

**Mandatory “bill and keep” would be wholly impermissible under the FCC’s forbearance authority**

The ILECs also claim that the FCC has sufficient authority under Section 10 of the Telecom Act (47 U.S.C. §160(a)) to forbear from requiring reciprocal compensation for ISP-bound traffic (Qwest Roadmap at 18-20).

However, the Commission’s forbearance authority does not extend to Section 271 checklist items, one of which requires the BOCs to offer “[r]eciprocal compensation arrangements in accordance with the requirements of section 252(d)(2).” 47 U.S.C. section 271(C)(2)(B)(xiii).

The FCC is forbidden from forbearing from any provision of Section 271 unless and until that provision is fully implemented. 47 U.S.C. section 160(d).

Regardless, the FCC cannot meet the three-part test established by section 10(a) because deciding not to enforce the statutorily-required reciprocal compensation regime would:

- (1) fail to ensure that the carriers’ charges and practices are just and reasonable, and are not unjustly or unreasonably discriminatory;
- (2) harm, rather than protect consumers, including ISPs and other end users; and
- (3) be inconsistent with the public interest.

## **Mandatory “bill and keep” would violate the APA’s requirement for sufficient notice**

The FCC also faces a significant procedural defect because it has never asked for comments on the question of whether it should adopt a mandatory bill and keep regime.

The Public Notice sought comments on the jurisdictional issues identified in the D.C. Circuit’s remand decision, as well as “comment regarding any new or innovative inter-carrier compensation arrangements for ISP-bound traffic parties may be considering or have entered into, either voluntarily or at the direction of a state commission, during the pendency of this proceeding.” 15 FCC Rcd 11311, 11312 (2000).

Bill and keep is not a “new or innovative inter-carrier compensation arrangement;” it is in fact the very absence of a compensation arrangement. Arguing, as the ILECs have done, that CLECs should not be eligible for reciprocal compensation as provided under section 251(b)(5), is a far cry from arguing that CLECs should receive no compensation at all.

**Mandatory bill and keep only for ISP-based traffic will be unjustly & unreasonably discriminatory**

**The FCC consistently has classified and treated ESPs/ISPs as unregulated end users, not carriers.**

Section 64.7 702(a) of the FCC's rules: ESPs "are not regulated under title II of the Act."

Section 69.2(m) of the FCC's rules: an end user is any customer of telecommunications service that is not a carrier.

**ISPs utilize the local network in the same way as other local business end users.**

Other end users of inbound telecommunication services includes call centers, credit card validation centers, travel reservation agencies, home shopping networks, call-in radio shows, ticket outlets, pizza delivery stores, taxicab companies, etc.

**The FCC cannot lawfully single out ISP traffic for differential treatment.**

Section 202(a) of the Communications Act of 1934, as amended, forbids "unjust or unreasonable discrimination in charges, practices, classifications, regulations, facilities, or services for or in connection with like communication services, directly or indirectly, by any means or device...."

Section 201(b) prohibits, and declares unlawful, any unjust or unreasonable "charges, practices, classifications and regulations...."

## **Mandatory “bill and keep” would further block the CLECs’ ability to provide local service**

Through their control over last-mile facilities, the ILECs have successfully foreclosed the CLECs from providing POTS service to residential and small business customers. Contrary to suggestions by some ILECs (Qwest Roadmap at 16-18), CLECs do not intentionally restrict their operations -- they serve customers where they are able. It is the ILECs who have intentionally sought, and largely succeeded, in limiting the customers that CLECs can profitably serve. As a direct result of the ILECs’ actions, CLECs have been able only to compete for the business of large, geographically-dense corporate customers.

When certain CLECs capitalized on the ILECs’ greed by developing a niche market based on signing up locally-based ISPs as end user customers, the ILECs now seek to eliminate this final revenue stream. A mandatory bill and keep requirement will leave CLECs completely uncompensated for the service they provide, and take away the viability of this one remaining addressable market.

**Mandatory “bill and keep” would provide fewer incentives for the ILECs to deploy advanced services and new technologies**

Because reciprocal compensation is tied directly to the ILECs' alleged costs of providing transport and termination, it provides important incentives for the ILECs to install and utilize more efficient, and hence less costly, network equipment. Thus, abandoning recip comp in favor of a mandatory “bill and keep” regime – coupled with the likely negative impact on local competition -- will take away these important incentives, and give the ILECs even less reason to upgrade the outmoded portions of their networks.

## **Mandatory “bill and keep” would accelerate the disintegration of a viable CLEC industry**

Verizon argues that a transition to bill and keep would not harm CLECs or their shareholders because the CLECs and their analysts have not factored reciprocal compensation revenues into their accounting systems and stock valuations (Verizon Ex Parte Letter, CC Docket No. 99-68, dated 11/1/00).

Of course, many of the CLECs have been forced into this precarious financial position precisely because the ILECs have refused to pay the reciprocal compensation revenues that are owed. In other words, the Commission has instructed to note the result of the ILECs' own intransigence and lack of good faith – the CLECs must write down reciprocal compensation revenue and avoid reciprocal compensation exposure -- as a positive reason for adopting mandatory bill and keep.

## Mandatory “bill and keep” would accelerate the disintegration of a viable CLEC industry

The simple truth is that, as numerous news stories attest, the CLEC industry is in dire straits. As one indicia -- recent stock market data for selected telecom companies -- reveals, the CLECs and other competitive providers have lost a tremendous portion of their value over the past few months. The average industry-wide stock price, as a percentage of the 52-week high during the period from 7/31/2000 to 11/20/00, is as follows:

RBOCs:	58-97%
Wireless providers:	37-50%
IXCs:	25-32%
CLECs:	5-20%
Data CLECs:	3-5%

While this snapshot does not tell the whole story, it does provide a pointed response to the ILECs' disingenuous statements about the relative health of the CLEC industry.

## **Mandatory bill and keep would leave the ISPs with no competitive alternatives to the ILECs**

One of the ILECs' unstated intentions (besides securing a cost-free ride on the CLECs' networks) is to drive the CLECs out of the local market, and lock up the ISPs as customers -- or perhaps eliminate the ISPs as competitors altogether. It is instructive that, in many cases, ISPs sought out the CLECs beginning in 1996 because the ISPs were interested in higher service quality and lower prices than they were receiving from the ILECs.

Adopting a mandatory bill and keep policy would reward the ILECs for ignoring and losing ISPs as customers in the first place, and would relegate the ISPs to a choice-free scenario of using the ILECs or nobody. In fact, given the ILECs' openly-acknowledged poor performance -- deliberate or otherwise -- in serving ISPs prior to the advent of competition, it is likely that the ILECs, as the sole remaining terminators of traffic, would cause tremendous damage to the ISP market.

**Mandatory “bill and keep” limited only to ISP-bound traffic, or to all local traffic, would be arbitrary and capricious**

The Commission long has recognized that the ILECs incur actual economic costs for originating, transporting, and terminating traffic on behalf of interexchange carriers.

Section 202(a) of the Communications Act of 1934, as amended, requires nondiscriminatory practices and charges for “like” services.

In the Local Competition Order, the FCC concluded that:

Telephone exchange providers and exchange access providers “us[e] essentially the same equipment to transmit and route traffic...” (para. 185).

“The facilities used to provide exchange access services are the same as those used to provide local exchange services.” (para. 363).

“We recognize that transport and termination of traffic, whether it originates locally or from a distant exchange, involves the same network functions. Ultimately, we believe the rates that local carriers impose for the transport and termination of local traffic and for the transport and termination of long distance traffic should converge.” (para. 1033).

**Thus, any proposal requiring bill and keep only for ISP traffic between carriers, or local traffic between carriers, must also require the ILECs not to recover costs incurred for transporting and terminating traffic on behalf of interexchange carriers.**

**Mandatory “bill and keep” limited only to ISP-bound traffic, or to all local traffic, would be arbitrary and capricious**

The Commission long has recognized that the ILECs incur actual economic costs for originating, transporting, and terminating traffic on behalf of their own end user customers.

In the Local Competition Order, the Commission found that:

“transport of traffic for termination on a competing carrier’s network is, therefore, largely indistinguishable from transport of termination of calls on a carrier’s own network.” (para. 1054).

**Thus, any proposal requiring bill and keep only for ISP traffic between carriers, or local traffic between carriers, must also require the ILECs not to recover costs incurred for transporting and terminating traffic on their own networks on behalf of their own end user customers.**



**Addressing  
The D.C. Circuit's Remand of  
the FCC's  
ISP Reciprocal Compensation  
Order**

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December 4, 2000*

# Summary

- ✓ Jurisdiction is not an issue - - the FCC has ample jurisdiction over both intrastate and interstate traffic under Sections 251 and 252 of the Act
- ✓ Local exchange carriers provide either “telephone exchange service” or “exchange access”
- ✓ ISPs are end users of telecommunications, not telecommunications carriers themselves
- ✓ ISP-bound calls within the same local service area terminate locally
- ✓ Dial-up calls to ISPs within the same local service area constitute telephone exchange service
- ✓ CLECs incur actual economic costs on behalf of the ILECs when terminating local calls to ISPs
- ✓ Thus, CLECs must receive reciprocal compensation pursuant to Section 251(b)(5) of the Act

## The Crux of the Issue

**The issue presented is straightforward: how does a local carrier get paid for participating in the origination or termination of a telephone call?**

The relevant statutory, regulatory, and equity principles are clear:

- ✓ *The telecommunications services provided by a local carrier constitute either telephone exchange service or exchange access service.*
- ✓ *In both cases, local carriers incur actual economic costs for originating, transporting, and terminating telecommunications.*
- ✓ *Local carriers are paid access charges for providing exchange access to create an interexchange call.*
- ✓ *Local carriers are paid reciprocal compensation for providing telephone exchange service to create an intra-exchange (local) call.*

## The Crux of the Issue

When applied to calls connecting one set of end users (an ILEC's residential customers) to another set of end users (a CLEC's ISP customers), these principles yield a consistent conclusion.

- ✓ *The ILEC's customers originate the calls, and the CLEC's customers receive the calls.*
- ✓ *Because the ILEC's customers are both the cost causers and the party responsible for paying for the calls, the ILEC must compensate the CLEC for the cost of terminating the calls.*
- ✓ *Where calls originate and terminate within the same local service area, the compensation to be paid is dictated by Section 251 of the Telecommunications Act of 1996 (as interpreted by the Commission).*

Thus, when ILEC residential customers call an ISP served by a CLEC within the same local service area, the ILEC must pay reciprocal compensation to the CLEC.

# The Remand Issues

## *ISPs Do Not Provide Telephone Toll Services*

- ✓ *The FCC determined that, under the Telecommunications Act, all local traffic is either “telephone exchange service” or “exchange access.”*  
*Advanced Service Order, 13 F.C.C.R. 24011, 24032 (1998);*  
*Advanced Services Order on Remand, 15 F.C.C.R. 385 (1999).*
- ✓ *The FCC did not explain how ISPs can be viewed as users of “exchange access” where they connect to the local network for the purpose of providing information services, not for the “origination or termination of telephone toll services.”* *Bell Atlantic v. FCC, 206 F.3d at 5, quoting 47 U.S.C. § 153 (16).*
- ✓ *The FCC did not explain why its traditional “end-to-end” communications analysis is relevant to whether a call to an ISP is telephone exchange or exchange access; in fact, such an analysis “yields intuitively backwards results.”*

# The Remand Issues

## *ISPs are end users*

- ✓ *The FCC did not explain why an ISP is not “simply a communications-intensive business end user selling a product to other consumer and business end-users.” Bell Atlantic v. FCC, 206 F.3d at 7.*

## *Calls to ISPs terminate locally under the FCC’s own regulations*

- ✓ *Local traffic terminates at the ISP, “clearly” the called party: “the mere fact that the ISP originates further telecommunications does not imply that the original telecommunications does not ‘terminate’ at the ISP.” Bell Atlantic v. FCC, 206 F.3d 1,7 (D.C. Cir. 2000).*

## The Remand Issues

● Thus, the D.C. Circuit found that “the Commission has not provided a satisfactory explanation why LECs that terminate calls to ISPs are not properly seen as ‘terminat[ing]... local telecommunications traffic,’” and why “such traffic is ‘exchange access’ rather than ‘telephone exchange service....’”

*Bell Atlantic v. FCC, 206 F. 3d at 8.*

● The Commission now must address these specific concerns in order to satisfy the D.C. Circuit.

## The D.C. Circuit Pointed The Way

**The FCC can achieve its goal of overseeing the pricing of reciprocal compensation, while maintaining the current carrier arrangements, by finding that calls terminating to ISPs constitute local exchange service**

- ✓ *As Affirmed By The U.S. Supreme Court's Iowa Utilities Board Decision, The FCC Has Ample Jurisdiction To Determine The Pricing Methodology For Local Exchange Services.*
- ✓ *Under The Telecommunications Act of 1996, The Great Majority Of Calls To ISPs Logically Fit Within The Definition Of "Telephone Exchange" Service.*
- ✓ *Most State Commissions, And All Courts, Considering The Issue Have Concluded That Calls To ISPs Within The Same Local Service Area Are Local Under The Terms Of The Parties' Interconnection Agreements.*

## Calls To ISPs Constitute Local Telephone Exchange Under The Act

**The Commission plainly has jurisdiction over ISP-bound traffic under Sections 251 and 252 of the Telecommunications Act of 1996**

✓ The FCC - “Sections 251 and 252 address both interstate and intrastate aspects of interconnection, resale services, and access to unbundled elements. The 1996 Act moves beyond the distinction between interstate and intrastate matters that was established in the 1934 Act, and instead expands the applicability of national rules to historically intrastate issues, and state rules to historically interstate issues. Local Competition Order, 11 F.C.C.R. 15499, 155137 (1996).

✓ The Supreme Court - “The FCC has rulemaking authority to carry out the provisions of this Act, which include sections 251 and 252, added by the Telecommunications Act of 1996.... Section 201 (b) explicitly gives the FCC jurisdiction to make rules governing matters to which the 1996 Act applies.”

AT&T v. Iowa Utilities Bd., 525 U.S. 366, 378, 380 (1999).

## Calls To ISPs Constitute Local Telephone Exchange Under The Act

**Contrary to the ILECs' dismissal of the statute as "irrelevant," the Commission must come to terms with the statutory classification of ISP-bound traffic**

✓ *The FCC has acknowledged that local telecom carriers provide either telephone exchange or exchange access.*

✓ *Calls to ISPs cannot be "exchange access."*

✓ *The statute defines "exchange access" as "for the purpose of the origination and termination of telephone toll service." 47 U.S.C. § 153 (16).*

✓ *End users do not connect to ISPs for this purpose - they connect to obtain information services.*

✓ *End users do not pay a "separate charge" for toll service. 47 U.S.C. § 153 (48).*

✓ *ISPs do not provide telecommunications services - they utilize telecom services to provide information services.*

✓ *The "two services" theory is alive and well - telecom services are provided to the calling party, while information services are provided by the called party.*

## Calls To ISPs Constitute Local Telephone Exchange Under The Act

*ISPs subscribe to “telephone exchange service.”*

- ✓ *The statute defines “telephone exchange” as service which occurs within a local exchange or system of exchanges, and which is covered by the exchange service charge. 47 U.S.C. § 153 (47)(A).*
  - *Both elements are met by ISP-bound traffic.*
  - *ISPs utilize local exchange services just as any other end user.*
- ✓ *The FCC repeatedly equates “telephone exchange” service with “local” service.*

## Calls To ISPs Constitute Local Telephone Exchange Under The Act

*“Information access” is not a stand-alone, separate category of service under the 1996 Act.*

- *FCC already has ruled that information access is only a specialized form of exchange telecom service. Advanced Services Order on Remand, 15 F.C.C.R. 385 (1999).*
- *The MFJ defines “information access” as exchange service. Modified Final Judgement, Section IV (I).*

**Thus, calls to ISPs qualify as telephone exchange service.**

## ISPs Are End Users, And Almost All Calls To ISPs Terminate Locally

*The ILECs would have the Commission classify and treat ISPs as carriers, not end users*

✓ *The “end-to-end” jurisdictional analysis only applies to telecom services and improperly renders ISPs as de facto common carriers.*

✓ *ISPs are end users, and end users are not carriers.*

– *ISPs “are not regulated under title II of the Act.” 47 CFR § 64.702(a).*

– *End users are “any customer of an interstate or foreign telecommunications service that is not a carrier ....” 47 CFR § 69.2(m).*

– *It is the policy of the United States “to preserve the vibrant and competitive free market that presently exists for the Internet and other interactive media.” 47 U.S.C. § 230 (b)(2).*

✓ *Telecommunications and information services are mutually exclusive categories of services under the 1996 Act.*

## ISPs Are End Users, And Almost All Calls To ISPs Terminate Locally

### **The Federal Courts Agree That ISP-Bound Traffic Terminates Locally**

✓ D.C. Circuit - *“Calls to ISPs appear to fit this definition [of termination]: the traffic is switched by the LEC whose customer is the ISP and then delivered to the ISP, which is clearly the ‘called party.’”*

*Bell Atlantic, 206 F.3d at 6.*

✓ Fifth Circuit - *“termination occurs when [the ISP's carrier] switches the call at its facility and delivers the call to ‘the called party’s premises,’ which is the ISP’s local facility. Under this usage, the call indeed ‘terminates’ at the ISP’s premises.”*

*Southwestern Bell, 208 F.3d at 483.*

# ISPs Are End Users, And Almost All Calls To ISPs Terminate Locally

## **The Facts Demonstrate That ISP-Bound Traffic Terminates Locally**

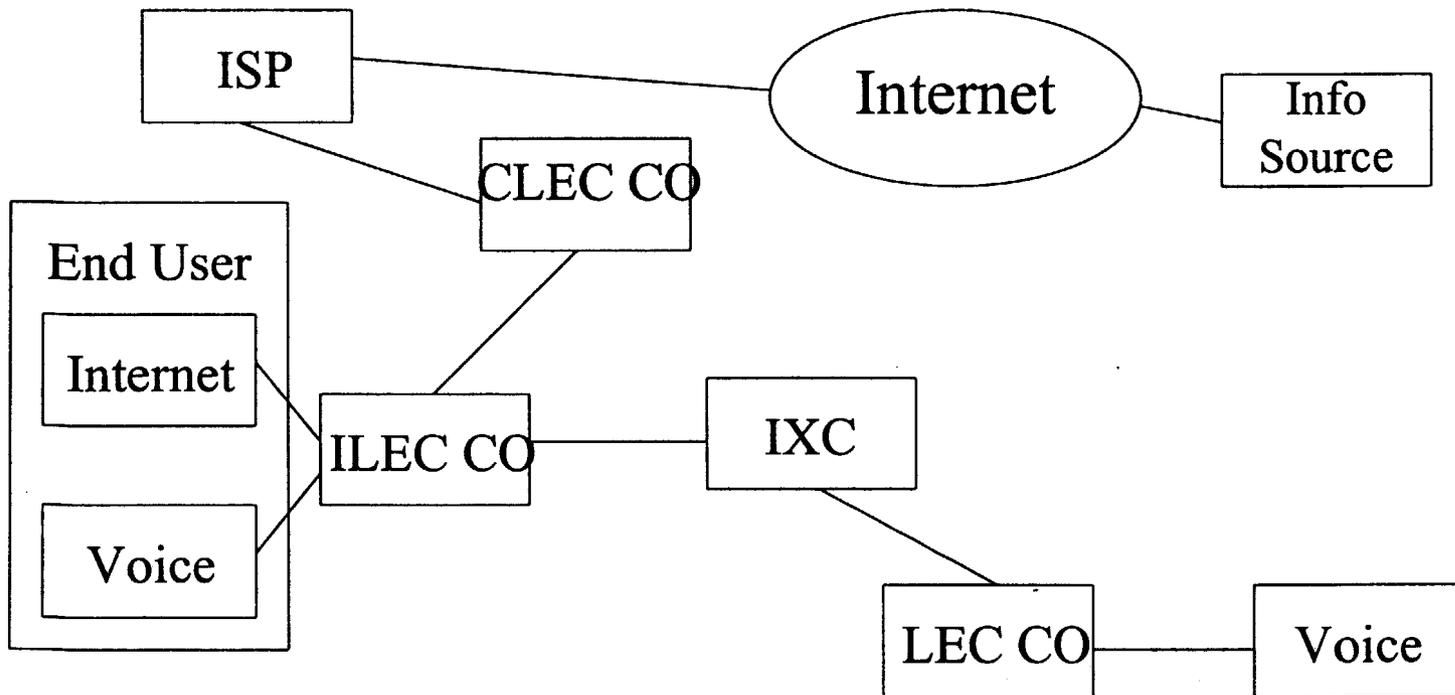
### ISP-Bound Traffic Mirrors Other Local Calls to End Users

- ✓ *End-user uses computer (CPE) to dial ISP's local access number.*
- ✓ *Terminating LEC provides notice of call connection when call is answered by ISP and of call completion when end-user disconnects.*

### Even Under The ILECs' Mistaken Jurisdictional Theory, Calls To ISPs Are Predominantly Local

- ✓ *According to the Hyperion Study, only 9 % of an ISP customer's total online connection time is interstate. Reply Comments of Hyperion Telecom, Inc., CC Docket No. 98-79, filed 1/19/99.*
- ✓ *ISPs increasingly use considerable local caching of website content.*
- ✓ *Many consumers interact with local content residing with local ISPs.*

# ISPs Are End Users, And Almost All Calls To ISPs Terminate Locally



## The Act Requires Reciprocal Compensation For Terminating ISP-Bound Traffic

**The ILECs would have CLECs incur the cost of terminating traffic without receiving just compensation**

- ✓ *LECs use the same local networks to terminate ISP-bound traffic as for other types of voice and data traffic.*
- ✓ *LECs incur actual costs to terminate traffic bound for ISPs -- cost imposed by the originating LEC's customers.*
  - *"...no matter what the payment arrangement, LECs incur a cost when delivering traffic to an ISP that originates on another LEC's network." ISP Declaratory Ruling, 14 F.C.C.R. 3689, 3707 (1999).*
- ✓ *ILEC costs to both originate and terminate ISP-bound traffic already are or could be recovered in their retail local end user rates.*
- ✓ *No cost differences have been demonstrated that would justify allowing the ILECs to discriminate against this particular type of end user-bound traffic.*
  - *ILECs ignore other end users of predominantly inbound calling (call centers, credit card validation centers, travel reservation agencies, home shopping networks, call-in radio shows, ticket outlets, pizza delivery outlets, taxicab companies, etc.).*

## The Act Requires Reciprocal Compensation For Terminating ISP-Bound Traffic

The ILECs would have CLECs incur the cost of transporting and terminating traffic without receiving just compensation

- ✓ *“Bill and keep” is an appropriate compensation mechanism only where telecommunications traffic between carriers is roughly balanced*
- ✓ *ILECs derided the concept in 1996 as “bilk and keep.”*
- ✓ *The FCC rejected “bill and keep” as a mandatory compensation mechanism. Local Competition Order, 11 FCCR. 15499, 16058 (1996).*
- ✓ *Parties remain free to agree to “bill and keep” as part of interconnection negotiations.*

## The Act Requires Reciprocal Compensation For Terminating ISP-Bound Traffic

**The ILECs seek to avoid the larger implications of subjecting ISP-bound traffic to a forward-looking costing methodology.**

- ✓ *CLECs seek to cover forward-looking costs, nothing more.*
- ✓ *To the extent the reciprocal compensation rates originally demanded by the ILECs now are above forward-looking cost, the ILECs are incented to adopt lower, cost-based rates for other interconnection services and network elements as well.*

**The ILECs seek to deny ISPs any competitive alternative for local exchange services.**

# What The Commission Should Do On Remand

## **The FCC should conclude that:**

- ✓ Calls to ISPs within the same LSA are compensable under Section 251 (b) (5) of the Telecommunications Act
- ✓ The Commission retains jurisdiction over ISP-bound local traffic via that same provision
- ✓ Compensation rates for ISP traffic should be:
  - *the same as rates for all other end user-bound traffic*
  - *symmetrical*
  - *based on forward-looking costs*
  - *based on the ILECs' costs of termination*
  - *equal or exceed sum of rates established for ILEC UNE switching and transport plus a portion of the local loop*