rebecca B. DeCook TM

Rebecca B. DeCook

Attachment
Cc: All Parties of Record

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Missouri Public Service Commission

BEFORE THE MISSOURI PUBLIC SERVICE COMMISSION

In the Matter of Southwestern Bell Telephone Company's Tariff to Initiate Residential Customer Winback Promotion	)))	Case No. TT-2002-472 Tariff No. 200200831
In the Matter of Southwestern Bell Telephone Company's Tariff Filing to Extend Business Customer Winback Promotions.	)))	Case No. TT-2002-473 Tariff No. 200200828

INITIAL POST HEARING BRIEF OF AT&T COMMUNICATIONS OF THE SOUTHWEST, INC.

Comes now AT&T Communications of the Southwest, Inc. ("AT&T") and submits its Initial Brief in the above-captioned matters.

INTRODUCTION

The Commission should reject Southwestern Bell Telephone Company's (SWBT's) proposed tariff sheets because the winback offers proposed therein are contrary to Missouri law, are unreasonable and unjust, and will impede the development of competition in the local services market in Missouri. The terms and conditions of SWBT's proposed tariffs limit the availability of the promotional waivers to specific customers, affording those customers the lower winback priced service to specific customers, while similarly situated customers are not given the same price break because they are not CLEC customers or do not meet the eligibility criteria set forth in the tariffs. Such preferential treatment violates Section 392.200. The tariffs create the situation where similarly situated customers who are making the same purchase decision as to whether or not to purchase service from SWBT are treated unreasonably differently.

From a competitive standpoint, these offers contained in these tariffs allow SWBT to selectively target its "competitive response" to only the subset of customers that are being served by competitors or that are considering switching to a competitor. This ability to engage in such a targeted competitive response will harm the long run prospects for local competition and deny the full benefits of competition to the vast majority of local customers in Missouri.

SWBT seeks to stall, or even reverse, the growth of competition for basic residential and business services by making these targeted offers to the very customers that have taken the risk of trying the services of competitive local exchange carriers ("CLECs"). Competition in the local services market has not developed to the level that it can effectively discipline SWBT's general pricing, policies, practices and conduct. Rather SWBT is trying to use these winback offers to stifle the ongoing development of competition before it can effectively discipline the local market.

SWBT still controls over 85% of the local service market in Missouri. In addition, SWBT controls the ubiquitous network that is used by CLECs to provision local services in Missouri. CLECs have not made sufficient inroads in the Missouri market to overcome SWBT's natural advantages as the historic monopoly provider. Now SWBT wants to lure away CLECs' small customer base with these discriminatory winback discounts. In short, SWBT seeks to regain the few customers it has lost in order to preserve its historic market dominance.

The Commission should not allow SWBT to impede competition in this way. Rather, the Commission should encourage SWBT to extend the pricing benefits it seeks to offer the few customers that have made competitive choices to all of its customers.

That was the intended effect of the Telecommunications Act of 1996 and Missouri law. The Commission should encourage a dynamic market, in which all SWBT customers can gain pricing benefits and enjoy the benefits of competition, not just a select few.

While SWBT's proposed tariffs should be rejected for these reasons alone, the Commission should also consider the effect of SWBT's winback practices and procedures on competition. SWBT begins barraging former customers who have switched to a CLEC with winback marketing campaigns, including letters and telemarketing contacts, almost immediately upon the customer's switch to the CLEC. These marketing efforts undermine the CLECs ability to win and retain customers before the customer has even begun to experience the service the CLEC offers. These contacts are clearly designed to hinder customer choice, confuse customers, minimize the financial impacts of competition, and, ultimately, thwart competitive entry.

These marketing efforts also include an initial contact letter by SWBT to "determine if the customer has been slammed." SWBT then uses that contact, and the confusion generated by such contact, to "win" the customer back to SWBT. While SWBT casts this as a "customer service," SWBT is in effect policing its competitors customer conversion. This should not be permitted of the incumbent provider, particularly where it makes no effort whatsoever to determine if the customer properly authorized the conversion to the CLEC. SWBT's contact is clearly designed to confuse and manipulate the customer conversion process to its competitive advantage. Such practices clearly undermine the development of competition in Missouri and must be stopped.

For all these reasons, the Commission should reject SWBT's winback tariffs.

BACKGROUND

SWBT is proposing several revised tariff sheets that waive the nonrecurring service installation charge for certain eligible customers. In Case No. TT-2002-472, SWBT seeks to implement a residential promotion that would waive the nonrecurring service installation charge for residential CLEC customers who were previously served by SWBT and who chose to leave the CLEC and return to SWBT. (Ex. 2, Regan Direct, p. 3; Regan Schedule 2). In addition, SWBT would waive additional nonrecurring charges if the customer elects to subscribe to one of SWBT's popular packages, as outlined in the tariff sheet. The tariff contains eligibility requirements that the customer must meet in order to receive the promotional waiver. In addition to having been a previous SWBT customer, the residential customer must:

- have purchased local exchange service from a competitive local exchange company (CLEC);
- not have had service disconnected for non-payment; and
- must not have any past due bills for regulated service owed to SWBT.

Ex. 2, Regan Schedule 2.

The residential promotion is not available to new SWBT customers, including current CLEC residential customers who did not previously have SWBT, or to wireless customers. (Tr. 290, 317).

In Case No. TT-2002-473, SWBT proposes a business promotion that waives the nonrecurring service installation charge for certain eligible business customers. As with the residential promotion, this offer is available to business CLEC customers who were previously served by SWBT and who chose to leave the CLEC and return to SWBT. (Ex. 2, Regan Direct, pp. 3-4; Regan Schedule 3-1). However, in addition, the proposed business tariffs would waive the nonrecurring service installation charge for business

customers that are currently customers of CLECs but who never had service with SWBT.[1]

The tariff contains eligibility requirements that the customer must meet in order to receive the promotional waiver. In addition, the business customer must:

- have purchased local exchange service from a competitive local exchange company (CLEC);
- not have had service disconnected for non-payment; and
- must not have any past due bills for regulated service owed to SWBT.

Ex. 2, Regan Schedule 3-1.

The business promotion is not available to all new subscribers of SWBT services. It is only available to those new subscribers who currently obtain service from a CLEC. (Tr. 281).

ARGUMENT

I. THE REVISIONS THAT SWBT PROPOSES TO BOTH THE RESIDENTIAL AND BUSINESS TARIFFS AT ISSUE ARE CONTRARY TO MISSOURI LAW.

SWBT's proposed winback offers must be rejected because the offers provide like services to the target customers under the same or substantially same conditions as are being offered to ineligible customers, but at a discount. There is no factual difference in the conditions experienced by or services provided to the eligible customers versus the ineligible customers. In addition, SWBT has failed to demonstrate any cost basis for the proposed discounted rate. Finally, the proposed tariff revisions would have a deleterious impact on the ongoing development of competition in Missouri. For all these reasons, the

[1] The record is very confusing on this aspect of the offer. (*See, e.g.*, Tr. 272-73, 280-82.) It is still not entirely clear whether this aspect of the business offer is available to all current business customers of the CLECs or if it is only available to some subset of business customers, i.e., those who obtain service from the CLEC via the resale of SWBT services (resale) or facilities (unbundled elements).

winback offers are contrary to Missouri law, are discriminatory and are unreasonable and unjust.

A. The Tariff Revisions are Contrary to the Statutory Requirements.

Section 392.200.2 provides in pertinent part as follows:

> No telecommunications company shall directly or indirectly or by any special rate, rebate, drawback or other device or method charge, demand, collect or receive from any person or corporation a greater or less compensation for any service rendered or to be rendered with respect to telecommunications or in connection therewith, except as authorized in this chapter, than it charges, demands, collects or receives from any other person or corporation **for doing a like and contemporaneous service with respect to telecommunications under the same or substantially the same circumstances and conditions**. Promotional programs for telecommunications services may be offered by telecommunications companies for periods of time so long as the offer is otherwise consistent with the provisions of this chapter and approved by the commission.

Section 392.200.3 provides as follows:

> No telecommunications company shall make or give any undue or unreasonable preference or advantage to any person, corporation or locality, or subject any particular person, corporation or locality to any undue or unreasonable prejudice or disadvantage in any respect whatsoever except that telecommunications messages may be classified into such classes as are just and reasonable, and different rates may be charged for the different classes of messages.

These statutes require that customers be treated in a nondiscriminatory fashion. They require that customers cannot be charged differing rates for "like or contemporaneous service" that is offered under "the same or substantially the same circumstances or conditions." They prohibit undue or unreasonable rate preferences. Regarding rate differences, the test is whether there is any "reasonable and fair difference in conditions which equitably and logically justifies a different rate." *State ex rel. DePaul Hospital v. PSC*, 464 S.W.2d 737, 740 (Mo. App. 1970). In *DePaul Hospital*, a

customer complained that it was being charged a different and higher rate for the same service based upon an arbitrary classification that had been created by Southwestern Bell. *Id.*, p. 739. In that case, the Court concluded:

> In *State ex rel. City of St Louis v. Public Service Commission*, 327 Mo. 318, 36 S.W.2d 937, 950, it was said that arbitrary discrimination alone are unjust, but, if the difference in rates be based upon a reasonable and fair difference in conditions which equitably and logically justify a different rate, it is not an unjust discrimination. In the instant case the overwhelming weight of the evidence is to the effect that the service rendered to complainant was of like character and under virtually the same conditions as those provided in Southwestern's service to Evangeline and Athletic Club, as well as to those other customers mentioned in evidence. However, the rates charged complainant were near three times those charged to the aforementioned customers under the "hotel-motel" rate.

Id. at 740.

Consequently, the Court concluded that the rate charged the complainant was discriminatory, in violation of Section 392.200.

The court in *City of Grain Valley v. P.S.C.* reached a similar conclusion in applying Section 392.200. (*City of Grain Valley v. P.S.C.*, 778 S.w.2d 287 (Mo.App. 1989). In determining that there was no justification for the difference in rates that had been established between the towns of Blue Springs and Grain Valley, the Court stated:

> The differences pointed out by the Commission between Blue Springs and Grain Valley do exist, but there is no relation between those differences and the conditions under which telephone service is furnished to the two areas. The telephone customers in Grain Valley received their dial tone from the Blue Springs office, received the same telephones service, were billed monthly just as the Blue Springs customers and were entitled to the same service from Bell as the Blue Springs customers. Bell did nothing differently in furnishing telephone service for the Grain Valley customers than it did for the Blue Springs customers.

Id. at 291.

This same logic applies to the arbitrary customer classification that SWBT seeks to establish here. SWBT contends that these CLEC customers are similarly situated and represent a unique class of customers. (*See* Ex. 4, Hughes Direct, p. 2; Ex. 5, Hughes Surrebuttal, pp. 4, 8). Southwestern Bell presents no factual evidence to support the assertion that the customers eligible for these winback offers (CLEC customers) are not similarly situated with it other new customers. (*See* Ex. 4, Hughes Direct, p. 2; Ex. 5, Hughes Surrebuttal, pp. 4, 8; Ex. 6, Thomas Rebuttal, p. 6; Ex. 10, Kohly Rebuttal, p. 8; Tr. 559). Nor does it present any evidence to support why these customers represent a unique class of customers. (*Id.*). Indeed, SWBT makes no attempt to explain why there is any factual difference in the conditions experienced by or services provided to the eligible customers versus the ineligible customers. The reason for this omission is a simple one. They cannot establish such factual differences.

To the contrary, it cannot be disputed that the services covered by the promotions are the same for both eligible and ineligible customers (i.e., both customers are seeking like and contemporaneous service). (Ex 10, Kohly Rebuttal, p. 8; Ex. 6, Thomas Rebuttal, p. 6; Tr. 559). Also, both eligible and ineligible customers are located in SWBT's local service territory, are not presently served by SWBT, and are making the same purchase decision (i.e., whether or not to purchase service from SWBT). (Ex 10, Kohly Rebuttal, p. 8).

In short, the ineligible customers are similarly situated with the eligible customers in terms of the nature and terms of service the customers seek from SWBT. There is no reasonable difference in the conditions under which the service at issue is being offered that would justify the eligibility limitations in the proposed tariffs. Accordingly, in the

words of the statute, SWBT would be providing "a like and contemporaneous service with respect to telecommunications under the same or substantially the same circumstances or conditions" (Section 392.200.2), but SWBT would be improperly charging a different rate for such service.[2]

While not dispositive, the Commission might also take guidance from the test for interpreting the term "like" that has been used by the FCC and Courts applying Section 202(a) of the federal Telecommunications Act. As Mr. Kohly indicated when pressed by counsel for SWBT during cross-examination, Section 202(a) and Section 392.200.2 of the Missouri statute are virtually identical. (Tr. 588-89). Under federal interpretations of Section 202(a), the standard for determining "likeness" is a functional equivalency test. As the Court stated in *American Broadcasting Companies, Inc., et al. v. FCC*, 663 F.2d 133, 138-39 (D.D.C. 1980):

> Under this test as developed by the Commission, the inquiry centers on whether the services are " different in any material functional respect." *American Trucking Associations, Inc. v. FCC*, 377 F.2d 121, 127 (D.C.Cir. 1966), *cert. denied*, 386 U.S. 943, 87 S.Ct. 973, 17 L.Ed.2d 874 (1987). The test looks to the nature of the services offered to determine likeness; the perspective of the customer faced with differing services is often considered a significant factor. *See American Telephone & Telegraph Co.* (WATS), 70 F.C.C.2d 593, 609 & 614 (1978).
>
> The Court went on to say:
>
> By looking to the nature and character of the services in question, the test focuses the initial inquiry under section 202(a) on the similarity of the services. Considerations of cost differentials and competitive necessity are properly excluded and introduced only when determining whether the discrimination is unreasonable or unjust. *See Western Union*

[2] SWBT seems to suggest that if SWBT's winback offers are rejected under Missouri law, that other providers' winback offer must be as well. AT&T disagrees with SWBT's interpretation of Missouri law, but, in any event, that issue raised by SWBT cannot be addressed in this proceeding. The only tariffs noticed for consideration in this case were SWBT's tariffs. Consideration of other parties' tariffs is beyond the scope of this proceeding and would be improper.

International, Inc. v. FCC, 568 F.2d 1012, 1019 n.15 (2d Cir. 1977), *cert denied*, 436 U.S. 944, 98 S.Ct. 2854, 56 L.Ed.2d 785 (1978).

Id.

Applying a functional test to the services offered to the customers eligible for the winback offer as compared to the services offered to the customers that are not eligible for the winback promotion, there can be no doubt that the services are like. There is no difference in the service being offered. The only difference is the rate being charged. As a result, SWBT's winback offers do not comply with Section 392.200.

SWBT's witness Hughes admits that it is the wording of SWBT's tariff that, in SWBT's view, determines that the customers are not similarly situated. (Tr. 316). Using SWBT's rationale, any arbitrary service or rate classification could be established simply by defining a class of customers in a tariff. And SWBT or any other provider could freely discriminate without impunity. Clearly, stricter scrutiny of the service and rate classification is mandated under Missouri law, as the case law reflects SWBT's tariff do not pass this scrutiny.

B. SWBT Has Presented No Cost Justification For The Discounted Rate in the Winback Offers.

Even if SWBT could somehow demonstrate that the winback offers were not "like" services, the offers are not reasonable or just. SWBT has not established that there is a cost justification for the discounted rate it seeks approval of in the winback offers. As Staff indicates, what SWBT is attempting to do is segment its customers based upon their willingness to pay. (Ex. 6, Thomas Rebuttal, p. 8). This is classic monopolistic price discrimination. In Staff's view: "to allow price discrimination without cost

justification would run contrary to the legislative goals of universal service and of bring the benefits of competition to every Missouri citizen." (Ex. 6, Thomas Rebuttal, p. 8)

While SWBT concedes that cost reasons did not drive SWBT's decision to limit these winback offers to the targeted customers and claims it is not required to show a cost basis for the different rate it seeks to offer to the eligible winback customers, it attempts to suggest that there is such a cost difference. (Tr. 321; Ex. 5, Hughes Surrebuttal, p. 10). SWBT claims that unlike new customers, there are no network costs associated with switching a CLEC customer back to SWBT where the CLEC is serving the customer via resale or UNE-P. While SWBT presents no evidence or cost studies to support this claim (Tr. 326), SWBT concedes that there would be central office costs to convert these customers back to SWBT. (Tr. 353). In addition, when Mr. Hughes is confronted with examples involving customers served by CLEC through other means he is forced to admit there are costs to convert those customers back to SWBT. For example, Mr. Hughes admits that customers who obtain services from a CLEC using unbundled loops would require central office and some field work by SWBT to convert them back to SWBT. (Id.) Moreover, Mr. Hughes admits that he completely ignored conversions from facilities based CLECs. (Tr. 354). Under SWBT's business promotion, new business customers that obtain service from the CLEC, but never had SWBT service, would be eligible for the promotion. These customers would be considered "new" SWBT customers and it is equally likely that SWBT would have no existing facilities to service these customers. When the "new" business customer is compared with the SWBT customer who moves across the street, but remains a SWBT customer—a customer that would be considered a "new" customer by SWBT and would be ineligible for the

promotion--the customer would cost SWBT less to reacquire than the "new" business customer that is eligible for the promotion. This scenario, at a minimum, supports Mr. Kohly's claim that there are circumstances where " the costs of reacquiring an eligible customer served by a competitor might actually be higher than the costs of initiating service with a new customer. (Ex. 10, Kohly Rebuttal, pp. 6-7). This example, along with the other cost scenarios Mr. Hughes agreed to during cross-examination, demonstrate that there is no cost justification for the winback offers and they are, therefore, unreasonable and unjust in violation of Section 392.200.

Next, SWBT claims that SWBT's tariff sheets comply with Missouri law because the same or similar tariffs have been previously approved by the Commission. (Ex. 4, Hughes Direct, pp. 3, 12; Ex. 5, Hughes Surrebuttal, p. 7). This logic is flawed for several reasons. First, technically, the Missouri Commission has never "approved" any of the prior winback tariffs. Rather, it allowed them to go into effect. (Tr. 301, 654). Until it heard Case Nos. TT-2002-108 and TT-2002-130, the Commission had never considered SWBT's winback tariffs in the context of a contested case, and had not made explicit rulings on those tariffs or their compliance with Section 392.200.

Second, the Commission has already considered and rejected this argument in Case Nos. TT-2002-108 and TT-2002-130, where it determined:

> the Commission is not bound to comply with its previous decisions. As an administrative agency the Commission is not bound by *stare decisis,* and the failure of the Commission to explain why it is not taking the same position in one case that it took in a previous case is not a basis for overturning the Commission's action.

Report and Order, p. 15.

In its Report and Order in Case Nos. TT-2002-108 and TT-2002-130, the Commission did however, acknowledge that Sections 392. 200.2 and 392.200.3:

> [have] been interpreted to 'forbid discrimination in charges for doing a like or contemporaneous service with respect to communication by telephone under the same or substantially the same circumstances and conditions.' Rate differences are permitted only if there is any 'reasonable and fair difference in condition which equitably and logically justifies a different rate.'[3]

In addition, the Commission rejected SWBT winback offer in that proceeding, concluding:

> Southwestern Bell's save and winback provisions would have much the same impact on the health of competition in the local service market as would term agreements. But, in addition to the anticompetitive effects resulting from the use of term agreements by a dominant ILEC, save and winback provisions can cause further damage to the emerging competitive market. Such provisions are targeted directly at the customer base of the CLECs. If Southwestern Bell takes back many of those customers with save and winback provisions, and then locks them up with long-term contracts, CLECs might be left without a customer base to which they can market. Edward J. Cadieux, witness for NuVox Communications of Missouri, Inc., one of the CLECs currently attempting to compete against Southwestern Bell, testified that the combination of term discounts and save and winback provisions might freeze competition at its currently inadequate level. If the CLECs are frozen out of the competitive market, they would then be forced to abandon their attempt to compete in Missouri, leaving only Southwestern Bell as a viable local service provider. Until the CLECs are in a strong enough position to effectively compete with Southwestern Bell, the use of save and winback provisions by Southwestern Bell is anticompetitive.

While AT&T acknowledges that this prior decision is not binding, the legal and factual landscape that existed when the Commission made this ruling has not changed in Missouri and, therefore, the SWBT winback tariff sheets that are at issue in this proceeding should be rejected for the same reasons the prior winback offer was previously rejected. Staff witness Chris Thomas agrees. He testified that "Staff believes

[3] Report and Order, p. 15.

that the Finding of Fact in the Commission's Order accurately characterizes the use of winback marketing activities by SWBT. (Ex. 6, Thomas Rebuttal, pp. 2-3.)

Third, as Mr. Hughes concedes, this Commission can only approve these tariffs if it finds them lawful and appropriate under Section 392.200. (Tr. 330). During the course of the proceeding, SWBT made much ado of certain policy statements of the Federal Communications Commission ("FCC") regarding winback offers. While this Commission is not bound by the FCC's statements of policy, such as those expressed in the CPNI Order, in this proceeding, the Missouri Commission is confronted with specific targeted winback proposals and whether such proposals are consistent with state law. As is evidenced by the FCC's statements in the CPNI Order, the FCC was not reviewing specific winback proposals. Nor was the FCC conducting a review of a specific winback proposal under state law. Therefore, the FCC's policy statements are simply not germane to this case.

C. The Proposed Winback Offers are Contrary to the Public Interest Because They Will Impede the Development of Competition.

This Commission is charged, *inter alia*, with construing Section 392 in a manner that "promotes diversity in the supply of telecommunications services and products throughout the state of Missouri" and "allows full and fair competition to function as a substitute for regulation when consistent with the protection of ratepayer and otherwise consistent with the public interest." Section 392.185(3) and (6).

In addition, as established by the Legislature when it adopted SB 507, the intent of SB 507 is to:

> bring the benefits of competition to **all** customers and to ensure that incumbent and alternative local telecommunications companies have the

> opportunity to price and market telecommunications service to **all** prospective customers in any geographic area in which they compete.

Section 392.200.4(2).

As part of its rationale in rejecting the winback provisions proposed by SWBT in Case Nos. TT-2002-108 and TT-2002-130, the Commission emphasized that it: "has a duty to regulate Missouri's telecommunications industry in such a way as to promote the development of full and fair competition.[4]

SWBT continues to possess significant market power, and has the ability and the incentive to utilize its market power in ways that are harmful to the competitive process and, over the long run, to Missouri telecommunications users.

Prior to the passage of the Act, SWBT provided local telecommunications services to customers without fear of competitive challenges, using a network financed by captive ratepayers at virtually no risk to SWBT and its shareholders. When SWBT's legal monopoly was abolished, SWBT inherited an existing, ubiquitous network with links to every business and residential premises in its service territory. As the FCC recognized, SWBT's network represents an asset of enormous strategic value to the company, stating:

> An incumbent LEC's existing infrastructure enables it to serve new customers at a much lower incremental cost than a facilities-based entrant that must install its own switches, trunking and loops to serve its customers. [...I Because an incumbent LEC currently serves virtually all subscribers in its local serving area, an incumbent LEC has little economic incentive to assist new entrants in their efforts to secure a greater share of that market. An incumbent LEC also has the ability to act on its incentive to discourage entry and robust competition by not interconnecting its network with the new entrant's network or by insisting on supracompetitive prices or other unreasonable conditions for terminating calls from the entrant's customers to the incumbent

[4] Report and Order, p. 14.

LEC's subscribers.[5]

In a recent opinion by the United States Supreme Court, the ILECs' strategic advantage flowing from their inherited networks was described by the Court as follows:

> It is easy to see why a company that owns a local exchange (what the Act calls an "incumbent local exchange carrier," 47 U.S.C. §251(h)), would have an almost insurmountable competitive advantage not only in routing calls within the exchange, but, through its control of this local market, in the markets for terminal equipment and long-distance calling as well. A newcomer could not compete with the incumbent carrier to provide local service without coming close to replicating the incumbent's entire existing network, the most costly and difficult part of which would be laying down the "last mile" of feeder wire, the local loop, to the thousands (or millions) of terminal points in individual houses and businesses.[6]

SWBT attempts to obscure these facts by focusing on SWBT's minimal market share losses. However, SWBT's witness could not explain how the line data that was compiled, so there was no way to verify the accuracy and the reliability of the data. (Tr. 333-34, 338-42, 346-47). Even if this data is determined to be accurate, SWBT still retains overwhelming control of the local market, with an 85 to 88% market share. Importantly, given there are 70 plus CLECs operating in Missouri according to SWBT (Tr. 416), clearly the 12 to 15% market share SWBT attributes to the CLEC is spread across many CLECs, with no one CLEC with sufficient market share to seriously threaten SWBT's market power. (Tr. 456). As Staff witness Thomas noted, while market share loss figures may evidence that " competition is moving forward, it is not an indication of a significant change in the relative market position of the players in the marketplace." (Ex. 6, Thomas Rebuttal, p. 4).

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[5] *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996,* First Report and Order, CC Docket No. 96-98, FCC No. 96-325, released August 8, 1996, pp. 5, 10. ("Local Competition Order")

[6] *Verizon v. FCC,* 535 U.S.___, 122 S.Ct. 1646, 1662, 152 L.ED.2d 701 (U.S. May 13, 2002)

Notwithstanding the marginal gains that CLECs have made in eroding SWBT's market share, SWBT retains an overwhelming majority of the potential customer base for telecommunications services. As Staff witness Thomas explained:

> The Commission should not confuse functioning competition with loss of market share. If the Commission's goal is to substitute competition for regulation, wherever possible, it is important to note that loss of market share and functioning competition are two very different concepts. SWBT can lose market share to CLECs without competition serving as effective price control. Many CLECs rely primarily on the use of UNEs and resale to provide service and SWBT's obligations to provide such elements could be removed at any point. As Staff has indicated in previous cases on this issue, local markets are not yet at a point where competition can successfully substitute for regulation.

(Ex. 6, Thomas Rebuttal, p. 5).

While competition may be increasing, as Mr. Kohly indicates, it is not increasing at the pace one would expect (Tr. 654-55), and it not at a level where it is disciplining the local market. (Ex. 6, Thomas Rebuttal, p. 5). Competition remains vulnerable to interference by SWBT. As Mr. Kohly explained:

> successful entry into the local exchange market requires a new entrant to achieve a sufficient amount of business to offset the significant capital investment required to off local service. Whether the CLEC is using unbundled elements or its own facilities, CLECs entering the market must make large up-front investments before they can begin offering service. A new entrant's decision to enter and expand (and its corresponding ability to obtain financing through today's capital markets) is, therefore, based on its expectation that it will be able to recover, within a reasonable time frame, its cost of these up-front investments, along with the on-going costs of providing services, plus a reasonable return on its investment. SWBT, the incumbent provider, has already sunk the large percentage of its costs associated with its network (costs that were largely funded by ratepayers) and has a customer base that allows it to benefit from significant economies of scale, resulting in lower marginal costs for the incumbent.

Ex. 10, Kohly Rebuttal, p. 13.

Mr. Kohly testified that, as the incumbent, SWBT has the long-term incentive to deprive entrants of the opportunity to achieve significant economies of scale to keep its rivals cost higher than its own. (*Id.*). By limiting the eligibility of a promotion to the narrow segment of CLEC customers, SWBT will still be able to maintain high rates or even increase rates for the vast majority of other customers while limiting price reductions to only those customers that have sought competitive choice during these initial stages of competition. These targeted eligibility limitations make it much less costly for SWBT to engage in the limited price competition aimed exclusively at CLEC customers. (*Id.*, p. 14.) Meanwhile, the competing CLECs will have to reduce rates for all customers in order to compete with SWBT, since once that CLEC gains a customer the customer is immediately eligible for SWBT's promotional rates. (Id.) In essence, SWBT's proposed tariffs would permit SWBT to fund its targeted competitive response from revenues derived from other SWBT customers. (Ex 10, Kohly Rebuttal, pp. 13-14; Ex. 7, Meisenheimer Rebuttal, p. 8). Competitors do not have this luxury. (Ex 10, Kohly Rebuttal, pp. 13-14; Ex. 8, Price Rebuttal, pp. 18-19). If permitted, this would unreasonably impede competition.

It was a similar concern that led the FCC to reject a proposal made by SWBT to permit targeting of dedicated access facilities that SWBT provided in competition with competitive access providers ("CAPs").[7] In rejecting that proposal, the FCC found that SWBT's proposal

> may permit SWBT unreasonably to deter or foreclose competitive entry into the markets in which it has a monopoly. As formulated, [SWBT's proposal] allows SWBT a virtually unlimited opportunity to preempt new market entrants in its territory by reducing rates to individual customers to

[7] CAPs have been providing inter and intrastate dedicated services since the 1980s in competition with SWBT.

which it believes new entrants may make offers, without making those rates available to similarly situated customers elsewhere[8].

SWBT's attempts to distinguish this decision by claiming that this FCC docket had nothing to do with winbacks. (Ex. 5, Hughes Surrebuttal, pp. 24-25). While that is true, the FCC was addressing targeted pricing by SWBT and its effect on competition. Targeted pricing is exactly what SWBT seeks to do with its winback tariffs. (Ex 10, Kohly Rebuttal, pp. 13-14; Ex 6, Thomas Rebuttal, p. 7; Ex. 7, Meisenheimer Rebuttal, p. 8). In any event, AT&T's purpose in citing this ruling is not to suggest that the FCC decision has precedental value, but rather to suggest that it lends support for the position AT&T is advancing in this proceeding.

By targeting CLEC customers, SWBT's offer will also have the effect of inhibiting the CLECs ability to recover its initial capital investments and expand and could lead to significant stranded investment. (Ex. 10, Kohly Rebuttal, pp. 15-16). This will be particularly true if SWBT is successful in its current campaign to eliminate the current unbundling requirements. Knowing this, new entrants will be less likely to enter the market or make further expansions if they believe that the incumbent can engage in pricing campaigns targeted only at the CLEC's customers.

SWBT's ability to limit the promotion only to customers that have left SWBT demonstrates SWBT's market power. If the market for local telecommunications services were one characterized by effective competition, SWBT would not attempt to compete by limiting such a promotion to its "former" customers. Rather, it would be compelled to try to attract ***any*** new customer, regardless of whether the customer was a former customer of SWBT or some other carrier.

[8] CC Docket No. 97-158, Transmittal No. 2633, *In the Matter of Southwestern Bell Telephone Company, Tariff F.C.C. No. 73*, Order Concluding Investigation and Denying Application for Review, Nov. 14, 1997.

In its Report and Order in consolidated Cases TT-2002-108 and TT-2002-130, the Commission concluded that "the use of save and winback provisions by Southwestem Bell is anticompetitive." Report and Order at 13. In considering the save and winback proposals at issue in that proceeding, the Commission stated its concem "about protecting the viability of the overall market for local exchange telecommunications services." *Id.* at 16. And rejecting SWBT's customer benefits argument, the Commission concluded "that Southwestem Bell's offers are a threat to the long-term health of the competitive market for local phone service." *Id.* Further, the Commission stated its "obligat[ion] to protect the viability of the competitive market in order to protect Missouri's telecommunications customers from the threat of monopoly power in a future without viable competition in the local telecommunications market." *Id.* at 17.

And responding to the SWBT argument that in supporting its 271 petition before the FCC the Missouri PSC had concluded that the local telecommunications market is "open to competition," the Commission underscored that "[u]nless the Commission acts to protect competition, the local exchange market may be open to competition but have no surviving competitors." *Id.* at 18.

In short, SWBT's proposed winback offers represent an attempt to exercise market power to the long-term detriment of the competitive process and to consumers. The Commission has already clearly articulated its recognition of, and agreement with, the need to prevent such exercises of market power by SWBT. The Commission should not change course now.

SWBT attempts to shift the debate to one under the antitrust laws. (Ex. 1, Aron Surrebuttal). While recognizing that no party to this proceeding has made any antitrust

claims, SWBT contends that the Commission should analyze the competitive impact of these tariffs using an antitrust analysis and, under such analysis, SWBT's tariffs could only be deemed anticompetitive if it is demonstrated that the SWBT is engaged in predatory pricing. (Tr. 45-46).

This view misses the mark for several reasons. First, this Commission's competitive and public interest review is not in any way constrained by antitrust principles. Second, the principles and "learnings" that SWBT espouses have been applied under the very strict confines of federal antitrust law. The statutory mandates for stating an antitrust claim are much different and stricter than the controlling statutory and policy principles that govern this Commission's assessment of the impact of these proposed tariffs on competition and the public interest.

Third, the use of the term anticompetitive was not intended to be an accusation of antitrust violations. (Ex. 6, Thomas Rebuttal, p. 3). It is clear from the testimony filed in this case that the use of the term anticompetitive was to express concern regarding the impact the proposed would have on the ongoing transition of the local market from a monopoly market to a competitive market. (*See also* Tr. 556).

As long as competition remains in its early stages, it would be unreasonable to allow SWBT to price in a manner meant to impede the competitive process. The Commission needs to assure that competition can grow and not allow the market to lapse back into monopoly. The targeted discounts at issue are unreasonable and contrary to the public interest because they would impede the development of competition in the basic local market. Accordingly, the proposed tariffs should be rejected.

While SWBT's proposed tariffs should be rejected for all of the above reasons alone, the Commission should also consider the effect of SWBT's winback practices and procedures on competition. SWBT begins barraging former customers who have switched to a CLEC with winback marketing campaigns, including letters and telemarketing contacts almost immediately upon the customer's switch to the CLEC. As Mr. Regan testified, SWBT begins sending winback letters to customers that have converted to CLECs within 2 days of the customer switching to the CLEC. (Tr. 202-05). Because SWBT did not make available a witness from the sales organization in this proceeding, the organization that actually conducts SWBT's winback activities, it cannot be verifed what the trigger is for the first letter. (Tr. 247). That is a critical issue because it would be patently unlawful for SWBT to commence winback activities before the customer is actually and completely converted to the CLEC. Because of an absence of a sales witness, CLECs could not fully explore documentation SWBT produced in discovery on this issue.

For residential customers, SWBT continues this letter campaign until the customer converts or SWBT sends at least 9 letters, whichever comes first. (Tr. 205) At the same time, SWBT, through third party telemarketers and internal recorded messages, begins contacting the CLEC customer through phone calls. (Tr. 206). These invasive marketing efforts undermine the CLECs ability to win and retain customers before the customer has even begun to experience the service the CLEC offers. (Tr. 205). These contacts are clearly designed to hinder customer choice, confuse customers, minimize the financial impacts of competition, and, ultimately, thwart competitive entry.

In addition, the first letter sent to the CLEC customer seeks to cast doubt on the CLECs conversion on the customer by seeking to "determine if the customer has been slammed." (Ex. 3, Regan Surrebuttal, p. 5; Tr. 199, 213-14; Ex. 14 and 15). SWBT provides no explanation or definition of the term "slammed" to the customer in the letter, but encourages the customer to contact an 800 number in the SWBT retail winback group. If the customer contacts SWBT, SWBT has no way to determine if the CLEC properly converted the customer. It has no access to any information to determine if the CLEC used proper third party verification procedures or if the person contacting SWBT was even the person that authorized the initial switch to the CLEC. Rather, SWBT simply takes the customer at his word. (Tr. 201-02). SWBT uses this highly improper contact with the CLEC customer to report to authorities that the CLEC has slammed the customer. SWBT also uses this contact with the CLEC customer, and the confusion it has generated by this contact to try to "win" the customer back. While SWBT portrays this as some sort of customer service, SWBT should not be policing its competitors' customer conversions, particularly where it makes no effort whatsoever to determine if the customer properly authorized the conversion. SWBT's contact is clearly designed to confuse and manipulate the customer conversion process to its competitive advantage. Such practices clearly undermine the development of competition in Missouri and must be stopped.

CONCLUSION

SWBT's proposed winback offers are contrary to Missouri law, are unjust and unreasonable and are contrary to the public interest, given SWBT's continued dominance over the local service market. Its proposed tariffs contain discriminatory discounts that

would unreasonably impede CLECs efforts to compete in that market. The proposed targeted discounts would target SWBT's competitive response on CLEC customer bases, rather than all customers, by offering competitive pricing only to CLEC customers. Accordingly, the Commission should reject SWBT's proposed tariffs.

Respectfully submitted this 21st day of October, 2002.

AT&T COMMUNICATIONS OF THE SOUTHWEST, INC.

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BEFORE THE MISSOURI PUBLIC SERVICE COMMISSION

In the Matter of Southwestern Bell Telephone Company's Tariff to Initiate Residential Customer Winback Promotion	)))	Case No. TT-2002-472 Tariff No. 200200831
In the Matter of Southwestern Bell Telephone Company's Tariff Filing to Extend Business Customer Winback Promotions.	)))	Case No. TT-2002-473 Tariff No. 200200828

PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW OF AT&T COMMUNICATIONS OF THE SOUTHWEST, INC.

Comes now AT&T Communications of the Southwest, Inc. ("AT&T") and submits its Proposed Findings of Fact and Conclusions of Law in the above-captioned matters.

I. Summary

Southwestern Bell Telephone Company has submitted several revised residential and business tariff pages in which it seeks to waive the nonrecurring service installation charge for certain eligible customers. In Case No. TT-2002-472, Southwestern Bell seeks to implement a residential promotion that would waive the nonrecurring service installation charge for residential CLEC customers who were previously served by Southwestern Bell and who chose to leave the CLEC and return to Southwestern Bell.

In Case No. TT-2002-473, Southwestern Bell proposes a business promotion that waives the nonrecurring service installation charge for certain eligible business customers. As with the residential promotion, this offer is available to business CLEC customers who were previously served by Southwestern Bell and who chose to leave the CLEC and return to Southwestern Bell. In addition, Southwestern Bell also proposes to

waive the nonrecurring service installation charge for CLEC business customers even though the customers were not originally served by Southwestern Bell.

The Commission suspended the tariffs and now finds that the proposed tariffs are contrary to Missouri law, are unreasonable and unjust and would harm the development of competition in the local exchange market. For those reasons, Southwestern Bell's tariffs are rejected.

II. Procedural History

On March 29, 2002, Southwestern Bell Telephone, L.P. d/b/a Southwestern Bell Telephone Company issued a tariff sheet that would revise its Local Exchange Tariff to offer, as a promotion, a waiver of the Service and Equipment Charge to residential customers who have disconnected their access line with Southwestern Bell for the purpose of establishing service with another local exchange carrier and now wish to return to Southwestern Bell. The tariff carried an effective date of April 9, 2002.

On March 29, 2002, Southwestern Bell Telephone, L.P. d/b/a Southwestern Bell Telephone Company issued tariff sheets that would extend certain winback promotions for business customers. The winback promotions included a waiver of the nonrecurring service installation charge for business customers who have disconnected their access line with Southwestern Bell for the purpose of establishing service with another local exchange carrier and now wish to return to Southwestern Bell. The winback promotions for business customers would also extend to business customer that had established service with the CLEC and had not previously obtained service from Southwestern Bell. The tariff sheets carried an effective date of April 9, 2002.

On April 3, 2002, the Staff of the Commission filed a motion asking the

Commission to suspend and reject Southwestern Bell's proposed tariff. Staff pointed out that the Commission, in its Report and Order in Case No. TT-2002-108, found that winback promotions, such as that established by this tariff, are anticompetitive. Staff contended that the tariff proposed by Southwestern Bell was also anticompetitive and should be rejected.

On April 3, 2002, the Staff of the Commission filed a motion asking the Commission to suspend and reject Southwestern Bell's proposed tariff. Staff pointed out that the Commission, in its Report and Order in Case No. TT-2002-108, found that winback promotions, such as that established by this tariff, are anticompetitive. Staff contended that the tariff proposed by Southwestern Bell was also anticompetitive and should be rejected.

On April 5, 2002, the Commission suspended the two tariff filings submitted by Southwestern Bell that would offer winback promotions to residential and business customers. The Commission initially suspended the tariff until May 9, 2002. Subsequently, the Commission further suspended the tariffs until August 7, 2002, 120 days from their originally proposed effective date of April 9, 2002.

Timely interventions were filed in both proceedings by AT&T Communciations of the Southwest, Inc., MCImetro Access Transmission Services, LLC, Brooks Fiber Communications of Missouri, Inc., and MCI WorldCom Communications, Inc, (collectively "WCOM") and NuVox, and the Commission granted those interventions on May 20, 2002.

A prehearing conference was held on May 22, 2002. On that same day, the Commission entered an order consolidating the two proceedings, Case No.TT-2002-472 and Case No. TT-2002-473.

On June 7, 2002, the Commission adopted a procedural schedule leading to a hearing beginning on September 23, 2002, and continuing on September 24. Because the hearing was not scheduled to begin until after the period of suspension has expired, the Commission further extended the suspension of the tariff sheets until November 7, 2002, or until otherwise ordered by the Commission.

Pursuant to the procedural schedule, the parties submitted pre-filed direct, rebuttal and surrebuttal testimony, as well as a list of issues and statements of position thereon. The Commission held hearings on September 23 and 24, 2002.

III. Witnesses and Positions of the Parties

Southwestern Bell presented witnesses Thomas F. Hughes, John Regan, Jr. and Dr. Debra J. Aron. Mr. Hughes is employed by Southwestern Bell as Vice President - Regulatory for Missouri. (Ex. 4, Hughes Direct, p. 1). Mr. Regan is employed by SBC Management Services as Vice President of Business Services, Product Offering and Planning and has business services product offering and planning responsibilities for Southwestern Bell in Missouri. (Tr. Vol. 2, pp. 84-85.). Mr. Hughes and Mr. Regan testified in support of Southwestern Bell's proposed tariffs. Dr. Aron testified on behalf of Southwestern Bell to provide her views on the economic and antitrust principles that should be used in evaluating Southwestern Bell's winback proposals.

MCImetro Access Transmission Services, LLC, Brooks Fiber Communications of Missouri, Inc., and MCI WorldCom Communications, Inc, (collectively "WCOM"),

presented witness Don Price. Mr. Price is employed by WorldCom, Inc, as a Senior Manager – Competition Policy Western Region. (Ex. 8, Price Rebuttal, p. 1). Mr. Price testified in opposition to Southwestern Bell's proposed tariffs.

AT&T presented witness R. Matthew Kohly. Mr. Kohly is Regulatory Manager - Government Affairs for AT&T in Missouri. (Ex. 10, Kohly Rebuttal, p. 1). Mr. Kohly testified in opposition to Southwestern Bell's proposed tariffs.

Staff presented the testimony of witness Christopher C. Thomas. Mr. Thomas is a Regulatory Economist with the Staff. (Ex. 6, Thomas Rebuttal, p. 1). Mr. Thomas recommended that the Commission reject Southwestern Bell's proposed tariffs.

Public Counsel presented the testimony of Barbara A. Meisenheimer. (Ex. 7, Meisenheimer Rebuttal, p. 1). Ms. Meisenheimer is Chief Utility Economist for the Office of the Public Counsel. Ms. Meisenheimer testified that Southwestern Bell has failed to establish that the proposed tariffs comply with Missouri law.

IV. Findings of Facts

Southwestern Bell filed several revised tariff sheets in which it seeks to waive the nonrecurring service installation charge for certain eligible customers. In Case No. TT-2002-472, Southwestern Bell seeks to implement a residential promotion that would waive the nonrecurring service installation charge for residential CLEC customers who were previously served by Southwestern Bell and who chose to leave the CLEC and return to Southwestern Bell. (Ex. 2, Regan Direct, p. 3; Regan Schedule 2). In addition, Southwestern Bell would waive additional nonrecurring charges if the customer elects to subscribe to one of Southwestern Bell's popular packages, as outlined in the tariff sheet. The tariff contains eligibility requirements that the customer must meet in order to

receive the promotional waiver. In addition to having been a previous Southwestern Bell customer, the residential customer must:

- have purchased local exchange service from a competitive local exchange company (CLEC);
- not have had service disconnected for non-payment; and
- must not have any past due bills for regulated service owed to Southwestern Bell.

Ex. 2, Regan Schedule 2.

The residential promotion is not available to new Southwestern Bell customers, including current CLEC residential customers who did not previously have Southwestern Bell service, or to wireless customers. (Tr. 290, 317).

In Case No. TT-2002-473, Southwestern Bell proposes a business promotion that waives the nonrecurring service installation charge for certain eligible business customers. As with the residential promotion, this offer is available to business CLEC customers who were previously served by Southwestern Bell and who chose to leave the CLEC and return to Southwestern Bell. (Ex. 2, Regan Direct, pp. 3-4; Regan Schedule 3-1). However, in addition, the proposed business tariffs would also waive the nonrecurring service installation charge for business customers that are currently customers of CLECs but who had obtained service previously from Southwestern Bell.

The tariff contains eligibility requirements that the customer must meet in order to receive the promotional waiver. In addition, the business customer must:

- have purchased local exchange service from a competitive local exchange company (CLEC);
- not have had service disconnected for non-payment; and
- must not have any past due bills for regulated service owed to Southwestern Bell.

Ex. 2, Regan Schedule 3-1.

The business promotion is not available to all new subscribers of Southwestern Bell services. It is only available to those new subscribers who currently obtain service from a CLEC. (Tr. 281).

Southwestern Bell claims that it is offering the winback offers to all similarly situated customers. (Ex. 4, Hughes Direct, p. 2; Ex. 5, Hughes Surrebuttal, pp. 7-8). Southwestern Bell presents no factual evidence to support the assertion that the customers eligible for these winback offers (CLEC customers) are not similarly situated with it other new customers. (*See* Ex. 4, Hughes Direct, p. 2; Ex. 5, Hughes Surrebuttal, pp. 4, 8; Ex. 6, Thomas Rebuttal, p. 6; Ex. 10, Kohly Rebuttal, p. 8; Tr. 559). Nor does it present any evidence to support why these customers represent a unique class of customers. (*Id.*).

The ineligible customers are similarly situated with the eligible customers in terms of the nature and terms of service the customers seek from Southwestern Bell. The services covered by the promotions are the same for both eligible and ineligible customers (i.e., both customers are seeking like and contemporaneous service). (Ex 10, Kohly Rebuttal, p. 8; Ex. 6, Thomas Rebuttal, p. 6; Tr. 559). Also, both eligible and ineligible customers are located in Southwestern Bell's local service territory, are not presently served by Southwestern Bell, and are making the same purchase decision (i.e., whether or not to purchase service from Southwestern Bell). (Ex 10, Kohly Rebuttal, p. 8).

Southwestern Bell's witness Hughes admits that it is the wording of Southwestern Bell's tariff that, in Southwestern Bell's view, determines that the customers are not similarly situated. (Tr. 316).

Southwestern Bell is attempting to segment its customers based upon their willingness to pay. (Ex. 6, Thomas Rebuttal, p. 8). To allow price discrimination without cost justification would run contrary to the legislative goals of universal service and of bring the benefits of competition to every Missouri citizen. (Ex. 6, Thomas Rebuttal, p. 8)

While Southwestern Bell concedes that cost reasons did not drive Southwestern Bell's decision to limit these winback offers to the targeted customers and Southwestern Bell claims it is not required to show a cost basis for the different rate it seeks to offer to the eligible winback customers, Southwestern Bell attempts to offer a cost justification for its proposed offers. Southwestern Bell claims that unlike new customers, there are no network costs associated with switching a CLEC customer back to Southwestern Bell where the CLEC is serving the customer via resale or UNE-P. (Tr. 321; Ex. 5, Hughes Surrebuttal, p. 10). Southwestern Bell presents no evidence or cost studies to support this claim (Tr. 326), Southwestern Bell concedes that there would be central office costs to convert these customers back to Southwestern Bell. (Tr. 353). In addition, when Mr. Hughes is confronted with examples involving customers served by CLECs through other means, he admits that customers who obtain services from a CLEC using unbundled loops would require central office and some field work by Southwestern Bell to convert them back to Southwestern Bell. (Id.) Mr. Hughes also admits that he completely ignored conversions from facilities-based CLECs. (Tr. 354). Mr. Kohly claims that there are circumstances where " the costs of reacquiring an eligible customer served by a competitor might actually be higher than the costs of initiating service with a new customer. (Ex. 10, Kohly Rebuttal, pp. 6-7).

The Missouri Commission has never "approved" any of the prior winback tariffs – it allowed them to go into effect. (Tr. 301, 654.)

Southwestern Bell continues to possess significant market power, and it has the ability and the incentive to utilize its market power in ways that are harmful to the competitive process and, over the long run, to Missouri telecommunications users. (Ex.9, Price Rebuttal, p. 3).

Prior to the passage of the Act, Southwestern Bell provided local telecommunications services to customers under a protected legal monopoly regime, with no risk of competitive challenge, using a network financed by captive ratepayers at virtually no risk to Southwestern Bell and its shareholders. When Southwestern Bell's legal monopoly was abolished, Southwestern Bell inherited an existing, ubiquitous network with links to every business and residential premises in its service territory. (Ex.9, Price Rebuttal, p. 4).

Southwestern Bell still retains overwhelming control of the local market with an 85 to 88% market share. (Ex. 4, Hughes Direct, pp. 6-9; Tr.375). Southwestern Bell claims there are 78 CLECs operating in Missouri. (Tr. 416). Based upon Southwestern Bell's evidence, CLEC have obtained a collective market share of 12 to 15%. (Tr. 456). As Staff witness Thomas noted, while "market share loss figures may evidence that competition is moving forward, it is not an indication of a significant change in the relative market position of the players in the marketplace." (Ex. 6, Thomas Rebuttal, p. 4). As Staff witness Thomas explained:

> The Commission should not confuse functioning competition with loss of market share. If the Commission's goal is to substitute competition for regulation, wherever possible, it is important to note that loss of market share and functioning competition are two very different concepts.

> Southwestern Bell can lose market share to CLECs without competition serving as effective price control. Many CLECs rely primarily on the use of UNEs and resale to provide service and Southwestern Bell's obligations to provide such elements could be removed at any point. As Staff has indicated in previous cases on this issue, local markets are not yet at a point where competition can successfully substitute for regulation.

(Ex. 6, Thomas Rebuttal, p. 5).

While competition may be increasing, as Mr. Kohly indicates, it is not increasing at the pace one would expect (Tr. 654-55), and it not at a level where it is disciplining the local market. (Ex. 6, Thomas Rebuttal, p. 5). Competition remains vulnerable to interference by Southwestern Bell. As Mr. Kohly explained:

> successful entry into the local exchange market requires a new entrant to achieve a sufficient amount of business to offset the significant capital investment required to off local service. Whether the CLEC is using unbundled elements or its own facilities, CLECs entering the market must make large up-front investments before they can begin offering service. A new entrant's decision to enter and expand (and its corresponding ability to obtain financing through today's capital markets) is, therefore, based on its expectation that it will be able to recover, within a reasonable time frame, its cost of these up-front investments, along with the on-going costs of providing services, plus a reasonable return on its investment. Southwestern Bell, the incumbent provider, has already sunk the large percentage of its costs associated with its network (costs that were largely funded by ratepayers) and has a customer base that allows it to benefit from significant economies of scale, resulting in lower marginal costs for the incumbent.

Ex. 10, Kohly Rebuttal, p. 13.

As the incumbent, Southwestern Bell has the long-term incentive to deprive entrants of the opportunity to achieve significant economies of scale to keep its rivals cost higher than its own. (*Id.*) By limiting the eligibility of a promotion to the narrow segment of CLEC customers, Southwestern Bell will still be able to maintain high rates or even increase rates for the vast majority of other customers while limiting price reductions to only those customers that have sought competitive choice during these

initial stages of competition. These targeted eligibility limitations make it much less costly for Southwestern Bell to engage in the limited price competition aimed exclusively at CLEC customers. (*Id.*, p. 14.) Meanwhile, the competing CLECs will have to reduce rates for all customers in order to compete with Southwestern Bell as once that CLEC gains a customer, that customer is immediately eligible for Southwestern Bell's promotional rates. (Id.) In essence, Southwestern Bell's proposed tariffs would permit Southwestern Bell to fund its targeted competitive response from revenues derived from other Southwestern Bell customers. (Ex 10, Kohly Rebuttal, pp. 13-14; Ex. 7, Meisenheimer Rebuttal, p. 8). Competitors do not have this luxury. (Ex 10, Kohly Rebuttal, pp. 13-14; Ex. 8, Price Rebuttal, pp. 18-19). If permitted, this would unreasonably impede competition.

By targeting CLEC customers, Southwestern Bell's offer will also have the effect of inhibiting the CLECs ability to recover its initial capital investments and expand and could lead to significant stranded investment. (Ex. 10, Kohly Rebuttal, pp. 15-16).

Southwestern Bell begins sending winback letters to customers that have converted to CLECs within 2 days of the customer switching to the CLEC. (Tr. 202-05). For residential customers, Southwestern Bell continues this letter campaign until the customer converts or Southwestern Bell sends at least 9 letters, whichever comes first. (Tr. 205). At the same time, Southwestern Bell, through third party telemarketers and its internal recorded message system, begins contacting the CLEC customer through phone calls. (Tr. 206-09).

In addition, the first letter sent to the CLEC customer seeks to cast doubt on the CLECs conversion on the customer by seeking to "determine if the customer has been

slammed." (Ex. 3, Regan Surrebuttal, p. 5; Tr. 199, 213-14; Ex. 14 and 15). Southwestern Bell provides no explanation or definition of the term "slammed" to the customer in the letter, but encourages the customer to contact an 800 number in the Southwestern Bell retail winback group. (*Id.*). Southwestern Bell has no access to any information to determine if the CLEC used proper third party verification procedures or if the person contacting Southwestern Bell was even the person that authorized the initial switch to the CLEC. Rather, Southwestern Bell simply takes the customer at his word. (Tr. 201-02).

V. Conclusions of Law.

The Missouri Public Service Commission has reached the following conclusions of law.

Southwestern Bell is a "Telecommunications Company" as that term is defined in Section 386.020(51), and is subject to the jurisdiction of the Commission pursuant to Section 386.250

Section 392.230.3, RSMo 2000, grants the Commission the authority to determine, after hearing, the propriety of any rate, rental, charge, regulation, or practice filed with the Commission by any telecommunications company. That same section authorizes the Commission to suspend the operation of such rate, rental, charge, regulation, or practice for a period of 120 days, plus an additional six months if the hearing regarding such suspension cannot be concluded within 120 days.

In 1996 the Missouri General Assembly passed legislation aimed at promoting competition in Missouri's telecommunications industry. Section 392.185, RSMo 2000, which establishes the purpose of that legislation, states that:

> The provisions of this chapter shall be construed to: (3) Promote diversity in the supply of telecommunications services and products throughout the state of Missouri; (6) Allow full and fair competition to function as a substitute for regulation when consistent with the protection of ratepayers and otherwise consistent with the public interest.

Therefore, the Public Service Commission has a duty to regulate Missouri's telecommunications industry in such a way as to promote the development of full and fair competition.

Section 392.200.2, RSMo 2000, provides in pertinent part as follows:

> No telecommunications company shall directly or indirectly or by a special rate, rebate, drawback or other device or method charge, demand, collect or receive from any person or corporation a greater or less compensation for any service rendered or to be rendered with respect to telecommunications or in connection therewith, except as authorized in this chapter, than it charges, demands, collects, or receives from any other person or corporation for doing a like and contemporaneous service with respect to telecommunications under the same or substantially the same circumstances and conditions. Promotional programs for telecommunications services may be offered by telecommunications companies or periods of time so long as the offer is otherwise consistent with the provisions of this chapter and approved by the commission.

This statute imposes an obligation on the Commission to review promotional offers made by telecommunications companies to ensure that those offers are compliant with the provisions of statute, consistent with the overarching obligation to ensure the development and preservation of full and fair competition.

Section 392.200.3, RSMo 2000, provides as follows:

> No telecommunications company shall make or give any undue or unreasonable preference or advantage to any person, corporation or locality, or subject any particular person, corporation or locality to any undue or unreasonable prejudice or disadvantage in any respect whatsoever except that telecommunications messages may be classified into such classes as are just and reasonable, and different rates may be charged for the different classes of messages.

This statute has been interpreted to "forbid discrimination in charges for doing a like or contemporaneous service with respect to communication by telephone under the same or substantially the same circumstances and conditions." *State ex rel. DePaul Hospital v. PSC*, 464 S.W.2d 737, 740 (Mo. App. 1970). Rate differences are permitted only if there is any "reasonable and fair difference in condition which equitably and logically justifies a different rate." *Id.*

The Commission has previously found, as a matter of fact, that Southwestern Bell's proposed promotional tariffs will be detrimental to the health and development of competition in Missouri's local exchange market. *See, e.g.*, Report and Order , Case Nos. TT-2002-108 and TT-2002-130. The tariffs at issue here are therefore unjust and unreasonable. In keeping with the Commission's obligation under Section 393.200, RSMo 2000, the Commission must reject Southwestern Bell's tariffs.

VI. Decision.

After applying the facts as it has found them to its conclusions of law, the Commission has reached the following decisions regarding the issues identified by the parties:

ISSUE 1: Should the Commission approve Southwestern Bell's proposed revision to Local Exchange Tariff PSC Mo-24 to offer a waiver of Service and Equipment Charges to residential customers who have disconnected their access lines with Southwestern Bell for the purpose of establishing service with another LEC within the Southwestern Bell service area and who now wish to return to service with Southwestern Bell?

ISSUE 2: Should the Commission approve Southwestern Bell's proposed revision to Local Exchange Tariff PSC Mo-24, Sections 2 and 3 of the Integrated Services Tariff PSC Mo-41 and Section 38 of the General Exchange Tariff PSC Mo-35 to offer a waiver of Service and Equipment Charges to business customers who have disconnected their access line with Southwestern Bell for the purpose of establishing service with another LEC within the Southwestern Bell service area and who now wish to return to service with Southwestern Bell?

Southwestern Bell argues that its tariffs should not be rejected for five reasons. The Commission is not persuaded by any of Southwestern Bell's arguments.

Southwestern Bell's first argument is that its proposed residential and business winback tariff revisions are being offered to all similarly situated customers. Southwestern Bell contends that the customers that it has designated as eligible for the winback promotions, the CLEC customers, is a unique class of customers. The Commission disagrees. The services covered by the promotions are the same for both eligible and ineligible customers. Both customers are seeking like and contemporaneous service. Also, both eligible and ineligible customers are located in Southwestern Bell's local service territory, are not presently served by Southwestern Bell, and are making the same purchase decision (i.e., whether or not to purchase service from Southwestern Bell). In short, the ineligible customers are similarly situated with the eligible customers in terms of the nature and terms of the service the customers seek from Southwestern Bell. There is no reasonable difference in the conditions under which the service at issue is being offered that would justify the eligibility limitations in the proposed tariffs.

Southwestern Bell's interprets Section 392.200 too broadly. The statute does not give Southwestern Bell the discretion to establish any arbitrary service or rate classification simply by defining a class of customers in a tariff. Stricter scrutiny of the service and rate classification is mandated under Missouri law. Southwestern Bell's tariffs do not pass this scrutiny. Southwestern Bell's tariffs seek to waive charges for like and contemporaneous services under the same or substantially the same circumstances and conditions to a subset of customers rather than all similarly situated customers. In light of these facts and the Commission's conclusion herein that Southwestern Bell's

tariffs would impede the development of competition in the local service market in Missouri, SWBT tariffs are not in compliance with Sections 392.200.2 and 392.200.3.

Even without this statutory concern, Southwestern Bell's winback offers are not reasonable or just. Southwestern Bell is attempting to improperly segment its customer, based upon their willingness to pay. To allow price discrimination without cost justification would run contrary to the legislative goals of universal service and would deprive all Missouri customers.

While Southwestern Bell concedes that cost reasons did not drive Southwestern Bell's decision to limit these winback offers to the targeted customers and Southwestern Bell claims it is not required to show a cost basis for the different rate it seeks to offer to the eligible winback customers, it attempts to suggest that there is such a cost difference. Southwestern Bell has presented no evidence to support any cost justification for its winback offers. The evidence presented in the hearing by other parties raises serious questions of any cost justification for these offers.

Southwestern Bell's second argument is that its winback promotions offer benefits to customers of lower prices. Again, while these offers may benefit individual customers, at least in the short term, the Commission has found that Southwestern Bell's offers are a threat to the long-term health of the competitive market for local phone service. Ultimately, if the market fails, customers will be left with no choice except Southwestern Bell.

Third, Southwestern Bell argues that its winback offers are being made in response to the demands of its customers. Southwestern Bell asserts that customers expect Southwestern Bell to waive the nonrecurring service installation charge if the

customer returns to Southwestern Bell. The Commission does not doubt that there are customers that want these charges waived and there will be demand for the offers that Southwestern Bell would like to make available. Customers are interested in getting the lowest price they can get. They are not necessarily concerned about the health of competition in Missouri. That is one of this Commission's charges. The Commission must protect the interest of all consumers and the public interest in general. In addition, the Commission is obligated to protect the viability of the competitive market in order to protect Missouri's telecommunications customers from the threat of monopoly power until the market is sufficiently competitive that the competitive market will discipline the market and the participants in the market, not the Commission.

Southwestern Bell's fourth argument is that its winback offers are in response to the competitive market and its proposed offers will increase rather than harm competition. Southwestern Bell argues that this Commission and the Federal Communications Commission have recently found that Southwestern Bell has opened its local market in Missouri to competition when they approved Southwestern Bell's application to provide interLATA long distance service in Missouri. Southwestern Bell also points to the fact that CLECs are offering competitive services in its exchanges, testimony indicated that approximately 12 to 15 percent of the local market is now controlled by CLECs.

While this Commission and the FCC have found that Southwestern Bell satisfied the fourteen-point checklist found in Section 271 of the Telecommunication Act of 1996,[10] that finding only indicates that the local telecommunications market in Missouri is open to competition. It does not mean that the competitive market is mature

enough to withstand the pressures that would be placed on it by the winback offers proposed by Southwestern Bell. It does not mean that the market is sufficiently competitive to discipline Southwestern Bell's pricing, policies and practices. Unless the Commission acts to protect competition, the local exchange market may be open to competition, but have no surviving competitors.

Southwestern Bell's fifth argument is that its winback offers are consistent with previous decisions of this Commission. Southwestern Bell presented evidence at the hearing of twelve tariffs containing winback offers of Southwestern Bell that the Commission allowed to go into effect..

Southwestern Bell is correct when it contends that the Commission has previously allowed tariffs containing provisions similar, or nearly identical to the provisions that it is rejecting in this order to go into effect. However, the Commission is not bound to comply with its previous decisions. As an administrative agency the Commission is not bound by stare decisis, [*State ex rel. GTE North v. PSC*, 835 S.w.2d 356 (Mo. App. W.d. 1992)] and the failure of the Commission to explain why it is not taking the same position in one case that it took in a previous case is not a basis for overturning the Commission's action. (*Id.*). Furthermore, only these two tariffs are currently before the Commission. In finding that these two particular tariffs will harm competition, the Commission is not attempting to establish a rule with application beyond the facts of these cases. If other tariffs are brought to the attention of the Commission, the Commission will deal with those tariffs on their own merits. Similarly, the Commission will examine on their own merits tariffs submitted by CLECs that may contain term or volume discounts, or save or winback provisions.

In addition, the Commission finds that SWBT's winback procedures could create customer confusion and do not allow the customer to gain any experience with the CLEC before SWBT begins its winback efforts. Further, SWBT should not be policing its competitors' customer conversions. Such practices will undermine the development of competition in Missouri and are not in the public interest and provide further support for the rejection of the tariffs at issue here.

Sound public policy requires that the Commission take the steps necessary to preserve the existence of the competitive market for local exchange telecommunications services in Missouri. Based on the evidence, the arguments of the parties, the Commission's Findings of Fact and its Conclusions of Law, the Commission determines that Southwestern Bell's winback offers in these two tariffs are contrary to Missouri law, are unjust and unreasonable and will impede the development of competition in Missouri and should, therefore, be rejected.

IT IS THEREFORE ORDERED:

1. That the proposed tariff sheet submitted on March 29, 2002, by Southwestern Bell Telephone Company, and assigned Tariff No. 200200831, is rejected. The tariff sheet rejected is:

P.S.C. Mo. – No. 24
Local Exchange Tariff
3rd Revised Sheet 2

2. That the proposed tariff sheets submitted on March 29, 2002, by Southwestern Bell Telephone Company, and assigned Tariff No. 200200828, are rejected. The tariff sheets rejected are:

P.S.C. Mo. – No. 24

Local Exchange Tariff
3rd Revised Sheet 1.03

P.S.C. Mo. – No. 35
General Exchange Tariff
Section 38
1st Revised Sheet 15

P.S.C. Mo. – No. 41
Integrated Services Tariff
Section 2
1st Revised Sheet 6.03

P.S.C. Mo. – No. 41
Integrated Services Tariff
Section 3
1st Revised Sheet 14.02

3. That this Report and Order shall become effective on _____, 2002.

BY THE COMMISSION

Dale Hardy Roberts
Secretary/Chief Regulatory Law Judge

(S E A L)