

**BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554**

In the Matter of)	
)	
Implementation of the Pay Telephone)	CC Docket No. 96-128
Reclassification and Compensation Provisions)	
of the Telecommunications Act of 1996)	

**RBOC PAYPHONE COALITION’S PETITION FOR
RECONSIDERATION AND CLARIFICATION**

INTRODUCTION AND SUMMARY

In its most recent *Reseller Order*,¹ the Commission, reversing a legal and policy judgment reached in 2001 and defended before the D.C. Circuit, decided that switch-based resellers (“SBRs”), and not facilities-based long distance carriers (“IXCs”), should bear primary regulatory responsibility for paying per-call compensation on payphone-generated “dial-around” calls that they both carry. The Commission’s decision will likely inflict significant – and avoidable – costs on all legitimate segments of the industry. The Commission should reconsider its decision or, at a minimum, clarify its order to head off the most serious negative consequences.

I. A. The *Reseller Order* is a textbook example of how *not* to regulate. The Commission has never claimed that this rule is either efficient or sensible, nor could it. To the contrary, the Commission’s heavy-handed regulatory regime will inflict substantial dead-weight losses on the industry, while ensuring that payphone service providers are *unable*, as a practical matter, to collect fair compensation for payphone-generated calls. Such action is contrary to the

¹ Report and Order, *Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-128, FCC 03-235 (rel. Oct. 3, 2003).

statutory fair-compensation requirement, conflicts with the deregulatory policies behind the 1996 Act, and is arbitrary and capricious.

B. The justifications the Commission offered for its decision are without merit. The Commission stated that the *Second Payphone Recon. Order* made IXCs “collection agents” for payphone service providers (“PSPs”). *Reseller Order* ¶ 20. That statement is erroneous and cannot provide any basis for the Commission’s determination at issue here. Under the *Second Payphone Recon. Order*, IXCs were responsible for paying compensation on all compensable calls they chose to accept from payphone providers: thus, in accepting such calls from PSPs, IXCs were assuming their *own* obligations to pay for such calls, not the obligations of any other party. To be sure, IXCs were expected to build the cost of paying such compensation into the rates they charged all of their customers, including their SBR customers. That does not mean they were acting as collection agents in any instance.

In the same vein, the Commission’s “primary economic beneficiary” rationale cannot justify the Commission’s policy choice. The Commission has recognized in the past (and in this order) that administrability considerations must control which long-distance carrier is responsible for per-call compensation; the Commission effectively ignored such considerations in the *Reseller Order*. And, in any event, the Commission’s ruling that the SBR, and not the IXC, was the primary beneficiary of payphone-generated calls that both carry is arbitrary. The IXC also benefits from PSPs’ services in connection with such calls – perhaps even more so than the SBR.

The Commission also expressed concern that under the *Second Payphone Recon. Order*, “PSPs may have been under or overcompensated.” *Reseller Order* ¶ 21. There is no evidence whatsoever that any PSP was ever overcompensated. Moreover, the Commission’s concern reflects an additional error of law. Nothing in the *Second Payphone Recon. Order* mandates any

overcompensation. The arrangements that IXC's choose to make to comply with their obligation cannot represent "overcompensation" as a matter of law; rather, they represent voluntary business arrangements designed to minimize collective costs of compliance. The Commission's rules and fundamental policies approve of such arrangements.

C. For reasons the Coalition has set out at length elsewhere, the Commission should return to the rule adopted in the *Second Payphone Recon. Order*, and clarify that the manner in which IXC's charge their customers for any per-call compensation charges incurred on calls that IXC's carry for those customers, including SBRs, is a matter to be left to resolution in the market.

II. At a minimum, the Commission should clarify that, in any case where a reseller fails to comply with the audit and verification requirements set forth in new section 64.1320, the underlying facilities based IXC remains responsible for paying compensation on any calls passed to such a reseller. That conclusion is compelled by the terms of the Commission's regulations, which make clear that compliance with those requirements is "a **precondition** to tendering payment pursuant to section 64.1310(a)." *Reseller Order*, App. C, 47 C.F.R. § 64.1320(a) (emphasis added). Until the SBR has complied, the IXC must be treated as the completing carrier for purposes of complying with the Commission's tracking and payment requirements.

Even if the Commission's rationale for rejecting the IXC-pays rule were valid in situations where SBRs comply with their audit and verification obligation, they plainly have no application in cases where an SBR is either unwilling or unable to meet those requirements. In such a case, the IXC has no reason to treat the call to the reseller any differently from any other call routed to a long-distance service customer. Moreover, if an SBR chooses to accept whatever reimbursement arrangements are available in the market rather than comply with the

Commission's audit requirements, their choice is presumptively efficient. The Commission would have no reason to interfere with such a choice.

DISCUSSION

The *Reseller Order* represents the Commission's most recent attempt to deal with a problem that has vexed the per-call compensation system since the Commission first attempted to implement the requirement, set forth in section 276(b)(1)(A), that payphone providers be "fairly compensated for each and every completed . . . call using their payphone." 47 U.S.C. § 276(b)(1)(A). Many payphone calls for which no other compensation is paid, and which are therefore subject to per-call compensation, are carried by multiple carriers. In particular, calls may be originated on a payphone, passed by the local exchange carriers ("LEC") to an IXC, which may, in turn, pass the call to an SBR. The SBR may pass the call to a second SBR, and so on.

In the first of its *Payphone Orders*,² the Commission decided that SBRs should be responsible for tracking and paying per-call compensation because the Commission believed that such carriers would have the ability to track their compensation obligations.³ Almost immediately, it became clear that placing tracking and payment obligations on SBRs was causing significant shortfalls in compensation. The Commission accordingly ordered IXCs to provide information to PSPs to enable PSPs to identify the calls passed to SBRs;⁴ SBRs have always

² Report and Order, *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, 11 FCC Rcd 20541 (1996) (subsequent history omitted) ("*First Payphone Order*"); Order on Reconsideration, *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, 11 FCC Rcd 21233 (1996) ("*First Payphone Recon. Order*").

³ *First Payphone Recon. Order*, 11 FCC Rcd at 21277, ¶ 92.

⁴ See Memorandum Opinion and Order, *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, 13 FCC Rcd 10893 (1998).

been subject to enforcement action for non-payment. Nonetheless, the Commission found that the system it had adopted was causing PSPs to “suffer shortfalls in compensation when calls are routed from an IXC to [an SBR]”; accordingly, the Commission found that it was required to revise its regulations “to fulfill the mandate of section 276.”⁵ The Commission therefore determined that “the carrier responsible for compensating the PSP for such calls is the first facilities-based interexchange carrier to which a completed . . . payphone calls is delivered by the LEC,” unless the SBR undertakes that responsibility.⁶

After the *Second Payphone Recon. Order* was reversed on procedural grounds, the Commission revisited this issue. The Commission had defended its prior order as legally sound and fully justified as a policy matter, and there was undisputed record evidence that the first-switch-carrier-pays system was reducing both PSP compensation shortfalls *and* disputes over per-call compensation. Nor was there any concrete evidence of implementation problems that could not be overcome through market mechanisms. Nonetheless, the Commission returned to its original rule, under which the SBR is responsible for tracking and paying compensation and the IXC is responsible merely for identifying the calls passed to the SBR. Although this time the Commission’s reporting and audit requirements are more elaborate, the legal obligations and enforcement mechanisms are essentially indistinguishable from those that the Commission found to be in violation of section 276 in the *Second Payphone Recon. Order*. Accordingly, the Commission should reconsider its determination and return to the rule adopted in the *Second Payphone Recon. Order*.

⁵ Second Order on Reconsideration, *Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, 16 FCC Rcd 8098, 8102, ¶ 8, 8103, ¶ 10 (2001) (“*Second Payphone Recon. Order*”).

⁶ *Id.*, at 8102-03, ¶ 9.

A. The *Reseller Order* Is Massively Inefficient and Will Be Ineffective

The *Reseller Order* is the wrong approach to a significant but ultimately simple problem. The Commission determined that, in order to avoid significant and unlawful shortfalls in compensation, it would be required to impose elaborate reporting and audit requirements on every single carrier that completes a call from a payphone – a requirement that covers hundreds of entities, many of which are not subject to any other significant regulation. In other words, the Commission’s approach – despite the Commission’s express policy of relying on market mechanisms to ensure fair compensation wherever possible – abandons market mechanisms in favor of heavy-handed, top-down regulation.

A quick examination of the structure of the industry reveals the basic problem with the Commission’s approach. According to the FCC’s own data, there are hundreds of entities engaged in resale of long-distance service that may be affected by the FCC’s new audit and reporting requirements. *See Reseller Order* ¶¶ 70, 72. By contrast, five IXCs filed comments in the proceeding leading up to the *Reseller Order* – AT&T, WorldCom (MCI), Sprint, Qwest, and Global Crossing. (In addition, ILECs carry a significant number of compensable calls; however, no ILEC objected to the first-switch-carrier-pays rule.)

Under the rule adopted in the *Second Payphone Recon. Order*, SBRs had no regulatory obligations whatsoever. They had no reporting obligations, no audit requirements, and no regulatory obligation to pay compensation. Their only obligation (and, as discussed below, this is a *market* obligation, not a regulatory obligation) was to make arrangements with IXCs – their suppliers – that would enable IXCs to comply with IXCs’ own payment obligations in the most efficient manner and that would ensure that IXCs were adequately compensated for the services

they performed. Under the *Reseller Order*, every SBR – hundreds of companies, many of them tiny – are ordered to comply with necessarily burdensome audit requirements, reporting requirements, and compensation requirements. Compliance costs for SBRs – assuming that the hundreds of SBRs subject to the requirements comply – will run into millions of dollars. Yet no less burdensome requirements could even begin to provide any assurance that SBRs’ obligations would be verifiable and enforceable.

Moreover, there is no regulatory relief for IXC. To the contrary, IXCs face *more* burdensome regulatory requirements under the *Reseller Order* than they did under the *Second Payphone Recon. Order*. Not only must IXCs continue to report on all completed calls that they carry, but they must also segregate all calls routed to certified SBRs and provide the number of call attempts, identified by ANI, along with the name and address of the SBR responsible for the call. *See Reseller Order*, App. C, 47 C.F.R. § 64.1310. In addition, IXCs are required to comply with unprecedented audit and certification requirements – even though PSPs have not raised complaints regarding compensation payments for calls completed on IXC networks. Indeed, the Commission’s audit requirements apply their terms to *all* entities that complete payphone-originated calls, even though the bulk of enforcement issues have related to calls delivered by SBRs.

Despite these costs, the Commission did not find, and could not have found, that the additional costs imposed on the industry would address PSPs’ concerns about undercompensation.⁷ The *Reseller Order* essentially re-adopts the regulations from the original *Payphone Orders* that the Commission already determined were incompatible with the fair

⁷ The Commission vaguely concluded that “these new measures will reduce the likelihood of any SBR misconduct” (*Reseller Order* ¶ 34), but even a reduced likelihood of misconduct leaves substantial room for undercompensation as a result of SBR non-compliance.

compensation requirement of section 276. The only change is that the Commission has imposed far more extensive reporting and certification requirements in an attempt to address rampant regulatory violations by SBRs. Given that SBRs massively violated their clear obligation to pay under the prior regime, however, there is no rational way for the Commission to assume that SBRs will comply effectively with the regime established in the *Reseller Order*.⁸

Indeed, recent evidence confirms that most SBRs will not comply with their obligations to audit, certify, and pay compensation. One member of the Coalition⁹ has examined carriers' compliance with interim compensation payments. In the order establishing interim compensation obligations, the Commission identified more than 500 long-distance carriers as responsible for payment of compensation. To date, the Coalition member has, after significant collection efforts, managed to recover only approximately 40% of the revenue to which it was entitled under the Commission's orders from 29 carriers. This is 14 months after the Commission established responsibility for Interim Compensation.¹⁰ Approximately 40% of the uncollected revenue is likely to be negatively affected by bankruptcies and other business failures. Whether the PSP will be able to collect the remaining 20% – owed by hundreds of additional carriers – is very much in doubt.

This example illustrates two important points. First, even on pain of penalty and even where clearly identified as responsible, the vast majority of SBRs will not voluntarily comply with their regulatory obligations to pay per-call compensation. Only a handful of SBRs ever

⁸ The Commission stated that it would “address past SBR alleged misconduct by imposing an affirmative duty to self-report, self-identify, and pay.” *Id.* But the SBRs' responsibility under the prior regime, as well, was to self-report, self-identify, and pay.

⁹ The Coalition includes the payphone operations of the Verizon telephone companies and SBC.

¹⁰ See Fifth Order on Reconsideration and Order on Remand, *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, 17 FCC Rcd 21274 (2002).

approached the PSP to resolve their outstanding compensation obligations; the rest had to be pursued. Second, it will likely be impossible, as a practical matter, for PSPs to pursue non-compliant SBRs. Even if an SBR certifies, if it fails to pay the amounts it owes and those amounts do not justify the cost of pursuing an enforcement action, a PSP will be left without any practical recourse. This will often be the case. The cost of pursuing a formal complaint with the Commission easily runs to many tens of thousands of dollars; the cost of federal court litigation can be higher. Such amounts likely exceed the compensation obligations of most resellers vis-à-vis most PSPs. Thus a PSP will be faced with the prospect of paying two dollars to collect a dollar (or a quarter) – a foolish investment and a practical impossibility.

Moreover, even if the PSP decides to invest in enforcement action, the possibility of obtaining effective relief from a non-compliant SBR is remote. According to the carrier mentioned above, perhaps as many as *half* of the entities identified in the Commission’s latest interim compensation order as responsible for payment of compensation have gone bankrupt and/or out of business since they incurred those obligations. SBRs that face enforcement action can simply fold up shop and start elsewhere or under a new name. To be sure, in theory, enforcement action can deal with such tactics, but in practice – as the Commission knows – it cannot.¹¹ The Commission’s enforcement resources are limited, and the dollars at stake in any individual case are likely to be relatively small. It is the cumulative effect of non-compliance that inflicts real harm on PSPs; yet the very fact that non-compliance will be so widespread – as

¹¹ The Commission noted that the D.C. Circuit “found that the PSPs had remedies to recover this debt from the delinquent carriers,” *Reseller Order* ¶ 32, but, as the Commission found in the *Second Payphone Recon. Order*, this legal remedy is not enforceable as a factual matter in the case of SBRs, *see* 16 FCC Rcd at 8102, ¶ 8 (finding that “PSPs have been frustrated in their efforts to receive compensation for certain coinless calls”).

past experience has proven beyond reasonable dispute – ensures that the Commission cannot deal with such non-compliance in a timely or effective way.

At bottom, the *Reseller Order* requires IXCs and SBRs to pay millions on compliance costs while promising little or nothing to PSPs except more frustration. It does not fulfill the fair compensation mandate of section 276. And it violates bedrock congressional and Commission policies. As the Commission has recognized in this very context, the Telecommunications Act of 1996 is intended to create a “pro-competitive *deregulatory* national framework.”¹² Moreover, the Commission specifically held that “[i]t is only in cases where the market does not or cannot function properly that the Commission needs to take affirmative steps to ensure fair compensation.”¹³ As discussed below, the market can ensure fair compensation by making IXCs responsible for paying compensation on completed calls they choose to accept from PSPs. The Commission abandoned that market mechanism in favor of regulatory requirements that penalize the entire industry on account of the regulatory non-compliance of one class of carriers – SBRs. Moreover, the Commission’s solution will not work. It is hard to conceive of a regulatory approach that is more flawed in conception or in execution.

B. The Commission’s Justification for the *Reseller Order* Were Legally Erroneous

The Commission did not find – and could not have found – that its new regulatory regime would be either efficient or effective. To the contrary, the Commission acknowledged the “low administrative cost and ease associated with placing liability” on IXCs, not SBRs. *Reseller Order* ¶ 31. Instead, the Commission justified its decision on three grounds. First, it found that it was inappropriate and legally suspect to require IXCs to act as “collection agents” for PSPs

¹² *First Payphone Order*, 11 FCC Rcd at 20543, ¶ 2 (quoting S. Conf. Rep. No. 104-230, at 1 (1996)) (emphasis added).

¹³ *Id.* at 20567, ¶ 49 (emphasis added).

with respect to compensation obligations incurred by SBRs. *See id.* ¶ 20. Second, the Commission found that SBRs are the “primary economic beneficiaries” of payphone-generated calls they carry and therefore should be responsible for paying compensation. Third, the Commission held that placing compensation obligations on IXC risks “overcompensating” PSPs. *Id.* ¶¶ 21, 27, 28.¹⁴ Each of these determinations is legally wrong.

First, the Commission never made IXCs “collection agents” for PSPs; the Commission has mistaken a lobbyist’s applause line for legal analysis. In fact, the *Second Payphone Recon. Order* provides that IXCs *themselves* should be responsible for payment of compensation on payphone-originated calls transmitted to SBRs. Thus, the Commission held that, to comply with its statutory obligations, it was *legally obligated* to “modify our payphone compensation rules to require the first underlying facilities-based interexchange carrier to whom the LEC directly delivers the call to compensate the PSP for each completed . . . payphone call.” 16 FCC Rcd 8105, ¶ 15. The Commission did *not* hold that IXCs should pay on SBRs’ behalf, nor did it hold that IXCs were required to collect compensation for any other party. It held, simply and directly, that IXCs should be responsible for paying for all completed calls they choose to accept from PSPs.

Relatedly, the Commission was never under any illusion about IXCs’ ability to track calls carried by SBRs to completion. *Cf. Reseller Order* ¶ 20. Rather, the Commission clearly and explicitly recognized that IXCs would sometimes have to obtain information about call completion from “the switch-based resellers that complete the calls.” *Id.* at 8106, ¶ 16; *see also id.* at 8105, ¶ 14 (noting evidence that only the “last switch” carrier “can know if a call is

¹⁴ The Commission also found that PSPs might be undercompensated under the IXC-pays regime. No PSP complained that the IXC-pays regime led to greater uncollectible problems than the SBR-pays regime; to the contrary, every PSP reported that collection performance improved.

completed”). Rather, the Commission determined that it would be more efficient to adopt a system that depends on market mechanisms – in particular, the contractual arrangements between IXCs and SBRs – to solve any technical issues related to tracking compensable calls. As the Commission held, “underlying facilities-based carriers, who have a customer relationship with resellers, are in a far better position to track the calls and provide adequate information to PSPs.” *Id.* at 8105, ¶ 16. The Commission also found that “facilities-based carriers may recover from their reseller customers the expense of payphone per-call compensation and the cost of tracking compensable calls.” *Id.*, at 8106, ¶ 18. Precisely because facilities-based carriers have a contractual relationship with their reseller customers, they are far better situated to enforce their rights than a PSP, which has no contractual relationship and no leverage in attempting to collect unpaid amounts.

Second, the Commission’s determination that SBRs are “the primary economic beneficiary” of the calls they deliver – even assuming it is correct – does not justify the Commission’s policy choice. The Commission has never held that the determination that a carrier is the “primary economic beneficiary” should determine responsibility for paying per-call compensation. If that were true, then non-switch-based resellers – which are also presumably the “primary economic beneficiary” of the calls they bill for, under the Commission’s analysis – would also be responsible for paying compensation, but they are not. *See First Payphone Recon. Order*, 11 FCC Rcd at 21277, ¶ 92 (holding that debit-card providers should not be required to track and pay compensation). Rather, the allocation of tracking and payment responsibility among interexchange carriers has always depended exclusively on considerations of

administrability.¹⁵ Thus, in the *First Payphone Recon. Order*, the Commission decided that switch-based resellers should be responsible for tracking and paying compensation because of their ability to do so using their own switching capacity. *See* 11 FCC Rcd at 21277, ¶ 92.¹⁶ When the Commission determined that SBRs' payment obligation could not be efficiently enforced, it shifted the responsibility to IXCs. To transfer the payment responsibility *back* to SBRs without an adequate showing that such administrative problems could be overcome, solely on the ground that the SBR is the "primary economic beneficiary" of certain calls, is inconsistent with the Commission's prior practice and unjustifiable.

In any event, the Commission's determination that SBRs are the "primary economic beneficiary" of calls they complete is purely arbitrary. In fact, IXCs benefit from the calls that they carry for SBR customers just as clearly as they benefit from calls they carry for other end-user customers: if reselling carriage of payphone-originated calls were not beneficial to IXCs, they would not be in the business. The Commission simply noted that "PSPs provide services to the SBRs so that the SBRs can render services to their SBR customers." *Reseller Order* ¶ 29. But the exact same thing can be said about IXCs and their SBR customers. The Commission offered no reason for designating SBRs, but not IXCs, *the* "primary" beneficiary.

Third, the Commission's concern about "overcompensation" as a result of requiring IXCs to pay compensation on all completed calls they carry ignores the fact that IXCs were not required to pay compensation on a single uncompleted call under the IXC-pays regime adopted

¹⁵ The Commission relied on its "primary economic beneficiary" analysis only in deciding that IXCs as a class – not LECs or end-users – should track and pay compensation. *See First Payphone Order*, 11 FCC Rcd at 20590, ¶ 97. There is no dispute about that allocation of responsibility here.

¹⁶ The Commission's statement that it found SBRs to be primary economic beneficiaries of the calls they delivered in the *First Payphone Recon. Order* is simply incorrect; the Commission never so held. Even if it had, the Commission revisited this issue in this rulemaking proceeding and could not simply rely on a prior (erroneous) determination.

in the *Second Payphone Recon. Order*.¹⁷ The Commission made clear that IXCs were only required to pay compensation on *completed* calls. And it found that IXCs are in a position to track calls to completion or to obtain information from their SBR customers. All evidence in the record confirms that view.¹⁸

Accordingly, to the extent that IXCs have chosen not to obtain tracking data on some calls and instead to pay on all calls completed to an SBRs platform, such an arrangement does not result in overcompensation but rather reflects efficient compliance with regulatory obligations. If an IXC chooses to pay on some calls that may (or may not) have been completed because it is too expensive to determine whether the call was in fact completed, and the PSP chooses to accept such payment, that voluntary arrangement fully *complies* with the Commission's rules. Indeed, the Commission has always held that the regulatory obligation to pay per-call compensation on every completed call and at the regulated rate applies only in the *absence* of a voluntary contractual relationship. See 47 C.F.R. § 64.1300(a); *Reseller Order*, App. C, § 64.1300(b). To be sure, parties reach agreements in the shadow of regulatory requirements. But if IXCs pay on certain calls that are not, in the end, completed, this is their choice, and is presumably cheaper and more efficient for them (and therefore better for consumers) than incurring additional expense to improve the accuracy of their tracking systems.

¹⁷ It is, moreover, ludicrous to assert that PSPs have ever been overcompensated for calls when the record evidence proves that PSPs have had significant uncollectible problems throughout the history of the per-call compensation system. Presumably, the Commission meant only to say that individual carriers could theoretically pay compensation on calls that were not actually completed, *not* that PSPs have ever actually been “overcompensated,” a proposition for which there is not a scintilla of record evidence.

¹⁸ IXCs confirmed that they have been able to obtain call-tracking data from their SBR customers, though some complained that SBRs were difficult to do business with. But if IXCs – which have a voluntary contractual relationship with SBRs – find them hard to deal with, the Commission must conclude that PSPs – who have no other business relationship with SBRs and no leverage over them at all – will be in a far worse position to enforce their rights against SBRs.

That result is therefore the economically rational outcome and cannot justify adopting a system that guarantees that PSPs will be unable to collect compensation owed from dozens if not hundreds of SBRs.

C. The Commission Should Return to the Rule Adopted in the *Second Payphone Recon. Order*

For reasons that the Coalition has set out at length elsewhere, the Commission should accordingly reconsider its misguided determination in the *Reseller Order* and return to the IXC-pays rule adopted in the *Second Payphone Recon. Order*. IXCs should pay for all completed payphone-originated calls they choose to accept. The manner in which IXCs charge their customers (end-users or SBRs) for their services is a matter to be left to the market. Indeed, the basic strength of the IXC-pays rule is that it depends on market mechanisms to ensure that IXCs and SBRs share information and allocate costs efficiently. IXCs and SBRs alike insist that the long-distance market is competitive, and the Commission has taken the same position for years. Accordingly, IXCs should be able to offer whatever business terms they wish to their SBR customers, including appropriate terms regarding payphone-originated calls. If an SBR does not find the terms acceptable, it can go elsewhere for service. There is no justification for adopting regulations to govern the flow of information and compensation from SBRs to IXCs: as the Commission has held, it would adopt such regulations only if the market could *not* address the issue. *First Payphone Order*, 11 FCC Rcd at 20567, ¶ 49.

Indeed, the Commission should have found the availability of market mechanisms under the IXC-pays rule to be a decisive advantage. The elaborate and costly safeguards that the Commission adopted in the *Reseller Order* would have been unnecessary. And costs for everyone – except SBRs who intend to cheat – will be higher under the system the FCC has adopted. A system that penalizes all legitimate segments of the industry and rewards scofflaws

surely “epitomizes arbitrary and capricious decisionmaking.” *Illinois Pub. Telecomms. Ass’n v. FCC*, 117 F.3d 555, 564 (D.C. Cir. 1997).

II. THE COMMISSION SHOULD CLARIFY THAT UNLESS SBRs QUALIFY AS “COMPLETING CARRIERS” BY COMPLYING WITH AUDIT AND CERTIFICATION REQUIREMENTS, IXCs REMAIN RESPONSIBLE FOR PER-CALL COMPENSATION PAYMENTS

In the event the Commission does not reconsider the *Reseller Order*, it is imperative that the Commission clarify the consequences when SBRs do not comply with the audit and certification requirements set forth in section 64.1320 of the rules adopted in the *Reseller Order*. With hundreds of SBRs subject to those requirements, many of them small operations with limited revenues, it is virtually certain that the vast majority will not comply with the audit and tracking requirements. Under a literal reading of the Commission’s rules, all of those carriers could be subject to criminal penalties. Such a reading is neither inevitable nor sensible.

Instead, the Commission should make clear that, in the event an SBR chooses not to comply with the audit and certification requirements, that SBR cannot be considered a “Completing Carrier” within the meaning of the Commission’s rules. Moreover, an IXC is relieved of responsibility for tracking and paying compensation only for calls transmitted to Completing Carriers – not for calls transmitted to non-certifying SBRs.

Those conclusions are the most logical reading of the *Reseller Order*. First, in the rules themselves, the Commission makes clear that compliance with the audit requirement is a “precondition to tendering payment pursuant to section 64.1310(a).” *Reseller Order*, App. C, § 64.1320(a) (emphasis added). A carrier is not permitted to participate in the per-call compensation system as a Completing Carrier *at all* unless the carrier has complied with its audit and certification requirements. Moreover, the Commission explicitly required complying SBRs to “send copies of the SBR System Audit Report to its interexchange carriers.” *Reseller Order*

¶ 38; *see also id.*, App. C, § 64.1320(e). That requirement indicates that *unless* an IXC has received appropriate certification from an SBR customer, the IXC should continue to track and pay compensation on all calls routed to that customer. Otherwise, there would have been no reason for the Commission to require SBRs to send such reports to their IXCs.

That conclusion is also the only reading of the *Reseller Order* that makes sense in light of the order's underlying rationale. The Commission decided to shift primary responsibility for paying compensation to SBRs based on its belief that “the SBR is the carrier best able to determine whether a payphone originated call directed to a SBR switch has been answered.” *Reseller Order* ¶ 35. In other words, an SBR has the *ability* – based on its position in the call path – to implement systems that would track completed calls accurately. But the mere *ability* to implement such systems does not mean that such systems have been implemented in fact. And if an SBR has not complied with the audit requirement, there is no basis for the Commission to conclude that they have *any* ability to track calls from PSPs. In that situation, the IXC is plainly the party best able to track and pay compensation.

Moreover, requiring IXCs to pay compensation in this circumstance, and leaving the relationship between the IXC and its non-complying SBR customer unregulated, presents no “fairness issues” of the type that the Commission (mistakenly) believed were presented by its prior IXC-pays regime. Most important, every SBR has the opportunity to comply with auditing requirements; every IXC has the choice of doing business only with SBRs that have complied with those requirements. An SBR never has to reimburse an IXC for per-call compensation payments unless it chooses not to comply with its regulatory obligations; no IXC ever has to pay compensation on a call routed to an SBR unless it chooses to provide service to non-compliant

SBRs. Any payments made by IXC for calls routed to SBRs will accordingly reflect purely voluntary choices by both parties.

There is every reason to hope that if the Commission issues the clarification, some of the benefits of the IXC-pays rule will be retained, while giving qualified SBRs the legal right to handle their own payment obligations. For many SBRs, it may be inefficient to implement the systems required to track calls, and the costs of regulatory compliance themselves may be prohibitive. By contrast, if such carriers experience high call completion rates – and in this age of answering machines and voice mail, call completion rates are likely to be high – they may consider it a reasonable bargain to pay IXCs for all calls delivered to their platforms.

Alternatively, some SBRs that have call tracking systems but prefer to avoid the expense of undergoing an audit, may be able to enter into voluntary arrangements to provide verifiable data to IXCs, who will in turn use that data to determine their ultimate payment obligations to PSPs.

A third possibility is that some IXCs may enter into voluntary arrangements with PSPs to dispense with per-call tracking altogether, or with respect to certain classes of calls, and to substitute a reasonable presumption, or an assumed call completion percentage based on traffic studies. For example, an IXC might offer to pay on 80% or 90% of all call attempts delivered to SBRs, and a PSP might well accept such a discount in exchange for greater certainty and verifiability. The IXC could then pass such savings on to its SBR customers, gaining a legitimate competitive advantage over other IXCs.

In sum, with appropriate clarification, the *Reseller Order* may still leave room for market mechanisms to operate; to the extent it does, all industry segments – and consumers – will be better off. For this reason, it is critical that the Commission act on the Coalition’s petition before the new rules go into effect. Even though the interpretation put forward here is plainly the most

reasonable understanding of the *Reseller Order*, the Commission knows from experience that, if there is any uncertainty, IXCs and SBRs will exploit it to underpay their compensation obligations, leaving PSPs holding the bag. *See Second Payphone Recon. Order*, 16 FCC Rcd at 8102, ¶ 15. IXCs may claim that they do not have to pay compensation on *any* calls routed to SBRs, even if the SBRs have not complied with the auditing requirements that are a “precondition” of participation as a completing carrier in the per-call compensation regime. The Commission should forestall that result, and the inevitable disputes that would ensue, by clarifying its rules in the manner set forth herein.

CONCLUSION

The Commission should grant the petition.

Respectfully submitted,



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