BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

November 13, 2000

IN RE:	)	
	)	
BELLSOUTH TELECOMMUNICATIONS, INC.'S TARIFF TO OFFER CONTRACT SERVICE AGREEMENT TN98-2766-00 FOR MAXIMUM 13% DISCOUNT ON ELIGIBLE TARIFFED SERVICES	)	**DOCKET NO. 99-00210**
BELLSOUTH TELECOMMUNICATIONS, INC.'S TARIFF TO OFFER CONTRACT SERVICE AGREEMENT KY98-4958-00 FOR AN 11% DISCOUNT OF VARIOUS SERVICES	)	**DOCKET NO. 99-00244**
PROCEEDING FOR THE PURPOSE OF ADDRESSING COMPETITIVE EFFECTS OF CONTRACT SERVICE ARRANGEMENTS FILED BY BELLSOUTH TELECOMMUNICATIONS, INC. IN TENNESSEE	)	**DOCKET NO. 98-00559**

ORDER GRANTING APPROVAL OF BELLSOUTH CONTRACT SERVICE ARRANGEMENT (TN 98-2766-00) IN DOCKET NO. 99-00210

This matter came before the Tennessee Regulatory Authority ("Authority") on September 2, 1999 for consideration of the tariff filing of BellSouth Telecommunications, Inc. ("BellSouth") for approval to offer Contract Service Arrangement No. TN 98-2766-00 ("CSA").[1] BellSouth filed Tariff No. 99-00210 on March 31, 1999, with a proposed effective date of April 30, 1999.

[1] The customer contracting with BellSouth pursuant to this CSA will hereinafter be referred to as "the Bank" or "the customer."

I. Procedural History

The Directors first considered this matter at the regularly scheduled Authority Conference held on April 20, 1999 and unanimously suspended the tariff for five (5) days until May 5, 1999. Time Warner Telecom of the Mid-South, L.P. ("Time Warner") filed a Petition to Intervene and Complaint for Contested Case Proceeding on April 27, 1999. NEXTLINK Tennessee, Inc. ("NEXTLINK") and the Southeastern Competitive Carriers Association ("SECCA") filed Petitions to Intervene on April 28, 1999. The Directors considered the tariff again at a regularly scheduled Authority Conference on May 4, 1999 and unanimously suspended the tariff for thirty (30) days. In addition, the Directors expressed concern over the specificity of the Petitions to Intervene and allowed Time Warner, NEXTLINK, and SECCA until May 7, 1999 to file amendments to their Petitions to Intervene. Time Warner filed an Amended Petition to Intervene and Complaint for Contested Case Proceeding on May 7, 1999. NEXTLINK and SECCA filed a supplement to their Petitions to Intervene on May 13, 1999 after discovering that their filing of same on May 7, 1999 contained docket number errors.

The Authority notified the parties that it would consider the tariff and Petitions to Intervene at the June 8, 1999 Authority Conference. Due to the unavailability of counsel, NEXTLINK and SECCA filed a Motion for Continuance on June 4, 1999. At the June 8th Authority Conference, the Directors unanimously granted the Petitions to Intervene in this docket and consolidated this docket with Docket Nos. 98-00559 and 99-00244.[2]

[2] The action of the Authority granting the Petitions to Intervene rendered the Motion for Continuance moot. The Authority issued a written order granting the Petitions to Intervene and Consolidating 99-00210 and 99-00244 with 98-00559 on August 24, 1999. The Authority consolidated 99-00210 and 99-00244 with 98-00559 for the purposes of allowing all intervenors in 98-00559 to participate in 99-00210 and 99-00244; allowing access to previously filed discovery in 98-00559; and resolving issues common to all three dockets.

The Authority held a hearing in Docket Nos. 99-00210 and 99-00244 on August 17 and 18, 1999.[3] In attendance at the hearing were the following parties:

BellSouth Telecommunications, Inc. ("BellSouth") - **Guy M. Hicks**, Esquire and **Patrick Turner**, Esquire, 333 Commerce Street, Suite 2101, Nashville, TN 37201;

NEXTLINK Tennessee, Inc. ("NEXTLINK") and Southeastern Competitive Carriers Association ("SECCA") - **Henry Walker**, Esquire, Boult, Cummings, Conners & Berry, 414 Union St., #1600, P. O. Box 198062, Nashville, TN 37219-8062. In addition, **Dana Shaffer,** Esquire, 105 Molloy Street, Suite 300 Nashville, TN 37201-2315, appeared on behalf of NEXTLINK;

Time Warner Communications of the MidSouth, L.P. ("Time Warner") and New South Communications, LLC ("New South") - **Charles B. Welch, Jr.,** Esquire, 511 Union Street, Suite 2400, Nashville, TN 37219;

AT&T Communications of the South Central States, Inc. ("AT&T") - **Val Sanford**, Esquire, Gullett, Sanford, Robinson & Martin, 230 Fourth Avenue North, 3rd Floor, P.O. Box 198888, Nashville, TN 37219-8888;

MCI WorldCom ("MCI") - **Jon E. Hastings**, Esquire, Boult, Cummings, Conners & Berry, 414 Union St., 1600, P. O. Box 198062, Nashville, TN 37219-8062 and **Susan Berlin**, Esquire, 6 Concourse Pkwy, Atlanta, GA 30328; and

Consumer Advocate Division, Office of the Attorney General ("Consumer Advocate") - **Vance Broemel**, Esquire, 426 5th Avenue, N., 2nd Floor, Nashville, TN 37243.

During the hearing, BellSouth presented Randall L. Frame, Sales Manager for BellSouth Business Systems, as its only witness. AT&T, NEXTLINK, SECCA, Time Warner, New South, MCI, and the Consumer Advocate cross-examined Mr. Frame after which BellSouth asked questions on re-direct examination. The Directors also questioned Mr. Frame. Time Warner presented David Darrohn, General Manager for Time Warner Telecom in

[3] As a result of the consolidation, the intervenors in Docket No. 98-00559 were now parties in Docket Nos. 99-00210 and 99-00244 and the record in Docket No. 98-00559 was now a part of the record in Docket Nos. 99-00210 and 99-00244. Nevertheless, because Docket No. 98-00559 involved issues beyond the scope of Docket Nos. 99-00210 and 99-00244, the resolution of the issues in Docket Nos. 99-00210 and 99-00244 do not conclude the proceedings in Docket No. 98-00559. The non-common, unresolved issues in 98-00559 remain.

Memphis, Tennessee, as a witness. Mr. Darrohn was subject to cross-examination, re-direct examination, and questioning by the Directors. NEXTLINK presented Jennifer West, Sales Representative for NEXTLINK in Memphis, Tennessee, and Margaret Brown, Regional Account Manager for Major Accounts in Nashville and the Southeast, as its witnesses. Both witnesses underwent cross-examination and re-direct examination, and Jennifer West also answered questions from the Directors. The Consumer Advocate presented as witnesses Robert T. Buckner, Senior Regulatory Analyst for the Consumer Advocate, and Stephen N. Brown, Economist for the Consumer Advocate. Both witnesses underwent cross-examination and re-direct examination.

On August 24, 1999, BellSouth, the Consumer Advocate, AT&T, SECCA, NEXTLINK, Time Warner, and NewSouth submitted post-hearing briefs. On that same day, MCI submitted a letter to the Executive Secretary stating that MCI adopted the post-hearing brief of NEXTLINK and SECCA. The Authority permitted the parties to present oral argument on September 2, 1999.

II. Burden of Proof

Because this docket addresses a CSA that is awaiting approval by the Authority, BellSouth has the burden to prove the validity of the CSA. Upon a showing of a prima facie case by BellSouth, those parties challenging the CSA have the burden of persuading the Authority that the CSA violates state and/or federal law.

III. Positions of the Parties

A. Discrimination

BellSouth claims that the CSA is not unlawfully discriminatory for two reasons. First, BellSouth makes them available to any similarly situated customer. Second, the other parties did

not or could not determine whether any customers similarly situated to the Bank were or were not offered or denied similar CSAs.

AT&T, MCI, SECCA, and NEXTLINK contend that BellSouth's failure to demonstrate a neutral, rational basis for the rate differences in the CSA makes it impossible to determine whether any customers are similarly situated. Consequently, BellSouth's offer to make the CSA available to similarly situated customers is meaningless, and the CSA is unlawfully discriminatory. Time Warner and New South claim that BellSouth's lack of a process or procedure for identifying customers similarly situated to the Bank makes this CSA unlawfully discriminatory.

The Consumer Advocate draws an analogy between BellSouth and transportation companies that cannot lawfully discriminate in rates when there is no difference in costs. BellSouth's policy that a customer without a "competitive offer" is not considered similarly situated is therefore improper according to the Consumer Advocate. Further, the Consumer Advocate claims that Mr. Frame's concession that no customer can discover another's product mix or contribution level makes it impossible for a customer to determine whether it is similarly situated to other BellSouth customers.

B. Anticompetitive

BellSouth argues that none of the provisions in the CSA are anticompetitive or exclusive. The Consumer Advocate claimed that BellSouth forces customers to accept terms they do not wish to accept, but both Dr. Brown and Mr. Buckner admitted they had no knowledge of actual negotiations. Dr. Brown admitted that termination charges apply in situations where a customer terminates the contract for reasons having nothing to do with a competitor. While Dr. Brown theorized that an incumbent could bar a competitor's entry into the market by setting a standing

offer to beat any credible offer by entrants, he also recognized that such entry has not been barred, as both NEXTLINK and Time Warner have their own contracts with business customers in BellSouth's territory. Mr. Buckner's claim that CSAs amount to tying arrangements was rebutted by Mr. Frame's explanation that this volume and term CSA does not require the customer to order any particular product or mix of products.

AT&T, MCI, SECCA, and NEXTLINK claim that each of these CSAs is anticompetitive by locking in the customer for the term of the contract. The CSAs accomplish this by giving the customer price discounts that increase with the dollar volume of its purchase from BellSouth and by imposing termination charges when the customer terminates the CSA. Further, AT&T, MCI, SECCA, and NEXTLINK argue that CSAs deprive nonCSA customers of the benefits of competition because BellSouth uses CSAs rather than changing the general tariff.

Time Warner and NewSouth contend that the CSA is part of a plan or scheme to frustrate the development of competition, which directly conflicts with both the Tennessee and federal telecommunications acts. Time Warner and New South contend BellSouth has sought to isolate its most profitable customers from its competitors through long-term CSAs. As evidence, Time Warner and New South point to the fact that BellSouth offered CSAs to only 0.085% of its Tennessee customers, but these CSAs account for 10.25% of its Tennessee revenues. Adherence of its customers to the terms of the CSAs is assured by the requirement that customers pay damages in the event of early termination of CSAs, over and above any tariffed termination charges that may apply.

C. Tennessee Contract Law

BellSouth argues that the termination provisions do not violate Tennessee law because the termination provisions result in a payment that is less than the anticipated damages from the

breach of the CSA. According to BellSouth, the Authority should determine whether the parties reasonably could anticipate the amount of damages. If the payment resulting from the termination provisions is equal to or less than the anticipated damages, then the payment is not a penalty. If it happens that the payment is more than the actual damages, then, BellSouth simply stated, "that's the way it goes."[4]

AT&T, Time Warner, and New South interpret the Tennessee Supreme Court decision in *Guiliano v. Cleo*, 995 S.W.2d 88 (Tenn. 1999), to allow liquidated damages only when the amount of compensation for breach is indeterminable. AT&T, Time Warner and New South contend that BellSouth's actual damages are readily determinable and certain. They rely on Mr. Frame's testimony that BellSouth's actual damages could be readily determined to support their position.

NEXTLINK, SECCA, and MCI argue that the Authority's duty goes beyond *Guiliano v. Cleo* to determining whether the termination provisions are just, reasonable, and pro-competitive. Further, NEXTLINK, SECCA, and MCI argue that the provisions should be stricken and the question of damages left to the trial courts.

The Consumer Advocate points out that the evidence establishes that BellSouth itself considers the payments resulting from the termination provisions to be penalties. In addition, the Consumer Advocate contends that BellSouth failed to establish that the damages provided by the termination provisions have any relation to BellSouth's costs.

[4] *Transcript of Oral Argument*, September 2, 1999, p. 21.

IV. Findings of Fact and Conclusions of Law

Immediately following oral argument on September 2, 1999, the Directors deliberated the issues and made the following findings:[5]

1. The purpose of this CSA is to provide a Volume and Term Discount to the customer identified in the filing. Through this arrangement, BellSouth is offering a thirteen percent (13%) discount on various eligible local exchange and private line services to a customer who has agreed to a minimum annual revenue commitment and a three (3) year contract term.

2. This CSA contains two termination provisions. The first relates to the termination of the underlying specific service and is linked to the tariff provision applicable to the underlying service. The second applies to the termination of the Volume and Term agreement. This termination provision calls for charges of $350,000 for an early termination occurring at the end of a contract year or $350,000 plus any unmet annual revenue commitment for a termination occurring during a contract year. Because the first termination provision is contained in the underlying, previously approved tariff, it is only the second termination provision that is before the Authority in this docket.[6]

3. The CSA involves a large company with extensive resources entering into a business arrangement that appears to be acceptable to both parties. In fact, the Bank resisted

---

[5] The findings included within the body of this Order formed the basis of Director Greer's motion to approve the CSA. Although Director Greer made the prevailing motion, he also made these qualifying comments:

> I do not want to say that I necessarily approve of the termination charge that they have agreed upon. The bank obviously rejected the termination provisions as put forth to them and chose these termination provisions.
>
> As I said, I don't think it is my responsibility to relieve parties from the consequences of their own improvidence. This is different from other termination charges that we have rejected in previous contracts. But the two parties agreed to them, it is obviously agreed to them, they signed the contract."

Transcript of September 2, 1999 Deliberations, p. 169.

[6] Director Kyle stated: "Since the public tariffs are not before the Authority in this proceeding, I do not draw any conclusions or make any decisions about the terms and conditions contained therein at this time." *Transcript of September 2, 1999 Deliberations*, p. 172.

BellSouth's efforts to negotiate termination charges other than the $350,000 termination provision.

4. The burden of proof in demonstrating that this CSA should be approved lay with BellSouth, and BellSouth carried its burden of proof.

5. The evidence put forth in the record fails to establish that the provisions of the CSA before the Authority are anti-competitive[7] or discriminatory.[8]

6. Authority Rule 1220-4-1-.07 permits public utilities and customers to enter into special contracts that prescribe and provide rates and services subject to the Authority's review and approval.

7. The evidence put forth in the record fails to establish that the rates resulting from the application of the Volume and Term discount violate the statutory price floor or force prices below cost.

8. The termination provisions in the CSA related to termination of the Volume and Term discount do not violate *Guiliano v. Cleo*. In *Cleo*, the Supreme Court adopted the "prospective approach" for "determining whether a liquidated damages provision constitutes a penalty." The Court stated:

> [T]he "prospective approach," focuses on the estimation of potential damages and the circumstances that existed at the time of contract formation. Under this approach, the amount of actual damages at the time of breach is of little or no significance to the recovery of liquidated damages. If the liquidated sum is a

[7] The evidentiary record reveals that during the course of negotiating with customers who have a competing offer in hand, BellSouth requires said customers to enter into an information exchange agreement and/or a nondisclosure form. *See Hearing Transcript, August 17, 1999,* Vol. I D, p. 283-87. Consistent with BellSouth's policy and practice, both the Bank and the Store signed such documents. *Id.* at 284. "[W]hile [the] negotiation process is going on, the customer cannot go to a competitor and say what BellSouth has offered." *Id.* at 285. Mr. Frame testified that competing providers employ nondisclosure practices as well. Chairman Malone is of the opinion that given the potential impact of such agreements in the developing environment, the Authority may later inquire further into such practices.

[8] With respect to the discrimination issue, Director Kyle found that "[n]o evidence was furnished which could support a showing that BellSouth has denied either CSA to similarly situated customers." *Transcript of September 2, 1999 Deliberations*, p. 172.

> reasonable prediction of potential damages and the damages are indeterminable or difficult to ascertain at the time of contract formation, then courts following the prospective approach will generally enforce the liquidated damages provision.
>
> . . . .
>
> . . . Under this approach, 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 satisfies those factors and reflects the parties' intentions to compensate in the event of a breach, then the provision will be upheld as a reasonable agreement for liquidated damages.

Guiliano v. Cleo, 995 S.W.2d 88, 98-99, 100-01 (Tenn. 1999) (citations and footnotes omitted).

9. It appears from the record that the liquidated sum was a reasonable estimate of potential damages given that the actual damages were difficult to measure at the time the parties entered into the CSA. The termination provisions reflect the parties' original intentions to compensate for termination of the contract. Further, the parties were in the best position to know what considerations influenced their bargaining at the time they entered into the contract. Given these conclusions, the contract termination provisions should be upheld as reasonable agreements between the parties.[9]

IT IS THEREFORE ORDERED THAT:

1. BellSouth Telecommunications, Inc.'s Tariff No. 99-00210, which seeks approval of Contract Service Arrangement No. TN 98-2766-00, is hereby granted.

2. Any party aggrieved with the Authority's decision in this matter may file a Petition for Reconsideration with the Authority within fifteen (15) days of the filing of this Order.

[9] Director Kyle stated: "I find that these termination provisions restore to BellSouth benefits that it has conferred upon the [bank] throughout contract performance . . . . I do not find these termination provisions to be unreasonable nor do I believe that such provisions have the effect of unreasonably locking the bank or the store into the respective volume and term agreements." *Transcript of September 2, 1999 Deliberations*, p. 174-750.

3. Any party aggrieved with the Authority's decision in this matter may file a Petition for Review with the Tennessee Court of Appeals, Middle Division, within sixty (60) days of the filing of this Order.

Melvin J. Malone, Chairman[10]

H. Lynn Greer, Jr., Director

Sara Kyle, Director

ATTEST:

K. David Waddell, Executive Secretary

[10] Prior to the consolidated hearing, Chairman Malone consistently voted against the approval of long term BellSouth CSAs that contain hefty termination provisions. Pursuant to previous action taken by the agency, a hearing was envisioned on each of the common issues then pending in TRA Docket No. 98-00559. Unfortunately, the consolidated hearing held in Docket Nos. 99-00210 and 99-00244 was not such a hearing. Certain compromises, however, have led to some positive, although limited, modifications to BellSouth's CSAs. It is due, in part, to said modifications, coupled with optimism that such amendments will continue, that Chairman Malone is able to support the result reached by his colleagues.

Moreover, one controlling fact cannot be either ignored or understated. According to the testimony, BellSouth was confronted with a bona fide competing offer as concerning both CSAs. *See Hearing Transcript, August 17, 1999, Vol. I A at 54; Pre-filed Testimony of Margaret Brown at 2; and Pre-filed Direct Testimony of Randall Frame at 5-8.* Significantly, the testimony supporting the assertion of a bona fide competing offer was either not challenged by the intervenors or was corroborated by them. Hence, these customers had what the Tennessee General Assembly and the United States Congress have declared that they should have - competitive choice. Notwithstanding the action taken here, Chairman Malone opined that the agency must remain ever mindful that the local telephony market in Tennessee is still in its infancy. During this delicate transitory period, the agency must be careful to employ assiduous reasoning and thoughtful analyses when reviewing BellSouth CSAs.

Chairman Malone emphasized the agency's conclusion that the "secondary" termination provisions related to the underlying tariff services were not at issue. If the agency had determined that the "secondary" termination provisions were, in fact, squarely before it in these consolidated cases, Chairman Malone would have yielded against approval on the grounds that the termination provisions, when taken as a whole, were so potentially anti-competitive as to warrant denial. When the agency reviews these "secondary" provisions, it must exercise care to not overlook or omit the fact that most, if not all, of the "secondary" termination provisions containing harsh buyouts were approved before the passage of both the State's Telecommunications Act of 1995 and the Federal Telecommunications Act of 1996. With few, if any, exceptions, the "secondary" termination provisions were approved during and in support of a rate base/rate of return environment. As is well known, the need to provide BellSouth with the opportunity to earn an authorized rate of return by guaranteeing its revenue streams via the allowance of severe termination provisions passed with the effectiveness of BellSouth's price regulation plan.