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

RECEIVED

**February 20, 2004**

T.R.A. DOCKET ROOM

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|---|---|---|
| *IN RE PETITION FOR ARBITRATION OF* | ) | *Docket No* 03-00119 |
| *ITC DELTACOM COMMUNICATIONS,* | ) | |
| *INC WITH BELLSOUTH* | ) | |
| *TELECOMMUNICATIONS, INC* | ) | |

## FINAL BEST OFFER

As directed by the Authority, ITC^DeltaCom Communications, Inc ("ITC^DeltaCom") hereby submits the following final best offers as to the remaining issues in the above-captioned arbitration proceeding

**Issue 2: Directory Listings**

ITC^DeltaCom provides the following offer

For initial "load" of base file, $ 04 per listing defined as ITC^DeltaCom subscriber
For updates, those listings which have been changed $ 06 each

In accordance with attached tariff pages A 38 2 Directory Publishers Database Service, ITC^DeltaCom proposes that the state Commission rates be applied as this is a comparable service

BellSouth has indicated that the source of the listing information is the LIST system, it is our understanding that BellSouth can withhold ITC^DeltaCom's listings from third party publishers Given this, BellSouth should be able to carve out ITC^DeltaCom's listings to send to ITC^DeltaCom

Alternatively, ITC^DeltaCom has received from another ILEC all directory listing information subject to a non-disclosure agreement, and ITC^DeltaCom would be willing to accept all directory listings subject to a similar limited use, non-disclosure agreement

## Issue 26 – Market Rate[1]

## Background

BellSouth is required to provide ITC^Deltacom access to unbundled local switching in accordance with section 271 of the Telecommunications Act, even where it may not be required to under section 251 Although the Tennessee Regulatory Authority is addressing BellSouth's section 251 unbundled local switching obligations in a parallel proceeding,[2] the TRA has been asked to arbitrate the appropriate section 271 rate to apply to address an interim gap in switching availability under federal rules [3]

Although BellSouth initially claimed it was entitled to "market rates" for section 271 network elements, the TRO eliminated <u>all</u> reference to a "market rate" pricing standard and made clear that the RBOCs were required to provide entrants local switching at rates that are "just, reasonable and nondiscriminatory" and which provide entrants "meaningful access "[4]

ITC^Deltacom continues to believe that the rates that best satisfy the section 271 "just and reasonable" pricing standard are the section 251 rates set by the Commission As a matter of law, the Telecommunications Act requires that section 251 (i e , TELRIC-based) rates must be "just and reasonable "[5] Although the FCC has determined that section 271 network elements need not *necessarily* be priced at TELRIC, both section 251 and section 271 rates must be with the *same range* of just and reasonable prices Moreover, BellSouth's own testimony (referenced below) indicates that TELRIC is *not* inappropriate for switching

In compliance with the Commission's request, however, ITC^DeltaCom herein proposes is best and final rate offer for unbundled local switching used to serve those lines (customer locations with 4 or more lines in Zone 1 end offices in the Nashville

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1 By offering to pay non-TELRIC rates in this circumstance, ITC^DeltaCom is reserving all rights to challenge BellSouth's TELRIC prices and unbundling obligations in any and all future proceedings and other jurisdictions ITC^DeltaCom's offer is limited solely to this arbitration and is tendered for the purposes of settlement only

2 Tennessee Regulatory Authority Docket No 03-00491

3 This interim gap concerns unbundled local switching used to serve customers with 4 or more lines in certain wire centers in Nashville Although the FCC has made clear that the "3-line rule" did not survive its TRO decision (n 1546), under certain conditions it may apply until a state commission concludes its investigation as to the appropriate boundary between the enterprise and mass markets

4 Triennial Review Order (TRO ¶ 663)

5 Section 252(d)(1) requires that the "just and reasonable rate for network elements" for purposes of subsection (c)(3) of such section shall be based on cost

MSA) where BellSouth's is obligated to offer unbundled local switching under section 271 of the federal Act

**Proposal**

For purposes of settlement, ITC^Deltacom offers the following rate proposal to apply to local switching used to serve customer locations in the Zone 1 wire centers in Nashville with more than 3 lines until replaced by the earlier of (a) the obligation to offer unbundled local switching in compliance with section 251 of the federal Act, (b) a different rate agreed to between BellSouth and ITC^DeltaCom, or (c) a new just and reasonable rate established by the Tennessee Regulatory Authority In such circumstances, ITC^DeltaCom offers to pay BellSouth a flat rate (i e , no additional usage[6] or feature charges would apply) of $5 08 per month, per analog switch port

All existing cost-based non-recurring charges would continue in effect without change (i e , the cost-based non-recurring charges would apply in connection with the section 271 monthly recurring rate offered here) In addition, the section 271 switching element must be treated identically to the section 251 unbundled local switching element, except as to its monthly recurring price, with respect to the terms and conditions of service, connection with other elements, interoperability with other elements, and pricing with other elements No changes to ordering, provisioning, maintenance or repair may be introduced that distinguish between the section 251 element and the section 271 element

**Just and Reasonable Justification**

The proposed flat-rate of $5 08 per analog switch port is based on BellSouth's "actual" (i e , embedded cost) for central office switching, plus a contribution equal to the average contribution of BellSouth's services in Tennessee in 2002 [7]

The rate development for the charge of $5 08 is provided in the attached worksheet The charge is based on BellSouth's reported central office switching expenses for 2002 and includes an estimated share of its depreciation costs for switching plant in service BellSouth's central office switching expenses is directly available in ARMIS 43-08 (row 6210), while the portion of its depreciation expense attributable to central office switching is estimated by applying the ratio of central office switching plant in service (ARMIS 43-08, row 2210) to Total Plant in Service (ARMIS 43-08, row 2001) to the annual depreciation of plant in service in 2002

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6 ITC^DeltaCom's proposed flat rate of $5 08 per port would apply in lieu of BellSouth's line port and end-office switching/trunk-port charges on all originating and terminating minutes from/to an ITC^DeltaCom leased switch port subject to non-TELRIC pricing

7 ITC^DeltaCom does not generally endorse rate setting based upon an embedded cost plus contribution methodology, but is making this offer in accordance with the Authority's request for settlement

The sum of central office expenses and central office depreciation is the estimated actual embedded cost of switching in Tennessee for BellSouth To this estimate of embedded cost, ITC^DeltaCom has added a contribution margin 43 2%, which is the average contribution (revenues in excess of expenses) from all BellSouth services in Tennessee in 2002

The proposed rate fully compensates BellSouth for its "actual embedded cost" of switching, plus provides it a more-than-fair contribution to its profits and other costs of 43%, and provides BellSouth a premium of 26% above TELRIC

In addition, the proposed flat-rate structure simplifies billing and is more in-line with principles of cost causation A number of states have reviewed RBOC switching contracts and have determined that a flat-rate structure better reflects the manner in which the RBOC actually incurs its switching costs States that have adopted a flat-rate structure for unbundled local switching include Illinois,[8] Minnesota,[9] Indiana,[10] Wisconsin[11] and Utah [12] In addition, the FCC has asked whether its TELRIC rules should be revised to require flat-rate pricing of local switching [13] When compared to the flat-rate switching prices established by these states, ITC^DeltaCom's offer is clearly attractive for BellSouth

| State | Flat-Rate | Docket | Date |
|---|---|---|---|
| Illinois | $2 18 | No 00-0700 | July 10, 2002 |
| Indiana | $2 98 | No 40611-S1 | March 28, 2002 |
| Wisconsin | $2 83 | No 6720-TI-161 | March 22, 2002 |
| Utah | $3 55 | No 01-049-85 | November 17, 2003 |
| Minnesota | $3 12 | P-421/CI-01-1375 | March 24, 2003 |

Flat-rate switching is an appropriate structure when the pricing standard is forward looking (as it is a TELRIC environment), which is the pricing standard applied by the above states The flat-rate structure is even more appropriate in situations (such as here) where the rate is developed based on embedded cost By this proposal, ITC^DeltaCom is leasing capacity in existing switches paying a price based on this

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8 *Second Interim Order*, ICC Docket 96-0486 and 96-0569 Consolidated, Illinois Commerce Commission, February 17, 1998 and *Order*, Illinois Commerce Commission Docket 98-0396,

9 *Order Setting Prices and Establishing Procedural Schedule*, MPUC Docket Nos P-421/CI-01-1375, *et al* (October 2, 2002)

10 Order, Cause No 40611-S1, Phase I, March 28, 2002, page 42

11 Open Meeting, December 13, 2001, Docket 6720-TI-161

12 *Report and Order*, Utah PSC Docket No 01-049-85 (May 5, 2003)

13 *NRPM*, WC Docket 03-173, September 15, 2003 The existing TELRIC rules permit states to choose whether local switching will be on an entirely, or partially, flat rate basis

historical cost of the switch These historic costs cannot vary with usage – indeed, they cannot vary at all ITC^DeltaCom's willingness to offer BellSouth an inflated rate for local switching based on BellSouth's embedded costs is part-and-parcel with its flat-rate proposal (which guarantees revenue recovery to BellSouth, irrespective of switch usage)

**Other Considerations**

As ITC^DeltaCom noted at the top, TELRIC-based local switching prices are by law just and reasonable Although, for purposes of settlement, ITC^DeltaCom has proposed a flat-rate price justified using an embedded cost methodology, ITC^DeltaCom does not believe that TELRIC-based rates are at the low-end of the just and reasonable range

First, it is important to appreciate that most contentious issues surrounding TELRIC pricing are loop-related, and do not apply to switching For instance, one of the principal areas being reviewed by the FCC is whether TELRIC rules should incorporate the incumbent's "actual network topology" (i e , how its network is actually laid-out) into the cost model However, the "actual network topology" is already a feature of the TELRIC process for local switching because the number of wire centers (and, therefore, the number and location of switches) is fixed Consequently, the "actual topology of the ILEC network" is already considered in determining TELRIC switching costs and the side-debate about the appropriateness of this aspect of TELRIC plays <u>no</u> role in evaluating whether switching prices are reasonable

Importantly, BellSouth has effectively conceded this point, testifying in South Carolina

> It is important to note that even though the fundamental cost methodologies (i e , TSLRIC and TELRIC methodologies are similar it is the additional constraints currently mandated by the FCC that the incumbent local exchange carriers (ILECs) object to with respect to TELRIC-based rates The use of a hypothetical network and most efficient, least-cost provider requirements have distorted the TELRIC results and normally understate the true forward-looking costs of the ILEC
>
> These distortions, however, are most evident in the calculation of unbundled loop elements, and they are less evident in the switching and transport network elements that make up switched access
>
> ***
>
> I emphasize that the main cost drivers for end office switching are the fundamental unit investments, which are identical in switching TSLRIC and TELRIC studies [14]

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[14] Direct Testimony on Robert McKnight on behalf of BellSouth, Public Service Commission of South Carolina (McKnight Direct), Docket No 1977-239-C, filed December 31, 2003, pages 7 and 9

BellSouth has acknowledged that its objections to TELRIC do <u>not</u> apply to switching,[15] that TELRIC and TSLRIC for switching are essentially the same, and that for the main cost drivers, they are identical Consequently, there is no reason to conclude that <u>different</u> just and reasonable rates are appropriate for section 271 switching network elements than for section 251 switching network elements

This point was echoed by BellSouth's economist, who argued in Florida last year that TELRIC-based rates are <u>above</u> forward-looking incremental cost and, as such, should not be used to establish the lower bound of its retail rates

> Cross-subsidization is measured using forward-looking incremental costs, not historical accounting costs Even reasonable allocations of fixed costs or common overhead costs to a service have no role in a subsidy test [16]
>
> ***
>
> The fact that TELRIC includes an allocation of shared fixed and common costs means that the TELRIC-based UNE price would be too high for a price floor [17]

Even BellSouth agrees that its TELRIC-based UNE rates for local switching are too high for its retail pricing decisions, which would suggest that TELRIC rates are (from BellSouth's perspective) above the lower end of the just and reasonable range already [18]

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15 This is not to say that BellSouth will not complain that the Georgia Commission has set switching rates incorrectly

16 Rebuttal Testimony of William Taylor on behalf of BellSouth, Docket Nos 02-0119-TP and 020578-TP, filed November 25, 2002 ("Taylor Rebuttal"), page 18

17 Taylor Rebuttal, Page 6

18 Although ITC^DeltaCom would agree that TELRIC rates are above the lower end of the range of just and reasonable rates, we would not agree that BellSouth should be permitted to price its retail services below TELRIC levels

## Issue 46 : BLV/BLVI

**To Be Completed Within 10 days after BellSouth filing.**

**Issue 47: Reverse Collocation:**

The language that should be included in this interconnection agreement that governs the Parties for the term of this agreement is as follows

Where BellSouth places equipment in ITC^DeltaCom space and uses that equipment to serve entities other than ITC^DeltaCom, BellSouth derives a benefit and shall abide by the same terms and conditions applied to ITC^DeltaCom for collocation and pay ITC^DeltaCom pursuant to the same rates, terms, and conditions for collocation that Bellsouth applies to ITC^DeltaCom

Due to the fact that this language will be included in an interconnection agreement that is effective upon the TRA's approval going forward for the term of the new agreement, this language cannot be applied on a retroactive basis ITCD will charge the same applicable non-recurring and recurring charges BellSouth charges ITCD on a going forward basis for those locations where BellSouth has placed equipment in ITCD space that is being used by BellSouth to sell to other entities

**Issue 62 – Limitation on Backbilling:**

As a compromise, ITCD proposes a backbilling limit not to exceed three billing cycles This proposal strikes the appropriate balance between a reasonable period of time for BellSouth to render a correct bill for those items billed in advance as well as those items billed in arrears

Additionally, this time frame allows ITCD to accurately apply charges to its end user customers in a fair and reasonable time period

Respectfully submitted,

BOULT, CUMMINGS, CONNERS & BERRY, PLC

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## Worksheet Calculating Average Embedded Switch Cost Plus Average Contribution

| | **Embedded Cost of Switching** | **Total** | **Per Line** | **Source** |
|---|---|---|---|---|
| (a) | Central Office Switching Expense | $33,676 | $1 13 | ARMIS 43-03 Row 6210 |
| (b) | Switching Share of Depreciatio/Amortization | $72,441 | $2 42 | Caclulated Below |
| (c) | Total Embedded Cost | $106,117 | $3 55 | (a) + (b) |
| (d) | Applying Average Contribution | 43 2% | 43 2% | (n) |
| (e) | Contribution | $45,792 | $1 53 | (c)*(d) |
| (f) | Embedded Cost plus Contribution | $151,909 | $5 08 | (e) + (c) |
| | **Proposed Flat-Rate Per Switch Port** | | **$5 08** | |

| | **Estimating Switching Share of Depreciation** | | **Source** |
|---|---|---|---|
| (g) | Switching Plant in Service | $1,076,322 | ARMIS 43-03 Row 2210 |
| (h) | Total Plant in Service | $6,081,484 | ARMIS 43-03 Row 2001 |
| (i) | Switchng Share | 17 7% | (g)/(h) |
| (j) | Depreciation on Plant in Service | $409,309 | ARMIS 43-03 Row 6561 |
| (k) | Switching Share of Depreciation/Amortization | $72,441 | (i)*(j) |
| | **Calculating Average Contribution** | | |
| (l) | Total Revenues in Tennessee | $1,677 242 | ARMIS 43-01 Row 1090 |
| (m) | Total Expenses (including Depreciation) | $1,171,650 | ARMIS 43-01 Row 1190 |
| (n) | Margin | 43 2% | (l-m)/(m) |
| | Switched Lines | 2,490,573 | ARMIS 43-08 Row 530 |

| | **Comparison to TELRIC** | | | |
|---|---|---|---|---|
| (o) | TELRIC Port Rate | $1 70 | | SGAT |
| | Estimating Average Usage Cost | **Usage** | **Rate** | |
| | Average Usage (originating and terminating) | 3,622 | | ARMIS 43-04 Row 1216 |
| | Originating Intraswitch | 724 | $0 0008041 | Assumes 40% intraswitch |
| | Originating Interswitch | 1,087 | $0 0008041 | |
| | Terminating Intraswitch | 724 | | Usage rate not applied twice |
| | Terminating Interswtch | 1,087 | $0 0008041 | |
| (p) | Average Monthly Usage | $2 33 | | Sum of Usage * usage rate |
| (q) | Total Average TELRIC Rate | $4 03 | | (o) + (p) |
| | Proposed Flat Rate | $5 08 | | (f) |
| | Premium | 26% | | (f-q)/(q) |

## CERTIFICATE OF SERVICE

I hereby certify that on February 20, 2004, a copy of the foregoing document was serviced on the parties of record, via US mail

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