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AMERICAN ARBITRATION ASSOCIATION
Commercial Arbitration

SATURN TELECOMMUNICATION
SERVICES, INC.,

Claimant,

v.

COVAD COMMUNICATIONS COMPANY,

Respondent.

ARBITRATION
AWARD

This is a dispute between two telecommunications companies, Saturn Telecommunications, Inc. ("STS") and Covad Communications Company ("Covad"), parties to a Broadband Internet Access Services Agreement ("BIA Agreement"). STS claims it was fraudulently induced by Covad to sign the BIA Agreement, the BIA Agreement was breached by Covad and Covad's actions violated the Florida Deceptive and Unfair Trade Practices Act ("FDUTPA"). Covad claims it did not commit fraud or breach the BIA Agreement and the law requires the BIA Agreement be enforced against STS. STS is represented by Alan Gold, Esq. and Covad is represented by Clay Deanhardt, Esq. The parties have agreed to binding arbitration subject to the commercial rules of the American Arbitration Association. Following a 10 day arbitration hearing held September 17 - 28, 2007, and receipt of post hearing briefing, this matter was submitted for decision.

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FACTS

The credibility of the witnesses is a serious issue. The facts and conclusions set forth herein are those supported by the weight of the evidence.

In 2004, STS was a Competitive Local Exchange Carrier ("CLEC") in the business of selling Unbundled Network Element Platform ("UNE-P") to small and medium size businesses. STS was a proud company with a reputation for superior customer service and an outstanding relationship with independent agents who sold its services. BellSouth provided the UNE-P sold by STS. Incumbent Local Exchange Carriers ("ILEC") such as BellSouth were no longer required to provide UNE-P after March 11, 2005, and STS was looking for an alternative to UNE-P, from which STS's imbedded base of customers would be transitioned. STS explored the possibility of a transition to Voice Over Internet Protocol ("VoIP"), using BellSouth internet access and broadband. These discussions began in summer, 2004. STS representatives knew BellSouth had very little experience with VoIP. STS representatives received e-mails from Covad promoting Covad's VoIP solutions. STS learned that Covad, a large California company, had recently acquired GoBeam, a provider of VoIP's solutions to small and medium sized customers. In one e-mail, the president and CEO of Covad stated: "We now have the winning combination of our nationwide broadband network, an award winning, market tested Voice over IP service that accelerates the offering of voice and data communication bundles nationwide."

In August, 2004, Mark Amarant and Keith Kramer, STS's CEO and Vice President, respectively, attended the alternate channels convention, also known as the independent agents' convention, in Chicago. Both STS and Covad had booths at the convention. Amarant and Kramer had read the e-mails from Covad which promoted VoIP and they wanted to see what Covad had to offer. At the

1 convention they met and talked with Tim Gaines, Vice President of Covad
2 and formerly President of GoBeam. Gaines talked about Covad's national
3 network for broadband symmetrical digital subscriber line ("SDSL"), optimized
4 for voice service, and how Covad's nationwide footprint was a perfect fit for
5 any VoIP company. He demonstrated the Sylanthro VoIP platform that was
6 used by Covad. He told them Covad was providing its retail VoIP service over
7 Covad's broadband internet access network. The significance to Amarant and
8 Kramer was that, as Gaines represented, STS would be able to provide VoIP
9 to customers over Covad's SDSL. In the conversations it was understood
10 that STS would be a wholesale partner, that STS wanted to have its own
11 facilities based VoIP platform and that STS was not going to be a reseller.
12 Gaines provided Kramer with a brochure, "VoIP Wholesale Offerings August
13 2004" which stated Covad provided voice access services; optimized voice
14 capabilities over T-1, ADSL and SDSL. Amarant and Kramer were excited.

15 After the convention, STS continued its discussions with BellSouth, but it
16 was primarily interested in pursuing a relationship with Covad. STS purchased
17 the same platform from Sylanthro that Covad had demonstrated at the Chicago
18 convention. Amarant and Kramer and other STS representatives followed
19 up with Covad's sales directors Jeff Rider and Priscilla Rhodes by telephone,
20 conference calls and e-mails. Prior to a December 21, 2004 meeting, Rhodes
21 recommended the Layer 3 (BIA) Agreement. On December 21, 2004 at a face
22 to face meeting at STS headquarters, Amarant and Kramer met with Rider
23 and Rhodes. Engineers from Covad and STS also attended and met together.
24 Amarant gave a power point presentation of what STS wanted to do. Rhodes
25 specifically represented that Covad was an expert in VoIP and that Covad was
26 providing VoIP over its network to small and medium size businesses, the
27 same model STS wanted to pursue as a provider, and that Covad was using its

1 broadband internet services nationwide. STS was referred to as "Covad's wholesale
2 partner". Now that STS had purchased the same Sylanro equipment used by
3 Covad, STS could use Covad's broadband internet services nationwide as well.
4 Rhodes referred to Covad and STS as a perfect fit and Covad's services as carrier
5 grade, a true ILEC replacement.

6 The BIA Agreement was signed on behalf of the parties on January 21, 2005.
7 Internal e-mails, engineering documents and other evidence demonstrate that at
8 that time, Rider, Rhodes and other Covad representatives, as well as Barry Bonso-
9 Bruce in Covad's engineering department, knew the access products purchased
10 under the BIA Agreement would not support STS's VoIP services with SDSL,
11 fractional T-1s or full T-1s, and serious problems and issues would occur. Covad's
12 internet access network was a single PVC network which was insufficient to conduct
13 the voice traffic STS required. Dual pipe PVC was necessary in order for VoIP to
14 work without jitter and packet loss. Covad was in the process of developing VOA
15 which was necessary for VoIP services, but it was not due for testing until June,
16 2005. STS's officers and representatives relied on Covad's representations and they
17 would not have entered into the BIA Agreement if they had known the truth.

18 What followed for STS was a business nightmare of major proportions.
19 STS prepared for the March, 2005 launch of its VoIP services and was highly
20 successful in its sales effort, but once installed, the services did not work. Covad
21 recommended STS switch its customers to fractional T-1s; they did so, but the
22 services did not work. Covad recommended STS switch its customers to full
23 T-1s; they did so, but the services did not work. It was only later that Covad
24 recommended VOA, its untested "Voice Optimized Access" product, which was not
25 yet fully developed and tested, and even that didn't work. STS continued to sell
26 the VOA service based on Covad's promise it would work. By then, STS was weary
27 of Covad's promises. STS had lost many customers and those remaining were

1 irate. STS had also lost the confidence and support of the agents who sold
2 its services. STS knew now what Covad representatives had known from the
3 beginning. Covad's network was not as represented and the access products
4 sold to STS would not work.

5 STS decided to switch its VoIP services from Covad to BellSouth with the
6 use of a special access ring, the alternative STS was considering in late 2004,
7 before the BIA Agreement was signed. The transition took approximately 120
8 days and was completed in December, 2005. Since STS made the transition to
9 BellSouth, BellSouth's internet access and broadband has successfully carried
10 and supported STS's VoIP services.

11 Covad's misrepresentations and nondisclosures have caused STS
12 significant and sustained financial harm, including lost revenue and profits, out
13 of pocket and mitigation losses.

14 ISSUES

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16 STS claims it was fraudulently induced to sign the BIA Agreement, Covad
17 breached the BIA Agreement and Covad violated Florida's unfair trade practices
18 statutes. In response, Covad contends that (1) none of STS's claims have
19 merit, (2) Covad made no misrepresentation, (3) STS could have terminated
20 services at any time, (4) the problems encountered by STS and its customers
21 were related to the failure of STS to adequately test STS's products, and to
22 factors unrelated to Covad's services and (5) STS has failed to prove Covad
23 was the proximate cause of any damages it claims and STS did not mitigate its
24 damages.

25 DECISION

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27 The elements of fraud are (a) a misrepresentation (false representation,

1 concealment, or non-disclosure); (b) scienter or knowledge of its falsity; (c) intent
2 to induce reliance; (d) justifiable reliance; and (e) resulting damage.

3 The testamentary and documentary evidence demonstrates Covad
4 fraudulently induced STS to sign the BIA Agreement by misrepresenting material
5 facts and by concealing and failing to disclose material facts. Gaines, Rider and
6 Rhodes represented that Covad's National Network for SDSL was optimized for
7 VoIP, that Covad was using its internet access network to provide VoIP services
8 and that STS would be able to successfully provide its VoIP services over the
9 same network. These representations were false and the evidence demonstrates
10 Covad's sales and engineering personnel knew they were false. They knew the
11 access products provided under the BIA Agreement would not support STS's effort
12 to provide VoIP services when the agreement was signed and when Covad later
13 recommended the T-1s and VOA as a solution. The representations were made
14 to induce STS to sign the BIA Agreement and STS's reliance was reasonable and
15 justified.

16 An important question addressed by the evidence and arguments of counsel
17 is why a large and successful company like Covad would risk its reputation by
18 defrauding a small and relatively insignificant company like STS. In his testimony,
19 Mark Amarant, STS's CEO, gave his answer:

20 Because you (Covad) needed us. You needed our company in order to
21 show that this was your ILEC replacement service. And, instead, you gambled
22 with us. You misguided us. You defrauded us and you used us as a guinea Pig
23 and a lab rat to get all the other ILEC replacement CLECS out there who were
vulnerable at the time.

24 This may be an overstatement, but it has a ring of truth. The evidence
25 demonstrates that Covad had high expectations for VOA, a product under
26 development. If successfully developed, there were thousands of UNE-P
27 providers like STS, looking for an alternative. The potential was enormous. The

1 misrepresentations made by Gaines, Rider and Rhodes were more than
2 reckless. The evidence shows they were intentionally false and motivated by an
3 opportunity of greater significance than just the financial relationship between
4 Covad and STS.

5 The evidence fails to support Covad's claim that problems experienced
6 by STS in the use of Covad's access products were the result of inadequate
7 testing or any factors other than those inherent in the limitations of the access
8 products sold by Covad to STS under the BIA Agreement. This was clearly
9 demonstrated when STS was later able to transition to the use of the BellSouth
10 network without any significant problems.

11 The evidence shows Covad's fraudulent conduct was the proximate cause
12 of damage to STS. On its fraud in the inducement claim, STS seeks to recover
13 compensatory damages for lost revenue and profits for a two year period
14 from June, 2005, through June, 2007, and out-of-pocket losses and mitigation
15 damages. Despite Covad's claim to the contrary, STS has shown with reliable
16 and convincing evidence it lost substantial revenue and profits as a result of
17 STS's inability to deliver the VoIP services promised to its customers. There
18 was no failure to mitigate damages. STS learned in July, 2005, that Covad's
19 access products would not work. It was reasonable for STS to temporarily rely
20 on promises from Covad's representatives that its VOA would eventually work.
21 The evidence shows STS found itself between a rock and a hard place. STS
22 knew a transition to BellSouth could take as much as 120 days, a risk that even
23 greater losses would occur. Considering the circumstances, STS engaged in a
24 reasonable and timely effort to mitigate its damages.

25 STS submitted its calculations of lost revenue and profits for June, 2005
26 to June, 2007. This evidence is reliable, conservative and compelling. STS also
27 submitted calculations based on the assumption of 12% annual growth. This

1 assumption, considering the entire evidence, is speculative and uncertain. STS also
2 seeks to recover its out of pocket losses. These same expenses were included in
3 the 33% cost of service in the determination of lost profits. To include these out of
4 pocket losses as damages would constitute double recovery. STS is entitled to lost
5 revenue and profits from June, 2005 to June, 2007, without assumption for growth,
6 an amount of \$6,087,598.50, and mitigation damages of \$958,644.93. The total
7 damages are \$7,046,243.43.

8 STS requests punitive damages. The evidence that Covad fraudulently
9 induced STS to sign the BIA Agreement is clear and convincing. Therefore, punitive
10 damages are authorized in these circumstances and within the discretion of the
11 Arbitrator. Despite a showing of fraud, the evidence fails to demonstrate a level of
12 conspiratorial and despicable behavior which would justify the need for punitive
13 damages.

14 As for the breach of contract claim, STS has failed to show Covad breached
15 any of the specific terms of the BIA Agreement. As for the FDUTPA claim, STS has
16 failed to show the choice of law, as a separate element of the parties consideration,
17 was the product of Covad's fraud. California law applies to this dispute and does not
18 recognize claims under FDUTPA.

19 AWARD

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21 STS is awarded \$7,046,243.43, and as the prevailing party, attorney fees in
22 the amount of \$233,402.50 and costs in the amount of \$20,363.83.

23 In addition, the administrative filing and case service fees of the AAA,
24 totaling \$11,250.00, shall be borne as follows: entirely by Covad. The other
25 administrative fees of the AAA, totaling \$2,000.00, shall be borne as follows:
26 entirely by Covad. The fees and expenses of the arbitrator, totaling \$51,001.06,
27 shall be borne as follows: entirely by Covad. Therefore, Covad shall reimburse STS

1 the sum of \$37,750.53, representing that portion of said fees and expenses in
2 excess of the apportioned costs previously incurred by STS.

3 This Award is intended to finally resolve all issues raised by the parties in the
4 claims, briefs and arguments. The arbitrator has given appropriate weight to the
5 testimony as elicited. Any claims, motions or defenses not specifically ruled on, are
6 denied.

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11 Dated: December 5, 2007



Hon. Chris Cottle, Ret.
Arbitrator