ORDER NO. 02-821

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BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UM 962

In the Matter of an Investigation of	)	ORDER
Wholesale Discounts Applicable to Resale.	)	

DISPOSITION: STIPULATION ADOPTED; WHOLESALE DISCOUNT RATE AND SCOPE OF APPLICABILITY DETERMINED

I. INTRODUCTION

Background. Section 252(d)(3) of the Telecommunications Act of 1996 (the Act) provides that "a State commission shall determine wholesale rates on the basis of retail rates charged to subscribers for the telecommunications service requested, excluding the portion thereof attributable to any marketing, billing, collection, and other *costs that will be avoided* by the local exchange carrier." (emphasis supplied).

The Federal Communications Commission (FCC) adopted the wholesale discount rule set forth in Rule 51.609 to implement that portion of the Act. The rule had several provisions: First, avoided retail costs were to be determined on the basis of a rule-compliant cost study. Second, "avoided costs" were "those costs that reasonably *can* be avoided." (emphasis supplied). Third, the FCC listed those accounts within the Uniform System of Accounts which were presumptively included or excluded from the category of avoided costs. Fourth, the rule provided parties with the opportunity to show, (1) with respect to the presumptively avoided costs, that they could be excluded by the incumbent local exchange carrier (ILEC) from the avoided cost category if the ILEC proved to the state commission that the specific costs in these accounts would actually be incurred and were not avoidable; and (2) that presumptively unavoidable expenses could be proved avoidable by intervening parties and not included in determining wholesale costs.

Shortly after the FCC issued Order FCC 96-325, which promulgated regulations to implement interconnection and pricing provisions of Sec. 251 and 252 of the Act, the wholesale discount rule was one of many that immediately became the subject of intense litigation. On October 15, 1996, the United States Court of Appeals for the Eighth Circuit (Eighth Circuit) issued a stay of some of those rules, including the wholesale discount rule. The stay remained in effect until a remand from the U.S. Supreme Court

(Supreme Court) in *AT&T Corp. v. Iowa Utilities Board, et al.,* 525 U.S. 366 (1999), to the Eighth Circuit caused it to lift the stay, at least temporarily. The Supreme Court directed the Eighth Circuit to modify its prior ruling in line with the Supreme Court decision.

Service resale was concurrently an issue before the Public Utility Commission of Oregon (Commission). Appeals from several arbitration orders, which applied the Rule 51.609 standards, went to the U.S. District Court for the District of Oregon (U.S. District Court). In a series of decisions, the U.S. District Court remanded the matters relating to wholesale discounts back to this Commission for further consideration.[1]

History of These Proceedings. The Commission's Order No. 00-007, entered January 6, 2000, in this docket ordered an investigation to be opened into the wholesale discounts applicable to resale, and referenced the December 8, 1999, Staff Report. The Staff Report referenced the Act, the FCC rules, and the U.S. District Court, including the decisions cited above, as mandating the instant investigation. Allan J. Arlow was designated as the Administrative Law Judge (ALJ) to preside in this matter.

A prehearing conference was held on May 11, 2000, in Salem, Oregon, at which time a hearing schedule was established. The schedule required all parties to submit direct testimony, and intervenors to submit their cost models, on or before July 21, 2000. Testimony was to be submitted in accordance with the requirements set forth in Rule 51.609.

On July 18, 2000, the Eighth Circuit in *Iowa Utilities Board, et al., v. Federal Communications Commission and United States of America,* Case No. 96-3321, Slip Opinion pages 16-18, ruled that Rule 51.609 was contrary to the meaning and intent of § 252(d)(3) of the Telecommunications Act of 1996. The Court vacated and remanded the rule. The Eighth Circuit's order swiftly became the subject of a petition for *certiorari* to the Supreme Court.

By Ruling of July 20, 2000, the ALJ suspended the procedural schedule in this docket. On October 20, 2000, pursuant to OAR 860-013-0031, Qwest Corporation (Qwest) filed a motion to lift this suspension and schedule a procedural conference to set a schedule for establishing wholesale discount rates as required by Section 251(c)(4) of the Act. Comments in opposition were timely filed by Advanced Telcom Group, Inc. (ATGI) and the Commission Staff (Staff).

By Ruling of November 16, 2000, the ALJ declined to lift the suspension. Based upon the arguments presented in the pleadings and his analysis of the administrative burdens currently being shouldered by the Commission, he did not find it appropriate to lift the stay and proceed with the development of a new avoided cost study methodology in this docket. First, the ALJ disagreed with Qwest's contention that the Commission was legally compelled to proceed because of the U.S. District Court remand. Second, he concluded that

[1] *U S WEST Communications, Inc. v. AT&T Communications of the Pacific Northwest, Inc.,* 31 F.Supp.2d 839 (D. Or 1998) and *MCI Telecommunications Corp., et al v. GTE Northwest, Inc., et al,* 41 F.Supp.2d 1157 (D. Or. 1999).

the FCC enacted Rule 51.609 for purposes above and beyond the setting of minimum standards. Paragraph 909 of the First Report and Order (FCC 96-325) in Docket No. 96-98, stated: "The criteria we adopt are designed to ensure that states apply consistent interpretations of the 1996 Act…to facilitate swift entry by national and regional resellers, which may include small entities." The Eighth Circuit did not find fault with the FCC's rationale for adopting national standards. To proceed with the development of an Oregon-unique methodology without the guidance of any nationwide minimum standards would have, in the opinion of the ALJ, undermined the goal of easing market entry via national consistency. Finally, in response to Qwest's submission of a contrary finding in a decision of the Montana Public Service Commission, he commented that "The Montana order nowhere addresses the issue of national consistency, which the FCC deemed so important. Furthermore, even if we were to disregard those FCC concerns, the Commission must still undertake to balance the two considerations that the Montana commission weighed against each other.... Each state must therefore use its own best judgment in determining what the order of priority should be in serving the public interest and what weight it should attach to the concerns voiced by the participants to the proceeding." (ALJ 11/16/02 Ruling).

Although Qwest had failed to state the extent to which it was disadvantaged by the July 20, 2000 Ruling, the ALJ granted Qwest an opportunity to provide a statement, no later than November 30, 2000, detailing the extent of any harm to Qwest that might be caused by the Commission's refusal to lift the stay in these proceedings. Interested parties were given until December 8, 2000, in which to respond.

On January 22, 2001, the Supreme Court issued its Order List: 531 U.S. Among the cases for which *certiorari* was granted were appeals from the Eighth Circuit's decision, *supra.* The grant of the petitions was, however, limited to only three questions, and the validity of the wholesale discount rule was not among them. The remainder of the Eighth Circuit's July 18, 2000 decision was allowed to stand, including the portion of its opinion that vacated and remanded Rule 51.609. As a consequence, further litigation on the current language of the rule ended, and the FCC became obligated to act upon the Court of Appeal's directive.[2] However, no deadline for compliance was placed on the FCC by the Eighth Circuit order.

A procedural conference was held on February 13, 2001, to discuss the impact of the Supreme Court's actions on the instant proceeding. Qwest Corporation, Verizon Corporation (Verizon), ATGI and Staff filed notices of appearance. To assist in an analysis of the procedural options, the ALJ provided the parties with the following list of questions, which he broke down into two categories:

General Questions

1. Should the Commission proceed with this docket before the FCC promulgates new rules implementing §252(d)(3) governing wholesale discounts?

[2] Staff notes that the methods described in the now-rejected FCC default or "Modified MCI Model," utilized in Order FCC 96-325, found at ¶930 using 1995 data, a discount rate of 18.80 percent for Qwest and 18.81 percent for Verizon. Staff/1,Turner/10-12.

2. If the Commission decides not to go forward with this proceeding pending new FCC rules, what standards should be used in arbitrations involving wholesale discounts pending completion of the proceeding?
3. What is the impact of *U S West Communications, Inc. v. AT&T Communications of the Pacific Northwest, Inc.,* 31 F.Supp.2d 839 (D. Or 1998) and *MCI Telecommunications Corp., et al v. GTE Northwest, Inc., et al,* 41 F.Supp.2d 1157 (D. Or. 1999), the Federal District Court decisions remanding wholesale discounts back to this agency?

Specific Questions

1. If the current suspension of proceedings in this docket is lifted, what are the possible alternative methodologies that the Commission could use to implement the intent of Section 252(d)(3) of the Act?
2. Do the orders of the District Court require the use of a particular methodology or approach, and if so, what?
3. What types of information and to what level of detail would each methodology require in order to satisfy the standards of administrative fairness?
4. What means should be used to reconcile differences between the Oregon-specific methodology and future rules promulgated by the FCC?
5. Should the Commission provide for the use of true-ups of arbitrated agreements after the fact once the Commission has adopted wholesale discount rules that result in different rates from those determined by the commission through arbitration?
6. If the FCC's new rules permit the states to develop alternative methodologies, what are the advantages and disadvantages in adopting the FCC's rules or maintaining Oregon-specific rules?
7. Should the adoption of FCC rules causing changes to the discount rate developed with Oregon-specific methodologies require true-ups or should they be on a going-forward basis only?

During the course of the conference, Qwest requested the opportunity to submit additional data addressing the impact of a delay in these proceedings upon Qwest's wholesale revenues. The ALJ ruled that such data, including supporting affidavits, should be submitted no later than February 20, 2001.

In order to facilitate the Commission's consideration of the pending request to lift the suspension of proceedings in this docket, the ALJ issued a further ruling permitting all parties, including Qwest, to submit comments on the Qwest data and/or upon the above-noted questions with respect to the conduct of the investigation in the docket. Qwest submitted the Affidavit of Mr. Don Mason, Qwest's Director-Oregon Regulatory (Affidavit), on February 20, 2001. Qwest, Verizon, ATGI, Staff and the Association of

Communications Enterprises (ASCENT) filed Comments with the Commission on or before March 9, 2001. ATGI and Qwest filed Reply Comments on March 16, 2001.

The Qwest Affidavit. According to the Affidavit, as of December 31, 2000, Qwest was reselling approximately 59,500 voice grade access lines, plus approximately 800 voice-grade-equivalent private lines in Oregon. (Affidavit, p. 1). For the three months preceding December, services for such lines sold at wholesale with an average discount rate of 18.5 percent. Those sales yielded revenues of approximately $2.57 million per month. If billed at retail, i.e., undiscounted, revenues from such services would have yielded revenues of approximately $3.15 million per month. (*Id.).* Thus, the 18.5 percent discount translated into a monthly revenue differential of $580,000 per month or $31,351 for each percent of discount.

Initial Comments of the Parties—General Questions. With respect to the first general question posed to the participants—whether Oregon should proceed before the FCC issues new wholesale discount rules—Qwest responded in the affirmative for both the legal reasons which it had previously argued and because of the continuation of financial harm noted in the Affidavit.

Verizon had no opinion with respect to Commission action as it affected Qwest and its customers, but opposed moving ahead in a proceeding which would establish binding, generic rules applicable to all ILECs. Verizon proposed to use the discount rates established under existing arbitration decisions consistent with its obligations under its Merger Decision and further stated that, to its knowledge, all CLECs were satisfied with that approach.

ATGI opposed lifting the suspension and disagreed with Qwest's assertion of financial harm. ATGI also disputed Qwest's interpretation of the U.S. District Court opinions, cited above, and opined that reducing the current discount rate would harm competition and Oregon consumers. ATGI argued that lifting the suspension will entail wasted time and money for all parties (which, it noted later, smaller CLECs can ill afford) because any adjudicated methodology would surely change once the FCC has promulgated new rules. It also found guidance from the Eighth Circuit and the Act to be either absent or insufficient.

ASCENT opposed lifting the suspension for reasons essentially identical to those offered by ATGI, emphasizing the value of uniform national standards articulated in the ALJ’s earlier rulings.

Staff reiterated its position that the schedule should remain suspended, but agreed with Qwest's view that "even after the FCC adopts new rules, there is a danger of lengthy litigation. However Staff recommends that once the FCC issues an order that the schedule in this docket proceed without further delay." (Comments, p. 2). Staff then offered the following proviso:

> If the ALJ chooses to proceed with Docket UM 962 without FCC guidance, Staff recommends at least one preliminary workshop to address methodologies for avoided cost determination. If the parties cannot agree on an appropriate methodology, the docket should be bifurcated to first address methodological issues. Once the Commission has issued an order on the appropriate cost method, QWEST and Verizon would file actual avoided-cost studies. (*Id.*)

Only Qwest and Staff submitted comments which addressed the remaining general questions posed at the procedural conference. In response to the second general question—what standards should be used in arbitrations in the absence of Oregon rules—Qwest commented that the arbitrator would have no standards whatsoever to apply and that moving at the high speed of arbitration cases would give results that would cause the U.S. District Court to find reversible error. Qwest also expressed the opinion that there was a minimal likelihood of wholesale rate arbitration cases, since it has been the CLEC practice to "opt-in" to existing agreements. Staff responded by saying that it would not oppose a settlement agreement among the parties setting an interim discount rate for Oregon, but noted that the Commission was required to arbitrate a disagreement if such a settlement failed to materialize.

In response to the third general question—what legal impact the remanding of the cited cases by the U.S. District Court had on this proceeding—Qwest reiterated that the Commission was bound by the U.S. District Court to move forward. Staff again disagreed on this issue, stating that the language in the opinion of the U.S. District Court and the Act itself gave the Commission sufficient discretion to stay the proceedings pending conclusion of the FCC's rulemaking proceeding.

Initial Comments of the Parties—Specific Questions. Only Qwest and Staff addressed the specific questions posed at the prehearing conference. In response to Question 1, Qwest indicated that the process for calculating the discounts is relatively straightforward, requiring the development and review of a detailed cost study which identifies all the costs that make up Qwest's retail telecommunications services rates and determines which costs Qwest will avoid when it sells those services to CLECs on a wholesale basis. Staff recommended the holding of a preliminary workshop to address alternative methodologies and, in the absence of consensus, that the docket be bifurcated to address methodological approaches first, followed by the following of avoided cost studies.

In response to Question 2, both Qwest and Staff indicated that the Commission had discretion to choose any methodology consistent with the Act.

In response to Question 3, Qwest indicated that the study should reflect only its Oregon-specific costs (Comments, p. 9-10). Staff expressed the view that the level of detail and type of evidence should be addressed at the workshop. (Comments, p. 3).

In response to Question 4, Qwest did not believe that differences between Oregon-specific methodology and future FCC rules must be reconciled, but if the

Commission chose to do so, it could be done in a separate docket. Staff indicated that procedures were available in the event a party felt aggrieved or the Commission wanted to open an investigation on its own motion.

In response to Question 5, both Qwest and Staff agreed that the Commission should not provide for the use of true-ups in arbitrated agreements. Qwest cited the agreements' usually short duration and Staff noted the potential risks posed to CLECs.

In response to Question 6, Qwest stated that, if Oregon-specific rules are adopted, the promulgation of new FCC rules should not necessarily cause the Commission to adopt those FCC rules for purposes of enhancing national uniformity. Staff recommended that the Commission defer consideration of the question until the FCC has acted.

In response to Question 7, both Qwest and Staff were of the opinion that changes to the discount rate developed with Oregon-specific methodologies caused by adoption of FCC rules should be made only on a going-forward basis.

Parties' Reply Comments. Reply Comments were submitted by Qwest and ATGI to the general questions posed by the ALJ. Qwest stated that, because Staff agreed with Qwest's assessment of the likelihood of litigation arising out of the promulgation of new wholesale discount rules by the FCC, it should support lifting the suspension. Qwest disagreed with Staff's recommendation to conduct a bifurcated proceeding, which establishes a methodology before conducting the cost study. Qwest's experience in other jurisdictions indicated that parallel processes work well and that the Commission's task "will be relatively straightforward." (Reply comments, p. 2).

Qwest responded to ATGI's Comments, stating that the United States Congress placed upon the states the obligation of developing wholesale discounts, that FCC rules were merely to provide guidance and that ATGI thus misapplies the law. With respect to the practical consequences of proceeding, Qwest argues that ATGI's concerns are speculative and unsupported by any evidence.

ATGI replied to Qwest's Comments in several ways. First, ATGI stated that Qwest had mischaracterized both the Eighth Circuit and U.S. District Court opinions. With respect to the Eighth Circuit's *vacatur* of Rule 51.609, ATGI argued that the Court did not "remand the 'definition' of an avoided cost discount but the *methodology* set forth by the FCC to calculate such a discount." (Reply Comments, p. 2, emphasis in text). ATGI contended that new FCC rules would be as detailed as former rule 609, but compliant with the Eighth Circuit's interpretation. ATGI concurred with Staff's analysis of the U.S. District Court's mandate in the remanded arbitration cases. ATGI also voiced its concern that the avoided cost discount might not reflect the forward-looking approach adopted by the FCC and thereby create an imbalance between resale and TELRIC-based UNE rates. Such an imbalance, ATGI contended, "could distort the economic evaluation of resale vs. facilities-based competition." (Reply Comments, p. 4). Finally ATGI argued that consideration of the appropriate cost methodology should await the adoption of new FCC rules and concurred with Staff that adopting a methodology should precede the submission of cost studies.

The ALJ's Analysis. In its Affidavit, the ALJ found that Qwest made a *prima facie* showing of harm by the Commission's failure to act, if the discount rate ultimately determined by the Commission were less than 18.5 percent. The extent of such lost revenues would be calculated by multiplying the discount differential in percent by $31,351 multiplied by the temporal delay in months. ATGI's skepticism, absent any evidentiary submission, failed, in the ALJ's view, to overcome Qwest's showing in this regard. Furthermore, the ALJ's examination of the language utilized by the Eighth Circuit in its ruling with respect to "avoided" versus "avoidable" costs, led him to find that there was a substantial likelihood that such financial harm would be significant. Given the likelihood of significant harm to Qwest and the regulatory uncertainty at the federal level, the ALJ found that good cause existed to reassess the impact of the U.S. District Court remand of the aforementioned arbitration cases.

The ALJ also noted that the parties to this proceeding had argued at length about the legality of suspending these proceedings in light of *US WEST Communications, Inc. v. AT&T Communications of the Pacific Northwest, Inc.,* 31 F.Supp.2d 839 (D. Or. 1998). Among the reasons for deferring action until the federal litigation had run its course, was that there was significant value in having uniform national standards, as the FCC indicated in its *First Report and Order.* However, in the wake of the Supreme Court's affirmation of the Eighth Circuit's remand, it was clear that such uniform, minimum standards would not be available anytime soon and the potential harm to Qwest would increase accordingly. In light of the change in circumstances, The ALJ determined to lift the suspension of proceedings and set a hearing schedule.

Finally, the ALJ also concluded that the Commission had latitude to fashion these proceedings in the manner necessary to develop an appropriate methodology and analyze any cost study submitted and decided that it would aid in the orderly conduct of the case, to begin with the consideration of a common methodology for both Qwest and Verizon, after which cost studies will be submitted and examined.

Qwest and Verizon filed testimony in June, 2001, which included cost studies using methodologies which, they contended, were in compliance with the FCC's rules, even though they had no independent force and effect on our determination of the proper standards to be applied in an avoided cost study. Qwest came up with a composite discount rate of 10.8 percent and Verizon came up with a composite rate of 12.2 percent.

II. THE STIPULATION

The Proceedings Leading Up to the Drafting of the Stipulation. At the wholesale discount cost methodology workshop conducted on July 11, 2001, pursuant to the schedule adopted in the April 27, 2001, Fourth Prehearing Conference Report and Ruling, Verizon indicated a willingness to enter into a stipulation settling the issues in this docket. Shortly thereafter, Qwest indicated a willingness to enter into a similar stipulation.

On August 6, 2001, Staff filed a Motion to Extend (Motion), requesting that the ALJ modify the schedule adopted in the April 27, 2001, Fourth Prehearing Conference Report and Ruling. In its Motion, Staff indicated its belief that a stipulated agreement was a reasonable and expeditious way to resolve the issues in this docket. In order to permit the settlement negotiations to go forward and potentially reduce the burden of preparing for litigation, by Ruling of August 21, 2001, the ALJ postponed the proceedings for a forty-five day period. Under that postponed schedule, Response Testimony by all parties was due October 2, 2001, Rebuttal Testimony was due October 30, 2001, the last day to serve data requests was November 6, 2001 and the dates of the hearing were November 29-30, 2001.

On September 28, 2001, Verizon filed a Motion to Suspend Testimony and Hearing Schedule and Establish a Date to Submit Stipulation and Supporting Testimony and Explanatory Briefs (Motion). In its Motion, at page 2, Verizon indicated that settlement conferences were held on August 15 and September 5, 2001, and that

> As a result of these discussions, Staff, Verizon and Qwest have reached a Stipulation to settle all issues except one: Issue 8: Should the Commission prospectively apply rates resulting from the adoption of wholesale discount rules to existing agreements whose rates had previously been determined by the commission through arbitration?

Verizon stated that the submission of the Stipulation would be contemporaneous with the filing of supporting testimony and/or explanatory briefs and that the signatories would also simultaneously file testimony and/or explanatory briefs with respect to Issue 8. In light of the ability of intervening parties to object to the Stipulation within 20 days of its filing, Verizon asks that the current schedule be suspended and a date for the submission of the Stipulation and supporting documents be set. Staff and Qwest supported the Motion. Pursuant to the ALJ's Ruling of October 2, 2001, Qwest, Verizon and the Commission Staff filed the Stipulation and supporting briefs and testimony on October 19, 2001, ASCENT and WorldCom filed Comments on November 8, 2001, and Qwest, Verizon and Staff filed replies on November 26, 2001.

The Terms of the Stipulation and the Arguments Related to Its Adoption. In September, 2001, Staff, Verizon and Qwest reached a joint stipulation on all of the issues in the proceeding, including the setting of a 17 percent default discount rate, except as to whether the rates should be applied to existing agreements or only prospectively. Staff, Qwest and Verizon filed briefs supporting the stipulation and opposing briefs with respect to the issue of prospective versus current contract application, on October 19, 2001. The Stipulation, a copy of which is affixed as Appendix A, contains nine provisions, which may be summarized as follows:

1. The Parties agreed to establish a permanent default wholesale discount rate for use in Oregon without endorsing any position on avoided cost methodology or the issues in the docket.
2. The wholesale discount rate is set at the greater of 17%, or the retail discount percentage plus one-half of the new discount rate (8.5%).[3]
3. The Parties agreed not to seek retroactive application of the 17% rate and adopted procedures for filing testimony and briefs supporting the Stipulation and discussing the scope of its applicability.
4. The parties agreed that the default discount rate would be the basis for resolving future arbitrations under the Act.
5. The term of the discount rate is the least of either three years, the date the Commission modifies the discount rate or the FCC directs the Commission to commence new proceedings.
6. The Parties will recommend to the Commission that it apply the new discount rate to existing arbitrated agreements as if the rate had been determined after review of a cost study.
7. The other terms and conditions of existing interconnection agreements are unchanged.
8. Issues 1 through 7 are deemed resolved by the Stipulation. Issue 8 will be separately briefed pursuant to Provision 3.
9. Parties may withdraw from the Stipulation should it be materially modified by the Commission.

As would be expected, each of the signatories to the Stipulation filed testimony supporting its adoption by the Commission. The Staff noted that the agreed rate was considerably higher than Verizon's and Qwest's original cost study discount rates. Furthermore, the settlement's 17 percent rate looked attractive when balanced against the uncertainty of the costs that would actually be avoided, coupled with the void of rules and methods to guide the Commission described above and the likelihood that any methodology held a considerable possibility of providing a much smaller discount.[4]

Qwest supported the Stipulation because the interim 22 percent discount rate established in the AT&T/MCI arbitration (ARB 3/6), and adopted by other CLEC's via "pick and choose" was, in Qwest's view, too high. Qwest also believed that U.S. District Court's decisions required the elimination of multiple discount rates for different CLECs and the establishment of uniform default rates. Qwest also was willing to accept the higher discount rate because it was for a limited period of time and allowed the company to avoid

[3] For example, if the retail discount were 8 percent, the reseller would get a 17 percent wholesale discount because 17 is greater than 8 + 8 ½. If the retail discount were 16 percent, the reseller would get a 24.5 percent discount (16+8.5).

[4] Staff/1, Turner/12-15. Staff's analysis, using various assumptions consistent with the Appellate Court's rulings, provided a discount range for Qwest of 12 to 14.3% and a discount range of 9.4 to 15.5% for Verizon.

the costs of litigating and then relitigating the same issues within a three-year period. Finally, Qwest wanted to remove the current "interim" label from the rates.[5]

Verizon supported the Stipulation because, in its view, the Stipulation would terminate prolonged and expensive legal proceedings, still provide CLECs with a rate "well above the rate Verizon and Qwest believe the law requires, " and will encourage CLEC competition by bringing certainty to the marketplace.[6]

ASCENT, the CLEC organization, and WorldCom each filed comments in opposition to the Stipulation on November 8, 2001. ASCENT argued that, since the ILECs sought the proceedings in the first place, they shouldn't be allowed to change their position and "hedge their bets" against new rules by entering into the Stipulation. ASCENT notes a series of ALJ Rulings designed to keep the methodology and cost study proceedings moving forward.[7] ASCENT further claimed that ILECs are asking CLECs, who generally lack the resources or capability to analyze the ILECs studies, to accept their calculations without scrutiny on a "take it or leave it" basis.[8] ASCENT was further concerned that the Oregon Stipulation might become an especially dangerous precedent which the ILECs could "export" to other jurisdictions.[9] Finally, while ASCENT acknowledged Staff's evaluative efforts, it argued that a proper methodology is a prerequisite for any Stipulation, regardless of how reasonable the numbers might, at first blush, appear.[10]

Verizon contended that ASCENT merely sought to benefit from unreasonably high discount rates without providing any valid reasons. Contrary to ASCENT's claims, Verizon asserted that it has provided cost studies showing rates well below the stipulated discount and which the Staff, even using outdated models, cannot raise to the existing level.[11] Staff likewise argued that ASCENT's objections are unsubstantiated and its claims that the Stipulation are insufficiently supported are incorrect.[12]

WorldCom objected to the Stipulation only in part, finding fault specifically with Provision 5 of the Stipulation, which prevents any person from filing a petition for a new discount rate for three years, unless the FCC directs the Commission to do so based upon changes and adoption of new resale rules. WorldCom claimed that such a provision violates carriers' arbitration rights because it prohibits non-signatories from petitioning the Commission for a different discount rate. WorldCom argued that any Commission order should state that the rights of non-signatories would not be abrogated.[13] Worldcom asserted that the Stipulation violates both Section 252(b)(1) of the Act and OAR 860-016-0030 because a CLEC has the right to have *any* disputed provisions of an interconnection

[5] Qwest/2, Mason/4-5.

[6] Explanatory Brief of Verizon Northwest Inc. in Support of the Stipulation (Verizon Brief), p. 5.

[7] Comments of the Association of Communications Enterprises (ASCENT Comments), pp. 2-3.

[8] *Id.*, p. 4.

[9] *Id.*, p. 6.

[10] *Id.*, pp. 6-7.

[11] Verizon Reply Comments, pp. 2-3.

[12] Staff Reply Comments, pp. 3-4.

[13] Comments of WorldCom, Inc., in Partial Opposition to the Stipulation (WorldCom Comments), p. 4.

agreement arbitrated. Thus, any party that wishes a locked-in three-year rate can individually contract for that term.[14]

Staff noted that WorldCom is not constrained from seeking a new discount rate because only a *default* rate is being established in this docket.[15]

Verizon also asserted that these rates are default rates and that WorldCom and other CLECs may negotiate different rates without waiting the three-year period described in Paragraph 5 of the Stipulation. It also noted Staff's and ASCENT's approval of the three-year period as being helpful to and requested by smaller CLECs, not Verizon.[16]

III. THE DISPUTE OVER THE APPLICABILITY OF THE RATE TO EXISTING CONTRACTS.

Staff could not reach an agreement with Qwest or Verizon with respect to Issue 8, which was defined as follows:

> Should the Commission prospectively apply rates resulting from the adoption of wholesale discount rules to existing agreements whose rates had previously been determined by the Commission through arbitration?

Staff believed that the issue, as framed by the ALJ, did not go to the heart of the dispute: "[T]he fact that a discount rate was determined by an arbitration, by itself, should not control whether the default rate adopted in this docket should apply. Rather the question should turn on the specific language of the interconnection agreements and/or the arbitrator's decision/Commission order."[17] Staff reviewed seven Commission arbitration orders [Agreements 1, 2, 3, 5, 6, 9 and 10] and concluded that, in four of them the Commission indicated that the rates were interim rates which "should be replaced when the Commission adopted a new wholesale discount rate at the conclusion of this docket…. The Commission was not clear in the other three orders that the rate should be replaced if and when the Commission adopted a wholesale discount rate in a docket such as this."[18] These latter three arbitrations are ARB 3 and ARB 6 (both decided in Order No. 97-003) and ARB 10 (Order 97-052). Staff argues that, since each agreement presumably has its own provisions that detail how the parties should treat changes in law or rates, the discount rate should be applied in accordance with those provisions. Each contract's provisions should govern how or if the new rate should be applied and the Commission should not apply such rates in any of the arbitrated agreements without giving the parties to such agreements the

[14] *Id.,* pp. 6-7.
[15] Staff Reply Comments, pp. 1-2.
[16] *Id.,* pp. 4-5.
[17] Staff's Brief Re: Issue No. 8, p. 2.
[18] *Id.* In ARB 1, neither the arbitrator's decision nor the Commission's Order stated that the discount rate was an interim rate. However, the arbitrator did adopt MFS's position that the rate was interim (Order No. 96-324, Arb Decision, p. 9).

opportunity to present their views as to the agreements' intents.[19] Staff further argued that, in those instances where the Commission wished to apply the new discount rate to contracts in a way not contemplated by the parties, the Commission might run afoul of Article I, section 21 of the Oregon Constitution under a claim of impairment of contractual obligations.[20]

WorldCom concurred in Staff's view that the applicability of any new rate should be decided on a case-by-case basis after review of the terms of each individual interconnection agreement, noting that MCIMetro's agreement with Qwest "does not contain any language even indirectly suggesting that the resale discount is interim, nor does the Commission decision approving that agreement.[21]

Qwest believed that the default rate should be applied to the existing arbitrated agreements and those agreements including terms resulting from other parties opting-in to existing arbitrated agreements, not, as intimated by WorldCom, to *all* agreements.[22] Qwest cited the ALJ's establishment of procedures well in advance of the Stipulation which placed the issue of the treatment of existing arbitrated agreements directly within the subject matter of the docket and that Staff's recommendation that the Commission not decide such matters is contrary to the issues list.[23] With respect to the legal precedents in the case, Qwest asserted that, contrary to the claims of Staff and WorldCom, the arbitrator's and Commission's decisions are all clear in their intention that the rates adopted as part of those agreements were interim and that the actions of the U.S. District Court support Qwest's contention and are not merely the "reviewing of selected agreements" as WorldCom contends.[24] Qwest contended that the Commission is obligated by the U.S. District Court's mandate to put the new rates into effect and that it would be unfair and a waste of expense and time to require Qwest and Verizon to negotiate with CLECs over this issue. The constitutional issue is, according to Qwest, merely a "red herring," because, among other things, the rates were interim, notice to all affected parties has been adequate and the public policy justification required by the Constitution is present.[25]

Verizon also asked the Commission order the immediate applicability of the new rates to Verizon's existing interconnection agreements. Verizon claimed that Staff and WorldCom have not offered a single interconnection agreement that does not unambiguously state that the discount rates are interim and that the plain language of the arbitrator's decisions support that view. Thus there is no basis for a "case-by-case" review of Verizon agreements after this proceeding and all parties have had adequate notice of the Commission's intention to set new default discount rates for all, pursuant to the mandate of the U.S. District Court.[26]

[19] *Id.*, p. 5.
[20] *Id.,* pp. 6-7.
[21] WorldCom Comments, pp. 7-8 citing Order No. 97-003 (January 6, 1997).
[22] Qwest Reply Comments, p. 2.
[23] *Id.,* p. 3.
[24] *Id.,* pp. 4-7.
[25] *Id.,* pp. 7-11.
[26] Verizon Comments, pp. 5-7.

IV. DISCUSSION

A. Acceptance of the Stipulation.

The interim rates which were in effect for many years, are, by everyone's admission, derived from a methodology which has been rejected by the Courts. At different judicial levels, the Courts have ordered both the FCC and this Commission to develop new rules and new default rates. The FCC has thus far failed to initiate any proceeding to respond to the Courts' mandate and CLECs have indicated that uniform national standards would make their participation in state proceedings such as this less burdensome. We therefore welcome any opportunity to fairly address this issue pending the development of national standards. The Stipulation fulfills this need.

Qwest and Verizon filed cost studies in compliance with the Eighth Circuit's decision (Qwest/1-Qwest/7 and Verizon/1). Staff reviewed and analyzed the cost data using Total Service Long Run Incremental Cost (TSLRIC) FCC and Oregon Commission-sanctioned methods (Staff/1-Staff/3) and concluded that "this approach would probably not lead us to higher discounts [than the Stipulation-provided 17%]."[27] Thus, the internally-derived compromise figure appears reasonable. For comparison purposes, it should be noted that, according to Qwest's July 12, 2002, Section 271 FCC filing, the stipulated 17 percent is a greater discount than that currently approved in Utah, Washington, Wyoming, Colorado, Iowa, North Dakota and Nebraska. Only Montana had a greater discount rate: 18.1 percent.

While ASCENT contended that the Commission should go through the entire process which we originally contemplated, even in the absence of definitive FCC rules, it made no showing as to why the Stipulation is not a fair, just and comparatively prompt resolution of an issue which has been facing the Commission for several years, especially in light of the fact that the rates are default rates and that they may be revisited in a comparatively short time period. We further note that ASCENT has had the benefit of the higher rates during the pendency of this proceeding, delay having worked in the favor of its membership. We reject ASCENT's unsubstantiated claims that the 17 percent rate is factually unsupported and unjustified. To the contrary, the studies submitted by Qwest and Verizon have been analyzed by the Staff in sworn testimony. We adopt the 17% rate as the default rate for the period set forth in the Stipulation.

We also reject WorldCom's argument that Provision 5 of the Stipulation violates carriers' arbitration rights because it prohibits non-signatories from petitioning the Commission for a different discount and, it argued, that a CLEC has the right to have *any* disputed provisions of an interconnection agreement arbitrated. As noted by Staff, we are establishing a default rate in this proceeding and parties are free to negotiate whatever terms they wish in any given agreement. Our decision here does not impinge upon that right. The Stipulation is adopted.

[27] Staff/1,Turner/16, line 14.

B. The Applicability of the Default Rate to Existing Agreements.

Staff, Qwest and Verizon are not as far apart as they might first appear to be with respect to Issue 8. For those arbitrations where the arbitrator or the Commission specifically noted that the discount rates were interim, all agree that adoption of the Stipulation would serve to immediately change the discount. This would also apply to contracts where the interim rate was adopted under Section 252(i), the "pick and choose" provisions, of the Act.[28] Verizon contended that all of its agreements specified interim rates[29] and thus, if true, all of its arbitrated contracts would reflect the new default rate. For the other arbitrated agreements, ARB 3, ARB 6 and ARB 10, and agreements where the resale discount rate was adopted from them under "pick and choose," Staff contended that the rate does not automatically change to the new default rate, but rather, parties may seek Commission review of the language of the agreement to determine whether such changes were contemplated.

While Qwest argued that the U.S. District Court's opinions require all of the arbitrated agreements to adopt the new default rate, we disagree. Several court orders dealing with the appeals of the arbitrations, each having different issues and fact patterns, were issued simultaneously. The language referred to by Qwest in the ARB3/6 order relies on Commission representations made in a case that was the subject of *another opinion issued the same day.* The Commission made no such representations in ARB 3/6. We are therefore of the view that the Court only intended its views to be non-binding dicta in ARB 3/6 itself, where the interim nature of the discount rate was not at issue. The language of the interconnection agreement itself is the appropriate source for determining whether the discount rate in any particular arbitrated agreement changes when there is a change in federal or state laws or regulations, or when judicial or agency rulings are issued.

ORDER

1. The default wholesale discount rate for retail services purchased from an incumbent local exchange carrier shall be the greater of

    a. 17%; or

    b. Any retail discount percentage, plus 8.5%.

2. The Stipulation, attached hereto as Appendix A is ADOPTED and made part of this Order.

[28] "A local exchange carrier shall make available without unreasonable delay to any requesting telecommunications carrier any individual interconnection*, service*, or network element arrangement contained in any agreement to which it is a party that is approved by a state commission pursuant to section 252 of the Act, upon the same rates, terms, and conditions as those provided in the agreement." (emphasis supplied).

[29] Verizon Comments, pp. 5-7.

3. The new default discount rate for wholesale purchase of incumbent local exchange carriers' retail services for resale shall immediately replace the resale discount rates contained in the arbitrated agreements which were the subjects of ARB 1, ARB 2, ARB 5 and ARB 9 and contracts opting in to those rates under the provisions of the Telecommunications Act of 1996.

4. Parties to arbitrated interconnection agreements which were the subject of ARB 3/6 and ARB 10 and parties to contracts that opted in to those rates under the provisions of the Telecommunications Act of 1996, may freely negotiate modifications to their agreements with respect to the discount rate. In the event that no agreement can be reached with respect to the discount rate provisions, and Commission arbitration is sought, the parties shall continue to utilize existing resale discount rates pending the outcome of any proceeding in which a party to such agreements seeks a decision from the Commission as to the applicability of the new discount rate to such existing arbitrated agreement.

Made, entered, and effective ____________________________.

____________________________ **Roy Hemmingway** Chairman	____________________________ **Lee Beyer** Commissioner
	____________________________ **Joan H. Smith** Commissioner

A party may request rehearing or reconsideration of this order pursuant to ORS 756.561. A request for rehearing or reconsideration must be filed with the Commission within 60 days of the date of service of this order. The request must comply with the requirements in OAR 860-014-0095. A copy of any such request must also be served on each party to the proceeding as provided by OAR 860-013-0070(2). A party may appeal this order to a court pursuant to applicable law.