

STATE OF TENNESSEE

Office of the Attorney General



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May 23, 2003

Chairman Sara Kyle
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, Tennessee 37243

**RE: BELLSOUTH TELECOMMUNICATIONS, INC. TARIFF FILING FOR
CONTRACT SERVICE ARRANGEMENTS, Docket Nos. 02-00534, 02-
00536 through 02-00545, 02-00550 through 02-00561, 02-00571 through 02-
00580, 02-00598 through 02-00607, 02-00614-02-00615, 02-00627 through 02-
00632, 02-00656 through 02-00662, 02-00669 through 02-00680**

Dear Chairman Kyle:

Enclosed is an original and thirteen copies of the Consumer Advocate and Protection Division of the Office of the Attorney General's Motion for Leave to File a Supplemental Complaint and Petition to Intervene and the attached Supplemental Complaint and Petition to Intervene for filing in the above-referenced matter. If you have any questions, kindly contact me at (615) 532-3382. Thank you.

Sincerely,

A handwritten signature in dark ink, appearing to read "T. Phillips", written over the printed name.

TIMOTHY C. PHILLIPS
Assistant Attorney General

Enclosures

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**BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE**

**IN RE: BELL SOUTH
TELECOMMUNICATIONS, INC.
TARIFF FILING FOR CONTRACT
SERVICE ARRANGEMENTS**

) Docket Nos. 02-00534, 02-00536 through
) 02-00545, 02-00550 through 02-00561,
) 02-00571 through 02-00580, 02-00598
) through 02-00607, 02-00614-02-00615,
) 02-00627 through 02-00632, 02-00656
) through 02-00662, 02-00669 through 02-
) 00680

SUPPLEMENTAL COMPLAINT AND PETITION TO INTERVENE

Comes now Paul G. Summers, the Attorney General and Reporter for the State of Tennessee, through the Consumer Advocate and Protection Division of the Office of Attorney General (hereinafter "Consumer Advocate"), pursuant to Tenn. Code Ann. § 65-4-118(c)(2)(A) and Rule 1220-1-2-.22(2) of the Tennessee Regulatory Authority (hereinafter "TRA"), and hereby files this Supplemental Complaint and Petition to Intervene on behalf of the public interest because consumers may be adversely affected by actions taken in the above-styled dockets. For cause, the Consumer Advocate would show unto the TRA as follows:

1. The Consumer Advocate has a duty and the authority under Tenn. Code Ann. § 65-4-118(c)(2)(A) to represent the interests of Tennessee consumers of public utility services and to initiate, participate or intervene in proceedings to represent the public interest in accordance with the Uniform Administrative Procedures Act.
2. Additionally, under Tenn. Code Ann. § 8-6-109, the Office of Attorney General has the duty and authority to attend to all business of the state.
3. BellSouth Telecommunications, Inc. (hereinafter "BellSouth") is a telecommunications utility regulated by the TRA pursuant to Title 65, Chapters 4 and 5, *Tennessee*

Code Annotated. BellSouth's usual address for service is 333 Commerce Street, Nashville, Tennessee 37201-3300.

4. BellSouth filed these Contract Service Arrangements ("CSAs") seeking approval to offer select business customers service arrangements that depart from the general tariffs. Current TRA Rule 1220-4-1-.07 permits such special contracts not covered by or permitted in the general tariffs, subject to supervision, regulation and control of the TRA.

5. On August 2, 2002, the Consumer Advocate filed its Complaint and Petition to Intervene ("Original Petition"), in which the Consumer Advocate alleged that: (1) BellSouth has not shown that the circumstances surrounding its CSAs are special or unique enough to warrant departure from the general tariffs; (2) BellSouth has not shown that its CSAs are made generally available to similarly-situated customers that purchase like services; and (3) BellSouth has not provided customers with the information necessary to properly evaluate CSA offerings in order to ascertain if they are similarly situated with other customers that receive discounted rates via CSAs.

6. The TRA found that the issues raised in the Original Petition were similar to some of the issues under consideration in the TRA's then ongoing rulemaking proceeding concerning special contracts and tariff term arrangements, Docket No. 00-00702.

7. Specifically, within the context of its rulemaking proceeding, the TRA was in the process of addressing appropriate regulations to assure that a telecommunications provider's program of special contracts and term arrangements was in compliance with: (1) the policy against unjust price discrimination among similarly-situated customers that purchase like telecommunications services, *see* Tenn. Code Ann. §§ 65-4-122 and 65-5-204; (2) the policy to make filings with state agencies generally available for public inspection pursuant to the Public Records

Act, *see* Tenn. Code Ann. § 10-7-503; and (3) the common law policy against imposing liquidated damages that impermissibly penalize a person for terminating a contract in favor of an alternative arrangement, *see Guiliano v. Cleo, Inc.*, 995 S.W.2d 88 (Tenn. 1999), *see also Testerman v. Home Beneficial Life Ins. Co.*, 524 S.W.2d 664 (Tenn. Ct. App. 1974).

8. Because of the similarities in the two cases, the TRA decided to hold the Original Petition in abeyance, and to allow BellSouth's CSAs to become effective pending the outcome of the rulemaking proceeding.

9. The Consumer Advocate participated in the rulemaking proceeding, and filed comments urging the TRA to adopt rules to assure that: (1) similarly-situated customers have a realistic opportunity to receive the same rates and terms for like telecommunications services; (2) telecommunications providers file in the public records of the TRA sufficient information concerning discounted rates so that consumers may adequately evaluate special contract offerings and make informed choices; and (3) the liquidated damages provisions in special contracts and term arrangements for telecommunications services do not exact impermissible penalties from customers that desire to cancel their service agreements, or unreasonably deter customers from terminating their service agreements in favor of competitive service alternatives. *See, e.g., Consumer Advocate Brief in Support of Adoption of Regulations for Special Contracts and Term Arrangements for Telecommunications Services*, Docket No. 00-00702 (Feb. 18, 2003).

10. While the Original Petition and the rulemaking proceeding were pending, the General Assembly passed Public Chapter No. 41, which provides that special rates and terms negotiated between telecommunications providers and business customers shall not constitute price discrimination and shall be presumed valid. The Governor approved this new legislation on April

23, 2003.

11. At the TRA Conference held on May 12, 2003, the TRA decided to close the rulemaking proceeding in recognition of the enactment of Public Chapter No. 41, and in recognition of its finding that any unresolved issues and claims relative to special contracts and term arrangements could be addressed sufficiently through the agency's contested case process.

12. Prior to the TRA's closing of the rulemaking proceeding, the Consumer Advocate was working under the belief that all issues relative to special contracts generally, including BellSouth's CSAs, would be addressed in the rulemaking proceeding.

13. Due to the intervening actions of the General Assembly and the TRA, the Consumer Advocate files this Supplemental Complaint and Petition to Intervene in order to bring before the TRA in one pleading the unresolved issues and claims that the Consumer Advocate has raised relative to BellSouth's CSAs in the Original Petition, and relative to special contracts generally in the rulemaking proceeding that are also applicable to BellSouth's CSAs. Accordingly, this pleading is intended to replace the Original Petition in its entirety.

14. With respect to the Consumer Advocate's prior claim that BellSouth has not shown any special circumstances that justify a departure from its general tariffs (*see* ¶5, *supra*), the Consumer Advocate is of the opinion that Public Chapter No. 41, if applied retrospectively to these contracts, substantially mitigates this claim.

15. The new legislation provides that special rates and terms negotiated between telecommunications providers and business customers, such as those contained in BellSouth's CSAs, shall be presumed valid. Accordingly, the new legislation contemplates such departures from the general tariffs.

16. While the doctrine against retrospective application of the law may prevent this claim from being mooted, the Consumer Advocate realizes that litigation of this claim may not have any significant impact on the TRA's future regulation of BellSouth's CSAs and similar contracts of other telecommunications providers. Therefore, the Consumer Advocate simply requests that the TRA address the retroactivity question in its final order.

17. With respect to the Consumer Advocate's prior claim that BellSouth has not shown that its CSAs are made generally available to similarly-situated customers that purchase like services (*see* ¶5, *supra*), the Consumer Advocate is of the opinion that enactment of Public Chapter No. 41, if applied retrospectively to these contracts, substantially mitigates this claim.

18. The new legislation appears to remove unjust price discrimination as a viable legal claim that consumers may use to challenge special rates and terms negotiated between telecommunications providers and business customers.¹ In other words, if a telecommunications provider negotiates a discounted rate with one business customer, another similarly-situated customer that purchases the same service is not entitled under the new law to the same discounted rate. Accordingly, pursuant to the changes in the law effectuated by Public Chapter No. 41, consumers are now unable to receive discounted rates by challenging such practices of telecommunications providers on the basis of unfair or unjust price discrimination.

¹ Notwithstanding the enactment of Public Chapter No. 41, the state's policy against unjust discrimination among similarly-situated customers remains applicable to a telecommunications provider's tariff offerings. The new legislation makes it clear that a telecommunications provider may engage in what would otherwise be unjust price discrimination only when the telecommunications provider and the business customer individually negotiate special rates and terms that are not offered in the tariffs. Unjust price discrimination, however, remains a viable legal claim under state law with respect to general tariff offerings, and under federal law with respect to both tariff offerings and special contract arrangements.

19. Although it is doubtful that the unjust price discrimination issue could be mooted by the retrospective application of Public Chapter No. 41, the Consumer Advocate sees no compelling reason to litigate this claim under state law as such litigation would likely have little impact on the TRA's regulation of CSAs in Tennessee's present legal and regulatory environment.² The Consumer Advocate simply requests that the TRA address the retroactivity question in its final order.

20. The Consumer Advocate is also concerned about the anti-competitive effects that BellSouth's CSAs may have on the development of robust competition in local telecommunications markets.

21. A dominant firm possesses a majority of the market share and may stave off competitors that desire to enter the market or expand their market shares by executing contracts with its customers. This is so because these contracts result in legal obligations that bind the customer to the dominant firm. The dominant firm may exercise even greater control by designing its system of contracts to allow for: (a) the execution of multi-year contracts that result in long-term commitments; (b) the inclusion of termination liability provisions which require the customer to pay cancellation fees if the customer desires to select a competitive alternative; and (c) the execution of contracts for higher-margin services or with larger-volume customers, both of which are more likely to attract new entrants into the market. Such conduct by a dominant firm impedes the development

² It should be noted that consumers may still pursue claims of unjust price discrimination against a telecommunications provider if the provider negotiates special rates and terms for interstate services that are provisioned to a similarly-situated customer. This is so because Tennessee's new legislation, which authorizes negotiation of certain rates and terms for intrastate services without regard to the state's policy against unjust price discrimination, is inconsistent with federal laws that prohibit such unfair or unjust practices by telecommunications providers that are regulated by the Federal Communications Commission. *See* 47 U.S.C. §§ 201 and 202. Accordingly, the claim of unjust price discrimination remains viable for challenging contracts that deliver interstate telecommunications services to select customers.

of competitive markets.

22. BellSouth is the dominant provider of telecommunications services in Tennessee.³ BellSouth's CSAs result in multi-year service agreements with its business customers, and these CSAs contain liquidated damages provisions which require the customer to pay fees in order to cancel the service commitment in favor of a competitive alternative. Moreover, based on available information and belief, the Consumer Advocate avers that many of BellSouth's CSAs are arrangements to provide high-speed data services and other higher-margin business services, and many other CSAs are so-called "volume and term" service arrangements with some of BellSouth's larger customers.

23. Accordingly, the Consumer Advocate is concerned about the potential anti-competitive effects that BellSouth's system of CSAs may have on the development of competition in local telecommunications markets. Our concerns in this regard are exacerbated by the ever-growing number of BellSouth business customers that enter into multi-year service commitments via CSAs.

24. It is Tennessee's policy to foster the development of an efficient, technologically advanced, statewide system of telecommunications services by permitting competition in all telecommunications services markets. *See* Tenn. Code Ann. § 65-4-123. The TRA has the power to investigate BellSouth's CSA practices and enter appropriate orders to assure the development of competitive telecommunications markets. *See* Tenn. Code Ann. §§ 65-4-104 and 65-5-208(c).

25. The Consumer Advocate is therefore of the opinion that the TRA should investigate

³ According to Glenn Bischoff's article entitled *FCC Stats Refute RBOCs' Plea for Relief* published in the December 16, 2002, issue of *Telephony*, the competing carriers' cumulative market share in Tennessee was 7% as of June 2002, which ranks among the bottom states for competitors.

and monitor BellSouth's use of CSAs in order to determine whether its system of delivering contracted services to certain business customers is an impediment to the development of competition in contravention of the state's telecommunications policy.

26. With respect to the Consumer Advocate's prior claim that BellSouth's customers do not have the information necessary to properly evaluate CSA offerings (*see* ¶5, *supra*), the Consumer Advocate is of the opinion that certain aspects of this claim are neither mooted nor significantly mitigated by the enactment of Public Chapter No. 41.

27. The new legislation specifically provides that special rates and terms negotiated between telecommunications providers and business customers shall be filed with the TRA. Consistent with the Public Records Act, such special rates and terms must be made available for public inspection.

28. It is universally accepted that those who possess timely and pertinent information are better able to negotiate favorable deals than those without such information. While business customers are apparently no longer entitled to the discounted rates that similarly-situated customers receive, public disclosure of such special rates and terms, as contemplated by Public Chapter No. 41 and the Public Records Act, will significantly assist consumers by enhancing their ability to negotiate special rates and terms of service. Accordingly, the public disclosure of these special rates and terms is in the interests of consumers.

29. To allow business consumers the opportunity to adequately prepare for negotiation of special contracts for telecommunications services, they should be provided with access to such information so that they may effectively evaluate and compare specific contract offers with other service alternatives. The special rates and terms that are disclosed to these consumers should include

such basic information as the name of the business customer executing the contract, a sufficient description of the contracted service, the quantity or volume of the contracted service, the contract price and related amount of discount, the length of the service term commitment, and the location where the service is provisioned. If business consumers are not provided with such basic information, they could be disadvantaged as they enter into negotiations with telecommunications providers for special rates and terms of service.

30. Another reason to publicly disclose the special rates and terms negotiated between an incumbent telecommunications provider and its business customer is to provide resellers of the incumbent's service with sufficient notice and information so that such resellers may have a realistic opportunity to resell the contracted services to the business customer.

31. Consistent with the federal Telecommunications Act of 1996, the TRA requires BellSouth to make its CSAs available for resale. *See Second and Final Order of Arbitration Awards*, Docket Nos. 96-01152 and 96-01271 (Jan. 23, 1997).

32. BellSouth has not disclosed all of the special rates and terms of service associated with these CSAs. Specifically, based upon available information and belief, the Consumer Advocate avers that BellSouth has not publicly disclosed in all instances the names of the business customers executing the contracts, the quantities or volumes of the contracted services, and the locations where the services are provisioned.

33. The Consumer Advocate also has asserted, within the context of the now closed rulemaking proceeding, that the termination liability provisions in the special contracts of telecommunications providers should be reviewed for consistency with the common law rule pertaining to liquidated damages.

34. This rule provides that liquidated damages are enforceable only if: (1) the liquidated sum is a reasonable estimate of compensatory damages in case of breach; and (2) actual damages for contractual breach are indeterminable or difficult to ascertain at the time the contract was formed. *See V.L. Nicholson Co. v. Transcon Inv. And Fin., Ltd., Inc.*, 595 S.W.2d 474, 484 (Tenn. 1980). The prospective approach should be utilized to evaluate the validity of liquidated damages clauses, which requires examination of the circumstances at the time of contract formation, as opposed to the time of breach. *See Guiliano v. Cleo, Inc.*, 995 S.W.2d 88, 100 (Tenn. 1999).

35. The public policy rationale behind the liquidated damages rule is straightforward. Because breach of contract is not viewed as tortious behavior, the rule is in place to assure that the breaching party is not impermissibly penalized by the non-breaching party. Accordingly, a liquidated damages clause that penalizes rather than compensates is invalid. *See Testerman v. Home Beneficial Life Ins. Co.*, 524 S.W.2d 664, 668 (Tenn. Ct. App. 1974).

36. In a breach of contract case, the non-breaching party is entitled to recover its expectancy damages, which are usually expressed as: (1) the value of the contract that the non-breaching party has lost by reason of the other party's breach; plus (2) incidental or consequential losses, such as the costs the non-breaching party has incurred in carrying out its own performance; less (3) any costs or other losses that the non-breaching party has avoided by not having to perform. *See BVT Lebanon Shopping Ctr., Ltd. v. Wal-Mart Stores, Inc.*, 18 S.W.3d 132, 136 (Tenn. 2001) (quoting Restatement (Second) of Contracts § 347 (1979)). In other words, the general contract remedy in Tennessee is to place the non-breaching party in as nearly as possible the same position had the contract been performed, but not a better one. *See Id.*

37. Accordingly, where the contract price and cost of performance over a fixed period

of performance are known or reasonably ascertainable when the contract is formed, a liquidated damages clause in the contract is ordinarily inappropriate and unenforceable because the non-breaching party's expectancy, or actual damages, are reasonably determinable from the outset of the contract.

38. These BellSouth CSAs contain liquidated damages provisions.

39. Based on available information and belief, the Consumer Advocate avers that, with respect to these CSAs, BellSouth either knows or can reasonably ascertain or calculate the price that the business customer is obligated to pay for the contracted service, the costs of providing the contracted service, and the length of the service term commitment. Because the contract price, cost of service, and fixed period of performance are the ordinary functions of actual damages, BellSouth can reasonably ascertain its breach of contract damages in the event of the customer's early termination of the CSA. Therefore, BellSouth's inclusion of liquidated damages provisions in the CSA is inconsistent with the liquidated damages rule.

40. Another problem with these liquidated damages provisions is that BellSouth has not shown that the liquidated sums resulting from the application of such provisions are a reasonable estimate of compensatory damages in the event of the customer's breach.

41. The liquidated damages provisions contained in BellSouth's CSAs require the payment of liquidated sums equal to: (a) the repayment of discounts received during the previous 12 months of service, or (b) 6% of the total contract amount or 24% of the average annual revenue for a contract with a term longer than four years.

42. The repayment of discounts that the customer receives off the normal, tariffed rate for contracted services appears to be an inappropriate method to estimate compensatory damages.

In the case of CSAs, the tariffed rate is not the market rate for contracted services because, as stated in the contracts themselves, these business customers have competitive alternatives available to them. Presumably, if discounts are not negotiated through CSAs, the customer will move service to a competitor that is offering a lower rate. It is unlikely that a liquidated damages provision that computes the liquidated sum based upon the tariffed rate results in a reasonable estimate of potential damages. This is so because BellSouth seeks compensation predicated upon a figure that the customer was never willing to pay, and that BellSouth never expected to collect from the outset of the contract.

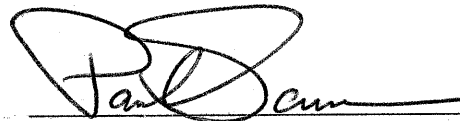
43. The 6% of total contract revenues and 24% of average annual revenues for contracts with a term longer than four years also appear to be inappropriate measures of potential damages. These provisions seem arbitrary because they uniformly appear in CSAs for various types and amounts of services without any tailoring to the specific circumstances of each case.

44. Based upon available information and belief, the Consumer Advocate avers that BellSouth has not produced any data or other analyses that relates the liquidated sums contained in its CSAs to the amount of actual damages that BellSouth will sustain on account of a customer's breach. It therefore cannot be reasonably concluded that such amounts represent a reasonable estimate of BellSouth's compensatory damages.

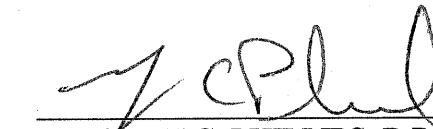
45. Accordingly, the liquidated damages provisions in BellSouth's CSAs are invalid and, therefore, should not be approved or allowed to become effective.

WHEREFORE, the Consumer Advocate prays that the TRA will continue to investigate and monitor the potential anti-competitive effects of BellSouth's system of CSAs; convene a contested case proceeding to evaluate the issues raised herein; grant the Consumer Advocate's Supplemental Complaint and Petition to Intervene; order BellSouth to publicly disclose all special rates and terms of its CSAs and direct BellSouth to make such disclosures on a going forward basis; order BellSouth to strike all invalid liquidated damages provisions from its CSAs and direct BellSouth to comport its contracting practices with the law relating to liquidated damages on a going forward basis; and grant the Consumer Advocate and the consumers of Tennessee such other relief as may be warranted by the evidence and applicable law.

RESPECTFULLY SUBMITTED,



PAUL G. SUMMERS, B.P.R. # 6285
Attorney General and Reporter



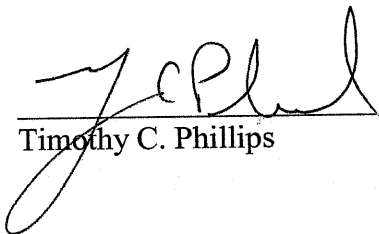
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Office of the Attorney General
Consumer Advocate and Protection Division
P.O. Box 20207
Nashville, Tennessee 37202
(615) 741-3533

Dated: May 23, 2003

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing Motion for Leave to File Supplemental Complaint and Petition to Intervene and attached Supplemental Complaint and Petition to Intervene was served on parties below via facsimile and U.S. Mail, postage prepaid, on the 23 day of May, 2003.

Guy M. Hicks, Esquire
General Counsel
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Nashville, Tennessee 37201-3300



Timothy C. Phillips

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