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August 24, 1999

VIA HAND DELIVERY

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REGULATORY AUTH.
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EXECUTIVE SECRETARY

Mr. David Waddell
Executive Secretary
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243-0505

RE: *Proceeding for the Purpose of Addressing Competitive Effects of Contract Service Arrangements filed by BellSouth Telecommunications, Inc. in Tennessee*
TRA Docket No. 98-00559 TRADD
TRA Docket No. 99-00210 TRADD
TRA Docket No. 99-00244 TRADD

Dear Mr. Waddell:

Enclosed for filing, please find the original plus thirteen (13) copies of Time Warner Communications of the Mid-South, L.P. and NewSouth Communications, Corp.'s Post-Hearing Brief in the above-referenced matter. As a supplement to our brief, Time Warner and NewSouth adopt the law and argument filed by AT&T in its Post-Hearing Brief. Copies are being served on parties of record.

If you have any questions or concerns with regard to this filing, please do not hesitate to contact me.

Very truly yours,

FARRIS, MATHEWS, BRANAN & HELLEN, P.L.C.

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Parties of record

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FILE

BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE

IN RE:	**PROCEEDING FOR THE PURPOSE OF ADDRESSING COMPETITIVE EFFECTS OF CONTRACT SERVICE ARRANGEMENTS FILED BY BELLSOUTH TELECOMMUNICATIONS, INC. IN TENNESSEE**	**) Docket No. 98-00559) Docket No. 99-00210) Docket No. 99-00244**

POST-HEARING BRIEF SUBMITTED ON BEHALF OF TIME WARNER TELECOM OF THE MID-SOUTH, L.P. and NEWSOUTH COMMUNICATIONS, CORP.

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August 24, 1999

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POST-HEARING BRIEF SUBMITTED ON BEHALF OF TIME WARNER TELECOM OF THE MID-SOUTH, L.P. and NEWSOUTH COMMUNICATIONS, CORP.

This Post-Hearing Brief is submitted on behalf of Time Warner Telecom of the Mid-South, L.P. ("Time Warner") and NewSouth Communications, Corp. ("NewSouth") and filed with the Tennessee Regulatory Authority ("Authority") in accordance with the instructions of the Directors following the conclusion of the hearing in Docket Nos. 99-00210 and 99-00244 held on August 17 and 18, 1999.

STATEMENT OF RELEVANT FACTS

With the exception of a very small portion of the Tennessee market, BellSouth Telecommunications, Inc. ("BellSouth") has enjoyed its role as the monopoly provider of local exchange telecommunications services for approximately 100 years. Upon the enactment of state legislation in 1995 and federal legislation in 1996, BellSouth recognized for the first time in its existence the possibility of competitive challenges, an erosion of its customer base and loss of significant revenues. This anticipated threat of competition has been very slow in its development. By BellSouth's own admission, the monopoly provider has been successful in maintaining a market share in excess of 90% of all business

customers and more than 90% of residential customers in its service area. Vol. I, p. 165, l. 23-25; p. 166, l. 1-3. By BellSouth's own admission, the company has maintained approximately 80% of all business customers.

BellSouth's success in maintaining its overwhelming market share is due, in significant part, to its marketing strategy of obtaining long-term contractual commitments to purchase BellSouth services from its most lucrative customers; thus, isolating these most profitable customers from the marketing efforts of competing providers. Shortly after the adoption of the Federal Telecommunications Acts of 1996 ("TA 96"), Pub. L. No. 104-104, 47 U.S.C. § 151 et. seq., which created the necessary framework for the evolution of competition, and while potential competitors designed their plans to enter the market, BellSouth announced to its sales and marketing personnel two plans which were internally referred to as the Top 500 List and the Premier or Mid-Market Retention List. Tr. Vol. I, p. 219, l. 1-4, 9-14; p. 220, l. 21-25; p. 244, l. 6-14.

The purpose of these plans was to offer contractual service arrangements ("CSAs") to targeted customers; the most profitable in the BellSouth service areas. Tr. Vol. I, p. 151, l. 11; p. 153, l. 21; p. 158, l. 16-25; p. 159, l. 1-4. An inspection of the Authority's records reveals that BellSouth's plans were implemented by way of increasing the volume of CSAs during the period of mid-1996 to the present. Tr. Vol. I, p. 246, l. 5-14 (13 CSAs filed in 1996; 116 filed in 1997; 42 filed in 1998). Until a very recent agreement, all BellSouth CSAs were negotiated, filed and approved in secret as confidential information. The increasing volume of BellSouth CSAs has been a growing concern of regulatory agencies' staff, competing providers and consumer advocates in almost every state for approximately two years. In Tennessee, two other proceedings have been initiated by the Consumer

Advocate Division of the Attorney General's office and competitive local exchange carriers seeking review and relief from the impact of BellSouth CSAs. The Authority initiated the instant docket on its own motion. The Authority has chosen two particular CSAs, not yet approved, for the purpose of developing a record in its generic docket no. 98-00559. For the purpose of preserving the confidentiality of the BellSouth customers, these CSAs have been referred to as that of the "Store" and that of the "Bank." The fundamental issue before the Authority at this stage of the proceeding is whether these two BellSouth CSAs should be approved, and therefore, BellSouth bears "the burden to prove their [CSAs] validity of both of these dockets". Fourth Report and Recommendation of the Hearing Officer, filed 07/08/99, adopted by the Authority on 7/13/99.

As explained by BellSouth's only witness, Mr. Randall Frame ("Frame"), the largest business customers which represent a very small percentage of the total customer base, provide a disproportionately large percentage of the total revenues available in the market. BellSouth generated 10.25% of its total revenue in the state of Tennessee through CSAs, but it offered CSA to only 0.085% of its customers. Substituted Pre-filed Testimony of Randall L. Frame, p. 4, l. 4-14. Thus, less than one percent of BellSouth's customers are producing over ten percent (10%) of its revenues in Tennessee.

Contract arrangements with these customers, therefore, are important to BellSouth and competing carriers. BellSouth employs CSAs to protect existing revenue streams while competing local exchange carriers ("CLECs") use contractual arrangements to secure a guaranteed stream of income for the purpose of constructing new network facilities to provide competing services. Frame stated that BellSouth's CSAs are "about preserving market share. . . and growing revenue." Tr. Vol. I, 158, p. 16-25; p. 159, l. 1-4, 20-25; p.

160, l. 1-3. In contrast, the CAD's witness, Roger T. Buckner, testified that CLECs enter into CSAs because "they're limited in resources and they don't have a captured customer base. They need a CSA to be able to afford to build the facilities and the certainty that they're going to receive those revenues for those facilities." Tr. Vol. II, p. 304, l. 11-25; p. 305, l. 1-11.

Although CLECs have been successful in securing a small percentage of the business customer market, estimated at approximately 7%, no publicly held CLEC has reported a profit for any reporting period. Tr. Vol. II, p. 99, l. 4-5. Over the course of the past two years, BellSouth has continued to obligate its largest revenue generating customers to service agreements with three to five year terms which obviously impairs the CLEC effort to gain revenues critical to their continued ability to compete in the marketplace. The BellSouth customer obligation is secured by the termination liability provisions of the CSAs. These termination provisions require CSA customers to pay BellSouth liquidated damages in the event of early termination. The termination liability is an insurmountable impediment to the marketing efforts of new competitors to influence the most profitable business customers to use the services of the competing providers.

ARGUMENT

BellSouth has Failed to Prove by the Preponderance of the Evidence that the CSAs Comply with Applicable Law.

In order to meet its burden of proof in this case, BellSouth must show by a preponderance or a greater weight of the evidence that its CSAs with the Bank and the Store comply with state and federal law and rules and orders of the Authority. Fourth Report and Recommendation of the Hearing Officer, 14; Tenn Admin. Register 1220-1-1-

.16(5); Rayder v. Grunow, 1993 Tenn. App. LEXIS 261, *21 fn. 6 (finding that the agencies customarily use the preponderance of evidence standard). BellSouth has failed not only to meet this burden, but the testimony of Mr. Frame elicited through cross-examination and the testimony of the witnesses produced by the other parties clearly demonstrates that these CSAs violate applicable law in four critical respects. Simply stated, the Bank and Store CSAs violate state and federal law which:

1. prohibits BellSouth from offering services priced below its cost;
2. prohibits the enforceability of termination liability provisions which constitute a penalty;
3. prohibits unjust discrimination in service offerings; and
4. prohibits anti-competitive practices designed to frustrate the orderly development of a competitive telecommunications market.

I. BellSouth Failed to Produce any Credible Evidence in Support of its Contention that the CSA Offered Services are Proposed at Rates at or Above its Cost.

BellSouth's one and only witness, Randall Frame, a sales and marketing manager, testified that "discounts offered under those contracts do not result in the discounting of services below costs". Pre-filed direct testimony of Randall L. Frame, p. 13, l. 2-3. The only support for Mr. Frame's assertion were certain documents attached to his Pre-filed testimony as an exhibit which purports to be a detailed cost analysis. On cross-examination, Mr. Frame admitted that he did not prepare this documentation, was not familiar with the methodology in preparing a cost accounting analysis, and that he could not verify the accuracy or the validity of the cost study. Frame at Tr. Vol. I, p. 190, l. 6-25

and p. 191, l. 1-5.

Admitting these documents into the record offends the most basic rules of evidence. In the absence of a properly qualified witness made available for cross-examination, these cost studies constitute the rankest form of hearsay offered for the proof of an outcome determinative issue of material fact. Without the aid of supporting expert testimony, the cost study becomes useless to the Authority in its determination of compliance with state law expressly establishing a cost floor for BellSouth and prohibiting cross subsidization and predatory pricing, both of which occur when the incumbent carrier provides services to customers at prices below cost. T.C.A. § 65-5-208(c).

As its witness, the Consumer Advocate Division offered Senior Regulatory Analyst, Robert T. Buckner. Mr. Buckner has been employed in the field of utility industry regulation for approximately 20 years and is a certified public accountant familiar with cost accounting principals and methodology customarily applicable to regulated public utilities. Buckner Pre-filed testimony at p. 1, l. 9-11. Mr. Buckner testified that the proposed rates of BellSouth in the CSA to the Bank represented 80 instances of services priced below cost and 15 instances of below cost pricing in the CSA with the store. Buckner Pre-filed testimony at p. 37, l. 18-21. His is the only competent admissible evidence in the record.

Time Warner and NewSouth submit that Mr. Buckner's testimony remains uncontradicted by any competent evidence. Based upon this record, the Authority must make a determination that BellSouth has failed to meet its burden of proof that the rates offered pursuant to the CSAs to the Store and the Bank are within the permissible statutory parameters.

II. BellSouth has Failed to Offer any Evidence Showing that the Termination Liability Provisions of the CSAs are Reasonable and Enforceable Liquidated Damages.

Tennessee case law unequivocally requires that early termination liability provisions or liquidated damage provisions result in agreed, calculated payments reasonably related to breach of contract damages anticipated on a prospective basis at the time of the execution of the agreement.

> Courts must focus on the intentions of the parties based upon the language in the contract and the circumstances that existed at the time of contract formation. Those circumstances include: whether the liquidated sum was a reasonable estimate of potential damages and whether actual damages were indeterminable or difficult to measure at the time the parties entered into the contract. . . . If the provision and circumstances indicate that the parties intended merely to penalize for a breach of contract, then the provision is unenforceable as against public policy.

Guiliano v. Cleo, Inc., 1999 Tenn. LEXIS 339, *32.

Thus, if early termination liability provisions result in payments in excess of reasonably foreseeable damages related to the breach, the payments constitute a penalty, and are void and unenforceable as a matter of public policy.

BellSouth failed to provide any explanation of the basis for its calculation of early termination liability with one unacceptable exception. Mr. Frame explained that the termination liability provisions did not have any relationship to anticipated damages that BellSouth would incur if the customer terminated the agreement early without cause, and that the early termination payment was designed as an incentive for the customer to honor its commitment for the entire term of the CSA. Tr. Vol. I, p. 87, l. 1-15. Upon questioning by Chairman Malone, the following exchange took place:

CHAIRMAN MALONE:

> So the figure [termination liability payments] is what it is. It is not related to what the damages might be expected to be?

MR. FRAME:

> Right. And I am not sure where the calculation came from.

CHAIRMAN MALONE:

> I understand. So just to check, whatever that figure is [the termination owed to BST], is just derived from the plain language of the tariff, and that language and the derivation thereof is not related to any analysis that BellSouth has performed to estimate the damages that would occur should a breach occur?

MR. FRAME:

> Not to my knowledge.

Tr. Vol. I, p. 236, l. 23-25, p. 237, l. 1-4.

Clearly, BellSouth has offered no proof that the termination liability provisions of the Bank and the Store CSAs are reasonably calculated to compensate BellSouth for its actual damages in the event of early termination of the contract by the customer without cause. Obviously, the Authority has no evidence upon which to make a determination that the BellSouth termination liability provisions are enforceable for any reason consistent with Tennessee case law, and these provisions should be deleted in their entirety.

III. BellSouth Has Adopted No Process or Procedure to Offer the Store and the Bank CSAs to Similarly Situated Customers and This Omission Violates Statutory Prohibitions of Unjust Discrimination.

On cross-examination, Mr. Frame admits that all BellSouth CSAs such as the CSAs offered to the Store and the Bank are offered only in response to an offer of a competing

carrier or a serious threat of such a competitive offer. Tr. Vol. I, p. 118, l. 7-11; p. 119, l. 4-5. As a result, customers generally have not enjoyed lower rates characteristic of a competitive environment. Mr. Frame admitted that BellSouth has never reduced its tariffed rates. Tr. Vol. I, p. 248, l. 16-17. Instead, BellSouth lowers its rates one customer at a time in an effort to protect its existing customer base and revenue. Frame at Tr. Vol. I, p. 242, l. 5-17 and p. 243, l. 9-12.

Although Mr. Frame discusses product mix and other factors considered by BellSouth in making CSAs available to customers such as the Store and the Bank, these factors only influence BellSouth's decisions in negotiating the effective rate charged for the services offered. Tr. Vol. I, p. 119, l. 16-22. These other factors mentioned by Mr. Frame have absolutely no impact on BellSouth's identification of customers similarly situated to CSA customers who enjoy lower rates pursuant to the negotiated terms of a CSA. According to Mr. Frame, BellSouth has adopted no policy or procedure which evaluates and extends the terms and conditions of existing CSAs to similarly situated customers. Tr. Vol. I, p. 243, l. 1-8. CSAs are offered by BellSouth only in a response to offers of competing carriers. Tr. Vol. I, p. 168, l. 16-25; p. 119, l. 1-7. Further, other customers have not been afforded any practical means of discovering the terms or conditions of CSAs or even the mere existence of the CSAs. Clearly, this process is discriminatory.

In order for this discrimination to be permissible, there must be some identifiable criteria to support the offer to this privileged class of customers. BellSouth has offered no basis for the limitation of its offering of services pursuant to contracts other than its illusory reference to product mix or combination of services required by the customer. Tr. Vol. I, p. 258, l. 14-20. Without further analysis of the type of services, the cost of those services

and the location and telecommunication service needs of other customers in a particular locale, BellSouth has no justifiable reason for failure to make available CSAs comparable to that offered to the Bank and the Store to other customers. BellSouth's simple criteria of making CSAs available to customers who are recipients of offers from competing carriers is simply not a rational basis for discriminatory pricing. The Bank and the Store CSAs violate the unjust discrimination prohibitions of state law and therefore should not be approved. See, Tenn. Code Ann. § 65-4-12, § 65-4-115, and § 65-4-204.

IV. The Proposed CSAs are Part of an Anti-Competitive Scheme to Frustrate the Orderly Development of an Effectively Competitive Market.

Within months after the adoption of legislation making competition in local exchange telecommunication markets a possibility, BellSouth designed its plans for identifying and obligating its most profitable customers to extended term contractual service arrangements. While competing carriers considered plans to enter the market, BellSouth formulated its Top 500 and Mid-market retention lists. Frame at Tr. Vol. I, p. 240, l. 10-23. By 1997, BellSouth had successfully executed contracts with over 125 of these most profitable customers. Tr. Vol. I, p. 246, l. 5-14. The approximately two hundred CSAs filed by BellSouth with the Authority require obligations from the customers on an average term from three to five years.

According to Mr. Frame, the purpose of BellSouth's unprecedented offering of services through CSAs is to preserve its market share and retain its customers and its existing source of revenue. Tr. Vol. I, p. 159, l. 20-25; p. 160, l. 1-3.

This practice is anti-competitive. BellSouth has been and remains virtually a monopoly provider of local exchange telecommunications services. It is the only provider such services with market power. This market power coupled with its ubiquitous network, name recognition and customer loyalty makes its extremely difficult for CLECs to compete for market share. CSAs designed to insolate the most profitable business customers from competition makes these efforts even more difficult. As part of a total plan or scheme to frustrate the development of competition, the Bank and Store CSAs represent a BellSouth effort which must be categorized as anti-competitive.

The only expert testimony offered to the Authority in this proceeding is that of the Consumer Advocate Division's witness, Dr. Stephen Brown. In reaching his conclusion that all BellSouth CSAs are anti-competitive, including the Bank and Store CSAs, Dr. Brown reasoned that:

> The CSAs are meant to protect the company's market share by making the customer pay a prohibitively expensive termination fee unrelated to the if it, the customer, seeks to replace BellSouth-supplied services with services from a BellSouth competitor. The CSAs are a market entry barrier aimed at BellSouth's competitors. The barrier is composed of and created by, one, the [BellSouth's] practice of unjustified discrimination between customers which is manifested through the company's practice of selectively offering the CSAs, and two, the barrier is composed of the CSA termination fees which are meant to be invoked or triggered only if the customer replaces its BellSouth-supplied services with a competitor's services. In the event that a CSA customer chooses to replace its BellSouth-supplied services with the services of BellSouth's competitor, the termination fee is economic dead weight borne either by the customer or its new provider of services.
>
> In the event that a customer replaces its BellSouth-supplied services which are discounted through the CSA with the services of a competitor, the CSA termination fees are invoked in tandem with the termination fees of the prevailing tariff . . . . The ability of the incumbent to apply two termination fees does not reflect the public interest goals in Tennessee's Telecom Act of 1995 and in the Federal Telecom Act of 1996, that goal being the

promotion of competition in local telecommunications markets.

Vol. II, p. 311, L. 16-25; p. 312, L. 1-11, 23-25; p. 313, L. 1-2, 10-14.

BellSouth's use of the CSAs clearly violates the strict intent of the State and Federal Telecommunications Acts which permit and provide a regulatory framework for the development of competition. For this reason, the BellSouth CSAs with the Store and the Bank cannot be approved.

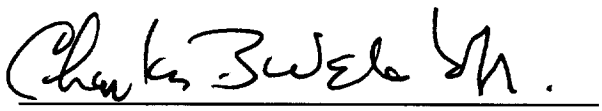
CONCLUSION

In the long-term, telecommunication service markets will be regulated by effective competition; not by regulatory agencies. In a truly competitive environment, service providers will undoubtedly use contractual arrangements to guarantee income. In order to reach the level of an effectively competitive market, impediments to the development of competition must be removed. Currently, BellSouth CSAs represent an unfair competitive advantage. In order to assist the development of competition, the Authority must restrict or prohibit the monopoly provider's use of CSAs. The timing of this regulatory response is critical. Over time, as CLECs gain market share and the market actually becomes competitive, the issue will become mute. Currently, however, BellSouth CSAs represent a serious impediment to the development of competition.

For the reasons stated herein, Time Warner and NewSouth respectfully request that BellSouth's petition for approval of the Bank and Store CSAs be denied.

Respectfully submitted,

FARRIS, MATHEWS, BRANAN & HELLEN, P.L.C.

By: 

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CERTIFICATE OF SERVICE

I, Charles B. Welch, Jr., hereby certify that I have served a copy of the foregoing Brief on the parties of record, by depositing a copy of same in the U.S. Mail, postage prepaid this the 24th day of August, 1999.

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