No.s 00-511, 00-555, 00-590 and 00-602

In the Supreme Court of the United States

VERIZON COMMUNICATIONS, INC., ET AL., PETITIONERS

v.

FEDERAL COMMUNICATIONS COMMISSION, ET AL.

WORLDCOM, INC., ET AL., PETITIONERS

v.

VERIZON COMMUNICATIONS, INC., ET AL.

AT&T CORP., PETITIONER

v.

IOWA UTILITIES BOARD, ET AL.

GENERAL COMMUNICATIONS, INC., PETITIONER

v.

IOWA UTILITIES BOARD, ET AL.

ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE FEDERAL COMMUNICATIONS COMMISSION AND THE UNITED STATES

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QUESTIONS PRESENTED

The questions presented in the petitions are those presented in our petition for a writ of certiorari in *Federal Communications Commission* v. *Iowa Utilities Board,* No. 00-587 (filed Oct. 13, 2000), as well as the following:

1. Whether the court of appeals erred in holding that neither the Takings Clause nor the Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56, requires incorporation of an incumbent local exchange carrier's "historical" costs into the rates that it may charge new entrants for access to its network elements.

2. Whether the court of appeals erred in invalidating certain of the Federal Communications Commission's rules concerning the applicability to rural and small local exchange carriers of certain obligations imposed by the Telecommunications Act—specifically, those rules that (a) construe the "unduly economically burdensome" standard of 47 U.S.C. 251(f) and (b) impose the burden of proof in proceedings under 47 U.S.C. 251(f)(1) on the carrier seeking to be excused from its obligations under the Act.

3. Whether the court of appeals erred in invalidating the Federal Communications Commission's rule governing the "wholesale rates" that incumbent local exchange carriers may charge when providing their retail services to new entrants for resale under 47 U.S.C. 251(c)(4) and 252(d)(3).

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OPINIONS BELOW

The opinion of the court of appeals (Verizon Pet. App. 1a-43a; WorldCom Pet. App. 1a-34a; AT&T Pet. App. 1a-38a; GCI Pet. App. 1a-37a) is reported at 219 F.3d 744. The Order of the Federal Communications Commission (excerpted in Verizon Pet App. 44a-151a; WorldCom Pet. App. 39a-133a; AT&T Pet. App. 39a-202a; GCI Pet. App. 38a-85a) is reported at 11 F.C.C.R. 15,499.

JURISDICTION

The judgment of the court of appeals was entered on July 18, 2000. Verizon Communications Inc., *et al.*, (Verizon) filed a petition for a writ of certiorari on October 4, 2000; WorldCom, Inc., filed a petition for a writ of certiorari on October 10, 2000; AT&T Corp. filed a petition for a writ of certiorari on October 13, 2000; and General Communications, Inc. (GCI), filed a petition for a writ of certiorari on October 16, 2000. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

On October 13, 2000, the Federal Communications Commission (FCC) and the United States filed a petition for a writ of certiorari in *Federal Communications Commission* v. *Iowa Utilities Board*, No. 00-587 (U.S. Pet.). That petition seeks review of the same court of appeals decision at issue in the petitions to which this brief responds. Our petition sets forth the statutory scheme and the procedural background of this case in detail, and we refer the Court to that discussion.

1. a. As explained in our petition (at 3-4), Congress enacted the Telecommunications Act of 1996 (1996 Act), Pub. L. No. 104-104, 110 Stat. 56 (codified at 47 U.S.C.

251 *et seq.*), to open local telecommunications markets to full competition.[1] To that end, the 1996 Act imposes several requirements on incumbent local exchange carriers (incumbent LECs), the carriers that have historically exercised monopoly control over local telecommunications markets. Section 251(c)(3) requires that new entrants be able to gain "access" to (*i.e.*, to lease) an incumbent LEC's "network elements," such as loops, switching capability, and other components and capabilities of the incumbent's network. Section 251(c)(2) requires that new entrants be able to "interconnect[]" their own facilities with those in the incumbent's network. And Section 251(c)(4) requires that new entrants be able to purchase an incumbent's retail services "at wholesale rates" and to resell those services to end users.

In Section 251(f), Congress qualified the applicability of those requirements with respect to two discrete categories of small LECs. First, Section 251(f)(1) exempts a "rural telephone company," as defined in 47 U.S.C. 153(37), from the obligations of Section 251(c) until the company receives "a bona fide request" from another carrier "for interconnection, services, or network elements" under Section 251(c). 47 U.S.C. 251(f)(1)(A). Section 251(f)(1) further provides that a state public utility commission, within 120 days after receiving notice of the request, "shall terminate the exemption if the request is not unduly economically burdensome, is technically feasible, and is consistent with" most provisions of 47 U.S.C. 254, which addresses universal service issues. 47 U.S.C. 251(f)(1)(B).

Second, Section 251(f)(2) separately establishes conditions under which "[a] local exchange carrier with

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[1] All citations of the 1996 Act are of Supp. IV 1998.

fewer than 2 percent of the Nation's subscriber lines" may apply for a suspension or modification of the requirements of 47 U.S.C. 251(b) and (c). The statute authorizes state public utility commissions to grant such applications "to the extent that, and for such duration as," the suspension or modification is "consistent with the public interest" and "necessary" to "avoid a significant adverse economic impact on users of telecommunications services generally," to "avoid imposing a requirement that is unduly economically burdensome," or to "avoid imposing a requirement that is technically infeasible." 47 U.S.C. 251(f)(2). The state commission has 180 days to act on a petition for suspension or modification.

b. In the *Local Competition Order*, the FCC adopted rules to guide state public utility commissions in their application of Section 251(f). *In re Implementation of the Local Competition Provisions in the Telecomms. Act of 1996, First Report & Order (Local Competition Order)*, 11 F.C.C.R. 15,499, ¶¶ 1255-1265 (1996) (reprinted in AT&T Pet. App. 186a-195a); 47 C.F.R. 51.401-51.405. The FCC construed the "unduly economically burdensome" language of Section 251(f)(1) to mean that, in order to justify a continued exemption once a "bona fide request" has been made, a rural telephone company must demonstrate "that the application of the requirements of section 251(c) of the Act would be likely to cause undue economic burden beyond the economic burden that is typically associated with efficient competitive entry." 47 C.F.R. 51.405(c). The FCC took a similar approach with respect to the "unduly economically burdensome" standard of Section 251(f)(2) applicable to small local exchange carriers. 47 C.F.R. 51.405(d).

In adopting that approach, the FCC reasoned that Congress "did not intend to insulate smaller or rural LECs from competition, and thereby prevent subscribers in those communities from obtaining the benefits of competitive local exchange service." AT&T Pet. App. 193a. Instead, the FCC explained, Congress "intended exemption, suspension, or modification of the section 251 requirements to be the exception rather than the rule, and to apply only to the extent, and for the period of time, that policy considerations justify" such special treatment. *Ibid.*

The FCC then turned to the question of which party —the requesting carrier or the carrier seeking the exemption, suspension, or modification—should bear the burden of proof in disputes arising under Section 251(f). The FCC determined that the burden of proof appropriately rests with the carrier seeking the exemption, suspension, or modification, because that carrier is "the party seeking relief from otherwise applicable requirements," because that carrier "is in control of the relevant information necessary for the state to make a determination regarding the request," and, more generally, because placing the burden on that carrier ensures consistency with "the pro-competitive focus of the 1996 Act." AT&T Pet. App. 193a-194a; see 47 C.F.R. 51.405 (codifying rule).

c. In its initial 1997 decision, the court of appeals held that the FCC lacked statutory jurisdiction to issue rules implementing Section 251(f). *Iowa Utils. Bd.* v. *FCC*, 120 F.3d 753, 802 (8th Cir. 1997). This Court reversed and remanded for consideration of the FCC's rules on the merits. See *AT&T* v. *Iowa Utils. Bd.*, 525 U.S. 366, 385 (1999) (*Iowa Utils. Bd. I*).

On remand, in the ruling under review here, the Eighth Circuit invalidated the FCC's implementation of

Section 251(f) in two principal respects. First, the court held that the FCC's construction of the phrase "undue economic burden" in 47 C.F.R. 51.405(c) and (d) improperly "eliminat[ed]" any consideration of the "economic burden that is typically associated with efficient competitive entry." AT&T Pet. App. 29a. The court, reasoning that the statutory language "looks to the whole of the economic burden the request imposes, not just a discrete part," concluded that the FCC had "impermissibly weakened the broad protection Congress granted to small and rural telephone companies." *Id.* at 30a.[2]

Second, the court of appeals invalidated the FCC's determination that an incumbent LEC must bear the burden of proof in proceedings under Section 251(f)(1). AT&T Pet. App. 30a-32a. Observing that a rural LEC's exemption remains in effect until it is "terminate[d]" in state proceedings, the court held that the "plain meaning of the statute requires the party making the request [under Section 251(c)] to prove that the request meets the three prerequisites" for termination of the exemption. *Id.* at 32a.

2. a. As noted above (at 3), the 1996 Act requires incumbent LECs to offer certain of their retail services

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[2] The court of appeals vacated 47 C.F.R. 51.405(c) on an additional ground. The court reasoned that the rule, if read in isolation, could be construed as conditioning any exemption on an incumbent's ability to satisfy the FCC's interpretation of "undue economic burden," and thus as requiring state commissions to "disregard[] two of the three statutory requirements that must be met before a state commission can terminate an exemption" (*i.e.*, technical feasibility and consistency with Section 254). AT&T Pet. App. 27a. At the same time, the court acknowledged that, in an order issued after the one under review here, the FCC had clarified that the regulation should *not* be so interpreted. *Ibid.*

at "wholesale rates" to competitors, which may then resell those services to their own subscribers. 47 U.S.C. 251(c)(4)(A). In the *Local Competition Order*, the FCC observed that such "[r]esale will be an important entry strategy for many new entrants, especially in the short term when they are building their own facilities." AT&T Pet. App. 165a. "[I]n some areas and for some new entrants," the FCC added, "we expect that the resale option will remain an important entry strategy over the longer term." *Ibid.*

The 1996 Act directs that the "wholesale rates" described in Section 251(c)(4) be determined "on the basis of retail rates * * *, excluding the portion thereof attributable to any marketing, billing, collection, and other costs that will be avoided by the local exchange carrier." 47 U.S.C. 252(d)(3). In the *Local Competition Order*, the FCC determined that, in establishing the "costs that will be avoided" for purposes of that provision, a state public utility commission should include "all of the costs that the LEC incurs in maintaining a retail, as opposed to a wholesale, business." AT&T Pet. App. 168a. "In other words," the FCC explained, "the avoided costs are those that an incumbent LEC would no longer incur if it were to cease retail operations and instead provide all of its services through resellers." *Ibid.* The FCC specifically rejected the argument "that the LEC must actually experience a reduction in its operating expenses for a cost to be considered 'avoided' for purposes of section 252(d)(3)." *Ibid.* The FCC explained that Congress did not intend "to allow incumbent LECs to sustain artificially high wholesale prices by declining to reduce their expenditures to the degree that certain costs are readily avoidable." *Ibid.* The FCC codified its approach in a regulation stating that state commissions should exclude "those costs that reasonably can be avoided when an incumbent LEC provides a telecommunications service for resale at wholesale rates to a requesting carrier." 47 C.F.R. 51.609(b); see 47 C.F.R. 51.609(c)-(e) (specifying categories of retail-oriented costs).

b. On remand from this Court's decision reinstating the FCC's jurisdiction to implement the pricing rules of Section 251(c), the Eighth Circuit invalidated, on the merits, the FCC's interpretation of the wholesale pricing standard. The court of appeals reasoned that "the phrase 'will be avoided' [in 47 U.S.C. 252(d)(3)] refers to those costs that the [incumbent LEC] will actually avoid incurring in the future, because of its wholesale efforts, not costs that 'can be avoided.'" AT&T Pet. App. 17a. Thus, the court concluded that "[t]he plain meaning of the statute" requires that only those "costs that are actually avoided, not those that could be or might be avoided, should be excluded" from an incumbent LEC's retail rates in calculating the wholesale rates to be charged new entrants. *Ibid.*

DISCUSSION

In No. 00-511, Verizon seeks this Court's review of its claim that, when leasing network elements to competitors pursuant to 47 U.S.C. 251(c)(3), an incumbent is entitled to charge rates based on the "historical" cost of those elements, *i.e.*, the costs reflected on its accounting books. Although that claim is without merit, it is nonetheless related to the question presented in our petition for a writ of certiorari in No. 00-587, and we therefore do not oppose Verizon's petition so long as our petition is granted. In Nos. 00-555, 00-590, and 00-602, petitioners challenge, *inter alia*, portions of the decision below invalidating the FCC's rules with respect to exemptions, suspensions, and modifications for small and rural LECs under Section 251(f) and the wholesale pricing standard under Section 252(d)(3). As discussed below, although we did not include those issues in our own petition, the Court could appropriately decide to grant certiorari with respect to them as well.[3]

1. Section 252(d)(1) provides that the rates that an incumbent LEC may charge for the use of its network elements shall be "based on the cost (determined without reference to a rate-of-return or other rate-based proceeding) of providing the * * * element" and "may include a reasonable profit." 47 U.S.C. 252(d)(1). As discussed in our petition (at 3-8, 16-20), the FCC reasonably implemented that provision to ensure recovery of the forward-looking cost of network elements: *i.e.*, the cost of replacing the functions of network assets on today's market. The FCC rejected, as economically unsound and inconsistent with the 1996 Act's pro-competitive objectives, the argument that Verizon renews here: that "compensation for network elements must recover the historical costs reflected on incumbents' books." Verizon Pet. 11; see U.S. Pet. 6-7. The Eighth Circuit upheld the FCC's determination on that point (Verizon Pet. App. 10a-18a), and Verizon challenges that portion of the court's decision.[4]

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[3] AT&T and WorldCom also seek review of the Eighth Circuit's invalidation of (i) a portion of the FCC's pricing rules for network elements and interconnection and (ii) the FCC's "combinations rules" in 47 C.F.R. 51.315(c)-(f). We have presented those issues in our own petition.

[4] In the court of appeals, some incumbent LECs separately claimed an entitlement to recover, through the rates for network elements (rather than some other mechanism), implicit subsidies for providing universal service. The Eighth Circuit rejected that

Verizon focuses not on the text of Section 252(d)(1), but on the principle of constitutional avoidance. It argues that, to avoid a Takings Clause violation, Section 252(d)(1) must be construed to allow an incumbent to recover whatever it actually paid in the past for the elements that it now leases to new entrants. In the Takings Clause context, however, this Court and others have persistently rejected efforts to resort to the avoidance principle to "frustrate[] permissible applications of a statute or regulation" absent a concrete showing that government action will necessarily produce confiscatory results. *United States* v. *Riverside Bayview Homes, Inc.*, 474 U.S. 121, 128 (1985); see *National Mining Ass'n* v. *Babbitt*, 172 F.3d 906, 917 (D.C. Cir. 1999). Verizon can make no such showing here.

As an initial matter, when the government commits private property to public uses (*e.g.*, when condemning a house), it does not compensate the property owner in the amount that he or she paid for the property in the past. Instead, the government pays the owner the fair market value of the property—*i.e.*, "what a willing buyer would pay in cash to a willing seller" in today's market. *United States* v. *Miller*, 317 U.S. 369, 374 (1943). A methodology based on fair market value is analogous to a methodology based on forward-looking costs.[5] What Verizon seeks here, in contrast, is a

claim on the ground that, whereas Section 252(d)(1)(A) "requires rates to be cost-based," "[u]niversal service charges are not based on the actual costs of providing * * * the requested network element." U.S. Pet. App. 15a. No party has sought review of the Eighth Circuit's ruling on that point.

[5] In many cases, the forward-looking cost of a network asset may actually *exceed* its fair market value, because the asset can be

compensation rule entitling it to recover its historical costs for its assets, even when those costs far exceed the fair market value of those assets. The Takings Clause does not compel that result.

Verizon's argument is particularly unsound because incumbent LECs, as regulated public utilities, are subject to the regulatory takings analysis of *Duquesne Light Co.* v. *Barasch*, 488 U.S. 299 (1989), and *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944). In *Duquesne*, the Court specifically rejected the argument that the Takings Clause entitles a utility to recover all of its prudently incurred historical costs. See 488 U.S. at 301-302, 307-316; accord *FERC* v. *Pennzoil Producing Co.*, 439 U.S. 508, 517-520 (1979); *Market St. Ry.* v. *Railroad Comm'n*, 324 U.S. 548, 553-554, 564-568 (1945). The Court explained that the Constitution protects a public utility only from "the net effect of the rate order on its property," *Duquesne*, 488 U.S. at 314, so that "[i]f the total effect of the rate order cannot be said to be unreasonable, judicial inquiry * * * is at an end," *id.* at 310 (quoting *Hope*, 320 U.S. at 602). Here, as in *Duquesne*, "[n]o argument has been made" that the regulatory measure at issue "jeopardize[s] the financial integrity of the companies, either by leaving them insufficient operating capital or by impeding their ability to raise future capital." *Id.* at 312. To the contrary, Verizon and its fellow petitioners have generally enjoyed quite healthy returns in recent years.[6] Moreover, the 1996 Act as a whole confers very significant bene-

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replaced in today's market only by an asset that has more sophisticated capabilities and therefore commands a higher price.

[6] See *Interstate Rate of Return Summary, Years 1991 Through 1999* (FCC Apr. 4, 2000) (http://www.fcc.gov/Bureaus/Common_Carrier/ Reports/FCC-State_Link/IAD/ror99.pdf).

fits on those carriers by, for example, eliminating or reducing restrictions on their entry into the long-distance market. See 47 U.S.C. 271 (prescribing method whereby Bell companies may obtain permission to enter that market); 1996 Act, Title VI, § 601(a)(2), 110 Stat. 143 (relieving GTE from restrictions on provision of long-distance service).[7]

There is, moreover, no merit to Verizon's contention (Pet. 15-16) that the FCC's use of a forward-looking approach is inconsistent with *Duquesne* on the theory that the FCC has improperly "switche[d]" compensation methodologies. To begin with, *Duquesne* specifically *affirms* the discretion of regulators to alter rate-setting methodologies to accommodate changes in regulatory policy, even if, as in *Duquesne* itself, the new methodology results in "stranded" investments.[8]

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[7] Verizon cites *Brooks-Scanlon Co.* v. *RailroadComm'n*, 251 U.S. 396 (1920), for the proposition that, in determining the "total effect" of a methodological decision for purposes of *Duquesne*, regulators must altogether disregard profits "earn[ed] in competitive lines of business." Pet. 17. *Brooks-Scanlon* holds no such thing. The Court there held that the government could not force a company engaged in an *unregulated* "sawmill and lumber business" to conduct, in addition, an unprofitable railroad operation. 251 U.S. at 399. No similar arrangement is at issue here. The "net effects" inquiry mandated by *Duquesne* may, at a minimum, take into account a utility company's overall rate of return with respect to its interrelated *regulated* activities. See, *e.g.*, *Baltimore & Ohio R.R.* v. *United States*, 345 U.S. 146, 148-150 (1953); see also *In re Valuation Proceedings Under Sections 303(c) and 306 of the Reg'l Rail Reorganization Act*, 439 F. Supp. 1351, 1357 n.12 (Spec. Ct. 1977) (Friendly, J.) (noting that modern Takings Clause jurisprudence has superseded the language in *Brooks-Scanlon* upon which petitioners rely).

[8] In *Duquesne*, the Court upheld a state law that "suddenly and selectively" (488 U.S. at 313) foreclosed recovery of a $35 million investment that was prudent when made, even though the "pru-

Second, *Duquesne* does not hold, as petitioners allege (Pet. 15), that a change in methodologies is permissible only if the new methodology produces a constitutionally adequate rate of return "*as measured under the prior system*." See *Duquesne*, 488 U.S. at 312 (stating sufficient, but not necessary, basis for rejecting constitutional claim). And, even if *Duquesne* did so hold, that would not assist petitioners here, because they make no effort to show that the "overall impact" (*ibid.*) of adopting a forward-looking methodology for network elements leaves them with a confiscatory overall return.

In any event, Verizon's argument rests on the false premise that, in implementing the local competition provisions of the 1996 Act, the FCC "abrupt[ly]

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dent investment" methodology in effect at the time of the investment would have provided for such recovery. The takings claim here is even weaker than in *Duquesne*. Although the essentials of the FCC's forward-looking cost methodology have governed the industry for more than four years (see U.S. Pet. 20-21), petitioners make no effort to document any concrete claim of "stranded" investments. Compare Verizon Pet. 8 (alleging "stranding" of investments) with *id.* at 16-17 (declining to make any empirical argument about practical consequences of employing TELRIC). Any such claim would be highly suspect on a variety of legal and factual grounds, as we have explained elsewhere. See U.S. Br. at 38-40 & n.32, *GTE Serv. Corp.* v. *FCC*, cert. dismissed, No. 99-1244 (Nov. 2, 2000); see generally Herbert Hovenkamp, *The Takings Clause and Improvident Regulatory Bargains*, 108 Yale L.J. 801 (1999). In all events, any remedy, if a need for one were established, would be appropriately obtained not through the rates charged for network elements, but through a competitively neutral funding mechanism, as the FCC has explained. See U.S. Pet. App. 95a (FCC "do[es] not completely foreclose the possibility that incumbent LECs will be afforded an opportunity to recover, to some extent, their embedded costs through a mechanism separate from rates for interconnection and unbundled network elements.").

jettison[ed]" the use of "historical costs" (Pet. 15). To begin with, Verizon's argument on this point mixes apples and oranges. The historical cost methodology to which Verizon refers (see *id.* at 5) was generally used by state and federal regulators in setting retail rates and charges for particular services, not in setting rates that new entrants must pay incumbents to lease network elements. Those quite different contexts present quite different issues. And, even in the context of setting retail rates, both the FCC and many state commissions largely abandoned a pure historical cost approach many years ago because of its long-recognized methodological shortcomings. See, *e.g.*, *National Rural Telecom Ass'n* v. *FCC*, 988 F.2d 174, 178 (D.C. Cir. 1993).

Finally, Verizon challenges (Pet. 10) the FCC's pricing rules on policy grounds, claiming that the use of forward-looking costs in this setting will produce "a sort of 'Potemkin village' competition" with a "rapid proliferation" of competitors providing service solely through the use of an incumbent's own facilities. To begin with, the policy concern that petitioners profess is analytically unhinged from the legal claim that they are making here. Congress, not the FCC, made the basic decision to jump-start competition by entitling competitors to enter local markets by leasing certain elements in the incumbent's network rather than duplicating all such elements on their own. See U.S. Pet. 6-7; 47 U.S.C. 251(c)(3) and (d)(2). Even if (as petitioners wrongly suggest) there were some plausible policy justification for slowing competition down or giving new entrants additional incentives to invest *immediately* in their own facilities, it would make little sense to accomplish that objective by forcing new entrants, in the circumstances in which they are entitled to lease elements, to pay whatever amount happens to appear on an incumbent's accounting books. That amount would vary widely and arbitrarily from incumbent to incumbent, and it could be higher or lower than the forward-looking economic costs of the elements at issue. See U.S. Pet. 6-8; see also U.S. Pet. App. 86a-87a. The FCC's decision to reject that approach was eminently reasonable, and it is entitled to substantial deference. See *Iowa Utils. Bd. I*, 525 U.S. at 397.

Verizon's policy concerns are, moreover, refuted by industry developments over the past four years. Since 1996, network element rates have reflected forward-looking cost principles. See U.S. Pet. 20-21. And, both before and after this Court's decision in *Iowa Utilities Board I*, new entrants have been able in many contexts to lease most of the elements necessary to provide service to their customers (as some of them must to develop a customer base sufficient to support further capital investments).[9] That established regulatory regime has not produced a "rapid proliferation" of "Potemkin village" competition. Indeed, in many settings, extensive competition has yet to develop; incumbents still control approximately 94% of total local telecommunications revenues (see *id.* at 2), and much of the existing competition in local markets, particularly in business markets, is provided by carriers that have built or purchased facilities of their own. In addition, new entrants have strong inherent incentives to build

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[9] See generally Third Report and Order, *In re Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, 15 F.C.C.R. 3696 (1999), petitions for review filed *sub nom. United States Telecom Ass'n* v. *FCC*, Nos. 00-1015 and 00-1025.

their own facilities so as to avoid having to deal with and rely on their chief competitors—the incumbent LECs—in order to do business.

We will address those issues in greater detail in our brief on the merits if certiorari is granted. We acknowledge that, as Verizon observes (Pet. 20 n.7), the issue presented in Verizon's petition is closely related to the first issue presented in our petition. For that reason, even though Verizon's claim is substantively unsound, we do not oppose Verizon's petition so long as ours is granted.

2. a. We agree with petitioners AT&T (Pet. 16-21) and GCI (Pet. 7-29) that the Eighth Circuit erred in invalidating the FCC's rules implementing the "exemption," "suspension," and "modification" provisions of Section 251(f) for rural and small LECs.

First, in vacating the FCC's construction of the "undue economic burden" that would enable such carriers to avoid the obligations imposed by Section 251(c), the court of appeals attacked a straw man. The FCC did not, as the Eighth Circuit believed, "eliminat[e]" from the analysis any consideration of the "economic burden that is typically associated with efficient competitive entry." AT&T Pet. App. 29a. Although the FCC determined that such a burden is not, in itself, *sufficient* to satisfy the statutory standard for an exemption, suspension, or modification, the FCC did not suggest that such a burden is *irrelevant* to the analysis. Instead, the FCC provided that a carrier must demonstrate some economic burden "beyond"—*i.e.*, in addition to—an "economic burden that is typically associated with efficient competitive entry." 47 C.F.R. 51.405(c) and (d); see AT&T Pet. App. 193a, 196a-197a.

Because the Eighth Circuit misunderstood that point, it is unclear whether the court meant to invalidate the approach that the FCC actually chose. If the decision below were construed to do so, it could significantly impede the development of local competition in many rural areas, because the introduction of competition inherently imposes an economic burden on a monopolist. See AT&T Pet. 17-19. Granting certiorari to review the Eighth Circuit's invalidation of 47 C.F.R. 51.405, as AT&T and GCI urge, would spare the industry another round of lower-court litigation on that point.[10]

Second, the court of appeals also erred in invalidating the FCC's determination with respect to the burden of proof in proceedings under Section 251(f)(1). As the FCC explained (AT&T Pet. App. 193a-194a), Section 251(f)(1) is most sensibly effectuated by imposing the burden on the LEC resisting the otherwise generally applicable obligations of Section 251(c). Among other considerations, that carrier has control of most of the relevant information. It would make little sense to expect a new entrant to bear the burden of proving, for example, that an incumbent would *not* suffer an "undue economic burden." See generally GCI Pet. 12-18; cf. *NLRB* v. *Transportation Mgmt. Corp.*, 462 U.S. 393, 403 (1983) (upholding agency's reasonable allocation of burden of proof).

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[10] As noted above, the Eighth Circuit invalidated 47 C.F.R. 51.405(c) on the additional ground that the rule, in isolation, could be read to imply that a state commission may disregard "two of the three statutory requirements that must be met before a state commission can terminate an exemption." AT&T Pet. App. 27a. Because (as the Eighth Circuit understood, see *ibid.*) the FCC has clarified that the rule should not be so construed, the Eighth Circuit's ruling on this point has no substantive significance and poses no obstacle to this Court's review of the question presented by AT&T and GCI.

Nothing in Section 251(f)(1) can plausibly be said to point in the *opposite* direction, although the court of appeals erroneously believed otherwise. Indeed, the court held that the "plain meaning of the statute" (AT&T Pet. App. 32a) forecloses the FCC's determination under the first step of the analysis set forth in *Chevron U.S.A. Inc.* v. *NRDC*, 467 U.S. 837, 842-843 (1984). The basis for that holding is obscure. The court appeared to rely on language in Section 251(f)(1)(A) providing that "the requirements of § 251(c) 'shall not apply to a rural telephone company *until*' a request has been made." AT&T Pet. App. 31a (quoting 47 U.S.C. 251(f)(1)(A)); but cf. 47 U.S.C. 251(f)(1)(B) (providing that, within 120 days of filing of request, "the State Commission *shall terminate* the exemption" unless certain showings are made) (emphasis added). But that fact, as well as the court's related point that Section 251(f)(1) addresses proceedings involving termination (rather than grants) of exemptions (AT&T Pet. App. 32a), is logically irrelevant to whether the incumbent should bear the burden of proof in such proceedings once a party challenges the exemption. See AT&T Pet. 20 & n.7. The court's apparent assumption to the contrary, which constitutes the whole of its analysis on the burden-of-proof issue, is plainly wrong.

b. We also agree with petitioners AT&T and WorldCom that the court of appeals erred in invalidating the FCC's rules governing the "wholesale rates" that an incumbent may charge new entrants that seek to purchase its services for resale to subscribers.

Section 252(d)(3) provides that "wholesale rates" for resellers shall be based on retail rates that an incumbent charges to its subscribers, "excluding the portion thereof attributable to any marketing, billing, collection, and other costs that will be avoided by the local exchange carrier." The Eighth Circuit construed Section 252(d)(3) to compel an approach under which the only costs that may be excluded from retail rates are those that "will be avoided *by selling to the competitor the services it requests*." AT&T Pet. App. 18a (emphasis added). The emphasized language, however, does not appear in the 1996 Act. Although the Act speaks of costs that "will be avoided," it contains a critical gap: It does not identify *what*, for statutory purposes, causes costs to be "avoided." The FCC reasonably filled that gap by construing Section 252(d)(3) to encompass the costs that "will be avoided" as the result of treating the incumbent as a wholesaler rather than a retailer by excluding its retail-oriented costs. See AT&T Pet. App. 168a ("[T]he avoided costs are those that an incumbent LEC would no longer incur if it were to cease retail operations and instead provide all of its services through resellers.").

That approach is sensible. If resale is to be a workable means of entry into local telecommunications markets, a reseller cannot be expected to pay—in addition to its *own* retail costs and the incumbent's wholesale costs—a share of the *incumbent's* retail costs as well. See AT&T Pet. 21-24; see also AT&T Pet. App. 168a-170a. But the apparent consequence of the Eighth Circuit's decision is to undermine the competitive position of resellers by requiring them to underwrite a substantial portion of the incumbent's retail costs as well as their own. Moreover, as petitioner WorldCom points out (Pet. 27), the Eighth Circuit's approach gives incumbents artificial inducements to defeat resale-based competition by unreasonably refusing to "avoid[]" costs of services that they provide to new entrants for resale. Unless reversed, therefore, the

Eighth Circuit's holding threatens to read resale out of the 1996 Act as an option for entry into local telecommunications markets.

c. Although we believe that the Eighth Circuit was wrong on the merits in invalidating the FCC's rules concerning exemptions, suspensions, and modifications under Section 251(f) and wholesale rates under Section 252(d)(3), we did not challenge those holdings in our own petition for a writ of certiorari. Our petition is limited to two questions on which, in our view, this Court's review is most urgently needed: the validity of the FCC's cost methodology for determining the rates for network elements and interconnection, and the validity of the "combinations" rules set forth in 47 C.F.R. 51.315(c)-(f). Both of those issues have immense significance for the telecommunications industry. In addition, the first issue presents largely the same methodological dispute as did another case that the Court granted certiorari to review this Term,[11] and the second issue is the subject of an explicit circuit conflict.

The additional questions presented by petitioners in Nos. 00-555, 00-590, and 00-602, although somewhat less important than the questions presented in our petition, are also of considerable importance. The Court could appropriately review those questions as well, and, in our view, it would be particularly constructive for the Court to review the questions related to Section 251(f). We are concerned that, as petitioner GCI observes

[11] On November 2, 2000, this Court granted Verizon's unopposed motion to dismiss *GTE Serv. Corp.* v. *FCC*, No. 99-1244, in which one of Verizon's corporate predecessors (GTE) was the petitioner. See U.S. Pet. 22-25 (discussing similarity of the pricing methodologies at issue in both cases). As we will discuss in the reply brief supporting our own petition in No. 00-587, the dismissal of that case reinforces the need for this Court to grant our petition.

(Pet. 7), the Eighth Circuit's erroneous rulings concerning Section 251(f) could be construed to leave much of "rural and small town America" without the primary benefits of Section 251, a result that Congress plainly did not intend.

CONCLUSION

We do not oppose the petition for certiorari in No. 00-511 so long as the Court grants certiorari with respect to the first question presented in our petition in No. 00-587. We also do not oppose the petitions for certiorari in Nos. 00-555, 00-590, and 00-602.

Respectfully submitted.

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