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Missouri Public  
Service Commission

Secretary of the Public Service Commission  
Missouri Public Service Commission  
200 Madison Street, Suite 100  
P.O. Box 360  
Jefferson City, Missouri 65102

Via Federal Express

Re: Case No. TO-2001-467

Dear Secretary of the Commission:

Enclosed please find for filing with the Commission an original and nine (9) copies of NuVox Communications of Missouri, Inc.'s, MCImetro Access Transmission Services, LLC's, Brooks Fiber Communications of Missouri, Inc.'s and MCI WorldCom Communications, Inc.'s Joint Initial Brief and Proposed Findings of Fact and Conclusions of Law in connection with the above-referenced matter. Upon your receipt, please file stamp the extra copy received and return to the undersigned in the enclosed, self-addressed, stamped envelope. If you have any questions, please do not hesitate to contact us.

Very truly yours,

  
Carl J. Lumley

CJL:dn  
Enclosures  
cc. Parties of Record (W/Enclosures)

FILED<sup>2</sup>

NOV 08 2001

Missouri Public  
Service Commission

BEFORE THE MISSOURI PUBLIC SERVICE COMMISSION

In the Matter of the Investigation of the  
State of Competition in the Exchanges of  
Southwestern Bell Telephone Company.

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Case No. TO-2001-467

**NUVOX COMMUNICATIONS OF MISSOURI, INC.'S**  
**MCImetro ACCESS TRANSMISSION SERVICES, LLC'S**  
**BROOKS FIBER COMMUNICATIONS OF MISSOURI, INC.'S and**  
**MCI WORLDCOM COMMUNICATIONS, INC.'S**  
**JOINT INITIAL BRIEF AND PROPOSED**  
**FINDINGS OF FACT AND CONCLUSIONS OF LAW**

COME NOW NuVox Communications of Missouri, Inc., MCImetro Access Transmission Services, LLC, Brooks Fiber Communications of Missouri, Inc., and MCI WorldCom Communications, Inc. and for their Joint Initial Brief and Proposed Findings of Fact and Conclusions of Law<sup>1</sup> state to the Commission as follows:

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<sup>1</sup> This pleading has been prepared in a format to serve as both a Brief and as proposed Findings of Fact and Conclusions of Law.

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### **Background Facts**

Southwestern Bell Telephone Company (SWBT) is a large incumbent local exchange telecommunications company (herein "ILEC") as defined in Section 386.020(22) R.S.Mo.<sup>2</sup> that requested and obtained price cap regulation pursuant to Section 392.245 (herein "the price cap statute") in 1997. (Ex. 16 Hughes Direct p. 14, Tr. 24). As a result, rate of return regulation of SWBT under Section 392.240.1 ended, as provided in Section 392.245.7. (Ex. 16 Hughes Direct, p. 6).

Alternative local exchange telecommunications companies (herein "CLEC") as defined in Section 386.020(1)<sup>3</sup> have been certified to provide local exchange telecommunications services as defined in Section 386.020(31)<sup>4</sup> and basic local telecommunications services as

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<sup>2</sup>An "incumbent local exchange telecommunications company" (herein "ILEC") is defined in Section 386.020(22) RSMo as follows:

A local exchange telecommunications company authorized to provide basic local telecommunications service in a specific geographic area as of December 31, 1995, or a successor in interest to such a company.

A "local exchange telecommunications company" is defined in Section 386.020(30) RSMo as follows:

Any company engaged in the provision of local exchange telecommunications service. A local exchange telecommunications company shall be considered a "large local exchange telecommunications company" if it has at least one hundred thousand access lines in Missouri and a "small local exchange telecommunications company" if it has less than one hundred thousand access lines in Missouri.

All statutory references herein are to R.S.Mo. except as otherwise noted.

<sup>3</sup>An "alternative local exchange telecommunications company" (herein "CLEC") is defined in Section 386.020(1) as follows:

A local exchange telecommunications company certified by the commission to provide basic or nonbasic local telecommunications service or switched exchange access service, or any combination of such services, in a specific geographic area subsequent to December 31, 1995.

<sup>4</sup>"Local exchange telecommunications service" is defined in Section 386.020(31) RSMo as follows:

Telecommunications service between points within an exchange.

An "exchange" is defined in Section 386.020(16) as follows:

... footnote continued on next page .....

defined in Section 386.020(4)<sup>5</sup> in all exchanges served by SWBT (herein "SWBT exchanges").  
(Ex. 16 Hughes Direct p. 26).

There is limited evidence regarding the dates on which various CLECs were certified to provide local exchange telecommunications services and basic local telecommunications services in each SWBT exchange. Public Counsel witness Barbara Meisenheimer provided the most comprehensive evidence, as follows:

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A geographical area for the administration of telecommunications services, established and described by the tariff of a telecommunications company providing basic local telecommunications service.

<sup>5</sup>"Basic local telecommunications service" is defined in Section 386.020(4) as follows:

Two-way switched voice service within a local calling scope as determined by the commission comprised of any of the following services and their recurring and nonrecurring charges:

- (a) Multiparty, single line, including installation, touchtone dialing, and any applicable mileage or zone charges;
- (b) Assistance programs for installation of, or access to, basic local telecommunications services for qualifying economically disadvantaged or disabled customers or both, including, but not limited to, lifeline services and link-up Missouri services for low-income customers or dual-party relay service for the hearing impaired and speech impaired;
- (c) Access to local emergency services including, but not limited to, 911 service established by local authorities;
- (d) Access to basic local operator services;
- (e) Access to basic local directory assistance;
- (f) Standard intercept service;
- (g) Equal access to interexchange carriers consistent with rules and regulations of the Federal Communications Commission;
- (h) One standard white pages directory listing. Basic local telecommunications service does not include optional toll free calling outside a local calling scope but within a community of interest, available for an additional monthly fee or the offering or provision of basic local telecommunications service at private shared-tenant service locations.

| <b>CLEC</b>   | <b>Certification Effective</b> | <b>SWBT Exchanges</b>  |
|---|--------------------------------|--|
| Dial US   | 2/24/97 Public Service Started | SWBT exchanges in the 417 area code  |
| Brooks Fiber  | 07/08/97 Tariff Effective      | Business-Principle Zone and MCA 1 of Kansas City and Springfield   |
| Max-Tel   | 12/05/97 Tariff Effective      | Pre-paid Residential All SWBT  |
| Intermedia  | 12/12/97 Tariff Effective      | KC Metro and Zones 1&2, St. Louis Metro and Zones 1&2, Springfield Metro and Metro calling zone (reduced to St. Louis Metro and Zones 1&2 on 11/14/98) |
| WorldCom  | 12/23/97 Tariff Approved       | Business Only  |
| Onyx/Mo Com South                                     | 01/05/98 Tariff Effective      | Pre-paid Residential All SWBT  |
| USA eXchange, LLC d/b/a Omniplex Communications Group | 01/30/98 Tariff Effective      | Resale Residential and Business All SWBT   |

(Ex. 19 Meisenheimer Rebuttal, p. 8-9).

There is also limited evidence regarding the duration of actual continuous provision of basic local telecommunications services by various CLECs in each SWBT exchange. Dial US, cited by SWBT as the first certificated CLEC, apparently began providing basic local service in the Springfield area in February 1997, but it subsequently went out of business. (Ex. 19 Meisenheimer Rebuttal p. 8; Ex. 18 Voight Rebuttal p. 13, Tr. 456). SWBT witness Thomas Hughes testified that Brooks Fiber, MFS and TCG began providing service in unspecified

portions of the MCA<sup>6</sup> areas of Kansas City and St. Louis at an unspecified time in 1997. (Ex. 16 Hughes Direct, p. 25). He also testified that there are no exchanges in which a CLEC has been providing basic local service for five years. (Tr. 438). Based on the evidence supplied by Public Counsel witness Meisenheimer, as stated above, it appears that the earliest possible date on which a period of continuous provision of basic local telecommunications service by a CLEC could have commenced would be sometime in July 1997 for the Principal Zone and MCA 1 tiers of Kansas City and Springfield and sometime in December 1997 for other SWBT exchanges. However, it was not established on the record that there has been continuous provision of basic local telecommunications services in each SWBT exchange by any particular CLEC or CLECs since those dates.

The Commission commenced this case, on Staff's motion, in March, 2001, "for the purpose of investigating the state of competition in SWBT exchanges in accordance with Section 392.245." See Order Establishing Case, Directing Notice, Joining Parties, and Granting Protective Order, Case No. TO-2001-467 (March 13, 2001). (Ex. 16 Hughes Direct p. 1-2). As explained below, this case specifically involves a determination under subsection 5 of the price cap statute (392.245) as to whether there is "effective competition" for each of SWBT's various telecommunications services in each of SWBT's exchanges.

SWBT provides the following telecommunications services<sup>7</sup> in its exchanges:

Core business switched services

Business line related services

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<sup>6</sup> Metropolitan Calling Area (MCA) service was created in 1992 by order of the Commission in Case No. TO-92-306 1992 (2 Mo. PSC 3<sup>rd</sup> 1) See also Report and Order (September 2000) Case No. TO-99-483. Maps of the various calling areas are set forth in Ex. 9 Jablonski Direct, Schedules 5, 6, and 7.

<sup>7</sup> The parties agreed to consider SWBT's services in the listed categories and did not demand greater differentiation. See, e.g. Ex. 18, Voight Rebuttal p. 7.

High capacity exchange access line services

Plexar services

IntraLATA private line/dedicate services

Residential access line services

Residential access line related services

IntraLATA toll services

Local Plus service

Optional Metropolitan Calling Area (MCA) service<sup>8</sup>

Wide Area Telecommunications Services (WATS) and 800 services

Special access services

Switched access services

Common Channel Signaling/Signaling System 7 (SS7) services

Line Information Database (LIDB) services

Directory Assistance (DA) services

Operator services (OS)

### **Evidence Regarding State of Competition**

SWBT witness Thomas Hughes provided an overview of SWBT's position on the issues in the case. (Ex. 16 Direct p. 1). He testified that SWBT believes there is "effective competition" for each of its services in each of its exchanges because "customers located in SWBT exchanges have many choices available to them." (*Id.* p. 4, 18-30, Ex. 17 Surrebuttal, p. 3-16). He referred to the Commission's decision in Case No. TO-99-227 regarding local

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<sup>8</sup> Optional MCA Service is not provided in all exchanges, but rather in specific exchanges surrounding the core metropolitan area of St. Louis, Kansas City and Springfield. See Ex. 9 Jablonski Direct, Schedules 5, 6 and 7.



markets. (Ex. 16 Direct p. 22, Ex. 17 Surrebuttal p. 17). He also identified various services that were previously classified under Section 392.370. (Ex. 16 Direct p. 10.) Mr. Hughes estimated that CLECs have gained a 15% share of the local market and indicated that their market share was growing. (Id. p. 26-27, Ex. 17 Surrebuttal p. 4). He also supplied market share estimates on an exchange-by-exchange basis. (Id. Schedule 2).

Mr. Hughes did not provide any evidence that competition has had any specific impact on SWBT's prices or its pricing and product policies, strategies or plans. He commented that additional pricing flexibility would "increase SWBT's ability to restructure services and offer value-added packaging." (Ex. 16 Direct p. 32). He observed that "SWBT has had only limited price changes for most of its services since 1984." (Ex. 17 Surrebuttal p. 30). He testified SWBT has no current plans to change rates. (Tr. 361, 445, 459). He supplied Exhibit 29, which provides information on recent SWBT price changes, including changes mandated by the price cap statute. There was no testimony that any specific changes were made as a result of competition or explaining the specific analysis that resulted in such changes.

SWBT witness Thomas Anvin provided general testimony about local telecommunications competition. (Ex. 15 Direct). He stated it was his view that the mere presence of a CLEC with a tariff, even without any customers, constituted "effective competition". (Tr. 335).

SWBT witness Sylvia Fernandez testified regarding SWBT's core business voice services. (Ex. 11 Direct p. 1-3). She described types and number of competitors. (Id. p. 5-31, Ex. 12 Surrebuttal, p. 3-10). She provided some examples of competitors' marketing. (Ex. 11 Direct p. 10). She testified that SWBT is experiencing a net loss of basic access lines, attributable in part to competition. (Ex. 12 Surrebuttal, p. 9).

Ms. Fernandez concluded that “there are alternative providers providing substitutable or functionally equivalent services to SWBT’s business core services and therefore, the Commission should find that effective competition exists for SWBT’s business core services.” (Id. p. 5). She also referred to existing pricing flexibility for Plexar under Section 392.200.8. (Id. p. 32). She presented no evidence that competition has had any impact upon SWBT’s prices or pricing and product policies, strategies, and plans. She indicated that SWBT continues to “balance revenue and contribution sources between an embedded base of lower margin residence and rural customers against higher margin business customers.” (Id. p. 7). Further, she commented that SWBT would likely engage in better pricing and product innovation if granted further pricing flexibility, but did not identify any specific plans. (Id. p. 34).

SWBT witness Thomas DeHahn testified regarding SWBT’s intraLATA private line/dedicated services. (Ex. 3 Direct, p. 1). He described types and numbers of competitors and ease of market entry. (Id. p. 5-11). He provided some examples of competitors’ marketing. (Id. p. 6).

Mr. DeHahn concluded that the existence of competition equates to “effective competition” under the price cap statute. (Id. p. 13). He also pointed to prior classifications under Section 392.370 and private line pricing flexibility under Section 392.200.8. (Id. 2, 6, 11, 13). He provided no evidence that competition has had any impact upon SWBT’s prices or pricing and product policies, strategies and plans. He commented SWBT would like more pricing flexibility, but did not identify any specific plans and further acknowledged that SWBT can already engage in customer specific pricing under Section 392.200.8. (Id. p. 12).

SWBT witness Aimee Fite testified regarding residential voice services. (Ex. 9 Direct p. 1-2). She described types and numbers of competitors. (Id. p. 2-22, Ex. 10 Surrebuttal, p. 3-9).

She provided some examples of competitors' marketing. (Ex. 9 Direct p. 12, Ex. 10 Surrebuttal, p. 9). She indicated that SWBT has experienced a net loss in residential access lines in 2001 for the first time. (Id. p. 2, 4).

Ms. Fite concluded that the availability of services for alternative providers demonstrates that "effective competition" exists. (Ex. 13 Direct, p. 2, 22-24, Ex. 14 Surrebuttal, p. 31, Tr. 310, 313). She did not provide any evidence that competition has had any impact on SWBT's prices or pricing or product policies, strategies or plans. She commented that SWBT might take advantage of additional pricing flexibility, although she conceded it enjoys some degree of flexibility at present and yet has no plans to change prices. (Ex. 13 Direct, p. 23, Ex. 14 Surrebuttal p. 8, Tr. 329).

SWBT witness Barbara Jablonski testified regarding intraLATA toll service, Local Plus service, and optional MCA service, as well as WATS and 800 services. (Ex. 9 Direct p. 1-2). She described types and numbers of competitors. (Id. p. 6-17, Ex. 10 Surrebuttal, p. 1-10). She provided some figures on the number of intraLATA toll customers that have selected a competitor to serve them. (Id. p. 9).

Ms. Jablonski opined that the existence of competition equates to "effective competition" under the price cap statute. (Ex. 9 Direct, p. 19). She stated: "Based on the interexchange service options available to all customers in Missouri, the Commission should declare SWBT's interexchange service to be competitive." (Id. p. 19-20). She also referred to prior classification of intraLATA toll and 800/WATS under Section 392.370. (Id. p. 3, 5-6, 16). Ms. Jablonski provided no evidence that competition has had any impact on SWBT's prices or pricing and product policies, strategies and plans. She commented that SWBT might consider price changes if it is granted greater pricing flexibility, although she did not identify any specific plans and

acknowledged that it may already have sufficient flexibility. (Id. p. 17-19, Ex. 10 Surrebuttal p. 5, Tr. 276-79).

SWBT witness Sandra Douglas testified regarding SWBT's special access, switched access, SS7 and LIDB services. (Ex. 7 Direct, p. 2). She described types and numbers of competitors. (Id. p. 6-18). She provided some examples of competitors' marketing. (Id. p. 16). She indicated that SWBT's switched access minutes of use continuously grew until 2001, but declined by 3% in the first half of 2001. (Ex. 8, Surrebuttal, p. 7).

Initially, Ms. Douglas opined: "SWBT's Switched Access, SS7 and LIDB services face numerous forms of competition from other companies which provide services that are substitutable for or functionally equivalent to SWBT's Special Access, Switched Access, SS7 and LIDB services. Therefore, these SWBT services should be designated as competitive and removed from Missouri's price cap regulation. The most significant competition is in the metropolitan areas, which have already seen the establishment of alternative transport via metropolitan fiber rings, collocation hotels, numerous competitive facilities based providers, and service offerings via viable network alternatives." (Ex. 7 Direct, p. 20). In other words she initially concluded that the existence of competition equates to "effective competition" under the price cap statute. She also pointed to prior classifications under Section 392.370 and special access pricing flexibility under Section 392.200.8. (Id., p. 21). She referenced the 271 proceeding and FCC interstate pricing flexibility proceedings. (Ex. 8 Surrebuttal p. 2-9). She provided no evidence that competition has had any impact upon SWBT's prices or pricing and product policies, strategies and plans.

In Surrebuttal and at hearing, however, Ms. Douglas admitted that switched access services do not face "effective competition" and indicated SWBT would defer a determination of

whether switched access service is subject to "effective competition." (Ex. 8 Surrebuttal, p. 3, Tr. 258, 260). She indicated SWBT simply wants to be able to consider engaging in revenue neutral rate rebalancing and restructuring. (Id., p. 1-2). She acknowledged SWBT's switched access prices are above cost and that SWBT is free to reduce them. (Ex. 8 Surrebuttal, p. 1). Ms. Douglas acknowledged that CLEC switched access rates in SWBT exchanges have been capped at SWBT's rates by the Commission (Ex. 7 Direct p. 19).<sup>9</sup>

SWBT witness Sandy Moore testified regarding Directory and Operator Services. (Ex. 5 Direct, p. 1-3). She described types and numbers of competitors and ease of market entry. (Id. 5-29, Ex. 6 Surrebuttal p. 2-7). She provided some examples of competitors' marketing. (Id.) She identified declines in SWBT Directory Services and Operator Services volumes since 1996. (Ex. 6 Surrebuttal, p. 4-6).

Ms. Moore concluded that SWBT's Directory and Operator Services face "effective competition" simply because there are alternative providers providing substitutable services at comparable rates, terms and conditions. (Ex. 5 Direct p. 17, 29, Tr. 239). Thus, she equated the existence of competition to "effective competition" under the price cap statute. She also pointed to prior classification of certain operator services under Section 392.370 (Id. p. 19, 28) and pointed to FCC unbundling decisions. (Id. p. 15, 28). She provided no evidence that competition has had any impact upon SWBT's prices or pricing and product policies, strategies and plans. She commented that SWBT would like more pricing flexibility, without any explanation of SWBT's failure to reduce prices under the price cap regime. (Id. 18, 30). She advised that SWBT has no current plans to change rates. (Tr. 235).

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<sup>9</sup> In Case No. TO-99-596, the Commission found that switched access services constitute a locational monopoly, regardless of the provider, and capped CLEC rates at ILEC rate levels. See Report and Order (June 2000).

SWBT witness Dr. Debra Aron, a Ph.D. economist, testified regarding economic principles that she believes “should guide the Commission in its evaluation of the state of competition” in SWBT exchanges. (Ex. 1 Direct, p. 4). She indicated that the Missouri statutes articulate a “preference for competition over regulation, when consistent with the public interest.” (Id. p. 28).

Throughout her testimony, Dr. Aron indicated that “effective competition” means competition that serves to constrain or discipline pricing and move it to the competitive level of true economic cost. (Id. p. 11, 17, 19, 27; Ex. 2 Surrebuttal p. 35, Tr. 139-41). She stated that “one of the fundamental tenets of basic economics is that competition tends to drive prices towards costs, thereby eroding profits.” (Ex. 2 Surrebuttal, p. 52, Tr. 30). Further, she testified that there must be “true, efficient competition that fosters society’s goals of a robust telecommunications infrastructure, availability of new services and packages with the resources efficiently used in producing the services and consistent with market demand.” (Ex. 1 Direct p. 30, Tr. 140). She testified that “pricing strategy in a competitive market involves the choice of - or invention of - new pricing structures, bundles and service offerings.” (Ex. 2 Surrebuttal p. 13).

Dr. Aron testified that the factors identified in Section 386.020(13) “do not constitute an exhaustive list of the relevant factors, nor is any one completely dispositive of the presence or absence of effective competition.” (Ex. 1 Direct, p. 8).

Dr. Aron testified that “barriers to entry into the local exchange market are relatively low in SWBT’s territory in Missouri,” relying on the Commission’s decision regarding SWBT’s 271 application. (Id., p. 26). However, she acknowledged that UNE loop prices exceed retail rates for local residential service, creating a barrier to facilities – based entry.” (Ex. 2 Surrebuttal p. 6-

7, Tr. 207-08). Further, she stated that below cost residential retail rates are a barrier to entry that needs to be addressed by establishing an explicit universal service mechanism. (Tr. 172-74, 177-78). She explained that when barriers are higher, it is "less likely that potential market entry can provide competitive discipline on the incumbent's pricing." (Ex. 1 Direct p. 17).

Dr. Aron discussed the potential benefits that may result from ending price cap regulation of SWBT "when effective competition exists." (Id. p. 33). However, she did not provide an opinion that effective competition exists for any SWBT service in any SWBT exchange. (Id. p. 34).

WorldCom witness Donald Price testified that SWBT's services are not subject to "effective competition." (Ex. 24 Rebuttal p.1). He indicated that premature deregulation of SWBT's prices would cause "harm to the public, competitors, and the competition process." (Id. p. 4).

Mr. Price explained that "the presence of competitors is a necessary condition for competition to exist, but that fact alone is not sufficient to determine that effective competition actually exists for any service or in any geographic area." (Id., p. 5). Mr. Price testified that currently competitors are not able to effectively check SWBT's market power because of barriers to entry such as poor financial markets, limited customer bases, and dependence upon SWBT's facilities. (Id. p. 6-10, Tr. 807-08). Regarding the last point, he added: "In particular, pricing UNEs above economic cost reduces an entities' ability to extend the reach of its network and at the same time renders uneconomic the delivery of services to certain customers." (Id. p. 11). Further, he identified restrictions on SWBT's UNE-P offering that impede competition. (Id. p. 12).

Sprint witness Dawn Ribbentrop testified that effective competition does not exist for switched access services. (Ex. 25 Rebuttal, p. 3). She explained that "utilization of alternative providers for switched access is not readily available or practical for IXC use in Missouri," because IXCs must use the services of the local service provider selected by the end user. (*Id.* p. 5-6). She called for access reform in Case No. TR-2001-65. (*Id.* p. 8). She indicated that ILECs and CLECs have an incentive to exploit the bottleneck, locational monopoly of switched access. (*Id.* p. 12). She noted the FCC has stated that "the market for access services does not appear to be structured in a manner that allows competition to discipline rates." (*Id.* p. 17, citing Seventh Report and Order and Further Notice of Proposed Rulemaking ¶32, April 26, 2001 (FCC 96-262)).

AT&T witness Matthew Kohly testified that SWBT's services do not face "effective competition." (Ex. 22 Rebuttal p. 34; Ex. 23 Surrebuttal, p. 2-11). He echoed the concerns of Ms. Ribbentrop, stating that premature deregulation of access services would result in runaway price increases, because the services remain a locational monopoly (Ex. 22 Rebuttal, p. 23-27, 34, Tr. 815-17). He expressed the further concern that premature deregulation of SWBT's retail services could allow SWBT to engage in predatory pricing. (Ex. 22 Rebuttal 28-34). He noted that competition must be "irreversible or sustainable" before the market can effectively replace price regulation. (*Id.* p. 12). He testified that currently "the relative lack of competition in Missouri indicates a presence of fundamental entry barriers in Missouri that will not permit truly sustainable competition." (*Id.* p. 13). Mr. Kohly identified several barriers, including weak financial opportunities for CLECs and ILEC efforts to eliminate certain UNEs. (*Id.* p. 17-18). Further, he described how SWBT has abused its market power, such as with regard to



interference with MCA service and Local Plus and misuse of competitors' information. (Id. p. 20, Ex. 23 Surrebuttal p. 11-20).

Mr. Kohly testified that reimposition of price caps after a premature release would not remedy the likely harm to the market. (Id. p. 19). He observed that SWBT has not made use of its existing downward pricing flexibility under price cap regulation. (Id. p. 26).

Public Counsel economist witness Barbara Meisenheimer testified that SWBT's services are not subject to "effective competition," with the possible exception of per-minute priced intraLATA toll. (Ex. 19 Rebuttal, p. 16, 21-22, Ex. 20 Surrebuttal, p. 2, 7-17). She described numerous barriers that presently preclude "effective competition." (Id.). She expressed concern that customers would be exposed to detrimental and unreasonable price increases because there is insufficient competition to constrain SWBT's prices. (Ex. 19 Direct p. 10, Ex. 20 Surrebuttal, p. 3). She observed that SWBT has not taken advantage of its downward pricing flexibility under the price cap statute. (Id. p. 14). She explained that SWBT still dominates the local market and controls the bottleneck loop facility. (Id. p. 17).

Staff witness William Voight testified that Staff agrees with SWBT that certain services are subject to "effective competition." (Ex. 18 Rebuttal, p. 2). Specifically, he indicated that MTS or Long Distance is provided by a number of alternative providers and was previously classified under Section 392.370; that WATS was previously classified under Section 392.370; that Centrex and private line services are subject to customer specific pricing under Section 392.200.8; that SS7 and LIDB are provided to other telecommunications companies; that business local service and associated vertical services, optional MCA, operator services and directory assistance services in the Kansas City and St. Louis metropolitan exchanges are provided by a number of facilities-based alternative providers; and that residential local service

and associated vertical services, optional MCA, operator services and directory services in the Harvester and St. Charles exchanges are provided by a single facilities-based competitor. (*Id.* p. 3-5).

Mr. Voight also testified that Staff disagrees with SWBT that other services are subject to “effective competition.” (*Id.* p. 2). Specifically, he testified that: switched access services are a locational monopoly service; other business services and associated services are not provided by sufficient alternative facilities-based providers; other residential service and associated services are not provided by sufficient alternative facilities-based providers; and Local Plus may be provided below cost without full opportunity for resale. (*Id.* p. 5-6). He testified that SWBT’s below-cost residential rates have impeded competition. (Tr. 704).

Mr. Voight also stated that “the mere presence of ‘alternative’ providers offering ‘substitutable’ services is insufficient to determine whether competition is ‘effective’”. (Ex. 18 Rebuttal p. 25).

Mr. Voight expressed concern about SWBT’s failure to use its existing downward pricing flexibility under the price cap statute. (*Id.* p. 9). He did not provide any evidence that competition has had any impact on SWBT’s prices or its pricing and product policies, strategies or plans.

### **Jurisdiction**

The Commission has jurisdiction in this case pursuant to its general authority over SWBT as a telecommunications company under Section 386.250 and pursuant to its specific responsibilities under the price cap statute, Section 392.245.

### The Price Cap Statute

Subsection 5 of the price cap statute provides as follows:

Each telecommunications service of an incumbent local exchange telecommunications company shall be classified as competitive in any exchange in which at least one alternative local exchange telecommunications company has been certified under section 392.455 and has provided basic local telecommunications service in that exchange for at least five years, unless the commission determines, after notice and a hearing, that effective competition does not exist in the exchange for such service. The commission shall, from time to time, on its own motion or motion by an incumbent local exchange telecommunications company, investigate the state of competition in each exchange where an alternative local exchange telecommunication company has been certified to provide local exchange telecommunications service and shall determine, no later than five years following the first certification of an alternative local exchange telecommunication company in such exchange, whether effective competition exists in the exchange for the various services of the incumbent local exchange telecommunications company. If the commission determines that effective competition exists in the exchange, the local exchange telecommunications company may thereafter adjust its rates for such competitive services upward or downward as it determines appropriate in its competitive environment. If the commission determines that effective competition does not exist in the exchange, the provisions of paragraph (c) of subdivision (2) of subsection 4 of section 392.200 and the maximum allowable prices established by the provisions of subsections 4 and 11 of this section shall continue to apply. The commission shall from time to time, but no less than every five years, review the state of competition in those exchanges where it has previously found the existence of effective competition, and if the commission determines, after hearing, that effective competition no longer exists for the incumbent local exchange telecommunications company in such exchange, it shall reimpose upon the incumbent local exchange telecommunications company, in such exchange, the provisions of paragraph (c) of subdivision (2) of subsection 4 of section 392.200 and the maximum allowable prices established by the provisions of subsections 4 and 11 of this section, and, in any such case, the maximum allowable prices established for the telecommunications services of such incumbent local exchange telecommunications company shall reflect all index adjustments which were or could have been filed from all preceding years since the company's maximum allowable prices were first adjusted pursuant to subsection 4 or 11 of this section.

Thus, subsection 5 of the price cap statute instructs the Commission, under several different scenarios (as discussed below), to determine whether "effective competition" exists in an exchange that meets certain criteria for each telecommunications service offered in that exchange by an ILEC that is subject to price cap regulation.<sup>10</sup> If the Commission determines that "effective competition" exists for a specific ILEC service in a specific exchange, the statute directs the Commission to classify the service as "competitive" under the price cap statute in that exchange. The ILEC "may thereafter adjust its rates for such competitive services upward or downward as it determines appropriate in its competitive environment" in the exchange, without regard to the long run incremental cost floor established in Section 392.200.4(2)(c) and without regard to the maximum price previously established by the price cap statute. Conversely, if "effective competition" does not exist for a specific service in a specific exchange, the cost floor and maximum price would continue to apply to that service in that exchange.

The scenarios under which the price cap statute directs the Commission to make a determination as to whether "effective competition" exists for a specific service in a specific exchange are as follows:

(1) under the second sentence, "in each exchange where [a CELC] has been certified to provide local exchange telecommunications service";

(2) under the first sentence, "in any exchange in which at least one [CLEC] has been certified under Section 392.455 [to provide basic local telecommunications service<sup>11</sup>] and has provided basic local telecommunications service in that exchange for at least five years";

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<sup>10</sup> Subsection 5 calls for consideration of "each" (in the first sentence) of the "various services" (in the second sentence) offered by the ILEC. Specifically, the Commission is to determine whether "effective competition . . . exists in the exchange for such service." The parties all agreed that the statute calls for an exchange-by-exchange, service-by-service analysis.

<sup>11</sup> See Section 392.455.

(3) under the fifth sentence, "in those exchanges where it has previously found the existence of effective competition".

Subsection 5 of the price cap statute also establishes various timeframes for Commission action in some (but not all) of the foregoing scenarios, as follows:

(1) under the second sentence, such determinations must be made "from time to time", with an initial determination to be made "no later than five years"<sup>12</sup> following the first certification of [a CLEC] in such exchange"<sup>13</sup>;

(2) under the first sentence, there is no specific timeframe for action;

(3) under the fifth sentence, such determinations must be made "from time to time, but no less than every five years".<sup>14</sup>

Subsection 5 also establishes different ultimate issues or decision points for the foregoing scenarios, as follows:

(1) under the second sentence, "whether effective competition exists";

(2) under the first sentence, whether "effective competition does not exist";

(3) under the fifth sentence, whether "effective competition no longer exists".

Any such decision by the Commission must be made after notice and hearing. While the second sentence makes no reference to notice or hearing, and the fifth sentence only refers to a

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<sup>12</sup> The price cap statute does not establish any consequence for a failure on the part of the Commission to make such an initial determination within the specified five-year period. Given the absence of an express statement entitling an ILEC to some form of automatic relief, the only appropriate consequence would be an ability on the part of the ILEC to obtain a court order mandating the Commission to make such an initial determination, one way or another, within a reasonable time.

<sup>13</sup> There does not appear to be any significant difference between the "first certification of a [CLEC]", which could involve certification "to provide basic or non-basic local telecommunications service or switched access service, or any combination of such services" under Section 386.020(1), and certification "of [a CLEC] to provide local exchange telecommunications service".

<sup>14</sup> Temporally, an investigation under the second sentence would necessarily come before an investigation under the first sentence.

hearing, and only the first sentence expressly refers to both notice and hearing, it is well-established that all decisions of the Commission must be based on competent and substantial evidence of record made in accordance with the fundamental due process components of notice and opportunity to be heard. See, e.g., State ex rel. Chicago Rock Island & Pacific R.R. v. PSC, 312 S.W.2d 791, 796 (Mo. 1958); State ex rel. Rice v. PSC, 220 S.W.2d 61, 64 (Mo. 1949); State ex rel. Anderson Motor Service Co. v. PSC, 154 S.W.2d 777 (Mo. 1941).

### **Effective Competition**

Contrary to the statements of various witnesses, the statutes do not define "effective competition".<sup>15</sup> Instead, Section 386.020(13) enumerates various factors upon which the Commission must base a subjective determination regarding "effective competition", as follows:

"Effective Competition" shall be determined by the Commission based on:

- (a) The extent to which services are available from alternative providers in the relevant market;
- (b) The extent to which the services of alternative providers are functionally equivalent or substitutable at comparable rates, terms and conditions;
- (c) The extent to which the purposes and policies of chapter 392, RSMo, including the reasonableness of rates, as set out in section 392.185, RSMo, are being advanced;
- (d) Existing economic or regulatory barriers to entry; and
- (e) Any other factors deemed relevant by the commission and necessary to implement the purposes and policies of chapter 392, RSMo;

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<sup>15</sup> Further, the definition of "competitive telecommunications services" expressly does not apply to Section 392.245, but rather only applies to certain other specified statutes."

Given the final factor, the Commission's analysis must include all relevant factors. As stated by several witnesses, including Dr. Aron, Mr. Price, Ms. Meisenheimer, and Mr. Voight, no single factor can be determinative.

The purposes and policies of Chapter 392 as set out in Section 392.185 (as referenced in subsection (c) of Section 386.020(13)) are as follows:

- (1) Promote universally available and widely affordable telecommunications services;
- (2) Maintain and advance the efficiency and availability of telecommunications services;
- (3) Promote diversity in the supply of telecommunications services and products throughout the state of Missouri;
- (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;
- (7) Promote parity of urban and rural telecommunications services;
- (8) Promote economic, educational, health care and cultural enhancements; and
- (9) Protect consumer privacy.

"Competition" is primarily defined as meaning "rivalry". See Random House Webster's Unabridged Dictionary, 2d Ed. As discussed above, subsection 5 of the price cap statute prescribes an examination of individual ILEC services on an exchange-by-exchange basis. When considered in the full context of Sections 392.245.5 and 386.020(13), "competition" as used in subsection 5 refers to the rivalry of "alternative providers" offering services that are

“functionally equivalent or substitutable”, relative to the ILEC service being examined, at “comparable rates, terms and conditions” in the “relevant market” of each separate exchange, unencumbered by “economic or regulatory barriers to entry”.

The primary definition of the word “effective” is: “adequate to accomplish a purpose; producing the intended or expected result.” See Random House Webster’s Unabridged Dictionary, 2d Ed. As discussed above, subsection 5 of the price cap statute involves the process of lifting cost floors and maximum prices, which maximum prices were in turn established in lieu of more intense rate of return regulation under Section 392.240.1.<sup>16</sup> Further, subsection 5 does not involve the automatic reinstatement of cost floors and maximum prices, but rather only contemplates periodic reexamination of the state of competition (at least once every five years). When considered in the full context of Sections 392.245.5 and 386.020(13), “effective” competition as used in subsection 5 of the price cap statute refers to competition that is adequate to accomplish the purposes that were previously to have been accomplished by the cost floors and maximum prices and to produce the intended or expected results, namely accomplishing the “purposes and policies of chapter 392 RSMo, including the reasonableness of rates, as set out in section 392.185”, over a sustained period running up to five years into the future. As witnesses such as Dr. Aron testified, this means that “effective competition” is competition that exerts sustainable discipline on prices and moves them to the competitive level of true economic cost.

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<sup>16</sup> See subsections 1 and 7 of Section 392.245.



### **Ultimate Issue**

As indicated above, the evidence shows that no CLEC has been providing basic local service in any SWBT exchange for a period of five years. Accordingly, the first sentence of subsection 5 of the price cap statute does not apply to this case.<sup>17</sup>

On the other hand, as indicated above, the evidence shows that CLECs have been certified to provide local exchange service and basic local service in all of SWBT's exchanges. Hence, the second sentence of subsection 5 does apply to this case.<sup>18</sup> While no CLEC has been certified for five years, the second sentence directs the Commission to consider the state of competition from time to time, and at least initially no later than five years after the first such certification. The Commission properly commenced this proceeding and there is no reason to discontinue the investigation short of rendering a decision.

Under the second sentence, as explained above, the ultimate issue or decision point as to each SWBT exchange is "whether effective competition exists in the exchange for the various telecommunications services of SWBT." See Section 392.245.5.

### **Burden of Proof**

The second sentence of subsection 5 requires an affirmative decision by the Commission as to "whether effective competition exists." The Commission can only make such an affirmative finding based on competent and substantial evidence. See, e.g., State ex rel. Rice v.

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<sup>17</sup> Accordingly, the debate over whether the first sentence establishes a rebuttable presumption of "effective competition" is not properly before the Commission.

<sup>18</sup> SWBT ultimately agreed with this conclusion. (Tr. 438-39).

PSC, 220 S.W.2d 61, 64 (Mo. 1949). Consequently, the debate between the witnesses and parties regarding who bears the burden of proof is moot. Regardless of who bears the burden of proof, absent competent and substantial evidence of "effective competition" the Commission cannot find that it exists.

Having said that, it must also be recognized that in this case it is SWBT (and to a lesser extent Staff) that requests the Commission to find that "effective competition" exists and in accordance therewith asks the Commission to change the manner in which it is regulated by terminating price cap regulation. Generally, the party seeking relief from the Commission bears the burden of proof. See Section 386.430; State ex rel. Rice v. PSC, 220 S.W.2d 61, 66 (Mo. 1949). The burden of proof remains upon the party asserting the affirmative of the ultimate issue throughout a proceeding. See, e.g., Been v. Jolly, 247 S.W.2d 840, 854 (Mo. 1952).

### Conclusions

There is no competent and substantial evidence that "effective competition" exists in any SWBT exchange for any of its services. The evidence clearly shows that competition exists,<sup>19</sup> but as several witnesses including Mr. Price and Mr. Voight observed, the mere existence of competition does not equate to "effective competition" under the statutes. To the contrary, proof of "effective competition" requires proof that competition has risen to such a level that is serving as an effective and sustainable constraint upon the pricing practices of the ILEC.

SWBT's evidence consisted solely of proof of the existence of competition. Its witnesses did not provide evidence that competition was exerting any discipline upon its pricing practices.

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<sup>19</sup> Competition exists whether or not all of the "alternative providers" identified by various parties are counted. It is not necessary to resolve the debate between SWBT and others as to precisely which "alternative providers" are to be included in the analysis, or to decide precisely which types of "services", whether within the definition of "telecommunication services" or not, should be considered.

Further, its witnesses all testified that SWBT simply wants more pricing flexibility even though it has no current pricing plans.

Absent proof that competition is exerting sustainable pricing discipline to warrant elimination of price cap regulation, there can be no finding that "effective competition" exists under Section 392.245.5.<sup>20</sup>

It is not determinative that certain of SWBT's services are subject both to price cap regulation under Section 392.245 and customer specific pricing flexibility under Section 392.200.8. These statutes were enacted together in 1996 and there is no indication that prices subject to Section 392.200.8 are exempt from Section 392.245, which on its face applies to all services.

Likewise, it is not determinative that certain of SWBT's services were classified under Section 392.370 prior to commencement of price cap regulation. The process of classifying services as competitive under the price cap statute is separate and distinct from the process of classifying services as competitive under Sections 392.361 and 392.370. The definition of "competitive telecommunications service" is limited to classifications made pursuant to Sections 392.361 and 392.370 and does not include classifications under Section 392.245. Likewise, Section 392.245 makes no provision for exempting any service which may have been previously classified competitive under Sections 392.361 and 392.370 from the application of cost floors and maximum prices unless and until the Commission determines effective competition exists for the service in particular exchanges. Instead, subsection 1 of the price cap statute expressly provides that the maximum prices cannot be increased in any manner except as provided in that statute. Further, all price changes not in excess of the maximum price are expressly governed by

subsection 4(5) of the statute. The price cap statute simply does not recognize the pricing flexibility afforded to companies whose services are classified under Sections 392.261 and 392.370. (See Sections 392.500 and 392.510). At least with regard to price, a company subject to the price cap statute is subject to a self-contained price control regime that applies according to its own terms and conditions without regard for any other statutory classification system.

Actions regarding the application of SWBT's parent corporation for relief under Section 271 of the Telecommunications Act of 1996 are also not determinative. An open local market does not equate to a market that is subject to "effective competition." SWBT witnesses agreed with this conclusion. (Tr. 217, 350, 389, 486).

There was a great deal of evidence regarding SWBT's current level of pricing flexibility under the price cap statute. However, such evidence is not pertinent to the ultimate issue to be decided in this case. What is pertinent is that the witnesses testified that SWBT rarely exercises its existing pricing flexibility, has not shown that its prices are disciplined by competition, and has no current pricing plans that it is willing to share with the Commission. Ultimately, even if the price cap statute does not afford SWBT the flexibility it wants or needs, SWBT is free to seek a release from such regulation under Section 392.246 without regard to whether "effective competition" exists. Until then, SWBT requested price cap regulation and must accept its provisions.

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<sup>20</sup> It should be noted that SWBT withdrew switched access services from consideration, after admitting that effective competition does not exist for those services.

**Resolution**

SWBT's telecommunications services are not subject to "effective competition", as that phrase is used in Section 392.245.5, in any SWBT exchange. Consequently, SWBT must remain subject to price cap regulation under Section 392.245.5 at this time.

Respectfully submitted,

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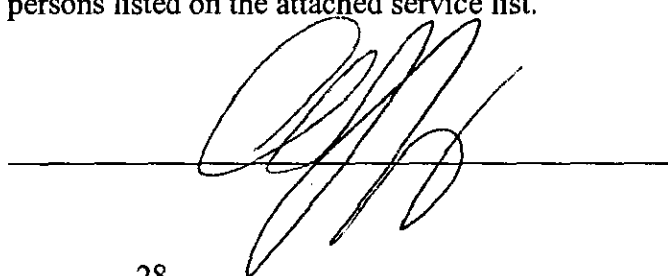


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**CERTIFICATE OF SERVICE**

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