Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Developing a Unified Intercarrier Compensation Regime	)	CC Docket No. 01-92
	)	
	)	

FURTHER NOTICE OF PROPOSED RULEMAKING

Adopted: February 10, 2005 **Released: March 3, 2005**

Comment Date: 60 days after publication in the Federal Register
Reply Comment Date: 90 days after publication in the Federal Register

By the Commission: Chairman Powell, Commissioners Abernathy, Copps, and Adelstein issuing separate statements.

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I. INTRODUCTION

1. With this Further Notice of Proposed Rulemaking (Further Notice), we begin the process of replacing the myriad existing intercarrier compensation regimes with a unified regime designed for a market characterized by increasing competition and new technologies.[1] In the *Intercarrier Compensation NPRM*, the Commission acknowledged a number of problems with the current intercarrier compensation regimes (access charges and reciprocal compensation) and expressed interest in identifying a unified approach to intercarrier compensation.[2] The Commission solicited comment on a bill-and-keep approach to reciprocal compensation payments governed by section 251(b)(5) of the Act.[3] The Commission also sought comment on alternative reform measures that would build upon the current requirements for cost-based intercarrier payments.[4]

2. In response to the *Intercarrier Compensation NPRM*, the Commission received extensive comment from individual carriers and economists, industry groups and associations, consumer advocates, and state regulatory commissions, among others.[5] The Commission also received numerous *ex parte* filings and considered detailed presentations from interested parties. In addition to the record developed in response to the *Intercarrier Compensation NPRM*, various industry groups and interested parties recently submitted comprehensive reform proposals and principles for consideration by the Commission in this proceeding.[6]

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[1]This examination was initiated in April 2001 by a Notice of Proposed Rulemaking. *See Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, Notice of Proposed Rulemaking, 16 FCC Rcd 9610 (2001) (*Intercarrier Compensation NPRM*).

[2]*Id.* at 9612, para. 2. As the Commission explained in the *Intercarrier Compensation NPRM*, the existing intercarrier compensation rules may be categorized as follows: access charge rules, which govern the payments that interexchange carriers (IXCs) and Commercial Mobile Radio Service (CMRS) providers make to local exchange carriers (LECs) to originate and terminate long-distance calls; and reciprocal compensation rules, which, generally speaking, govern the compensation between telecommunications carriers for the transport and termination of "local" traffic. *Id.* at 9613, para. 6. Nevertheless, both sets of rules are subject to various exceptions, such as the enhanced service provider (ESP) exemption from the payment of access charges. *Id.*

[3]*Id*. at 9612-13, para. 4.

[4]*Id.*

[5]A complete list of comments and reply comments filed in response to the *Intercarrier Compensation NPRM* can be found in Appendix A. The Commission received 75 comments and 62 reply comments. *See* Appendix A.

[6]*See infra* Section II.C.

3. As a general matter, the record confirms the need to replace the existing patchwork of intercarrier compensation rules with a unified approach. Many commenters observe that the current rules make distinctions based on artificial regulatory classifications that cannot be sustained in today's telecommunications marketplace.[7] Under the current rules, the rate for intercarrier compensation depends on three factors: (1) the type of traffic at issue; (2) the types of carriers involved; and (3) the end points of the communication.[8] These distinctions create both opportunities for regulatory arbitrage and incentives for inefficient investment and deployment decisions. The record in this proceeding makes clear that a regulatory scheme based on these distinctions is increasingly unworkable in the current environment and creates distortions in the marketplace at the expense of healthy competition. Additional problems with the existing intercarrier compensation regimes result from changes in the way network costs are incurred today and how market developments affect carrier incentives. These developments and others discussed herein confirm the urgent need to reform the current intercarrier compensation rules.

4. Since the Commission adopted the *Intercarrier Compensation NPRM* acknowledging the need for reform, several industry groups have developed proposals for comprehensive reform of existing intercarrier compensation regimes and submitted those proposals to the Commission. In this *Further Notice*, we solicit comment on these proposals, including the legal and economic bases for these proposals, as well as the end-user effects and universal service issues implicated by them. We also ask parties to comment on whether and how these reform proposals would affect network interconnection and seek comment on the implementation issues associated with any reform measures. In addition to the comprehensive reform proposals submitted in the record, we seek comment on alternative reform measures, including changes to the existing intercarrier compensation regimes and cost standards. Finally, we seek comment on issues relating to the regulation of transit services and additional CMRS compensation issues.

II. FURTHER NOTICE OF PROPOSED RULEMAKING

A. The Need For Reform

1. Introduction

5. As the Commission explained in the *Intercarrier Compensation NPRM*, interconnection arrangements between carriers are currently governed by a complex system of intercarrier compensation mechanisms that distinguish among different types of carriers and different types of services based on regulatory classifications.[9] Federal and state access charge rules govern the payments that interexchange carriers (IXCs) and commercial mobile radio service (CMRS) providers make to local exchange carriers (LECs) that originate and terminate long-distance calls, while the reciprocal compensation rules established under section 251(b)(5) of the Act generally govern the compensation between

[7] *See, e.g.,* Allegiance Comments at 7, 11-12; ALLTEL Comments at 6-7; Cable & Wireless Comments at 8; CompTel Comments at 8; Global NAPs Comments at 7; AT&T Reply at 1, 5-6.

[8] For instance, a long-distance call carried by an IXC is subject to a different regime than a local call carried by two LECs. Moreover, CMRS providers and LECs are subject to different intercarrier compensation rules, and ISP-bound calls are subject to yet another regime.

[9] *Intercarrier Compensation NPRM*, 16 FCC Rcd at 9613, para. 5.

telecommunications carriers for the transport and termination of calls not subject to access charges.[10] These rules apply different cost methodologies to similar services based on traditional regulatory distinctions that may have no bearing on the cost of providing service and many of which are increasingly difficult to maintain. In this section, we briefly describe the existing intercarrier compensation mechanisms and then explain why these mechanisms are difficult to sustain in the current marketplace.

a. Access Charges

6. Prior to the AT&T divestiture in 1984, most telephone subscribers obtained local services from the Bell Operating Companies (BOCs) and long-distance services from AT&T Long Lines, both of which were owned and operated by AT&T.[11] In preparation for divestiture, the Commission in 1983 established a formal system of tariffed access charges.[12] These rules apportioned charges for common line costs between a monthly flat-rated subscriber line charge (SLC) assessed on end users and a per-minute carrier common line (CCL) charge assessed on the IXCs, which ultimately was recovered from end users through long-distance charges.[13] The SLC for residential users was capped at $3.50 and any remaining common line costs were recovered through the CCL charge.[14] Switching costs were recovered through per-minute charges assessed on IXCs.[15] The Commission required that these access charges be

[10] *See* 47 C.F.R. § 51.701. Intrastate access charges, and intrastate calling generally, are governed by state public utility commissions. Thus, different intercarrier compensation regimes apply to a call originating in New York City depending on, for example, whether it terminates in New York City, elsewhere in the state of New York, or in another state. Different rules also apply depending on whether the calling and called parties are using wireline or wireless services.

[11] *MTS and WATS Market Structure*, CC Docket No. 78-72, Third Report and Order, Phase 1, 93 FCC 2d 241 (*1983 Access Charge Order*), *recon., MTS and WATS Market Structure*, CC Docket No. 78-72, Memorandum Opinion and Order, 97 FCC 2d 682 (1983) (*First Reconsideration of 1983 Access Charge Order*), *second recon., MTS and WATS Market Structure*, CC Docket No. 78-72, Memorandum Opinion and Order, 97 FCC 2d 834 (1984) (*Second Reconsideration of 1983 Access Charge Order)*.

[12] *1983 Access Charge Order*, 93 FCC 2d at 245-54, paras. 9-35.

[13] Although the access charge regime adopted in 1983 and contained in the Commission's Part 69 access charge rules includes charges that LECs impose on their subscribers, in this item we generally use the term "access charges" to mean charges imposed by a LEC on another carrier.

[14] *Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charges*, CC Docket Nos. 96-262, 94-1, 91-213, 95-72, First Report and Order, 12 FCC Rcd 15982, 15999, para. 37 (1997) (*Access Charge Reform Order*) (subsequent history omitted). The Commission emphasized that its long range goal was for LECs to recover a large share of their non-traffic sensitive common line costs on a flat-rated basis from end users instead of from carriers. *1983 Access Charge Order*, 93 FCC 2d at 264-65. The Commission found that a subscriber who does not use the subscriber line to place or receive interstate calls imposes the same non-traffic sensitive costs as a subscriber who does use the line. Thus, simply by requesting telephone service, the subscriber causes the carrier to incur local loop costs whether he or she uses the service for intrastate or interstate calls or not at all. *Id.* at 278. Initially, the residential SLC was capped at $1.00. The cap was raised to $3.50 on April 1, 1989. *See Federal Communications Commission Releases Study on Telephone Trends*, Industry Analysis and Technology Division, Wireline Competition Bureau, at Tab 1.1 (rel. May 6, 2004) (*Telephone Trends Report*).

[15] *Access Charge Reform Order*, 12 FCC Rcd at 16006, para. 61.

calculated based on the average embedded cost of providing such services.[16]

7. At that time, the Commission acknowledged that enhanced service providers (ESPs) were among a variety of users of LEC interstate access services.[17] Since 1983, however, the Commission has exempted ESPs, now known as information service providers (ISPs), including those that provide service related to the Internet, from the payment of certain interstate access charges.[18] Rather, ISPs are treated as end users for the purpose of applying access charges and are entitled to pay local business rates for their connections to LEC central offices.[19]

8. In the 1996 Act, Congress sought to foster competition in the local telephone market, while at the same time ensuring the continued provision of affordable service to all Americans.[20] Following its passage, the Commission commenced reform of both interstate access charges and federal universal service support mechanisms in accordance with directives of the Act. In its 1997 *Access*

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[16]*See generally 1983 Access Charge Order*, 93 FCC 2d at 241; *First Reconsideration of 1983 Access Charge Order,* 97 FCC 2d at 682; *Second Reconsideration of 1983 Access Charge Order*, 97 FCC 2d at 834.

[17]*First Reconsideration of 1983 Access Charge Order*, 97 FCC 2d at 711 (ESPs are "[a]mong the variety of users of access service" and "obtain[ ] local exchange services or facilities which are used, in part or in whole, for the purpose of completing interstate calls which transit [their] location and, commonly, another location."). The Commission defines "enhanced services" as "services, offered over common carrier transmission facilities used in interstate communications, which employ computer processing applications that act on the format, content, code, protocol or similar aspects of the subscriber's transmitted information; provide the subscriber additional, different, or restructured information; or involve subscriber interaction with stored information." 47 C.F.R. § 64.702(a). The 1996 Act describes these services as "information services." *See* 47 U.S.C. § 153(20) ("information service" refers to the "offering of a capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information via telecommunications."). *See also Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report to Congress, 13 FCC Rcd 11501, 11516 (1998) (*Universal Service Report to Congress*) (the "1996 Act's definitions of telecommunications service and information service essentially correspond to the pre-existing categories of basic and enhanced services").

[18]This policy, known as the "ESP exemption," has been reviewed by the Commission on a number of occasions and retained each time. *See First Reconsideration of 1983 Access Charge Order*, 97 FCC 2d at 715 (ESPs have been paying local business service rates for their interstate access and would experience rate shock that could affect their viability if full access charges were instead applied); *see also Amendments of Part 69 of the Commission's Rules Relating to Enhanced Service Providers*, CC Docket 87-215, Order, 3 FCC Rcd 2631, 2633 (1988) (*ESP Exemption Order*) ("the imposition of access charges at this time is not appropriate and could cause such disruption in this industry segment that provision of enhanced services to the public might be impaired"); *Access Charge Reform Order*, 12 FCC Rcd at 16133-35, paras. 344-48 ("[m]aintaining the existing pricing structure … avoids disrupting the still-evolving information services industry").

[19]*ESP Exemption Order*, 3 FCC Rcd at 2635 n.8, 2637 n.53. *See also Access Charge Reform Order*, 12 FCC Rcd at 16133-35, paras. 344-48.

[20]47 U.S.C. §§ 217, 254. Traditionally, rates for local telephone service in rural and high cost areas had been implicitly subsidized by charging high-volume long-distance callers and urban residents artificially higher rates. The 1996 Act recognized, however, that these implicit subsidies could not continue in a competitive marketplace and directed the Commission to create explicit universal service support mechanisms that are specific, predictable and sufficient. *See* 47 U.S.C. § 254(e); *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report and Order, 12 FCC Rcd 8776, 9164-65 (1997) (*Universal Service First Report and Order*) (subsequent history omitted).

Charge Reform Order, the Commission reformed the manner in which price cap LECs recover access costs by aligning the rate structure more closely with the manner in which costs are incurred.[21] Accordingly, the Commission began phasing out per-minute charges for loop and other non-traffic sensitive costs, and providing for recovery of such costs through flat monthly charges.[22]

9. The *CALLS Order* continued the process of access charge and universal service reform for these carriers through a more straightforward, economically rational common line rate structure.[23] These reforms advanced the goals of requiring price cap LECs to recover their non-traffic sensitive common line costs from end users, instead of carriers, and of recovering these costs on a flat-rated, rather than a per-minute, basis.[24] In addition, the Commission approved an immediate $2.1 billion reduction in per-minute switched access charges, which the CALLS interexchange carrier members committed to pass through to their customers.[25] To offset these reductions in per-minute switched access charges, the Commission established a new explicit, portable universal service support mechanism, targeted at $650 million per year for five years.[26]

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[21] *See Access Charge Reform Order*, 12 FCC Rcd at 16007-33, paras. 67-120. In particular, the Commission decided that loop costs should be recovered entirely through flat rates rather than per-minute rates. *Id*. at 16004, para. 54.

[22] *Id.* at 15998, para. 35. In order to reduce per-minute CCL charges, the Commission created the presubscribed interexchange carrier charge (PICC), a flat, monthly charge imposed on IXCs on a per-line basis. *Id*. at 15998-16000, paras. 37-40. The Commission also shifted the cost of line ports from per-minute local switching charges to the common line category and established a mechanism to phase out the per-minute Transport Interconnection Charge (TIC). *Id*. at 16035-40, 16073-86, paras. 125-34, 210-43. Line ports connect subscriber lines to the switch in the LEC central office. *See id.* at 16034-35, para. 123.

[23] *See Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers*, CC Docket Nos. 96-262 and 94-1, Sixth Report and Order, *Low-Volume Long Distance Users*, CC Docket No. 99-249, Report and Order, *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Eleventh Report and Order, 15 FCC Rcd 12962, 12991-93, paras. 76-79 (2000) (increasing SLC caps and phasing out the residential and single-line business PICC) (*CALLS Order*), *aff'd in part, rev'd in part, and remanded in part*, *Texas Office of Public Util. Counsel et al. v. FCC*, 265 F.3d 313 (5th Cir. 2001), *cert. denied*, *National Association of State Utility Consumer Advocates v. FCC*, 535 U.S. 986 (2002); *on remand*, *Access Charge Reform; Price Cap Performance Review for LECs; Low-Volume Long Distance Users; Federal-State Joint Board on Universal Service*, CC Docket Nos. 96-262, 94-1, 99-249 and 96-45, Order on Remand, 18 FCC Rcd 14976 (2003) (*CALLS Order on Remand*). To compensate for the loss of revenues from the elimination of the PICC, the Commission raised the SLC cap for primary residential and single-line business lines from $3.50 to $6.50 over a period of several years. *See CALLS Order*, 15 FCC Rcd at 12974-5, 12991-93, 13004-7, paras. 30, 76-79, 105-112. As promised in the *CALLS Order*, the Commission reviewed the network costs of price cap carriers and determined that the SLC increases should proceed as scheduled. *Cost Review Proceeding for Residential and Single-Line Business Subscriber Line Charge (SLC) Caps; Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers*, CC Docket Nos. 96-262 and 94-1, Order, 17 FCC Rcd 10868 (2002), *aff'd Nat'l Ass'n of State Util. Consumer Advocates v. FCC*, 372 F.3d 454 (D.C. Cir. 2004).

[24] *See 1983 Access Charge Order*, 93 FCC 2d at 264-65, 278; *see also Access Charge Reform Order*, 12 FCC Rcd at 16007, para. 67.

[25] *CALLS Order*, 15 FCC Rcd at 13025, paras. 151-52.

[26] *Id.* at 13039, paras. 185-86.

10. In the *MAG Order*, the Commission reformed the interstate access charge and universal service support system for incumbent LECs subject to rate-of-return regulation.[27] As with the *CALLS Order*, these reforms were designed to rationalize the interstate access rate structure by aligning it more closely with the manner in which costs are incurred. The *MAG Order* increased the SLC caps for rate-of-return carriers to the levels established for price cap carriers[28] and eliminated the CCL charge from the common line rate structure as of July 1, 2003, when SLC caps reached their maximum levels.[29]

11. In addition, a new universal service support mechanism, Interstate Common Line Support (ICLS), was implemented to replace the CCL charge beginning July 1, 2002.[30] This mechanism recovers any shortfall between the allowed common line revenue requirement of rate-of-return carriers and their SLC and other end-user revenues, thereby ensuring that changes in the rate structure did not affect the overall recovery of interstate access costs by rate-of-return carriers serving high-cost areas.[31] To reform the local switching and transport rate structure of rate-of-return carriers, the Commission shifted the non-traffic sensitive costs of local switch line ports to the common line category, and reallocated the remaining costs contained in the Transport Interconnection Charge (TIC) to other access rate elements, thus reducing per-minute switched access charges.[32]

b. Reciprocal Compensation

12. Reciprocal compensation for the transport and termination of telecommunications traffic

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[27] *Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, CC Docket No. 00-256, Second Report and Order and Further Notice of Proposed Rulemaking, *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Fifteenth Report and Order, *Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation*, CC Docket No. 98-77, Report and Order, *Prescribing the Authorized Rate of Return From Interstate Services of Local Exchange Carriers*, CC Docket No. 98-166, Report and Order, 16 FCC Rcd 19613 (2001) (*MAG Order*), *recon. in part, Multi-Association Group (MAG) Plan for Regulation of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, CC Docket No. 00-256, First Order on Reconsideration, *Federal-State Joint Board on Universal Service*, CC Docket 96-45, Twenty-Fourth Order on Reconsideration, 17 FCC Rcd 5635 (2002), *amended on recon., Multi-Association Group (MAG) Plan for Regulation of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, CC Docket No. 00-256, *Federal-State Joint Board on Universal Service*, CC Docket 96-45, Third Order on Reconsideration, 18 FCC Rcd 10284 (2003). *See also Multi-Association Group (MAG) Plan for Regulation of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, CC Docket No. 00-256, *Federal-State Joint Board on Universal Service*, CC Docket 96-45, Report and Order and Second Further Notice of Proposed Rulemaking, 19 FCC Rcd 4122 (2004).

[28] *MAG Order*, 16 FCC Rcd at 19621, para. 15. The *MAG Order* increased the residential and single-line business SLC cap to $5.00 on January 1, 2002, to $6.00 on July 1, 2002, and to $6.50 on July 1, 2003. The multi-line business SLC cap increased to $9.20 on January 1, 2002. *Id.* at 19634, 19638, paras. 42, 51.

[29] *Id*. at 19642, para. 61.

[30] *Id*.

[31] *Id*. at 19642, 19667-73, paras. 61, 128-41.

[32] *Id.* at 19649-61, paras. 76-111.

is governed by sections 251(b)(5) and 252(d)(2) of the Act.[33] Section 251(b)(5) generally governs the compensation between telecommunications carriers for the transport and termination of calls not subject to access charges.[34] Section 252(d)(2)(A) states that, for the purpose of incumbent LEC compliance with section 251(b)(5), a state commission shall not consider the terms and conditions for reciprocal compensation to be just and reasonable unless such terms and conditions: (i) provide for the "mutual and reciprocal recovery by each carrier of costs associated with the transport and termination on each carrier's network facilities of calls that originate on the network facilities of the other carrier;" and (ii) "determine such costs on the basis of a reasonable approximation of the additional costs of terminating such calls."[35]

13. Current Commission rules require the calling party's LEC to compensate the called party's LEC for the additional costs associated with transporting a call subject to section 251(b)(5) from the carriers' interconnection point to the called party's end office, and for the additional costs of terminating the call to the called party.[36] The rules further require that the charges for both transport and termination must be set at forward-looking economic cost.[37] The Commission concluded that the "additional cost" standard of section 252(d)(2) permits the use of the same Total Element Long Run Incremental Cost (TELRIC) standard that it established for interconnection and unbundled elements.[38] The TELRIC cost standard establishes prices based on the average cost of providing a particular

[33]Section 251(b)(5) imposes on all LECs a "duty to establish reciprocal compensation arrangements for the transport and termination of telecommunications." 47 U.S.C. § 251(b)(5).

[34]*See* 47 C.F.R. § 51.701.

[35]47 U.S.C. § 252(d)(2)(A). Section 252(d)(2)(B) further provides that the language in section 252(d)(2)(A) shall not be construed "to preclude arrangements that afford the mutual recovery of costs through the offsetting of reciprocal obligations, including arrangements that waive mutual recovery (such as bill-and-keep arrangements)" or to authorize the Commission or any state to "engage in any rate regulation proceeding to establish with particularity the additional costs of transporting or terminating calls, or to require carriers to maintain records with respect to the additional costs of such calls." 47 U.S.C. § 252(d)(2)(B)(i)-(ii).

[36]47 U.S.C. § 252(d)(2)(A); 47 C.F.R. § 51.701. *See also Implementation of the Local Competition Provisions in the Telecommunications Act of 1996 and Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers*, CC Docket Nos. 96-98 and 95-185, First Report and Order, 11 FCC Rcd 15499, 16024-25, paras. 1056-59 (1996) (subsequent history omitted) (*Local Competition First Report and Order*). Section 51.701(c) of our rules defines transport as "the transmission and any necessary tandem switching of telecommunications traffic subject to section 251(b)(5) of the Act from the interconnection point between the two carriers to the terminating carrier's end office switch that directly serves the called party, or equivalent facility provided by a carrier other than an incumbent LEC." 47 C.F.R. § 51.701(c). Section 51.701(d) of our rules defines termination as "the switching of telecommunications traffic at the terminating carrier's end office switch, or equivalent facility, and delivery of such traffic to the called party's premises." 47 C.F.R. § 51.701(d). In the *Local Competition First Report and Order*, the Commission also concluded that "the new transport and termination rules should be applied to LECs and CMRS providers." *Local Competition First Report and Order*, 11 FCC Rcd at 16016-17, para. 1043.

[37]47 C.F.R. § 51.705. *See also Local Competition First Report and Order*, 11 FCC Rcd at 16054-58, paras. 1111-18.

[38]*Local Competition First Report and Order*, 11 FCC Rcd at 16023, para. 1054.

function.[39]

14. In the *Local Competition First Report and Order*, the Commission identified the wireline network costs that are recoverable through reciprocal compensation rates.[40] Specifically, the Commission concluded that "[f]or the purposes of setting rates under section 252(d)(2), only that portion of the forward-looking, economic cost of the LEC's end-office switching that [is] usage sensitive constitutes an 'additional cost' to be recovered through termination charges."[41] The Commission also concluded that the "additional costs" incurred when terminating a call were likely to be greater when termination involved the use of an incumbent LEC's tandem switch.[42] The Commission found that the higher rate for tandem switching would be available to carriers other than incumbent LECs if those carriers utilize a switch that serves a geographic area comparable to that served by the incumbent LEC's tandem switch.[43] In the *CMRS Termination Compensation Order*, the Commission affirmed that a carrier is entitled to the tandem interconnection rate under section 51.711(a)(3) of the Commission's rules if it can satisfy a comparable geographic area test and need not also satisfy a functional equivalency test.[44]

2. The Current Intercarrier Compensation Regimes Cannot Be Sustained in the Developing Marketplace

a. Introduction

[39] *See Review of the Commission's Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Service by Incumbent Local Exchange Carriers*, WC Docket No. 03-173, Notice of Proposed Rulemaking, 18 FCC Rcd 18945, 18953, para. 18 (2003), Erratum, 18 FCC Rcd 20265 (2003) ("*TELRIC NPRM*").

[40] *Local Competition First Report and Order*, 11 FCC Rcd at 16024-25, para. 1057. In the *Local Competition First Report and Order*, the Commission permitted carriers to receive compensation only for "the traffic-sensitive components of local switching," and not for local loop costs, which it concluded were not considered traffic-sensitive. *Id*.

[41] *Id.* By contrast, the Commission did not address at that time the traffic sensitive costs of wireless network components that are appropriately recovered through reciprocal compensation rates. The Commission recently clarified the application of these rules to CMRS providers, however. *See* Letter from Thomas J. Sugrue, Chief, Wireless Telecommunications Bureau, and Dorothy T. Attwood, Chief, Common Carrier Bureau, to Charles McKee, Senior Attorney, Sprint PCS, CC Docket Nos. 95-185 and 96-98, and WT Docket No. 97-207, 16 FCC Rcd 9597 (2001) ("Joint Letter"), *affirmed, Cost-Based Terminating Compensation for CMRS Providers, Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, Calling Party Pays Service Offering in the Commercial Mobile Radio Services*, CC Docket Nos. 95-185 and 96-98, and WT Docket No. 97-207, Order, 18 FCC Rcd 18441 (2003) ("*CMRS Termination Compensation Order"*), *appeal filed, SBC Communications v. FCC,* Case No. 03-4311 (3d Cir. filed Nov. 3, 2003). It determined that a CMRS carrier is entitled to receive reciprocal compensation for the additional costs of terminating traffic on its network at a rate exceeding the incumbent LEC rate if it can demonstrate that its termination costs exceed those of the incumbent LEC and that those costs are traffic-sensitive. *CMRS Termination Compensation Order*, 18 FCC Rcd at 18445, paras. 8-9; Joint Letter, 16 FCC Rcd at 9598.

[42] *Local Competition First Report and Order*, 11 FCC Rcd at 16042, para. 1090.

[43] *Id.*

[44] *CMRS Termination Compensation Order*, 18 FCC Rcd at 18447-49, paras. 17-21; Joint Letter, 16 FCC Rcd at 9599 (citing *Intercarrier Compensation NPRM*, 16 FCC Rcd at 9648, para. 105).

15. The record in this proceeding shows that the three basic principles underlying our existing intercarrier compensation regimes must be re-examined in light of significant market developments since the adoption of the access charge and reciprocal compensation rules. First, our existing compensation regimes are based on jurisdictional and regulatory distinctions that are not tied to economic or technical differences between services. As the Commission observed in the *Intercarrier Compensation NPRM*, regulatory arbitrage arises from different rates that different types of providers must pay for essentially the same functions.[45] Our current classifications require carriers to treat identical uses of the network differently, even though such disparate treatment usually has no economic or technical basis.[46] These artificial distinctions distort the telecommunications markets at the expense of healthy competition.[47] Moreover, the availability of bundled service offerings and novel services blur the traditional industry and regulatory distinctions that serve as the foundation of the current rules.[48]

16. Second, our existing compensation regimes are predicated on the recovery of average costs on a per-minute basis. Under average cost pricing, a network can invest in facilities to attract subscribers and recover a share of those costs from subscribers choosing competing networks. As competition has increased, the ability to shift costs to competitors through intercarrier charges increasingly distorts the competitive process. In addition, advancements in telecommunications infrastructure affect the way carrier costs are incurred and call into question the use of per-minute pricing.

17. Third, under the existing regimes, the calling party's carrier, whether LEC, IXC, or CMRS provider, compensates the called party's carrier for terminating the call.[49] Thus, as a general matter, our existing regimes are based on a "calling-party-network-pays" (CPNP) approach to compensation. Developments in the ability of consumers to manage their own telecommunications services undermine the premise that the calling party is the sole cost causer and should be responsible for all the costs of a call. As discussed below, we find that all these developments compel the Commission to move toward a new, unified intercarrier compensation regime that is better suited to a market characterized by competition among multiple types of carriers and technologies.

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[45] *Intercarrier Compensation NPRM*, 16 FCC Rcd at 9616, para. 12.

[46] *See, e.g.*, AOL Comments at 2-3; Global NAPs Comments at 7; Level 3 Comments at 25-26. For instance, a LEC providing terminating access service may charge an IXC ten or more times the reciprocal compensation rate it charges another LEC to provide the same transport and termination service for similar traffic. AT&T Comments at 12. There is an even greater difference for originating traffic, where not only is the rate different, but the direction of payment is different as well.

[47] As AT&T observes in its comments, "[t]he existing patchwork of rules -- under which a local exchange carrier's charges for use of the same facilities in the same manner can vary by an order of magnitude or more based upon such economically irrelevant considerations as the identity or status of the interconnecting carrier or the called party -- is wholly incompatible with the competitive environment Congress envisioned." AT&T Comments at 1. AT&T goes on to state that inappropriate intercarrier charges create barriers to entry, tilt the competitive playing field, and distort investment and use. *Id.*

[48] For instance, the Commission has struggled to determine the appropriate regulatory regime for Internet traffic. *See ISP Remand Order. Intercarrier Compensation for ISP-Bound Traffic*, CC Docket No. 99-68, Order on Remand and Report and Order, 16 FCC Rcd 9151, 9161-62, paras. 18-20 (2001) (*ISP Remand Order*), *remanded, WorldCom v. FCC*, 288 F.3d 429 (D.C. Cir. 2002), *cert. denied*, 538 U.S. 1012 (2003). In this proceeding, the Commission hopes to address the compensation regime for all types of traffic, including ISP-bound traffic.

[49] *See Intercarrier Compensation NPRM*, 16 FCC Rcd at 9614-15, para. 9.

b. Developments in Service Offerings

18. The telecommunications marketplace has changed dramatically since the Commission adopted the existing intercarrier compensation regimes. For instance, most wireless services were not widely available in the 1980s, when the Commission adopted the access charge regime, and wireless services were only beginning to gain a foothold in the market in 1996. Today, there are at least 160 million wireless subscribers and the numbers continue to increase.[50] Due in part to the Commission's deregulatory approach to these services, wireless providers were able to offer bundled local and long-distance packages, and the availability of these bundled packages contributed to the astounding growth of wireless services.

19. Prior to 1996, most wireline carriers were limited to providing a single type of service, such as local or long-distance. The 1996 Act fundamentally changed the telecommunications marketplace by opening all market segments to competition and by lifting existing restrictions on the provision of specific services by some classes of carriers.[51] It is undisputed that carriers are taking advantage of the competitive opportunities presented by the 1996 Act.[52] These legal and regulatory changes enable carriers to offer a broad range of services to their customers, including flat-rated "bundles" of two or more services.[53] Carriers such as Verizon, MCI, and AT&T now offer unlimited

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[50]*See Telephone Trends Report* at Table 11.1 (showing 160 million wireless subscribers as of December 2003). Nationwide, mobile wireless telephone subscribers increased six percent during the first six months of 2003, from 138.9 million to 147.6 million. *Federal Communications Commission Releases Data on Local Telephone Competition*, Industry Analysis and Technology Division, Wireline Competition Bureau, at 1 (rel. Dec. 22, 2003) (*Local Competition Report*). For the full twelve-month period ending June 30, 2003, the number of mobile wireless subscribers increased 13 percent. *Id. See also* Cellular Telecommunications Industry Association, Survey (visited April 22, 2004) <http://www.wocom.com/pdf/CTIA_Semiannual_Survey_YE2003.pdf> (indicating that as of December 2003, the number of national subscribers was approximately 158,721,981).

[51]*See generally Local Competition First Report and Order*, 11 FCC Rcd at 15505-07, paras. 1-5 (1996) (discussing the competitive changes contemplated by the 1996 Act).

[52]For instance, as of June 2003, competitive local exchange carriers (LECs) provided 14.7 percent of the nationwide local telephone lines that were in service to end users. *See Telephone Trends Report* at 1. Moreover, the Bell Operating Companies (BOCs) are now able to provide in-region long-distance services in all 50 states and the District of Columbia. *Federal Communications Commission Authorizes Qwest To Provide Long Distance Service in Arizona – Bell Operating Companies Long Distance Application Process Concludes, Entire Country Authorized for "All Distance" Service*, WC Docket No. 03-194, FCC News, at 2 (rel. Dec. 3, 2003). The BOCs did not require such authorization in Alaska and Hawaii.

[53]*See Federal-State Joint Board on Universal Service; 1998 Biennial Regulatory Review – Streamlined Contributor Reporting Requirements Associated with Administration of the Telecommunications Relay Service, North American Numbering Plan, Local Number Portability, and Universal Service Support Mechanisms; Telecommunications Services for Individuals with Hearing and Speech Disabilities, and the Americans with Disabilities Act of 1990; Administration of the North American Numbering Plan and North American Numbering Plan Cost Recovery Contribution Factor and Fund Size; Number Resource Optimization; Telephone Number Portability; Truth-in-Billing and Billing Format*, CC Docket Nos. 96-45, 98-171, 90-571, 92-237, 99-200, 95-116, 98-170, NSD File No. L-00-72, Further Notice or Proposed Rulemaking and Report and Order, 17 FCC Rcd 3752, 3808-09, para. 133 (2002) (observing that carriers increasingly bundle telecommunications services, such as flat-rate packages that include both local and long distance services) (*Universal Service et al. Further Notice*).

local, long-distance, and other services in one flat-rated service package.[54] These offerings, which from the customer's perspective do not distinguish between local and long-distance service, are dramatically different than the retail offerings that existed prior to the 1996 Act.

20. In addition to competitive developments within the wireless and wireline sectors, the advent of voice-over-internet protocol (VoIP) technology has introduced another mass market alternative to traditional fixed telephone service. New entrants, such as Vonage, have initiated VoIP services in recent years, and a number of other service providers, including Qwest, Verizon, and a number of cable operators, have begun to use or will soon use Internet protocol to provide voice services.[55] These developments have raised a number of regulatory issues for the Commission to resolve.[56]

21. These bundled offerings and novel services blur traditional industry and regulatory distinctions among various types of services and service providers, making it increasingly difficult to enforce the existing compensation regimes. Moreover, in a market where carriers are offering the same services and competing for the same customers, disparate treatment of different types of carriers or types of traffic has significant competitive implications. For instance, if one type of carrier primarily recovers costs from other carriers, rather than its retail customers, it may have a competitive advantage over another type of carrier that must recover the same costs primarily from its own retail customers.[57]

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[54]For instance, Verizon offers "Verizon Freedom Packages," which include unlimited local and regional calls, unlimited long-distance calls across the U.S. and Canada, five call features (such as Caller ID and Voice Mail), and DSL service and wireless. *See* Verizon, Verizon Freedom Packages (visited Dec. 21, 2004) <http://www22.verizon.com/foryourhome/sas/FreedomLongDesc.asp?ID=10008&state=DC&NPA=&NXX=&TrackID=VF>. Verizon states that, as of year-end 2003, 48 percent of Verizon residential customers purchased local services in combination with either Verizon long-distance or Verizon DSL, or both. Verizon, Verizon Reports Solid Overall Fourth-Quarter and Year-End Results, Based on Strong Fundamentals, News Release dated Jan. 29, 2004. (visited Dec. 21, 2004) <http://newscenter.verizon.com/proactive/newsroom/release.vtml?id=83519&PROACTIVE_ID=cecdc9cecbcbcac8c6c5cecfcfcfc5cecec9c9c8cbc9ccc8cbc5cf>. In addition, an MCI offering entitled The Neighborhood gives customers unlimited local, long-distance and high speed Internet service for one monthly fee. *See* MCI, MCI The Neighborhood – Home Page (visited Dec. 21, 2004) <http://consumer.mci.com/TheNeighborhood/res_local_service/jsps/default.jsp>. AT&T's One Rate USA and Unlimited Plus plans offer unlimited local and long-distance. *See* AT&T, Compare AT&T Calling Plans (visited Dec. 21, 2004) <http://www.shop.att.com/plancomparison/#datatable>.

[55]*See IP-Enabled Services*, WC Docket No. 04-36, Notice of Proposed Rulemaking, 19 FCC Rcd 4863, 4871-73, para. 10 & n.39 (2004) (*IP-Enabled Services NPRM*).

[56]For instance, the Commission recently initiated a rulemaking proceeding to consider the appropriate regulatory treatment of VoIP services. *See generally id*. *See also, e.g., Vonage Holdings Corporation Petition for Declaratory Ruling Concerning an Order of the Minnesota Public Utilities Commission*, WC Docket No. 03-211, Memorandum Opinion and Order, FCC 04-267, para. 14 (rel. Nov. 12, 2004) (preempting an order of the Minnesota Public Utilities Commission on the basis that the IP-based service at issue could not be separated into interstate and intrastate communications for purposes of effectuating a dual federal/state regulatory scheme and that permitting state regulation would thwart federal law and policy); *Pleading Cycle Established for Petition of Level 3 for Forbearance from Assessment of Access Charges on Voice-Embedded IP Communications,* WC Docket No. 03-266, Public Notice, DA 04-1 (rel. Jan. 2, 2004) (seeking forbearance from the application of access charges to IP-PSTN traffic).

[57]*See ISP Remand Order*, 16 FCC Rcd at 9154-55, para. 5.

22. Even if there were economic or technical differences among the different types of services that warranted different termination rates, the increased use of alternative services makes it difficult to sustain current regulatory distinctions. Technological alternatives to POTS service that are not tied to a geographic location, such as wireless services and some IP-based services, make regulatory distinctions based on jurisdiction difficult to enforce. Combined with other developments, such as our recent decision requiring wireline-wireless (intermodal) local number portability,[58] the availability of these alternatives makes it difficult to identify the geographic end points of a call using telephone numbers.[59] Further, as one commenter notes, services provided via the Internet "neither respect nor reflect most of the traditional boundaries and classifications of service used to define regulatory status."[60] As the demand for these new services and offerings continues to grow, so will the challenges associated with determining the appropriate intercarrier compensation for this traffic under our current rules.

c. Developments in Telecommunications Infrastructure

23. Another consideration is how the telecommunications infrastructure has developed, which affects the way carrier costs are incurred and recovered under the intercarrier compensation regimes. Our existing compensation regimes are based largely on the recovery of switching costs through per-minute charges.[61] In a separate rulemaking before the Commission,[62] however, a number of carriers argue that a substantial majority of switching costs do not vary with minutes-of-use (MOU). MCI argues, for example, that vendor contracts for switches establish per-line prices, rather than per-minute prices, and thus LECs do not incur switching costs on a per-minute basis.[63] Similarly, AT&T argues that switches generally have excess capacity so that increases in usage do not increase the cost of a switch.[64] In addition, the overall capacity of telecommunications networks has increased dramatically due to the increased deployment of fiber optic facilities.[65] It appears, therefore, that most network costs, including

[58]*See CTIA Petitions for Declaratory Ruling on Wireline-Wireless Porting Issues*, CC Docket No. 95-116, Memorandum Opinion and Order and Further Notice of Proposed Rulemaking, 18 FCC Rcd at 23698, para. 1(2003) (*CTIA Number Portability Order*).

[59]Telecommunications carriers typically compare the telephone numbers of the calling and called party to determine the geographic end points of a call, which may be relevant for jurisdiction and compensation purposes. *See Starpower Communications, LLC v. Verizon South Inc*., EB-00-MD-19, Memorandum Opinion and Order, 18 FCC Rcd 23625, 23633, para. 17 (2003).

[60]ALLTEL Comments at 6.

[61]*See Intercarrier Compensation NPRM*, 16 FCC Rcd at 9618, para. 17 (discussing rate structure issues raised by the existing intercarrier compensation regulations).

[62]*See TELRIC NPRM*, 18 FCC Rcd at 18945.

[63]*Review of the Commission's Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Service by Incumbent Local Exchange Carriers*, WC Docket No. 03-173, Comments of MCI, at 30 (filed Dec. 16, 2003) (MCI TELRIC Comments).

[64]*Review of the Commission's Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Service by Incumbent Local Exchange Carriers*, WC Docket No. 03-173, Comments of AT&T, at 73-76 (filed Dec. 16, 2003) (AT&T TELRIC Comments).

[65]*See* Fred Donovan, *Carrier Fiber-Optic Spending to Top $24B in 2004*, Vol. 21, Issue 4, Fiber Optic News (2001) (noting the findings of a study done by the Telecommunications Industry Association (TIA) concluding that (continued….)

switching costs, result from connections to the network rather than usage of the network itself.[66] This development in infrastructure calls into question whether intercarrier compensation mechanisms based on per-minute charges remain appropriate or necessary.[67]

24. Exacerbating the issue of inefficient rates is the problem of terminating access monopolies. Even when an end user takes service from two providers, *e.g*., wireless and wireline, the originating carrier must deliver the call to the terminating carrier with the telephone number dialed by the calling party. Other carriers seeking to deliver calls to that end user have no choice but to purchase terminating access from the called party's LEC. Originating carriers generally have little practical means of affecting the called party's choice of access provider, and the called party's LEC may take advantage of the situation by charging excessive terminating rates to a competing LEC. To address the terminating access monopoly problem, the Commission generally has determined that carriers should not be permitted unilaterally to impose termination charges that are not subject to regulation.[68]

d. Developments in Consumer Control Over Telecommunications Services

25. Finally, there have been major developments in the ability of customers to manage their telecommunications services. Carriers now offer a number of call screening services that permit customers to block unwanted calls, such as telemarketing calls. Screening services such as caller ID, privacy messages, and non-solicitation messages give customers greater control over the calls they receive.[69] The fact that recipients of calls can and do pay for these services indicates that these customers

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fiber-optic deployment by incumbent LECs doubled in 2000 and that deployment by competitive LECs rose 23.2 percent); *Despite Fears, fiber-optic deployment continues to increase (Industry Trend or Event)*, Vol. 18, Issue 6, Lightwave (2001) (citing the TIA report findings that fiber miles deployed by carriers grew 168.7 percent in 2000, compared to 55.7 percent in 1999).

[66] *See infra* para. 67.

[67] For instance, reciprocal compensation rates often substantially exceed the per-minute incremental cost of terminating a call and therefore create a potential windfall for carriers that serve customers that primarily or exclusively receive traffic. *ISP Remand Order*, 16 FCC Rcd at 9182-83, paras. 68-71; *see also Intercarrier Compensation NPRM*, 16 FCC Rcd at 9616, para. 11. Because of these inefficient termination charges, the Commission found that some competitive LECs were targeting such customers, particularly ISPs, in order to profit from the one-way flow of traffic. *ISP Remand Order*, 16 FCC Rcd at 9182-83, paras. 68-70; *see also Intercarrier Compensation NPRM*, 16 FCC Rcd at 9625, para. 38. This reciprocal compensation asymmetry created artificial incentives for entry by LECs intent on serving ISPs. It distorted competition because ISPs were charged rates well below the cost of providing them with service. *ISP Remand Order*, 16 FCC Rcd at 9162, para. 21.

[68] *See Access Charge Reform, Reform of Access Charges Imposed by Competitive Local Exchange Carriers*, CC Docket No. 96-262, Seventh Report and Order, 16 FCC Rcd 9923 (2001) ("*CLEC Access Charge Order*") (establishing benchmark rates for CLEC access charges), *recon*., *Access Charge Reform, Reform of Access Charges Imposed by Competitive Local Exchange Carriers, Petition of Z-Tel Communications, Inc. For Temporary Waiver of Commission Rule 61.26(d) to Facilitate Deployment of Competitive Service in Certain Metropolitan Statistical Areas*, CC Docket No. 96-262 and CCB/CPD File No. 01-19, Eighth Report and Order and Fifth Order on Reconsideration, 19 FCC Rcd 9108 (2004) (*CLEC Access Charge Recon. Order*); *see also Petitions of Sprint PCS and AT&T Corp. For Declaratory Ruling Regarding CMRS Access Charges*, WT Docket No. 01-316, Declaratory Ruling, 17 FCC Rcd 13192 (2002) (allowing CMRS access charges only pursuant to contracts with IXCs).

[69] Qwest Comments at 39.

benefit from receiving calls, and indeed benefit more from receiving some types of calls than others. Moreover, federal agencies and state lawmakers have established "do not call" options for consumers. The Commission recently established a nationwide Do-Not-Call Registry for consumers who wish to avoid telemarketing calls.[70] The Do-Not-Call-Registry, which is being implemented in conjunction with the Federal Trade Commission, gives consumers the choice of whether or not to receive telemarketing calls in their homes.

26. This general increase in the ability of customers to manage their telecommunications services has been accelerated by the introduction of IP-enabled services, which provide consumers far greater control over if, how, and when they receive calls.[71] Some IP-enabled telephone services include automated voicemail attendants, call pre-screening, and call forwarding of pre-screened calls.[72] Other services include unified messaging or a unified mailbox that may be accessed by any IP-enabled device. Services such as these permit users to determine the media by which they would like to respond to a given message.[73] As the Commission recently observed, with IP-enabled services, "[e]nd users are likely to enjoy greater and greater flexibility in designing or selecting communications packages that suit their individual needs, and can be expected to access those packages over networks of their choosing, on devices of their choosing."[74] Thus, IP-enabled services provide many more options for consumers seeking to control how and when they receive telephone calls.

27. This increased ability of consumers to avoid calls for which they may not perceive a benefit (*e.g*., telemarketing calls) means that they generally will benefit from calls they choose to accept. As a result, we question the assumption underlying our current rules that the calling party is the primary beneficiary of any given call and therefore should bear all the costs of the call.[75] As the Commission observed in the *Intercarrier Compensation NPRM*, it may be more rational to assume that both the calling and called party benefit from any given call.[76] Indeed, for customer choice in a competitive marketplace to be economically meaningful, customers should bear the cost of the network of their choosing and avoid the cost of the networks rejected. Similarly, networks should make investment decisions based on whether they can recover costs from the customers that investment will attract.[77]

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[70] *See* Federal Communications Commission, *FCC Authorizes Nationwide Do-Not-Call Registry*, News, at 1 (rel. June 26, 2003). The rules establishing the nationwide Do-Not-Call Registry were recently upheld on appeal. *See Mainstream Marketing v. FTC*, 358 F.3d 1228 (10th Cir. 2004).

[71] *See IP-Enabled Services NPRM*, 19 FCC Rcd at 4877, 4879, paras. 18, 22.

[72] *See id*. at 4877, para. 18.

[73] *Id.*

[74] *Id*. at 4879, para. 22.

[75] *Intercarrier Compensation NPRM*, 16 FCC Rcd at 9624-25, para. 37. We note, however, with respect to CMRS calls, that the Calling-Party's-Network-Pays (CPNP) regime typically does not assign the full cost to the originating carrier and caller because CMRS providers typically charge their own subscribers for incoming calls. *Id*. at 9624, n.54.

[76] *Id*. at 9624-25, para. 37.

[77] Further, if discrete calls are a *de minimis* source of costs, then the occurrence of such calls should not transfer significant costs between networks. That is, even if it makes sense as a policy matter for carriers to recover costs (continued….)

28. All of these developments warrant a re-evaluation of the existing regimes, and the record confirms the need for comprehensive reform efforts. In addition to the extensive record received in response to the *Intercarrier Compensation NPRM*, industry groups have been negotiating and developing comprehensive reform proposals for consideration in this proceeding.[78] Recognizing that the marketplace has changed significantly since these regimes were established, all of the proposals advocate replacing the existing rules with a more unified approach to intercarrier compensation.[79]

B. Goals of Intercarrier Compensation Reform

29. Acknowledging that significant reform might be needed, the Commission requested comment in the *Intercarrier Compensation NPRM* on the appropriate goals of intercarrier compensation regulation in a competitive market and discussed specific goals that should be considered in evaluating a new regime.[80] In particular, the Commission asked about the role efficiency should play in developing intercarrier compensation regulations and whether a new regime should be technologically and competitively neutral.[81] The Commission also sought comment on whether, in evaluating a new regime, it should consider the degree of regulatory intervention required to implement the new rules, and on the weight to be given to these considerations.[82] Further, the Commission found it reasonable to consider the

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from competing carriers with whom they exchange traffic, rather than their own customers, a compensation approach based on average costs (rather than actual costs) would overcompensate the receiving carrier, thereby creating an arbitrage opportunity.

[78] *See infra* Section II.C.1 (discussing the specific proposals in the record).

[79] *See generally* Regulatory Reform Proposal of the Intercarrier Compensation Forum, October 5, 2004 (ICF Proposal), attached to Letter from Gary M. Epstein and Richard R. Cameron, Counsel for the Intercarrier Compensation Forum, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, Tab A (filed Oct. 5, 2004) (ICF Oct. 5 *Ex Parte* Letter); EPG Comprehensive Plan For Intercarrier Compensation Reform, Nov. 2, 2004, (EPG Proposal), attached to Letter from Glenn H. Brown, EPG Facilitator, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92 (filed Nov. 2, 2004); Alliance for Rational Intercarrier Compensation (ARIC) -- Fair Affordable Comprehensive Telecommunications Solution (FACTS), attached to Letter from Wendy Thompson Fast, President, Consolidated Companies and Ken Pfister, Great Plains Communications, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket Nos. 01-92, 96-45, 04-36, 99-68, and 96-98 (filed Oct. 25, 2004); Cost-Based Intercarrier Coalition, Sept. 2, 2004 (CBICC Proposal), attached to Letter from Richard Rindler, Counsel for the Cost-Based Intercarrier Compensation Coalition, to Marlene Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92 (filed Sept. 2, 2004); Updated Ex Parte of Home Telephone Company , Inc. and PBT Telecom, Nov. 2, 2004 (Home/PBT Proposal), attached to Letter from Keith Oliver, Vice-President, Finance, Home Telephone Company, Inc. and Ben Spearman Vice President, Chief Regulatory Officer, PBT Telecom, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92 (filed Nov. 2, 2004); NASUCA Intercarrier Compensation Proposal, December 14, 2004, at 1 (NASUCA Proposal), attached to Letter from Philip F. McClelland, Senior Assistant Consumer Advocate, to Marlene Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, Attach. (filed Dec. 14, 2004); Western Wireless Intercarrier Compensation Reform Plan, December 1, 2004, at 6 (Western Wireless Proposal), attached to Letter from David L. Sieradzki, Counsel for Western Wireless Corp., to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, Attach. (filed Dec. 1, 2004).

[80] *Intercarrier Compensation NPRM*, 16 FCC Rcd at 9623-24, paras. 31-36.

[81] *Id*. at 9923-24, para. 33.

[82] *Id.* at 9924, para. 34.

extent to which a new regime would resolve the problems identified with the current intercarrier compensation regimes.[83] Finally, the Commission sought comment on the possible advantages and disadvantages of moving to a single, unified approach to intercarrier compensation.[84]

30. Commenters identify a number of important goals for consideration in adopting a new intercarrier compensation system. Many commenters either explicitly support the goal of promoting competition,[85] or suggest that competition is a critical goal of this proceeding.[86] Other commenters focus on the need to promote efficiency.[87] State commissions also suggest that any compensation scheme should maintain and promote universal service.[88] Other parties urge us to adopt a regime that minimizes the need for regulatory intervention and reduces transaction costs.[89] A number of commenters also ask the Commission to consider the goal of regulatory certainty,[90] and to adopt an approach that is legally supportable,[91] will result in reasonable and affordable end-user rates,[92] and will avoid rate shock.[93]

31. Although the commenters differ somewhat on the specific goals of an intercarrier compensation regime, some common themes emerge. Based on the record, we agree with commenters that any new approach should promote economic efficiency. As the Commission noted in the *Intercarrier Compensation NPRM*, any new approach should encourage the efficient use of, and investment in, telecommunications networks, and the development of efficient competition.[94] Indeed, one of the

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[83] *Id.* at 9924, para. 35.

[84] *Id.* at 9924, para. 36.

[85] *See, e.g.,* Allegiance Comments at 6; Texas Counsel Comments at 51; WorldCom Comments at 4-6, 20; Taylor Reply at 4; Texas Counsel Reply at 8-9.

[86] *See, e.g.,* AT&T Comments at 1-2; AT&T Wireless Comments at 6-14; CompTel Comments at 2, 9-10, 16-21, 25-29; Florida Commission Comments at 2-3; Taylor Reply at 4.

[87] *See, e.g.*, Cable & Wireless Comments at 2; AT&T Reply at 2; Texas Counsel Reply at 8-9. *See also* ALLTEL Comments at 3 (supporting increased efficiency based on deregulation); AOL Comments at 8 (supporting the deployment of efficient network infrastructure).

[88] *See, e.g.*, California Commission Comments at 3; Texas Commission Comments at 6; Texas Counsel Reply at 8-9.

[89] *See, e.g.*, USTA Comments at 19; Level 3 Reply at 11.

[90] *See, e.g.,* Allegiance Comments at 6; Focal *et al*. Comments at 1-4; Texas Counsel Comments at 43, 50; Taylor Reply at 3.

[91] *See, e.g.*, Texas Counsel Comments at 51.

[92] *See, e.g.*, California Commission Comments at 3-4; Florida Commission Comments at 3; New York Commission Comments at 2; Texas Counsel Comments at 51; Texas Commission Comments at 6; Wisconsin Commission Comments at 4-5.

[93] *See, e.g.,* Alaska Commission Comments at 2-3; California Commission Comments at 3-4; CenturyTel Comments at 6-7; Florida Commission Comments at 3-4; Sprint Comments at 24-25; Taylor Reply at 4.

[94] *Intercarrier Compensation NPRM*, 16 FCC Rcd at 9612, para. 2.

Commission's most important policies is to promote facilities-based competition in the marketplace.[95] An approach that encourages the development of efficient competition is consistent with the goals of the 1996 Act, which was intended to both open markets to competitive entry and promote increased competition in telecommunications markets.[96]

32. Preservation of universal service is another priority under the Act and we recognize that fulfillment of this mandate must be a consideration in the development of any intercarrier compensation regime.[97] This Commission remains committed to universal service, and we are particularly sensitive to the interests of rural and high-cost communities. Given the relationship between intercarrier compensation and universal service support, we recognize that reforms to the intercarrier compensation regime may warrant changes to universal service support mechanisms. Any proposal that would result in significant reductions in intercarrier payments should include a proposal to address the universal service implications, if any, of such reductions. In particular, many rural LECs collect a significant percentage of their revenue from interstate and intrastate access charges.[98] Because of the high costs associated with serving rural areas, we must be certain that any reform of compensation mechanisms does not jeopardize the ability of rural consumers to receive service at reasonable rates. Indeed, the Commission would be particularly receptive to any plan that offers expanded choices and lower rates to rural consumers. For this reason, we seek comment in this item on universal service related issues raised by commenters, including the need to maintain reasonable and affordable end-user rates and the avoidance of rate shock.

33. We also agree that any new intercarrier compensation approach must be competitively and technologically neutral. Given the rapid changes in telecommunications technology, it is imperative that new rules accommodate continuing change in the marketplace and do not distort the opportunity for carriers using different and novel technologies to compete for customers. In addition, we favor an approach that provides regulatory certainty where possible and limits both the need for regulatory intervention and arbitrage concerns arising from regulatory distinctions unrelated to cost differences. Similar types of traffic should be subject to similar rules. Similar types of functions should be subject to similar cost recovery mechanisms. We are interested in not only similar rates for similar functions, but also in a regime that would apply these rates in a uniform manner for all traffic.[99] To the extent a proposed regime would preserve distinctions between types of carrier or types of traffic, such distinctions should be based on legitimate economic or technical differences, not artificial regulatory distinctions. An approach requiring minimal regulatory intervention and enforcement is consistent with the pro-competitive de-regulatory environment envisioned by the 1996 Act.[100] Consequently, proposals that rely on negotiated agreements between carriers might be preferable to regimes requiring detailed rules and

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[95] *See, e.g. TELRIC NPRM*, 18 FCC Rcd at 19947, para. 3 (stating that facilities-based competition is "one of the central purposes of the Act").

[96] *See Local Competition First Report and Order*, 11 FCC Rcd at 15505, para. 3.

[97] *See* 47 U.S.C. § 254(b).

[98] *See infra* para. 107 (according to NTCA, rural LECs receive on average 10 percent of their revenue from interstate access charges and 16 percent from intrastate access charges).

[99] For instance, it is possible to have a uniform rate for all types of traffic, but have that rate apply differently depending on the traffic type.

[100] *See Local Competition First Report and Order*, 11 FCC Rcd at 15505, 15512, paras. 3, 21.

regulations.

34. There are a number of additional criteria we must consider in assessing whether a particular proposal will help achieve the Commission's policy goals. For example, any proposal for reform of compensation mechanisms should address the impact of such changes on network interconnection rules. As the Commission made clear in the *Intercarrier Compensation NPRM* it is important to have clear rules regarding how and where carriers interconnect and the allocation of responsibilities for any facilities needed to connect two networks.[101]

35. In addition, any reform proposal should explain the Commission's legal authority to adopt it. The Commission clearly has authority under section 201 to adopt or modify compensation mechanisms that apply to jurisdictionally interstate traffic, and it clearly has authority to modify the pricing methodology that applies to reciprocal compensation under section 252(d)(2). Any proposal that contemplates reform of intrastate mechanisms, however, must include an explanation of the Commission's legal authority to implement the proposal.

36. Finally, there will be numerous implementation issues associated with any significant reform of intercarrier compensation mechanisms. As just one example, adoption of a unified regime will require the Commission to decide whether compensation, if any, should be pursuant to tariffs (as in the access charge regime) or agreements (as in the reciprocal compensation regime). Moreover, to the extent a proposal includes significant changes in the level of compensation carriers might receive, we would expect to see a detailed transition plan that will give carriers time to adjust their business plans.

C. Specific Proposals for Intercarrier Compensation Reform

37. Having concluded that there is an urgent need to reform the existing intercarrier compensation rules, we now turn to the question of what reforms best serve the goals we have identified. Many parties advocate a unified regime, but there is little consensus as to what type of unified regime we should adopt.[102] In the *Intercarrier Compensation NPRM*, the Commission re-evaluated the rationale for the traditional CPNP regimes and identified new approaches to intercarrier compensation, including a bill-and-keep approach.[103] Under a bill-and-keep approach, neither of the interconnecting networks charges the other network for terminating traffic that originates on the other carrier's network.[104] Rather, "each network recovers from its own end users the cost of both originating traffic delivered to the other network, and terminating traffic received from the other network."[105]

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[101] *See Intercarrier Compensation NPRM*, 16 FCC Rcd at 9650-52, paras. 112-14 (seeking comment on the interplay between the network interconnection rules and the reciprocal compensation rules).

[102] *See, e.g.*, ALLTEL Comments at iii; AOL Comments at 3; AT&T Comments at 1, 12; BellSouth Comments at 2; Cable & Wireless Comments at 8; Cbeyond Comments at 7; CompTel Comments at 5; Global NAPs Comments at ii, 20; GSA Comments at 6; Illinois Commission Comments at 1, 3; Level 3 Comments at 3-4; Mid Missouri Cellular Comments at ii; Qwest Comments at 3; Texas Counsel Comments at 10; Time Warner Comments at 4; Wisconsin Commission Comments at 3; WorldCom Comments at 2.

[103] *Intercarrier Compensation NPRM*, 16 FCC Rcd at 9619-24, paras. 19-36.

[104] *Local Competition First Report and Order*, 11 FCC Rcd at 16045, para. 1096.

[105] *Id.*

38. The *Intercarrier Compensation NPRM* generated considerable discussion of bill-and-keep.[106] Many commenters, including rural LECs, have substantial concerns about moving to a bill-and-keep approach and support retaining a CPNP regime.[107] Other commenters urge the Commission to maintain but reform the existing CPNP approach to intercarrier compensation.[108] These commenters contend that a reformed CPNP regime is economically efficient and easier to implement than a bill-and keep approach.[109] Some argue that the Commission has failed to identify a systemic failure in the CPNP system[110] or that any failures of the CPNP approach are attributable to departures from cost-based rates rather than to the approach itself.[111] Other commenters claim that the record fails to support a departure from the Commission's previous conclusions concerning bill-and-keep.[112]

39. In parallel with the Commission's consideration of the record developed in response to the *Intercarrier Compensation NPRM*, various industry groups have been negotiating proposals for comprehensive reform of federal and state intercarrier compensation mechanisms. These negotiations have resulted in proposals from a number of groups – the Intercarrier Compensation Forum (ICF), the Expanded Portland Group (EPG), the Alliance for Rational Intercarrier Compensation (ARIC), the Cost-Based Intercarrier Compensation Coalition (CBICC), and two rural LECs, Home Telephone Company and PBT Telecom (Home/PBT).[113] In addition, we discuss a statement of principles submitted by CTIA as well as a specific reform proposal filed by Western Wireless.[114] We also discuss a proposal by NASUCA that would reduce certain intercarrier compensation rates.[115] Moreover, NARUC has developed a set of principles that it believes should guide any consideration of intercarrier compensation

[106]Attached as Appendix C is a staff analysis of the record on bill-and-keep. The views expressed in this staff analysis do not represent the views of, and are not endorsed by, the Commission.

[107]*See, e.g.*, GVNW Comments at 3-13; ICORE Comments at 6-8; Minnesota Independent Coalition Comments at 2-10; MSTG Comments at 9-12; NTCA Comments at 5-13; Oklahoma Rural Telephone Coalition Comments at 15-45; RICA Comments at 4-10; United Utilities Comments at 4; Western Alliance Comments 23-27; ALLTEL Reply at 2-3; NECA Reply at 3-4, 6-8; TCA Reply at 3-4.

[108]*See, e.g.*, Ad Hoc Comments at 1, 10; Allegiance Comments at 10-13; AT&T Comments at 21-29; CompTel Comments at 18-21; Focal *et al*. Comments at 46; MD-OPC Comments at 20-21; MECA Comments at 38.

[109]*See* AT&T Comments at 21-29.

[110]*See* CompTel Comments at 9.

[111]*See, e.g.,* Ad Hoc Comments at 2; AT&T Comments at 13-14; CompTel Comments at 9; AT&T Reply at 11.

[112]*See, e.g.,* Allegiance Comments at 13-16; Focal *et al*. Reply at 4-8; NASUCA Reply at 10-11. In the *Local Competition First Report and Order*, the Commission concluded that, as long as the costs of terminating traffic are positive, bill-and-keep arrangements are not economically efficient. *Local Competition First Report and Order*, 11 FCC Rcd at 16055, para. 112.

[113]*See supra* note 79.

[114]*See* Letter from Steve Largent, President/CEO, CTIA – The Wireless Association, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, at 1 (filed Nov. 29, 2004) (CTIA Nov. 29 *Ex Parte* Letter); Western Wireless Proposal at 6.

[115]*See* NASUCA Proposal at 1.

reform.[116] Below, we provide an overview of these proposals and principles. We then seek comment on specific questions concerning discrete aspects of these comprehensive reform plans.

1. Description of Industry Proposals[117]

40. *Intercarrier Compensation Forum (ICF)*. The ICF is a diverse group of nine carriers that represent different segments of the telecommunications industry.[118] The ICF has developed a comprehensive plan for reforming current network interconnection, intercarrier compensation, and universal service rules. With respect to network interconnection, the ICF plan establishes default technical and financial rules that generally require an originating carrier to deliver traffic to the "Edge" of a terminating carrier's network.[119] The designated network Edge must accept all kinds of public switched telephone network (PSTN) traffic, must allow other carriers to interconnect using multiple methods, and must consist of certain types of facilities, among other things.[120] Under this proposal, each carrier must have at least one Edge in every LATA where it needs to receive traffic; however, a carrier having no network within a LATA may designate another carrier to provide the Edge function.[121] A modified version of the Edge proposal applies to eligible rural carriers, called "Covered Rural Telephone Companies" (CRTCs), which have no obligation to deliver originating traffic beyond the boundaries of the study area in which a call originates.[122]

41. With respect to compensation, the ICF plan would reduce per-minute termination rates from existing levels to zero over a six-year period.[123] Specifically, the compensation rate for interstate access, intrastate access, and most other types of non-access traffic[124] would be reduced in equal steps

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[116]The National Association of Regulatory Utility Commissioners Study Committee on Intercarrier Compensation – Goals for a New Intercarrier Compensation System (May 5, 2004) (NARUC Principles). This document is available on NARUC's web site at http://www.naruc.org/associations/1773/files/intercarriercompgoals_whitepaper04.pdf (Visited February 14, 2005).

[117]The summaries provided herein do not attempt to capture every aspect of the detailed proposals submitted in this proceeding. Interested parties are strongly encouraged to review these proposals in their entirety.

[118]The nine carriers are AT&T, GCI, Global Crossing, Iowa Telecom, Level 3, MCI, SBC, Sprint and Valor. ICF Oct. 5 *Ex Parte* Letter at 1.

[119]ICF Proposal at 3-9. Specific obligations depend on whether a carrier operates a hierarchical network or a non-hierarchical network. *See id*. at 9-13.

[120]*Id*. at 4. "Edges" may be access tandems, end offices, wireless MSCs, points of presence (POPs), or "trunking media gateways." *Id.* at 6-7.

[121]*Id*. In addition, the proposed rules limit the number of a carrier's Edges to the lower of the total number of incumbent LEC access tandems in a LATA or the number of the carrier's network-defined Edges in the LATA. *Id.* These rules are intended to "prevent a carrier from proliferating Edges in order to shift transport responsibility from itself to other carriers, and ensure that an interconnecting carrier can choose direct interconnection." *Id.* at 5.

[122]*Id.* at 19-25. A CRTC may designate an end office within its study area or an access tandem outside its study area as an Edge. *Id.* at 19-20.

[123]*Id.* at 31.

[124]Although not entirely clear, "non-access" traffic for purposes of the ICF proposal appears to include ISP-bound traffic and section 251(b)(5) traffic (including foreign exchange (FX) or virtual FX traffic provided on a non-access (continued….)

over four years to a unified rate of $.000175 per MOU.[125] This rate is further reduced in the fifth year of the transition to $.0000875 per MOU and finally eliminated a year later.[126] The plan also includes a settlement proposal to address existing intercarrier compensation disputes between CRTCs and CMRS providers.[127]

42. Revenue eliminated as a result of the transition to bill-and-keep under the ICF plan would be replaced by a combination of end-user charges and a new universal service support mechanism.[128] As intercarrier payments decline, the cap on the subscriber line charge (SLC) would increase in equal steps from the current level of $6.50 to $10.00 in areas served by non-rural carriers and up to $9.00 in areas served by CRTCs.[129] In addition, the ICF plan permits SLC pricing flexibility for price cap incumbent LECs, subject to certain consumer protection safeguards.[130] The ICF plan also includes a "more measured transition" for CRTC customers and gives CRTCs the option to increase the residential monthly SLC cap by two additional $.50 annual increments beginning July 1, 2010.[131]

43. The ICF proposal includes two new universal service mechanisms to provide explicit support for amounts that otherwise are not recoverable under the plan. One mechanism, the Intercarrier Compensation Recovery Mechanism (ICRM), is available to non-rural incumbent LECs and all competitive eligible telecommunications carriers (CETCs) on a per-line basis in non-CRTC areas.[132] The other mechanism, the Transitional Network Recovery Mechanism (TNRN), is available only to CRTCs and certain eligible CETCs.[133] Under this mechanism, rate-of-return CRTCs would receive support based

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basis), among other things. *Id.* at 40-41. Although the ICF touts a uniform rate approach, we note that its detailed proposal contains numerous exceptions and different transition rates and rules for some types of non-access traffic. *See* ICF Proposal at 40-48.

[125] *Id*. at 31-33, 42-47. The ICF plan also includes new transit service, interconnection transport, and CRTC terminating transport rates that replace the existing transport rate structure. *Id*. at 25-31, 36-40.

[126] *Id*. at 37. In the fifth year of the plan, the ICF proposal calls for a further proceeding to evaluate whether or not the timing of the rate reductions should be modified. *Id*. at 82

[127] *Id.* at 46-47. The proposed settlement provides clarification as to when reciprocal compensation applies to traffic exchanged between CMRS providers and CRTCs and establishes default reciprocal compensation rates that apply in the absence of an agreement between the parties. *Id.*

[128] *Id*. at 48.

[129] *Id.* at 60-63. *See also* Regulatory Reform Proposal of the Intercarrier Compensation Forum, August 13, 2004 (ICF August Proposal), attached to Letter from Gary Epstein, Counsel for the Intercarrier Compensation Forum, to Marlene Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, Tab 3, at 27 (filed Aug. 16, 2004) (providing a comprehensive overview of the SLC transition under the ICF plan).

[130] ICF Proposal at 63-68.

[131] *Id*. at 62-63.

[132] *Id.* at 69-73. By default, ICRM is available as a uniform, per-line amount to all eligible lines. *Id*. at 69. Alternatively, a recipient incumbent LEC may establish a Zone Disaggregation Plan or a Residential Targeting Plan. *Id*. at 69-72.

[133] *Id.* at 73. TNRN support may be disaggregated under the existing Commission rules governing disaggregation for rural carriers. *Id*.

on their revenue requirement, without regard to the number of lines they serve.[134]

44. Finally, the ICF plan includes several changes to existing universal service support mechanisms.[135] These changes include a modification to the rural high cost loop support and the safety valve support mechanisms.[136] In addition, the proposal provides an option for certain price cap CRTCs to receive support under the non-rural, model-based high cost mechanism.[137] The existing per-line universal service support amount would remain portable to eligible competitive carriers.[138] The ICF plan also prescribes a single contribution methodology used to collect funding for both the new and existing universal service support mechanisms.[139]

45. *Expanded Portland Group (EPG)*. The EPG is a group of small and mid-sized rural LECs (and consulting organizations serving rural carriers) that came together to develop a proposal distinct from a bill-and-keep mechanism.[140] Stage one of the EPG proposal is intended to address more immediate issues arising under the current regimes, including unidentified or "phantom" traffic, the scope of the ESP exemption, and the termination of traffic in the absence of agreements between carriers.[141] To address these issues, the EPG plan would implement "truth-in-labeling" guidelines, establish default termination rules and rates, and eliminate the ESP exemption for ISPs terminating traffic to the PSTN.[142] ISPs would be permitted to continue to use flat-rated business lines to receive calls from their customers, however.[143]

46. In the second stage of the EPG plan, all per-minute rates would be set at the level of interstate access charges and a new Access Restructure Charge (ARC) would be implemented to make up any revenue shortfall.[144] The EPG proposes that a national benchmark price level of $21.07 per line be established for computing the eligibility for ARC funding.[145] Carriers with rates below the national

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[134] *Id.* at 54-58, 73.

[135] *See id*. at 75-81.

[136] *Id*. at 80-81.

[137] *Id*. at 81.

[138] *Id*. at 80.

[139] *Id*. at 75-78 (describing a "unit-based" assessment of working telephone numbers and non-switched, high-speed, dedicated network connections).

[140] EPG Proposal at 1-2.

[141] *Id*. at 5-6, 15-20.

[142] *Id.*

[143] *Id.* at 5, 20.

[144] *Id*. at 7, 21-22. Under the EPG plan, the ARC initially equals the residual intercarrier "revenue requirement" offset by net intercarrier revenues, universal service support, and subscriber line charges. *Id*. at 26-27. Calculation of the "intercarrier revenue requirement" is done using the current process laid out in the Commission's rules. *Id.*

[145] *Id*. at 7, 23-26. Thus, a company with basic rate plus SLC of less than $21.07 would not qualify for full ARC recovery for their intercarrier revenue reductions. *Id.* at 25. The $21.07 per line benchmark is the sum of the (continued….)

benchmark would be subject to reduced ARC funding they otherwise would qualify for.[146] The ARC would be a capacity-based charge calculated by NECA and bulk-billed to all carriers based on working telephone numbers, but distributed only to those carriers that lose access charge revenue, *i.e.*, wireline LECs.[147] The EPG asserts that it is not a universal service mechanism and therefore need not be portable to wireless carriers.[148]

47. In the final stage of the EPG plan, per-minute access charges are converted to a capacity-based "Port and Link" structure.[149] Under the EPG plan, carriers would purchase "Ports" to provide a connection into a local carriers network and "Links" to connect the two networks.[150] The Port and Link charges would be set to recover the average equivalent interstate per minute rate with rate banding.[151] Initially, the EPG plan would convert only dedicated switched transport services (*i.e.*, direct interconnection) to a capacity-based structure.[152] Common switched transport services (*i.e.*, indirect interconnection) would remain on a per MOU basis with the option of converting to a capacity-based rate structure.[153] These Port and Link charges would not apply to local traffic, including Extended Area Service (EAS), and ISP-bound traffic.[154]

48. *Alliance for Rational Intercarrier Compensation (ARIC) – Fair Affordable Comprehensive Telecom Solution (FACTS)*. ARIC is comprised of small telecommunications companies providing service in rural, high-cost areas.[155] The FACTS plan developed by ARIC calls for a unified per-minute rate for all types of traffic that would be capped at a level based on a carrier's unseparated,

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average urban residential rate and the average residence and single line SLC. *Id*. at 24 (citing rates from the Commission's *Reference Book of Rates, Price Indicies, and Household Expenditures for Telephone Service, Industry Analysis and Technology Division*, Wireline Competition Bureau, at Table 1.2 (rel. July 1, 2004)).

[146] *Id*. at 24-25. Under the EPG plan, carriers subject to reduced ARC funding could either request a basic rate increase from state commissions or obtain additional revenue from individual end users under their access tariffs. *Id.* at 25.

[147] *Id*. at 7, 22.

[148] *Id*. at 22-23.

[149] *Id*. at 7-8, 29-33.

[150] *Id*. at 7, 30. It is unclear whether all carriers, or only LECs, are entitled to assess Port and Link charges on other carriers.

[151] *Id.* at 31. Link charges would be set equal to the charge for the equivalent interstate special access service, and rate banding may be necessary to recognize the high cost of transport in rural areas. *Id*.

[152] *Id*. at 32.

[153] *Id*. The EPG states that many small LECs connect with most other carriers using common transport arrangements. *Id*. at 31.

[154] *Id*. at 32-33. Per minute reciprocal termination charges would apply to local or EAS traffic, and the existing compensation rules governing the compensation for ISP-bound traffic would remain in effect. *Id*.

[155] ARIC Proposal at 1.

interoffice embedded costs.[156] Specifically, the unified compensation rates for rate-of-return carriers would be calculated by dividing the appropriate interoffice, traffic-sensitive, unseparated, embedded costs by minutes (both access and reciprocal compensation) that utilize a company's interoffice facilities.[157] The rates for price cap carriers would be determined by calculating reinitiated price cap rates on an unseparated basis to be applied to all network minutes.[158] If the existing price cap rates are higher than the reinitiated rates, the rates would be reset to the reinitiated rates; if the existing rates are lower, the price cap rates would remain in place.[159] The FACTS plan also includes a proposal for extending this compensation regime to IP-enabled services.[160]

49. In addition to more uniform rates, the FACTS plan calls for local retail rate rebalancing to benchmark levels established by state commissions.[161] These benchmarks would be set within a nationwide rate range recommended by the Joint Board on Universal Service and approved by the Commission.[162] In adopting these benchmark levels, state commissions may consider local calling scope and affordability between rural and non-rural exchanges.[163] In addition to rate rebalancing, the FACTS plan would retain the federal SLC cap and unify SLCs among all companies on a state-specific basis.[164] For rural carriers, these SLCs would be set at the weighted-average residential and business SLCs for price cap carriers in that state.[165] The SLCs for price cap carriers will depend on whether there is an excess of revenues from the reinitiated access rates or current price cap rates.[166]

50. The FACTS plan also includes a joint process by which the Commission and the states review the procedures and data to determine the appropriate unified rates.[167] The resulting per-minute rates would be charged to the retail service provider, *i.e.*, the originating LEC on a local call or the IXC

[156]*Id.* at 2. Under the FACTS plan, special access rates would be unified at interstate levels at which time carriers will have an opportunity to revise and file unified cost-based rates for both jurisdictions. *Id*. at 44.

[157]*Id.* at 39-41. The rates developed under the FACTS plan would be developed separately for both switching and transport. *Id*. at 42.

[158]*Id*.

[159]*Id*. at 42-43. Under the FACTS plan, unified compensation rates for competitive LECs are capped at the level of the competing incumbent LEC in the same market, unless an exemption applies. *Id*. at 44-45.

[160]*Id*. at 46-54, 89-107.

[161]*Id.* at 61-62.

[162]*Id*. at 61, 63-65.

[163]*Id.*

[164]*Id*. at 68-69.

[165]*Id*.

[166]*Id.* at 70.

[167]*Id.* at 37-39. Specifically, the FACTS plan would be implemented through the section 410(c) Joint Board mechanism. *Id.* at 56-57.

on both ends of an interexchange call.[168] Any costs still not recovered through application of these per-minute compensation rates, rebalanced local service rates, and unified SLCs would be recovered through a state equalization fund (SEF).[169] SEFs would be under the control of state commissions but would be funded from both federal and state sources.[170] SEF distributions would be available to all ETCs.[171]

51. *Cost-Based Intercarrier Compensation Coalition (CBICC)*. The CBICC is a coalition of competitive LECs. The CBICC proposal calls for the Commission to require that carriers adopt a single termination rate in each geographic area that would apply to all types of traffic.[172] The rate would be based on the incumbent LEC's cost of providing tandem switching, transport, and end office switching, calculated using the Commission's TELRIC methodology.[173] Under the CBICC plan, interstate access rates immediately would be reduced to this TELRIC level, while the question of how to transition intrastate rates would be referred to a Joint Board.[174] Any loss of revenue associated with these reductions would be offset by increases in end-user charges and, in the case of rural LECs, increased universal service support.[175] CBICC proposes no change in network interconnection rules, and under this plan the carrier with the retail relationship with the originating caller pays all other carriers whose networks are used to complete a call.[176] The CBICC proposal also covers VoIP traffic to the extent that it originates or terminates as circuit-switched traffic.[177]

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[168] *Id*. at 33-35. The retail provider also would be responsible for any transiting costs. *Id*. at 35. Additionally, under the FACTS plan, the tandem owner is responsible for the payment of compensation to the terminating carrier for all unidentified traffic. *Id.* at 55.

[169] *Id*. at 73-75. Stated differently, under the FACTS plan, per-minute compensation rates would be designed to recover only those costs not recovered through local service rates, special access, SLCs, and existing federal and state universal service support mechanisms. Consequently, where these other revenue streams are sufficient to recover all of a carrier's costs, that carrier might not be able to impose any per-minute rate at all. Any costs still not recovered after application of the per-minute compensation rate would be recovered through a state equalization fund (SEF). *See id*. at 74.

[170] *Id*. at 76-80. The minimum federal contribution would be 25 percent and the maximum would be 75 percent. *Id*. at 77-79.

[171] *Id*. at 85. The FACTS plan also retains existing federal universal service support, although it would move some traffic-sensitive costs to the new per-minute compensation rates and lift the existing cap on High Cost Loop support. *Id*. at 71-72.

[172] CBICC Proposal at 1.

[173] *Id*. Because the CBICC advocates use of the TELRIC cost methodology, it supports an average, rather than incremental, cost approach.

[174] *Id*. at 2.

[175] *Id*.

[176] *Id*. at 2-3. Thus, under this proposal, IXCs would continue to pay LECs for the origination of interexchange traffic. *Id*. at 2. Further, transit service providers would charge TELRIC-based rates for the functions actually provided, such as tandem switching and/or interoffice transport. *Id.*

[177] *Id*. at 3.

52. *Home Telephone Company and PBT Telecom (Home/PBT).* Home Telephone Company and PBT Telecom are rural LECs that developed an alternative proposal to those advanced by the larger groups discussed above.[178] Under this proposal, all carriers offering service to customers that make telecommunications calls would be required to connect to the PSTN and obtain numbers for assignment to customers.[179] The plan would replace existing per minute access charges and reciprocal compensation with connection-based intercarrier charges. Specifically, every carrier would develop and tariff a charge to be assessed on all interconnected carriers based on a DS-0 level of connection.[180] If the carrier has an access tandem, it would develop an alternative access tandem connection (ATC) fee that would include the additional costs of the tandem service, including the connections to subtending switches and transport to those offices.[181] Under this proposal, network interconnection between carriers would be accomplished through one POI per LATA, except in the case of rural carriers.[182]

53. To help offset revenues lost from elimination of the current intercarrier compensation charges, the proposal permits carriers to increase SLCs up the current federal cap.[183] Any remaining revenue shortfall may be recovered from a new bulk-billed intercarrier cost recovery fund, called the high cost connection fund (HCCF).[184] Some of the existing universal service mechanisms would be added into the HCCF and one existing mechanism would be eliminated from universal service.[185] The HCCF funding mechanism would be administered by NECA and carriers seeking HCCF funding would need to submit cost support to use in developing the HCCF charge.[186] The HCCF would be funded through a monthly assessment based on activated telephone numbers and such assessment may be passed through to subscribers.[187] Home and PBT explain that, under this plan, the “access charges” are placed on the number which allows connectivity to the network.[188]

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[178] Home/PBT Proposal at 1.

[179] *Id*. at 12-13.

[180] *Id.* at 13. The connection charge is intended to cover the switching and transport costs for use of the local calling network and may not exceed the national average retail fee for a standard business line. *Id*.

[181] *Id*. at 14. The ATC fee is assessed on trunks the tandem owner requires for intra-company traffic and is specific to each tandem. *Id*.

[182] *Id.* In the case of rural carriers, the POI must be located within the local exchange area established by the state commission. *Id*.

[183] *Id*.

[184] *Id*. at 14-15. Home and PBT state that the HCCF represents “the above average network cost required to be recovered from all connected to the network.” *Id*. at 15.

[185] Id. at 15. Specifically, the Local Switching Support mechanism and the ICLS would be added to the HCCF, and the Interstate Access Support for non-rural carriers would be taken out of the existing universal service fund. *Id*. The plan would retain the remaining universal service mechanisms. *Id*. at 17. The states may elect to add intrastate universal service or other funding mechanisms to the HCCF. *Id.* at 16.

[186] *Id*. at 17.

[187] *Id*. at 16.

[188] *Id.* at iii.

54. *Western Wireless Proposal.* Western Wireless is a wireless carrier that has been designated as an eligible telecommunications carrier (ETC) in 14 states and the Pine Ridge Indian reservation. On December 1, 2004, Western Wireless submitted a reform plan based on a unified bill-and-keep system for all forms of traffic.[189] This plan would reduce per-minute compensation rates to bill-and-keep in equal steps using targeted reductions over a four-year period, with a longer transition period for small rural incumbent LECs.[190] Over the four-year transition period, incumbent LECs would be permitted to increase SLCs as proposed in the ICF plan, except that there would be no difference between the SLC caps for rural and non-rural incumbent LECs.[191] At the end of the four-year transition, the SLC would be deregulated for an incumbent LEC that can demonstrate that it is subject to competition.[192] The Western Wireless proposal also includes default network architecture rules based on carrier "edges" or mutual meet-point arrangements.[193] The plan relies on carrier-to-carrier negotiation of interconnection agreements pursuant to section 251(b)(5) of the Act.[194]

55. The Western Wireless proposal also would replace all existing universal service mechanisms with a unified high-cost mechanism based on forward-looking costs.[195] This new support would be fully portable to all designated ETCs and additional portable funds could be dispersed in states with forward-looking costs higher than the national average.[196] The plan also would include a transition period for rural incumbent LECs and ETCs during which existing USF funds would be phased out, and new funds phased in, over four years.[197] This transition would be extended to six years for the smallest

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[189] *See* Western Wireless Proposal at 6. *See also* Letter from David L. Sieradzki, Counsel for Western Wireless Corp., to Marlene H. Dortch, Secretary Federal Communications Commission, CC Docket No. 01-92, Attach. (filed Nov. 18, 2004) (attaching an outline of the Western Wireless Proposal). We note that the Western Wireless Proposal incorporates many of the reforms it proposed in October 2003 in a Petition for Rulemaking in which it urged the Commission to eliminate rate-of-return regulation of rural incumbent LECs for purposes of determining their federal high-cost universal service support and interstate access charges. *See generally Elimination of Rate-of-Return Regulation of Incumbent Local Exchange Carriers*, RM-10822, *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Western Wireless Petition for Rulemaking to Eliminate Rate-of-Return Regulation of Incumbent Local Exchange Carriers (filed Oct. 30, 2003). Due to the similarity of issues and reform proposals raised in the petition and in this *Further Notice*, we assume that the more recent reform plan represents the most comprehensive version of the reforms advocated by Western Wireless.

[190] Western Wireless Proposal at 13.

[191] *Id.* at 14. Under the Western Wireless plan, carriers must identify the SLC as part of the basic price of service rather than as a regulated "add-on" charge. *Id*.

[192] *Id*. Western Wireless also includes a description of the criteria used to determine whether an incumbent LEC is subject to competition. *Id*.

[193] *Id*. at 12. For interconnection between hierarchal incumbent LECs and other carriers, the proposal permits interconnection at the carrier "edge" or under a shared transport arrangement at the option of the competitive carrier. *Id*. The proposal also requires incumbent LECs to offer transit service at capped rates. *Id*.

[194] *Id*. at 10, 20.

[195] *Id*. at 15.

[196] *Id.* Western Wireless states that, at the end of the four-year transition, the fund would be "right-sized," with "sufficient" support, but provides no further detail on fund size and support amounts. *Id*.

[197] *Id*. at 16

rural incumbent LECs and other ETCs, and would include additional support for a limited period if a carrier can demonstrate "extreme hardship."[198]

56. *National Association of State Utility Consumer Advocates (NASUCA) Principles*. NASUCA advocates a minimalist approach that addresses the disparity among some existing intercarrier compensation rates and reduces certain rate levels over a five-year period.[199] Under the NASUCA plan, the Commission would establish a target rate in each year of a five-year transition down to a rate of $0.0055 per minute.[200] Intercarrier compensation rates already under the target rate (*e.g*., reciprocal compensation rates) would remain at current levels.[201] State commissions would be encouraged to match the target rate for intrastate rates, but they would retain authority concerning how to reach that rate.[202] The NASUCA plan also would retain the existing network interconnection rules and existing wholesale and retail relationships.[203] Further, it would retain the current USF mechanisms[204] and the current SLC rate caps.[205] In addition to its proposal, NASUCA urges the Commission to reject efforts to guarantee current revenue streams, such as access revenues.[206] It argues that revenue assumptions in the absence of demonstrated financial need would create artificial incentives for customers to migrate to services that generate fewer access revenues.[207] NASUCA concludes by proposing ways to address access revenue reduction issues.[208]

57. *NARUC Principles*. In an effort to create a vehicle for evaluating the various reform proposals developed by the industry, a group of NARUC commissioners and staff developed a set of principles addressing the design and functioning of any new intercarrier compensation plan, as well as

[198] *Id.*

[199] *See* NASUCA Proposal at 1. NASUCA believes that elimination of the rate disparities combined with revenue reductions will encourage carriers to enter into negotiated bill-and-keep arrangements. *Id*. at 1-2. NASUCA states, however, that a mandatory elimination of intercarrier payments is ill-advised and unnecessary. *Id*. at 2.

[200] *Id.* The plan would permit a higher target rate ($0.0095 per minute) for rural carriers. *Id*. The NASUCA plan contemplates interim reform but not a final comprehensive solution. *Id*. at 1, 3.

[201] *Id*.

[202] *Id*. Thus, under the NASUCA plan, the Commission would continue to have jurisdiction over interstate access rates and the state commissions would continue to have jurisdiction over intrastate access rates and local service rates. *Id.*

[203] *Id*.

[204] *Id*. NASUCA states that the existing local switching support (LSS) fund could be amended to allow recovery of a portion of the revenue shortfall if necessary. *Id*.

[205] *Id*. Additional funding could be recovered, however, through local rates or universal service as determined by the states. *Id*.

[206] *Id*. at 2.

[207] *Id*. at 2.

[208] *Id.* at 3.

prerequisites for implementation of any plan.[209] NARUC favors the application of a unified regime to all companies that exchange traffic over the Public Switched Telephone Network.[210] NARUC would permit a carrier to impose charges to recover the cost of services requested by another carrier (*e.g*., terminating access service) provided that those charges do not discriminate based on the classification of the requesting carrier or its customers, the location of those customers, or the network architecture of the requesting carrier's network.[211] NARUC also favors charges that are competitively and technologically neutral and reflect underlying economic costs.[212]

58. NARUC supports market-based intercarrier compensation rates in competitive markets, and supports price-regulated rates based on a "reasonable return" in non-competitive markets.[213] In addition, NARUC advocates a continuing and significant role by the states in establishing rates and protecting consumers, including the ability to exercise substantial discretion in developing retail rates for providers of last resort.[214] NARUC favors an approach that ensures continuity of services, reasonable and affordable retail rates (especially for rural consumers), and minimizes the impact on universal service support programs.[215] Finally, the principles include a number of issues the Commission should consider before implementing any new plan, such as the estimated cost impact on a carrier-by-carrier basis, the impact on universal service support mechanisms, and any effects on consumer rates.[216]

59. *CTIA – The Wireless Association (CTIA) Principles*. On November 29, 2004, CTIA submitted a statement of principles for the Commission to consider as part of its review of any proposals to reform intercarrier compensation.[217] In its statement, CTIA expresses concern that the comprehensive reform proposals submitted in the record do not reflect an appropriate balancing of consumer and carrier interests and do not adequately reflect the views and concerns of wireless carriers and customers.[218]

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[209] NARUC Principles at 1.

[210] *Id*.

[211] *Id*. at 2.

[212] *Id*. Moreover, NARUC believes that any intercarrier compensation system should be simple and inexpensive to administer. *Id.*

[213] *Id*. at 2-3. Although NARUC supports a "rigorous definition of 'competitive markets,'" it does not provide a suggested definition.

[214] *Id*. at 3.

[215] *Id*. at 3-4.

[216] *Id*. at 4.

[217] *See* CTIA Nov. 29 *Ex Parte* Letter at 1. Prior to the filing of the principles submitted by CTIA, a group of independent wireless carriers (IWCs) submitted a statement of principles for consideration in this proceeding. *See* Letter from Thomas J. Sugrue, Vice President, Government Affairs, T-Mobile USA, Inc., Gene A. DeJordy, Vice President, Regulatory Affairs, Western Wireless Corp., and David M. Wilson, Counsel to Dobson Cellular Systems, Inc., to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, at 1 (filed Nov. 17, 2004). We note that the general principles supported by the IWCs are substantially similar to those submitted by CTIA and that the IWCs are members of CTIA. Thus, we need not separately detail the earlier principles submitted by the IWCs.

[218] CTIA Nov. 29 *Ex Parte* Letter at 1.

CTIA supports a bill-and-keep approach to intercarrier compensation reform under which carriers would "have the flexibility to design their rate structures to recover a larger portion of costs from end-user customers – while ensuring that end-user rates remain affordable."[219] It explains that any rules should focus on the benefits to consumers and not guarantee revenue neutrality for incumbent carriers.[220] CTIA states that the new rules should encourage economic efficiency and promote competition through deregulation.[221] CTIA also supports rules that are technologically neutral through uniform application to all categories of services and carriers.[222] In terms of universal service reform, CTIA supports the creation of a single, unified universal service support mechanism that calculates support based on the forward-looking economic costs of serving customers.[223] Finally, CTIA observes that many of the reform proposals would increase the administrative complexity of the intercarrier compensation rules and universal service systems. Accordingly, CTIA urges the Commission to adopt rules that are simple to administer in order to avoid increased compliance costs than may result in additional charges to consumers.[224]

2. Discussion

60. We commend all the industry parties that have been involved in the process of developing these proposals for their substantial efforts to reach agreement on these complicated issues. It is apparent from these efforts that there is widespread agreement with our assessment that today's intercarrier compensation mechanisms no longer are sustainable. Although there are numerous paths the Commission may take as we begin to reform the current regime, we are encouraged by this acknowledgement of the need for fundamental change.

61. We also commend the work done by NARUC in developing a set of principles that can be used in evaluating these proposals. Many of the principles identified by NARUC are consistent with the policy goals we have identified above. For example, we share NARUC's view that any new plan should be simple to administer, competitively and technologically neutral, and should minimize arbitrage opportunities. We also share NARUC's desire to adopt an approach that ensures reasonable and affordable rates, especially for rural consumers, and that minimizes the impact on universal service support programs.

62. Given the extensive negotiations that formed the basis for some of these proposals, we ask parties to comment on whether it is preferable for the Commission to adopt a single proposal in its entirety, rather than adopting a modified version of any particular proposal or attempting to combine

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[219] *Id*. at 2.

[220] *Id.* at 1-2. Specifically, CTIA appears concerned that, because some of the proposals make universal service funding unavailable to competitors, these proposals would deny the benefits of competition to rural consumers. *Id*. at 2.

[221] *Id.* at 2.

[222] *Id*.

[223] *Id*. at 3.

[224] *Id.*

different components from individual plans.[225] If we were to adopt one proposal or combine different components of the plans, we seek comment on implementation and transition issues for such an approach.

D. Legal Issues

63. As the Commission considers the record developed in response to the NPRM and the specific proposals recently filed in this proceeding, we are mindful of our obligation to comply with the statutory provisions governing intercarrier compensation, such as sections 251(b)(5) and 252(d)(2) of the Act.[226] In addition, we recognize that any unified regime requires reform of intrastate access charges, which are subject to state jurisdiction. We further recognize that reform of the access charge regime must take into account the Commission's rate averaging and rate integration requirements codified in section 254(g) of the Act.[227] In this section, we ask parties to consider these and other legal issues associated with comprehensive reform efforts. Specifically, we ask parties to comment on whether the various reform proposals adequately address the legal issues identified below. In addition, we discuss alternative approaches to intercarrier compensation reform that could be accomplished through changes to our interpretation of the statutory requirements, and ask parties to comment on whether such changes should be adopted, either as a transitional mechanism or as part of a more permanent solution.

1. Section 252(d)(2) "Additional Cost" Standard

64. Section 252(d)(2) sets forth an "additional cost" standard for reciprocal compensation under section 251(b)(5).[228] As discussed above, in the *Local Competition First Report and Order*, the Commission interpreted the "additional cost" standard of section 252(d)(2) to permit the use of the TELRIC cost standard that was established for interconnection and unbundled elements.[229] In this section, we solicit comment on whether this standard is, or could be, satisfied by the various reform proposals. We also solicit comment on a number of alternatives for modifying or replacing the current TELRIC cost standard that could be considered in conjunction with certain of the proposals or as independent alternatives.

a. Comprehensive Proposals

65. Many of the proposals include a specified rate or pricing methodology for the termination of traffic subject to section 251(b)(5). We ask parties to address whether these proposals

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[225]We note that the ICF participants view their plan as a unified proposal that the Commission should adopt "without modification." ICF Proposal at 2. They also would oppose any attempt to adopt individual parts of the plan while "modifying, rejecting, or deferring others." *Id*.

[226]*See* 47 U.S.C. §§ 251(b)(5), 252(d)(2).

[227]*See* 47 U.S.C. § 254(g).

[228]Specifically, section 252(d)(2)(A) states that, for the purpose of incumbent LEC compliance with section 251(b)(5), a state commission shall not consider the terms and conditions for reciprocal compensation to be just and reasonable unless such terms and conditions: (i) provide for the "mutual and reciprocal recovery by each carrier of costs associated with the transport and termination on each carrier's network facilities of calls that originate on the network facilities of the other carrier;" and (ii) "determine such costs on the basis of a reasonable approximation of the additional costs of terminating such calls." 47 U.S.C. §252(d)(2)(A).

[229]*Local Competition First Report and Order*, 11 FCC Rcd at 16023, para. 1054.

satisfy the statutory pricing standard in section 252(d)(2). Except for the CBICC proposal, which supports a TELRIC cost standard, each proposal would require some departure from the Commission's implementation of the section 252(d)(2) "additional cost" standard. The ICF addresses this question in its *ex parte* brief filed in support of its proposal.[230] It contends that a unified bill-and-keep regime, such as that proposed by the ICF, is consistent with section 252(d)(2).[231] Similarly, ARIC maintains that its FACTS proposal would comply with the "additional cost" standard.[232] We ask parties supporting these proposals or others to comment on whether the specified rate or pricing methodology complies with these statutory provisions.

b. Limit recovery under existing rules

66. As noted above, the use of the TELRIC standard for reciprocal compensation has created some problems. If the Commission decides to retain the current TELRIC methodology for reciprocal compensation (*e.g.*, as part of the CBICC plan), we ask parties to address whether we should define more precisely what costs are traffic-sensitive, and thus recoverable through reciprocal compensation charges, and what costs are non-traffic-sensitive, and not recoverable through reciprocal compensation charges. As a first step in providing such guidance, we must be more specific about the meaning of the term "traffic-sensitive." If costs for a portion of the network vary with the number of customers on the network, would those costs be considered "traffic-sensitive"? Or must costs vary with usage of a particular customer to be "traffic-sensitive"?

67. We seek comment on what components of the wireline network should be considered traffic-sensitive. Should the Commission revisit its decision in the *Local Competition First Report and Order* that loop costs are not traffic-sensitive? Should we provide more detail as to which switching components, if any, are traffic-sensitive? In the Commission's pending TELRIC rulemaking,[233] a number of parties have argued that the substantial majority of switching costs do not vary with minutes of use (MOU) and that switching should be offered on a flat-rated basis rather than a per-minute basis.[234] These arguments are consistent with the decisions of a number of state commissions finding that end-office switching costs are not traffic-sensitive and therefore should be recovered on a flat, per-line basis, and not on a per-MOU basis.[235] We ask parties to comment on whether the Commission should reach a similar

[230]*See* ICF Oct. 5 *Ex Parte* Letter, Attach. at 38-42 (filed Oct. 5, 2004) (attaching Ex Parte Brief of the Intercarrier Compensation Forum in Support of the Intercarrier Compensation and Universal Service Reform Plan) (ICF Supporting Brief).

[231]*See id*. Similarly, Western Wireless maintains that the Commission and the states may require bill-and-keep under section 252(d)(d) of the Act. Western Wireless Proposal at 10. *But see* ARIC Proposal at 18-19 (claiming that a mandatory bill-and-keep approach is not permitted under the Act).

[232]ARIC Proposal at 41.

[233]*See TELRIC NPRM*, 18 FCC Rcd at 18953, para. 18.

[234]MCI argues, for example, that vendor contracts for switches establish per-line prices, rather than per-minute prices, and thus LECs do not incur switching costs on a per-minute basis. MCI TELRIC Comments at 30. Similarly, AT&T argues that switches generally have substantial excess capacity so that increases in usage do not increase switching costs. AT&T TELRIC Comments at 73-76.

[235]*See Determination of the Cost of the Unbundled Loop of Qwest Corp*., Docket No. 01-049-85, Report and Order (Utah PSC May 5, 2003); *Re Ameritech Indiana*, Cause No. 40611-51 (Ind. URC Mar. 28 2002); *Investigation into Ameritech Wisconsin's Unbundled Network Elements*, Docket 6720-TI-161, Final Decision (Wisc. PSC Mar. 22,
(continued….)

result with respect to recovery of switching costs for purposes of reciprocal compensation.

68. We invite comment on the proposition that digital switching costs no longer vary with minutes of use due to increased processor capacity. Is this proposition correct for both end office switches and tandem switches? What about competitive LEC switches that have characteristics of both tandems and end offices? To what extent do any capacity constraints become obsolete as carriers migrate to Internet-protocol switching?[236] Parties taking the position that switching costs do vary with minutes of use should identify the specific portions of the switch for which costs increase when minutes of use increase. Similarly, those parties should explain how costs decrease as minutes on the switch decrease. We ask parties to provide objective evidence demonstrating that their switching costs have increased or decreased with MOU.

69. We also solicit comment on which components of a wireless network (*e.g.*, spectrum, cell sites, backhaul links, base station controllers, mobile switching centers) should be considered traffic-sensitive. Would the classification of switching costs on wireline networks as traffic-sensitive or non-traffic-sensitive apply equally to wireless networks? If we retain the rule limiting wireline LECs to recovery of traffic-sensitive switching costs, should we establish a similar limitation on the costs that wireless carriers may recover through reciprocal compensation charges? What are the competitive implications of a finding that wireless networks have more traffic-sensitive costs than wireline networks?[237] Should competitive neutrality play a role in this determination? Should we limit reciprocal compensation recovery to ensure that one type of network is not advantaged by a greater ability to shift costs to other carriers?

70. Once we identify the traffic-sensitive costs, we must determine whether they should be recovered on a per-minute or flat-rated capacity basis.[238] The Commission's UNE rules specify that rate structures reflect the manner in which the costs are incurred.[239] Our rules require that the costs of shared facilities be recovered in a manner that efficiently apportions them among users, either through usage-sensitive charges or capacity-based flat-rated charges.[240] We solicit comment on whether state

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2002); *Commission Review and Investigation of Qwest's Unbundled Network Elements Prices*, Docket No. P-421/CI-01-1375, Order Setting Prices and Establishing Procedural Schedule (Minn. PUC Oct. 2, 2002); *Investigation Into the Compliance of Illinois Bell Telephone Company with the Order in Docket No. 96-0486/0569 Consolidated*, Docket No. 98-0396, Order (Ill. CC Oct. 16, 2001).

[236]For example, we note that Cisco Systems, Inc. has introduced a new router with so much capacity that it can transfer the entire collection of the U.S. Library of Congress in 4.6 seconds. *See* Charles Waltner, *A New Era for Communications Begins with CRS-1* (visited February 11, 2005) http://newsroom.cisco.com/dlls/2004/hd_052504c.html.

[237]*CMRS Termination Compensation Order*, 18 FCC Rcd at 18444-47, paras. 6-16.

[238]State public utility commissions, in applying the Commission's rules governing reciprocal compensation, have generally adopted average per-minute rates.

[239]47 C.F.R. § 51.507(a); *Local Competition First Report and Order*, 11 FCC Rcd at 15874, para. 743.

[240]47 C.F.R. § 51.507(c); *Local Competition First Report and Order*, 11 FCC Rcd at 15878, para. 755. The Commission's rate structure rule for the local switching UNE requires that costs for this element be recovered through a combination of a flat-rated charge for line ports and one or more flat-rated or per-MOU charges for the switching matrix and trunk ports, but it does not specify a particular combination or means for determining the (continued….)

commissions should retain discretion to establish per-minute reciprocal compensation rates, or whether, in light of the harmful consequences of per-minute reciprocal compensation charges,[241] we should require flat-rated recovery of costs, regardless of whether they are traffic-sensitive. If the latter, we solicit comment on how to structure these charges. For example, is a port charge feasible? If so, would a port charge be related to capacity (*e.g.*, DS1 trunk port, DS3 trunk port)? Alternatively, would it be feasible for carriers to provide other carriers with "buckets" of minutes as wireless carriers offer their retail customers?

c. Replace current rules with an incremental cost standard

71. The statutory pricing standard for reciprocal compensation ("additional cost") is not the same as the statutory pricing standard for UNEs (cost plus a reasonable profit) set forth in the Act.[242] Although the Commission decided in the *Local Competition First Report and Order* that the TELRIC pricing methodology satisfied both standards,[243] our subsequent experience suggests that TELRIC is not necessarily consistent with the "additional cost" standard. Specifically, TELRIC measures the *average* cost of providing a function,[244] which is not necessarily the same as the *additional* cost of providing that function.

72. We solicit comment on whether a true incremental cost methodology is more appropriate for establishing "additional costs" under section 252(d)(2).[245] How should we determine what costs are "incremental"? How would we apply an incremental cost methodology to the various components of the network, either wireline or wireless? Is it clear that the incremental cost of loop plant is zero? With respect to switching costs, should we assume that carriers purchase digital switches that are equipped with the capacity to originate and terminate all of the traffic of a carrier's retail customers? If so, are there any switching costs that would be considered incremental? We ask parties to comment on whether the Commission should interpret the "additional cost" standard to be the difference between the long-run forward-looking total cost of a network and that of a network with the same number of subscribers in the same locations that differs only in that it was designed assuming each subscriber makes additional calls.

73. Alternatively, what are the merits of using short-run incremental costs when determining the "additional costs" incurred to terminate calls that originate on another carrier's network? Is there a difference between short-run incremental costs and traffic-sensitive costs? What are the merits of a long-run approach? Would the "additional" costs of terminating traffic under a long-run incremental cost methodology differ significantly from the average costs calculated under TELRIC? Once we identify the relevant incremental costs, how should they be recovered? Should we allow recovery through usage

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appropriate combination. 47 C.F.R. § 51.509(b). *Local Competition First Report and Order*, 11 FCC Rcd at 15878, para. 757.

[241] *See supra* para. 23 n.67

[242] *Compare* 47 U.S.C. § 252(d)(2) *and* 47 U.S.C. § 252(d)(1).

[243] *See Local Competition First Report and Order*, 11 FCC Rcd at 15844-56, 16023, paras. 672-703, 1054.

[244] *See TELRIC NPRM*, 18 FCC Rcd at 18953, para. 18.

[245] We note that the term "additional cost" is found only in one other place in the Act. *See* 47 U.S.C. § 224(d)(1). In that context, the statutory language makes clear that this is an incremental cost standard. *Id*.

sensitive, per-minute charges, or non-traffic-sensitive, flat-rated (per-trunk port) charges?

d. Forbear from section 251(b)(5) compensation requirement

74. We seek comment on whether the Commission could use its authority under section 10 of the Act to forbear from certain aspects of the compensation requirement of section 251(b)(5) as part of any intercarrier compensation reform effort.[246] Section 10 establishes a three-part test to determine whether forbearance is appropriate.[247] In the *Intercarrier Compensation NPRM*, the Commission sought comment on whether the imposition of a bill-and-keep regime would require that it forbear from section 252(d)(2)'s "additional cost" pricing standard and whether the prohibition on forbearance from section 271 makes imposition of bill-and-keep legally problematic.[248] Commenters differ as to whether the Commission can impose a bill-and-keep regime under section 252(d)(2), absent forbearance.[249] They also differ on whether the Commission could exercise its forbearance authority in order to impose a bill-and-keep regime.[250] In this section, we explore further whether our statutory forbearance authority permits us to consider proposed bill-and-keep regimes for traffic subject to section 251(b)(5), regardless of the appropriate construction of sections 251(b)(5) and 252(d)(2). We ask parties to comment on whether the forbearance criteria would be satisfied with respect to the section 251(b)(5) compensation requirement.

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[246]The Commission previously concluded in the *Local Competition First Report and Order* that bill-and-keep is a permissible reciprocal compensation arrangement provided that the traffic exchanged between interconnecting carriers is relatively balanced. *See Local Competition First Report and Order*, 11 FCC Rcd at 16054-55, paras. 111-12. In the *Intercarrier Compensation NPRM,* the Commission sought comment on whether the statute can be read to permit bill-and-keep for all traffic subject to section 251(b)(5), even if it is not balanced. *See Intercarrier Compensation NPRM,* 16 FCC Rcd at 9635-37, 9644-45, paras. 73-77, 97.

[247]Specifically, section 10(a) states that the Commission shall forbear from applying any regulation or provision of the Act to a telecommunications carrier or telecommunications service, or class of carriers or services, in any or some of its or their geographic markets, if it determines that (1) enforcement of such regulation or provision is not necessary to ensure that the charges, practices, classifications, or regulations by, for, or in connection with that telecommunications carrier or telecommunications service are just and reasonable and are not unjustly or unreasonably discriminatory; (2) enforcement of such regulation or provision is not necessary for the protection of consumers; and (3) forbearance from applying such provision or regulation is consistent with the public interest. 47 U.S.C. § 160(a).

[248]*Intercarrier Compensation NPRM,* 16 FCC Rcd at 9637, para. 77. Section 10(d) states that, except as provided in section 251(f), the Commission may not forbear from applying the requirements of sections 251(c) or 271 until it determines that those requirements have been fully implemented. 47 U.S.C. § 160(d).

[249]*Compare* AT&T Reply at 29 (rejecting the notion that bill-and-keep provides for the mutual and reciprocal recovery of costs as required by section 252(d)(2) of the Act) *with* SBC Comments at 44 (arguing that bill-and-keep appears to satisfy section 252(d)(2) of the Act if there is an end user recovery mechanism).

[250]*Compare* AT&T Comments at 39-40 (arguing that the Commission cannot satisfy the forbearance criteria and that forbearance from certain sections of the Act is not possible until it finds that those requirements have been fully implemented) *and* Time Warner Comments at 27-30 (stating that the Commission appears to lack the authority to forbear from certain sections of the Act) *with* Sprint Comments at 21-22 (maintaining that the statutory criteria for forbearance may be satisfied). In addition, NASUCA states that the Commission cannot forbear from applying sections 251 and 252, but it provides no analysis or further explanation to support this position. NASUCA Comments at 29. *See also* Cable & Wireless Reply at 20-21; e.spire and KMC Telecom Reply at 11; Focal *et al*. Reply at 36-37; Taylor Communications Reply at 26.

75. We assume that, if any forbearance were needed to support a bill-and-keep regime, such forbearance would apply only with respect to the compensation requirement of section 251(b)(5) and not to the requirement to enter into reciprocal arrangements for the transport and termination of traffic. Under this approach, state commissions would continue to review interconnection agreements to determine if they meet the requirements of section 251(b)(5), but states no longer would consider, as part of that review, whether the rates for transport and termination of traffic are consistent with the pricing requirements of section 252(d)(2) and our rules. We ask parties to comment on this approach and to identify any new rules or requirements that would be needed to implement such an approach.

76. We seek comment on whether the bar to forbearance contained in section 10(d) precludes exercise of forbearance in this case.[251] On its face, section 10(d) precludes forbearance only until section 251(c) is implemented and is silent with respect to obligations imposed under section 251(b). We note, however, that the predecessor to the Wireline Competition Bureau previously held that section 251(b) obligations are incorporated by reference into section 251(c).[252] Was this holding correct and, if not, should the Commission take this opportunity to reverse it?

77. Assuming that we can forbear from imposing section 251(b) obligations, we solicit comment on whether the Commission also should forbear from enforcing the compensation requirement contained in section 271(c)(2)(B)(xiii). If we forbear from section 251(b)(5), is there any reason not to forbear from section 271(c)(2)(B)(xiii) as well?[253] We seek comment on whether forbearance from section 271(c)(2)(B)(xiii) satisfies the requirements of section 10(a).

2. State Jurisdiction and Joint Board Issues

78. As discussed above, the Commission has authority under section 201 to adopt or modify compensation mechanisms that apply to jurisdictionally interstate traffic and it clearly has authority to modify the pricing methodology that applies to reciprocal compensation under section 252(d)(2).[254] Because access charges for intrastate traffic historically have been an area within the exclusive jurisdiction of state commissions, however, any proposal that includes reform of intrastate mechanisms

[251] 47 U.S.C. § 160(d).

[252] *See Application of GTE Corp., Transferor, and Bell Atlantic Corp., Transferee, For Consent to Transfer Control of Domestic and International Sections 214 and 310 Authorizations and Application to Transfer Control of a Submarine Cable Landing License*, CC Docket No. 98-184, Letter from Carol Mattey, Deputy Chief, Common Carrier Bureau, to Michael L. Shor, Swidler Berlin Shereff Friedman, 16 FCC Rcd 22, 23 (Comm. Car. Bur. 2000).

[253] Section 10(d) precludes forbearance from the requirements of section 271 until they have been fully implemented. Based on the Commission's previous determination that all of the BOCs have fully implemented section 271, *see* Petition for Forbearance of the Verizon Telephone Companies Pursuant to 47 U.S.C. § 160(c), SBC Communications Inc.'s Petition for Forbearance Under 47 U.S.C. § 160(c), Qwest Communications International Inc. Petition for Forbearance Under 47 U.S.C. § 160(c), BellSouth Telecommunications, Inc. Petition for Forbearance Under 47 U.S.C. § 160(c), WC Docket Nos. 01-338, 03-235, 03-260, and 04-48, Memorandum Opinion and Order, FCC 04-254, paras. 12, 15 (rel. Oct. 27, 2004), section 10(d) does not bar the Commission from forbearing from the compensation requirement contained in section 271(c)(2)(B)(xiii) if forbearance otherwise meets the requirements of section 10.

[254] *See AT&T v. Iowa Utils. Bd.*, 525 U.S. 366, 385 (1999) (holding that the Commission has jurisdiction to design a pricing methodology to be applied under section 252(d) of the Act).

must address the Commission's legal authority to implement such reform.

79. In the 1996 Act, Congress adopted section 251(b)(5) which, on its face, applies to all telecommunications. As noted above, however, Congress "carved out" access traffic from the scope of section 251(b)(5).[255] In the *Local Competition First Report and Order*, the Commission found that the section 251(g) carve-out includes intrastate access services.[256] Based on this statement in the *Local Competition First Report and Order* and the Commission's authority under section 251(g) to supersede that carve-out,[257] we ask parties to comment on whether the Commission has authority to replace intrastate access regulation with some alternative mechanism. If so, must the mechanism comply with the requirements of sections 251(b)(5) and 252(d)(2)?

80. We also seek comment on alternative legal theories under which the Commission could reform intrastate access charges. For example, under the "mixed use" doctrine, traffic is treated as jurisdictionally interstate if it is impossible or impractical to separate the interstate and intrastate components.[258] We ask parties to comment on whether this same analysis applies to other types of traffic, such as calls that originate or terminate with other types of VoIP service or on a CMRS network. With the advent of intermodal number portability, how, practically, can one be sure of a customer's physical location? Does the inability to determine the actual geographic end points of a call provide a basis on which to conclude that the intrastate component of certain types of traffic is not severable from the interstate component? If it becomes impossible or impractical to determine the end points of a substantial portion of traffic, would that justify a finding that all traffic should be treated as jurisdictionally interstate for purposes of intercarrier compensation? Do certain characteristics of IP-enabled services counsel interstate treatment for intercarrier compensation purposes, such as the inseverability of multiple features that can be accessed simultaneously, the irrelevance of geography to the provisioning and use of the service, or the lack of service-related reasons to incorporate geographic or jurisdictional tracking systems into the IP network?

81. We recognize that some of the industry proposals call for a cooperative process between the Commission and states, which may minimize concerns about this Commission's jurisdiction. For instance, the ARIC proposal calls for a joint process to establish unified compensation rates and both the

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[255] 47 U.S.C. § 251(g).

[256] *Local Competition First Report and Order*, 11 FCC Rcd at 15869, para. 732.

[257] 47 U.S.C. § 251(g). (providing for continued enforcement of exchange access and interconnection agreements "… until such restrictions and obligations are explicitly superseded by regulations prescribed by the Commission after the date of such enactment.")

[258] *See MTS and WATS Market Structure, Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board*, CC Docket Nos. 78-72, 80-286, Decision and Order, 4 FCC Rcd 5660, n.7 (1989) (*MTS/WATS Market Structure Separations Order*) (the Commission found that "mixed use" special access lines carrying more than a de minimis amount of interstate traffic to private line systems are subject to the Commission's jurisdiction because traffic on many such lines could not be measured without "significant additional administrative efforts") *See also Petition For Declaratory Ruling That pulver.com's Free World Dialup Is Neither Telecommunications Nor A Telecommunications Service*, WC Docket No. 03-45, Memorandum Opinion and Order, 19 FCC Rcd 3307, at 16 (2004) (finding Pulver's Free World Dialup (FWD) service to be analogous to services subject to the "mixed use" doctrine).

ARIC and CBICC proposals would involve a Joint Board.[259] We solicit comment on whether the Commission should refer any of the issues related to intrastate access charges to a Federal-State Joint Board, as ARIC and CBICC suggest.[260] Under section 410(c) of the Act, the Commission is required to refer "any proceeding regarding the jurisdictional separation of common carrier property and expenses between interstate and intrastate operations" to a Federal-State Joint Board.[261] In addition, that same statutory provision permits the Commission to refer "any other matter relating to common carrier communications of joint Federal-State concern."[262] Do any of the issues addressed in this Further Notice fall within the scope of the mandatory referral requirement of section 410(c)?

82. The ICF maintains that the Commission already has the authority to address intrastate access reform by virtue of sections 201, 251(b)(5), and 254 of the Act.[263] According to the ICF, section 201 gives the Commission authority to implement section 251(b)(5), which covers compensation for all telecommunications involving a LEC, including intrastate telecommunications.[264] In addition, the ICF argues that the Commission may assert preemptive authority over intrastate traffic under section 254.[265] It claims that the Commission "can and should preempt intrastate access charges on the ground that they are inconsistent with the Commission's duty under section 254 to rationalize universal service support."[266] We take our charge under section 254 seriously, but are also mindful of the states' historical authority over charges for intrastate services. Accordingly, we seek comment on the legal analysis presented by these proposals concerning the Commission's authority over intrastate access reform, and specifically whether the changes wrought by the 1996 Act give the Commission the power to assert authority over the intrastate charges at issue in this proceeding.

3. Rate Averaging and Integration Requirements

83. In section 254(g), Congress codified the Commission's pre-existing geographic rate averaging and rate integration policies.[267] The Commission implemented section 254(g) by adopting two

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[259] *See* ARIC Proposal at 37-38; CBICC Proposal at 2. The EPG plan would reduce intrastate access rates to interstate rate levels but does not explain how the Commission could require such reductions.

[260] *See* ARIC Proposal at 37-38, 56-57; CBICC Proposal at 2. *See also* NARUC Principles at 4 (suggesting that the Commission refer issues to the Joint Board in order to ensure state input). The ICF takes the position that its plan may be adopted without a joint board referral. *See* ICF Supporting Brief at 45 n.73.

[261] 47 U.S.C. § 410(c).

[262] *Id*.

[263] *See* ICF Supporting Brief at 28-38.

[264] *Id*. at 28-32.

[265] *Id.* at 35-38. Section 254 of the Act governs universal service support and Commission duties relating to universal service. *See* 47 U.S.C. § 254.

[266] ICF Supporting Brief at 35.

[267] *See Policy and Rules Concerning the Interstate, Interexchange Marketplace*, CC Docket No. 96-61, Report and Order, 11 FCC Rcd 9564, 9566-67, paras. 3-5, 9568–69, para. 9 *(Geographic Rate Averaging Order)* (citing S. Rep. No. 230, 104th Cong., 2d Sess. 1) (1996)).

requirements.[268] First, providers of interexchange telecommunications services are required to charge rates in rural and high-cost areas that are no higher than the rates they charge in urban areas.[269] This is known as the geographic rate averaging rule. Second, providers of interexchange telecommunications services are required to charge rates in each state that are no higher than those in any other state.[270] This is known as the rate integration rule.

84. In the *Geographic Rate Averaging Order*, the Commission explained that geographic rate averaging benefits rural areas by providing access to a nationwide telecommunications network at rates that do not reflect the disproportionate burdens that may be associated with recovery of common line costs in rural areas.[271] The Commission also noted that geographic rate averaging ensures that rural customers will share in lower prices resulting from nationwide interexchange competition.[272] Similarly, the Commission enunciated that its policy of integrating "offshore points" such as Hawaii and Alaska into the mainland's interstate interexchange rate structure brings the benefits of growing competition to the entire nation.[273]

85. Under the Commission's rate averaging and rate integration requirements, IXCs bear the burden of averaging on a nationwide basis the different per-minute switched access rates charged by LECs. This results in an implicit subsidy flowing from customers in low-cost areas served by IXCs to customers in high-cost service areas. The Commission historically has taken steps to facilitate IXC compliance with these requirements. For example, the averaging of the CCL charge in the NECA pool and the subsequent adoption of the LTS mechanism each reduced the access rate differentials that IXCs had to accommodate in their interstate long-distance rates.[274]

86. Absent some further reform of the access charge regime, we are concerned that the rate averaging and rate integration requirements eventually will have the effect of discouraging IXCs from serving rural areas. These requirements may place IXCs that serve rural areas at a competitive disadvantage to those that focus on serving urban areas. For instance, the BOCs offer long-distance services only within their regions and not to customers served by high-cost rural LECs. Nationwide IXCs such as AT&T, on the other hand, offer long-distance services in both urban and rural areas, including areas served by rural LECs. We are thus concerned that the competitive realities of the marketplace may drive increasing specialization of companies serving rural as opposed to non-rural areas, ultimately leading to higher costs and fewer competitive choices for rural consumers. We ask parties to comment on the relationship between the rate averaging and rate integration requirements and the access charge reform

[268] *Id.* at 9565-66, para. 2.

[269] 47 C.F.R. § 64.1801; *see Geographic Rate Averaging Order,* 11 FCC Rcd at 9568-69, para. 9, 9574, para. 20.

[270] 47 C.F.R. § 64.1801; *see Geographic Rate Averaging Order,* 11 FCC Rcd at 9588, para. 52.

[271] *Geographic Rate Averaging Order,* 11 FCC Rcd at 9567, para. 6.

[272] *Id*.

[273] *Id*. at 9588, para. 52.

[274] *See Access Charge Order,* 93 FCC 2d at 328, paras. 314-15*; MTS and WATS Market Structure Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board*, CC Docket No. 78-72, CC Docket No. 80-286, Report and Order, 2 FCC Rcd 2953, 2956 para. 24 (1987).

proposals described above. Do any of the proposals ease concerns about the disparate impact of rate averaging and rate integration requirements on nationwide IXCs? If not, are there additional steps the Commission should take to address these concerns? For example, are there circumstances where the Commission should forbear from the rate averaging and rate integration requirements? Or is section 254 amenable to an interpretation that would permit the Commission to treat a portion of the high costs of interstate local switching and transport as universal service? Parties are asked to comment on the legality of such an interpretation and the desirability of taking such an approach.

E. Network Interconnection Issues

1. Background

87. Under section 251(c)(2)(B), an incumbent LEC must allow a requesting telecommunications carrier to interconnect at any technically feasible point.[275] The Commission has interpreted this provision to mean that competitive LECs have the option to interconnect at a single point of interconnection (POI) per LATA.[276] In addition, our rules preclude a LEC from charging carriers for traffic that originates on the LEC's network.[277] For traffic subject to section 251(b)(5) of the Act, our rules permit a terminating carrier to recover from the originating carrier the cost of certain facilities from an "interconnection point" to the called party.[278] In the *Intercarrier Compensation NPRM*, the Commission solicited comment on whether an incumbent LEC should be obligated to bear its own costs of delivering traffic to a single POI when that POI is located outside the calling party's local calling area.[279] Alternatively, the Commission asked whether a carrier should be required to interconnect in every local calling area or pay the incumbent transport and/or access charges if the location of the single POI requires transport beyond the local calling area.[280] The Commission also sought comment on

[275] 47 U.S.C. § 251(c)(2)(B).

[276] *Application by SBC Communications Inc., Southwestern Bell Tel. Co. and Southwestern Bell Communications Services, Inc., d/b/a Southwestern Bell Long Distance pursuant to Section 271 of the Telecommunications Act of 1996 to Provide In-Region, InterLATA Services in Texas*, CC Docket No. 00-65, Memorandum Opinion and Order, 15 FCC Rcd 18354, 18390, para. 78 n.174 (2000).

[277] 47 C.F.R. § 51.703(b). At least two courts have held that this rule applies even in cases where an incumbent LEC delivers calls to a POI located outside its customer's local calling area. *See Southwestern Bell Tel. Co. v. Public Utils. Comm'n of Texas*, 348 F.3d 482, 486-87 (5th Cir. 2003); *MCImetro Access Transmission Services, Inc. v. BellSouth Telecommunications, Inc*., 352 F.3d 872, 881 (4th Cir. 2003). Local calling areas are established or approved by state commissions. *Local Competition First Report and Order*, 11 FCC Rcd at 16013-14, para. 1035.

[278] Specifically, our rules permit recovery of the costs of transport and termination of telecommunications traffic between LECs and other telecommunications carriers. 47 C.F.R. § 51.701. The rules define "transport" as the "transmission and any necessary tandem switching of telecommunications traffic subject to section 251(b)(5) of the Act from the interconnection point between the two carriers to the terminating carrier's end office switch that directly serves the called party, or equivalent facility provided by a carrier other than an incumbent LEC." *Id.* § 51.701(c). The rules define "termination" as the "switching of telecommunications traffic at the terminating carrier's end office switch, or equivalent facility, and delivery of such traffic to the called party's premises." *Id.* § 51.701(d).

[279] *Intercarrier Compensation NPRM*, 16 FCC Rcd at 9651, para. 113.

[280] *Id.* The Commission also asked whether its regulations permit the imposition of access charges for calls that originate and terminate within one local calling area but cross local area boundaries due to the placement of the POI. *Id*.

whether current rules result in inefficient network design by forcing the originating LEC to bear the cost of transport outside the local calling area, or whether requiring competitors to establish multiple POIs or pay for transport beyond the local calling area forces competitive carriers to replicate the incumbent LEC network.[281]

88. In addition to these specific questions, the Commission sought comment on two working papers describing bill-and-keep approaches to intercarrier compensation and default interconnection rules that would apply when carriers cannot agree on the terms for interconnection.[282] Under the Central Office Bill and Keep (COBAK) approach, no carrier may recover any costs of its customers' local access facilities from interconnecting carriers, and the calling party's network is responsible for the cost of transporting the call to the end office serving the called party.[283] This approach would require the calling party's network to construct transport facilities to the called party's end office or purchase transport facilities or services from another carrier (including possibly the called party's network). Under the Bill Access to Subscribers – Interconnection Cost Split (BASICS) approach, networks would recover all intra-network costs from their end-user customers and divide equally the costs that result from interconnection.[284] The BASICS approach would require networks to distinguish between intra-network costs and the incremental costs of interconnection.[285]

89. In response to the *Intercarrier Compensation NPRM*, most competitive LECs and CMRS providers urge the Commission to maintain the single POI per LATA rule.[286] They argue that the current rule prevents incumbent LECs from imposing costly and burdensome interconnection requirements, thereby creating barriers to entry.[287] According to these commenters, a rule requiring competitors to interconnect in every local calling area or pay for transport to the POI outside the local calling area would essentially require new entrants to replicate the existing incumbent LEC network, regardless of whether it is efficient to do so.[288] Competitive LECs emphasize that they are willing to establish additional POIs

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[281] *Id.* at 9652, para. 114.

[282] *See id.* at 9620-22, paras. 22-30.

[283] *Id.* at 9620-21, para. 23.

[284] *Id.* at 9621, para. 25.

[285] *Id*. at 9622, para. 28.

[286] *See, e.g.*, Cbeyond Comments at 9; Focal *et al*. Comments at 56; Global NAPs Comments at 7 n.11; Level 3 Comments at 28; PCIA Comments at 30; Sprint Comments at 29; Time Warner Comments at 15; WorldCom Comments at 8l; AT&T Wireless Reply at 29; e.spire and KMC Reply at 14-15; Focal *et al*. Reply at 43; Level 3 Reply at 3; PCIA Reply at 11; Taylor Communications Reply at 34; VoiceStream Reply at 31-32; WebLink Wireless Reply at 17. Some CMRS providers maintain that they should not be required to maintain more than one POI per MTA. *See* CTIA Comments at 34; PCIA Comments at 30; Arch Wireless Reply at 7.

[287] *See* AT&T Comments at 57; Cablevision Lightpath Comments at 5; Time Warner Comments at 14; AT&T Reply at 36-37; AT&T Wireless Reply at 30.

[288] *See* Cablevision Lightpath Comments at 3; PCIA Comments at 31; AT&T Reply at 36; Focal *et al*. Reply at 43; Taylor Communications Reply at 36. *See also* Letter from Patrick H. Merrick, Director, Regulatory Affairs, AT&T, to William Caton, Acting Secretary, Federal Communications Commission, CC Docket No. 01-92, at 11 (filed May 1, 2002) (claiming that mirroring the incumbent LEC network is not economic for new entrants and will stifle competition) (AT&T May 1 *Ex Parte* Letter).

when traffic levels warrant them,[289] and they contend that any additional transport costs are minimal in any event.[290]

90. As discussed in the *Intercarrier Compensation NPRM*, the incumbent LECs support a requirement that competitive carriers establish a POI in each local calling area or pay the transport costs to reach a POI outside the local calling area.[291] Incumbent LECs argue that, under the current rules, they bear a disproportionate amount of transport costs when a competitive LEC primarily terminates traffic and the recipient of the traffic is located near the competitive LEC's switch.[292] The competitive LECs and many CMRS providers oppose the idea of paying for transport and contend that the incumbent LEC should be required to deliver all traffic originating on its network to the selected POI at no charge.[293] Other commenters suggest that the interconnecting carrier selecting the POI be responsible for some portion of the transport costs to a POI located outside the local calling area, or that the interconnecting carrier establish additional POIs once certain criteria are met.[294] These commenters propose different criteria for establishing additional POIs, including specific traffic volume or distance thresholds.[295]

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[289] *See* Allegiance Comments at 27; AT&T Comments at 59; Time Warner Comments at 14; WorldCom Comments at 22; AT&T Reply at 37; WorldCom Reply at 8; AT&T May 1 *Ex Parte* Letter at 12. They reason that additional POIs increase network reliability, and that network planners and engineers are in the best position to determine when additional POIs are warranted. *See* Allegiance Comments at 27-28.

[290] *See* PCIA Comments at 32.

[291] *See Intercarrier Compensation NPRM*, 16 FCC Rcd at 9651, para.112. *See also* MECA Comments at 44; SBC Comments at 18-19. *But see* Focal *et al*. Reply at 44-45 (pointing out that the incumbent LECs appear to support a single POI per LATA rule in the context of bill-and-keep). In addition, SBC argues that the single POI per LATA rule diminishes competitive LEC incentives to build their own networks. SBC Comments at 18. *But see* AT&T Reply at 37 (arguing that the existence of numerous POIs belies SBC's assertions).

[292] *See* Letter from Karen Brinkmann, Counsel to CenturyTel, Inc., to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket Nos. 96-98, 99-68, and 01-92, Attach. at 1-2 (filed Sept. 30, 2004); Letter from Donna Epps, Vice President, Federal Regulatory Advocacy, Verizon, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket Nos. 99-68 and 01-92, at 2-3 (filed Dec. 16, 2004). *See also* Time Warner Reply at 28 (explaining that "free riding" can occur when a competitive LEC terminates more traffic than it originates and the recipient of the traffic is located near the competitive LEC's switch, thereby forcing the originating carrier to bear a disproportionate amount of transport costs).

[293] *See* Advanced Paging, *et al*. Reply at 5-6; AT&T Reply at 34; Cablevision Lightpath Reply at 8. *See also* AT&T May 1 *Ex Parte* Letter at 6. Indeed, some commenters maintain that the interconnection "at any technically feasible point" language in section 251(c)(2)(B) of the Act precludes the Commission from modifying this rule. *See, e.g*., Allegiance Comments at 26-27; AT&T Comments at 56; AT&T Reply at 34; Taylor Communications Reply at 34-35. Thus, they maintain that each carrier should bear all transport costs on its side of the POI.

[294] *See* CenturyTel Comments at 31-32; Sprint Comments at 29-30; Texas Commission Comments at 11. AT&T Wireless, for instance, suggests that the carriers share (split) the transport costs because such an approach will encourage both parties to negotiate efficient POIs. *See* AT&T Wireless Reply at 29-30. *See also* Time Warner Reply at 29 (suggesting that the Commission establish a presumption that the current rules apply if the traffic originates and terminates in the same local calling area, and permit the states to address "outlier" situations).

[295] *See* Level 3 Comments at 29; Sprint Comments at 31 (suggesting a combined traffic volume and distance threshold); Texas Commission Comments at 12 (supporting a traffic volume threshold); Level 3 Reply at 24-25 (supporting a default traffic volume threshold). *See also* Time Warner Comments at 14 (stating that it agreed to establish additional POIs once traffic volumes reach a DS1 threshold).

2. Discussion

91. The comments confirm that issues related to the location of the POI and the allocation of transport costs are some of the most contentious issues in interconnection proceedings.[296] In particular, the record suggests that there are a substantial number of disputes related to how carriers should allocate interconnection costs, particularly when the physical POI is located outside the local calling area where the call originates or when carriers are indirectly interconnected. These disputes arise in part because of a lack of clarity among the various rules governing the costs of interconnection facilities and the relationship of those rules to the single POI rule.[297] In addition, our current rules may encourage traffic imbalances because terminating networks not only collect reciprocal compensation, they also avoid financial responsibility for transport facilities. When traffic is out of balance, the cost of interconnection is borne primarily by the originating carrier, and the terminating carrier may lack the incentive to minimize the transport costs associated with connecting the two networks.[298] For instance, competitive LECs appear to have targeted customers that primarily or solely receive traffic, such as ISPs, in order to become net recipients of traffic.[299]

92. In this Further Notice, we solicit additional comment on changes to our network interconnection rules to accompany proposed changes to the intercarrier compensation regimes. The record contains a number of different proposals concerning the responsibility for network interconnection costs. For example, BellSouth asks that we establish a default POI at the incumbent LEC's tandem office and hold each carrier responsible for transport costs on its side of the POI.[300] Qwest proposes a POI at the "edge" of the network, with each carrier responsible for costs on its side of the POI.[301] Qwest identifies

[296] *See, e.g.*, Sprint Comments at 29 (urging the Commission to provide more definitive default rules concerning the obligations of carriers to establish POIs and the responsibility for transport costs); Level 3 Reply at 22-23 (asking the Commission to clarify its POI rules); PCIA Reply at 11 (stating that clarification of the interconnection rules is "long overdue"); Time Warner Reply at 28 (requesting that the Commission ensure that competitors are able to take advantage of the efficiencies of a single POI in a LATA without "free riding" on the incumbent LEC network).

[297] We note that there are petitions for declaratory ruling pending before the Commission that raise issues related to the responsibility for interconnection costs under our existing rules. *See Comment Sought on Sprint Petition for Declaratory Ruling Regarding the Routing and Rating of Traffic by ILECs*, CC Docket No. 01-92, Public Notice, 17 FCC Rcd 13859 (2002); *Pleading Cycle Established for Comments on @ Communications Petition for Declaratory Ruling*, CC Docket No. 02-4, Public Notice, 17 FCC Rcd 1010 (2002). We will clarify the application of our current rules when we address these petitions.

[298] *See* Sprint Comments at 29.

[299] *Intercarrier Compensation NPRM*, 16 FCC Rcd at 9616, para. 11. In such situations, the originating carrier bears the cost of interconnection to the single POI selected by the competitive LEC in addition to paying reciprocal compensation for the termination of traffic. Because ISP customers rarely, if ever, originate traffic, there is little traffic flow in the opposite direction, and the originating carrier bears the majority of the interconnection costs between the two carriers.

[300] *See* Letter from W.W. Jordan, Vice President – Federal Regulatory, BellSouth, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, at Attach. (filed June 14, 2002). Similarly, Verizon proposes default interconnection points at incumbent LEC tandem wire centers. *See* Verizon Reply at 13-18.

[301] *See* Letter from John W. Kure, Executive Director – Federal Policy and Law, Qwest Communications International, Inc., to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, at Attach. (filed Aug. 2, 2002).

specific locations for the "edge" of the network depending on the network and/or the type of interconnecting carrier.[302] Similarly, the ICF proposes a new approach to network interconnection based on carrier "Edges."[303] As discussed above, the ICF plan establishes default technical and financial rules that generally require an originating carrier to deliver traffic to the "Edge" of a terminating carrier's network.[304]

93. We ask parties to comment on the network interconnection proposals in the record and on the ICF's proposed default network interconnection rules.[305] Is the level of detail proposed by the ICF appropriate for inclusion in federal rules, or would it be better for the Commission to establish more general requirements that leave the details to be negotiated between the carriers? What are the costs and benefits of establishing different interconnection rules for hierarchical, non-hierarchical, and CRTC networks, as the ICF proposes? Is this approach philosophically consistent with the goal of a unified regime? Is this a sensible way to approach interconnection between different types of networks, or are there other factors we should consider?

94. We also seek comment on whether the Commission should consider different network interconnection rules for small incumbent LECs or rural LECs.[306] Would different network interconnection rules for small incumbent LECs or rural LECs serve the Commission's goals of promoting economic efficiency and facilities-based competition? Would a rule requiring competitors to pay for transport outside the local calling area to the POI essentially require new entrants to replicate the existing incumbent LEC network, regardless of whether it is efficient to do so? Further, is such an approach competitively and technologically neutral given the different network architectures of competitive networks, including wireless networks?

95. Other proposals, such as the ARIC, CBICC, and NASUCA proposals, do not address changes to the existing network interconnection rules. If we do not adopt the ICF proposal, we seek comment on whether to retain our existing network interconnection rules as part of our reform efforts or whether we should consider alternative methods of determining financial responsibility for network interconnection costs. Parties that support retention of the existing network interconnection rules should address the issues arising under the current rules (as described above) and also the impact of any particular compensation reform proposal on the existing network interconnection rules. Parties that do not support retention of our existing network interconnection rules should comment on alternative methods of determining financial responsibility for network interconnection costs.

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[302]*Id*.

[303]*See* ICF Proposal at 3-31. *See also supra* para. 40.

[304]*See* ICF Proposal at 4-9.

[305]In addition, we note that the default network interconnection rules proposed by Western Wireless appear to be based, in part, on the ICF's "Edge" approach. *See* Western Wireless Proposal at 12. For interconnection between hierarchal incumbent LECs and other carriers, the Western Wireless proposal permits interconnection at the carrier "edge" or under a shared transport arrangement at the option of the competitive carrier. *Id.*

[306]For example, under the EPG proposal, the incumbent LEC would not be responsible for delivering traffic or paying any costs to a POI located outside the incumbent LEC's contiguous service area or beyond the serving area boundary. EPG Proposal at 33.

96. We also solicit comment on whether changing our pricing methodology for reciprocal compensation, as proposed above, will have any effect on the incentives of competitive carriers, including CMRS providers, to establish multiple POIs. For example, if the Commission adopts a bill-and-keep approach and competitors pay the same rate (zero) to terminate calls wherever they connect to the incumbent LEC network, will there be incentives to interconnect at more than one POI per LATA? If reducing reciprocal compensation rates also reduces the incentive to establish multiple POIs, is there a need for the Commission to establish ground rules to facilitate more efficient interconnection? Parties proposing to require competitive carriers to establish multiple POIs per LATA should explain clearly what standards they would apply and provide objective evidence demonstrating the reasonableness of their proposal.

97. Finally, we ask parties to address whether any additional rule changes are needed to harmonize the network interconnection rules that apply to section 251(b)(5) traffic with the rules that apply to access traffic. For example, if we adopt a unified rate that applies to all types of traffic but retain interconnection rules that vary by type of traffic, carriers still may have an incentive to classify traffic as one type or the other in order to reduce their share of the interconnection costs. Should different rules apply to interconnection facilities connecting an IXC POP and a LEC switch?

F. Cost Recovery Issues

1. Interstate Access Charges

a. Price Cap LECs

98. By any measure, interstate access charges imposed on IXCs by price cap carriers have declined significantly over the years. At the time the original access charge regime was adopted, the average interstate traffic-sensitive switching rate was 3.1 cents per minute and the average total access charge was 17.26 cents per minute.[307] Most recent figures show the average interstate traffic-sensitive rate to be 0.48 cents per minute and the average total access charge to be 1.44 cents per minute.[308] Notwithstanding these reductions, access charges continue to represent a significant revenue source for these carriers and a significant cost component for IXCs.[309]

99. Many of the reform proposals include mechanisms by which some carriers will be permitted to offset revenues previously recovered through interstate access charges.[310] Other proposals question the need to offset revenues and oppose proposals that include revenue guarantees or assumptions

[307] *Telephone Trends Report*, Table 1.2. These figures represent the average rates (weighted by minutes of use) for all LECs that file access tariffs subject to price-cap regulation and all LECs in the National Exchange Carrier Association (NECA) pool.

[308] *Id.*

[309] In 2003, BOC interstate access revenues for switching amounted to approximately $1.8 billion. Source: Automated Reporting Management Information System (ARMIS) Annual Summary Report (FCC Report 43-01), Table 1, Cost and Revenue (1996-2003).

[310] For instance, the ICF Proposal calls for increased SLCs and two new universal service recovery mechanisms. *See* ICF Proposal at 69-74.

concerning revenue neutrality.[311] We solicit comment on whether these mechanisms, or something comparable, must be adopted if we reduce or eliminate the ability of LECs to impose interstate switched access charges on IXCs. What is the Commission's legal obligation to provide alternative cost recovery mechanisms? Would the elimination of interstate switched access charges be confiscatory in the absence of such mechanisms? Should carriers be required to demonstrate that they will be unable to recover their switching and transport costs from other sources before we establish such mechanisms? For instance, NASUCA states that the Commission "should not assume that preservation of the current levels of access revenues is justified without any explanation of the financial need of the carriers."[312]

100. If we conclude that alternative cost recovery mechanisms are needed, we solicit comment on the various proposals that have been submitted. The ICF proposal, for example, includes elaborate rules designed to ensure that any revenue reductions are offset by new revenue opportunities.[313] In considering the ICF and other proposals, we ask parties to address whether the Commission is legally obligated to make any transition to a new compensation regime revenue neutral for the affected carriers. Should we define revenue neutrality based on a carrier's actual earnings, the authorized rate of return of 11.25 percent, or some other measure?[314] Does this obligation extend only to incumbent LECs, or does it apply to other carriers as well? If revenue neutrality is not mandatory, what criteria should we use in calculating the revenue opportunity that should be provided to LECs? How should revenue received from other wholesale services be factored into this analysis? What about new revenue opportunities (or cost reductions) that might be expected to arise if there were no more access charges? We encourage price cap carriers, both individually and collectively, to provide data regarding the amount of revenue that would be lost if the Commission no longer permits the imposition of interstate access charges. We also encourage price cap companies to provide data regarding the cost reductions they would experience if they no longer had to pay to terminate calls on other carriers' networks.

101. Two of the proposals rely primarily on two mechanisms – subscriber charges and some form of universal service support – for offering price cap carriers the opportunity to recover costs previously recovered from IXCs through interstate switched access charges.[315] We ask parties to comment on whether the Commission should rely solely on end-user charges, or whether it also should rely on universal service support mechanisms (new or existing) to offset revenues no longer recovered through interstate access charges. If additional recovery is permitted through federal subscriber charges, how should such charges be implemented? Specifically, we question whether it is realistic to institute a regulated SLC for years to come, when market conditions may not allow carriers to charge such a SLC. Is there sufficient competition in the marketplace to allow us to eliminate the SLC cap and permit price

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[311]See NASUCA Proposal at 2; Western Wireless Proposal at 18. *See also* CTIA Principles at 1-2.

[312]NASUCA Proposal at 2.

[313]*See* ICF Proposal at 51-54.

[314]*See Represcribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers*, CC Docket No. 89-624, Order, 5 FCC Rcd 7507 (1990) (the Commission prescribes for the interstate access services of local exchange carriers an authorized, overall rate of return on investment of 11.25 percent). *See* 47 C.F.R. § 65.700.

[315]*See, e.g.*, CBICC Proposal at 2; ICF Proposal at 48.

cap LECs to charge end users whatever the market will bear?[316] Would such a finding preclude the need for any additional universal service funding for price cap carriers? If such an option is not feasible today, under what circumstances might it become feasible? We also solicit comment on the extent to which SLCs lead to inefficient charges by serving as a pricing umbrella for competitive LECs.

102. If a cap on federal subscriber charges is needed, we ask parties to comment on the level at which the cap should be set if the jurisdictionally interstate costs of providing switched access no longer are recovered from IXCs through access charges. For example, are the rate caps proposed by the ICF appropriate?[317] Parties advocating a cap on subscriber charges are encouraged to provide data regarding elasticity of demand for telephone service and the number of subscribers that would be expected to terminate service if the cost of subscribership increases. If there is evidence that increased subscription costs would cause users to terminate service, would it make sense to give carriers the option to offer calling plans targeted to low usage customers that would impose federal subscriber charges on a per-minute or per-call basis?[318]

103. We ask parties to discuss what type of findings the Commission must make before using additional universal service funding to offset lost access charge revenues. Must carriers demonstrate that they are unable to recover interstate-allocated costs in the absence of such funding? To the extent that the Commission provides additional universal service support, how should such an approach be implemented? Should additional funding be made available through existing universal service support mechanisms or is it necessary to create an entirely new mechanism? We note that some of the proposals include cost recovery through a combination of the existing universal service support mechanisms and new sources of support.[319]

104. Commenters should also address the competitive neutrality of any new proposed universal service mechanism with respect to competitive eligible telecommunications carriers. For example, some of the proposals appear to limit additional support to certain types of carriers.[320] Parties that favor additional or alternative universal service support funding should be explicit in proposing how much additional funding is needed for price cap LECs, how they calculate such amounts, and how such funding should be raised and distributed.

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[316]Under the ARIC proposal, the current SLC caps would continue, but would be redesigned to recover both non-traffic sensitive and traffic sensitive costs. ARIC Proposal at 68-69. Rural carriers would bill SLCs at the weighted average residential and business SLCs for the price cap carriers in each state. *Id*. at 68.

[317]*See* ICF Proposal at 60-63.

[318]*See* Michael H. Riordan, *An Economist's Perspective on Universal Residential Telephone Service, in*, The Internet Upheaval: Raising Questions, Seeking Answers in Communications Policy, 309-30 (Ingo Vogelsang and Benjamin M. Compaine, eds. MIT Press, 2000).

[319]For instance, the EPG proposal appears to retain the existing universal service support, while including a new additional source of support via the "Access Restructure Charge." EPG Proposal at 22. Similarly, the ARIC proposal would retain existing federal universal service support and add a new SEF. ARIC Proposal at 71-88.

[320]*See, e.g.*, ICF Proposal at 73 (stating that the TNRM recovery mechanism is available only to a CETC that has lost access revenue); EPG Proposal at 22-23 (stating that the new ARC charge is available only to regulated carriers for usage of their local networks). *But see* Western Wireless Proposal at 15 (proposing new support that would be fully portable to all designated ETCs operating in a geographic area).

105. We solicit comment on alternative approaches that would give LECs the opportunity to recover costs previously recovered from IXCs through interstate access charges. Would some sort of flat-rated connection charge on IXCs, as proposed by EPG, be appropriate either as an end in itself, or as a transition to a regime that depends solely on subscriber charges and universal service support? Would it be feasible simply to allow IXCs to subscribe to a LEC's tariffed retail services, as we have done with ISPs under the ESP exemption? Parties that favor an approach based on flat-rated charges should be specific in identifying what costs should be recovered from IXCs, how these charges should be calculated, and the length of any transition period.

106. We ask parties to comment on the impact on consumers of replacing access charges with additional subscriber charges and/or universal service support. To the extent reduced access charges lead to reduced retail rates for interexchange services, what would be the net impact on consumers? Would it be necessary for the Commission to require IXCs to pass through reductions in access charges? Or is such an approach unnecessary given the competitive state of the interexchange market? How, if at all, does the growing prevalence of bundled "all distance" offerings affect the ultimate costs and benefits for end-user customers of a proposal to eliminate interstate access charges? Should we be concerned if high-volume users reap most of the benefits of such a proposal? Should additional funding for Lifeline service be made available to offset the impact of such a proposal on low-volume, low-income consumers?

b. Rate-of-Return LECs

107. As compared to price cap LECs, rate-of-return LECs derive a much greater share of their revenue from access charges. According to NTCA, rural LECs receive on average, 10 percent of their revenue from interstate access charges and 16 percent from intrastate access charges.[321] In comparison, it asserts that the BOCs receive only four percent of their revenue from interstate access charges and six percent from intrastate access charges.[322]

108. Because many rate-of-return LECs depend so heavily on access charge revenue, some of the proposals submitted in this proceeding include special provisions for these carriers. For example, under the ICF proposal, the TNRM support mechanism for rate-of-return CRTCs is based on a revenue requirement rather than on line count.[323] We seek comment on the extent to which the Commission should give rate-of-return LECs the opportunity to offset lost access charge revenues with additional universal service funding, additional subscriber charges, or some combination of the two. If we eliminate SLC caps for price cap LECs, should we do the same for rate-of-return LECs? Or is such an approach not yet justified given the more limited competition that exists in most rural areas? If we authorize additional federal subscriber charges, should such charges be subject to the same caps, if any, that apply to price cap

[321] Letter from Scott Reiter, National Telecommunications Cooperative Association (NTCA), to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, at 7 (filed Jan. 7, 2004) (NTCA Jan. 7 *Ex Parte* Letter). Fred Williamson states that rural LECs in Kansas receive 37 percent of their revenue from interstate access charges and 12 percent from intrastate access charges, while rural LECs in Oklahoma receive 28 percent of their revenue from interstate access charges and 42 percent from intrastate access charges. *See* Letter from Tom Karalis, Fred Williamson & Associates, Inc., to Marlene H. Dortch, Secretary, Federal Communications Commission, RM-10822, CC Docket Nos. 96-45 and 02-361, at Tab 2 (filed Jan. 7, 2004) (opposing the Western Wireless Petition on Elimination of Rate-of-Return Regulation of Incumbent LECs).

[322] NTCA Jan. 7 *Ex Parte* Letter at 8.

[323] *See* ICF Proposal at 54, 73.

LECs?[324] Should we also adopt some sort of benchmark for local retail rates within the state jurisdiction, as proposed by ARIC?[325] We encourage parties to make specific proposals as to how any additional end-user charges should be calculated.

109. To the extent the Commission decides that additional universal service support also is necessary, we seek comment on how much additional support we must provide and how such support should be distributed. Should rate-of-return carriers be required to demonstrate that they are unable to recover their interstate-allocated costs from other sources before we authorize any additional universal service funding? Or should the Commission adopt a support mechanism that fixes or caps the amount of support at a level estimated by the Commission as necessary to achieve its goals?

110. If we conclude that additional universal service funding is necessary, one possible approach would be to provide such funding through the ICLS mechanism. Under such a methodology, ICLS would be expanded to include not just common line costs, but also switching and transport costs. Alternatively, the Commission could create a new interstate access support mechanism. With respect to any proposed support methodologies, commenters should provide a detailed explanation as to how support should be calculated and the administrative burdens involved. In particular, parties should address the amounts of universal service funding that would be required under the various proposals described above. NTCA stated that $884 million would be needed to offset lost interstate access revenues if the Commission adopts a bill-and-keep regime.[326] EPG states that there will be a $900 million revenue shortfall under its plan, although this appears to be entirely associated with intrastate rate reductions.[327] Interstate revenues would remain the same under the EPG plan, but would be recovered through flat-rated charges, rather than per-minute charges for some rate elements.[328] We seek comment on the accuracy of these estimates and the validity of the underlying assumptions. Commenters should also address the competitive neutrality of any new proposed universal service mechanisms with respect to competitive eligible telecommunications carriers.

111. We ask parties to comment on the impact on rural consumers of replacing access charges with additional universal service support and/or subscriber charges. NTCA states that currently rural consumers tend to make more interexchange calls than urban customers (because there are fewer customers in their local calling areas) and that IXCs do not always offer their lowest priced calling plans in rural areas.[329] Substantially reducing the access charges imposed on IXCs has the potential to resolve both these issues in a manner that benefits rural consumers. If interexchange rates decline with reductions in access charges, as we would expect in a competitive marketplace, rural customers could benefit even more than urban customers from a transition to a regime with substantially lower intercarrier payments.

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[324]*See supra* paras. 101-02.

[325]*See* ARIC Proposal at 61-62.

[326]NTCA Jan. 7 *Ex Parte* Letter at slide 61.

[327]*See* Letter from Glenn H. Brown, Expanded Portland Group, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, Attach. at 15 (filed May 12, 2004) (EPG May 12 *Ex Parte* Presentation).

[328]EPG Proposal at 31-32.

[329]NTCA March 2004 White Paper at 16-21.

In addition, reductions in access charges would eliminate barriers to IXCs entering rural markets and offering their lowest priced calling plans. Furthermore, to the extent access charge revenues decline, and long-distance prices decline, are LECs more likely to offer long distance services in lieu of providing only access services? We seek comment on whether and to what extent the benefits of reduced access charges would offset the burden associated with any additional subscriber charges that might be imposed.

112. With respect to rate-of-return LECs in particular, we recognize that an approach that retains some intercarrier payments from IXCs for switched access services may be appropriate. The CBICC, ARIC, EPG, and Home/PBT proposals call for unified termination rates based on different cost methodologies or on existing rates, that will remain in effect indefinitely.[330] Similarly, NASUCA proposes a interim regime based on target rates to be established by the Commission.[331] The ICF proposes a specific, declining termination rate, although even this plan includes some rates that would remain indefinitely.[332] Western Wireless proposes to eliminate per-minute compensation rates using targeted reductions over a four-year period, with a longer transition period for small rural incumbent LECs.[333] In addition to these proposals, parties should comment on whether the $0.0095 rate adopted in the *CALLS Order* might be an appropriate rate, either as a transitional rate or as an end point. Parties suggesting a different rate should explain why that rate would be more appropriate. Parties suggesting that multiple rates should be adopted should specify the rates to be used and the parameters that would determine the rates a carrier could charge.

113. If we were to adopt a target rate proposal, such as that proposed by NASUCA, either as a transition or for an indefinite duration, parties should address whether there is a need to establish rules governing how that rate should be distributed among the different access categories or rate elements and, if so, what those rules should be. In this connection, commenters should pay particular attention to the potential that, in the absence of such rules, rate-of-return LECs could target reductions to areas they perceived to be subject to the most competitive risk. Parties should also address whether the definition of average traffic sensitive rates in section 61.3(e) should apply to rate-of-return LECs, or whether conditions unique to rate-of-return LECs require development of a different definition.[334]

2. Intrastate Access Charges

114. If the Commission acts to reduce or eliminate intrastate switched access charges, it may be necessary to give price cap and rate-of-return LECs the opportunity to offset those revenue losses with alternative cost recovery mechanisms. As with interstate access charges, the two primary mechanisms for doing this are increased subscriber charges and increased universal service funding. We ask parties to comment on how these mechanisms should be structured to give LECs the opportunity to offset lost

[330] *See* ARIC Proposal at 37 (proposing rates based on embedded costs); CBICC Proposal at 1 (proposing TELRIC-based rates); EPG Proposal at 21 (proposing rates based on interstate access levels); Home/PBT Proposal at 14 (proposing connection-based intercarrier charges capped at the national average retail fee for a standard business line).

[331] NASUCA Proposal at 1.

[332] ICF Proposal at 36-38.

[333] Western Wireless Proposal at 13.

[334] 47 C.F.R. § 61.3(e).

intrastate access charge revenue. In sections II.F.1.a and II.F.1.b above, we solicit comment on a number of important questions related to replacing interstate switched access charges with additional universal service funding and subscriber charges. We ask parties to address these same questions as they relate to intrastate access charges.

115. If the states reduce access charges as part of a comprehensive reform effort adopted by the Commission, issues may arise as to whether the Commission or the state is responsible for establishing an alternative revenue source. Under the ARIC proposal, for example, additional universal service support would come from both federal and state sources, but it would be distributed by the states.[335] We seek comment on whether the Commission should create a federal mechanism to offset any lost intrastate revenues, or whether the states should be responsible for establishing alternative cost recovery mechanisms for LECs within the intrastate jurisdiction. We ask parties to provide specific proposals that identify the amount of revenue at issue, how such calculations were made, and the specific means by which recovery should be made available. In the event that the Commission thinks that a federal mechanism should be created to offset intrastate access charge revenue reductions, should the Commission refer to the Federal-State Joint Board on Universal Service issues related to the establishment and design of that mechanism?

G. Implementation Issues

116. Under our access charge regime, the rates, terms and conditions under which carriers provide interstate access services are generally contained in tariffs filed with this Commission.[336] In contrast, the exchange of traffic under section 251(b)(5) is governed by interconnection agreements.[337] We seek comment on how to reconcile these two approaches if we move to a unified rate for all types of traffic. Is a regime based solely on agreements feasible if the Commission retains intercarrier payments for origination and termination of traffic? What would be the default compensation rule if parties exchanged traffic in the absence of some type of interconnection agreement? While price cap LECs have ample experience with the negotiation and arbitration of such agreements, the same is not true for all rate-of-return LECs because new entrants have been slower to enter their service areas. In addition, many rate-of-return LECs may be exempt from some of the requirements of section 251 by virtue of the rural exemption in section 251(f).[338] We ask parties to identify any unique obstacles that may arise for rate-of-return LECs in connection with a regime based solely on agreements and to propose solutions to overcome those obstacles. For example, is it possible to develop something comparable to the pooling process that takes place for carriers that participate in the NECA tariff? If not, are there other mechanisms available to rate-of-return LECs to guard against the risks pooling is designed to reduce? We also ask parties to discuss how regulation of intercarrier payments for interexchange traffic would operate with respect to LECs that have received a suspension or modification of the requirements of section 251(b) pursuant to section 251(f)(2).

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[335] *See* ARIC Proposal at 76-80.

[336] 47 U.S.C. § 203. Competitive LECs are permitted, at their option, to file tariffs for interstate access services at rates at or below a prescribed benchmark. They are subject to mandatory detariffing with respect to rates above that benchmark. *See CLEC Access Charge Recon. Order*, 18 FCC Rcd at 9110-11, para. 4.

[337] 47 U.S.C. §§ 251, 252.

[338] 47 U.S.C. § 251(f).

117. Many of the proposals submitted in this record include some sort of transition period to give carriers sufficient time to make necessary changes in their business operations. Given the substantial changes that are possible in this rulemaking, we seek comment on what type of transition would be needed for a new regime. What type of transition would be needed if we reduced, but did not eliminate, interstate switched access charges? Should one component of any such transition be conversion of per-minute charges to flat-rated charges that better reflect the manner in which switching costs are incurred? Parties should be specific in proposing time frames and milestones that would be part of any transition to a new access charge regime. Further, if the Commission has legal authority to reduce or eliminate intrastate access charges, should intrastate access charges be reduced or eliminated on the same schedule as interstate access charges, or would it be better to give states more flexibility in light of the role they historically have played in addressing these issues?

118. Parties also should address whether there are any adverse consequences associated with transitioning rate-of-return LECs toward a new unified regime at a slower pace than price cap LECs. For example, are there arbitrage issues associated with maintaining a rate differential between rural and non-rural LECs? Does such an approach place nationwide long distance carriers at a competitive disadvantage relative to IXCs that focus on lower cost areas (*e.g.*, the BOCs)?

119. Some rate-of-return LECs state that they are not authorized to provide interexchange services.[339] If the Commission moves to reduce, and possibly eliminate, the imposition of access charges by rate-of-return LECs, is there any reason for states to prohibit them from providing toll services? Would preemption of any such prohibitions be appropriate under section 253 of the Act, which generally prohibits state and local governments from preventing any carrier from providing any intrastate or interstate telecommunications service?[340] Parties should discuss the benefits that might accrue to rural customers if all rate-of-return LECs were permitted to provide interexchange services.

H. Additional Issues

1. Transit Service Issues

a. Background

120. Transiting occurs when two carriers that are not directly interconnected exchange non-access traffic by routing the traffic through an intermediary carrier's network.[341] Typically, the intermediary carrier is an incumbent LEC and the transited traffic is routed from the originating carrier through the incumbent LEC's tandem switch to the terminating carrier. The intermediary (transiting) carrier then charges a fee for use of its facilities. Although many incumbent LECs, mostly BOCs,

[339] *See, e.g.,* Letter from Sylvia Lesse, Counsel to the Missouri Companies, to William F. Caton, Acting Secretary, Federal Communications Commission, CC Docket No. 01-92, at 6 (filed Mar. 22, 2003); Letter from Glenn H. Brown, Great Plains Communications, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, at 8 (filed Sept. 23, 2003); Letter from W.R. England, III, Counsel to the Missouri Small Rural Incumbent Local Exchange Companies, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, at 3 (filed Oct. 31, 2003).

[340] 47 U.S.C. § 253.

[341] The exchange of access traffic, including the joint provision of access by two or more carriers, is governed by federal and state access charge rules.

currently provide transit service pursuant to interconnection agreements,[342] the Commission has not had occasion to determine whether carriers have a duty to provide transit service. The reciprocal compensation provisions of the Act address the exchange of traffic between an originating carrier and a terminating carrier, but the Commission's reciprocal compensation rules do not directly address the intercarrier compensation to be paid to the transit service provider.[343]

121. In the *Intercarrier Compensation NPRM*, the Commission sought comment on issues that arise under the current intercarrier compensation rules when calls involve a transit service provider, and how a bill-and-keep regime might affect such calls.[344] Specifically, the Commission sought comment on the transport obligations of interconnected LECs and whether it should allow LECs to charge each other for delivering transit traffic that originates on the networks of other carriers.[345] The Commission recognized that CMRS carriers also originate and terminate section 251(b)(5) traffic that transits incumbent LEC networks, and requested comment on the issues or problems that the current rules present for these calls.[346] In this section, we solicit further comment on whether there is a statutory obligation to provide transit services under the Act, and, if so, what rules the Commission should adopt to advance the goals of the Act.

122. Incumbent LECs argue that they are not required to provide transit service under the Act and that transit service offerings should remain voluntary.[347] They explain that they limit the availability

[342]Indeed, the record suggests that most BOCs currently offer transit service to competitive LECs and CMRS providers pursuant to agreements. *See, e.g.*, Verizon Reply at 26-27.

[343]*See* 47 U.S.C. § 252(d)(2)(A)(i) (requiring that the terms and conditions for reciprocal compensation provide for the "recovery by each carrier of costs associated with the transport and termination on each carrier's network facilities of calls that originate on the network facilities of the other carrier").

[344]*Intercarrier Compensation NPRM*, 16 FCC Rcd at 9634, para. 71. In a related proceeding, Qwest had argued that a bill-and-keep arrangement does not work when three carriers are involved in the transport and termination of traffic because the carrier providing the transit service does not have a customer involved in the call from which it can recover costs. *Id.* (citing Letter from Lynn R. Charytan, Counsel for Qwest Communications International, Inc. to Magalie R. Salas, Secretary, Federal Communications Commission, CC Docket Nos. 96-98 and 99-68, App. B, at ii (filed Nov. 22, 2000)). *See also* Qwest Reply at 25 n.14 (clarifying that its concern applied only to the situation where the intermediary carrier has no relationship with the end-user, and, therefore, cannot recover its costs from the end-user).

[345]*Intercarrier Compensation NPRM*, 16 FCC Rcd at 9634, para. 71.

[346]*See id*.

[347]*See* MITG Reply at 9-10; SBC Reply at 19; Verizon Reply at 25-26. *See also* Letter from Glenn Reynolds, Vice President, Federal Regulatory, BellSouth Corporation, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92 at 6 (filed Aug. 29, 2003) (BellSouth Aug. 29 *Ex Parte* Letter); Letter from Glenn Reynolds, Vice President, Federal Regulatory, BellSouth Corporation, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92 (filed May 16, 2003) (attaching Letter from Glenn Reynolds, Vice President, Federal Regulatory, BellSouth Corporation, to William Maher, Chief, Wireline Competition Bureau, Federal Communications Commission, CC Docket No. 01-92 at 3 (filed May 15, 2003) (BellSouth May 16 *Ex Parte* Letter); Letter from Joseph Mulieri, Executive Director – Federal Affairs, Verizon, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92 at 2-6 (filed June 13, 2003) (Verizon June 13 *Ex Parte* Letter); Letter from Joseph Mulieri, Assistant Vice President, Federal Regulatory (continued….)

of such services in order to prevent traffic congestion and tandem exhaust, and to encourage carriers to establish direct interconnection when traffic volumes warrant it.[348] According to these commenters, transiting should be treated as an unregulated service offered at market-based prices, or, alternatively, as special access.[349]

123. Competitive LECs and CMRS providers argue that incumbent LECs are required to provide transit service under the Act,[350] and they urge the Commission to ensure continued access to transit service.[351] These carriers explain that indirect interconnection via a transit service provider is the most efficient means of interconnection and that the availability of transiting is critical to the development of competition.[352] CMRS providers in particular argue that the low volume of traffic exchanged with smaller LECs does not warrant direct interconnection and that transit service is necessary for indirect interconnection.[353] These commenters urge the Commission to set cost-based compensation for transit

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Advocacy, Verizon, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, at 2-4 (filed Sept. 4, 2003) (Verizon Sept. 4 *Ex Parte* Letter).

[348]Verizon Reply at 26-27. *See also* Verizon June 13 *Ex Parte* Letter at 6; Verizon Sept. 4 *Ex Parte* Letter at 6. Moreover, the smaller incumbent LECs complain that the larger incumbent LECs, *i.e*., the BOCs, have entered into transiting arrangements with other carriers, whereby the BOC delivers traffic destined for a rural LEC to that LEC for termination without authorization or any agreement among all the carriers involved. *See* Alliance of Incumbent Rural Telephone Companies and Independent Alliance Reply at 6-7. They further argue that such transiting arrangements preempt any opportunity for the small incumbent LEC to establish an agreement with the originating carrier and provide interconnection services. *See id.* at 7; MITG Reply at 9.

[349]*See* SBC Reply at 19 (advocating market-based rates); USTA Reply at 22 (arguing that transit service should be treated as an unregulated service or, in the alternative, treated as special access); Verizon Reply at 27 (advocating market-based rates); BellSouth Aug. 29 *Ex Parte* Letter at 11 (supporting market-based rates); Verizon Sept. 4 *Ex Parte* Letter at 2 (supporting market-based rates). *Cf.* MITG Reply at 11-15 (arguing that access charges must apply to transit service because three carriers are involved in the call rather than two).

[350]*See* Sprint Comments at 34 (relying on sections 251(a) and 251(c)(2)(B) of the Act); AT&T Reply at 48 (discussing sections 251(a) and 251(c)(2)(B) of the Act); VoiceStream Reply at 22 (citing section 251(a) of the Act). *See also* Letter from Laura H. Phillips, Counsel to Nextel Communications, Inc. and T-Mobile USA, Inc., to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92 at Attach. (filed May 16, 2003) (stating that sections 251(a)(1), 251(b)(5), 251(c) and 332(c) of the Act require incumbent LECs to provide transit service at cost-based rates) (Nextel/T-Mobile May 16 *Ex Parte* Letter).

[351]*See* Triton Comments at 13; Verizon Wireless Comments at 42-44; AT&T Reply at 48; Nextel Reply at 10; Sprint Reply at 16-18; Triton Reply at 8-9; Verizon Wireless Reply at 16; VoiceStream Reply at 22.

[352]*See* Sprint Comments at 33; Triton Comments at 13-14; AT&T Reply at 48; Nextel Reply at 10; Sprint Reply at 16-17; Triton Reply at 9; VoiceStream Reply at 22. In response to claims that transiting hinders the development of facilities-based competition, Sprint responds that duplicating incumbent LEC facilities would only impose unnecessary costs on new entrant carriers. *See* Sprint Reply at 17.

[353]*See* Triton Comments at 13-14 (arguing that transiting traffic is the only economically justifiable way for a CMRS provider to exchange traffic in rural areas); Verizon Wireless Comments at 43 (stating that transiting is the best way to ensure cost-effective service availability to rural customers); Nextel Reply at 10 (asking the Commission to ensure that indirect transit traffic arrangements remain a viable option because indirect interconnection is far more efficient in circumstances where a relatively small volume of traffic is exchanged); Triton Reply at 8-9 (urging the Commission to facilitate indirect interconnection through transiting arrangements); VoiceStream Reply at 22 (stating that CMRS carriers do not have the traffic volumes to justify direct connections).

service using the Commission's forward-looking TELRIC cost methodology.[354]

124. In addition to these comments, several of the reform proposals include new rules addressing the regulation of transit services. For instance, the ICF proposal includes, as part of its network interconnection rules, a finding that tandem transit service is an interstate common carrier offering subject to regulation by the Commission.[355] Under this proposal, incumbent LECs already providing transit service would continue to offer the service for the entire term of the ICF plan.[356] The ICF plan also includes a clarification of carrier responsibilities in a transit service arrangement and specified rate caps for transit services, which vary depending on the stage of the ICF plan.[357] In contrast, under the CBICC proposal, transit service providers would charge TELRIC-based rates for the functions provided.[358] Under the Western Wireless proposal, incumbent LECs would be required to offer transit service at capped rates.[359]

b. Discussion

125. The record suggests that the availability of transit service is increasingly critical to establishing indirect interconnection – a form of interconnection explicitly recognized and supported by the Act.[360] It is evident that competitive LECs, CMRS carriers, and rural LECs often rely upon transit service from the incumbent LECs to facilitate indirect interconnection with each other. Without the continued availability of transit service, carriers that are indirectly interconnected may have no efficient means by which to route traffic between their respective networks.

126. Moreover, it appears that indirect interconnection via a transit service provider is an efficient way to interconnect when carriers do not exchange significant amounts of traffic.[361] Competitive LECs and CMRS carriers claim that indirect interconnection via the incumbent LEC is an efficient form of interconnection where traffic levels do not justify establishing costly direct connections. As AT&T explains, "transiting lowers barriers to entry because two carriers avoid having to incur the costs of constructing the dedicated facilities necessary to link their networks directly."[362] This conclusion appears to be supported by the widespread use of transiting arrangements.

[354]Sprint Comments at 35; Sprint Reply at 18; VoiceStream Reply at 25.

[355]*See* ICF Proposal at 25.

[356]*See id*. Further, a carrier seeking to discontinue offering tandem transit service would need to obtain section 214 authorization under the ICF plan. *Id*.

[357]*Id*. at 25-29. Moreover, the ICF proposal includes certain traffic volume limitations and other restrictions in situations of tandem congestion or exhaust. *Id.* at 30-31.

[358]*See* CBICC Proposal at 2.

[359]Western Wireless Proposal at 12.

[360]*See* 47 U.S.C § 251(a)(1).

[361]*See* Triton Comments at 13-14; AT&T Reply at 48; Nextel Reply at 10; Sprint Reply at 17; Triton Reply at 8-9; VoiceStream Reply at 22.

[362]AT&T Reply at 48.

127. We seek comment on the Commission's legal authority to impose transiting obligations. For example, competitive LECs and CMRS carriers point to sections 251(a)(1) and 251(c)(2)(B) of the Act in support of transiting obligations.[363] AT&T and Sprint contend that the language in section 251(a) regarding indirect interconnection requires carriers to provide transiting arrangements.[364] In addition, these carriers rely on the "at any technically feasible point" language in section 251(c)(2)(B) in support of transiting obligations.[365] They explain that interconnection at the tandem switch provides access to the full tandem switching functionality, including access to subtending end offices owned by carriers other than the tandem provider.[366] Furthermore, Sprint points to the language of section 251(c)(2)(a), requiring incumbent LECs to interconnect with requesting carriers for the "transmission and routing of telephone exchange service and exchange access," to support transiting obligations.[367]

128. Under section 251(a) of the Act, telecommunications carriers "should be permitted to provide interconnection pursuant to section 251(a) either directly or indirectly, based upon their most efficient technical and economic choices."[368] The Commission's rules define the term "interconnection" to mean "the linking of two networks for the mutual exchange of traffic" and not "the transport and termination of traffic."[369] We seek comment on whether that definition applies, or should apply, in the context of section 251(a).[370] In particular, we ask parties to comment on whether the statutory language regarding the duty to interconnect directly or indirectly under section 251(a) should be read to encompass an obligation to provide transit service. To whom would that implied obligation run?[371] Parties commenting on this issue should address the positions raised in the record and any other arguments concerning the Commission's legal authority to impose transiting obligations. For instance, we seek

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[363] 47 U.S.C. § 251(a)(1) (requiring telecommunications carriers to "interconnect directly or indirectly with the facilities and equipment of other telecommunications carriers"); 47 U.S.C. § 251(c)(2)(B) (requiring incumbent LECs to provide interconnection "at any technically feasible point within the carrier's network").

[364] Sprint Comments at 34; AT&T Reply at 48. *See also* VoiceStream Reply at 22. For instance, Sprint states that 251(a)(1) becomes "meaningless" if the BOCs can ignore their transiting obligations. *See* Letter from Luisa L. Lancetti, Vice President, Regulatory Affairs, Sprint, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92 at 6 (filed Aug. 6, 2003) (Sprint Aug. 6 *Ex Parte* Letter). *But see* Verizon June 13 *Ex Parte* Letter at 2 (arguing that nothing in the Act requires Verizon to accept and transport traffic destined for a third party carrier).

[365] Sprint Comments at 34; AT&T Reply at 48.

[366] Sprint Comments at 34; AT&T Reply at 48.

[367] Sprint Aug. 6 *Ex Parte* Letter at 6 (citing 47 U.S.C. § 251(c)(2)(A)).

[368] *Local Competition First Report and Order*, 11 FCC Rcd at 15991, para. 997 (defining interconnection obligations under section 251(a)).

[369] 47 C.F.R. § 51.5. *See also Local Competition First Report and Order*, 11FCC Rcd at 15590, para. 176 (interpreting section 251(c)(2) of the Act).

[370] 47 U.S.C. § 251(a).

[371] For example, if two carriers choose to meet their obligation under section 251(a) by interconnecting directly, should each be obligated to pass traffic to other carriers through the direct connection?

comment on whether a transiting obligation could also arise under section 251(b)(5)[372] or other sections of the Act, including section 201(a).[373] Parties should also identify and address other regulatory implications of the Commission's conclusions on this issue.[374]

129. Assuming that the Commission has the necessary legal authority, we solicit comment on whether we should exercise that authority to require the provision of transit service. We recognize that many incumbent LECs, mostly BOCs, voluntarily provide transit service pursuant to interconnection agreements. These carriers argue that there is no need to adopt rules for transit service.[375] The record suggests, however, that some carriers may experience difficulty in obtaining transit service,[376] and the record is silent on whether transit service is currently available at reasonable rates, terms, and conditions. We acknowledge the concerns of competitors that the unavailability of transit service at reasonable rates, terms, and conditions could pose a barrier to entry, and we also recognize the importance of identifying and implementing appropriate interconnection incentives for the future. Thus, we seek additional comment on the extent to which providers (including non-incumbent LECs) make transit service available in the marketplace at reasonable rates, terms, and conditions, and the extent to which rules implementing transit service obligations are warranted at this time. In this regard, we seek comment on the possibility that mandated transiting or regulated rates for such service might discourage the development of this market. Conversely, we seek comment on whether any rules adopted should encourage the provision of transit service by carriers other than incumbent LECs and, if so, how.

130. If rules regarding transit service are warranted, we seek comment on the scope of such regulation. Specifically, we seek comment on whether transit service obligations under the Act should extend solely to incumbent LECs or to all transit service providers, including competitive LECs.[377] Parties advocating that any rules should apply exclusively to incumbent LEC transit service should address whether the regulation of some transit service providers but not others would create arbitrage risks or result in an unfair competitive advantage.

131. We also seek comment on the need for rules governing the terms and conditions for transit service offerings. In particular, we seek comment on whether limitations on transit service obligations should be considered and the legal authority for imposing such limitations if transit service

[372] *See* 47 U.S.C. § 251(b)(5) (requiring that LECs establish reciprocal compensation arrangements for the transport and termination of telecommunications).

[373] *See* 47 U.S.C. § 201(a) (giving the Commission the authority to establish physical connections and through routes if it, after opportunity for hearing, finds such action necessary or desirable in the public interest).

[374] For example, a determination that incumbent LECs have a transiting obligation pursuant to section 251(c)(2) would also trigger an obligation to provide such a service under section 271(c)(2)(B)(i).

[375] *See* Verizon Reply at 26 (stating that carriers will offer transit service where it is economical for them to do so). *See also* USTA Reply at 22 (stating that the better policy option is to permit all carriers the ability to offer transit service as an unregulated service).

[376] Sprint Comments at 33 (stating that some BOCs have refused, or announced their intention to refuse, to provide indirect interconnection or transiting). *See also* Triton Comments at 13 (describing difficulties experienced in trying to obtain transit arrangements).

[377] The source of legal authority affects the scope of the obligation. *See supra* para. 128 (seeking comment on which section of the Act provides legal authority for the imposition of transiting service obligations).

rules are adopted. For instance, if a transit service obligation is imposed, indirectly interconnected carriers may lack the incentive to establish direct connections even if traffic levels warrant it.[378] As mentioned above, some incumbent LECs currently limit the availability of transit services in order to prevent traffic congestion and tandem exhaust, and to encourage carriers to establish direct interconnection when traffic volumes warrant it.[379] We ask parties to comment on whether similar limitations should apply to any transit service obligations, and under what conditions.

132. Further, if the Commission determines that rules governing transit service are warranted, we seek additional comment on the appropriate pricing methodology, if any, for transit service. The reciprocal compensation provisions of the Act address the exchange of traffic between two carriers, but do not explicitly address the intercarrier compensation to be paid to the transit service provider for carrying section 251(b)(5) traffic.[380] Similarly, section 251(a)(1) does not address pricing. Most commenters agree that incumbent LECs should be compensated for transit service, but they disagree as to the appropriate pricing methodology for this service.[381] Thus, we seek further comment on the appropriate pricing methodology, including the possibility of requiring that transit service be offered at the same rates, terms, and conditions as the incumbent LEC offers for equivalent exchange access services (*e.g.*, tandem switching and tandem switched transport) and how this option would be affected by our proposals to alter the current switched access regime.[382] Moreover, if transit service is treated as an access service, we seek comment on whether pricing flexibility could be obtained based on our existing rules, and seek input on the appropriate test to determine when pricing flexibility would be appropriate. Parties should provide evidence of the degree to which there is, or could be, competition for transit services and how the level of competition should be reflected in our choice of a pricing methodology. Further, we ask parties to comment on whether the efficient pricing of transit service would eliminate the need for any explicit limitations on transit obligations, *i.e.*, whether the correct price signals would encourage direct connections when necessary.

133. Finally, we recognize that the ability of the originating and terminating carriers to determine the appropriate amount and direction of payments depends, in part, on the billing records generated by the transit service provider. Thus, we ask carriers to comment on whether the current rules and industry standards create billing records sufficiently detailed to permit the originating and terminating

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[378] *See* Verizon Reply at 27 (arguing that limitations are necessary to provide the incentive for direct connections between carriers).

[379] *See, e.g.*, Verizon Reply at 26-27. Verizon, for instance, offers transit service and tandem switching of transit traffic up to a DS-1 capacity level and offers special access arrangements for traffic above a DS-1 level. *Id.* at 27.

[380] *See* 47 U.S.C. § 251(b)(5); 47 U.S.C. § 252(d)(2)(A)(i) (requiring that the terms and conditions for reciprocal compensation provide for the "recovery by each carrier of costs associated with the transport and termination on each carrier's network facilities of calls that originate on the network facilities of the other carrier").

[381] The Illinois Commission supports cost-based rates for transit service, but it does not advocate a specific pricing methodology. Illinois Commission Comments at 10. It supports market-based rates once "sufficient competition develops." *Id.* at 9.

[382] *See* MITG Reply at 11 (concluding that, if reciprocal compensation rates do not apply to this traffic, then access rates must apply).

carriers to determine the appropriate compensation due.[383] For instance, although current billing records include call detail information, it is unclear whether and to what extent these billing records include carrier identification information. We seek further comment on the extent to which billing information in a transiting situation may be inadequate to determine the appropriate intercarrier compensation due, and we ask carriers to identify possible solutions to the extent that billing problems exist today.[384] Specifically, we request comment about whether to impose an obligation on the transiting carrier to provide information necessary to bill, including both the identity of the originating carrier, and the nature of the traffic.[385] Parties should explain whether this obligation to exchange information is necessary if we move to a bill-and-keep regime. In the absence of such information, it may be difficult for carriers exchanging traffic indirectly to identify each other and to determine the type and quantity of traffic that they exchange with each other. This may affect not only the exchange of compensation between the parties, but also may hinder the ability to establish direct connections. Parties should address whether such solutions are best implemented by this Commission, industry organizations, or some combination of the two.

2. CMRS Issues

a. The IntraMTA Rule

134. In the *Local Competition First Report and Order*, the Commission stated that traffic to or from a CMRS network that originates and terminates within the same Major Trading Area (MTA)[386] is subject to reciprocal compensation obligations under section 251(b)(5), rather than interstate or intrastate access charges.[387] The Commission reasoned that, because wireless license territories are federally authorized and vary in size, the largest FCC-authorized wireless license territory, *i.e.*, the MTA, would be the most appropriate local service area for CMRS traffic for purposes of reciprocal compensation under section 251(b)(5).[388] Thus, section 51.701(b)(2) of the Commission's rules defines telecommunications

[383]For example, VoiceStream complains that it does not always receive the information it needs to bill the originating carrier for traffic it terminates, and asks us to direct tandem switch owners to provide the identity of the carrier to be billed with each call. VoiceStream Reply at 26. VoiceStream claims that the SS7 signaling in use has never been modified to identify and convey in the trunk signaling messages the carrier to be billed. *Id.*

[384]In the VoIP context, for instance, Level 3 suggests using the Originating Line Information (OLI), also known as ANI II, SS7 call set-up parameter to identify IP-enabled services traffic. *See* Letter from John T. Nakahata, Counsel for Level 3, to Marlene H. Dortch, Secretary, Federal Communications Commission, WC Docket Nos. 03-266 and 04-36, at 2-3 (filed Sept. 24, 2004). Moreover, the EPG proposal in this proceeding includes support for a "Truth-in-Labeling" policy. *See* EPG Proposal at 16-17.

[385]In certain situations, obligating the transiting carrier to pass on the billing information in its records may not be sufficient. For example, the transiting carrier may be aware of the identity of the originating carrier, based on the facilities over which it receives the traffic, and of the trunk group (local exchange service or exchange access) that carries the traffic, even though that information is not formally recorded in the billing record. Under the ARIC reform proposal, the tandem owner would be responsible for compensation payments in the case of unidentified traffic. *See* ARIC Proposal at 55.

[386]The definition of an MTA can be found in section 24.202(a) of the Commission's rules. 47 C.F.R. § 24.202(a).

[387]*Local Competition First Report and Order*, 11 FCC Rcd at 16014, para. 1036.

[388]*Id.*

traffic exchanged between a LEC and a CMRS provider that is subject to reciprocal compensation as traffic "that, at the beginning of the call, originates and terminates within the same Major Trading Area."[389]

135. The purpose of the intraMTA rule is thus to distinguish access traffic from section 251(b)(5) CMRS traffic. Given our goal of moving toward a more unified regime, we seek comment on whether the Commission should eliminate the intraMTA rule. We note that many of the proposals would eventually eliminate the intraMTA rule and treat CMRS traffic the same as all other wireline traffic for compensation purposes.[390] Parties that support maintaining the intraMTA rule or some modification of that rule should address why a CMRS-specific approach is necessary or desirable in light of our goal of adopting a more unified regime. Commenters should also discuss the impact of eliminating the intraMTA rule prior to the adoption of a new unified regime. Parties that advocate eliminating the intraMTA rule should discuss the effect such a change would have on existing compensation arrangements if we maintain separate reciprocal compensation and access charge regimes.

136. We further invite commenters to discuss how parties should determine which LEC-CMRS calls are subject to reciprocal compensation in the absence of the intraMTA rule. Are wireline local calling areas the appropriate geographic scope for both LEC-originated and CMRS-originated reciprocal compensation calls? Assuming so, how should the end-point of the mobile call be determined? In the *Local Competition First Report and Order*, the Commission suggested that the cell-site in use at the beginning of the call or the point of interconnection might be used as proxies for the location of the mobile caller.[391] Should these continue to be alternatives in the absence of the intraMTA rule? If not, what other methods exist for determining whether calls are subject to reciprocal compensation or access charges? Should these methods also be used to determine the appropriate intercarrier compensation for calls between two wireline carriers to ensure a unified regime? Can these methods be applied to transited traffic, such that terminating incumbent LECs will be able to distinguish reliably between terminated traffic subject to reciprocal compensation (for which they will charge the CMRS carriers) and access traffic (for which they would presumably charge the IXC)? We seek comment on these questions.

137. We also note that carriers have disagreed regarding the meaning of the existing intraMTA rule. Many rural LECs argue that intraMTA traffic between a rural LEC and a CMRS provider must be routed through an IXC and therefore is subject to access charges, rather than reciprocal compensation.[392]

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[389] 47 C.F.R. § 51.701(b)(2).

[390] *See, e.g.,* ARIC Proposal at 35, 37 (describing a mechanism that would apply to all traffic traversing the network); CBICC Proposal at 3 (proposing a plan that eliminates concerns with respect to the intercarrier compensation for CMRS traffic); EPG Proposal at 21-22 (advocating a convergence of the disparate intercarrier rates); Home/PBT Proposal at 13 (supporting unified connection-based rates); ICF Proposal at 46-47 (proposing a default termination rate for CMRS traffic that eventually becomes the uniform rate on July 1, 2008); Western Wireless Proposal at 13 (supporting a four-year transition to bill-and-keep for all traffic).

[391] *Local Competition First Report and Order*, 11 FCC Rcd at 16017-18, para. 1044.

[392] *See* MECA Comments at 37. They explain that, because traffic is routed to and from wireless NXXs located outside of the rural LEC's local calling scope, it is toll traffic routed via an IXC, and traffic routed to or from an IXC is subject to access charges rather than reciprocal compensation. *See, e.g.,* Letter from Sylvia Lesse, Counsel to the Missouri Companies, to William F. Caton, Acting Secretary, Federal Communications Commission, WT Docket No. 01-316 and CC Docket No. 01-92, Attach. at 6 (filed Mar. 22, 2002) (Missouri Companies Mar. 22 *Ex Parte* Letter); Letter from W.R. England, III, Counsel for Citizen Telephone Company of Missouri, *et al.*, to (continued….)

CMRS providers, however, argue that all CMRS traffic that originates and terminates within a single MTA is subject to reciprocal compensation.[393] In the event that we retain the rule and interpret its scope in the more limited fashion advocated by the rural LECs, should the rule be changed so that all intraMTA traffic to or from a CMRS provider is subject to reciprocal compensation? Under such an approach, would LECs be required to route all such intraMTA traffic to CMRS carriers rather than to IXCs, even if dialed on a 1+ basis? We seek comment on the relative merits and drawbacks of such an approach, and ask parties to identify any technical impediments to such routing requirements.

138. For instance, we recognize that the current Commission rules may require that intraMTA calls dialed on a 1+ basis be routed through IXCs. Specifically, section 51.209 of the Commission's rules requires LECs to implement toll dialing parity through a presubscription process that permits a customer to select a carrier to which all designated calls on a customer's line will be routed automatically.[394] Should this rule be changed? We ask parties to explain what technical or network changes would be needed if all intraMTA CMRS traffic were routed to CMRS providers. We also seek comment on whether, in the alternative, all intraMTA calls can be made subject to reciprocal compensation without requiring LECs to alter the routing of their originated traffic. We ask parties supporting a particular approach to address any other Commission rules that may be implicated.

b. Negotiation of Interconnection Agreements

139. As the Commission recognized in the *Intercarrier Compensation NPRM*, CMRS providers typically interconnect indirectly with smaller LECs via a BOC tandem.[395] In this scenario, a CMRS provider delivers the call to a BOC tandem, which in turn delivers the call to the terminating LEC. The indirect nature of the interconnection has enabled CMRS providers to send traffic to rural LECs with which they have no interconnection agreement or other compensation arrangement.[396] Rural carriers in these circumstances have argued that they should not be required to terminate traffic without

(Continued from previous page)
Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket Nos. 01-92, 96-45, and 95-116, at 2 (filed Oct. 31, 2003) (Citizen Oct. 31 *Ex Parte* Letter). *See also* Letter from Glenn H. Brown, Counsel to Great Plains Communications, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, Attach. at 8 (filed Sept. 23, 2003) (stating that the local exchange is the incumbent LEC's local service area rather than the MTA). They further argue that calls dialed on a 1+ basis must be routed to the presubscribed IXC under existing equal access rules. *See, e.g.,* Missouri Companies Mar. 22 *Ex Parte* Letter, at 6; Citizen Oct. 31 *Ex Parte* Letter, at 3.

[393] *See* Mid-Missouri Cellular Comments at 4; ALLTEL Reply at 10; Arch Wireless Reply at 7; AT&T Wireless Reply at 27; CTIA Reply at 11; Nextel Reply at 2; PCIA Reply at 12; Sprint Reply at 14; Triton Reply at 7; VoiceStream Reply at 33.

[394] 47 C.F.R. § 51.209(b).

[395] *See Intercarrier Compensation NPRM*, 16 FCC Rcd at 9643, para. 91 n.148. *See also* Nextel Comments at 10-11; Triton PCS Comments at 13; MSTG Reply at 2; *T-Mobile USA, Inc. et al. Petition for Declaratory Ruling: Lawfulness of Incumbent Local Exchange Carrier Wireless Termination Tariffs*, CC Docket Nos. 01-92, 95-185, 96-98, Petition of T-Mobile, *et al*. (filed Sept. 6, 2002) (T-Mobile Petition), at 2. Comments and replies filed in response to the T-Mobile Petition will be identified as "T-Mobile Comments" and "T-Mobile Reply."

[396] *See* Alliance of Incumbent Rural Independent Telephone and Independent Alliance Reply at 6-7; MITG Reply at 6; MSTG Reply at 7.

compensation, and have sought compensation through various means.[397] While many CMRS providers express willingness to enter into compensation agreements, they also assert that the cost of engaging in a negotiation and arbitration process with small incumbent LECs is often prohibitive due to the small amount of traffic at issue in each individual negotiation.[398]

140. We seek comment on what measures we might adopt to reduce the costs associated with establishing compensation arrangements. We recognize that a formal negotiation and arbitration process could impose significant burdens on the parties. One possible alternative to the negotiation and arbitration process would be to establish national terms and rates for LEC-CMRS interconnection, perhaps available only where traffic volume between the two carriers is *de minimis*. We seek comment on the merits and drawbacks of this approach, on whether it would provide a better option than the section 252 process, and on how the terms and rates would be determined and applied. Alternatively, we seek comment on whether we can and should authorize states to establish uniform terms or master agreements for interconnection between CMRS providers and small incumbent LECs within the state. We also invite parties to comment on measures or procedures we could adopt to make the negotiation and arbitration process more efficient, such as measures to promote the consolidation of cases.

c. Rating of CMRS Traffic

141. It is standard industry practice for telecommunications carriers to compare the NPA/NXX codes of the calling and called party to determine the proper rating of a call.[399] As a general matter, a call is rated as local if the called number is assigned to a rate center within the local calling area of the originating rate center. If the called number is assigned to a rate center outside the local calling area of the originating rate center, it is rated as a toll call. These local calling areas are established or approved by state commissions.[400]

142. Although rating of calls based on a comparison of the NPA/NXX codes is standard

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[397] *See, e.g.*, Frontier and Citizens T-Mobile Comments at 7; ICORE T-Mobile Comments at 5, 7; Michigan Rural Incumbent Local Exchange Carriers T-Mobile Comments at 3; Minnesota Independent Coalition T-Mobile Comments at 1-2; NTCA T-Mobile Comments at 2-3; Rural ILECs T-Mobile Comments at 7-8; Rural Iowa Independent Telephone Association T-Mobile Comments at 6. *See also*, *generally*, T-Mobile Petition.

[398] *See*, *e.g.*, AT&T Wireless T-Mobile Comments at 3; Triton PCS T-Mobile Comments at 6-7. Some small LECs have also asserted that negotiations are not cost-justified for the amount of traffic at issue. *See* Montana LECs T-Mobile Comments at 6; TCA T-Mobile Comments at 2. *But see* Rural ILECs T-Mobile Comments at 7 (asserting that volume of traffic is significant in proportion to the total traffic for small incumbent LECs); Frontier & Citizens T-Mobile Comments at 4 (amount of CMRS-to-rural incumbent LEC traffic is significant and growing).

[399] *See Starpower Communications, LLC v. Verizon South Inc.*, EB-00-MD-19, Memorandum Opinion and Order, 18 FCC Rcd 23625, 23633, para. 17 (2003). One commenter suggests, however, that use of NPA/NXX codes to determine proper rating is not as widespread a practice among rural carriers as it is among the larger LECs. *See* Independent Rural Telephone Companies Alliance/Independent Alliance R&R Comments at 7-8 (describing arrangements to provide other carriers with local calling scopes on a case-by-case basis).

[400] *See Local Competition First Report and Order*, 11 FCC Rcd at 16013-14, para. 1035 (stating that state commissions have the authority to determine what geographic areas are considered "local areas" for purposes of applying reciprocal compensation obligations, consistent with the state commissions' historical practice of defining local service areas). In establishing local calling areas, state commissions consider a number of factors, including community interests and the impact on toll revenues.

industry practice, it may be possible for an originating LEC to change its switch translations so that a call to an NPA/NXX assigned to a rate center that is local to the originating rate center must be dialed on a 1+ basis and rated as a toll call, rather than a local call. Under such circumstances, a call made to what appears to be a local number would be routed to an IXC and the calling party would be billed for a toll call. A LEC may have the incentive to engage in this practice for a variety of reasons, including increased access revenue, reduced reciprocal compensation payments, and less significant transport obligations. Alternatively, LECs may engage in such practices pursuant to a state requirement.[401]

143. We note that petitions have been filed seeking to clarify a LEC's current obligations with regard to the rating and routing of calls to wireless numbers that are associated with the LEC's rate center.[402] We seek comment on whether we should modify any part of the existing rating obligations of carriers. Are there any rating issues unique to CMRS providers or is this a concern for other types of competitive carriers? We recognize that attempts to address some of the rating issues may raise the question of whether preemption of state commission jurisdiction over the retail rating of intrastate calls and the definition of local calling areas is necessary.[403] Parties supporting preemption should comment on the source of the Commission's authority to preempt and the reasons why preemption of retail rating is warranted in this context. Parties also should comment on whether blanket preemption is necessary or whether such action should be considered on a case-specific basis.

III. PROCEDURAL MATTERS

A. Supplemental Initial Regulatory Flexibility Analysis

144. As required by the Regulatory Flexibility Act of 1980, as amended ("RFA"),[404] an Initial Regulatory Flexibility Analysis (IRFA) was incorporated in the Intercarrier Compensation NPRM.[405] The Commission sought written public comment on reforming the existing intercarrier compensation regime,[406] on alternate approaches to reforming that regime, on whether those alternate approaches will encourage efficient use of and investment in the telecommunications network,[407] on whether they will

[401]For example, on December 22, 2003, ASAP Paging, Inc. (ASAP) filed a petition requesting that the Commission preempt an order of the Public Utility Commission of Texas (Texas Commission) that required toll treatment of calls to ASAP's local numbers, as well as certain provisions of the Texas Public Utility Regulatory Act and certain Texas Commission substantive rules. *See Pleading Cycle Established for Petition of ASAP Paging, Inc. for Preemption of the Public Utility Commission of Texas Concerning Retail Rating of Local Calls to CMRS Carriers*, WC Docket No. 04-6, Public Notice, 19 FCC Rcd 936 (2004) (ASAP Paging Petition Public Notice).

[402]*See Comment Sought on Petitions for Declaratory Ruling Regarding Intercarrier Compensation for Wireless Traffic*, CC Docket No. 01-92, Public Notice, 17 FCC Rcd 19046 (2002); ASAP Paging Petition Public Notice.

[403]*See* ASAP Paging Petition Public Notice.

[404]*See* 5 U.S.C. § 603. The RFA, see 5 U.S.C. §§ 601-612, has been amended by the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA), Pub. L. No. 104-121, Title II, 110 Stat. 857 (1996).

[405]*Intercarrier Compensation NPRM*, 16 FCC Rcd at 9611 para. 1.

[406]*Id.* at 9658 para. 134.

[407]*Id.* at 9658 para. 135.

solve interconnection problems,[408] and on the extent to which they are administratively feasible.[409] The Intercarrier Compensation NPRM also sought comment on the IRFA.[410] The Commission received extensive comment in response to the Intercarrier Compensation NPRM,[411] including several comments addressing the IRFA directly.[412]

145. With this Further Notice, the Commission continues the process of intercarrier compensation reform. The Commission has prepared this present Supplemental Initial Regulatory Flexibility Analysis ("Supplemental IRFA") of the possible significant economic impact on a substantial number of small entities by the policies and rules proposed in this Further Notice. This Supplemental IRFA conforms to the RFA.[413] Written public comments are requested on this Supplemental IRFA. Comments must be identified as responses to the Supplemental IRFA and must be filed by the deadlines for comments on the Further Notice provided in paragraph 214. To the extent that any statement in this Supplemental IRFA is perceived as creating ambiguity with respect to Commission rules or statements made in sections of this Further Notice that precede this Supplemental IRFA, the rules and statements set forth in those preceding sections are controlling. The Commission will send a copy of this entire Further Notice, including this Supplemental IRFA, to the Chief Counsel for Advocacy of the Small Business Administration ("SBA").[414] In addition, this Further Notice and the Supplemental IRFA (or summaries thereof) will be published in the Federal Register.[415]

1. Need for, and objectives of, the proposed rules

146. The Commission's goal in this proceeding is to reform the current intercarrier compensation regimes and create a more uniform regime that promotes efficient facilities-based competition in the marketplace.[416] As discussed above, the Commission believes that this goal will be served by creating a technologically and competitively neutral intercarrier compensation regime that is consistent with network developments. It is also critical that this regime be implemented in a manner that will provide regulatory certainty, limit the need for regulatory intervention,[417] and preserve universal service.[418]

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[408] *Id.* at 9658 para. 134.

[409] *Id*.

[410] *Id.* at 9657 para. 131.

[411] *See infra* at Appendix A.

[412] *See* NECA Comments at 17; NTCA Comments at 23; and SBA Reply at 12-14.

[413] *See* 5 U.S.C. § 604.

[414] *See id*. § 604.

[415] *Id.*

[416] *See supra* para. 31.

[417] *See supra* para. 33.

[418] *See supra* para. 32.

147. The current intercarrier compensation system is governed by a complex set of federal and state rules.[419] This system applies different cost methodologies to similar services based on traditional regulatory distinctions that may have no bearing on the cost of providing service, are not tied to economic or technical differences between services,[420] and are increasingly difficult to maintain.[421] These regulatory distinctions provide an opportunity for regulatory arbitrage activities, and distort the telecommunications markets at the expense of healthy competition.[422]

148. The current intercarrier compensation system also does not take into account recent developments in service offerings, including bundled local and long distance services[423], and voice over Internet Protocol (VoIP) services.[424] These developments blur traditional industry and regulatory distinctions among various types of services and service providers, making it increasingly difficult to enforce the existing regulatory regimes.[425] Additionally, the current intercarrier compensation system does not account for recent developments in telecommunications infrastructure. The existing intercarrier compensation regimes are based largely on the recovery of switching costs through per-minute charges.[426] As a result of developments in telecommunications infrastructure, it appears that most network costs, including switching costs, result from connections to the network rather than usage of the network itself.[427] Finally, developments in consumer control over telecommunications services bring into question the assumption that calling parties receive 100 percent of the benefits from a telephone call, a fundamental premise of the current intercarrier compensation regimes.[428]

149. The Commission received several intercarrier compensation reform proposals in response to the NPRM.[429] In this Further Notice, the Commission seeks comment on numerous legal issues it must consider as part of intercarrier compensation reform, whether it adopts one of these proposals or develops a separate approach. Specifically, the Commission seeks comment on whether the cost standards proposed satisfy the requirements of the Act,[430] on the possible exercise of its forbearance authority,[431]

[419] *See supra* para. 5.

[420] *See supra* para. 15.

[421] *See supra* paras. 5, 15.

[422] *See supra* para. 15.

[423] *See supra* para. 19.

[424] *See supra* para. 20.

[425] *See supra* para. 21.

[426] *See supra* para. 23.

[427] *See supra* para. 23.

[428] *See supra* para. 27.

[429] *See* supra note 79.

[430] *See supra* para. 65.

[431] *See supra* paras. 74-77.

and on the appropriate role of state regulation in the intercarrier compensation reform process.[432] The Commission also seeks comment on proposed changes to current interconnection rules.[433]

150. Further, the Commission seeks comment on its obligation to provide cost-recovery mechanisms,[434] the need, if any, for new cost-recovery mechanisms, the appropriate level of different types of cost recovery mechanisms including end-user charges and universal service,[435] and on the impact of replacing access charges with other types of cost recovery mechanisms.[436] The Commission also seeks comment on the whether price cap and rate-of-return LECs must be treated equally with regard to cost recovery mechanisms, whether such treatment would be competitively neutral,[437] and the appropriate role for state cost recovery mechanisms.[438] Additionally, the Commission seeks comment on how best to transition from the current regime to unified intercarrier compensation regime.[439] Finally, the Commission seeks comment on additional issues stemming from intercarrier compensation reform including transit service obligations,[440] the appropriate treatment of intraMTA CMRS traffic,[441] interconnection agreement negotiation obligations,[442] and routing and rating of CMRS calls.[443]

2. Legal Basis

151. The legal basis for any action that may be taken pursuant to this *Further Notice* is contained in sections 1-5, 7, 10, 201-05, 207-09, 214, 218-20, 225-27, 251-54, 256, 271, 303, 332, 403, 405, 502 and 503 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151-55, 157, 160, 201-05, 207-09, 214, 218-20, 225-27, 251-54, 256, 271, 303, 332, 403, 405, 502, and 503 and sections 1.1, 1.421 of the Commission's rules, 47 C.F.R. §§ 1.1, 1.421

3. Description and Estimate of the Number of Small Entities to Which the Proposed Rules will Apply

152. The RFA directs agencies to provide a description of, and, where feasible, an estimate of

[432] *See supra* paras. 78-82.

[433] *See supra* para. 92.

[434] *See supra* paras. 99-100.

[435] *See supra* paras. 101-02.

[436] *See supra* para. 106.

[437] *See supra* paras. 107-11.

[438] *See supra* paras. 114-15.

[439] *See supra* paras. 116-19.

[440] *See supra* paras. 128-30.

[441] *See supra* paras. 135-38.

[442] *See supra* paras. 139-40.

[443] *See supra* para. 143.

the number of small entities that may be affected by rules adopted herein.[444] The RFA generally defines the term "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction."[445] In addition, the term "small business" has the same meaning as the term "small business concern" under the Small Business Act.[446] A "small business concern" is one that: 1) is independently owned and operated; 2) is not dominant in its field of operation; and 3) satisfies any additional criteria established by the Small Business Administration (SBA).[447]

153. In this section, we further describe and estimate the number of small entity licensees and regulatees that may also be indirectly affected by rules adopted pursuant to this *Further Notice*. The most reliable source of information regarding the total numbers of certain common carrier and related providers nationwide, as well as the number of commercial wireless entities, appears to be the data that the Commission publishes in its *Trends in Telephone Service* report.[448] The SBA has developed small business size standards for wireline and wireless small businesses within the three commercial census categories of Wired Telecommunications Carriers,[449] Paging,[450] and Cellular and Other Wireless Telecommunications.[451] Under these categories, a business is small if it has 1,500 or fewer employees. Below, using the above size standards and others, we discuss the total estimated numbers of small businesses that might be affected by our actions.

154. *Wired Telecommunications Carriers*. The SBA has developed a small business size standard for Wired Telecommunications Carriers, which consists of all such companies having 1,500 or fewer employees.[452] According to Census Bureau data for 1997, there were 2,225 firms in this category, total, that operated for the entire year.[453] Of this total, 2,201 firms had employment of 999 or fewer employees, and an additional 24 firms had employment of 1,000 employees or more.[454] Thus, under this

[444] 5 U.S.C. § 604(a)(3).

[445] 5 U.S.C. § 601(6).

[446] 5 U.S.C. § 601(3) (incorporating by reference the definition of "small business concern" in the Small Business Act, 15 U.S.C. § 632). Pursuant to 5 U.S.C. § 601(3), the statutory definition of a small business applies "unless an agency, after consultation with the Office of Advocacy of the Small Business Administration and after opportunity for public comment, establishes one or more definitions of such term which are appropriate to the activities of the agency and publishes such definition(s) in the Federal Register."

[447] 15 U.S.C. § 632.

[448] FCC, Wireline Competition Bureau, Industry Analysis and Technology Division, *Trends in Telephone Service*, Table 5.3 (May 2002) (*Trends in Telephone Service*).

[449] 13 C.F.R. § 121.201, North American Industry Classification System (NAICS) code 517110.

[450] *Id*. § 121.201, NAICS code 517211.

[451] *Id*. § 121.201, NAICS code 517212.

[452] 13 C.F.R. § 121.201, NAICS code 517110.

[453] U.S. Census Bureau, 1997 Economic Census, Subject Series: Information, "Establishment and Firm Size (Including Legal Form of Organization)," Table 5, NAICS code 517110.

[454] *Id.* The census data do not provide a more precise estimate of the number of firms that have employment of 1,500 or fewer employees; the largest category provided is "Firms with 1,000 employees or more."

size standard, the majority of firms can be considered small.

155. *Local Exchange Carriers*. Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to local exchange services. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees.[455] According to Commission data, 1,310 carriers reported that they were incumbent local exchange service providers.[456] Of these 1,310 carriers, an estimated 1,025 have 1,500 or fewer employees and 285 have more than 1,500 employees.[457] In addition, according to Commission data, 563 companies reported that they were engaged in the provision of either competitive access provider services or competitive local exchange carrier services.[458] Of these 563 companies, an estimated 472 have 1,500 or fewer employees and 91 have more than 1,500 employees.[459] In addition, 37 carriers reported that they were "Other Local Exchange Carriers."[460] Of the 37 "Other Local Exchange Carriers," an estimated 36 have 1,500 or fewer employees and one has more than 1,500 employees.[461] Consequently, the Commission estimates that most providers of local exchange service, competitive local exchange service, competitive access providers, and "Other Local Exchange Carriers" are small entities that may be affected by the rules and policies adopted herein.

156. *Interexchange Carriers*. Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to interexchange services. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees.[462] According to Commission data, 281 companies reported that they were interexchange carriers.[463] Of these 281 companies, an estimated 254 have 1,500 or fewer employees and 27 have more than 1,500 employees.[464] Consequently, the Commission estimates that the majority of interexchange service providers are small entities that may be affected by the rules and policies adopted herein.

157. *Wired Telecommunications Carriers*. The SBA has developed a small business size standard for Wired Telecommunications Carriers, which consists of all such companies having 1,500 or

[455] 13 C.F.R. § 121.201, NAICS code 517110.

[456] *Trends in Telephone Service*, Federal Communications Commission, Wireline Competition Bureau, Industry Analysis and Technology Division, Table 5.3 (May 2004) (*Trends in Telephone Service*).

[457] *Id*.

[458] *Id*.

[459] *Id*.

[460] *Id*.

[461] *Id*.

[462] 13 C.F.R. § 121.201, NAICS code 517110.

[463] *Trends in Telephone Service*, Table 5.3.

[464] *Id*.

fewer employees.[465] According to Census Bureau data for 1997, there were 2,225 firms in this category, total, that operated for the entire year.[466] Of this total, 2,201 firms had employment of 999 or fewer employees, and an additional 24 firms had employment of 1,000 employees or more.[467] Thus, under this size standard, the majority of firms can be considered small.

158. *Incumbent Local Exchange Carriers (LECs)*. Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to incumbent local exchange services. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees.[468] According to Commission data,[469] 1,337 carriers reported that they were engaged in the provision of local exchange services. Of these 1,337 carriers, an estimated 1,032 have 1,500 or fewer employees and 305 have more than 1,500 employees. Consequently, the Commission estimates that most providers of incumbent local exchange service are small businesses that may be affected by the rules and policies adopted herein.

159. *Competitive Local Exchange Carriers (CLECs), Competitive Access Providers (CAPs), and "Other Local Exchange Carriers."* Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to providers of competitive exchange services or to competitive access providers or to "Other Local Exchange Carriers," all of which are discrete categories under which TRS data are collected. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees.[470] According to Commission data,[471] 609 companies reported that they were engaged in the provision of either competitive access provider services or competitive local exchange carrier services. Of these 609 companies, an estimated 458 have 1,500 or fewer employees and 151 have more than 1,500 employees.[472] In addition, 35 carriers reported that they were "Other Local Service Providers." Of the 35 "Other Local Service Providers," an estimated 34 have 1,500 or fewer employees and one has more than 1,500 employees.[473] Consequently, the Commission estimates that most providers of competitive local exchange service, competitive access providers, and "Other Local Exchange Carriers" are small entities that may be affected by the rules and policies adopted herein.

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[465] 13 C.F.R. § 121.201, NAICS code 517110.

[466] U.S. Census Bureau, 1997 Economic Census, Subject Series: Information, "Establishment and Firm Size (Including Legal Form of Organization)," Table 5, NAICS code 513310.

[467] *Id.* The census data do not provide a more precise estimate of the number of firms that have employment of 1,500 or fewer employees; the largest category provided is "Firms with 1,000 employees or more."

[468] 13 C.F.R. § 121.201, NAICS code 517110.

[469] *Trends in Telephone Service* at Table 5.3.

[470] 13 C.F.R. § 121.201, NAICS code 517110.

[471] *Trends in Telephone Service* at Table 5.3.

[472] *Id.*

[473] *Id.*

160. *Interexchange Carriers (IXCs)*. Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to interexchange services. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees.[474] According to Commission data,[475] 261 companies reported that their primary telecommunications service activity was the provision of interexchange services. Of these 261 companies, an estimated 223 have 1,500 or fewer employees and 38 have more than 1,500 employees.[476] Consequently, the Commission estimates that the majority of interexchange service providers are small entities that may be affected by the rules and policies adopted herein.

161. *Operator Service Providers (OSPs).* Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to operator service providers. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees.[477] According to Commission data,[478] 23 companies reported that they were engaged in the provision of operator services. Of these 23 companies, an estimated 22 have 1,500 or fewer employees and one has more than 1,500 employees.[479] Consequently, the Commission estimates that the majority of operator service providers are small entities that may be affected by the rules and policies adopted herein.

162. *Payphone Service Providers (PSPs).* Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to payphone service providers. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees.[480] According to Commission data,[481] 761 companies reported that they were engaged in the provision of payphone services. Of these 761 companies, an estimated 757 have 1,500 or fewer employees and four have more than 1,500 employees.[482] Consequently, the Commission estimates that the majority of payphone service providers are small entities that may be affected by the rules and policies adopted herein.

163. *Prepaid Calling Card Providers.* The SBA has developed a size standard for a small business within the category of Telecommunications Resellers. Under that SBA size standard, such a business is small if it has 1,500 or fewer employees.[483] According to Commission data,[484] 37 companies

[474] 13 C.F.R. § 121.201, NAICS code 517110.

[475] *Trends in Telephone Service* at Table 5.3.

[476] *Id.*

[477] 13 C.F.R. § 121.201, NAICS code 517110.

[478] *Trends in Telephone Service* at Table 5.3.

[479] *Id.*

[480] 13 C.F.R. § 121.201, NAICS code 517110.

[481] *Trends in Telephone Service* at Table 5.3.

[482] *Id*.

[483] 13 C.F.R. § 121.201, NAICS code 517310.

reported that they were engaged in the provision of prepaid calling cards. Of these 37 companies, an estimated 36 have 1,500 or fewer employees and one has more than 1,500 employees.[485] Consequently, the Commission estimates that the majority of prepaid calling card providers are small entities that may be affected by the rules and policies adopted herein.

164. *Local Resellers.* The SBA has developed a small business size standard for the category of Telecommunications Resellers. Under that size standard, such a business is small if it has 1,500 or fewer employees.[486] According to Commission data,[487] 133 carriers have reported that they are engaged in the provision of local resale services. Of these, an estimated 127 have 1,500 or fewer employees and six have more than 1,500 employees. Consequently, the Commission estimates that the majority of local resellers are small entities that may be affected by our action.

165. *Toll Resellers.* The SBA has developed a small business size standard for the category of Telecommunications Resellers. Under that size standard, such a business is small if it has 1,500 or fewer employees.[488] According to Commission data,[489] 625 carriers have reported that they are engaged in the provision of toll resale services. Of these, an estimated 590 have 1,500 or fewer employees and 35 have more than 1,500 employees. Consequently, the Commission estimates that the majority of toll resellers are small entities that may be affected by our action.

166. *Other Toll Carriers.* Neither the Commission nor the SBA has developed a size standard for small businesses specifically applicable to "Other Toll Carriers." This category includes toll carriers that do not fall within the categories of interexchange carriers, operator service providers, prepaid calling card providers, satellite service carriers, or toll resellers. The closest applicable size standard under SBA rules is for Wired Telecommunications Carriers. Under that size standard, such a business is small if it has 1,500 or fewer employees.[490] According to Commission's data,[491] 92 companies reported that their primary telecommunications service activity was the provision of other toll carriage. Of these 92 companies, an estimated 82 have 1,500 or fewer employees and ten have more than 1,500 employees.[492] Consequently, the Commission estimates that most "Other Toll Carriers" are small entities that may be affected by the rules and policies adopted herein.

167. *Paging*. The SBA has developed a small business size standard for Paging, which

(Continued from previous page)
[484]*Trends in Telephone Service* at Table 5.3.

[485]*Id.*

[486]13 CFR § 121.201, NAICS code 513330.

[487]*Trends in Telephone Service at Table 5.3.*

[488]13 CFR § 121.201, NAICS code 513330.

[489]*Trends in Telephone Service at Table 5.3.*

[490]13 C.F.R. § 121.201, NAICS code 517110.

[491]*Trends in Telephone Service* at Table 5.3.

[492]*Id*.

consists of all such firms having 1,500 or fewer employees.[493] According to Census Bureau data for 1997, in this category there was a total of 1,320 firms that operated for the entire year.[494] Of this total, 1,303 firms had employment of 999 or fewer employees, and an additional seventeen firms had employment of 1,000 employees or more.[495] Thus, under this size standard, the majority of firms can be considered small.

168. *Cellular and Other Wireless Telecommunications*. The SBA has developed a small business size standard for Cellular and Other Wireless Telecommunication, which consists of all such firms having 1,500 or fewer employees.[496] According to Census Bureau data for 1997, in this category there was a total of 977 firms that operated for the entire year.[497] Of this total, 965 firms had employment of 999 or fewer employees, and an additional twelve firms had employment of 1,000 employees or more.[498] Thus, under this size standard, the majority of firms can be considered small.

169. *Broadband Personal Communications Service.* The broadband Personal Communications Service (PCS) spectrum is divided into six frequency blocks designated A through F, and the Commission has held auctions for each block. The Commission defined "small entity" for Blocks C and F as an entity that has average gross revenues of $40 million or less in the three previous calendar years.[499] For Block F, an additional classification for "very small business" was added and is defined as an entity that, together with its affiliates, has average gross revenues of not more than $15 million for the preceding three calendar years."[500] These standards defining "small entity" in the context of broadband PCS auctions have been approved by the SBA.[501] No small businesses, within the SBA-approved small business size standards bid successfully for licenses in Blocks A and B. There were 90 winning bidders that qualified as small entities in the Block C auctions. A total of 93 small and very small business

[493] 13 C.F.R. § 121.201, NAICS code 513321.

[494] U.S. Census Bureau, 1997 Economic Census, Subject Series: Information, "Establishment and Firm Size (Including Legal Form of Organization)," Table 5, NAICS code 513321.

[495] *Id*. The census data do not provide a more precise estimate of the number of firms that have employment of 1,500 or fewer employees; the largest category provided is "Firms with 1,000 employees or more."

[496] 13 C.F.R. § 121.201, NAICS code 513322.

[497] U.S. Census Bureau, 1997 Economic Census, Subject Series: Information, "Establishment and Firm Size (Including Legal Form of Organization)," Table 5, NAICS code 513322.

[498] *Id*. The census data do not provide a more precise estimate of the number of firms that have 1,500 or fewer employees; the largest category provided is "Firms with 1,000 employees or more."

[499] *See Amendment of Parts 20 and 24 of the Commission's Rules – Broadband PCS Competitive Bidding and the Commercial Mobile Radio Service Spectrum Cap*, WT Docket No. 96-59, Report and Order, 61 FR 33859 (July 1, 1996); *see also* 47 C.F.R. § 24.720(b).

[500] *See id*.

[501] *See. e.g., Implementation of Section 309(j) of the Communications Act – Competitive Bidding*, PP Docket No. 93-253, Fifth Report and Order, 59 FR 37566 (July 22, 1994).

bidders won approximately 40 percent of the 1,479 licenses for Blocks D, E, and F.[502] On March 23, 1999, the Commission re-auctioned 347 C, D, E, and F Block licenses. There were 48 small business winning bidders. On January 26, 2001, the Commission completed the auction of 422 C and F Broadband PCS licenses in Auction No. 35. Of the 35 winning bidders in this auction, 29 qualified as "small" or "very small" businesses. Based on this information, the Commission concludes that the number of small broadband PCS licenses will include the 90 winning C Block bidders, the 93 qualifying bidders in the D, E, and F Block auctions, the 48 winning bidders in the 1999 re-auction, and the 29 winning bidders in the 2001 re-auction, for a total of 260 small entity broadband PCS providers, as defined by the SBA small business size standards and the Commission's auction rules. We note that, as a general matter, the number of winning bidders that qualify as small businesses at the close of an auction does not necessarily represent the number of small businesses currently in service. Also, the Commission does not generally track subsequent business size unless, in the context of assignments or transfers, unjust enrichment issues are implicated.

170. *Narrowband Personal Communications Services.* The Commission has adopted a two-tiered small business size standard in the *Narrowband PCS Second Report and Order*.[503] A "small business" is an entity that, together with affiliates and controlling interests, has average gross revenues for the three preceding years of not more than $40 million. A "very small business" is an entity that, together with affiliates and controlling interests, has average gross revenues for the three preceding years of not more than $15 million. The SBA has approved these small business size standards.[504] In the future, the Commission will auction 459 licenses to serve Metropolitan Trading Areas (MTAs) and 408 response channel licenses. There is also one megahertz of narrowband PCS spectrum that has been held in reserve and that the Commission has not yet decided to release for licensing. The Commission cannot predict accurately the number of licenses that will be awarded to small entities in future actions. However, four of the 16 winning bidders in the two previous narrowband PCS auctions were small businesses, as that term was defined under the Commission's Rules. The Commission assumes, for purposes of this analysis, that a large portion of the remaining narrowband PCS licenses will be awarded to small entities. The Commission also assumes that at least some small businesses will acquire narrowband PCS licenses by means of the Commission's partitioning and disaggregation rules.

171. *220 MHz Radio Service – Phase I Licensees.* The 220 MHz service has both Phase I and Phase II licenses. Phase I licensing was conducted by lotteries in 1992 and 1993. There are approximately 1,515 such non-nationwide licensees and four nationwide licensees currently authorized to operate in the 220 MHz band. The Commission has not developed a small business size standard for small entities specifically applicable to such incumbent 220 MHz Phase I licensees. To estimate the number of such licensees that are small businesses, we apply the small business size standard under the SBA rules applicable to "Cellular and Other Wireless Telecommunications" companies. This standard

[502]FCC News, Broadband PCS, D, E and F Block Auction Closes, No. 71744 (rel. January 14, 1997). *See also Amendment of the Commission's Rules Regarding Installment Payment Financing for Personal Communications Services (PCS) Licenses*, WT Docket No. 97-82, Second Report and Order, 62 FR 55348 (Oct. 24,1997).

[503]*Amendment of the Commission's Rules to Establish New Personal Communications Services, Narrowband PCS*, Docket No. ET 92-100, Docket No. PP 93-253, Second Report and Order and Second Further Notice of Proposed Rulemaking, 65 FR 35875 (June 6, 2000).

[504]*See* Letter to Amy Zoslov, Chief, Auctions and Industry Analysis Division, Wireless Telecommunications Bureau, FCC, from Aida Alvarez, Administrator, SBA (Dec. 2, 1998).

provides that such a company is small if it employs no more than 1,500 persons.[505] According to Census Bureau data for 1997, there were 977 firms in this category, total, that operated for the entire year.[506] Of this total, 965 firms had employment of 999 or fewer employees, and an additional 12 firms had employment of 1,000 employees or more.[507] If this general ratio continues in the context of Phase I 220 MHz licensees, the Commission estimates that nearly all such licensees are small businesses under the SBA's small business size standard.

172. *220 MHz Radio Service – Phase II Licensees.* The 220 MHz service has both Phase I and Phase II licenses. The Phase II 220 MHz service is a new service, and is subject to spectrum auctions. In the *220 MHz Third Report and Order*, we adopted a small business size standard for "small" and "very small" businesses for purposes of determining their eligibility for special provisions such as bidding credits and installment payments.[508] This small business size standard indicates that a "small business" is an entity that, together with its affiliates and controlling principals, has average gross revenues not exceeding $15 million for the preceding three years.[509] A "very small business" is an entity that, together with its affiliates and controlling principals, has average gross revenues that do not exceed $3 million for the preceding three years. The SBA has approved these small business size standards.[510] Auctions of Phase II licenses commenced on September 15, 1998, and closed on October 22, 1998.[511] In the first auction, 908 licenses were auctioned in three different-sized geographic areas: three nationwide licenses, 30 Regional Economic Area Group (EAG) Licenses, and 875 Economic Area (EA) Licenses. Of the 908 licenses auctioned, 693 were sold. Thirty-nine small businesses won licenses in the first 220 MHz auction. The second auction included 225 licenses: 216 EA licenses and 9 EAG licenses. Fourteen companies claiming small business status won 158 licenses.[512]

173. *800 MHz and 900 MHz Specialized Mobile Radio Licenses.* The Commission awards "small entity" and "very small entity" bidding credits in auctions for Specialized Mobile Radio (SMR) geographic area licenses in the 900 MHz bands to firms that had revenues of no more than $15 million in each of the three previous calendar years, or that had revenues of no more than $3 million in each of the

[505] 13 C.F.R. § 121.201, NAICS code 517212.

[506] U.S. Census Bureau, 1997 Economic Census, Subject Series: Information, "Employment Size of Firms Subject to Federal Income Tax: 1997," Table 5, NAICS code 513322.

[507] *Id*. The census data do not provide a more precise estimate of the number of firms that have employment of 1,500 or fewer employees; the largest category provided is "Firms with 1,000 employees or more."

[508] *Amendment of Part 90 of the Commission's Rules to Provide for the Use of the 220-222 MHz Band by the Private Land Mobile Radio Service*, PR Docket No. 89-552, GN Docket No. 93-252, PP Docket No. 93-253, Third Report and Order and Fifth Notice of Proposed Rulemaking, 12 FCC Rcd 10943, 11068-70, paras. 291-95 (1997) (*220 MHz Third Report and Order*).

[509] *Id*. at 11068-70, para. 291.

[510] *See* letter to D. Phythyon, Chief, Wireless Telecommunications Bureau, FCC, from Aida Alvarez, Administrator, SBA (Jan. 6, 1998).

[511] *See generally* Public Notice, "220 MHz Service Auction Closes," 14 FCC Rcd 605 (1998).

[512] Public Notice, "Phase II 220 MHz Service Spectrum Auction Closes," 14 FCC Rcd 11218 (1999).

previous calendar years.[513] The SBA has approved these size standards.[514] The Commission awards "small entity" and "very small entity" bidding credits in auctions for Specialized Mobile Radio (SMR) geographic area licenses in the 800 MHz bands to firms that had revenues of no more than $40 million in each of the three previous calendar years, or that had revenues of no more than $15 million in each of the previous calendar years.[515] These bidding credits apply to SMR providers in the 800 MHz and 900 MHz bands that either hold geographic area licenses or have obtained extended implementation authorizations. The Commission does not know how many firms provide 800 MHz or 900 MHz geographic area SMR service pursuant to extended implementation authorizations, nor how many of these providers have annual revenues of no more than $15 million. One firm has over $15 million in revenues. The Commission assumes, for purposes here, that all of the remaining existing extended implementation authorizations are held by small entities, as that term is defined by the SBA. The Commission has held auctions for geographic area licenses in the 800 MHz and 900 MHz SMR bands. There were 60 winning bidders that qualified as small or very small entities in the 900 MHz SMR auctions. Of the 1,020 licenses won in the 900 MHz auction, bidders qualifying as small or very small entities won 263 licenses. In the 800 MHz auction, 38 of the 524 licenses won were won by small and very small entities. We note that, as a general matter, the number of winning bidders that qualify as small businesses at the close of an auction does not necessarily represent the number of small businesses currently in service. Also, the Commission does not generally track subsequent business size unless, in the context of assignments or transfers, unjust enrichment issues are implicated.

174. *Private and Common Carrier Paging.* In the Paging *Third Report and Order*, we developed a small business size standard for "small businesses" and "very small businesses" for purposes of determining their eligibility for special provisions such as bidding credits and installment payments.[516] A "small business" is an entity that, together with its affiliates and controlling principals, has average gross revenues not exceeding $15 million for the preceding three years. Additionally, a "very small business" is an entity that, together with its affiliates and controlling principals, has average gross revenues that are not more than $3 million for the preceding three years. The SBA has approved these size standards.[517] An auction of Metropolitan Economic Area licenses commenced on February 24, 2000, and closed on March 2, 2000.[518] Of the 985 licenses auctioned, 440 were sold. Fifty-seven companies

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[513] 47 C.F.R. § 90.814(b)(1).

[514] *See* Letter from Aida Alvarez, Administration, Small Business Administration to Daniel B. Phythyon, Chief, Wireless Telecommunications Bureau, Federal Communications Commission (Oct. 27, 1997). *See* Letter from Aida Alvarez, Administrator, Small Business Administration to Thomas Sugrue, Chief, Auctions and Industry Analysis Division, Wireless Telecommunications Bureau, Federal Communications Commission (Aug. 10, 1999).

[515] 47 C.F.R. § 90.814(b)(1) A request for approval of 800 MHz standards was sent to the SBA on May 13, 1999. The matter remains pending.

[516] *220 MHz Third Report and Order*, 12 FCC Rcd at 11068-70, paras. 291-295, 62 FR 16004 at paras. 291-295 (1997).

[517] *See* Letter from Aida Alvarez, Administrator, Small Business Administration to Thomas Sugrue, Chief, Auctions and Industry Analysis Division, Wireless Telecommunications Bureau, Federal Communications Commission (June 4, 1999).

[518] *Revision of Part 22 and Part 90 of the Commission's Rules to Facilitate Future Development of Paging Systems*, WT Docket No. 96-18, PR Docket No. 93-253, Memorandum Opinion and Order on Reconsideration and Third Report and Order, 14 FCC Rcd 10030, 10085, para. 98 (1999).

claiming small business status won. At present, there are approximately 24,000 Private-Paging site-specific licenses and 74,000 Common Carrier Paging licenses. According to the most recent *Trends in Telephone Service,* 471 carriers reported that they were engaged in the provision of either paging and messaging services or other mobile services.[519] Of those, the Commission estimates that 450 are small, under the SBA business size standard specifying that firms are small if they have 1,500 or fewer employees.[520]

175. *700 MHz Guard Band Licensees.* In the 700 MHz Guard Band Order, we adopted a small business size standard for "small businesses" and "very small businesses" for purposes of determining their eligibility for special provisions such as bidding credits and installment payments.[521] A "small business" as an entity that, together with its affiliates and controlling principals, has average gross revenues not exceeding $15 million for the preceding three years. Additionally, a "very small business" is an entity that, together with its affiliates and controlling principals, has average gross revenues that are not more than $3 million for the preceding three years. An auction of 52 Major Economic Area (MEA) licenses commenced on September 6, 2000, and closed on September 21, 2000.[522] Of the 104 licenses auctioned, 96 licenses were sold to nine bidders. Five of these bidders were small businesses that won a total of 26 licenses. A second auction of 700 MHz Guard Band licenses commenced on February 13, 2001 and closed on February 21, 2001. All eight of the licenses auctioned were sold to three bidders. One of these bidders was a small business that won a total of two licenses.[523]

176. *Rural Radiotelephone Service.* The Commission has not adopted a size standard for small businesses specific to the Rural Radiotelephone Service.[524] A significant subset of the Rural Radiotelephone Service is the Basic Exchange Telephone Radio System (BETRS).[525] The Commission uses the SBA's small business size standard applicable to "Cellular and Other Wireless Telecommunications," *i.e.*, an entity employing no more than 1,500 persons.[526] There are approximately 1,000 licensees in the Rural Radiotelephone Service, and the Commission estimates that there are 1,000 or fewer small entity licensees in the Rural Radiotelephone Service that may be affected by the rules and policies adopted herein.

177. *Air-Ground Radiotelephone Service.* The Commission has not adopted a small business size standard specific to the Air-Ground Radiotelephone Service.[527] We will use SBA's small business

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[519]*Trends in Telephone Service* at Table 5.3.

[520]*Id*. The SBA size standard is that of Paging, 13 C.F.R. § 121.201, NAICS code 517211.

[521]*See Service Rules for the 746-764 MHz Bands, and Revisions to part 27 of the Commission's Rules*, WT Docket No. 99-168, Second Report and Order, 15 FCC Rcd 5299, 5344, para. 108 (2000).

[522]*See generally* Public Notice, "220 MHz Service Auction Closes," Report No. WT 98-36 (Wireless Telecommunications Bureau, Oct. 23, 1998).

[523]Public Notice, "700 MHz Guard Band Auction Closes," DA 01-478 (rel. Feb. 22, 2001).

[524]The service is defined in § 22.99 of the Commission's Rules, 47 C.F.R. § 22.99.

[525]BETRS is defined in §§ 22.757 and 22.759 of the Commission's Rules, 47 C.F.R. §§ 22.757 and 22.759.

[526]13 C.F.R. § 121.201, NAICS code 517212.

[527]The service is defined in § 22.99 of the Commission's Rules, 47 C.F.R. § 22.99.

size standard applicable to "Cellular and Other Wireless Telecommunications," *i.e.*, an entity employing no more than 1,500 persons.[528] There are approximately 100 licensees in the Air-Ground Radiotelephone Service, and we estimate that almost all of them qualify as small under the SBA small business size standard.

178. *Aviation and Marine Radio Services.* Small businesses in the aviation and marine radio services use a very high frequency (VHF) marine or aircraft radio and, as appropriate, an emergency position-indicating radio beacon (and/or radar) or an emergency locator transmitter. The Commission has not developed a small business size standard specifically applicable to these small businesses. For purposes of this analysis, the Commission uses the SBA small business size standard for the category "Cellular and Other Telecommunications," which is 1,500 or fewer employees.[529] Most applicants for recreational licenses are individuals. Approximately 581,000 ship station licensees and 131,000 aircraft station licensees operate domestically and are not subject to the radio carriage requirements of any statute or treaty. For purposes of our evaluations in this analysis, we estimate that there are up to approximately 712,000 licensees that are small businesses (or individuals) under the SBA standard. In addition, between December 3, 1998 and December 14, 1998, the Commission held an auction of 42 VHF Public Coast licenses in the 157.1875-157.4500 MHz (ship transmit) and 161.775-162.0125 MHz (coast transmit) bands. For purposes of the auction, the Commission defined a "small" business as an entity that, together with controlling interests and affiliates, has average gross revenues for the preceding three years not to exceed $15 million dollars. In addition, a "very small" business is one that, together with controlling interests and affiliates, has average gross revenues for the preceding three years not to exceed $3 million dollars.[530] There are approximately 10,672 licensees in the Marine Coast Service, and the Commission estimates that almost all of them qualify as "small" businesses under the above special small business size standards.

179. *Fixed Microwave Services.* Fixed microwave services include common carrier,[531] private operational-fixed,[532] and broadcast auxiliary radio services.[533] At present, there are approximately 22,015 common carrier fixed licensees and 61,670 private operational-fixed licensees and broadcast auxiliary radio licensees in the microwave services. The Commission has not created a size standard for a small

[528] 13 C.F.R § 121.201, NAICS codes 517212.

[529] 13 CFR § 121.201, NAICS code 517212.

[530] Amendment of the Commission's Rules Concerning Maritime Communications, PR Docket No. 92-257, *Third Report and Order and Memorandum Opinion and Order*, 13 FCC Rcd 19853 (1998).

[531] *See* 47 C.F.R. §§ 101 *et seq*. (formerly, Part 21 of the Commission's Rules) for common carrier fixed microwave services (except Multipoint Distribution Service).

[532] Persons eligible under parts 80 and 90 of the Commission's Rules can use Private Operational-Fixed Microwave services. *See* 47 C.F.R. Parts 80 and 90. Stations in this service are called operational-fixed to distinguish them from common carrier and public fixed stations. Only the licensee may use the operational-fixed station, and only for communications related to the licensee's commercial, industrial, or safety operations.

[533] Auxiliary Microwave Service is governed by Part 74 of Title 47 of the Commission's Rules. *See* 47 C.F.R. Part 74. This service is available to licensees of broadcast stations and to broadcast and cable network entities. Broadcast auxiliary microwave stations are used for relaying broadcast television signals from the studio to the transmitter, or between two points such as a main studio and an auxiliary studio. The service also includes mobile television pickups, which relay signals from a remote location back to the studio.

business specifically with respect to fixed microwave services. For purposes of this analysis, the Commission uses the SBA small business size standard for the category "Cellular and Other Telecommunications," which is 1,500 or fewer employees.[534] The Commission does not have data specifying the number of these licensees that have more than 1,500 employees, and thus is unable at this time to estimate with greater precision the number of fixed microwave service licensees that would qualify as small business concerns under the SBA's small business size standard. Consequently, the Commission estimates that there are up to 22,015 common carrier fixed licensees and up to 61,670 private operational-fixed licensees and broadcast auxiliary radio licensees in the microwave services that may be small and may be affected by the rules and policies adopted herein. We noted, however, that the common carrier microwave fixed licensee category includes some large entities.

180. *Offshore Radiotelephone Service.* This service operates on several UHF television broadcast channels that are not used for television broadcasting in the coastal areas of states bordering the Gulf of Mexico.[535] There are presently approximately 55 licensees in this service. We are unable to estimate at this time the number of licensees that would qualify as small under the SBA's small business size standard for "Cellular and Other Wireless Telecommunications" services.[536] Under that SBA small business size standard, a business is small if it has 1,500 or fewer employees.[537]

181. *Wireless Communications Services*. This service can be used for fixed, mobile, radiolocation, and digital audio broadcasting satellite uses. The Commission established small business size standards for the wireless communications services (WCS) auction. A "small business" is an entity with average gross revenues of $40 million for each of the three preceding years, and a "very small business" is an entity with average gross revenues of $15 million for each of the three preceding years. The SBA has approved these small business size standards.[538] The Commission auctioned geographic area licenses in the WCS service. In the auction, there were seven winning bidders that qualified as "very small business" entities, and one that qualified as a "small business" entity. We conclude that the number of geographic area WCS licensees affected by this analysis includes these eight entities.

182. *39 GHz Service.* The Commission created a special small business size standard for 39 GHz licenses – an entity that has average gross revenues of $40 million or less in the three previous calendar years.[539] An additional size standard for "very small business" is: an entity that, together with affiliates, has average gross revenues of not more than $15 million for the preceding three calendar years.[540] The SBA has approved these small business size standards.[541] The auction of the 2,173 39 GHz

[534] 13 C.F.R. § 121.201, NAICS code 517212.

[535] This service is governed by Subpart I of Part 22 of the Commission's Rules. *See* 47 C.F.R. §§ 22.1001-22.1037.

[536] 13 C.F.R. § 121.201, NAICS code 517212.

[537] *Id*.

[538] *See* Letter to Amy Zoslov, Chief, Auctions and Industry Analysis Division, Wireless Telecommunications Bureau, FCC, from Aida Alvarez, Administrator, SBA (Dec. 2, 1998).

[539] *See* Amendment of the Commission's Rules Regarding the 37.0-38.6 GHz and 38.6-40.0 GHz Bands, ET Docket No. 95-183, *Report and Order*, 63 FR 6079 (Feb. 6, 1998).

[540] *Id.*

licenses began on April 12, 2000 and closed on May 8, 2000. The 18 bidders who claimed small business status won 849 licenses. Consequently, the Commission estimates that 18 or fewer 39 GHz licensees are small entities that may be affected by the rules and policies adopted herein.

183. *Local Multipoint Distribution Service.* Local Multipoint Distribution Service (LMDS) is a fixed broadband point-to-multipoint microwave service that provides for two-way video telecommunications.[542] The auction of the 1,030 Local Multipoint Distribution Service (LMDS) licenses began on February 18, 1998 and closed on March 25, 1998. The Commission established a small business size standard for LMDS licenses as an entity that has average gross revenues of less than $40 million in the three previous calendar years.[543] An additional small business size standard for "very small business" was added as an entity that, together with its affiliates, has average gross revenues of not more than $15 million for the preceding three calendar years.[544] The SBA has approved these small business size standards in the context of LMDS auctions.[545] There were 93 winning bidders that qualified as small entities in the LMDS auctions. A total of 93 small and very small business bidders won approximately 277 A Block licenses and 387 B Block licenses. On March 27, 1999, the Commission re-auctioned 161 licenses; there were 40 winning bidders. Based on this information, we conclude that the number of small LMDS licenses consists of the 93 winning bidders in the first auction and the 40 winning bidders in the re-auction, for a total of 133 small entity LMDS providers.

184. *218-219 MHz Service.* The first auction of 218-219 MHz spectrum resulted in 170 entities winning licenses for 594 Metropolitan Statistical Area licenses. Of the 594 licenses, 557 were won by entities qualifying as a small business. For that auction, the small business size standard was an entity that, together with its affiliates, has no more than a $6 million net worth and, after federal income taxes (excluding any carry over losses), has no more than $2 million in annual profits each year for the previous two years.[546] In the *218-219 MHz Report and Order and Memorandum Opinion and Order*, we established a small business size standard for a "small business" as an entity that, together with its affiliates and persons or entities that hold interests in such an entity and their affiliates, has average annual gross revenues not to exceed $15 million for the preceding three years.[547] A "very small business" is defined as an entity that, together with its affiliates and persons or entities that hold interests in such an

(Continued from previous page)

[541] *See* Letter to Kathleen O'Brien Ham, Chief, Auctions and Industry Analysis Division, Wireless Telecommunications Bureau, FCC, from Aida Alvarez, Administrator, SBA (Feb. 4, 1998).

[542] *See Rulemaking to Amend Parts 1, 2, 21, and 25 of the Commission's Rules to Redesignate the 27.5-29.5 GHz Frequency Band, to Reallocate the 29.5-30.0 GHz Frequency Band, and to Establish Rules and Policies for Local Multipoint Distribution Service and for Fixed Satellite Services*, CC Docket No. 92-297, Second Report and Order, 12 FCC Rcd 12545 (1997).

[543] *Id.*

[544] *See id*.

[545] *See* Letter to Dan Phythyon, Chief, Wireless Telecommunications Bureau, FCC, from Aida Alvarez, Administrator, SBA (Jan. 6, 1998).

[546] *Implementation of Section 309(j) of the Communications Act – Competitive Bidding*, PP Docket No. 93-253, Fourth Report and Order, 59 FR 24947 (May 13, 1994).

[547] *Amendment of Part 95 of the Commission's Rules to Provide Regulatory Flexibility in the 218-219 MHz Service*, WT Docket No. 98-169, Report and Order and Memorandum Opinion and Order, 64 FR 59656 (Nov. 3, 1999).

entity and its affiliates, has average annual gross revenues not to exceed $3 million for the preceding three years.[548] The SBA has approved these size standards.[549] We cannot estimate, however, the number of licenses that will be won by entities qualifying as small or very small businesses under our rules in future auctions of 218-219 MHz spectrum.

185. *24 GHz – Incumbent Licensees.* This analysis may affect incumbent licensees who were relocated to the 24 GHz band from the 18 GHz band, and applicants who wish to provide services in the 24 GHz band. The applicable SBA small business size standard is that of "Cellular and Other Wireless Telecommunications" companies. This category provides that such a company is small if it employs no more than 1,500 persons.[550] According to Census Bureau data for 1997, there were 977 firms in this category that operated for the entire year.[551] Of this total, 965 firms had employment of 999 or fewer employees, and an additional 12 firms had employment of 1,000 employees or more.[552] Thus, under this size standard, the great majority of firms can be considered small. These broader census data notwithstanding, we believe that there are only two licensees in the 24 GHz band that were relocated from the 18 GHz band, Teligent[553] and TRW, Inc. It is our understanding that Teligent and its related companies have less than 1,500 employees, though this may change in the future. TRW is not a small entity. Thus, only one incumbent licensee in the 24 GHz band is a small business entity.

186. *24 GHz – Future Licensees.* With respect to new applicants in the 24 GHz band, the small business size standard for "small business" is an entity that, together with controlling interests and affiliates, has average annual gross revenues for the three preceding years not in excess of $15 million.[554] "Very small business" in the 24 GHz band is an entity that, together with controlling interests and affiliates, has average gross revenues not exceeding $3 million for the preceding three years.[555] The SBA has approved these small business size standards.[556] These size standards will apply to the future auction, if held.

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[548] *Id*.

[549] *See* Letter to Daniel B. Phythyon, Chief, Wireless Telecommunications Bureau, Federal Communications Commission, from Aida Alvarez, Administrator, Small Business Administration (Jan. 6, 1998).

[550] 13 C.F.R. § 121.201, NAICS code 517212.

[551] U.S. Census Bureau, 1997 Economic Census, Subject Series: Information, "Employment Size of Firms Subject to Federal Income Tax: 1997," Table 5, NAICS code 513322.

[552] *Id*. The census data do not provide a more precise estimate of the number of firms that have employment of 1,500 or fewer employees; the largest category provided is "Firms with 1,000 employees or more."

[553] Teligent acquired the DEMS licenses of FirstMark, the only licensee other than TRW in the 24 GHz band whose license has been modified to require relocation to the 24 GHz band.

[554] *Amendments to Parts 1, 2, 87 and 101 of the Commission's Rules to License Fixed Services at 24 GHz*, WT Docket No. 99-327, Report and Order, 15 FCC Rcd 16934, 16967 (2000); *see also* 47 C.F.R. § 101.538(a)(2).

[555] *Amendments to Parts 1, 2, 87 and 101 of the Commission's Rules to License Fixed Services at 24 GHz*, WT Docket No. 99-327, Report and Order, 15 FCC Rcd at 16967; *see also* 47 C.F.R. § 101.538(a)(1).

[556] *See* Letter to Margaret W. Wiener, Deputy Chief, Auctions and Industry Analysis Division, Wireless Telecommunications Bureau, FCC, from Gary M. Jackson, Assistant Administrator, SBA (July 28, 2000).

187. *Satellite Service Carriers*. The SBA has developed a size standard for small businesses within the category of Satellite Telecommunications. Under that SBA size standard, such a business is small if it has 1,500 or fewer employees.[557] According to Commission data, 31 carriers reported that they were engaged in the provision of satellite services.[558] Of these 31 carriers, an estimated 25 have 1,500 or fewer employees and six, alone or in combination with affiliates, have more than 1,500 employees.[559] Consequently, the Commission estimates that there are 31 or fewer satellite service carriers which are small businesses that may be affected by the rules and policies proposed herein.

188. *Cable and Other Program Distribution***.** This category includes cable systems operators, closed circuit television services, direct broadcast satellite services, multipoint distribution systems, satellite master antenna systems, and subscription television services. The SBA has developed small business size standard for this census category, which includes all such companies generating $12.5 million or less in revenue annually.[560] According to Census Bureau data for 1997, there were a total of 1,311 firms in this category, total, that had operated for the entire year.[561] Of this total, 1,180 firms had annual receipts of under $10 million and an additional 52 firms had receipts of $10 million or more but less than $25 million. Consequently, the Commission estimates that the majority of providers in this service category are small businesses that may be affected by the rules and policies adopted herein.

189. *Internet Service Providers.* The SBA has developed a small business size standard for Internet Service Providers (ISPs). ISPs "provide clients access to the Internet and generally provide related services such as web hosting, web page designing, and hardware or software consulting related to Internet connectivity."[562] Under the SBA size standard, such a business is small if it has average annual receipts of $21 million or less.[563] According to Census Bureau data for 1997, there were 2,751 firms in this category that operated for the entire year.[564] Of these, 2,659 firms had annual receipts of under $10 million, and an additional 67 firms had receipts of between $10 million and $24, 999,999. Consequently, we estimate that the majority of these firms are small entities that may be affected by our action.

190. *All Other Information Services*. This industry comprises establishments primarily engaged in providing other information services (except new syndicates and libraries and archives)."[565]

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[557] 13 CFR § 121.201, NAICS code 517410.

[558] *Telephone Trends Report* at Table 5.3.

[559] *Id.*

[560] 13 CFR § 121.201, NAICS code 517510.

[561] U.S. Census Bureau, 1997 Economic Census, Subject Series: Information, "Establishment and Firm Size (Including Legal Form of Organization)," Table 4, NAICS code 513220.

[562] 13 CFR § 121.201,NAICS code 518111.
<www.census.gov>.

[563] 13 C.F.R. § 121.201, NAICS code 518111.

[564] U.S. Census Bureau, 1997 Economic Census, Subject Series: Information, "Establishment and Firm Size (Including Legal Form of Organization)," Table 4, NAICS code 514191.
<www.census.gov>.

[565] U.S. Census Bureau, "2002 NAICS Definitions: 519190 All Other Information Services" (Feb. 2004)
(continued….)

We note that, in this *Further Notice*, we have described activities such as email, online gaming, web browsing, video conferencing, instant messaging, and other, similar IP-enabled services. The SBA has developed a small business size standard for this category; that size standard is $6 million or less in average annual receipts.[566] According to Census Bureau data for 1997, there were 195 firms in this category that operated for the entire year. Of these, 172 had annual receipts of under $5 million, and an additional nine firms had receipts of between $5 million and $9,999,999.[567] Consequently, we estimate that the majority of these firms are small entities that may be affected by our action.

4. Description of Projected Reporting, Recordkeeping and Other Compliance Requirements for Small Entities

191. This supplemental IRFA seeks comment on several rule changes and intercarrier compensation reform proposals under consideration that may affect reporting, recordkeeping and other compliance requirements for small entities. The type of rule changes under consideration are described below.

192. Any intercarrier compensation reform measures that achieve the Commission's goal of moving toward a more unified regime will relieve small entities of some administrative, recordkeeping, and other compliance requirements, but may also create new burdens.[568] As discussed within this *Further Notice*, the Commission is considering, and seeks comment on, several options for moving to a unified intercarrier compensation regime.[569] Each of these options relieves certain compliance burdens that exist under the current system, but, no option under consideration would be burden-free. Consequently, in this Supplemental IRFA the Commission seeks comment on burdens to small entities associated with each reform proposal under consideration.

193. Small entities face significant recordkeeping and compliance burdens under the current intercarrier compensation system, including determining the appropriate regulatory category for all traffic they send or receive, measuring the quantity of each type of traffic, and maintaining administrative systems and processes for intercarrier payments. Additionally, small entities must devote considerable resources to resolving disputes arising due to ambiguities in the rules defining the current intercarrier compensation regimes. A unified intercarrier compensation system with clear rules would reduce the need for small entities to devote resources to these tasks.

a. Bill-and-Keep

194. Some of the intercarrier compensation reform proposals received in this proceeding are

(Continued from previous page)
<www.census.gov>.

[566] 13 C.F.R. § 121.201, NAICS code 519190.

[567] U.S. Census Bureau, 1997 Economic Census, Subject Series: Information, "Establishment and Firm Size (Including Legal Form of Organization)," Table 4, NAICS Code 514199 (issued Oct. 2000). This category was created for the 2002 Economic Census by taking a portion of the superseded 1997 category, "All Other Information Services," NAICS code 514199. The data cited in the text above are derived from the superseded category.

[568] *See infra* paras. 194-202.

[569] *See supra* para. 39; See*, e.g.,* ARIC Proposal; CBICC Proposal; EPG Proposal.

based on a bill-and-keep approach.[570] Under a bill-and-keep approach, carriers would look to their own customers, rather than to other carriers, to recover costs. Carriers, including small entities, might have to modify their systems and processes to reflect this change in cost recovery. These modifications may present a compliance burden to small entities. Any compliance burden, however, may be outweighed by the burdens eliminated by the elimination of intercarrier charges. Additionally, carriers, including small entities, already have systems and processes designed to bill customers with which they have a retail relationship. While these systems and processes may have to be modified, these modifications are similar to those that occur in the normal course of business already.

195. If a bill-and-keep approach were adopted, the current network interconnection rules may have to be revised or replaced. Carriers would have to ensure that their agreements or arrangements with other carriers comply with any new network interconnection rules. Complying with any new or modified interconnection rules may impose a compliance burden on all carriers, including small entities. This burden may be offset by streamlined operation under new interconnection rules that resolve or eliminate the potential for the types of interconnection disputes that arise under the current rules.

196. The bill-and-keep plans under consideration include new universal service mechanisms.[571] Under these plans, carriers will have to determine their costs and demonstrate a shortfall between their costs and revenues in order to qualify for funding from cost recovery mechanisms. Further, some types of carriers, including small entities, may not be eligible for some of the cost recovery mechanisms included in some of the plans. Determining costs, determining eligibility under any new universal service plan, and administration related to any new universal service plan may represent significant burdens to small entities under a bill-and-keep plan.

b. Unified CPNP

197. The Commission is considering several unified CPNP plans submitted by industry groups comprised of small and medium sized rural LECs and CLECs.[572] Although these proposals are designed to reduce the overall compliance burdens associated with each compensation regime by applying the same rate to all types of traffic, they may cause certain specific compliance burdens to increase.

198. Under any CPNP approach, carriers would continue to look to other carriers to recover a portion of their costs, and would have to maintain systems and processes to bill other carriers for these new charges. The cost standard that would be used to determine the rates varies with each plan.[573] Under plans that apply a TELRIC or embedded cost methodology, carriers may need to perform cost studies using a methodology they have not previously used. Such cost calculations potentially represent a significant compliance and recordkeeping burden for small entities. Moreover, some of the unified CPNP

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[570] *See* ICF Proposal; Western Wireless Proposal.

[571] *See* ICF Proposal; Western Wireless Proposal.

[572] *See* ARIC Proposal, EPG Proposal, CBICC Proposal; ARIC is comprised of small rural LECs. EPG is comprised of small and medium sized rural LECs. CBICC is comprised of small and medium sized CLECs.

[573] For instance, the CBICC plan uses the TELRIC cost methodology to set compensation rates, CBICC Proposal at 1, the ARIC plan uses embedded carrier costs, ARIC Proposal at 39, and the EPG plan uses interstate access rates, EPG Proposal at 21.

plans under consideration in this proceeding propose rates that would vary by carrier and/or by state.[574] If such plans were adopted, carriers would have to design and implement administrative systems that track the origin and destination of traffic and account for differing state or carrier rates. Developing and implementing such administrative systems may present a significant compliance burden for small entities.

199. The *Further Notice* seeks comment on the need for new or revised network interconnection rules. Some of the CPNP plans submitted for consideration in this proceeding retain the current network interconnection rules. Varying and inconsistent interpretations of these interconnection rules have led to numerous disputes and uncertainty about how the rules are to be applied.[575] A CPNP plan that retains the current network interconnection rules will inherit this uncertainty surrounding the existing rules. Any changes in such rules also could result in new burdens for some carriers.

200. Adoption of a unified CPNP plan may necessitate changes in interconnection agreements. Interconnection agreements may be premised on rates that would be modified under a unified CPNP plan. Similarly, any change in interconnection rules could lead to renegotiation of agreements. Carriers, including small entities, would likely seek to renegotiate their existing interconnection agreements as a result of any new regime. Renegotiation of existing interconnection agreements may present a significant burden to small entities under a CPNP approach.

201. Each of the unified CPNP plans under consideration assumes revenue neutrality for incumbent LECs with significant funding coming from universal service mechanisms. Some of the plans also include new universal service mechanisms.[576] Under some plans, carriers will have to determine their costs and demonstrate a shortfall between their costs and revenues in order to qualify for funding from cost recovery mechanisms. Further, some types of carriers, including small entities, may not be eligible for some of the cost recovery mechanisms included in some of the plans. Determining costs, determining eligibility under any new universal service plan, and administration related to any new universal service plan may represent significant burdens to small entities under a unified CPNP plan.

c. Other Issues

202. In this *Further Notice*, the Commission seeks comment on several issues related to transit service.[577] If, as a result of this Further Notice, new rules related to transit service come into existence, these rules may impose burdens on some entities. Rules imposing transit service obligations would likely have no significant impact on ILECs already providing, or carriers already using transit service. For carriers that would be affected, the burdens may include determining the price of transit service purchased or provided, and developing additional administrative capabilities to account for providing or receiving transit service.

203. The Commission also seeks comment regarding possible changes to the intraMTA rule,

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[574] *See e.g.*, ARIC Proposal.

[575] *See e.g.*, *Sprint Corp. Petition for Declaratory Ruling Regarding the Routing and Rating of Traffic by ILECs*, CC Docket No. 01-92, Petition of Sprint (filed May 9, 2002) (Sprint Petition).

[576] For example, the ARIC plan proposes a State Equalization Fund, and the EPG plan includes an Access Restructure Charge. *See* ARIC Proposal at 73; EPG Proposal at 22.

[577] *See supra* Section II.H.1.

negotiation of CMRS interconnection agreements, and rating of CMRS traffic, as discussed in this *Further Notice*.[578] If the Commission changes the intraMTA rule, or otherwise changes parties' obligations, the new rules will likely relieve some burdens, including lowering the level of resources carriers must devote to resolving disputes arising from ambiguities in the current rules. Carriers may also experience burdens associated with bringing operations and interconnection agreements into compliance with the new rules.

5. Steps Taken to Minimize Significant Economic Impact on Small Entities, and Significant Alternatives Considered.

204. The RFA requires an agency to describe any significant alternatives that it has considered in reaching its proposed approach, which may include the following four alternatives (among others): (1) the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (2) the clarification, consolidation, or simplification of compliance or reporting requirements under the rule for small entities; (3) the use of performance, rather than design, standards; and (4) an exemption from coverage of the rule, or any part thereof, for small entities.

205. In this *Further Notice*, the Commission seeks comments on a variety of intercarrier compensation reform plans submitted in the record in this proceeding, as well as on other issues related to reform of the existing intercarrier compensation system. The Commission is aware that some of the proposals under consideration may create burdens for small entities. Consequently, the Commission seeks comments on alternatives that will minimize burdens, discussed below.

206. Several commenters have expressed a preference for maintaining a CPNP regime, and have submitted plans to replace or reform the current intercarrier compensation system with a more unified CPNP approach.[579] For instance, the ARIC plan includes a single rate based on embedded costs for each carrier.[580] The EPG plan uses current interstate access rates as a cost standard.[581] The CBICC plan uses the TELRIC costs of ILEC tandem switching to determine the intercarrier compensation rate.[582] The Commission seeks comment on the economic impact on small entities of these plans relative to other plans contained in the record, and to a bill-and-keep approach.

207. One non-unified option under consideration for intercarrier compensation system reform is to maintain a CPNP based system without immediately adopting a unified approach. For instance, NASUCA recommends a plan that reduces intrastate access charges over a five-year transition period, and

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[578] *See supra* Section II.H.2.

[579] *See supra* paras. 45-47; 48-50; 51 (discussing the EPG proposal, ARIC proposal, and CBICC proposal).

[580] *See* ARIC Proposal at 39.

[581] *See* EPG Proposal at 21.

[582] *See* CBICC Proposal at 1.

then moves to more unified rates.[583]

208. Another non-unified approach the Commission is considering includes use of an incremental cost methodology to meet the section 252(d) "additional cost" standard for reciprocal compensation.[584] The Commission seeks comment on the economic impact of such a plan relative to other plans contained in the record, and to a bill-and-keep approach.

209. Throughout this proceeding, the Commission has recognized the unique needs and interests of small entities.[585] In this *Further Notice* the Commission seeks comment on several issues and measures under consideration that are uniquely applicable to small entities. Specifically, the Commission seeks comment on whether any intercarrier compensation reform measures adopted should be revenue neutral.[586] The Commission also seeks comment on the impact of reduced intercarrier revenues to small entities in the event that a bill-and-keep approach is adopted.[587]

210. The Commission also seeks comment on whether separate network interconnection rules are necessary or appropriate for small entities, such as rate-of-return carriers.[588] Parties responding to this supplemental IRFA supporting such an approach should explain how separate rules would be structured, and what criteria would be used to determine whether an entity qualified to use the separate rules.

211. Additionally, the Commission seeks comment on whether separate cost recovery mechanisms unique to small entities are necessary or appropriate. Parties responding to this Supplemental IRFA in support of separate cost recovery mechanisms for small entities should explain how the separate cost recovery mechanisms would operate, how they would be funded, and what criteria would be used to determine what entities qualify for funding from the separate mechanisms. Further, the Commission seeks comment on the feasibility of retaining an intercarrier compensation mechanism for small entities only, while moving to another system (*e.g.* bill-and-keep) for all other entities. Parties advocating this approach should explain how a system of intercarrier payments available only to small entities would be integrated with another intercarrier compensation mechanism, such as a bill-and-keep system, that is in place for other carriers.

212. Finally, the Commission seeks comment on whether separate consideration for small entities is necessary or appropriate for each of the following issues previously discussed in this *Further Notice*: the potential impact of rules imposing transit service obligations;[589] the potential impact of rules

[583] *See* NASUCA Intercarrier Compensation Proposal, December 14, 2004, attached to Letter from Phillip F. McClelland, Senior Assistant Consumer Advocate, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92 (filed December 14, 2004).

[584] *See supra* para. 72.

[585] *See Intercarrier Compensation NPRM*, 16 FCC Rcd at 9656, para. 128.

[586] *See supra* para. 100.

[587] *See supra* para. 106.

[588] *See supra* para. 94.

[589] *See supra* paras. 127-33.

related to negotiation of CMRS interconnection;[590] and the potential impact of rules related to rating and routing of CMRS traffic.[591]

6. Federal Rules that may duplicate, overlap, or conflict with the proposed rules

213. Implementation of any of the rule changes the Commission is considering in this Further Notice may require extensive modifications to existing Federal Rules. The need for modifications does not necessarily mean that the new rules duplicate, overlap, or conflict with existing rules. Rather, amendments to the existing rules would be necessary to codify the policies the Commission adopts. The sections of the Commission's rules that would likely have to be amended include, without limitation, the following: Part 32: Uniform System of Accounts for Telecommunications Companies;[592] Part 36: Jurisdictional Separations Procedures; Standard Procedures for Separating Telecommunications Property Costs, Revenues, Expenses, Taxes, and Reserves for Telecommunications Companies;[593] Part 51: Interconnection;[594] Part 54: Universal Service;[595] Part 61: Tariffs;[596] and Part 69: Access Charges.[597]

B. Comment Filing Procedures

214. Pursuant to sections 1.415 and 1.419 of the Commission's rules,[598] interested parties may file comments within 60 days after this *Further Notice* is published in the Federal Register and reply comments within 90 days after this *Further Notice* is published in the Federal Register. Comments may be filed using the Commission's Electronic Comment Filing System (ECFS) or by filing paper copies.[599] Comments filed through the ECFS can be sent as an electronic file via the Internet to http://www.fcc.gov/cgb/ecfs/. Generally, only one copy of an electronic submission must be filed. If multiple docket or rulemaking numbers appear in the caption of the proceeding, commenters must transmit one electronic copy of the comments to each docket or rulemaking number referenced in the caption. In completing the transmittal screen, commenters should include their full name, U.S. Postal Service mailing address, and the applicable docket or rulemaking number, in this case, **CC Docket No. 01-92**. Parties may also submit an electronic comment by Internet e-mail. To get filing instructions for e-

[590] *See supra* paras. 139-40.

[591] *See supra* paras. 141-43.

[592] 47 CFR § 32.1 *et seq*.

[593] 47 CFR § 36.1 *et seq*.

[594] 47 CFR § 51.1 *et seq*.

[595] 47 CFR § 54.1 *et seq*.

[596] 47 CFR § 61.1 *et seq*.

[597] 47 CFR § 69.1 *et seq*.

[598] 47 C.F.R. §§ 1.415, 1.419.

[599] *See Electronic Filing of Documents in Rulemaking Proceedings*, GC Docket No. 97-113, Report and Order, 13 FCC Rcd 11322 (1998).

mail comments, commenters should send an e-mail to ecfs@fcc.gov, and should include the following words in the body of the message, "get form." A sample form and directions will be sent in reply. Parties who choose to file by paper must file an original and four copies of each filing. If more than one docket or rulemaking number appears in the caption of this proceeding, commenters must submit two additional copies for each additional docket or rulemaking number.

215. Filings can be sent by hand or messenger delivery, by commercial overnight courier, or by first-class or overnight U.S. Postal Service mail (although we continue to experience delays in receiving U.S. Postal Service mail). **Parties are strongly encouraged to file comments electronically using the Commission's ECFS.**

216. The Commission's contractor, Natek, Inc., will receive hand-delivered or messenger-delivered paper filings for the Commission's Secretary at 236 Massachusetts Avenue, N.E., Suite 110, Washington, D.C. 20002.

-The filing hours at this location are 8:00 a.m. to 7:00 p.m.

-All hand deliveries must be held together with rubber bands or fasteners.

-Any envelopes must be disposed of before entering the building.

-Commercial overnight mail (other than U.S. Postal Service Express Mail and Priority Mail) must be sent to 9300 East Hampton Drive, Capitol Heights, MD 20743.

-U.S. Postal Service first-class mail, Express Mail, and Priority Mail should be addressed to 445 12th Street, SW, Washington, D.C. 20554.

217. All filings must be addressed to the Commission's Secretary, Marlene H. Dortch, Office of the Secretary, Federal Communications Commission, 445 12th Street, SW, Washington, D.C. 20554. Parties should also send a copy of their filings to Victoria Goldberg, Pricing Policy Division, Wireline Competition Bureau, Federal Communications Commission, Room 5-A266, 445 12th Street, SW, Washington, D.C. 20554, or by e-mail to victoria.goldberg@fcc.gov. Parties shall also serve one copy with the Commission's copy contractor, Best Copy and Printing, Inc. (BCPI), Portals II, 445 12th Street, SW, Room CY-B402, Washington, D.C. 20554, (202) 488-5300, or via e-mail to fcc@bcpiweb.com.

218. Documents in CC Docket No. 01-92 are available for public inspection and copying during business hours at the FCC Reference Information Center, Portals II, 445 12th St. SW, Room CY-A257, Washington, DC 20554. The documents may also be purchased from BCPI, telephone (202) 488-5300, facsimile (202) 488-5563, TTY (202) 488-5562, e-mail fcc@bcpiweb.com.

C. Initial Paperwork Reduction Act Analysis

219. This document does not contain proposed information collection(s) subject to the Paperwork Reduction Act of 1995 (PRA), Public Law 104-13. In addition, therefore, it does not contain any new or modified "information collection burden for small business concerns with fewer than 25 employees," pursuant to the Small Business Paperwork Relief Act of 2002, Public Law 107-198, *see* 44 U.S.C. 3506(c)(4).

IV. ORDERING CLAUSES

220. Accordingly, IT IS ORDERED that, pursuant to the authority contained in sections 1-5, 7, 10, 201-05, 207-09, 214, 218-20, 225-27, 251-54, 256, 271, 303, 332, 403, 405, 502 and 503 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151-155, 157, 160, 201-05, 207-09, 214, 218-20, 225-27, 251-54, 256, 271, 303, 332, 403, 405, 502, and 503 and sections 1.1, 1.421 of the Commission's rules, 47 C.F.R. §§ 1.1, 1.421, NOTICE IS HEREBY GIVEN of the rulemaking and COMMENT IS SOUGHT on those issues.

221. IT IS FURTHER ORDERED that the Commission's Consumer and Governmental Affairs Bureau, Reference Information Center, SHALL SEND a copy of this Further Notice of Proposed Rulemaking, including the Supplemental Initial Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration.

FEDERAL COMMUNICATIONS COMMISSION

Marlene H. Dortch
Secretary

APPENDIX A

INTERCARRIER COMPENSATION NPRM
CC DOCKET NO. 01-92

COMMENTS

ACS of Anchorage, Inc.
Ad Hoc Telecommunications Users Committee (Ad Hoc)
Alaska Telephone Association
Allegiance Telecom, Inc.
Allied Personal Communications Industry
ALLTEL Communications Inc.
America Online, Inc. (AOL)
AT&T Corp.
AT&T Wireless Services, Inc.
BellSouth Corp.
Cable & Wireless USA
Cablevision Lightpath, Inc.
California Public Utilities Commission (California Commission)
Cbeyond Communications
Cellular Telecommunications & Internet Association (CTIA)
CenturyTel, Inc.
Competitive Telecommunications Association (CompTel)
Florida Public Service Commission (Florida Commission)
Focal Communications Corp., Pac-West Telecomm, Inc., RCN Telecom Services, Inc., and US LEC Corp. (Focal *et al.*)
General Services Administration (GSA)
Global Crossing Ltd.
Global NAPs Inc.
Guyana Telephone & Telegraph Ltd.
GVNW Consulting, Inc.
Home Telephone Company, Inc.
ICORE Inc.
Illinois Commerce Commission (Illinois Commission)
Independent Telephone & Telecommunications Alliance
Information Technology Association of America
Iowa Utilities Board (Iowa Commission)
ITC's, Inc.
KMC Telecom, Inc.
Level 3 Communications
Maryland Office of the People's Counsel (MD-OPC)
Michigan Exchange Carriers Association, Inc. (MECA)
Mid Missouri Cellular
Minnesota Independent Coalition
Missouri Public Service Commission (Missouri Commission)
Missouri Small Telephone Company Group (MSTG)
Mpower Communications Corp.
National Association of Regulatory Utility Commissioners (NARUC)

National Association of State Utility Consumer Advocates (NASUCA)
National Exchange Carrier Association, Inc. (NECA)
National Telephone Cooperative Association (NTCA)
New York State Department of Public Service (New York Commission)
Nextel Communications, Inc.
North County Communications
National Rural Telecom Association and the Organization for the Promotion and Advancement of Small Telecommunications Companies (NRTA/OPASTCO)
Office of the Public Utility Counsel of Texas (Texas Counsel)
Oklahoma Rural Telephone Coalition
Onvoy, Inc.
Parrish, Blessing & Associates
Personal Communications Industry Association (PCIA)
Public Service Commission of Wisconsin (Wisconsin Commission)
Public Utility Commission of Texas (Texas Commission)
Qwest Communications International Inc.
Regulatory Utility Commission of Alaska (Alaska Commission)
Ronan Telephone Company Consumer Advisory Committee (Ronan Advisory)
Ronan Telephone Company and Hot Springs (Ronan/Hot Springs)
Rural Independent Competitive Alliance (RICA)
Rural Telecommunications Group (RTG)
SBC Communications, Inc.
Singapore Telecommunications Limited
Sprint Corp.
Telecom Consulting Associates, Inc. (TCA)
Time Warner Telecom
Triton PCS License Company, LLC
United States Telecom Association (USTA)
United Utilities, Inc.
Verizon
Verizon Wireless
VoiceStream Wireless Corp.
Western Alliance
WorldCom, Inc.
Z-Tel Communications, Inc.

REPLIES

ACS of Anchorage, Inc.
Ad Hoc Telecommunications Users Committee
Advanced Paging, Inc., A.V. Lauttamus Communications, Inc., and NEP, LLC (Advanced Paging *et al.*)
Allegiance Telecom, Inc.
Alliance of Incumbent Rural Independent Telephone Companies and the Independent Alliance
Allied Personal Communications Industry Association of California
ALLTEL Communications, Inc.
Arch Wireless, Inc.
Association for Local Telecommunications Services (ALTS)
AT&T
AT&T Wireless Services, Inc.

BellSouth Corp.
Cable & Wireless USA
Cablevision Lightpath, Inc.
California Public Utilities Commission (California Commission)
Cellular Telecommunications & Internet Association (CTIA)
Cincinnati Bell Telephone
Cook Telecom, Inc.
District of Columbia Office of the People's Counsel (DC People's Counsel)
e.spire Communications, Inc. and KMC Telecom, Inc. (e.spire and KMC)
Focal Communications Corp., Pac-West Telecomm, Inc., RCN Telecom Services, Inc. and US LEC Corp. (Focal *et al.*)
General Services Administration (GSA)
Genuity Solutions, Inc.
Global NAPs, Inc.
GVNW Consulting, Inc.
Independent Telephone & Telecommunications Alliance
Information Technology Association of America
Leap Wireless International
Level 3 Communications, LLC
Maryland Office of People's Counsel (MD-OPC)
Midwest Wireless Communications LLC, Midwest Wireless Iowa LLC, and Midwest Wireless Wisconsin LLC (Midwest)
Missouri Independent Telephone Group (MITG)
Missouri Small Telephone Company Group (MSTG)
National Association of State Utility Consumer Advocates (NASUCA)
National Exchange Carrier Association, Inc. (NECA)
National Rural Telephone Association and Organization for the Promotion and Advancement of Small Telecommunications Companies (NRTA/OPASTCO)
National Telephone Cooperative Association (NTCA)
Network Services LLC
Nextel Communications, Inc.
North County Communications
Office of the Public Utility Counsel of Texas (Texas Counsel)
Personal Communications Industry Association (PCIA)
Qwest Communications International, Inc.
Ronan Telephone Company Consumer Advisory Committee (Ronan Advisory)
Rural Cellular Association
Rural Independent Competitive Alliance (RICA)
Rural Telecommunications Group (RTG)
SBC Communications, Inc.
Small Business Administration, Office of Advocacy (SBA)
Small Company Group of New York
Sprint Corp.
SureWest Communications
Taylor Communications Group, Inc.
Telecom Consulting Associates, Inc. (TCA)
Time Warner Telecom
Triton PCS License Company, LLC
United States Telecom Association (USTA)

Verizon
Verizon Wireless
VoiceStream Wireless Corp.
WebLink Wireless, Inc.
WorldCom, Inc.

APPENDIX B

T-MOBILE USA, WESTERN WIRELESS, NEXTEL COMMUNICATIONS
AND NEXTEL PARTNERS PETITION
CC DOCKET NO. 01-92

COMMENTS

Alliance of Incumbent Rural Independent Telephone Companies
AT&T Corp.
AT&T Wireless Services, Inc.
BellSouth Corp.
Cellular Telecommunication & Internet Association (CTIA)
Cingular Wireless LLC
Fred Williamson & Associates, Inc.
Frontier & Citizens Incumbent Local Exchange Carriers
ICORE, Inc.
John Staurulakis, Inc. (JSI)
Michigan Rural Incumbent Local Exchange Carriers
Minnesota Independent Coalition
Missouri Independent Telephone Company Group (MITG)
Missouri Small Telephone Company Group (MSTG)
Montana Local Exchange Carriers
National Telecommunications Cooperative Association (NTCA)
Nebraska Rural Independent Companies
Oklahoma Rural Telephone Companies
Organization for the Promotion and Advancement of Small Telecommunications Companies (OPASTCO)
Qwest Communications International, Inc.
Rural Cellular Association and Rural Telecommunications Group
Rural Incumbent Local Exchange Carriers (Rural ILEC)
Rural Iowa Independent Telephone Association
SBC Communications, Inc.
South Dakota Telephone Assoc., et. al.
Sprint Corp.
Telecom Consulting Associates, Inc.
Triton PCS License Company, LLC
United States Cellular Corp.
United States Telecom Association (USTA)
Verizon Wireless
Warinner, Gesigner & Associates, LLC
Warinner, Gesigner & Associates on behalf of KLM Telephone Company, *et al*.

REPLIES

Alabama Rural Local Exchange Carriers
AT&T Corp.
AT&T Wireless Services, Inc.
Beacon Telecommunications Advisors, LLC
California RTCs
Cellular Telecommunication & Internet Association (CTIA)
Fred Williamson & Associates Inc.
GVNW Consulting, Inc.
Joint CMRS Petitioners
Minnesota Independent Coalition
Missouri Independent Telephone Company Group (MITG)
Missouri Small Telephone Company Group (MSTG)
Montana Local Exchange Carriers
National Exchange Carrier Association, Inc. (NECA)
Nebraska Rural Independent Companies
Oklahoma Rural Telephone Companies
Organization for the Promotion and Advancement of Small Telecommunications Companies (OPASTCO)
Rural Carriers (TDS Telecommunications Corp. *et al.*)
SBC Communications, Inc.
Supra Telecommunications & Information Systems, Inc.
Triton PCS License Company, LLC
Verizon Wireless

APPENDIX C

A BILL-AND-KEEP APPROACH TO INTERCARRIER COMPENSATION REFORM

An Analysis of Pleadings in CC Docket No. 01-92 by the Staff of the Wireline Competition Bureau

The following report was prepared by the staff of the Wireline Competition Bureau for inclusion in the record of the *Intercarrier Compensation* rulemaking.[1] As explained in footnote 106 of the *Further Notice*, this staff report does not represent the views of, and is not endorsed by, the Commission.[2]

In the *Further Notice* in this proceeding, the Commission concluded that there is an urgent need for comprehensive reform of the existing intercarrier compensation rules. The Commission noted that many parties support moving to a unified compensation regime, but that there is no consensus as to what type of regime the Commission should adopt. As a general matter, parties have advocated two different types of unified regimes – a bill-and-keep regime and a unified calling party's network pays (CPNP) regime. Bill-and-keep can be thought of as a unified compensation regime with a rate of zero. Under a bill-and-keep regime, carriers do not charge each other for the origination and termination of traffic. Rather, carriers recover all their costs from their subscribers. In contrast, under a unified CPNP regime, carriers would continue to compensate each other for the termination of traffic, but the rate charged by any particular carrier would be the same for all types of traffic. In some cases, a unified CPNP regime also would require long distance carriers to continue paying local exchange carriers for the origination of traffic.

In response to the *Intercarrier Compensation NPRM*, many parties submitted comments on the relative merits of bill-and-keep and a unified CPNP approach to intercarrier compensation reform. The following staff analysis of the principle arguments in the record regarding bill-and-keep is offered to aid the Commission and interested parties in further consideration of these issues.[3]

1. Bill-and-Keep and Cost Causation

In the *Intercarrier Compensation NPRM*, the Commission sought comment on the assumption underlying its current rules that the calling party is the sole cost causer and sole beneficiary of a call and therefore bill-and-keep makes sense only in certain narrow circumstances. In this section, we re-evaluate

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[1] *Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, Notice of Proposed Rulemaking, 16 FCC Rcd 9610 (2001) (*Intercarrier Compensation NPRM*); Further Notice of Proposed Rulemaking, FCC 05-33 (rel. Mar. 3, 2005) (*Further Notice*).

[2] *See Further Notice*, para. 38 n.106.

[3] This report focuses on the question of whether a regime with a compensation rate of zero is preferable to one with a positive compensation rate. The report does not address the interconnection and transport issues that must be considered as part of either type of regime. These issues are discussed in section II(E) of the *Further Notice*.

the relative benefits of a bill-and-keep approach to intercarrier compensation based on the record developed in this proceeding.

Bill-and-keep provides a mechanism whereby end users pay for the benefit of making and receiving calls.[4] Thus, bill-and-keep is consistent with the assumption that both the calling party and the called party may benefit from any given call, and, therefore, that the originating and the terminating networks should share the costs associated with the call by recovering their costs from their own end-user customers. Several commenters support the notion that both the calling and called parties benefit from any given call.[5] Similarly, some parties recognize that the nature of telephonic communication is the interactive process of exchanging information between two parties rather than the relaying of data in one direction.[6] For example, Level 3 argues that bill-and-keep is consistent with the way customers currently use communications networks and cause costs to be incurred.[7]

Other commenters, however, contend that there is an insufficient basis for altering the historical assumption that the calling party is responsible for the costs of the call.[8] They also challenge the notion that the benefits of any given call are always shared between the calling party and called party.[9] For instance, some commenters argue that only the calling party can assess the benefit of any given call because only the calling party knows the content of the call.[10] They explain that the called party does not benefit in the case of unwanted calls, and that a bill-and-keep regime would require the called party to pay for receipt of these calls.[11] Moreover, even if the called party receives some benefits of a call, commenters contend that a bill-and-keep approach assumes incorrectly that the calling and called parties benefit equally, and that, therefore, such an approach would not accurately capture the relative benefits of a call.[12]

We are not persuaded that principles of cost causation require retention of a CPNP regime. The purpose of a telephone call is to facilitate communications between two or more parties.[13] These

[4] *Intercarrier Compensation NPRM*, 16 FCC Rcd at 9625, para 37.

[5] *See, e.g.*, AT&T Wireless Comments at 30; Verizon Wireless Comments at 17, 19; AT&T Wireless Reply at 14-17; Cable & Wireless Reply at 5-6.

[6] *See, e.g.,* AT&T Wireless Comments at 30; AT&T Wireless Reply at 15-16; Level 3 Reply at 13.

[7] *See* Level 3 Reply at 13.

[8] *See, e.g.,* Allegiance Reply at 5; SBA Reply at 3-6.

[9] *See, e.g.,* Allegiance Reply at 5; ALTS Reply at 7; MD-OPC Reply at 20-21; NTCA Reply at 7-8.

[10] *See, e.g.,* MD-OPC Comments at 24-26; NTCA Comments at 16; Allegiance Reply at 5; Focal *et al.* Reply at 23; MD-OPC Reply at 16-18; SBA Reply at 5.

[11] *See, e.g.,* ALTS Reply at 7; AT&T Reply at 16; Focal *et al*. Reply at 21-22; MD-OPC Reply at 8-9, 20-21; NTCA Reply at 8.

[12] *See, e.g.,* Ad Hoc Comments at 5; Focal *et al*. Comments at 43-44; Allegiance Reply at 5; ALTS Reply at 7; AT&T Reply at 17; DC People's Counsel Reply at 15; Focal *et al*. Reply at 20, 24; NASUCA Reply at 18-19. *See also* Ad Hoc Reply at 15-16 (arguing that bill-and-keep would entail making untested assumptions about benefits and responsibilities).

[13] *See* AT&T Wireless Comments at 25; AT&T Wireless Reply at 15.

communications enable the exchange of information between the parties, not just the relaying of information to a recipient.[14] Although the calling party decides to place the call, the called party must decide to answer and continue the communication.[15] The communication therefore is a two-way joint interaction between the calling party and called party.[16] Each party is capable of taking measures to avoid call-related costs, if any.[17] Moreover, in the current networking environment, consumers are increasingly connected through a number of communications devices and express a desire to be connected with others through these devices.[18] Thus, the need or desire to exchange information causes the communications, rather than the party initiating the communication.[19]

AT&T initially supported a CPNP approach on the grounds that all calls have both positive and negative externalities, and that only a CPNP regime permits parties to internalize properly these externalities.[20] By positive externalities, AT&T appears to refer to the fact that called parties benefit from receiving calls even though they generally do not pay for them.[21] Negative externalities, on the other hand, result from the fact that the called party does not want some calls even if there is no cost associated with them.[22] AT&T explains that CPNP requires the calling party to internalize a greater portion of the costs, which limits incentives to make unwanted calls, and it states that there are a variety of conventions under CPNP that allow parties to align the costs of calls with the corresponding benefits.[23]

For a variety of reasons, we disagree that a consideration of the externalities identified by AT&T justifies retention of a CPNP approach. With respect to negative call externalities, *i.e.*, unwanted calls, the Commission explains in the *Further Notice* that there have been significant developments in the

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[14]*See* A&T Wireless at 16-17.

[15]*See, e.g.,* Qwest Comments at 20; Cable & Wireless Reply at 6; Qwest Reply at 14.

[16]*See, e.g.,* Qwest Comments at 20; Cable & Wireless Reply at 6.

[17]*See, e.g.,* Sprint Comments at 15; Qwest Reply at 14.

[18]*See* Level 3 Reply at 13.

[19]*See* AT&T Wireless Comments at 25.

[20]AT&T Reply at 14-15. We note that AT&T's position regarding bill-and-keep has evolved over the course of this proceeding and, as a member of the Intercarrier Compensation Forum, AT&T now supports a bill-and-keep proposal. We nevertheless address many of the concerns initially identified by AT&T in order to provide a more thorough analysis.

[21]AT&T Comments, Attached Declaration of Janusz A. Ordover and Robert D. Willig, at 14, para. 27.

[22]*Id*. at 14-15, para. 28. The externalities addressed by AT&T are externalities associated with individual calls. The economics literature also recognizes network externalities that result because the addition of a new subscriber to a network benefits other subscribers on the network, as well as subscribers of any interconnected networks, none of whom pays for this benefit. We note that this is the rationale usually given for universal service programs, in which some users subsidize other subscribers. A CPNP approach is not necessary, however, for funding a universal service program. Funding universal service through a CPNP regime means that rates are set above incremental cost, which may discourage efficient usage of the network.

[23]AT&T Reply at 15 (describing these conventions as agreements between the parties to take turns calling each other or to limit the length of a telephone conversation).

marketplace that can assist consumers in managing if, how, and when they use telecommunication services.[24] Accordingly, customers now possess the ability to reduce significantly any negative externalities on their own.[25] Moreover, if the incremental cost of origination and termination is zero (or close to zero), even a regime that requires the calling party to bear all the costs of the call may be a very limited deterrent for unwanted calls.[26] Conversely, setting prices high enough to deter unwanted calls also would be expected to deter many calls that are mutually beneficial to both parties to a call.

Similarly, we are not convinced that a CPNP regime addresses positive call externalities any better than a bill-and-keep regime would. AT&T assumes that parties will take turns calling each other or follow other tacit conventions so that they bear costs in relation to the benefit they receive from calls. Despite the theoretical ability of callers under a CPNP regime to internalize positive call externalities in this way, it is not at all clear whether this occurs in practice to any significant extent. Indeed, it seems likely that one reason consumers have embraced flat-rated, bundled service offerings is because, for a consumer who subscribes to such an offering, there is no additional cost to being the calling party and therefore no need to worry about taking turns or otherwise shifting costs among parties. If the type of coordination described by AT&T is not actually used to redistribute the benefits of calls, and if the benefits of a call to the calling and called parties are relatively equal on average, then it is reasonable to expect that a greater proportion of socially efficient calls will be completed under a bill-and-keep regime than under a CPNP regime.

Some commenters contend that bill-and-keep assumes incorrectly that each party benefits equally from a call and therefore does not capture the relative benefits of a call to the calling and called parties.[27] Regulators cannot realistically institute a regime that perfectly reflects the division of benefits for each and every call. Thus, any approach that the Commission adopts must generalize the relative benefits to some degree. The relevant question is whether, judging from the overarching policy goals discussed in the *Further Notice*,[28] the simplifying assumptions underlying a bill-and-keep regime are preferable to the assumptions underlying a CPNP regime.[29] As one commenter points out, there is no evidence that the prevailing assumption that all the benefits flow to the calling party and none to the called party is more realistic than an assumption that the benefits flow to each party equally.[30] Indeed, because consumers have the incentive and the ability to avoid, or reduce the duration of, unwanted calls, we believe that the

[24]*Further Notice*, paras. 25-27.

[25]*See* Sprint Reply at 8.

[26]The immediate success of the Do Not Call list suggests that direct regulation of the problem of unwanted calls has provided a far greater deterrent effect than our intercarrier compensation rules ever did. *See* News Release, Statement of FTC Chairman Timothy J. Muris, Federal Trade Commission, 2004 WL 1217081 (June 3, 2004) (describing the overwhelming success of the National Do-Not-Call Registry).

[27]*See, e.g.,* Ad Hoc Comments at 5-8; Focal *et al*. Comments at 43-44; Allegiance Reply at 5; ALTS Reply at 7; AT&T Reply at 17; DC People's Counsel Reply at 15; Focal *et al*. Reply at 20, 24; NASUCA Reply at 18-19.

[28]*See Further Notice*, paras. 29-36.

[29]*See, e.g.,* Cable & Wireless Reply at 5-6; Qwest Reply at 14-15.

[30]*See* Cable & Wireless Reply at 5.

better assumption is one that reflects some benefit to both the calling party and the called party.[31]

Commenters opposing a bill-and-keep regime on efficiency grounds often cite the example of unwanted calls, such as telemarketing calls, to demonstrate a case where the called party receives no benefit and must cover some cost of the unwanted call.[32] Intercarrier compensation is neither the source of unwanted calls nor the solution to the unwanted call problem. The most direct and efficient response to the problem of unwanted calls is to empower consumers to manage their own telecommunications services. Consumers can avail themselves of a number of tools to manage if, how, and when they use telecommunication services.[33] Screening services such as caller ID and others give customers greater control over the calls they receive.[34] The development of "Do-Not-Call" registries also gives consumers greater control over unwanted calls. Moreover, called parties always have the ability immediately to terminate an unwanted call.[35] In light of these developments, we do not see any reason why the possibility of unwanted calls should preclude us from adopting a compensation regime that is premised on the assumption that both parties may benefit from any given call.

Additional arguments opposing bill-and-keep on economic grounds are based on the assumption that costs depend on the number or duration of calls on the network, rather than on connectivity to the network (*i.e.*, that costs are incurred on a per-minute or per-call basis, rather than a per-line basis). For instance, the Maryland Office of People's Counsel makes a number of arguments alleging subsidization, "free" service, and the potential misallocation of common costs under a bill-and-keep regime.[36] Similarly, the Ad Hoc Telecommunications Users Committee asserts that a fundamental flaw of a bill-and-keep approach is that it would essentially price traffic below cost, and that pricing below cost distorts the market as much as pricing above cost.[37]

We have two responses to these arguments. First, as explained above, we believe that a CPNP approach is problematic in a competitive marketplace because it allows networks to shift costs to other networks. Consequently, even if additional minutes or calls increase a carrier's costs, there is no reason why each carrier should not recover these costs from its subscribers, rather than from each other. Second, underlying all these arguments is a fundamental presumption that most network costs are incurred on a per-minute or per-call basis, *i.e.*, that a doubling of the number of calls or minutes would double total network costs, and that each call therefore imposes additional costs on recipients. As described by the Commission in the *Further Notice*, it does not appear that minutes-of-use are a significant determinant of

[31] *See, e.g.,* Qwest Comments at 20-21.

[32] *See, e.g.,* ALTS Reply at 7; AT&T Reply at 16; Focal *et al*. Reply at 21-22; MD-OPC Reply at 8-9, 20-21.

[33] *See Further Notice*, paras. 25-27.

[34] *See, e.g.*, AT&T Wireless Comments at 31; Qwest Comments at 39; Verizon Wireless Comments at 19; Qwest Reply at 18.

[35] *But see* MD-OPC Reply at 18-19 (arguing that most costs are incurred before the called party can terminate the unwanted call).

[36] *See* MD-OPC Reply at 6-8, 13-15, 21-22, 28-30. *See also* Focal *et al*. Reply at 17 (arguing that incumbent LECs would experience a windfall under bill-and-keep because termination costs are already built into local rates).

[37] Ad Hoc Comments at 2-3. *See also* NASUCA Reply at 14.

costs given developments in telecommunications technologies.[38] The Commission long ago recognized this with respect to loop costs, which are a function of subscriber density and choice of technology.[39] For similar reasons, it appears that switching costs are primarily a function of the number of subscribers, rather than the number of calls or MOU, because a reduction in call minutes per subscriber would not substantially reduce the investment and operating cost of the switch serving those customers, at least in the case of wireline networks.[40] In the *Further Notice*, the Commission seeks additional comment on the degree to which network costs vary with MOU for different types of networks and technologies, and whether to change its rules in order to reduce, if not eliminate, per-minute charges.[41]

2. Bill-and-Keep and Competitive Neutrality

As the Commission acknowledged in the *Intercarrier Compensation NPRM*, any discrepancy in regulatory treatment that is not based on differences in underlying economic costs is likely to raise regulatory arbitrage concerns.[42] In particular, the Commission observed that "parties will revise or rearrange transactions to exploit a more advantageous regulatory treatment, even though such actions, in the absence of regulation, would be viewed as costly or inefficient."[43] Under the existing regimes, different types of carriers are subject to different rules and pricing methodologies when they provide services with the same or similar costs. For example, according to the Intercarrier Compensation Forum, interexchange carriers pay average interstate access charges ranging from 0.6 cents per minute to 1.8 cents per minute to terminate traffic, depending on the LEC involved, whereas LECs pay average reciprocal compensation rates of 0.2 cents per minute to terminate traffic.[44] Moreover, CMRS carriers are

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[38]*See Further Notice*, paras. 23, 67-68. *See also* Qwest Comments at 13 (arguing that per-minute cost recovery fails to reflect the way costs actually are incurred).

[39]*See MTS and WATS Market Structure*, CC Docket No. 78-72, Third Report and Order, Phase 1, 93 FCC 2d 241, 278, para. 121 (1983) (finding that a subscriber who does not use the subscriber line to place or receive interstate calls imposes the same non-traffic sensitive costs as a subscriber who does use the line) (subsequent history omitted).

[40]*See Further Notice*, paras. 67-68 (discussing the comments of MCI and AT&T in the TELRIC proceeding). The Bureau reached a similar conclusion in the Virginia Arbitration proceeding. *See In the Matter of Petition of WorldCom, Inc. Pursuant to Section 252(e)(5) of the Communications Act for Preemption of the Jurisdiction of the Virginia State Corporation Commission Regarding Interconnection Disputes with Verizon Virginia Inc., and for Expedited Arbitration*, CC Docket Nos. 00-218, 00-251, Memorandum Opinion and Order, 18 FCC Rcd 17722, 17903-10, paras. 463-483 (2003) (establishing flat-rated switching charges based on a finding that the substantial majority of switching costs are not traffic-sensitive), *app. for rev. pending*.

[41]*See Further Notice*, paras. 67-68. The proposition that switching costs generally are fixed and do not vary with call volume or MOU is important to our conclusions regarding a unified bill-and-keep regime. Should the record in response to the *Further Notice* prove otherwise, we would reassess these conclusions.

[42]*Intercarrier Compensation NPRM*, 16 FCC Rcd at 9616, para. 12.

[43]*Id.*

[44]*See* Regulatory Reform Proposal of the Intercarrier Compensation Forum (ICF), October 5, 2004, attached to Letter from Gary M. Epstein and Richard R. Cameron, Counsel for the Intercarrier Compensation Forum, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, Tab C, at 2 (filed Oct. 5, 2004).

subject to different compensation rules because they have larger local calling scopes than wireline carriers.[45] Thus, based on this evidence, the existing regimes are not technologically or competitively neutral.

A bill-and-keep approach may be more technologically and competitively neutral than the current regimes because it moves the intercarrier compensation system away from traditional regulatory and jurisdictional classifications that are not based on actual economic cost differences.[46] A bill-and-keep approach would free the Commission from the difficult task of making regulatory distinctions that are no longer sustainable. We acknowledge that, as compared to the current regimes, any unified approach would have these benefits.[47] A unified CPNP regime, however, would still afford carriers the opportunity to shift costs to competitors rather than recover these costs from their subscribers. Because this type of regime distorts the pricing signals received by consumers, it does not serve the Commission's goal of competitive neutrality.[48]

Some commenters contend that a bill-and-keep approach is not competitively neutral because it favors carriers with balanced traffic exchanged with interconnected carriers, such as incumbent LECs, and assumes that competitive LECs should have the network architecture, customer base, and customer calling patterns of incumbent LECs.[49] For instance, some commenters claim that, because incumbent LECs have a larger and more diverse customer base than competitive LECs, they will have more opportunities to recover costs across broad classes of customers.[50] We disagree that a bill-and-keep approach necessarily favors incumbent LECs or carriers with characteristics similar to them. As an initial matter, these commenters confuse average costs with incremental costs, and assume that a call actually imposes a measurable incremental cost on the terminating network. Further, concerns about the balance of traffic exchanged reflect the assumption, which we question, that the calling party's network should bear all the costs of a call. As discussed above, an important benefit of a bill-and-keep regime is that it puts all carriers in a position where they must recover their own costs from their own retail customers. Under this regime, success in the marketplace will reflect a carrier's ability to serve customers efficiently, rather than its ability to extract payments from other carriers.

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[45]*See Local Competition First Report and Order*, 11 FCC Rcd at 16014, para. 1036.

[46]*See* Level 3 Reply at 13-14.

[47]*See* Global NAPs Comments at 9-11. To the extent a unified CPNP regime retained some form of originating access charges for some calls, however, there still would be disputes as to whether, on a particular call, such charges apply or whether, instead, the originating carrier is obligated to compensate the terminating carrier. These disputes are common today in cases where the called party's telephone number does not reflect its geographic location. *See Further Notice*, para. 22. A bill-and-keep regime would eliminate such disputes.

[48]Furthermore, a unified CPNP approach may require the Commission to apply regulated charges to services and service providers currently subject to an exemption under the rules, while a bill-and-keep approach would avoid this problem. For instance, service providers currently subject to the ESP exemption may be subject to regulated intercarrier charges. Moreover, under a unified CPNP approach, the Commission may be required to permit and regulate charges that are not subject to Commission regulation at this time, such as CMRS access charges.

[49]*See, e.g.,* Allegiance Comments at 3-4, 16-18. Allegiance goes on to state that bill-and-keep would favor incumbent LECs because it would allow them to shift their costs to competitive LECs. *Id.* at 3-4. *See also* ALTS Reply at 4-6.

[50]*See, e.g.*, Allegiance Comments at 16-17; KMC Comments at 4.

3. Bill-and-Keep and the Deployment of Efficient Technologies

In the *Intercarrier Compensation NPRM*, the Commission observed that an intercarrier compensation regime that involves termination payments, such as a CPNP regime, may create the opportunity for the terminating carrier to exploit undesirable pricing power.[51] The terminating carrier has a monopoly of sorts over the facilities serving the end user who receives calls because any interconnecting carrier attempting to reach that customer must use the terminating carrier's network.[52] If the originating carrier is prohibited from blocking or declining traffic based on the identity of the terminating carrier, and the terminating carrier may unilaterally impose charges (*e.g*., by filing a tariff), the originating carrier cannot avoid unreasonable termination charges. Moreover, in many cases, the originating carrier is unable to pass these charges on to the end-user customer.[53] Because the end-user customer receives no market signals to avoid these costs, the unreasonable termination charges may persist.[54] There is no market pressure to moderate these rates.

In contrast, under an approach where terminating carriers cannot impose payment obligations unilaterally, such as bill-and-keep, the terminating carrier must recover its costs from its own end-user customers, thereby allowing that customer to compare the prices charged for termination and choose the most efficient carrier.[55] The end user thus controls the decision whether to purchase from the lowest cost provider and may select providers based on considerations of cost and functionality.[56] Bill-and-keep therefore encourages the development of competition by rewarding carriers based on their ability to serve customers efficiently rather than their ability to shift costs to other carriers.

Some commenters contend that a bill-and-keep approach is not technologically neutral because it would uniquely affect specific services or service providers.[57] For instance, they contend that a bill-and-

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[51]*See Intercarrier Compensation NPRM*, 16 FCC Rcd at 9625, para. 38.

[52]*Id.; In the Matter of Access Charge Reform*, *Reform of Access Charges Imposed by Competitive Local Exchange Carriers,* CC Docket No. 96-262, Seventh Report and Order and Further Notice of Proposed Rulemaking, 16 FCC Rcd 9923, 9934-35, para. 28 (2001) (*CLEC Access Reform Order*). *See also* Qwest Comments at 9-11 (describing the terminating access monopoly problem).

[53]*Intercarrier Compensation NPRM*, 16 FCC Rcd at 9625, para. 38. For example, IXCs are subject to the rate averaging requirements of section 254(g) and therefore cannot charge rates that impose on the calling party the specific costs of originating that particular party's calls; nor can IXCs charge the calling party different rates to terminate calls to different called parties. *See* 47 U.S.C. 254(g) (requiring that the rates charged by IXCs to subscribers in rural and high cost areas be no higher than the rates charged to subscribers in urban areas, and that the rates charged by IXCs to subscribers in each state be no higher than those charged to subscribers in any other state); *see also* 47 C.F.R. § 64.1801.

[54]*Intercarrier Compensation NPRM*, 16 FCC Rcd at 9625, para. 38.

[55]*See, e.g*., Qwest Comments at 9-11; SBC Comments at 50; USTA Comments at 21.

[56]*See* Level 3 Reply at 17.

[57]AT&T, for instance, argues that a bill-and-keep regime would not permit long-distance carriers to continue to offer toll-free service because, under a bill-and-keep regime, the service would no longer cover the costs associated with originating and terminating access. *See* AT&T Comments, Declaration of Janusz A. Ordover and Robert D. Willig, para. 30 & n.7. We question this conclusion. Under both the current access charge regime and a bill-and-keep regime, the calling party must pay for the local connection to the telecommunications network in order to make (continued….)

keep approach would disadvantage paging carriers because there is no mutuality of benefit as between the carriers.[58] Paging carriers argue that, due to the one-way nature of paging traffic, the originating carrier always receives a greater benefit than the terminating paging carrier.[59] The rationale underlying bill-and-keep is not premised on the mutuality of benefits as between the *carriers*, but rather the mutuality of benefit as between the *customers* of the carriers involved. The principle that both the calling and called party benefit from any given call is even more compelling in the case where the calling party is attempting to contact the called party and the called party has supplied a paging number to the calling party for that very purpose. Further, we see no reason why paging carrier customers should not pay for the costs of calls terminated to their paging devices, especially considering the benefit to the customers of the paging service received. Indeed, the very purpose of a paging service is the benefit of notification when a party is attempting to contact the paging subscriber. Given the mutual benefit received by customers in the paging context, we do not believe that a bill-and-keep approach would somehow disadvantage paging carriers.

4. Bill-and-Keep and Regulatory Oversight

In the *Intercarrier Compensation NPRM*, the Commission discussed several potential advantages of a bill-and-keep approach, including the claim that it eliminates the need for regulators to set the level and structure of termination rates.[60] Under a CPNP approach, because of the "terminating monopoly" issue, there is an obvious need to regulate the termination rates that carriers charge each other. Commenters contend that, absent a truly competitive marketplace, ratesetting requires considerable resources from carriers and regulators, leads to litigation, and results in considerable uncertainty in the marketplace.[61] As Qwest observes, the development of competition, combined with various carriers deploying different network technologies and services, makes it extremely difficult for regulators to establish a single CPNP regulatory scheme for intercarrier cost recovery.[62] Similarly, Level 3 observes that, due to the differing efficiencies associated with individual network architectures, each carrier incurs distinct costs of termination, and that regulators would need to account accurately for individual costs associated with different services, features, and technologies.[63] Considering all these factors and variables, they argue that regulators are unlikely to establish rates that accurately reflect costs and thereby

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a toll-free call, and the business that subscribes to the toll-free number covers the IXC's costs. AT&T may be correct that toll-free services are less valuable to business and consumers as toll charges decline, which we would expect under a bill-and-keep regime, but that is not a valid reason to retain a CPNP regime.

[58] *See, e.g.*, Arch Wireless Reply at 3-6.

[59] *Id.*

[60] *See Intercarrier Compensation NPRM*, 16 FCC Rcd at 9630, para. 56. The Commission also discussed claims that a bill-and-keep approach enables regulators to avoid the allocation of common costs among services, and gives end users direct control over their access arrangements. *Id.* at 9626, paras. 39-40.

[61] *See, e.g.*, Level 3 Reply at 11; Qwest Reply at 3.

[62] *See, e.g.*, Qwest Comments at 14 (arguing that the pragmatic obstacles associated with ratesetting may be insurmountable); Verizon Wireless Comments at 25 (stating that the primary benefit of bill-and-keep is its ability to minimize the need to regulate rates); Qwest Reply at 8-11 (discussing the reason why regulation is incapable of getting the rates "right"). *See also* Qwest Comments at 13 (emphasizing that a carrier incurs the costs associated with transport and termination when it purchases the network capacity necessary to handle peak load call volume).

[63] Level 3 Reply at 12. *See also* Nextel Comments at 28.

eliminate inefficient, market-distorting behavior.[64]

Other commenters, however, maintain that a bill-and-keep approach would require more regulatory intervention than a CPNP approach. For instance, some commenters contend that converting intercarrier charges to end-user charges would create additional means for incumbent LECs to engage in anticompetitive conduct.[65] They further argue that a bill-and-keep regime would result in new arbitrage issues requiring regulatory intervention, including disputes over interconnection costs and demarcation requirements.[66] Similarly, ALTS argues that bill-and-keep would create even more regulatory uncertainty.[67] Other commenters express general concern over the many implementation issues arising under a bill-and-keep regime, including the potential need to adjust and regulate end-user rates and safeguard against cross-subsidization.[68]

While a bill-and-keep regime would undoubtedly require regulatory oversight, we do not believe it can be reasonably argued that bill-and-keep is somehow “more regulatory” than a CPNP regime. Given that a CPNP regime requires regulation of both retail and wholesale rates, while bill-and-keep requires only retail rate regulation, bill-and-keep would appear to require substantially less regulatory intervention. Indeed, our experience with CPNP regimes demonstrates the need for substantial regulation of terminating charges because of the terminating access monopoly. Because the terminating carrier controls the only line and local switch connecting the called party to the network, that carrier has strong incentives to extract as high a payment as possible from the calling party’s carrier.[69] Competition at the retail level has not diminished the terminating access monopoly of the carrier selected by the called party.[70] Even if the called party takes service from two different networks (*e.g.*, a LEC network and a CMRS network), it will have a different telephone number for each service and the originating network has no choice but to terminate the call on the network to which the called number is assigned.

As a result, under a CPNP approach, regulators must ensure that terminating rates are cost-based,

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[64]Level 3 Reply at 12; s*ee also* Qwest Comments at 12-15 (providing numerous reasons why regulators are unlikely to set termination rates at truly efficient levels).

[65]*See, e.g*., AT&T Reply at 21 (explaining that, because state commissions typically adopt UNE switching rates when determining reciprocal compensation rates and because incumbent LECs could be net payors of reciprocal compensation, the current system provides some incentive to seek reasonable, cost-based UNE switching rates in order to lower potential reciprocal compensation payments); ALTS Reply at 5-6 (discussing the relationship between UNE, collocation, and reciprocal compensation rates); e.spire and KMC Reply at 8-9 (arguing that bill-and-keep would create incentives for higher UNE rates).

[66]*See, e.g.*, Allegiance Reply at 8; AT&T Reply at 22; NASUCA Reply at 12-13.

[67]ALTS Reply at 3-4.

[68]*See* Allegiance Reply at 8; ALTS Reply at 3; AT&T Reply at 22; MD-OPC Reply at 22; NASUCA Reply at 12-13; Taylor Reply at 6; Time Warner Reply at 3.

[69]*See* Qwest Reply at 4 (discussing the terminating access monopoly problem).

[70]*See CLEC Access Reform Order*, 16 FCC Rcd at 9934-35, paras. 10, 28 (discussing why terminating access providers may be insulated from the effects of competition); *In the Matter of Access Charge Reform*, CC Docket No. 96-262, Notice of Proposed Rulemaking, 11 FCC Rcd 21354, 21476, para. 279 (1996) (explaining why all access providers may possess market power over IXCs needing to terminate calls) (subsequent history omitted).

and the need for regulation continues indefinitely. If regulators had perfect information at their disposal and easily could set cost-based prices, this constant need for rate regulation might be tolerable. In practice, however, regulators rarely have sufficient information or sufficient resources to establish rates that accurately reflect the cost of providing service. For example, notwithstanding the Commission's extensive experience with circuit switching technology, the issue of what portion of switching costs are traffic-sensitive is highly controversial.[71]

Furthermore, as new technologies and network architectures develop, the challenges associated with setting cost-based rates will only increase. The ratemaking experience of state and federal regulators generally has been limited to incumbent LEC wireline networks. Regulators are far less familiar with the costing of other types of networks, such as wireless networks, that have not previously been subject to cost-based rate regulation. The Commission then would be faced with the choice of examining the costs of these other types of networks, which would be an overwhelming task, or establishing rates based on incumbent LEC networks, which could lead to significant arbitrage issues if the costs of the networks differ. In either case, the inevitable result of maintaining a CPNP regime in the face of these new technologies would be increased litigation and regulatory uncertainty. As one commenter observed, "opponents [of bill-and-keep] both overestimate the ability of regulators to 'get the price right' and underestimate the social and economic costs of getting the price wrong."[72]

AT&T suggests that a bill-and-keep approach would have no effect on the need to regulate termination rates. It contends that bill-and-keep would change only the identities of the parties that pay such rates because dominant carriers may still have the ability and incentive to charge their end users more than the economic cost of the services provided.[73] AT&T's argument assumes that dominant carriers will retain their position in the marketplace.[74] One of the fundamental goals of the 1996 Act and the Commission's rules is to encourage competition in the marketplace, and, as discussed in the *Further Notice*, such competition is developing.[75] Competitive LECs already terminate a significant amount of traffic and hold a terminating monopoly over access to these end users.[76] Moreover, there is increased intermodal competition from cable and CMRS providers.[77] We believe a bill-and-keep approach is more

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[71] *See Further Notice*, paras. 67-68.

[72] Qwest Reply at 8. Some commenters are concerned about consistent pricing policies and the opportunity to raise UNE rates. *See, e.g.,* Texas Counsel Comments at 14; Allegiance Reply at 6. We note that the Commission has a separate proceeding to consider UNE pricing and the relationship, if any, that should be maintained between UNE pricing and intercarrier compensation rules. *See generally Review of the Commission's Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Service by Incumbent Local Exchange Carriers*, WC Docket No. 03-173, Notice of Proposed Rulemaking, 18 FCC Rcd 18945 (2003).

[73] *See* AT&T Comments at 17.

[74] *See* Qwest Reply at 7.

[75] *See Further Notice*, paras. 18-21.

[76] *See* Qwest Reply at 5.

[77] *See, e.g.*, *Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993*, *Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services*, WT Docket No. 04-111, Ninth Report, 19 FCC Rcd 20597, 20684, para. 213 (2004) (finding that consumers are substituting wireless service for traditional wireline communications).
(continued….)

likely to be sustainable in a competitive marketplace and that the marketplace, rather than regulatory intervention, is the best mechanism for constraining end-user rates. In markets where competition has not taken hold at the retail level, states historically have regulated end-user rates and we have no reason to believe that they will not continue to do so.

Further, we are not convinced that a cost-based CPNP regime would provide more regulatory certainty for carriers and investors than a bill-and-keep regime.[78] Some commenters suggest that changing the current rules will upset carrier expectations and investments.[79] We question the wisdom of retaining the current approach based on these considerations. As an initial matter, carriers have been on notice for almost four years that the Commission was considering significant reform of intercarrier compensation regimes, and many commenters support such reform.[80] In addition, some of these carrier expectations arose from regulatory arbitrage incentives that the Commission is seeking to eliminate in this proceeding.[81] These incentives give rise to many of the problems and intercarrier compensation disputes that currently plague the industry. Thus, we do not believe that carrier and investor expectations based on these arbitrage incentives justify retention of a CPNP approach. We do, however, recognize that there are significant implementation issues that will be associated with any such change and that transitional mechanisms may be necessary.

Finally, we address claims that a bill-and-keep regime is not deregulatory because implementation of such a regime would require Commission oversight.[82] For instance, ALTS observes that a move to a bill-and-keep regime would require the Commission to transform the access charge regime into a program of federal end-user charges and to address the political issues associated with such changes.[83] ALTS argues that a bill-and-keep approach would simply toss the existing intercarrier compensation issues "back on the table and create more uncertainty in the market."[84] Because a bill-and-keep approach, once implemented, would eliminate intercarrier compensation payments between carriers, it should dispose of most, if not all, of the existing compensation disputes between carriers. Further, although a bill-and-keep regime would call for Commission oversight during its implementation, the need for regulation after implementation would be greatly reduced as compared to the regulatory oversight required by a cost-based CPNP regime. ALTS is correct that any additional end-user charges initially would require Commission oversight, but we anticipate that these charges increasingly will be constrained by competitive forces. In contrast, a cost-based CPNP regime would necessitate ratesetting indefinitely, and on the basis of a number of factors and variables that will continue to change over time. Thus, although bill-and-keep may require additional regulatory oversight in the near term, we believe that such an approach is ultimately more deregulatory than the other alternatives proposed.

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[78] *See, e.g.*, Allegiance Comments at 6-10.

[79] *See, e.g.*, *id*. at 2-3, 8-10; Focal *et al*. Comments at 3; GVNW Comments at 8; ALTS Reply at 3-4.

[80] *See Further Notice*, paras. 37-39.

[81] *Id.*, para. 33.

[82] *See, e.g.*, ALTS Reply at 3-4.

[83] *Id.* at 3.

[84] *Id*. at 3-4.

5. Bill-and-Keep and Universal Service

Many commenters, including carriers, state commissions, and consumer groups, express concern about the potential impact of bill-and-keep on end-user charges.[85] They contend that a bill-and-keep regime is not in the public interest because it would affect the affordability of telecommunications services in rural and remote areas.[86] Several commenters also argue that a bill-and-keep approach would have significant implications for universal service and may necessitate changes to the existing universal service support mechanisms.[87]

We recognize the need to address the universal service consequences of a bill-and-keep regime. As the Commission made clear in the *Further Notice*, it is committed to ensuring the availability of telecommunications services in rural and high-cost areas at rates that are affordable and reasonably comparable to rates in urban areas, consistent with section 254 of the Act.[88] We acknowledge the many commenters, including carriers, state commissions, and consumer groups, that express concerns that bill-and-keep will raise end-user charges and may affect the affordability of telecommunications services, particularly in rural and high-cost areas.[89] We recognize that addressing these affordability concerns will require further adjustments to the Commission's existing explicit universal service mechanisms and may require additional commitments of universal service funds.

[85] *See, e.g.,* ALTS Reply at 6-7; DC People's Counsel Reply at 4-5, 10-1, 17-21; e.spire and KMC Reply at 9; MD-OPC Reply at 3-4; NASUCA Reply at 3, 5-8; NECA Reply at 3-4; Ronan Advisory Reply at 1, 8; Texas Counsel Reply at 4, 6.

[86] *See, e.g.*, MITG Reply at 4; NASUCA Reply at 3, 5-8; NECA Reply at 2-4; Ronan Advisory Reply at 1-8; RICA Reply at 2. *See also* Letter from Scott Reiter, Sr. Telecom Specialist, NTCA, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, at Attach. (filed Mar. 10, 2004) (attaching a paper entitled "Bill and Keep: Is It Right for Rural America?" prepared by the NTCA Intercarrier Compensation Work Group).

[87] *See* NECA Reply at 6-7; NRTA/OPASTCO Reply at 3, 10-15; SBA Reply at 10-11; Taylor Reply at 41-42; TCA Reply at 3-4; Texas Counsel Reply at 3-4, 6, 11. *See also* BellSouth Reply at 2-3 (stating that the Commission must address legacy issues, particularly implicit subsidies, and outstanding universal service issues).

[88] *See Further Notice*, para. 32; 47 U.S.C. § 254.

[89] *See, e.g.*, Alaska Commission Comments at 2; Alaska Telephone Association Comments at 3-4; Century Tel Comments at 21; Home Telephone Comments at 1; ICORE Companies Comments at 8; Iowa Commission Comments at 3; ITCs Comments at 2; Level 3 Comments at 30-31; MECA Comments at 49; Minnesota Independent Coalition Comments at 2; MSTG Comments at 2; NASUCA Comments at 31; NECA Comments at 4-6; NRTA/OPASTCO Comments at 15-19; Texas Counsel Comments at 17-18; Oklahoma Rural Telephone Coalition Comments at 43-45; Ronan Advisory Comments at 2,7; Sprint Comments at 24-25; USTA Comments at 22-23; United Utilities Comments at 4; Western Alliance Comments at 6-17; Wisconsin Commission Comments at 5.

SEPARATE STATEMENT OF
CHAIRMAN MICHAEL K. POWELL

RE: Developing a Unified Intercarrier Compensation Regime (CC Docket No. 01-92).

Today we act to begin the second-phase of our unified intercarrier compensation docket. This proceeding sets in motion an ambitious task for the agency because it touches upon two of our most cherished principles – ensuring fair competition and protecting universal service. Currently, different compensation rules apply to different types of traffic even if carriers are using the Public Switched Telephone Network in the same way. In today's rapidly changing telecommunications marketplace, however, different treatment creates both opportunities for regulatory arbitrage and incentives for inefficient investment and deployment decisions. These disparities mean that we simply do not have a choice to reform the current intercarrier payment system; we must, or technology will render it a quaint antique of a forgotten time when only one carrier provided service to all customers.

A number of parties have proposed answers to the interrelated set of questions we pose today – including the Intercarrier Compensation Forum (ICF), Western Wireless, the Alliance for Rational Intercarrier Compensation (ARIC) and the Expanded Portland Group (EPG). The record generated from previous Commission inquiries into this subject teaches us that certain abiding principles must be followed if intercarrier reform is to be durable. First, rate structures should be *unitary* and must eliminate arbitrage opportunities between federal and state jurisdictions and between local and long distance termination rates. Second, our rules should better reflect sound economic principles. In my view, a regime built upon "bill-and-keep" proposals is the solution that is most faithful to principles of cost causation. As the staff report demonstrates, a bill and keep regime encourages the development of competition by rewarding carriers based on their ability to serve customers efficiently rather than their ability to exploit regulatory arbitrage opportunities. It sends rational pricing signals to the market because consumers are equipped with information that allows them to avoid higher cost networks. Third, to the extent reforms are made to our compensation rules that raise universal service concerns from rural carriers, forgone access revenues should be replaced by support mechanisms that are both explicit and portable. By adhering to these principles we ensure that our compensation rules are competitively neutral and support the goal of achieving lasting facilities-based competition.

I am disappointed that the Commission was unwilling to resolve most of the disputes that have been raised in declaratory ruling petitions – many of which have been pending for years. The Wireline and Wireless Bureaus jointly proposed a balanced solution to these very difficult issues and it is unfortunate that some of my colleagues declined to fully consider the merits of this proposal. This Commission bears an important responsibility to provide regulatory clarity to parties who have waited for years in intractable intercarrier disputes. I have heard the concerns of some who argue that the Commission should avoid a piecemeal approach – but the torrent of state litigation that we leave unresolved is far more piecemeal and disruptive to carriers than decisions by this Commission. I urge my colleagues to reconsider their positions and act upon the pending petitions for declaratory ruling expeditiously – these problems are not going to get any easier with time.

SEPARATE STATEMENT OF
FCC COMMISSIONER KATHLEEN Q. ABERNATHY

Re: Developing a Unified Intercarrier Compensation Regime, CC Docket No. 01-92, Further Notice of Proposed Rulemaking.

I am pleased that the Commission is launching this important rulemaking regarding intercarrier compensation. There is no shortage of metaphors to describe these rules that have been developed by the FCC and state commissions over the previous decades — quicksand and quagmire leap to mind — and all of them recognize the troubled state of affairs for the industry and consumers. The rules are premised on at least two eminently sound principles: ensuring full compensation for the costs of building and operating telecommunications networks, and promoting universal service in all areas of the Nation. But a system premised on neat jurisdictional distinctions (intrastate versus interstate) and legacy service categories (telecommunications service versus information service) is no longer sustainable in light of the inexorable march of technological innovation and marketplace convergence.

As reflected in the varying proposals submitted in the record, we are a long way from reaching consensus on appropriate reforms. But the good news is that most, if not all, industry and consumer groups recognize the crying need for change, and most appear to agree that we must develop a *unified* compensation system. The upcoming proceeding will determine whether the best solution is a unified system based primarily on bill-and-keep principles, or instead one that entails positive payments based on embedded or forward-looking costs. The one certainty is that the status quo must yield, because it is increasingly untenable to have carriers subject to several vastly different rate structures depending on arcane service classifications and jurisdictional assignments. Until policymakers develop a fairer and simpler set of requirements, connecting carriers unfortunately will remain embroiled in disputes over payment obligations, and many will continue to devise ways to avoid payment or bypass the public switched network altogether.

I am disappointed that the Commission was unable to resolve the disputes that have been raised in declaratory ruling petitions and have been pending for some time. I am also disappointed that several of my colleagues refused to allow the Commission to seek comment on the staff analysis of intercarrier compensation reform proposals. I would encourage commenters to read this analysis and submit any comments they may have.

I am encouraged, however, that we are commencing the reform process in earnest, and I look forward to working with my colleagues in an open dialogue where all options are on the table. I also want to thank all of the industry groups, state regulators, and others who have been laboring for more than a year to develop comprehensive reform proposals, and I urge all of you to say involved and to be open to compromise solutions. The Commission cannot possibly duplicate the knowledge base of the industry, and our best hope for a workable reform involves continued discussions with all of the interested parties.

SEPARATE STATEMENT OF
COMMISSIONER MICHAEL J. COPPS

Re: *Developing a Unified Intercarrier Compensation Regime*, Further Notice of Proposed Rulemaking (CC Docket Nos. 01-92)

Our intercarrier compensation system is Byzantine and broken. We have in place today a scheme under which the direction and amount of payments vary depending on whether carriers route traffic to a local provider, a long distance provider, an Internet provider, a CMRS carrier or a paging provider. In a marketplace defined by convergence and technological change, this hodgepodge of rates looks more like an historical curiosity than a rational compensation system.

Intercarrier compensation is a must-do item for this Commission this year. It should be our number one telecommunications priority. I believe we can do this. If it turns out we cannot and we have to go to Congress, so be it, but for my part—and I'll bet for Congress' part, too—the preference is to resolve this issue here at the Commission. To really get reform done this year, we must have everyone engaged in the intercarrier compensation dialogue. I am pleased that so many groups and individual carriers provided us with detailed proposals. Putting these proposals out in a neutral and open fashion is the best way to ensure the kind of dialogue we need to get the job done. To those who participated in early industry talks and left them, I hope today's Further Notice brings you back to the table. To those who are not yet a part of the discussions, become a part—and remember the old adage that "Decisions without you are very often decisions against you." I look forward especially to the active participation of our colleagues at the state regulatory level. Their experience, judgment and granular knowledge are essential to any successful outcome. In this regard, let me take a moment to commend my friends at NARUC for the tremendous effort they are putting into convening different parties and varying viewpoints in an attempt to build understanding—maybe even something approaching occasional consensus—on the thorny issues teed up by this discussion. I urge carriers of all types to socialize their plans and ideas with our state counterparts. Their input and insights will be especially important as we map a course that leads us toward a unified rate structure.

Appended to today's Further Notice is a staff report on bill-and-keep. Bill-and-keep has much to recommend it as a theoretical construct. But its operational realities leave me with deep concerns about its impact on communications in rural America. I welcome the opportunity for debate on this issue, but wish to note that the staff appendix is not the product of a Commission vote, nor does it reflect my opinion at this time.

Finally, there is at least one issue that merits prompt resolution that is not a part of today's effort. It is not a part because my sense is that several of us, including me, believe it should be dealt with on a separate but still fast track. Two and a half years ago, a group of wireless carriers jointly filed a petition for declaratory ruling asking the Commission to clarify that wireless termination tariffs are not the right mechanism for establishing reciprocal compensation arrangements for the transport and termination of traffic. In the intervening years, disagreements have grown and devolved into litigation. We have an opportunity to fix this now. I hope we can seize that opportunity. Were a decision clarifying this issue to cross my desk today, I would vote it today. If it takes longer to reach my office, I will vote it as soon as it does.

Countless individuals in the Wireline Competition and Wireless Telecommunications Bureaus worked long hours to bring us this item. So did our able and dedicated personal staffs. I am impressed with the depth of their knowledge and appreciate their unwavering commitment to finding the right answer. They will remain a tremendous resource for us all in the great press for intercarrier compensation

reform. By pulling and hauling together, we can—we must—bring these issues to resolution this year.

SEPARATE STATEMENT OF
COMMISSIONER JONATHAN S. ADELSTEIN

Re: Developing a Unified Intercarrier Compensation Regime, CC Docket No. 01-92, Further Notice of Proposed Rulemaking.

With this item, the Commission adopts a detail-rich inquiry into vexing questions about how telecommunications firms compensate one another. We should not conclude, however, that this is a proceeding solely of interest to rival companies on the rapidly-evolving telecommunications landscape. The decisions that this Commission will make in this proceeding will have profound effects on the prices that consumers pay for telecommunications services and on the choice of services available to them.

This Notice is not the first step in the Commission's revision of its intercarrier compensation regime. Since the passage of the Telecommunications Act of 1996, the Commission has acted on several occasions to address the interplay of its long-standing access charge rules and its reciprocal compensation rules, adopted to implement the 1996 Act. In that time, the Commission has also made substantial changes to the pre-1996 Act rules, reducing rates for access services and seeking to preserve universal service by providing explicit support for hard-to-serve areas of our country.

These actions notwithstanding, there is a widespread call for further reform of the intercarrier compensation regime, particularly with developing intermodal competition and the advent of Internet-Protocol-based services like VoIP. The voices calling for further reform represent a wide diversity of interests: state policymakers, consumer groups, incumbent and competitive local wireline carriers, wireless carriers, long distance carriers, VoIP providers, and others. It is remarkable and encouraging that numerous parties from all segments of the industry have come forward to offer goals, principles and specific proposals for further reform. These parties have expended significant resources to develop proposals and many have tried to find common ground, even if it means moving off of their initial positions.

With this Notice, we hope to capitalize on these parties' hard work and to encourage others to roll up their sleeves and recommit themselves to this effort. Without that broad participation and commitment to find compromise, we may end up with a less than optimal result, and parties may find that the final solutions do not fully reflect their interests.

The proposals included in this Notice are diverse in scope and solutions: some advocate moderate reform, others more far-reaching changes. I'm pleased that this Notice seeks comment on these proposals comprehensively and quickly, so that we can harness the momentum provided by these collective efforts. While this Notice may not precisely reflect my balance of the competing policy goals for intercarrier compensation reform, I am pleased that the item sets out our commitment to harmonize and unify our rules. Given the rapid changes in the communications marketplace, we must work both promptly and carefully to make sure that our regulatory framework continues to promote the innovation and customer choice that drive so much economic growth and benefit for American consumers.

I also give heavy weight to our statutory obligation to preserve and advance universal service even as we move forward with reform proposals. We must quantify with some specificity and weigh carefully the impact of any proposals on all consumers, including those consumers who live in high costs areas or who are low volume users. In addition, this Commission has traditionally been sensitive to drastic shifts in the way that carriers, particularly small companies serving the hardest-to-reach areas, recover their costs. We will need more than idle assurances about the importance of universal service to

be successful here; rather, we must develop coherent and responsive approaches to this Congressional directive.

As we move forward, I want to commend in particular the National Association of Regulatory Commissioners (NARUC) for its efforts to bring parties together. A collaborative process is essential, particularly given the complex jurisdictional issues raised in this proceeding, and I appreciate NARUC's leadership on this front.

Finally, I want to thank the staff of the Wireline Competition Bureau and the Wireless Telecommunications Bureau. While I cannot endorse today the separate staff analysis of intercarrier compensation proposals, which is not the product of Commission vote, I thank the staff for their dedication from the beginning to the end of this process and look forward to working with them as we tackle the challenges ahead.