BEFORE THE MISSOURI PUBLIC SERVICE COMMISSION

In the Matter of AT&T Communications of the Southwest, Inc.'s Proposed Tariff to Establish a Monthly Instate Connection Fee and Surcharge	**)))**	**Case No. TT-2002-129**
In the Matter of Sprint Communications Company, L.P.'s Proposed Tariff to Introduce an In-State Access Recovery Charge and Make Miscellaneous Text Changes.	**))))**	**Case No. TT-2002-1136**
In the Matter of MCI WorldCom Communications, Inc.'s Proposed Tariff to Add an In-State Access Recovery Charge and Make Miscellaneous Text Changes.	**))))**	**Case No. XT-2003-0047**
In the Matter of MCI WorldCom Communications, Inc.'s Proposed Tariff to Increase its Intrastate Connection Fee to Recover Access Costs Charged by Local Telephone Companies.	**)))))**	**Case No. LT-2004-0616**
In Re the Matter of Teleconnect Long Distance Services and Systems Company, a MCI WorldCom Company d/b/a Telecom USA's Proposed Tariff to Increase its Intrastate Connection Fee to Recover Access Costs Charged by Local Telephone Companies.	**)))))))**	**Case No. XT-2004-0617**

INITIAL BRIEF OF MCI COMMUNICATIONS SERVICES, INC. AND TELECONNECT LONG DISTANCE SERVICES AND SYSTEMS COMPANY

Carl J. Lumley, #32869
Leland B. Curtis, #20550
CURTIS, HEINZ, GARRETT & O'KEEFE, PC
130 S. Bemiston, Suite 200
St. Louis, Missouri 63105
(314) 725-8788
(314) 725-8789 (FAX)
clumley@lawfirmemail.com
lcurtis@lawfirmemail.com
ATTORNEYS FOR: MCI Communications Services, Inc. and Teleconnect Long Distance Services and Systems Company

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Introduction

This proceeding concerns similar tariffs filed by MCI Communications Services, Inc. (MCI)[1], Teleconnect Long Distance Services and Systems Company (Teleconnect), AT&T Communications of the Southwest, Inc. (AT&T) and Sprint Communications Company, L.P. (Sprint) to establish and/or increase specific additional rate elements for their intrastate long distance services in Missouri, so that the overall charges for such services would better reflect the higher switched access charges imposed on them by Missouri local exchange carriers (LECs).

In this brief, MCI and Teleconnect specifically address their respective tariff filings, although by and large the legal arguments (and in some instances the facts as well) apply to all the tariffs at issue.

Facts and Procedural Background

MCI and Teleconnect presented the testimony of Andrew M. Graves, Director of Marketing Strategy and Policy for the Mass Markets Division of their ultimate corporate parent MCI, Inc. in support of the tariff provisions at issue in this proceeding. Mr. Graves has twelve years of experience in the telecommunications field, all with MCI, Inc. or its predecessor companies or subsidiaries. He has held his current position since February, 2004. (Ex 5, Graves Amended Direct, p. 1).

Mr. Graves' duties include overseeing all legal and regulatory issues related to marketing MCI, Inc.'s local and long distance services to residential customers. He works with the company's legal and regulatory groups to ensure favorable business conditions, and he works to make certain that the long distance and local operations comply with all regulations. He also

[1] See Case No. TN-2006-0014.

works very closely with sales and product marketing groups to help formulate sales plans and product and pricing strategies. As a result, Mr. Graves is personally knowledgeable about MCI, Inc.'s mass market customer base and MCI, Inc.'s and its subsidiaries' relationships with its mass markets customers. (Ex. 5, Graves Amended Direct, p. 1).

MCI Communications Services, Inc. is a Delaware corporation in good standing with the Missouri Secretary of State. It is a subsidiary of MCI, Inc. It was originally named WorldCom Technologies, Inc. In 1997, it obtained a certificate of authority to provide interexchange telecommunications services in Missouri from the Commission and was classified under Section 392.361 as a competitive company providing competitive services by the Commission in Case No. TA-98-16. In 1999, it was renamed MCI WorldCom Communications, Inc. in connection with mergers approved by the Commission in Case No. TM-99-588. (Ex. 5, Graves Amended Direct, p. 1-2).

After testimony was filed in this proceeding, on September 1, 2005 the Commission approved a change in MCI WorldCom Communications, Inc. name to MCI Communications Services, Inc. (Case No. TN-2006-0014).[2]

Teleconnect Long Distance Services and Systems Company is an Iowa corporation in good standing with the Missouri Secretary of State. It is also a subsidiary of MCI, Inc. Teleconnect was originally named Teleconnect Co. In 1987 it obtained a certificate of authority to provide interexchange telecommunications services in Missouri from the Commission in Case No. TA-86-114. In 1988, Teleconnect adopted the original tariffs of its parent company Teleconnect Co. In 1989, it was classified under Section 392.361 as a competitive company

[2] MCI requests the Commission to take notice of its proceedings in Case No. TN-2006-0014 regarding the name change.

providing competitive services by the Commission in Case No. TO-88-142. (Ex. 5, Graves Amended Direct, p. 2).

On August 3, 2002, pursuant to Section 392.500, MCI filed Original Tariff Page No. 40.2 for its Missouri PSC Tariff No. 1, adding section 6.10 Instate Access Recovery Fee, providing as follows:

> Instate Access Recovery Fee
>
> MCI(R) is charged to originate and terminate its instate long distance calls over other companies networks. MCI will assess a monthly fee to residential customers to recover these charges. Customers will be exempt from this charge during any monthly billing period where their MCI spending is less than $1.00.
>
> Residential Customers
>
> An Instate Access Recovery Fee of $1.95 per account per month will be applied to invoices of customers of the following residential services under this tariff.
>
> Option A (Dial One/Direct Dial)
> Option B (Credit Card)

The tariff was assigned no. 200300092. As the Commission has previously confirmed in its August 27, 2002 order referenced below, MCI provided at least 10 days advance notice to customers of the tariff filing as required by Section 392.500, by including a notice in customer billing. (Ex. 5, Graves Amended Direct, p. 3).

Public Counsel filed a motion to suspend the tariff filing, resulting in the opening of Case No. XT-2003-0047. After MCI and Staff responded, on August 27, 2002, the Commission issued its Order Denying Suspension and Approving Tariff with an effective date of September 3, 2002, which approved the tariff to become effective September 3, 2002. (Ex. 5, Graves Amended Direct, p. 3-4).

In approving the MCI tariff, the Commission noted that similar tariffs had recently been approved for AT&T (Case No. TT-2002-129) and Sprint (Case No. TT-2002-1136). (Ex. 5, Graves Amended Direct, p. 4).

Public Counsel pursued judicial review of all three of the foregoing orders. The Cole County Circuit Court initially affirmed the Commission's orders. However, on August 10, 2004, the Missouri Court of Appeals, Western District, reversed the Commission's orders and the matters were remanded to the Commission "with directions to make findings of fact and conclusions of law, in accordance with the Mandate of the Missouri Court of Appeals." (Ex. 5, Graves Amended Direct, p. 4).

In its Opinion, the Court of Appeals held that the Commission "failed to make sufficient findings of fact and conclusions of law to justify its orders." Specifically, the Court determined that the Commission "does not articulate, as required, the factual basis for its conclusion that the alleged [by Public Counsel] disparate treatment of residential, low volume, and rural customers was not a violation of 392.200.2 and .3 as claimed by OPC" and "fail[s] to articulate the factual basis for the Commission's conclusion that the proposed tariff revisions are just and reasonable." The Court indicated that the Commission "may reopen the case and hear additional evidence, if a majority of the Commission desires to do so. [citation omitted] Otherwise, it may make the required findings of fact and conclusions of law based on the evidence already presented." (Ex. 5, Graves Amended Direct, p. 4).

On May 28, 2004, MCI made a tariff filing that included, among other things, a first revised page 40.2 for Missouri PSC Tariff No. 1 that proposed an increase to the Instate Access Recovery Fee of $1.00 (an increase from $1.95 to $2.95). (Ex. 5, Graves Amended Direct, p. 5).

As the Commission has previously confirmed in its July 22, 2004 order referenced below, MCI provided at least 10 days advance notice to customers of this increase as required by Section 392.500, by including a notice in customer billing. This tariff filing was assigned number JL-2004-1424. Public Counsel filed pleadings opposing the tariff filing, which resulted in the opening of Case No. LT-2004-0616. (Ex. 5, Graves Amended Direct, p. 5).

The Commission suspended the tariff filing, directed MCI to respond to Public Counsel's pleadings (which it did), and held oral argument. On July 22, 2004, the Commission issued its Order Denying Suspension and Approving Tariff, effective August 1, 2004. (Ex. 5, Graves Amended Direct, p. 5).

At the same time, Teleconnect filed fourth revised page 14 to its Missouri Tariff No. 1, proposing the same $1.00 increase to the fee. (Ex. 5, Graves Amended Direct, p. 5).

When Teleconnect introduced the fee (after providing the required notice to customers), the tariff took effect as proposed without any formal proceedings before the Commission. The revised tariff page included the original tariff language, as only the rate was changed. The language is as follows:

> Instate Access Recovery Fee
>
> A monthly service charge that is applied to Customers subscribed to the Company for long distance services associated with a residential telephone line or billed to a residential account. This charge reflects costs incurred by the Company in providing in-state long distance service over Customer's local exchange provider's network. You will be exempt from this charge during any monthly billing period where your MCI spending is less than $1.00. The fee will be listed as a separate line item in your invoice as Instate Recovery Fee.
>
> Monthly Charge: $2.95

As confirmed by the Commission in its July 22, 2004 order referenced below, Teleconnect provided at least 10 days advance notice to customers of this increase as required by Section 392.500, by including a notice in customer billing. This tariff filing was assigned number JX-2004-1436. Public Counsel filed pleadings opposing the tariff filing, which resulted in the opening of Case No. XT-2004-0617. (Ex. 5, Graves Amended Direct, p. 6).

The Commission suspended the tariff filing, directed Teleconnect to respond to Public Counsel's pleadings (which it did), and held oral argument. On July 22, 2004, the Commission issued its Order Denying Suspension and Approving Tariff, effective August 1, 2004, and issued a subsequent Notice of Correction correcting errors in references to the tariff pages at issue. (Ex. 5, Graves Amended Direct, p. 6-7).

Public Counsel sought judicial review of the Commission's Orders in Case Nos. LT-2004-0616 and XT-2004-0617. Subsequently, as discussed above, the appellate proceedings regarding the initial MCI tariff filing were concluded. As a result, by stipulation, the cases concerning the $1.00 increases were remanded to the Commission for further consideration. (Ex. 5, Graves Amended Direct, p. 7).

In February 2005, the Commission reopened Case Nos. XT-2003-0047, LT-2004-0616 and XT-2004-0617 and set simultaneous conferences in those cases as well as the original AT&T and Sprint cases. Subsequently, the Commission consolidated these cases, informed the parties that it wanted to hear additional evidence on these tariffs, and directed the parties to file a proposed procedural schedule. The parties agreed to a proposed procedural schedule that the Commission then approved. (Ex. 5, Graves Amended Direct, p. 7).

Ultimately, the parties stipulated that the case be decided based upon the pre-filed testimony and briefs, without a hearing. The Commission approved that stipulation. (Order dated August 25, 2005).

MCI and Teleconnect continue to charge the fees that are at issue in this case, as the tariffs covering this rate remain in effect, pending final resolution of this matter. (Ex. 5, Graves Amended Direct, p. 7).

MCI and Teleconnect each have a wide variety of rates, depending on programs, plans, and discounts. As of the filing of testimony, MCI's highest rate for Option A (Dial One/Direct Dial) service was 25 cents per minute, MCI's highest rate for Option B (Credit Card) service was 55 cents per minute, and Teleconnect's highest rate was the top rate for its Hello America service at 25 cents per minute. (Ex. 5, Graves Amended Direct, p. 7-8).

However, as the FCC has observed, such basic schedule rates are essentially obsolete due to the availability of numerous calling plans. In its latest "Reference Book of Rates, Price Indices, and Household Expenditures for Telephone Service", (at p. iv, I4-I6) the FCC states:

> Toll Service Rates:
>
> ▪ The increased availability and marketing of discount and promotional long distance plans, as well as the popularity of wireless "bucket-of-minutes" plans, has made basic schedule rates obsolete for many long distance customers, particularly business customers and high volume residential consumers. Today wireline, wireless, and cable companies are offering consumers bundled packages of local and long distance service, and buckets of minutes that can be used to call anyone, anywhere, and anytime.
>
> ▪ The average revenue per minute of long distance calling, which reflects rates paid by residential and business consumers, has fallen from 15 cents in 1992, when discount and promotional long distance plans were introduced, to 7 cents in 2003, a decrease of 53%.[3]

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[3] This refers to interstate rates (see below).

- During 2004, the consumer price index for interstate toll service fell 8.7% and the consumer price index for intrastate service fell 6.6%, while the overall consumer price index rose 3.3%.

* * *

C. Toll Service Rates

Since 1992, carriers have introduced an impressive array of discount and promotional plans, and many long distance residential customers subscribe to these plans. These plans take a variety of formats. Some plans offer a block of calling times for a fixed fee and reduced per minute rates for additional calling while others give volume discounts or discounts for calls to certain phone numbers or area codes. One common trend has been the introduction of flat-rate calling plans, which eliminate the mileage bands associated with traditional basic schedules. For example, Verizon's "Freedom" plan offers unlimited long-distance and local calling (as well as unlimited voice mail, caller ID, call waiting, speed dialing, and three-way calling) for as low as $49.95 per month (not including add-on charges). In addition, Verizon offers discounts on its high-speed Internet and wireless offerings to those subscribers who sign up for the "Freedom" plan.

Section 271 of the Telecommunications Act of 1996 allowed the Regional Bell Operating Companies (RBOCs) to provide in-region interLATA toll services once the companies satisfied a fourteen-point "checklist" of conditions which demonstrates that their local exchange markets are open to entry by competitive local exchange carriers. All of the RBOCs attained section 271 approvals for their particular markets, and many are now offering discounted bundled packages of voice and popular calling features.

Wireless companies and prepaid calling cards offer more options for long-distance customers. Wireless companies now offer packages which enable customers to purchase a set number of minutes of usage per month at a set rate (some with unlimited nights and weekends) and allow customers to use these minutes for local or long distance calling. Consumers may also purchase prepaid calling cards, which contain an allotted number of minutes, with some charging rates less than three cents per minute.

Using revenue per-minute data for both residential and business interstate toll traffic, Table 1.15 illustrates the downward trend in long distance rates since discount long distance plans were introduced in 1992. The carriers' average revenue per interstate toll minute has fallen by 53% since 1992, demonstrating that the advent of discount long distance plans has produced lower rates for both business and residential consumers.

* * *

> 2. Toll Rates
>
> Up until August 2001, all interstate interexchange carriers were required to file tariffs setting forth their rates with the FCC. These filings were available for public inspection at the FCC's Reference Information Center, Washington, DC. As of August 1, 2001, interstate carriers were no longer required to file tariffs setting for their interstate long distance rates. Since that date, carriers are required to post their rates on their websites.
>
> The BLS publishes a number of price indices that follow trends in toll rates. Part III of this report reviews these indices. The most current figures can be obtained at stats.bls.gov.
>
> Finally, there are a number of firms that specialize in monitoring major long distance companies and their rates, and many of these firms maintain Internet sites. Some examples are Abtolls.com, a free directory service guide to long distance carriers and their rates; Telecommunications Research and Action Center, which uses a search engine to find the lowest long distance rates for any selected calling pattern; *Phone Bill Busters*, which lists discount long distance plans and uses a search engine to find the lowest long distance rates for any selected calling pattern; and *Discount Long Distance Digest*, an Internet newsletter which offers a "free multi-carrier cost comparison service." One can access these services on the Internet at www.abtolls.com, www.trac.org, www.phone-bill-busters.com and www.thedigest.com

(Ex. 5, Graves Amended Direct, p. 8-10).

There are hundreds of companies authorized to provide intrastate interexchange services in Missouri in competition against MCI and Teleconnect. Some are exclusively interexchange carriers, known as IXCs. Others also provide local services and are either incumbents (ILECs) that were providing local services before the passage of the Telecommunications Act of 1996 or are new market entrants known as alternative or competitive LECs (CLECs). According to the Commission's 2004 Annual Report, there are 495 authorized IXCs, 43 ILECs and 88 CLECs in Missouri. Most prominent among interexchange providers are the larger incumbent local exchange companies and their affiliates, such as SBC, Sprint, CenturyTel and Spectra. SBC is in the process of acquiring AT&T, which is another significant competitor. (Ex. 5, Graves Amended Direct, p. 10).

In November 2001, in Case Nos. TA-2001-475 and TA-99-47, when the Commission granted authority to a separate affiliate (then known as SBCS) of SBC Missouri to enter the interLATA market in Missouri pursuant to Sections 271 and 272 of the Telecommunications Act of 1996, it found that it "has regularly issued certificates to more than 600 IXCs - including affiliates of other ILECs - classified as 'competitive' in Missouri." Further, the Commission found that "A minimum of 74 carriers serve with 1+ service in each SWBT exchange in Missouri." And the Commission found that "the enhanced competition provided by SBCS in the long-distance market will 'ensure that customers pay only reasonable charges … for [those] services.'" (Ex. 5, Graves Amended Direct, p. 11).

Additionally, wireless carriers and VOIP providers offer long distance services. According to the FCC's December 2004 report there were 2,859,953 wireless subscribers (as compared to wireline subscribers of about 3.5 million) in Missouri, with 12 providers reporting. The Commission Telecommunications Staff reported these figures in their 2004 "In Review" report. VOIP providers are not required to obtain PSC certificates of authority. A copy of the Staff report is attached to Mr. Graves' testimony as **Schedule AG-1**. (Ex. 5, Graves Amended Direct, p. 11).

In the Brief (at page 12) that Public Counsel filed in the Circuit Court in the review proceeding concerning the original MCI tariff filing at issue, Public Counsel stated: "the competitive marketplace determines to what extent the carrier will seek to recover all or any part of [its] costs in its rates." Thus, Public Counsel has openly acknowledged that the long distance market is competitive in Missouri. A copy of the first page and page 12 of Public Counsel's

Brief is attached to Mr. Graves' testimony as **Schedule AG-2**. (Ex. 5, Graves Amended Direct, p. 11-12).

MCI and Teleconnect rates are competitive and as a result customers regularly select these companies to be their providers, and choose to remain with them. Prospective customers can easily obtain information to allow them to compare one provider to another. For example, the Commission's website provides rate comparisons and links to other sources for rate comparisons. Sample printouts of information obtained through the Commission's website are attached to Mr. Graves' testimony as **Schedule AG-3**. The FCC also provides guidance to people looking for a provider. A printout of information from the FCC's website is attached to Mr. Graves' testimony as **Schedule AG-4**. Each company also disseminates information to customers in a wide variety of ways, including TV, radio, print media, direct mail, and telemarketing. Additionally, each company posts rate information on its website. (Ex. 5, Graves Amended Direct, p. 12).

If an existing customer is dissatisfied with MCI's or Teleconnect's rates, it can easily change providers. Changing interexchange providers is something that customers do all the time. It is a simple process. A customer need only authorize the new provider to make the change (as well as lift any freeze on changes that the customer may have placed to guard against unauthorized changes). The Commission and the FCC have implemented rules to make certain that such changes are processed immediately. For example, see 4 CSR 240-33.150. Once the customer changes their presubscribed carrier, when they dial 1 plus the called telephone number, they will get service from the new carrier. Customers can even choose separate providers for intraLATA long distance and interLATA/interstate long distance (as well as international calling). (Ex. 5, Graves Amended Direct, p. 13).

Based on his experience and expertise, Mr. Graves testified that it was his opinion, to a reasonable degree of certainty, that the MCI and Teleconnect rates, including the fee at issue, are reasonable. He testified that these rates are reasonable charges for intrastate long distance service and are competitive with market rates charged by other companies, as shown above. He explained that this case concerns a total additional charge of less than $36 per year for MCI and Teleconnect customers that use the services in question. (Ex. 5, Graves Amended Direct, p. 13).

Mr. Graves further testified that the Commission can rely on the market to assure long distance rates are reasonable. He explained that under Section 392.185(6), the Commission can and should allow competition to function as a substitute for regulation to assure that rates are reasonable. (Ex. 5, Graves Amended Direct, p. 13).

In Case No. IO-2003-0281, the Commission released Sprint from price cap regulation for intrastate intraLATA long distance services throughout the state, which means the amount Sprint charges for such services has been deregulated. The Commission granted similar relief to SBC in Case No. TO-2001-0467, and although that decision was recently reversed and remanded, SBC has been able to set its prices without regulatory oversight as to reasonableness for a period of over four years and has not been required to change rates since the reversal of the Commission's decision. These two carriers serve areas in which the vast majority of the population of Missouri resides, and the Commission has been relying on the market to control intraLATA toll prices charged by them throughout the state. (Ex. 5, Graves Amended Direct, p. 13-14).

SBC witness Craig Unruh recently testified in Case No. TO-2005-0035 that:

> "SBC Missouri did restructure its intraLATA toll service because the competitive market for toll had evolved to a different pricing structure. Prior to a competitive classification, SBC Missouri's intraLATA toll pricing was based on numerous mileage bands so the price of a call depended on how far the call was between the

> two parties (e.g., a 10 mile call cost less than a 50 mile call). The marketplace for basic long distance had evolved to a more simple time of day approach where it no longer mattered how far you were calling. To remain competitive, SBC Missouri restructured its toll pricing to match the structure that had become prevalent in the marketplace."

A copy of this testimony excerpt (pages 13-14) is attached to Mr. Graves' testimony as **Schedule AG-5**. (Ex. 5, Graves Amended Direct, p. 14).

Under SB 237, the Commission has recently been releasing more ILEC companies and services from price caps. (See Case Nos. TO-2006-0092, TO-2006-0093, TO-2006-0102, TO-2006-0108, TO-2006-0109).

As discussed above, SBC has been providing interLATA long distance services through SBCS n/k/a SBC Long Distance, Inc. under Section 272 of the Telecommunications Act of 1996, and while the obligation to use a separate subsidiary expired in November 2004 it appears SBC continues to provide such services through the subsidiary. The Commission granted authority to the subsidiary in Case Nos. TA-2001-475 and TA-99-47, and classified the company and its services as competitive. (The company changed its name to the current one in Case No. TN-2005-0149). (Ex. 5, Graves Amended Direct, p. 14-15).

Mr. Graves testified that MCI and Teleconnect regularly monitor the rates charged by their competitors and make sure that their rates remain competitive. (Ex. 5, Graves Amended Direct, p. 15).

As Mr. Graves testified, it does not make a difference in terms of what the customer pays, whether the fee is stated as a separate surcharge or simply included in the rate. Either way, the customer's total payment would be the same. (Ex. 5, Graves Amended Direct, p. 15).

Mr. Graves explained that MCI and Teleconnect want the fee at issue to be a separate charge, rather than simply including it in the base rates, because the companies offer services throughout the country and need uniform base rates for market-driven block-of-time or all-jurisdiction pricing. MCI and Teleconnect disclose during their marketing activities that additional charges can apply depending on location. As discussed above, existing customers were given notice when the fee was introduced, and when it was increased, as required by law. And of course, customers are reminded of the charge each time it appears on their bill and can always change carriers if they are dissatisfied. The fee is not hidden from customers. (Ex. 5, Graves Amended Direct, p. 15).

MCI and Teleconnect introduced the fee, and subsequently increased it, because the rates charged to them by local exchange carriers for originating and terminating switched access services (that enable long distance calls to originate and terminate on the local facilities that serve the end user) are significantly higher in Missouri than in some other states. MCI and Teleconnect introduced the fee and increased it in an effort to have total rates that take these unusually exorbitant access charges into account. (Ex. 5, Graves Amended Direct, p. 15-16).

As reflected in the Telecommunications Department Staff's 2004 "In Review" report (which provides further information regarding switched access charges at pages 9-11), average access charges in Missouri can be as high as 26.63 cents per minute, depending on the local exchange carrier. The Staff's chart shows ILEC rates, and CLECs are allowed to charge as much as the ILEC under the standard conditions that the Commission includes with CLEC certificates of authority. (Ex. 5, Graves Amended Direct, p. 16).

Staff witness Ben Johnson testified in Case TR-2001-65 that Missouri rates are generally higher than rates in other states. He stated:

> "The Missouri rates are generally higher. Rates for other states are set forth on Schedule 6. The total rates range from a low of $0.0029 to a high of $0.0998 with an overall average of $0.0240. The average rate of the Missouri large ILECs is close to the high end of the national range and considerably higher than the

average of the other states. The average rate of the small Missouri ILECs is also much higher than the average rate charged by the ILECs in the other states. However, the latter comparison must be viewed with caution, since the rate data from other states was obtained from large ILECs."

A copy of page 134 of Mr. Johnson's Direct testimony, together with his Schedule 6, is attached to Mr. Graves' testimony as **Schedule AG-6**. (Ex. 5, Graves Amended Direct, p. 16).

AT&T witness Matthew Kohly testified in the same case, stating:

> "Undeniably, Missouri's access rates are among the highest in the nation. Based upon AT&T's own data, Missouri ranks fifth in the nation for the highest average switched access rates. The only states exceeding Missouri in this category are North Dakota, South Dakota, New Mexico, and Alaska."

A copy of page 24 of Mr. Kohly's Surrebuttal testimony is attached to Mr. Graves' testimony as **Schedule AG-7.** (Ex. 5, Graves Amended Direct, p. 16-17).

In its Report and Order in Case TR-2001-65, the Commission acknowledged that Missouri switched access charges are high and problematical. The Commission stated at pages 11-13 (footnotes deleted):

> "Intrastate exchange access, or switched access, is a telecommunications service that permits interexchange calls between subscribers located in different local exchanges within the state of Missouri. It is a wholesale service that local exchange telecommunications companies sell to other carriers to permit them to "access" their customers through their networks. A long distance or "toll" call incurs access charges at each end, originating and terminating. Switched access is not sold to end users, that is, residential and business customers, but to other telecommunications carriers. The access charge regime came into existence in 1983 with the break up of AT&T."
>
> "Switched access service is a locational monopoly. Consequently, competitive pressure cannot exert sufficient market discipline to maintain access rates at a reasonable level in the absence of a cap. For ILECs subject to price-cap regulation, the cap is provided by the provisions of Section 392.245, the Price Cap Statute. For ILECs subject to traditional rate-of-return regulation and for telephone cooperatives, the cap is found in the Commission's authority to directly set access rates. For CLECs, the cap is imposed by the Commission as a condition of competitive classification."
>
> "Historically, state commissions and the federal government have acted to keep residential telephone service rates low in order to encourage a high level of

> participation in the local telephone network by residential customers. As a result, business rates, toll rates and access rates have historically been set high, in order to produce sufficient revenue to support the low residential rates. In Missouri, urban areas provide such support to rural areas, business customers support residential customers, and heavy users of toll services support light users. Additionally, high access rates provide important support in high cost, rural areas."
>
> "IXCs, such as AT&T, have complained about high Missouri intrastate switched access rates for years. High switched access rates impact the carriers that terminate toll calls to those exchanges and necessarily result in higher prices for toll services. Some IXCs refuse to serve some rural areas because of high access rates. Others have imposed access recovery surcharges in Missouri. Additionally, these high access rates discourage the small ILECs from cooperating to provide expanded local calling scopes to their subscribers. For example, it is difficult for a carrier to offer its subscribers either an expanded calling scope plan or a block-of-time plan for a monthly charge when it has to pay high access charges per minute to another ILEC to terminate those calls. Lower access rates would make plans of this sort more attractive. High access rates also distort the IXC market, create disincentives for IXCs to serve certain markets, and provide opportunities for discriminatory pricing. They are anti-competitive and deter local market entry by imposing increased business expenses on new entrants."

(Ex. 5, Graves Amended Direct, p. 17-18).

MCI and Teleconnect have these fees in other states for the same reason, including Alabama, Arkansas, Arizona, Colorado, Florida, Georgia, Iowa, Idaho, Kansas, Kentucky, Maryland, Michigan, Minnesota, Mississippi, Montana, North Carolina, North Dakota, New Hampshire, New Jersey, New Mexico, New York, Ohio, Oklahoma, Oregon, Pennsylvania, South Dakota, Texas, Utah, Virginia, Washington, Wisconsin, and Wyoming, where switched access charges are also well above their economic cost. (Ex. 5, Graves Amended Direct, p. 18).

Mr. Graves testified that there is not anything unusual about including such an additional charge in the rate structure. To the contrary, such additional charges are common. Many carriers exercise their business judgment to have multiple components in their rate structures. Indeed, it has always been commonplace in the industry to have multiple rate elements for various services. It even appears that other companies have the same type of surcharge in Missouri and are not the subject of any pending challenge. At the oral argument regarding the increase to the MCI and Teleconnect fee, Staff counsel referred to US Telecom and Artech Telecom as examples (Case Nos. XT-2003-256, XT-2003-267, XT-2003-268). (Tr. 78-79). (Ex. 5, Graves Amended Direct, p. 18).

MCI and Teleconnect set rates within the constraints of the market. Cost studies are not conducted. Overall the companies derive a profit by controlling expenses and generating sufficient revenues. In this instance, because the cost of switched access is outside the companies' control, additional revenues are obtained through the fee. (Ex. 5, Graves Amended Direct, p. 19).

The fee at issue applies to residential customers who subscribe to MCI's option A (dial one/direct dial) and option B (credit card) intrastate long distance services, and to residential customers who subscribe to Teleconnect's intrastate long distance services. The charge does not apply if other MCI spending is less than $1.00 for the monthly billing period. The charge does not apply to customers who subscribe to other services, but rather only to those that subscribe to these specific intrastate long distance services. It is an intrastate long distance rate element. The charge does not apply if MCI spending is less than $1.00, because the companies do not feel it is necessary to apply the charge to customers with such minimal usage. (Ex. 5, Graves Amended Direct, p. 19).

The charge does not apply if the customer also subscribes to MCI local service. Mr. Graves testified that it was never MCI's intent to apply the charge to long distance customers that also subscribe to MCI local service. The tariff does not clearly state this exemption, but MCI has not applied the charge to its local customers. Upon the conclusion of these proceedings, MCI needs to revise the tariff to make this exemption clear. (Ex. 5, Graves Amended Direct, p. 19).

The charge does not apply to MCI's local service subscribers, because when MCI provides local service through its own facilities, including unbundled local loops and either its own switches or unbundled switching, its long distance affiliate does not have to pay originating access charges to an unrelated carrier. In some instances the other party to the call will also be an MCI local customer, and external terminating access charges will also not apply, but on average MCI incurs only about half of the external access costs when the long distance customer is also its local service customer. The charge at issue does not come close to recovering all the excessive access costs imposed on MCI in Missouri, but MCI nonetheless concluded that it was reasonable to exempt its local customers from the charge. (Ex. 5, Graves Amended Direct, p. 20).

Residential and business long distance rates are not the same. As has been common practice in the industry for decades, there are various differences between the rates charged to businesses and the rates charged to residential customers. During the oral argument regarding the tariff pages that increased the MCI and Teleconnect fees, counsel for Public Counsel stipulated that business and residential customers are two separate classes of customers. (Tr. 46-47). (Ex. 5, Graves Amended Direct, p. 20).

Mr. Graves testified that there is not anything unusual about using a fixed fee to partially recover costs that vary with usage. He explained it is simply a matter of business judgment that the simplicity of the flat rate is preferable to adding a rate element that varies with usage. In this case, the unique access costs that are of concern will vary with usage, but MCI and Teleconnect decided that a flat rate element was the appropriate choice. As indicated above, if customers disagree they can simply choose a provider with a different rate structure. Typically, a residential customer will have varying usage from month to month, and an average or flat rate applies fairly to all. (Ex. 5, Graves Amended Direct, p. 21).

The fee at issue does not apply differently to urban versus rural customers. (Ex. 5, Graves Amended Direct, p. 21).

The fee at issue in this case does not violate the Commission's new rule that will take effect on October 15, 2005 after proceedings in Case No. TX-2005-0258. The rule implicitly confirms that such separate charges are acceptable, but would establish "minimum requirements for clarity in billing separately identified charges." Consistent with the rule, MCI and Teleconnect do not misrepresent the fee to be a governmentally mandated or authorized fee. (Ex. 5, Graves Amended Direct, p. 21).

In its Second Report and Order, Declaratory Ruling, and Second Further Notice of Proposed Rulemaking, in CC Docket No. 98-170 (Truth and Billing Format), Adopted March 10, 2005 and Released March 18, 2005, the FCC reiterated that its rules permit non-misleading line item fees. Specifically, the FCC concluded that there is no basis to conclude that line item charges are unreasonable. (Ex. 5, Graves Amended Direct, p. 21-22).

In surrebuttal testimony, Mr. Graves responded to the rebuttal testimony filed by Staff witness Voight and Public Counsel witness Meisenheimer.

On page 5 of his rebuttal testimony, Mr. Voight discusses the impact of Senate Bill 237 upon the prior holding of the Court of Appeals regarding the tariffs at issue in this proceeding. Mr. Graves observed that:

> "Senate Bill 237 does seem to make a pertinent change in the statutes, in that new text added to Section 392.500 indicates that subsection 1 of Section 392.200 will no longer apply to rate changes under Section 392.500." He also stated that "new section 392.200.12 indicates that subsections 1 through 5 will not apply to packages of services, which would seem to have a bearing upon arguments about exempting local customers from the interexchange fee at issue." And he indicated

> that "at least in some instances customer-specific pricing for business customers will be authorized under subsection 392.200.8."

He also explained how new text in section 392.245.1 may have a bearing upon arguments about the reasonableness of rates in some instances. He stated, "For example, even with the surcharge MCI's rates are less than SBC's capped daytime rates of 0.27 for residents and 0.302 for businesses[4] and, therefore, would seem to be presumptively reasonable under the statute." He suggested that changes in section 392.245.5 would also seem to have a bearing upon the differences between business and residential services. (Ex 6, Graves Surrebuttal, p. 1-2).

Mr. Graves noted that it does not appear that Ms. Meisenheimer has any background regarding marketing or competitive pricing. He stated, "The background she describes appears to be exclusively based upon 'traditional' utility regulation of earnings and rate design." He also commented that her testimony is "long on unsubstantiated commentary and short on factual information." (Ex 6, Graves Surrebuttal, p. 2).

Mr. Graves responded to Ms. Meisenheimer's summary of her "specific objections" to MCI's rate design, located on pages 8-11 of her rebuttal testimony. First, he noted that she objects to the fact that the fee at issue can apply "even in cases in which customers have no instate calling." He noted that she also objects to the use of a flat rate when underlying costs are charged on a per-minute basis. Mr. Graves responded that "it is evident throughout her testimony that Ms. Meisenheimer confuses the way in which companies set end user rates with the way in which costs are determined." For example, he observed that "the majority of the industry currently offers 'all you can eat' plans, where consumers purchase a flat rated bucket of minutes covering all of their transactions." With such a plan, he explained, "the company determines how to recoup its costs for providing the service based on estimates of gross usage volumes for

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[4] SBC Missouri Mo PSC Tariff No. 26, 24th revd sheet 21 (effective 7-15-04).

all of its customers." Mr. Graves testified that "the market dictates that flat rates must be used more and more, in order to satisfy customer demands and expectations." He explained that, "While there cannot be a perfect match between usage sensitive costs and flat rates, experience has allowed MCI to estimate these costs and develop pricing plans accordingly." As to Ms. Meisenheimer's point that the result can be that "customers who use less will pay proportionately more", Mr. Graves observed that "this principal applies throughout our economy as a result of the myriad forms of available volume discounts." He also pointed out that subsection 392.200.5 expressly authorizes volume discounts. Further, he noted that "customers are free to alter their usage and do so all the time, so there really is no set class of 'customers who use less'". (Ex 6, Graves Surrebuttal, p. 2-3).

Next, Mr. Graves responded to Ms. Meisenheimer's argument that MCI cannot consider the differential between interstate and intrastate access rates without taking into account the Federal Subscriber Line Charge. "What she fails to disclose," he observed, "is that MCI as an IXC does not receive the Federal Subscriber Line Charge, as it applies to local bills and is recovered by LECs." Accordingly, Mr. Graves testified that "it is in fact appropriate for MCI to ignore an unavailable revenue stream when it designs its interexchange rates." Moreover, Mr. Graves explained that "the existence of the SLC is yet another reason why it is perfectly appropriate to exempt MCI's own local customers from the fee at issue, notwithstanding Ms. Meisenheimer's seemingly inconsistent objection to that exemption." Further, he stated that "the SLC demonstrates the propriety of using a flat surcharge." (Ex 6, Graves Surrebuttal, p. 3).

Mr. Graves responded to Ms. Meisenheimer's objection to the fact that the fee only applies to residential customers. He said "the nature of her arguments on this point later in her testimony demonstrate that her argument could only hold sway if the Commission were to conclude that all existing rate differences between residential and business customers are unlawful and unreasonable (including, for example, the SBC long distance rates cited above)." Further, he testified, "In fact, the legitimacy of rate designs that treat residential and business customers differently is so well established that it is hard to give serious attention to Ms. Meisenheimer's objection." He observed that "Even the most recent changes to the Missouri telecommunications statutes confirm that business and residential customers are distinct customer classes. (See 392.200.8 and 392.245.5)." Mr. Graves concluded, "At bottom, her objection is simply another unsubstantiated attack on the discretionary business judgment of the companies regarding rate design." (Ex 6, Graves Surrebuttal, p. 4).

Mr. Graves pointed out that "Ms. Meisenheimer makes the fallacious argument that the fee effectively discriminates against rural customers who cannot qualify for the local exemption, when in fact any long distance customer that is not also a local customer is not eligible for the exemption, regardless of where they live, whether urban or rural." (Ex 6, Graves Surrebuttal, p. 4).

Finally, Mr. Graves responded to Ms. Meisenheimer's contention that MCI's direct evidence is inadequate and her unexplained assertion that the surcharge does not meet the standards of subsections 4(1) and 5 of Section 392.200. Mr. Graves stated:

> "While our attorneys will address the statutes in argument and brief, I feel that I should at least point out that subsection 4(1) has nothing to do with this case, as MCI does not propose to define a service as different based upon geographic area or market segmentation. It also does not appear to me that subsection 5 applies, and again I would note the potential impact of Senate Bill 237 in the immediate future. The service at issue is the same in all areas and has a rate design that properly takes various conditions and circumstances into account." (Ex 6, Graves Surrebuttal, p. 4-5).

He continued:

> "Regarding our direct evidence, notwithstanding Ms. Meisenheimer's unsubstantiated comments, I submit that the companies have all demonstrated that the fees in question are lawful, just and reasonable. She contends that our explanation of the thought process that led to the fees in question is 'brazen' and 'compelling', but does not offer any explanation. She issues vague warnings about opening the 'floodgates', but she offers no details. Public Counsel's position appears to be that the Commission was wrong in finding interexchange services to be competitive, yet the Commission's decision in Case No. TO-88-142 states that Public Counsel stipulated to the point. Since 1988 long distance rates have consistently moved downward. As reported in the FCC's 2005 Reference Book, the average revenue per minute from long distance calling has fallen from 15 cents in 1992 to 7 cents in 2003, a decrease of 53%. Further, the Reference Book at page iv states 'During 2004, the consumer price index for interstate toll service fell 8.7% and the consumer price index for intrastate toll service fell 6.6%, while the overall consumer price index rose 3.3%.' It would seem indisputable that competitive market forces are keeping long distance rates reasonable, despite Public Counsel's attempts to 'sound an alarm.'" (Ex 6, Graves Surrebuttal, p. 5-6).

Starting at page 11 of her rebuttal, Ms. Meisenheimer makes general arguments about all the fees at issue. First, she responds to AT&T witness Rhinehart's testimony about the Commission's authority. Mr. Graves replied:

> "As I indicated above in response to Mr. Voight's testimony, it would appear that there are statutory changes that will take effect on August 28, 2005 and that will have a bearing upon the Commission's authority regarding these tariffs. I would also observe that Section 392.185 does not appear to be an independent source of authority, but rather a source of interpretative guidance. I do not mean to argue these points, as the attorneys can present our legal arguments. I simply want to alert the Commission that this is a point of controversy." (Ex 6, Graves Surrebuttal, p. 6).

Next Mr. Graves addressed Ms. Meisenheimer's response to Sprint witness Appleby's testimony regarding the competitive nature of the long distance market.

> "Ms. Meisenheimer does not dispute that the Missouri long distance market is competitive, or "highly competitive" to use Mr. Appleby's words. Instead she skirts the issue and hypothesizes that it might be possible to have unreasonable rates in a competitive market. In doing so, she ignores all the facts presented by the companies regarding the overall decline in long distance rates and diminished reliance upon usage charges due to competition. She totally misses the point that customers <u>will</u> change providers if their current carrier's rates become

> unreasonable. She totally ignores the statutory intent (set forth in the statute she cites on the same page) to allow competition to substitute for regulation to assure that rates are reasonable, and instead argues that the Commission should analyze the rates in question without regard to the level of competition in the market, stating that 'section 392.200 contains no excuse for competition.' This statement exemplifies her unfortunate bias towards a traditional monopoly regulatory approach that has no application to the long distance market of 2005." (Ex 6, Graves Surrebuttal, p. 6-7).

At page 12 of her rebuttal, Ms. Meisenheimer discusses the companies' compliance with state and federal rules. Mr. Graves responded as follows:

> "I would simply observe that she tacitly admits that the companies all have complied with state and federal rules. MCI's charges are clearly stated on its bills and customers are able to call 1-888-624-5622 toll free or access the company website at www.mci.com/service to obtain additional information." (Ex 6, Graves Surrebuttal, p. 7).

At page 13 of her rebuttal, Ms. Meisenheimer again criticizes the companies for charging different rates to residential customers than to business customers. Mr. Graves responded:

> "She admits on page 14 that these are two different customer classes. And of course they are, and have been recognized as such for years. One would not think that Ms. Meisenheimer would want residential customers to have to pay the same local rates as small businesses, yet that is the direction her testimony would lead the Commission. It is not discrimination to charge different rates to different classes of customers, regardless of cost considerations. The companies have the business discretion to develop different rates for different classes of customers. As the other IXC witnesses have testified, different parts of the companies are responsible for making such decisions and that is because totally different analyses are involved." (Ex 6, Graves Surrebuttal, p. 7-8).

At page 14 of her rebuttal, Ms. Meisenheimer again criticizes the exemption afforded to local customers. Mr. Graves replied:

> "Again, she totally ignores the facts and makes a nonsensical argument. Local residential customers are exempted because there is a cost difference. On the prior two pages of her testimony, she argues that we cannot charge different rates to different classes of customers without showing a cost difference, yet now she argues that we cannot charge different rates to customers within the same class when there is an indisputable cost difference. Basically, Ms. Meisenheimer shows over and over that she does not like our surcharges and based solely on her personal preference contends that the Commission

> should override the market and reject them. But any customer that shares her preference can simply change carriers - they do not have to come to the Commission and try to make a mountain out of a molehill. Further, as I have already testified, there is no basis for her conclusion that there is different treatment of rural customers versus urban customers." (Ex 6, Graves Surrebuttal, p. 8).

At page 15 of her rebuttal, Ms. Meisenheimer argues that the difference between interstate access and intrastate access rates is irrelevant. Mr. Graves responded:

> "Her opinions would no doubt be different if she had to pay switched access rates. I have not delved into the record in the TR-2001-65 case, as she purports to have done (she does not support any of her assertions with citations). But I have examined the Commission's Order - and I understand that it is the Commission that decides what the evidence in a case shows, not the parties. As I quoted in my direct testimony (p. 17-18), the Commission found that Missouri switched access charges are problematical. To quote another portion (p. 20) of the Commission's Order, 'The evidence is persuasive that access rates are high in comparison to costs for all of the LECs.' Ms. Meisenheimer would apparently have written the order differently, but that is not her prerogative.
>
> "IXCs pay different switched access rates depending on whether a call is interstate or intrastate. They are entitled to charge different rates for such calls. They are entitled to exercise their business discretion in deciding how to do that, including by choosing to use a combination of usage charges and flat rates." (Ex 6, Graves Surrebuttal, p. 9).

Finally, at page 16 of her rebuttal, Ms. Meisenheimer purports to sponsor a schedule to illustrate "absurd results and discriminatory effects." In response, Mr. Graves stated:

> "She offers no explanation of the purported illustration. What I see is that customers with lower volumes can effectively have a higher rate per minute. That is a very normal pricing structure. And it is certainly to be expected when there is a combination of flat and usage sensitive rates. I also see that there can be instances where customers with no intrastate calling in a particular month will pay the fee. Again, that is simply part of the rate design. Finally, I see that local customers do not pay the fee, which is of course true because they are not subject to it for the reasons set forth herein and in the direct testimony of all the company witnesses." (Ex 6, Graves Surrebuttal, p. 9-10).

Mr. Graves concluded his surrebuttal testimony by stating,

> "I have reviewed the Commission's recent comments to the FCC and am aware that at least some Commissioners seem to share Public Counsel's general dislike for surcharges. I find that most unfortunate. There is no distinction in terms of financial impact on

> customers between the various surcharges that the government places on telephone bills and company surcharges. A dollar is a dollar to the customer. There is no sound reason for government to be willing to utilize such surcharges for its purposes, but then turn around and restrict use of them in a competitive market. A debate over the clarity of specific charges may certainly be appropriate, but that is not the issue here. As the FCC has concluded in its *Second Report and Order, Declaratory Ruling, and Second Further Notice of Proposed Rulemaking*, In the Matter of Truth-in-Billing and Billing Format, CC Docket No. 98-170 (March 18, 2005), companies have a legitimate right to make use of such surcharges as part of their rate designs. The Commission should abide by that decision and not allow personal biases and preferences such as those put forth by the witness for Public Counsel to override the varied desires of customers that are being addressed fairly in the competitive market. Companies must be allowed the discretion to design their competitive rates in the way they conclude will work best. Customers (and competitive responses) will determine whether or not the companies make good decisions. If companies make mistakes, the market will correct them very quickly and often permanently, as a customer lost due to dissatisfaction is a customer that is quite difficult to regain." (Ex 6, Graves Surrebuttal, p. 10-11).

Throughout these lengthy proceedings, the companies have more than adequately defended their tariffs. Despite Public Counsel's ongoing opposition, neither the Commission or the courts have found anything wrong with the tariffs. The companies simply ask the Commission to stand by its prior approvals of the tariffs and issue a more detailed decision to meet the requirements of the courts. (Ex. 5, Graves Amended Direct, p. 22).

Argument

I. Based on the following sub-issues, should the Commission reject the AT&T, Sprint and MCI tariffs at issue in this case?

No, based on the following sub-issues, the Commission should allow the tariffs at issue in this case to remain in effect.[5]

A. Should the Commission apply the provisions of subsection 392.200.1 to the AT&T, Sprint and MCI surcharges at issue, and if so, are the surcharges just and reasonable under subsection 392.200.1?

The MCI companies involved in this proceeding are competitive companies providing competitive services pursuant to the provisions of Section 392.361. (Ex. 5, Graves Amended Direct, p. 1-2). Like AT&T and Sprint, with the prior authorization of the Commission under Section 392.500, the MCI companies currently charge a distinct line item fee to residential long distance service customers (who are not also MCI local service customers) to help offset the high intrastate switched access charges that these companies must pay to other local carriers for the origination and termination of long distance calls. MCI customers with spending under $1.00 in a particular month are exempt. (Ex. 5, Graves Amended Direct, p. 3-7, 15-16, 19).

Since August 28, 2005, when SB 237 took effect, Section 392.200.1 has not applied to the surcharges at issue. Moreover, to the extent the Commission previously had the discretion to apply Section 392.200.1 to the surcharges at issue, it correctly determined that the surcharges were (and they still are) just and reasonable. The long distance market remains

[5] Per Order issued on March 30, 2005, "Any issue not contained in this list of issues will be viewed as uncontested and not requiring resolution by the Commission."

competitive and MCI's rates, including the surcharges, remain competitive. The Commission has regularly and properly ruled that competition in the Missouri long distance market assures the reasonableness of rates, consistent with statutory guidance. Indeed, MCI's rates are less than those of price cap companies and, therefore, by statute are deemed reasonable. Customers can readily obtain rate information, shop around, and choose either to stay with their provider or to change providers based on rates or other competitive factors such as service. Many customers stay with the MCI companies, demonstrating that they find value in MCI's services and reasonableness in MCI's rates.

There is nothing unjust or unreasonable about the surcharge being a separately stated charge, rather than being rolled into other rate elements. The customer's payment amount would be the same in either instance. A separate charge is appropriate because intrastate access charges vary from state to state and are particularly high in Missouri. The charge is properly disclosed and complies with federal and state regulations (including new Missouri regulations taking effect in October).[6] MCI has properly exercised its business discretion in setting its rate structure in Missouri and the Commission should continue to refrain from interfering with MCI's business decisions regarding its competitive rates.

As indicated above, the law applicable to the tariffs at issue changed on August 28, 2005 when Senate Bill 237 took effect.

In particular, SB 237 revised Section 392.500, by adding the limitation that only subsections 2 to 5 of Section 392.200 apply to changes in tariffs regarding competitive telecommunications services. Because of this amendment, subsection 1 of Section 392.200 can no longer be said to apply to competitive tariff filings such as those at issue in this case.

[6] Compliance with these rules has not been presented as an issue in this case. Indeed, Public Counsel tacitly admits compliance. (Ex. 6, Graves Surrebuttal, p. 7; Meisenheimer Rebuttal, p. 12).

Thus, while the Court of Appeals held in the prior proceedings regarding these tariffs that the Commission had discretion pursuant to Section 392.361.5 and 392.390 to decide whether to apply the "just and reasonable" standard of subsection 1 to competitive tariff filings, (150 S.W. 3d at 100), the Legislature has now taken away such discretion away with the revision to Section 392.500. Accordingly, now that subsection 1 of Section 392.200 expressly no longer applies to competitive tariff filings, the Commission no longer has the discretion to consider Public Counsel's complaints regarding the reasonableness of the tariffs at issue.

When the Court of Appeals remanded these proceedings, it directed the Commission to make new findings regarding its discretionary consideration of Public Counsel's assertions regarding subsection 1 of Section 392.200. Given the change in law, the Commission should now address this point solely by conclusions of law that discuss the new legislation and the elimination of this aspect of its prior discretion.

Having said all that, MCI's rates, including the fees at issue, remain reasonable as previously determined by the Commission.

The rates, terms and conditions for the intrastate long distance services of the MCI companies - competitive services - are constrained by what the market will bear. There are hundreds of companies competing against MCI and Teleconnect in Missouri. (Ex. 5, Graves Amended Direct, p. 10-11). Customers have extensive options, and may choose MCI or Teleconnect. (Id. p. 12). They can easily change providers. (Id. p. 13).

Mr. Graves specifically opined that the MCI and Teleconnect rates are reasonable. He indicated the rates are competitive and that the Commission can rely on the market to assure reasonableness. He testified that the companies regularly evaluate the market to ensure their rates remain competitive. (Ex. 5, Graves Amended Direct, p. 13-15).

Mr. Graves explained that the fees in question only apply to specific pricing plans, and that customers have many choices even while remaining with MCI and Teleconnect. Further, he described how the basic pricing plans to which the surcharges apply are nearly obsolete due to the numerous calling plans that are available. For those customers that like the pricing plans affected by the surcharge, their total payment would be the same regardless of whether the fee is separately stated. But by stating it separately, MCI and Teleconnect can communicate the differences in prices between various states based on differences in switched access charges. (Ex. 5, Graves Amended Direct, p. 7-10, 15; Ex. 6, Graves Surrebuttal, p. 5-6).

From the outset of these proceedings, the statutes have required that the Commission generally rely upon market forces rather than apply the close scrutiny historically reserved for monopoly telephone service rate changes. See, e.g. Section 392.185. And again, with recent revisions to Section 392.500 the statutes now preclude any scrutiny of the "reasonableness" of such rates.

The Commission has been routinely relying on such market forces to assure reasonableness. When it authorized SBC's affiliate to enter the market, it stated: "The enhanced competition provided by SBCS in the long distance market will ensure that customers pay only reasonable charges." (Ex. 5, Graves Amended Direct, p. 11, 14-15). Since then, the Commission has relieved Sprint and SBC from any rate regulation over intrastate long distance services (although its SBC decision was remanded). (Ex. 5, Graves Amended Direct, p. 13-14).

In the proceedings under review, the Commission properly allowed the modest increase contained in MCI's tariffs at issue to take effect under prior law, because there was no reason to conclude the increase would result in unreasonable rates. The Commission expressly considered the reasonableness of the tariff change as a whole, stating in its Order:

> MCI WorldCom is a competitive company providing competitive telecommunications services. A proposed tariff that increases rates or charges of a competitive telecommunications company is governed by Section 392.500(2). That statute allows a proposed tariff increasing rates or charges to go into effect after the proposed tariff has been filed with the Commission and the affected customers are given at least ten days' notice. The Commission finds that MCI WorldCom has complied with the technical requirements of Section 392.500(2).
>
> In interpreting the various provisions of Chapter 392, the Commission turns to the purposes of the chapter as specified in Section 392.185.
>
> That section states in part:
>
> The provisions of this chapter shall be construed to:
>
> * * *
>
> (4) Ensure that customers pay only reasonable charges for telecommunications service;
>
> (5) Permit flexible regulation of competitive telecommunications companies and competitive telecommunications services;
>
> (6) Allow full and fair competition to function as a substitute for regulation when consistent with the protection of ratepayers and otherwise consistent with the public interest;
>
> * * *
>
> It is the Commission's task to balance these purposes.
>
> Because MCI WorldCom's proposed monthly service charge of $1.95 applies only to a competitive service, consumers are free to obtain service from an alternative provider if they object to the charge. Considering the competitive climate in which this service is offered, the Commission finds that the allowing full and fair competition to substitute for regulation will ensure that consumers pay only reasonable rates. As Staff noted, monthly recurring charges and surcharges are common in the telecommunications industry and MCI WorldCom should not be treated differently than other similarly situated telecommunications companies. The Commission determines that the proposed tariff is just and reasonable and should be approved. Therefore, the Commission will deny the motion to suspend and will approve the tariff sheet.

(Order Denying Suspension and Approving Tariff, effective September 3, 2002; Ex. 5, Graves Amended Direct, p. 3-4). The Court of Appeals did not challenge the substance of these findings and conclusions; it just called for a more extensive discussion. (Ex. 5, Graves Amended Direct, p. 4).

Additionally, beyond reasonableness no longer being an issue legally before the Commission and never having been a factual issue anyway, under another change in law effectuated by SB 237, MCI's rates are now deemed reasonable because they are less than those of price cap companies. New language in Section 392.245.1 now provides that "any rate, change, toll or rental that does not exceed the maximum allowable price [the price cap] under this Section shall be deemed just, reasonable and lawful." Regardless of whether a company is price cap regulated or not, if its rates are below the cap they are deemed reasonable. The rates of the MCI companies, with the surcharge, are below the price cap and, therefore, are now deemed reasonably by statute. (Ex. 6, Graves Surrebuttal, p. 1-2).

Public Counsel has recognized throughout these proceedings that there are inherent price controls in competitive markets. It has admitted, "the competitive marketplace determines to what extent the carrier will seek to recover all or any part of [its] costs in its rates." OPC Circuit Court Brief, p. 12. (Ex. 5, Graves Amended Direct, p. 11-12). This admission confirms the total lack of foundation for Public Counsel's challenge to the reasonableness of the rates in question.

Public Counsel's assertions regarding cost recovery are misplaced. Competitive companies, like MCI, do not have to provide cost justification for their rates. Rather, as Public Counsel admits, competitive companies set their rates within the constraints of the competitive market. If a company errs and sets a rate too high, the customers simply choose another provider. There is simply no basis for an assertion that a competitive company is recovering some specific cost twice, just as there is no basis for an assertion that a competitive company is actually recovering the total of all its costs at a particular point in time. Cost studies are not required or conducted and the absence of such studies in this matter is immaterial. Rather, competitive firms derive a profit if they are able to control their expenses and generate sufficient revenues from all lines of business.

Nonetheless, MCI and Teleconnect have explained that the surcharges at issue are reasonably related to excessive switched access charges that are imposed on them in Missouri by ILECs. They have taken similar pricing action in other states for the same reason. The evidence is clear that the access rates are a problem for IXCs. The Commission has previously reached this conclusion itself in other proceedings. The MCI companies have properly exercised their business discretion to set rates that deal with this problem. (Ex. 5, Graves Amended Direct, p. 15-21).

The Commission has already correctly concluded in these proceedings that MCI's customers can change carriers if they are not satisfied with its rates. There are numerous other carriers serving the market, competition is vigorous, and customers can and do change providers.

The Commission properly exercised its prior discretion in allowing MCI's and Teleconnect's tariff changes to take effect. The Commission expressly indicated that it was balancing the provisions of Section 392.185, just as Public Counsel insists it should have done. With no reason to believe that the small competitive rate increase in question would be unreasonable, the Commission naturally allowed MCI's tariff to take effect.

Under current law, no further analysis of the reasonableness of the rates is allowed. The Commission cannot lawfully apply subsection 1 of Section 392.200 to the tariffs at issue. Nor does it need to be concerned about these surcharges, which are patently reasonable.

B. Do the AT&T, Sprint and MCI surcharges at issue comply with subsections 392.200.2 and 392.200.3 RSMo.?

The surcharges are non-discriminatory and comply with subsections 392.200.2 and 392.200.3. There is nothing unusual about having such separate charges. Further, there is nothing unusual about having a different rate structure for residential customers than for business customers. These distinct classes of customers have been established for many years and are validated by statute. Use of a flat fee is not discriminatory, as it applies fairly to all customers as their usage varies over time. The surcharges apply to rural and urban customers alike. In all respects, the surcharges fully comply with subsections 392.200.2 and 392.200.3.

The approved tariffs are reasonable on their face. They simply added a modest monthly surcharge to customer's intrastate long distance bills. The FCC expressly allows such surcharges. <u>See</u> 47 CFR 64.2400 et seq. The charge applies uniformly to all MCI intrastate residential long distance customers that are not MCI local customers; it does not discriminate between such customers. There is absolutely no distinction drawn between urban and rural customers. (Ex. 5, Graves Amended Direct, p. 21-22; Ex. 6, Graves Surrebuttal, p. 4).

Residential and business long distance rates are not the same. It has been common practice for decades to have different rates for these different classes of customers. Public Counsel has stipulated to the Commission that these are distinct classes of customers (Tr. 46-47; Meisenheimer Rebuttal, p. 14), yet it frivolously continues to present unfounded arguments to the contrary. A far more serious approach is warranted, given the degree to which the Commission and the industry currently rely (and historically have relied) on different pricing structures for business customers. (Ex. 5, Graves Amended Direct, p. 20; Ex. 6, Graves Surrebuttal, p. 4, 7-8).

SB 237 endorsed again the legitimacy of having distinct pricing plans for residential and business customers. Revised Section 392.245 now directs the Commission to separately consider the markets for service to residential versus business customers. Further, the statutes now authorize customer-specific pricing plans for business customers in certain circumstances under Section 392.200.8, which by definition means there will be differences in residential and business prices.

The exemption of MCI local customers from the surcharge is also perfectly reasonable and non-discriminatory. When MCI is the local provider, it does not incur the same switched access costs as it does as a stand-alone interexchange service provider. Such a cost different irrefutably supports the exemption. (Ex. 5, Graves Amended Direct, p. 19-20; Ex. 6, Graves Surrebuttal, p. 8).

Moreover, under SB 237, new Section 392.200.12 makes clear that subsection 2 and 3 of 392.200 do not apply to packages of services. MCI exempts customers who buy the package of local and long distance services from the surcharge. Under Section 392.200.12 such package pricing is not subject to subsections 2 and 3 of Section 392.200.

Public Counsel also criticizes the rate structure selected by the MCI companies. Apparently Public Counsel would prefer that the MCI companies implement a different rate structure. But Public Counsel is not charged with such discretionary authority over MCI. Nor does its witness have any expertise regarding competitive pricing decisions. (Ex. 6, Graves Surrebuttal, p. 2). In fact, even the Commission does not have the authority to micromanage these competitive rates in the way advocated by Public Counsel.

Mr. Graves testified that there is nothing unusual about the rate structure selected by MCI and Teleconnect. He explained that it is simply a matter of business judgment that the simplicity of the flat rate is preferable to a usage-sensitive rate element. Usage may vary, but an average rate still applies fairly to all. To the extent a flat rate effectively can be viewed as conferring a discount to higher volume users, such discounts are expressly allowed under Section 392.200.5. (Ex. 5, Graves Amended Direct, p. 21; Ex. 6, Graves Surrebuttal p. 2-3).

The Commission does not have authority to totally usurp the discretion of MCI management to select among various reasonable alternative structures for rates for MCI's services. See, e.g., State ex rel. Kansas City Transit v. PSC, 406 SW2d 5 (Mo. 1966). Such management discretion includes the ability to use average rate structures, instead of using usage sensitive structures, as well as discretion to use different rate structures for residential versus business rates.

Further, there is no basis for Public Counsel's implicit assertion that Section 392.200 prohibits average charges. Public Counsel cites no authority for such a proposition. Customer usage varies from month to month and from year to year. There is no fixed class of low-volume or high-volume users - any customer can change usage at any time he or she chooses. MCI had the discretion to develop an average charge for customers.

MCI's and Teleconnect's tariffs are lawful. Pricing differences for residential versus business customers are routine. Pricing differences between packaged local and long distance services versus stand-alone long distance services are statutorily - permitted and rationally related to cost differences. Companies are free to use their competitive discretion to incorporate flat or usage-sensitive rates into their prices. In short, there is no basis whatsoever for Public Counsel's continuing opposition to these tariffs.

Conclusion

MCI and Teleconnect conduct business in a highly competitive market. Customers are free to choose carriers and calling plans that suit their needs - or can make their decisions on a whim if they desire. If customers do not like the surcharges, they can change plans or carriers. The Commission should not attempt to decide whether customers like the surcharge, but rather should simply determine whether the surcharges are lawful. The surcharges are lawful parts of the companies' discretionary competitive pricing structures.

Particularly in light of the changes in law effectuated by SB 237, the Commission should abide by its repeated prior decisions to approve these surcharges. It is time to bring these lengthy proceedings to an end with a clear set of findings and conclusions that will satisfy the Court of Appeals.

CURTIS, HEINZ,
GARRETT & O'KEEFE, P.C.

/s/ Carl J. Lumley

Carl J. Lumley, #32869
Leland B. Curtis, #20550
130 S. Bemiston, Suite 200
St. Louis, Missouri 63105
(314) 725-8788
(314) 725-8789 (FAX)
clumley@lawfirmemail.com
lcurtis@lawfirmemail.com

Attorney for MCI Communications Services, Inc.
and Teleconnect Long Distance Services and Systems Co.

CERTIFICATE OF SERVICE

A true and correct copy of the foregoing document was emailed, faxed or mailed by U.S. Mail, postage paid this 7th day of October, 2005, to:

David A. Meyer
Senior Counsel
Missouri Public Service Commission
P.O. Box 360
Jefferson City, Missouri 65102
david.meyer@psc.mo.gov

Kevin K. Zarling
AT&T Communications of the Southwest
919 Congress Avenue, Suite 900
Austin, Texas 78701
kzarling@att.com

Mark W. Comley
Newman, Comley & Ruth
601 Monroe Street, Suite 301
P.O. Box 537
Jefferson City, Missouri 65102
comleym@ncrpc.com

Michael Dandino
Office of Public Counsel
P.O. Box 2230
Jefferson City, Missouri 65102
mdandino@ded.mo.gov

Brett D. Leopold
Sprint Communications Co.
6450 Sprint Parkway, Bldg. 14
Mail Stop: KSOPHN212-2A353
Overland Park, Kansas 66251

Dana K. Joyce
Missouri Public Service Commission
P.O. Box 360
200 Madison Street, Suite 800
Jefferson City, Missouri 65102
gencounsel@psc.mo.gov

Stephen F. Morris
MCI WorldCom
701 Brazos, Suite 600
Austin, Texas 78701
stephen.morris@mci.com

/s/ Carl J. Lumley