

ORIGINAL



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MEMORANDUM

TO: Docket Control

FROM: Ernest G. Johnson  
*sen* Director  
Utilities Division

DATE: July 17, 2008

RE: IN THE MATTER OF THE APPLICATION OF CBeyond COMMUNICATIONS, LLC FOR APPROVAL OF A CERTIFICATE OF CONVENIENCE AND NECESSITY TO PROVIDE FACILITIES BASED LOCAL EXCHANGE TELECOMMUNICATIONS SERVICES AS WELL AS RESOLD LONG DISTANCE TELECOMMUNICATIONS SERVICES DOCKET NO. T-20497A-06-0802

Attached is the Staff Report for the above referenced application. The applicant is applying for approval to provide the following services:

- Facilities-Based Local Exchange Services
- Resold Long Distance Services

Staff is recommending approval of the application.

Originator: Candrea Allen

Attachment: Original and thirteen Copies

Arizona Corporation Commission  
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DOCKET NO. T-20497A-06-0802

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STAFF REPORT  
UTILITIES DIVISION  
ARIZONA CORPORATION COMMISSION

CBEYOND COMMUNICATIONS, LLC  
DOCKET NO. T-20497A-06-0802

IN THE MATTER OF THE APPLICATION OF CBEYOND COMMUNICATIONS, LLC FOR  
APPROVAL OF A CERTIFICATE OF CONVENIENCE AND NECESSITY TO PROVIDE  
FACILITIES BASED LOCAL EXCHANGE TELECOMMUNICATIONS SERVICES AS  
WELL AS RESOLD LONG DISTANCE TELECOMMUNICATIONS SERVICES

JULY 17, 2008

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## STAFF ACKNOWLEDGEMENT

The Staff Report for the application of Cbeyond Communications, LLC for approval of a Certificate of Convenience and Necessity to provide Facilities Based Local Exchange Telecommunications Services as well as Resold Long Distance Telecommunications Services (Docket No. T-20497A-06-0802) was the responsibility of the staff member listed below. Candrea Allen was responsible for the review and analysis of the application.

A handwritten signature in black ink, appearing to read 'Candrea Allen', written over a horizontal line.

Candrea Allen  
Executive Consultant I

## 1. INTRODUCTION

On December 28, 2006, Cbeyond Communications, LLC ("Cbeyond" or "Applicant" or "Company") filed an application for a Certificate of Convenience and Necessity ("CC&N") to provide facilities-based local exchange and resold long distance telecommunications services within the State of Arizona. The Applicant petitioned the Arizona Corporation Commission ("Commission") for a determination that its proposed services should be classified as competitive.

Staff's review of this application addresses the overall fitness of the Applicant to receive a CC&N. Staff's analysis also considers whether the Applicant's services should be classified as competitive and if the Applicant's initial rates are just and reasonable.

### *1.1 Technical Capability to Provide the Requested Services*

Cbeyond indicated that it currently provides telecommunications services in California, Colorado, Georgia, Illinois, and Texas. The Applicant also indicated that it is authorized to provide services in Florida, Massachusetts, Michigan, Minnesota, Missouri, New York, North Carolina, Pennsylvania, Virginia, Washington, and the District of Columbia. Based on this, Staff believes Cbeyond possesses the technical capabilities to provide the services it is requesting the authority to provide.

### *1.2 Financial Capability to Provide the Requested Services*

The Applicant provided audited financial statements of its parent company, Cbeyond, Inc., for the year ending December 31, 2006. These financial statements list assets of \$144,393; equity of \$91,108; and a net income of \$7,780. The Applicant provided notes related to the financial statements.

The Applicant states in its Local Exchange Telecommunications Services Tariff (reference Sections 2.10 and 2.11 on Page 22) that it may collect deposits from its local exchange service or interexchange service customers. The Applicant also states that it will not require advanced payments from its local exchange or interexchange service customers. Staff recommends that the Applicant procure a performance bond or an irrevocable sight draft Letter of Credit equal to \$110,000. The minimum bond or draft amount of \$110,000 should be increased if at any time it would be insufficient to cover advances, deposits, and/or prepayments collected from the Applicant's customers. The performance bond or irrevocable sight draft Letter of Credit amount should be increased in increments of \$55,000. This increase should occur when the total amount of the advances, deposits, and prepayments is within \$11,000 of the bond amount. If the Applicant desires to discontinue service, it must file an application with the Commission pursuant to A.A.C. R14-2-1107. Additionally, the Applicant must notify each of its customers and the Commission 60 days prior to filing an application to discontinue service. Failure to meet this requirement should result in forfeiture of the Applicant's performance bond or irrevocable sight draft Letter of Credit. Staff further recommends that proof of the above

mentioned performance bond or irrevocable sight draft Letter of Credit be docketed within 30 days of the effective date of an Order in this matter and must remain in effect until further order of the Commission.

### ***1.3 Establishing Rates and Charges***

The Applicant would initially be providing service in areas where an incumbent local exchange carrier ("ILEC"), along with various competitive local exchange carriers ("CLECs") and interexchange carriers are providing telephone service. Therefore, the Applicant would have to compete with those providers in order to obtain subscribers to its services. The Applicant would be a new entrant and would face competition from both an incumbent provider and other competitive providers in offering service to its potential customers. Therefore, the Applicant would generally not be able to exert market power. Thus, the competitive process should result in rates that are just and reasonable.

Both an initial rate (the actual rate to be charged) and a maximum rate must be listed for each competitive service offered, provided that the rate for the service is not less than the Company's total service long-run incremental cost of providing the service pursuant to A.A.C. R14-2-1109.

The rates proposed by this filing are for competitive services. In general, rates for competitive services are not set according to rate of return regulation. Staff obtained information from the Company indicating that its fair value rate base is zero. Accordingly, the Company's fair value rate base is too small to be useful in a fair value analysis. On December 28, 2006, Cbeyond submitted a tariff reflecting the actual rates that Cbeyond will be charging for its local and interexchange services. Staff has reviewed these rates and believes they are comparable to the rates charged by competitive local carriers, local incumbent carriers, and major long distance carriers operating in the State of Arizona. Therefore, while Staff considered the fair value rate base information submitted by the Company, the fair value rate base information provided should not be given substantial weight in this analysis.

## **2. LOCAL EXCHANGE CARRIER SPECIFIC ISSUES**

Issues related to the provision of that Local Exchange service are discussed below.

### ***2.1 Number Portability***

The Commission has adopted rules to address number portability in a competitive telecommunications services market. Local exchange competition may not be vigorous if customers, especially business customers, must change their telephone numbers to take advantage of a competitive local exchange carrier's service offerings. Consistent with federal laws, federal rules and A.A.C. R14-2-1308(A), the Applicant shall make number portability available to facilitate the ability of a customer to switch between authorized local carriers within

a given wire center without changing their telephone number and without impairment to quality, functionality, reliability or convenience of use.

## ***2.2 Provision of Basic Telephone Service and Universal Service***

The Commission has adopted rules to address universal telephone service in Arizona. A.A.C. R14-2-1204(A) indicates that all telecommunications service providers that interconnect into the public switched network shall provide funding for the Arizona Universal Service Fund ("AUSF"). The Applicant will make the necessary monthly payments required by A.A.C. R14-2-1204(B).

## ***2.3 Quality of Service***

Staff believes that the Applicant should be ordered to abide by the quality of service standards that were approved by the Commission for Qwest (fka USWC) in Docket No. T-0105 1B-93-0183 (Decision No. 59421). Because the penalties developed in that docket were initiated because Qwest's level of service was not satisfactory and the Applicant does not have a similar history of service quality problems, Staff does not recommend that those penalties apply to the Applicant. In the competitive market that the Applicant wishes to enter, the Applicant generally will have no market power and will be forced to provide a satisfactory level of service or risk losing its customers. Therefore, Staff believes that it is unnecessary to subject the Applicant to those penalties at this time.

## ***2.4 Access to Alternative Local Exchange Providers***

Staff expects that there will be new entrant providers of local exchange service who will install the plant necessary to provide telephone service to, for example, a residential subdivision or an industrial park much like existing local exchange companies do today. There may be areas where the Applicant installs the only local exchange service facilities. In the interest of providing competitive alternatives to the Applicant's local exchange service customers, Staff recommends that the Applicant be prohibited from barring access to alternative local exchange service providers who wish to serve such areas. This way, an alternative local exchange service provider may serve a customer if the customer so desires. Access to other providers should be provided pursuant to the provisions of the 1996 Telecommunications Act, the rules promulgated there under and Commission rules on interconnection and unbundling.

## ***2.5 911 Service***

The Commission has adopted rules to address 911 and E911 services in a competitive telecommunications services market. The Applicant has certified that in accordance with A.A.C. R14-2-1201 (6)(d) and Federal Communications Commission 47 CFR Sections 64.3001 and 64.3002, it will provide all customers with 911 and E911 service, where available, or will coordinate with ILECs and emergency service providers to provide 911 and E911 service.

## ***2.6 Custom Local Area Signaling Service***

Consistent with past Commission decisions, the Applicant may offer Caller ID provided that per-call and line blocking, with the capability to toggle between blocking and unblocking the transmission of the telephone number, are provided as options to which customers could subscribe with no charge. Also, Last Call Return service that will not return calls to telephone numbers that have the privacy indicator activated, indicating that the number has been blocked, must be offered.

## **3. REVIEW OF COMPLAINT INFORMATION**

The Applicant indicated that it has neither had an application for service denied, nor revoked in any state. Consumer Services reports no complaint history within Arizona. The Applicant indicated that none of its officers, directors or partners has been involved in any civil or criminal investigations, or any formal or informal complaints. The Applicant also indicated that none of its officers, directors or partners has been convicted of any criminal acts in the past ten (10) years.

On April 21, 2006, the Enforcement Bureau (the "Bureau") of the Federal Communications Commission ("FCC") issued a Notice of Apparent Liability for Forfeiture ("NAL").<sup>1</sup> The Bureau had determined that Cbeyond had failed to produce and make publicly available an annual certificate stating that the Company had adequate operating procedures to ensure compliance with section 64.2009(e) of the FCC's rules concerning Customer Proprietary Network Information ("CPNI").<sup>2</sup> The Bureau found that Cbeyond was liable for a monetary forfeiture of \$100,000 for violating section 64.2009(e) of the FCC's rules and the CPNI Order. In response to Staff's Second and Fourth Sets of Data Requests, Cbeyond filed, on October 16, 2007, the Bureau's Order and Consent Decree between Cbeyond and the Bureau dated October 9, 2007.<sup>3</sup> In the FCC order, the Bureau terminated the NAL. The Bureau also entered into a Consent Decree with Cbeyond. The Consent Decree stated that during the time frame that Cbeyond was issued the NAL, the Bureau was investigating allegations that Cbeyond received proprietary information from another carrier and used the information obtained in violation of the Communications Act of 1934, as amended, and the FCC's rules. The agreement between the Bureau and Cbeyond consisted of (1) the termination of the NAL and the Investigation in accordance with the Consent Decree, (2) the voluntary contribution to the United States Treasury in the amount of \$200,000 by Cbeyond, (3) Cbeyond agreeing to submit to the Bureau annual certification of compliance with the FCC's CPNI rules, and (4) Cbeyond agreeing to continue with the operating procedures established by the Company to ensure compliance with the FCC's

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<sup>1</sup> See FCC *Notice of Apparent Liability and Forfeiture* DA 06-916

<sup>2</sup> See 47 C.F.R. § 64.2009(e); *Implementation of the Telecommunications Act of 1996: Telecommunications Carriers' Use of Customer Proprietary Network Information and Other Customer Information and Implementation of the Non-accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended*, Order and Further Notice of Proposed Rule Making, 13 FCC Rcd 8061 (1998) ("CPNI Order")

<sup>3</sup> See FCC Consent Decree *DA 07-4090*

CPNI rules. The Consent Decree is scheduled to expire twenty four months from the effective date of the Bureau Order which was adopted on October 5, 2007.

Staff was able to obtain the following information from the five State Commissions (California, Colorado, Georgia, Illinois, and Texas) in which Cbeyond currently provides service:

State	No. Complaints	No. of Complaints Resolved in Favor of the Customer
Colorado	34	5
Georgia <sup>4</sup>	39	N/A
Illinois	3	0
Texas	30	2

According to the California Commission Staff, there have been no complaints filed against Cbeyond. In Colorado from June 2006 to June 2008, thirty-four complaints were filed against Cbeyond, and all have been closed. The five complaints filed in Colorado that were resolved in favor of the customer were billing (one complaint), cramming (one complaint), and slamming (three complaints) issues. The customer complaints filed in Georgia were from 2001 to 2007, and all have been closed. Staff was not able to obtain any details from the Georgia Commission Staff about the resolution of the complaints. The three complaints that were filed in Illinois from September 2006 through January 2007 were all service complaints (service availability, service reconnection/disconnection, and service interruption) and all have been closed. Of the thirty complaints filed in Texas from March 2005 to December 2006, only two complaints were resolved in favor of the customers: a quality of service issue and a telephone solicitation matter.

#### **4. COMPETITIVE SERVICES ANALYSIS**

The Applicant has petitioned the Commission for a determination that the services it is seeking to provide should be classified as competitive.

##### ***4.1 Competitive Services Analysis for Local Exchange Services***

###### ***4.1.1 A Description Of The General Economic Conditions That Exist Which Makes The Relevant Market For The Service One That Is Competitive.***

The local exchange market that the Applicant seeks to enter is one in which a number of new CLECs have been authorized to provide local exchange service. Nevertheless, ILECs hold a virtual monopoly in the local exchange service market. At locations where

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<sup>4</sup> Because Staff was not able to obtain information form the Georgia Commission Staff relative to the resolution of the complaints that were filed, the information that was provided was not given substantial weight in this analysis.

ILECs provide local exchange service, the Applicant will be entering the market as an alternative provider of local exchange service and, as such, the Applicant will have to compete with those companies in order to obtain customers. In areas where ILECs do not serve customers, the Applicant may have to convince developers to allow it to provide service to their developments.

*4.1.2 The number of alternative providers of the service.*

Qwest and various independent LECs are the primary providers of local exchange service in the State. Several CLECs and local exchange resellers are also providing local exchange service.

*4.1.3 The estimated market share held by each alternative provider of the service.*

Since Qwest and the independent LECs are the primary providers of local exchange service in the State, they have a large share of the market. Since the CLEC and local exchange resellers have only recently been authorized to offer service they have limited market share.

*4.1.4 The names and addresses of any alternative providers of the service that are also affiliates of the telecommunications Applicant, as defined in A.A.C. R14-2-801.*

None.

*4.1.5 The ability of alternative providers to make functionally equivalent or substitute services readily available at competitive rates, terms and conditions.*

ILECs have the ability to offer the same services that the Applicant has requested in their respective service territories. Similarly many of the CLECs and local exchange resellers also offer substantially similar services.

*4.1.6 Other indicators of market power, which may include growth and shifts in market share, ease of entry and exit, and any affiliation between and among alternative providers of the service(s).*

The local exchange service market is:

- a. One in which ILECs own networks that reach nearly every residence and business in their service territories and which provide them with a virtual monopoly over local exchange service. New entrants are also beginning to enter this market.
- b. One in which new entrants will be dependent upon ILECs:

1. To terminate traffic to customers.
  2. To provide essential local exchange service elements until the entrant's own network has been built.
  3. For interconnection.
- c. One in which ILECs have had an existing relationship with their customers that the new entrants will have to overcome if they want to compete in the market and one in which new entrants do not have a long history with any customers.
- d. One in which most customers have few, if any choices since there is generally only one provider of local exchange service in each service territory.
- e. One in which the Applicant will not have the capability to adversely affect prices or restrict output to the detriment of telephone service subscribers.

#### ***4.2 Competitive Services Analysis for Interexchange Services***

##### *4.2.1 A description of the general economic conditions that exist, which makes the relevant market for the service one that, is competitive.*

The interexchange market that the Applicant seeks to enter is one in which numerous facilities-based and resold interexchange carriers have been authorized to provide service throughout the State. The Applicant will be a new entrant in this market and, as such, will have to compete with those companies in order to obtain customers.

##### *4.2.2 The number of alternative providers of the service.*

There are a large number of facilities-based and resold interexchange carriers providing both interLATA and intraLATA interexchange service throughout the State. In addition, various ILECs provide intraLATA interexchange service in many areas of the State.

##### *4.2.3 The estimated market share held by each alternative provider of the service.*

The large facilities-based interexchange carriers (AT&T, Sprint, MCI WorldCom, etc.) hold a majority of the interLATA interexchange market, and the ILECs provide a large portion of the intraLATA interexchange market. Numerous other interexchange carriers have a smaller part of the market and one in which new entrants do not have a long history with any customers.

##### *4.2.4 The names and addresses of any alternative providers of the service that are also affiliates of the telecommunications Applicant, as defined in A.A.C. R14- 2-801.*

None.

*4.2.5 The ability of alternative providers to make functionally equivalent or substitute services readily available at competitive rates, terms, and conditions.*

Both facilities-based and resold interexchange carriers have the ability to offer the same services that the Applicant has requested in their respective service territories. Similarly, many of the ILECs offer similar intraLATA toll services.

*4.2.6 Other indicators of market power, which may include growth and shifts in market share, ease of entry and exit, and any affiliation between and among alternative providers of the service(s).*

The interexchange service market is:

- a. One with numerous competitors and limited barriers to entry.
- b. One in which established interexchange carriers have had an existing relationship with their customers that the new entrants will have to overcome if they want to compete in the market.
- c. One in which the Applicant will not have the capability to adversely affect prices or restrict output to the detriment of telephone service subscribers.

## **5. RECOMMENDATIONS**

The following sections contain the Staff recommendations on the application for a CC&N and the Applicant's petition for a Commission determination that its proposed services should be classified as competitive.

### ***5.1 Recommendations on the Application for a CC&N***

Staff recommends that the Applicant's application for a CC&N to provide intrastate telecommunications services, as listed in this Report, be granted. In addition, Staff further recommends:

1. That the Applicant comply with all Commission Rules, Orders, and other requirements relevant to the provision of intrastate telecommunications services;
2. That the Applicant abide by the quality of service standards that were approved by the Commission for Qwest in Docket No. T-01051B-93-0183;
3. That the Applicant be prohibited from barring access to alternative local exchange service providers who wish to serve areas where the Applicant is the only provider of local exchange service facilities;

4. That the Applicant be required to notify the Commission immediately upon changes to the Applicant's name, address, or telephone number;
5. That the Applicant cooperate with Commission investigations including, but not limited to, customer complaints;
6. The rates proposed by this filing are for competitive services. In general, rates for competitive services are not set according to rate of return regulation. Staff obtained information from the Company and has determined that its fair value rate base is zero. Staff has reviewed the rates to be charged by the Applicant and believes they are just and reasonable as they are comparable to other competitive local carriers, local incumbent carriers, and major long distance companies offering service in Arizona and comparable to the rates the Applicant charges in other jurisdictions. The rate to be ultimately charged by the Company will be heavily influenced by the market. Therefore, while Staff considered the fair value rate base information submitted by the Company, the fair value information provided was not given substantial weight in this analysis;
7. That the Applicant offer Caller ID with the capability to toggle between blocking and unblocking the transmission of the telephone number at no charge;
8. That the Applicant offer Last Call Return service that will not return calls to telephone numbers that have the privacy indicator activated;
9. That the Commission authorize the Applicant to discount its rates and service charges to the marginal cost of providing the services;
10. That the Applicant submit interexchange tariffs which state that it does not collect advances, deposits, and/or prepayments;
11. That Cbeyond be required to file with the Commission in this docket, copies of the certifications sent to the FCC stating the Company's compliance with the FCC's rules concerning CPNI. Staff also recommends that Cbeyond be required to file these certifications with the Commission for twenty-four month subsequent to a Decision in this matter.
12. That Cbeyond be required to continue operating under the operating procedures established by the Company to ensure compliance with the FCC's CPNI rules as specified in the Consent Decree until further Order of the Commission.

Staff further recommends that the Applicant be ordered to comply with the following. If it does not do so, the Applicant's CC&N shall be null and void, after due process without further order of the Commission and no time extensions shall be granted.

1. The Applicant shall docket conforming tariffs for each service within its CC&N within 365 days from the date of an Order in this matter or 30 days prior to providing service, whichever comes first. The tariffs submitted shall coincide with the application and shall state that the Applicant does not collect advances, deposits and/or prepayments from its customers.
2. The Applicant shall:
  - a. Procure a performance bond or irrevocable sight draft Letter of Credit in the amount of \$110,000. The minimum performance bond or irrevocable sight draft Letter of Credit amount of \$110,000 should be increased if at any time it would be insufficient to cover advances, deposits, and/or prepayments collected from the Applicant's customers. The performance bond or irrevocable sight draft Letter of Credit amount should be increased in increments of \$55,000. This increase should occur when the total amount of the advances, deposits, and prepayments is within \$11,000 of the performance bond or irrevocable sight draft Letter of Credit amount.
  - b. Staff recommends that Cbeyond file the original performance bond or irrevocable sight draft Letter of Credit with the Commission's Business Office and copies of the performance bond or irrevocable sight draft Letter of Credit with Docket Control, as a compliance item in this docket, within 30 days of the effective date of a decision in this matter. The performance bond or irrevocable sight draft Letter of Credit must remain in effect until further order of the Commission. The Commission may draw on the performance bond or irrevocable sight draft Letter of Credit, on behalf of, and for the sole benefit of the Company's customers, if the Commission finds, in its discretion, that the Company is in default of its obligations arising from its Certificate. The Commission may use the performance bond or irrevocable sight draft Letter of Credit funds, as appropriate, to protect the Company's customers and the public interest and to take any and all actions the Commission deems necessary, in its discretion, including, but not limited to, returning prepayments or deposits collected from the Company's customers.

### ***5.2 Recommendation on the Applicant's Petition to have Proposed Services Classified as Competitive***

Staff believes that the Applicant's proposed services should be classified as competitive. There are alternatives to the Applicant's services. The Applicant will have to convince customers to purchase its services, and the Applicant has no ability to adversely affect the local exchange or interexchange service markets. Therefore, the Applicant currently has no market power in the local exchange or interexchange service markets where alternative providers of

telecommunications services exist. Staff therefore recommends that the Applicant's proposed services be classified as competitive.