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EX PARTE

Filed via ECFS

June 28, 2006

Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street SW
Washington, DC 20554

Re: *In the Matter of Payphone Access Line Rates* - CC Docket No. 96-128

Dear Ms. Dortch:

On June 27 2006, Lynn Starr and Melissa of Qwest, met with Michelle Carey to discuss the above-captioned proceeding.

The attached powerpoint presentation was used as the basis for discussion.

Also attached is a memorandum that further details Qwest's position. The memorandum is identical to the *ex parte* presentation submitted by Qwest on June 22, 2006 in this docket, with the exception that several minor typographical errors have been corrected.

This *ex parte* is being filed electronically pursuant to 47 C.F.R. §§ 1.49(f) and 1.1206(b). Please contact me at 202.429.3125 if you have any questions.

Sincerely,

/s/ Lynn Starr

Attachments

Copy to:
Michelle Carey

Qwest®

Spirit of Service℠

In the Matter of Payphone Access Line Rates
CC Docket No. 96-128

June 27, 2006

Overview

- The FCC cannot grant refunds to the payphone providers.
- The FCC cannot order refunds under the Communications Act without suspension and accounting order.
- Delegation of authority to the states did not reserve refund authority.
- Refund evaluation would need to be conducted on a case-by-case basis—essentially through federal rate cases.
- The "Wisconsin Order" was a rate order and operates only prospectively.
- The payphone providers' "waiver" argument is spurious, and does not apply to Qwest in any event.

What Payphone Providers Want the FCC to Do

- Rule that ILEC intrastate PAL rates were unlawful between 1997 and (in Qwest's case) 2002.
- Rule that this unlawfulness is caused by failure to abide by a ratemaking order in 2002 (the *Wisconsin Order*).
- Rule that normal principles of filed rate and retroactive rulemaking do not apply because the RBOCs made a "promise" in 1997 that essentially eviscerates these doctrines forever.
- Rule that a federal right of refund exists, and that this right supersedes:
  - Federal law on federal refunds.
  - State law on refunds based on intrastate tariffs.

What the FCC did Concerning PAL Tariffs

- Delegated authority to states to review intrastate PAL tariffs under state tariff processes.
- Described standards under which such review was to be conducted (e.g., "new services test").
- Maintained oversight to describe additional standards for state tariffs.
- In *Wisconsin Order*, provided final (as of this time) set of rules to be followed by states and RBOCs.
- Otherwise relegated issue to state processes.

What the FCC Could Have Done

- Could have required that PAL tariffs be filed at FCC subject to federal tariff procedures and processes.
- Could have reserved additional authority over state PAL rates (subject to basic division of jurisdiction concerns).
- Could have intervened in state rate cases and other proceedings.
- In any or all of these events, basic legal protections against unlawful refunds through retroactive ratemaking would have had to be preserved.
- But the FCC chose a different route.

FCC's Refund Authority is Limited by Statute

- FCC has been delegated extensive preemptive authority over state payphone services.
- This did not include preemption of state refund rules in a manner that bypassed the FCC's own refund statute.
- In order to accomplish that preemption, FCC would have needed to adhere to its own statutorily mandated rules regarding refunds.
- The FCC instead left the matter of refunds to state law.
- This is not a question of what preemptive power the FCC might have exercised—it is a question of what power it actually exercised in a lawful fashion.

What Payphone Providers Have Done

- Filed complaints under state law objecting to intrastate PAL tariffs.
- Objected to intrastate rates.
- Sought refunds and/or reparations under state law.
- Used state appellate procedures if state regulatory authority did not apply both state law and FCC guidelines appropriately.
- Filed federal lawsuits seeking damages.

FCC Cannot Bypass Statutory Limits on Refunds Through Delegation

- FCC refund authority limited by federal statute.
- State refund authority limited by state statutes.
- Payphone providers want to bypass both protections against unlawful refunds by having a federal refund from charges under a state tariff.
- Such action would clearly be unlawful.

So-called “Waiver” Argument is Spurious

- Payphone providers claim that a promise by RBOCs that, if they filed new PAL rates between April 4 and May 19, 1997, these rates would be effective as of April 15, 1997, constituted an eternal waiver of the filed rate doctrine and all FCC and state rules regarding tariff processes and retroactive ratemaking.
- This argument is frivolous on its face.
- In addition, Qwest had no tariffs covered by this promise or the subsequent ***Waiver Order***.
- Moreover, Qwest’s certification of compliance with the “new services” test was challenged before the FCC, and the challenge was rejected.

Qwest. Spirit of Service

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EX PARTE

June 27, 2006

Marlene H. Dortch
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Federal Communications Commission
Room TW B-204
445 12th Street, S.W.
Washington, DC 20554

RE: *In the Matter of Payphone Access Line Rates* – CC Docket No. 96-128

Dear Ms. Dortch:

The purpose of this memorandum is to examine the arguments by various payphone providers to the effect that the Federal Communications Commission ("Commission") should issue an order essentially decreeing that the payphone access line ("PAL") rates of Qwest Corporation ("Qwest") and other Regional Bell Operating Companies ("RBOCs") were unlawful between April 15, 1997 and sometime in 2002 (depending on the individual state) when rates modified to take account of the new Commission guidelines set forth in the *Wisconsin Order*[1] took effect. There are currently at least five proceedings at the Commission in which this issue has been raised,[2] one of which is just entering the comment cycle.[3] In addition, state regulators have asked

[1] *In the Matter of Wisconsin Public Service Commission, Order Directing Filings*, Memorandum Opinion and Order, 17 FCC Rcd 2051 (2002) ("*Wisconsin Order*").

[2] Illinois Public Telecommunications Association Petition for a Declaratory Ruling, CC Docket No. 96-128, filed July 30, 2004; Petition of the Independent Payphone Association of New York, Inc. for an Order of Pre-emption and Declaratory Ruling, CC Docket No. 96-128, filed Dec. 29, 2004; Southern Public Communications Association Petition for a Declaratory Ruling, CC Docket No. 96-128, filed Nov. 9, 2004; Petition of the Florida Public Telecommunications Association, Inc. for a Declaratory Ruling and for an Order of Preemption, CC Docket No. 96-128, filed Jan. 31, 2006; Michigan Pay Telephone Association Second Petition for Declaratory Ruling, CC Docket No. 96-128, filed May 22, 2006.

[3] *See Public Notice*, Pleading Cycle Established for Michigan Pay Telephone Association Petition for Declaratory Ruling, DA 06-1190, rel. June 2, 2006.

for guidance on the issues raised by the payphone providers.[4] Qwest is subject to a continuing state action in the State of Oregon where the Oregon Public Utility Commission recently asked this Commission to advise it of whether "the Waiver Order requires Qwest to refund a portion of the intrastate PAL rates paid by Payphone Service Providers (PSPs) since April 15, 1997, because those rates do not comply with the 'New Services Test' established in the Commission's *Payphone Orders*."[5] Finally, Qwest itself is the defendant/appellee in two federal appellate court proceedings in which the identical issues are raised.[6]

The positions taken by the payphone providers are utterly spurious, and are generally based on theories of the Communications Act and the Commission's payphone rules promulgated thereunder that are simply not accurate. As a basic proposition, Qwest has complied with the Commission's payphone rules, and has made modifications to its intrastate payphone tariffs as required by state regulatory commissions and, when appropriate, to ensure that its intrastate payphone rates were consistent with the Commission's most current guidelines. The concept that this pattern of universal compliance could give rise to federally ordered refunds of rates paid pursuant to lawful intrastate tariffs is simply not one that is sustainable. Whatever rights the payphone providers have or had to refunds from rates paid pursuant to intrastate tariffs are limited to their refund rights under state law. The Commission could not order refunds under federal law without having afforded carriers the protection guaranteed by statute as a prerequisite to ordering refunds.

While this action should not be necessary because the claims of the payphone providers are spurious, we request that the Commission terminate these proceedings with an order that clarifies that:

- Nothing in any of the Commission's rules regarding intrastate payphone rates was intended to supersede a state's authority over its own intrastate rate processes. Specifically, if a customer claimed that a carrier's intrastate PAL

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[4] *See, e.g.*, letter and attached Order of the Supreme Judicial Court for Suffolk County, Commonwealth of Massachusetts, DTE 97-88/97-18, *New England Public Communications Council, Inc. v. Department of Telecommunications and Energy and Verizon Communications of New England, Inc.*, both dated Mar. 6, 2006, as posted to the Commission's web site (in ECFS) in CC Docket No. 96-128 on Mar. 15, 2006; *see also generally*, Comments of New York State Department of Public Service, CC Docket No. 96-128, filed Jan. 24, 2005; Comments of the Florida Public Service Commission, CC Docket No. 96-128, filed Feb. 28, 2006; Comments of the Illinois Commerce Commission, CC Docket No. 96-128, filed Aug. 26, 2004; Comments of the Public Utilities Commission of Ohio, CC Docket No. 96-128, filed Dec. 10, 2004.

[5] Letter from Oregon Public Utility Commission to Chairman Kevin Martin, dated Nov. 23, 2005.

[6] *See TON Services v. Qwest Corp.*, No. 06-4052 (10th Cir., docketed Feb. 27, 2006); *Davel Communications, Inc. v. Qwest Corp.*, No. 04-35677 (9th Cir., docketed Aug. 6, 2004).

rates were inconsistent with either the state's requirements or the federally-imposed "new services" test, the only remedy for refunds or damages would be governed by state law. No federal cause of action for refunds was created.

- In requiring that states apply the "new services" test to intrastate PAL rates, the Commission was not prescribing intrastate PAL rates, but simply describing a methodology for rate-setting. Under the 2002 *Wisconsin Order* states retained considerable discretion to set or approve the appropriate rates, including the right to select a cost methodology.

- The Commission's *Wisconsin Order* was a rate order, and as such as a matter of law had prospective application only. The guidelines set forth in the *Wisconsin Order* were new limitations on state ratemaking authority under the "new services" test, and applied to state regulators on a prospective basis only. These guidelines did not supersede or invalidate past state actions approving intrastate PAL tariffs, nor did they require or permit states to conduct refund or reparations proceedings based on an inconsistency between past intrastate PAL rates and the prospective *Wisconsin Order*.

- The "refund commitment" made by the RBOCs on April 10, 1997, as cast into order form by the Common Carrier Bureau's ("Bureau") *April 15, 1997 Waiver Order*,[7] was intended to apply only to situations where an incumbent local exchange carrier ("ILEC") in a particular state did not have unbundled intrastate PAL tariffs in effect on April 15, 1997, and provided only that the new PAL rates that took effect after April 15, 1997, would be effective back to that date. It did not apply to tariffs that were already on file. Any waiver of rights by an ILEC derived from that *April 15, 1997 Waiver Order* did not apply to pre-existing tariffs.

- The argument that any ILEC "waived" its right to rely on state (or federal) filed tariff defenses and protections beyond the very limited terms of the *April 15, 1997 Waiver Order* (that is, between the date of the *April 15, 1997 Waiver Order* and the date of the effective date of the tariffs that permitted lawful certification) twists the *April 15, 1997 Waiver Order* beyond any semblance of legality or rationality. The waiver was a temporary agreement by RBOCs that they would make the post-April 15 – May 19 tariffs effective back to that date, not that they would permanently waive the filed tariff doctrine and the rule against retroactive ratemaking.

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[7] *In the Matter of Implementation of the Payphone Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, Order, 12 FCC Rcd 21370 (1997) ("*April 15, 1997 Waiver Order*").

- In the case of those ILECs, like Qwest, that were not covered by the *April 15, 1997 Waiver Order* because their tariffs were filed well before April of 1997 (and, in Qwest's case, because the relevant dumb PAL tariffs had actually taken effect prior to the issuance of the *April 15, 1997 Waiver Order*) the payphone providers' argument becomes incoherent because it simply has no applicability.

- In the case of Qwest and other ILECs whose certifications were subject to formal challenge before the Commission, the Commission's denial of these challenges is final and binding, and could not be retroactively reversed in the *Wisconsin Order* even if the Commission so intended.

I. BACKGROUND

Much of the support of the position of the payphone providers is predicated on a misunderstanding of Section 276 of the Act and, more especially, on what the Commission did in enforcing that section of the Act. Some background is necessary.

As part of its duty to enforce Section 276 of the 1996 Act, the Commission was charged with taking a number of actions with respect to the provision of payphone service, which gives the Commission jurisdiction over the services offered to payphone providers by RBOCs.[8] The Commission's rules ultimately required ILECs to file PAL tariffs at the state level, but directed that these tariffs conform to what is called generically the "new services" test for pricing purposes.[9] States were directed to apply this test in reviewing intrastate payphone tariffs. Qwest and other ILECs/RBOCs were required to maintain intrastate tariffs for unbundled PALs (both for "smart" lines with the intelligence in the switch and for "dumb" lines permitting the intelligence to be lodged in the set itself), to file new tariffs if those services were not already unbundled, and to ensure that these tariffs (existing or new) conformed to this test.

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[8] The Commission had originally asserted jurisdiction over PAL rates of all ILECs, but subsequently modified this decision in its *Wisconsin Order* to include only RBOC payphone services. This jurisdictional approach was affirmed by the D.C. Circuit Court of Appeals in *New England Public Communications Council, Inc. v. FCC*, 334 F.3d 69, 75-78 (D.C. Cir. 2003), *reh'g and reh'g en banc denied*, 2003 U.S. App. Lexis 19628, 19629 (Sept. 22, 2003), *cert. denied, N.C. Payphone Ass'n v. FCC,* 541 U.S. 1009 (2004).

[9] *In the Matter of Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, Order on Reconsideration, 11 FCC Rcd 21233 (1996) ("*Payphone Reconsideration Order*"). This requirement that the "new services" test apply to intrastate payphone rates was ultimately imposed only on BOCs. *Wisconsin Order*, 17 FCC Rcd at 2060-61 ¶ 31.

As originally applied to payphone line rates in 1996, the "new services" test was stated by the Commission as follows:

> LECs must file intrastate tariffs for these payphone services and any unbundled features they provide to their own payphone services. The tariffs for these LEC payphone services must be: (1) cost based; (2) consistent with the requirements of Section 276 with regard, for example to the removal of subsidies from exchange and exchange access services; and (3) nondiscriminatory. States must apply these requirements and the Computer III guidelines for tariffing such intrastate services.[10]

The "new services" test had been applied in the context of *Computer III*, in which pricing guidelines for new interstate Open Network Architecture ("ONA") services were examined by the Commission. In the ONA context, the "new services" test required a direct cost analysis and a "reasonable" allocation of overhead, and called on the Commission to examine ONA tariffs on an individual basis to determine if they were reasonable. No specific methodology was prescribed, other than the requirement that a consistent methodology be applied to all related services.[11]

In early 1997, ILECs were required to certify[12] that they had complied with the Commission's payphone rules in order to receive compensation from interexchange carriers ("IXCs") for their own (ILEC) payphone offerings. Tariffs implementing the "new services" test for PAL rates were to be effective on April 15, 1997 in order for the ILEC to be eligible for compensation. Noting that the industry was having difficulty complying with these deadlines, the Bureau issued a *sua sponte* waiver of certain aspects of the rules.[13] Significantly, the *April 15, 1997 Waiver Order* was more specific in specifying that the "new services" test, made explicit in reference to federal tariffs to be filed for payphone features, was applicable to intrastate payphone tariffs as well.[14] The waiver applied to ILECs filing PAL tariffs after April 4, 1997.[15]

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[10] *Payphone Reconsideration Order*, 11 FCC Rcd at 21308-09 ¶ 163. The "new services" test had been applied for a number of years in other contexts, but had governed only interstate services.

[11] *In the Matter of Amendments of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Subelements for Open Network Architecture, Policy and Rules Concerning Rates for Dominant Carriers*, Report and Order & Order on Further Reconsideration & Supplemental Notice of Proposed Rulemaking, 6 FCC Rcd 4524, 4531 ¶¶ 39-44 (1991).

[12] The certification was provided to other carriers, not directly to the Commission.

[13] *In the Matter of Implementation of the Payphone Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, Order, 12 FCC Rcd 20997 (1997) ("*Bureau's Waiver Order*").

[14] *See April 15, 1997 Waiver Order*, 12 FCC Rcd at 21378 ¶ 18.

The actual certification described in the Commission's *Orders* did not discuss the "new services" test. In relevant part, an ILEC was required to certify, as a precondition to obtaining payphone compensation for its own payphones (from IXCs) that: "(3) It has effective intrastate tariffs reflecting the removal of charges that recover the costs of payphones and any intrastate subsidies; . . . (5) It has in effect intrastate tariffs for basic payphone services (for "dumb" and "smart" payphones. . .)."[16]

A group known as the RBOC Payphone Coalition, of which Qwest was a member, immediately returned to the Bureau with a request for a further waiver, claiming that the earlier *Orders* had not specified that the "new services" test was applicable in these particulars to intrastate payphone rates for existing services. The RBOC Payphone Coalition requested this further waiver to permit its members to obtain payphone compensation while states examined their intrastate payphone tariffs in those cases where intrastate PAL tariffs had not been filed.[17] In its waiver petition, the RBOC Payphone Coalition indicated that its members were prepared to certify that their existing rates complied with the "new services" test and would file new tariffs in those states in which their rates did not comply. The RBOC Payphone Coalition requested payment of per-call compensation starting on April 15, 1997 and promised refunds for customers where the new rates were lower than the existing rates that ultimately took effect after April 15, 1997. The waiver petition applied only to new rates for "dumb" payphone lines filed under its terms.

By *Order* of April 15, 1997, the Bureau granted the waiver petition, and allowed ILECs to collect payphone compensation and file intrastate payphone line tariffs up to May 19, 1997, subject to a number of terms and conditions.[18] The Bureau treated the waiver petition as a concession by the RBOC Payphone Coalition members (including Qwest) that their intrastate tariffs were subject to the "new services" test and that the Commission's rules required that these tariffs be cost-supported according to the rules specified for that test. The waiver applied to tariffs filed after April 4, 1997. It did not apply to tariffs already in effect.

The Bureau made it clear that it did not expect that new tariff filings would be made in most states, and that the expectation was that the affected carriers would examine their tariffs and determine whether they complied with the various required certifications.[19] These certifications were to be filed with carriers, not with the Commission or state regulators.

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[15] *Id.* at 21379 ¶ 19.

[16] *Payphone Reconsideration Order*, 11 FCC Rcd at 21293-94 ¶ 131.

[17] Letter from Michael Kellogg to William F. Caton, April 10, 1997.

[18] *See April 15, 1997 Waiver Order*, 12 FCC Rcd 21370.

[19] *Id.* at 21380 ¶¶ 21-22.

Qwest distributed the requisite certifications that it was in compliance with the payphone rules, including the conformance of its tariffs to the "new services" test on May 20, 1997 and November 12, 1997. These certifications were self-effectuating in that the Commission did not need to approve or examine Qwest's payphone tariffs to affirmatively determine that they complied with the "new services" test. As noted, the certification included Qwest's tariffs for so-called "dumb" payphone lines that had been filed well prior to the *April 15, 1997 Waiver Order*.

Among other things, this certification stated:

> In addition, U S WEST certifies that it has effective intrastate payphone services tariffs which are cost-based, consistent with the requirements of Section 276, nondiscriminatory and consistent with Computer III guidelines. Pursuant to the Commission's limited waiver of the "new services" test granted in its Order of April 15, 1997 (DA 97-805), U S WEST has filed any rate changes required in the existing intrastate tariffs for unbundled functionalities to achieve compliance with the "new services" test.

MCI and several other carriers challenged Qwest's certifications by refusing to pay the proper per-call compensation that was dependent on these certifications. These challenges claimed that the certifications had been erroneous, and were denied by the Commission.[20] Qwest has been receiving compensation from IXCs for payphone services based on these certifications.

Qwest's PAL rates for intrastate "smart" payphone lines (that is, the lines used by Qwest's own payphone services) were filed on January 13 and 15, 1997. These rates were effective on or before April 15, 1997. However, these rates are not challenged by the payphone providers, because they do not purchase smart PALs. The rates challenged by the payphone providers had been in effect since prior to 1997. Qwest reviewed these rates and determined that they met the terms of the Commission's rules.

The Bureau's guidelines had also provided that state regulators who did not desire to conduct a "new services" analysis of an ILEC's intrastate payphone rates could refer the matter to the Commission for review. Only one state, Wisconsin, made such a referral, claiming that it did not have statutory authority to review intrastate services under the "new services" test. On March 2, 2000,[21] the Bureau issued an *Order* describing how the four ILECs filing PAL tariffs in Wisconsin would need to justify their rates in order to meet the "new services" test at the

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[20] Qwest's certification was challenged and upheld in a Bureau *Order* of November 9, 1999. *See Ameritech Illinois, U S WEST Communications, Inc., et al. v. MCI Telecommunications Corporation*, Memorandum Opinion and Order, 14 FCC Rcd 18643 (1999).

[21] *In the Matter of Wisconsin Public Service Commission, Order Directing Filings*, Order, 15 FCC Rcd 9978 (2000) ("*Bureau's Wisconsin Order*").

Commission. The requirements of this *Order*, were expressly limited to the specific proceeding before the Bureau, and were different than requirements applicable to states when they conducted their own proceedings:

- Cost study inputs and assumptions were required to be "consistent with the cost inputs used in computing rates for other services offered to competitors." "Costs must be determined by the use of an appropriate forward-looking, economic cost methodology that is consistent with the principles the Commission set forth in the Local Competition First Report and Order." The cost methodology specified in the *Bureau's Wisconsin Order* is Total Element Long Run Incremental Cost ("TELRIC").[22]

- Overhead allocations were required to be based on overhead allocations applied to "comparable services." The most comparable services located by the Bureau were unbundled network elements ("UNEs"), and the filing ILECs were required to "explain any overhead allocations for their payphone line services that represent a significant departure from overhead allocations approved for UNE services."

- Because the specified cost methodology was based on unseparated costs, the filing ILECs were required to "demonstrate that [their] payphone line rates [have] taken into account other sources of revenue (*e.g.*, SLC/EUCL, PICC, and CCL access charges) that are used to recover the costs of the facilities involved."[23]

The *Bureau's Wisconsin Order* "only applie[d] to the LECs in Wisconsin specifically identified herein."[24] The Bureau did not direct the Wisconsin LECs to file interstate tariffs for their payphone services. Instead, the Bureau directed those LECs to demonstrate that their intrastate tariffs complied with the Commission's "new services" test, and interpreted that test in detail.

Concerned that state regulators and courts would take the *Bureau's Wisconsin Order* as representing more than an individual order in a rate case, the RBOC Payphone Coalition filed both an application for review of the *Bureau's Wisconsin Order* by the full Commission and a motion for stay of that *Order*. Both documents were filed on April 3, 2000.

In the meantime, Qwest continued to interact with state regulators in filing and maintaining intrastate PAL rates via tariffs that conformed to the "new services" test as that concept was developed and analyzed by the various state regulators. Qwest filed modified intrastate tariffs

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[22] *Id.* at 9981 ¶ 9.

[23] *Id.* at 9982 ¶ 12.

[24] *Id.* ¶ 13.

for PAL services in four of its fourteen states between 1998 and when the Commission ultimately issued the *Wisconsin Order* in 2002.

On January 31, 2002, the Commission issued the *Wisconsin Order* affirming, in many particulars, the *Bureau's Wisconsin Order*.[25] This affirmance included some interpretations of the Bureau's earlier *Order* that are not consistent with the language of the Commission's *Order*. More significantly, the Commission used the opportunity of the *Wisconsin Order* to specify that the new guidelines adopted in that *Order* would from thence forth constitute direction to state regulators in the future application of the "new services" test to ILEC payphone rates.[26] The key components of the *Wisconsin Order* are:

- While the Commission affirmed its jurisdiction over the rates of Qwest's intrastate payphone access services, it ruled that this jurisdiction extended only to those services offered by RBOCs, not other ILECs.

- The Commission "clarified" that the Bureau's reference to TELRIC pricing was illustrative only, and a state could utilize "its accustomed TSLRIC methodology (or another forward-looking methodology)" to develop the direct costs of payphone line service costs."[27]

- The direct Total Service Long Run Incremental Costs ("TSLRIC") could, for example, include "those 'retail' costs, such as marketing and billing costs, that they can show are attributable to payphone line services."[28] These costs would be excluded from a TELRIC methodology.

- The approach to overhead loadings is more flexible than in the *April 15,1997 Waiver Order*, although the RBOC Payphone Coalition's insistence that there were few, if any limitations on overhead was rejected. The Commission stated that overhead should be reasonable and that the three preferred methodologies for overhead calculation were: 1) UNE rules; 2) physical collocation rules; or 3) the rules applicable to ONA services.[29]

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[25] *See Wisconsin Order*, 17 FCC Rcd 2051.

[26] The *Wisconsin Order* found that the Commission's jurisdiction did not extend to the intrastate PAL rates of non-RBOCs. We continue to use the term ILEC herein for the sake of consistency. However, it is clear that the rules apply only to ILECs that are controlled by RBOCs.

[27] *Id.* at 2066 ¶ 49.

[28] *Id.* at 2066-67 ¶ 50.

[29] *Id.* at 2072 ¶ 68.

- The Commission clarified that it expected that the filing ILEC would calculate a payphone rate under the "new services" test and then subtract the Subscriber Line Charge ("SLC") from that rate.

- Finally, the Commission declined to take any further action concerning the Wisconsin payphone tariffs themselves, simply "urging" the State of Wisconsin to reexamine its jurisdiction over intrastate payphone rates in light of the *Wisconsin Order*.

The *Wisconsin Order* was appealed by the RBOC Payphone Coalition to the D.C. Circuit. In briefing the appeal to the Court, the Commission objected to the ripeness of the appeal, and proclaimed that the *Wisconsin Order* did not actually set any rates or direct any rate reductions, but instead provided guidance for state regulators to follow whenever they undertook to examine the PAL rates of BOCs.

> In order to show injury, the BOCs would have to demonstrate that as a result of the *Order* on review they must charge less for payphone line service than they otherwise would have. At this point, with no change in the existing rate having been ordered, such a showing would appear impossible to make. "Indeed, the BOCs previously indicated to the Commission that their existing tariffs meet the new services test. . . . Nor can the Court presume an injury; the burden is on the petitioner to demonstrate one."[30]

That is, the Commission's characterization was accurate but not sufficient to affect the ripeness of the appeal.

The Court rejected the Commission's ripeness argument, but made it very clear that the directives in the *Wisconsin Order* were viewed as prospective only, potentially affecting BOCs only when they actually filed for a rate increase.

> The *Order's* forward-looking cost-based methodology means that the BOCs cannot recover certain expenses beyond the current costs of providing service -- namely, expenses owing to inefficiencies such as poor management or inflated capital and depreciation -- that they could recover under a historical-cost method. . . . To comply with the *Wisconsin Order*, the BOCs will almost certainly have to modify their tariffs to lower their existing rates -- or at the very least, refrain from raising their rates -- before submitting the tariffs for state review.[31]

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[30] *See* Brief of Respondent, filed Jan. 16, 2003 at 19 in *New England v. FCC*, 334 F.3d 69.

[31] *New England v. FCC*, 334 F.3d at 74.

On March 5, 2002, the Bureau issued a declaratory ruling following complaints by payphone providers in three states.[32] Petitioners challenged ILECs' intrastate payphone line rates in several states as being above cost and inconsistent with the "new services" test. The Bureau generally agreed with the petitioners and directed the state regulatory agencies involved to "re-evaluate their respective decisions concerning the pricing of BOCs' intrastate payphone line rates and overhead ratios to ensure compliance with the *Wisconsin Order*."[33]

As discussed above, there are three current requirements of the "new services" test as currently espoused by the Commission in the *Wisconsin Order*:

- Direct costs calculated on the basis of a long run incremental cost methodology.

- "Reasonable overhead" calculated on the basis of ONA, UNE or collocation methodologies (or similar methodologies). Originally, this requirement was for "reasonable overhead" only, and prior case law permitted overhead allocations of up to 400%. Overhead was first severely curtailed in the *Bureau's Wisconsin Order*, where it was stated that UNE overhead calculations were required. However, this approach was rejected in the Commission's *Wisconsin Order*, which allowed more flexibility in overhead calculations, even though it rejected the 400% overhead rate as unreasonable in all but the most unusual circumstances.

- Adjustment for interstate SLC. This adjustment was not discussed until the *Wisconsin Order*.

Qwest's initial methodology for certifying that its payphone rates were in compliance with the Commission's "new services" test in 1997[34] was as follows: Qwest calculated an unseparated TSLRIC cost for its payphone lines. It compared this cost to its existing payphone rates and, by dividing the cost by the price, derived an overhead percentage. Qwest then added the SLC into the total price and calculated a second overhead. If the overhead percentages were deemed to be within the realm of reasonableness as used by the Commission in its *Order* evaluating filings under the new services test, Qwest did not modify its prices. Modifications to Qwest's PAL

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[32] *In the Matter of North Carolina Payphone Association, Petition for Declaratory Ruling, Oklahoma Local Exchange Carrier Petition for Declaratory Ruling, Michigan Payphone Association Petition for Declaratory Ruling*, Order, 17 FCC Rcd 4275 (2002).

[33] *Id.* at 4276 ¶ 3.

[34] Qwest did not actually file new tariffs with cost support, etc., for PALs in 1997. Instead, Qwest, as was permissible, examined its PAL rates and determined that they complied with the Commission's guidelines.

rates were made over the next five years based on the requirements of state regulators as they further refined the tariffs.

After the adoption of the *Wisconsin Order*, Qwest reexamined its PAL tariffs. It determined, as part of an overall evaluation of intrastate ratemaking, including various state positions on proper calculations of long run incremental costs, to reduce its PAL rates in all states. These reductions were not based on a conclusion that Qwest's PAL rates were unreasonable, that they could not have withstood scrutiny under the *Wisconsin Order*, or that these were the only rates that would have satisfied the *Wisconsin Order.* These rate reductions went into effect between July 15, 2002 and December 17, 2003.

II. ANALYSIS

As a general matter, it is apparent from the foregoing that the payphone providers are trying to mangle the dual jurisdiction situation for PAL rates to seek to accomplish what could be done in no single jurisdiction. As far as we can determine (the payphone providers are often imprecise in defining just what they base their legal position on), the payphone providers' claims can be parsed as follows:

- ILECs were required to file intrastate tariffs for PALs that complied with the Commission's "new services" test by April 15, 1997.

- Some ILECs did not have such tariffs on file and were not able to meet this deadline.

- Accordingly, the Commission granted a temporary waiver to ILECs who did not meet this deadline, so long as their new tariffs would be retroactive back to April 15, 1997.

- As Qwest had already filed compliant tariffs, Qwest is not covered by the *April 15, 1997 Waiver Order*. But the *April 15, 1997 Waiver Order* applies to Qwest anyway.

- All ILECs were required to certify to IXCs that their payphone rates complied with the "new services" test.

- Qwest made such certification on May 20, 1997 and November 12, 1997 (the second filing necessitated by adding New Mexico for "smart" PAL rates only).

- The Commission issued a rate order (*Wisconsin Order*) in 2002 that directed ILECs and state commissions to modify some of their practices regarding the "new services" test and PAL tariffs.

- The 1997 certifications would not have complied with the 2002 rate order (*Wisconsin Order*) if they had been circulated in 2002 (at least so the payphone providers argued).

- Therefore, argue the payphone providers, the 1997 certifications were false, and that Qwest has agreed, because of the *April 15, 1997 Waiver Order*, that payphone providers have an open ended federal refund right if their 1997 tariffs did not conform to the 2002 rate order (*Wisconsin Order*).

This chain of logic by itself is self-evidently faulty. But the payphone providers' argument is even further undercut by other relevant facts:

- It is unquestioned that, if the tariffs in question had been filed at the Commission, not at the states, there would be no "refund" rights vesting in the payphone providers because: 1) they would be barred by the filed tariff doctrine; and 2) the Commission did not undertake the refund processes that are required by statute (*i.e.*, by Section 204 of the Act).

- It is also unquestioned, at least in thirteen of Qwest's states, that state-filed tariffs and retroactive ratemaking laws also bar the collection of refunds based on these facts.

- Qwest's certification was challenged and the challenge was denied by the Commission in 1999.

- Nevertheless, the payphone providers posit that a federal right of action to intrastate refunds based on a hypothetical recalculation of Qwest's PAL rates back to April 15, 1997 based on the 2002 *Wisconsin Order* and the phantom "waiver" of the filed tariff doctrine has magically accrued, overriding both the prevailing federal and state law that prevents such refunds.

Merely setting forth what the position of the payphone providers really is, is sufficient to damn the legitimacy of their arguments. The payphone providers seek to accomplish through a mushing of the rules of the two relevant jurisdictions (Commission and state) what could not be accomplished in either jurisdiction.

The bottom line is simple. Qwest's certifications in 1997 that it had filed PAL tariffs consistent with the "new services" test were accurate, and its tariffs were compliant with federal and state law. The 2002 *Wisconsin Order* was a ratemaking order, and as such was prospective-only as a matter of law. It had no impact on Qwest's or anyone else's intrastate PAL rates, other than to require carriers to examine their filed rates to determine if they should be modified in order to reflect, within the overall context of ratemaking, the principles set forth in the *Wisconsin Order*. Qwest was fully compliant with the law in this regard as well.

A. The Payphone Providers have no Federal Right to Refunds.

The payphone providers have no federal cause of action -- either at the Commission or in court. In addition, the *Wisconsin Order* is not a deviation from the normal principles that govern rate orders -- that is, that they are prospective-only.

It is important not to confuse the preemptive power that the Commission did exercise with the power that it did not exercise. The Commission could have required that PAL tariffs be filed at the Commission itself -- something that it, in fact, initially required.[35] In that case the Commission clearly would have had the authority to order refunds for rates that it reasonably concluded were unjust and unreasonable. But the Commission's refund authority in that event would have been bounded by the statutory limitations in the Communications Act.

In rate proceedings at the Commission, the general principle is that rate orders are prospective, not retroactive. It is a fundamental tenet of federal common carrier law that regulators are prohibited from engaging in what is called "retroactive ratemaking," setting prospective rates to account for past losses or excesses.[36] As the Supreme Court stated in *Arkansas Louisiana Gas Co. v. Hall*,[37]

> [N]ot only do the courts lack authority to impose a different rate than the one approved by the Commission, but the Commission itself has no power to alter a rate retroactively.

During the period for which Qwest's and other carriers' intrastate PAL rates are challenged (1997-2002), carriers filing federal tariffs were entitled to two critical protections before the Commission could order refunds. State versions of these protections were relied on in defending challenges to Qwest's intrastate tariffs. Because of the jurisdictional split that the Commission chose to rely on, neither of these protections would be available if the Commission were to accept the arguments of the payphone providers. The payphone providers seek to have this Commission supersede state protections against retroactive ratemaking without following the protections against that same regulatory abuse contained in the Communications Act.

The most significant protection that the Communications Act ensures carriers is the guarantee that no refund from a filed tariff will be ordered in the absence of a valid suspension and accounting order. This statutory protection is not only absolute, it is viewed as a vital protection

[35] *In the Matter of Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, Report and Order, 11 FCC Rcd 20541, 20615 ¶ 147 (1996) (subsequent history omitted).

[36] *See City of Picqua v. FCC*, 610 F.2d 950, 955 (D.C. Cir. 1979).

[37] *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 578 (1981).

for carriers in that they are advised early on in the rate process of the fact that their newly-filed rates may be in jeopardy. As the D.C. Court of Appeals found in *Illinois Bell Telephone Company v. FCC*:[38]

> Thus, under the plainest guide to congressional intent - the words of the statute - the Commission's authority to order the refund follows the exercise of the suspension process under § 204(a)(1).

The Court was equally clear as to the reason for this critical precondition to refunds:

> The statute provides not only for the suspension but also that the statement suspending a rate inform the carrier in writing of the Commission's reasons for the suspension. Having been given this notice, the carrier may realize that the FCC's objections are well taken, or not worth a fight, and it may seek to bring itself within compliance and obviate the whole process. The statute does not impose a rule without a reason.[39]

The Court approved and enforced exactly the same regulatory requirements as recently as Monday, June 20, 2006.[40]

Had the Commission chosen to adopt a regulatory structure that reserved refund rights to the Commission, it could have done so. But it could not have done so without including in it the suspension and accounting order protections that are a critical part of that refund authority.

What is more, during the relevant period, the statutory prerequisite that a suspension precede a refund took on even greater importance. A carrier filing a tariff on fifteen-days notice is entitled to have that tariff "deemed lawful" unless the Commission suspends it within the statutory

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[38] *Illinois Bell v. FCC,* 966 F.2d 1478, 1481 (D.C. Cir. 1992).

[39] *Id.* at 1482. The Court relied heavily on the landmark case of *Sea Robin Pipeline Co. v. FERC*, 795 F.2d 182 (D.C. Cir. 1986).

[40] *Verizon Telephone Companies v. FCC,* No. 04-1331 (D.C. Cir. June 20, 2006), in which the Court held:

> If the Commission 'fails to order a suspension,' that failure 'does not mean that the Commission cannot take action to correct an unreasonable rate.' [citing to *Illinois Bell]* In 'Section 205, Congress provided the mechanism for prospective relief from unreasonable rates.' . . . In '[Section] 204,' however, 'it provided the mechanism for preventing an unreasonable rate from being filed, or at least from taking effect only subject to an accounting order and such further order as would be required. The one supposes prospective relief, the other the possibility of refund.' Slip Op. at 18.

period. Qwest customarily files its interstate tariffs under this section of the Act wherever possible. Under this statutory structure, Qwest could have filed interstate payphone tariffs and these tariffs would have been the lawful rate for all purposes unless suspended by the Commission.[41] The Commission, of course, chose not to require federal tariffs (except for some features which are not at issue here), and relegated the tariff process to state regulators.

Fundamentally, had the Commission chosen to reserve refund power in itself, it would have been required to exercise such power lawfully. A basic prerequisite of such lawful exercise of federal refund authority would have included affording carriers the protections mandated by Section 204(a) of the Act. Having chosen to delegate the tariff review process to the states, it also delegated to states the power to order refunds based upon federal standards (including the "new services" test), but only subject to the companion protections that states offer under their own rules concerning refunds, filed tariffs, suspensions and retroactive ratemaking.

To be plain, we are not suggesting that the Commission established a scheme in which its orders could go unheeded. To the contrary, if Qwest filed or maintained a PAL rate that was inconsistent with the Commission's "new services" test, payphone providers had full opportunity to challenge those rates under state processes, and courts have not proven unwilling to insist that state regulators follow the Commission's rules when examining state PAL tariffs.[42] Nor are we claiming that the Commission's rules are not binding on the states -- although, as noted, the *Wisconsin Order* is a ratemaking order and as such is prospective-only as a matter of law. The Commission's ability to interpret, modify and reinterpret its rules is well settled and tested. Nor, obviously, do we contest the Commission's ability to federalize the entire PAL rate tariff process and subject it to the rigors of Section 204 of the Act. Our position is much simpler. Having delegated the responsibility for examining and approving intrastate PAL tariffs to state regulators, the Commission also necessarily relied on those state processes for the protections against retroactive ratemaking that states had enacted that would have been available had the Commission instead federalized the entire process. The Commission cannot lawfully abrogate the refund protections of Section 204 by delegating the tariff processes to state regulators without at the same time leaving in place companion protections enacted by state legislators and regulators.

B. The Payphone Providers' "Waiver" Argument is Frivolous.

It is also necessary to spend some time on the specific question asked by the Oregon Public Utility Commission, because it appears that that the "waiver" issue has now become the central

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[41] *See Virgin Islands Telephone Corporation v. FCC*, 444 F.3d 666 (D.C. Cir. 2006) for a discussion of the importance of the issuance of a suspension order in the process of evaluating possible refunds in a situation where refunds could otherwise lawfully have been made.

[42] *See Northwest Public Communications Council v. Public Utility Commission of Oregon*, 100 P.3d 776 (Or. Ct. App. Nov. 10, 2004).

focus of their position. The Oregon Commission stated in its November 23, 2005 letter to the Commission:

> We are writing to request prompt Commission action in CC Docket 96-128, the Consolidation Petition proceeding. Commission action in the docket would allow states, including Oregon, to determine whether incumbent local exchange carriers are bound by the refund provisions of Commission Order DA 97-805 (the *Waiver Order*).

The theory is that the *April 15, 1997 Waiver Order* created a perpetual waiver of the filed rate doctrine for intrastate PAL rates, permitting "refunds" (as a matter of federal right) when federal and state law would otherwise prohibit refunds. There are multiple reasons why the argument that ILECs did not "waive" their filed tariff defenses to refund claims in response to the *April 15, 1997 Waiver Order* must fail.

- In Qwest's case, whatever it said, the *April 15, 1997 Waiver Order* did not apply to Qwest. Qwest's "dumb" PAL rates were not even filed in 1997, and the *April 15, 1997 Waiver Order* applied only to tariffs filed between April 4, 1997 and May 19, 1997. The "smart" PAL rates that were filed in January of 1997 applied to Qwest's own payphones, and were typically not used by the members of the payphone providers. The terms of the *April 15, 1997 Waiver Order* simply do not apply to Qwest, no matter what those terms may be.

- Also in Qwest's case, the certification of compliance released by Qwest that it was in compliance with the "new services" test was challenged before the Commission, and this challenge was denied by the Commission.

- More importantly, it is very clear that any commitment made in compliance with the *April 15, 1997 Waiver Order* extended only to refunds based on tariffs filed in 1997 (*i.e.*, within 45 days of April 15, 1997), and only to the differential between the rates paid under earlier tariffs and the rates that would have been paid under the tariffs that the ILECs certified as compliant with the *April 15, 1997 Waiver Order*. There is no reasonable reading of the *April 15, 1997 Waiver Order* that would provide a blanket waiver of the filed tariff doctrine and the rules against retroactive ratemaking extending to the indefinite future. That was clearly not the intent of the RBOCs' offer to have their post-April 15, 1997 tariff filings effective on April 15. The waiver actually accepted by the ILECs was very limited, and the payphone providers' efforts to turn it into a monstrosity are clearly contrary to the plain language of the waivers themselves (even for those ILECs that relied on the *April 15, 1997 Waiver Order*).

- The latest cut-off date for the waiver period would be issuance of the certification of compliance by the ILECs.

- The bottom line of the payphone providers' argument -- that ILECs falsely certified in 1997 that they were in compliance with the 2002 *Wisconsin Order* is simply not supportable under any theory.

The arguments advanced by the payphone providers in support of a federal refund right based on intrastate tariffs between 1997 and 2002 are patently frivolous. Nevertheless, given the persistence of the payphone providers, it is necessary that the Commission resolve this matter definitively.

C. The Payphone Providers have not Shown a Right to Refunds Even if the Commission was Authorized to Order Them.

Finally it is necessary to observe that the payphone providers have decidedly not shown that they would be entitled to a refund even if the Commission had the power to grant them one. In the event of a challenge, the payphone providers would have the burden of proving that Qwest's rates between 1997 and 2002 were in fact unjust and unreasonable. Qwest would obviously defend, offering proof of reasonableness in addition to the customary equitable carrier defenses against refund requirements.[43] Presumably, the Commission would not attempt to apply the *Wisconsin Order* retroactively, but, even if it did, there is tremendous flexibility in the *Wisconsin Order* itself, especially in the choice of a costing methodology, that would permit multiple defenses to a tariff challenge.

The point is, the rules regarding retroactive ratemaking outlined in Subsection A above were designed to prevent occurrences of the types of proceedings that would be necessary if the Commission were to undertake to adjudicate the lawfulness of ILEC PAL rates from 1997 – 2002. Congress clearly recognized the impropriety of such an undertaking. The Commission should make such recognition explicit too.

III. CONCLUSION

Qwest requests that the Commission issue an order as outlined above.

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[43] *See Virgin Islands Telephone Corporation v. FCC*, 989 F.2d 1231, 1240 (D.C. Cir. 1993).