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APR 3 - 1998

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

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April 3, 1998

VIA HAND DELIVERY

Mr. William Caton
Secretary
Federal Communications Commission
1919 M Street, NW
Room 222
Washington, DC 20554

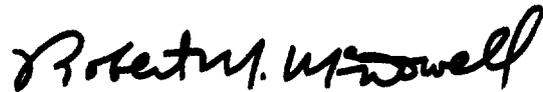
Re: In the Matter of Internet Phone; RM # 8775

Dear Mr. Caton:

Transmitted herewith, on behalf of America's Carriers Telecommunication Association ("ACTA"), are an original and two copies of ACTA's written presentation to the Chairman in the above-referenced proceeding. This letter is being submitted in accordance with Section 1.1200 *et seq.* of the Commission's rules governing *ex parte* presentations.

Please date stamp the extra copy of this filing and return it with the courier. All inquiries regarding this matter should be addressed to the undersigned.

Respectfully submitted,



Robert M. McDowell
Deputy General Counsel
ACTA

rmm/070/ex parte.ltr

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April 2, 1998

VIA HAND DELIVERY

The Honorable William E. Kennard
Chairman
Federal Communications Commission
1919 M Street, NW
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APR 3 - 1998

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Re: In the Matter of Internet Telephone; RM # 8775

Dear Mr. Chairman:

In March of 1996, America's Carriers Telecommunication Association ("ACTA") filed with the Commission a ground breaking petition for rulemaking and declaratory ruling regarding Internet telephony ("Internet Petition"). In that petition, subsequent comments, reply comments and in ACTA's comments in the access charge reform proceeding (CC Docket Nos. 96-262, 95-72, 94-1 and 91-213) as well as in the Notice of Inquiry regarding Usage of the Public Switched Network by Information Service and Internet Access Providers (CC Docket No. 96-263), ACTA has consistently maintained that information service providers ("ISPs"), especially Internet phone providers, should be required to pay local exchange carriers access charges and pay into the Universal Service Fund ("USF") because ISPs are configured into the public switched telephone network in an identical manner as interexchange carriers ("IXCs"). For the reasons stated herein, the Commission is long overdue on ruling on these issues. The Commission must squander no more time and seize the opportunity to heed ACTA's call to lower access charges to cost using forward-looking pricing models and spread the burden of paying access costs and USF contributions fairly to all users of the PSTN. In short, ACTA is proposing a fair, simple and affordable "flat tax" approach to Universal Service and access charges.

Founded in 1985, ACTA is a national trade association of over 230 telecommunications service providers including small to medium-sized IXCs, CLECs, ISPs, wireless providers and others. Most of ACTA's members are facilities-based. Many of ACTA's members are either contemplating deploying Internet Protocol-based telephony ("IP Phone") services or are already offering such services because current government mandated artificial pricing makes such services attractive. Such artificial arbitrage stems from the Commission's insistence that ISPs should be

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exempt from paying access charges and USF contributions (the "ISP Exemption"). ACTA estimates that the Commission has created a \$40 billion artificial incentive to pipe traditional voice traffic over the Internet. In response to this government created pricing, private market players have been funneling millions, if not billions, of dollars into research and development of IP Phone services. The private sector is responding in this fashion not because the technology alone makes IP Phone more attractive, but because the Commission has created an irrational economic playing field. Among the companies investing considerable sums into IP Phone ventures are: AT&T, Qwest, MCI, GTE, ICG, IDT, VocalTec, Level 3, and many others including equipment manufacturers such as Lucent, Cisco Systems and Nortel.¹ Within the next four years, demand for IP Phone equipment is expected to top \$14 billion while 13% of all phone calls are expected to be piped over the Internet.² That translates into the equivalent of nine billion minutes of use per month or \$24 billion per year by 2002.³

Furthermore, by not having to pay access charges or Universal Service contributions, ISPs are receiving an implied subsidy in violation of Section 254(e) of the Telecommunications Act of 1996. Wall Street analysts agree with ACTA that the ISP industry is heavily subsidized. In March, George Reed-Dellinger, senior vice president of HSBC Securities, told the Senate Communications Subcommittee that the ISP Exemption has created distorted pricing of the Internet and has encouraged irrational usage patterns. In essence, he said that voice and data traffic are becoming the same and should be treated the same by regulators.

ACTA applauds market players who use the power of the Internet to make money. In fact, several of ACTA's members have been IP Phone pioneers. However, ACTA contends that the Commission's refusal to address the complex implications of encouraging IP Phone service providers to invest heavily into a government created scheme reveals an appalling denial of reality. Although ACTA has briefed its legal arguments several times for the Commission and the U.S. Court of Appeals for the Eighth Circuit, for the Commission's convenience, ACTA provides the following summary.

¹ See *Business Week*, "The New Trailblazers," April 6, 1998, pp. 88-102.

² *Id.*

³ *Id.* If anything, these figures should be deemed conservative as the IP Phone explosion has, thus far, surpassed even the most optimistic of predictions. Certainly, the IP Phone phenomenon has rendered the Commission's analysis that it has only a "hobbyists'" appeal ridiculous. See *First Report and Order, In the Matter of Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charges*, CC Docket No. 92-262, 94-1, 91-213 & 95-72, FCC 97-158 (rel. May 16, 1997). *review pending sub nom. Southwestern Bell Tel. Co. v. FCC*, Nos. 97-2866/2873/2875/3012 (8th Cir.) ("First Report").

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1) Access charges should be reduced to true cost using a forward-looking pricing model. Currently, they are still inflated, even after so-called "reform."

2) ISPs no longer need government protection as embodied in the ISP Exemption because the ISP industry is no longer nascent or "fledgling."⁴ Also, if access charges are reduced to true cost, ISPs will no longer need to be exempt because more players will be paying less rather than a few players paying more (the "flat tax" concept). ISPs should have to pay access charges because they are identically configured into the PSTN as IXC's. In the alternative, if the Commission chooses to continue exempting ISPs, then IXC's should also be exempted because they are identically situated as ISPs.

3) IP Phone is basic service and should be treated accordingly. Nowhere in the U.S. Code or the Commission's rules is two-way, real-time voice telephony given special legal treatment due solely to the technology a provider of such services chooses to use. That is, the courts and the Commission have long held that a phone call is a regulated service whether it travels over Class V circuits, or any other technology, such as the Internet.⁵

4) If the Commission continues to exempt IP Phone from USF and access charge obligations: market players will accelerate their artificially stimulated investments into this medium; USF contributions will nose-dive, thus undermining the Commission's and Congress's Universal Service policies and; this rush to the Internet will divert already-inflated access revenues from LECs who will then insist that such charges should be inflated even further to compensate for "lost monies."

5) With a Universal Service and access charge regime in shambles, the Commission will have no other choice but to lift the ISP Exemption after the damage has been done and after market players have invested billions into this government created scheme. In short, those who invested in IP Phone merely because it is "cheaper" will have the rug, in the form of artificial pricing, pulled out from under them. The government giveth, the government taketh away.

In short, on-going developments in the IP Phone phenomenon, not to mention sound public policy and the black letter of the law, leave the Commission no choice but to respond favorably to

⁴ See *MTS and WATS Market Structure, Memorandum Opinion and Order*, Docket No. 78-72, 97 FCC 2d 682, 711-22; see also *In the Matter of Amendments of Part 69 of the Commission's Rules Relating to Enhanced Service Providers*, 3 FCC Rcd. 2631 (1988).

⁵ See *AT&T v. FCC*, 572 F.2d 17, 24 (D.C. Cir. 1978); see also *NARUC v. FCC*, 525 F.2d 630, 641-642 (D.C. Cir. 1976); see also 47 C.F.R. § 64.702(a).

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what ACTA has been proposing for over two years. Not to adopt ACTA's proposals immediately will produce a bigger and more embarrassing mess for the Commission to try to clean up later.

Respectfully submitted,

AMERICA'S CARRIERS
TELECOMMUNICATION ASSOCIATION

By: Robert M. McDowell

Robert M. McDowell

Deputy General Counsel