BEFORE THE

Federal Communications Commission

WASHINGTON, D.C.

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

COMMENTS OF TIME WARNER TELECOM INC., CBEYOND, INC. AND XSPEDIUS COMMUNICATIONS, LLC

WILLKIE FARR & GALLAGHER LLP
1875 K Street, N.W.
Washington, D.C. 20006
(202) 303-1000

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Time Warner Telecom Inc. ("TWTC"), Cbeyond, Inc. ("Cbeyond"), and Xspedius Communications, LLC ("Xspedius") (collectively, the "Joint Commenters"), by their attorneys, hereby submit these comments in response to the public notice seeking comment on the Missoula Plan.[1]

I. Introduction and Summary

In assessing the optimal approach to intercarrier compensation reform, the Commission must weigh the costs and benefits of the possible approaches. If undertaken pragmatically and honestly, such an assessment yields the conclusion that a central component of reform must be the requirement that, to the extent possible, each carrier charge a single, cost-based rate for the exchange of all types of traffic. Any plan should eliminate arbitrage opportunities, minimize unnecessary increases to the universal service fund, and treat CLECs, ILECs and wireless

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[1] *See* Missoula Intercarrier Compensation Reform Plan ("Missoula Plan" or "Plan") attached to Letter from Tony Clark, Commissioner and Chair, NARUC Committee on Telecommunications, Ray Baum, Commissioner and Chair, NARUC Task Force, and Larry Landis, Commissioner and Vice-Chair, NARUC Task Force to Marlene H Dortch, Secretary, FCC, CC Dkt. No. 01-92 (filed Jul. 24, 2006).

carriers in the same manner to the extent possible. Issues unrelated to intercarrier compensation reform are properly dealt with in other contexts.

The Missoula Plan fails on many if not all of these counts, and should therefore be rejected, not only as a solution in itself, but also as a foundation for ongoing intercarrier compensation reform discussions. The rate provisions of the Plan favor especially ILECs and Rural LECs ("RLECs") over wireless carriers and CLECs and are unnecessarily complex. The Plan sets widely varying rates for the termination of traffic among ILECs depending on their size, location, and, in many cases, the jurisdiction of traffic, while CLECs are subject to the lowest rate regardless of their size, location or the traffic at issue. A far superior approach would be to require that all terminating rates be set at TELRIC-based rates. Moreover, the Plan includes an incoherent provision that ILECs should be able to determine whether CLECs charge for originating access. This is obviously flawed and should be rejected (indeed, the reverse approach where CLECs determine rates for ILECs would never be accepted). Finally, the Plan's proposal with respect to tandem transit rates would permit ILECs to charge high and, in many cases, unregulated rates for what the FCC has determined is a monopoly service.

The Plan makes changes to and increases funding for existing universal service support mechanisms and creates two huge new funds (the Restructure Mechanism and Early Adopter Fund) while likely leaving CLECs and wireless carriers unable to receive compensation from these new sources of funding. These new funds are poorly designed, would raise the USF contribution factor to untenably high levels, and would actually guarantee ILECs additional funding beyond what they would lose from intercarrier payments. Crucially, neither fund conditions the receipt of monies on states rebalancing their residential retail rates to reasonable benchmark levels. In the absence of such rebalancing, it is difficult or impossible for CLECs to compete in states and areas of states with below-cost residential retail rates.

The Plan's treatment of end-user charges also creates serious problems. Specifically, to make ILECs whole and "mitigate" an even larger increase in universal service funding, the Plan permits substantial SLC pricing flexibility which would only encourage ILEC discrimination. The Plan permits ILECs to target those product and geographic markets with little competition for large SLC price increases while reducing SLC rates in those markets with more extensive competition.

Finally, the Plan's proposal for changes to interconnection architecture is an already rejected solution in search of a problem since the current interconnection scheme is working efficiently. The proposed changes, previously put forth by the ICF and rejected by most carriers, would permit ILECs to choose a "financial" point of interconnection ("POI") separate and apart from the actual physical POI. Among other problems, this proposal would increase costs for CLECs (especially with respect to interconnection with rural carriers) and would require the re-writing of nearly every interconnection agreement. This wrongheaded proposal has nothing to do with intercarrier compensation reform, and should therefore again be rejected. For the same reason, the FCC should reject proposals to increase certain carriers special access pricing flexibility.

II. The Rates Proposed In The Missoula Plan Are Inefficient.

The manner in which the Missoula Plan proposes to set rate levels is fraught with problems. The Plan's rate scheme is absurdly complex, fails to ensure that each carrier charges the same rate for terminating all types of traffic, offers no basis in cost for its proposed rates, and introduces numerous other inefficiencies.

First, the schema in the Plan is extremely complex. The level of complexity by itself introduces costs. As the Commission pointed out in its *2001 Notice*, "it is appropriate to consider the degree of regulatory intervention required to implement various interconnection regimes…Market-oriented solutions may provide more timely adjustments and avoid distortions resulting from incorrect or outdated regulatory decisions. They may also avoid substantial litigation costs."[2] The complexity of the various rates and tracks established by the Missoula Plan will require substantial regulatory oversight, which bodes a slow-paced reform with benefits that may never be realized given the rapid shifts of the industry. Moreover, any savings that may be achieved by the Plan may be offset by increased costs in litigation and administration, as suggested by the Commission in its *2001 Notice*. *See id.*

Second, the Missoula Plan fails to achieve the most fundamental objective of intercarrier compensation reform by continuing to allow the same LEC to charge different rates for terminating different types of traffic. For example, if the terminating intrastate access charges for a Track 3 carrier are lower than its terminating interstate access charge, the carrier may continue to charge the higher interstate terminating rate for interstate traffic. *See* Missoula Plan at 18. In addition, Track 3 carriers may continue to charge existing reciprocal compensation rates under the Plan if those rates are lower than the current interstate terminating access charge rates. *See id.* Finally, Track 3 carriers that had been subject to a state-determined reciprocal compensation rate of "zero" may begin charging reciprocal compensation rates at levels that are not necessarily equal either to intrastate or interstate terminating access rates. *See id.* The result is that Track 3 carriers are apparently free in certain (possibly many) circumstances to charge

[2] *Developing a Unified Intercarrier Compensation Regime*, Notice of Proposed Rulemaking, 16 FCC Rcd 9610, ¶ 34 (2001) ("*2001 Notice*").

three different rates (*i.e*. interstate access, intrastate access, and reciprocal compensation) for the same terminating function depending on the jurisdiction of the traffic. This is exactly the situation that intercarrier compensation reform should *prevent*.

Third, the rates prescribed in the Plan are not cost-based. The Plan does not discuss a pricing methodology or the components on which the rates are based and the $0.0005 target rate for Track 1 carriers is well below any measure of cost yielded by regulatory commission proceedings. This is all the more troubling since TELRIC offers an established and well-understood methodology for setting cost-based rates. TELRIC accounts for the additional costs incurred by each increment of use, and it therefore produces rates that closely approximate the cost of providing the origination and termination services. In an industry characterized by a large proportion of fixed costs, the only practical way to set prices is by using long run or "average" costs. This was the premise upon which the Commission established TELRIC. Indeed, even competitors that pay TELRIC-based prices have conceded that a forward-looking pricing methodology must use long run, or average, costs.[3] Moreover, while ISP-bound traffic is not set at TELRIC-based rates today, there would be little harm in doing so in the future since dial-up traffic will be virtually non-existent in several years. All of this suggests that unified terminating rates based on TELRIC are optimal.

Furthermore, it makes sense to apply a single cost methodology, to the extent the applicable law permits, to the origination and termination of all traffic. Indeed, when setting the rates for UNE switching, the Commission established only one rate for UNE switching regardless of the nature of the traffic that passed through that switch. The Commission also

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[3] *See* Affidavit of William J. Baumol, Janusz A. Ordover, and Robert D. Willig, attached as Appendix B to AT&T Comments, ¶ 3, CC Dkt. No. 96-98 (filed May 20, 1996).

noted that there is no distinction between the cost of terminating reciprocal compensation or ISP-bound traffic.[4] In other words, switching is switching and like services should be subject to the same rates. Shearing away from this principle will only create new incentives for inefficient arbitrage.

Fourth, the differences in the rates proposed in the Plan reflect what is apparently an arbitrary bias in favor of rural carriers, *i.e.* the Track 2 and 3 carriers. Because the Plan sets rates for Track 2 and 3 carriers at levels well above those for Track 1 carriers, CLECs (which count as Track 1 carriers) would be required to pay more under the Plan to terminate local traffic to rural ILEC customers than rural ILECs would pay for terminating traffic *in the same area* to CLEC customers. Moreover, IXCs would pay more to rural ILECs to terminate long distance traffic than they would pay CLECs in the same location to perform the same function. *See* Missoula Plan at 7 *et seq*. This approach will obviously harm competition in rural areas in direct contradiction with the goals of the 1996 Act.

Fifth, the treatment of originating access under the Plan creates significant additional distortions. For example, the Plan impermissibly leaves the determination of whether CLECs may charge originating access to the Track 1 *ILECs* serving the same area. *See id.* at 10. There is no basis for leaving this decision to ILECs. Indeed, it is a fundamentally sound principle that any LEC should be free to charge IXCs that seek to use the LEC's network to originate calls. Nor would allowing CLECs to charge for originating access have a particularly meaningful effect on the market. Originating access does not implicate the "terminating monopoly" problem

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[4] *See Implementation of the Local Competition Provisions in the Telecommunications Act of 1996 et al.*, Order on Remand and Report and Order, 16 FCC Rcd 9151, ¶ 92 (2001) ("Nor does the record demonstrate that CLECs and ILECs incur different costs in delivering traffic that would justify disparate treatment of ISP-bound traffic and local voice traffic under section 251(b)(5).").

associated with terminating access since customers can choose their originating carriers. Moreover, as customers increasingly purchase long distance and local services from the same carrier and as the BOCs have received Section 271 approval in just about every state in the country,[5] originating access is a less and less significant component of the overall intercarrier compensation regime. There is therefore no reason not to permit all LECs to recover the costs of originating access if they think it is appropriate to do so. That choice should of course be made by each carrier for itself and no carrier should be able to make it on behalf of other carriers. Moreover, if an ILEC decides not to charge originating access, it should not be permitted to recover any resulting shortfall in intercarrier revenues from the Restructure Mechanism.

Finally, the treatment of tandem transit rates is fatally flawed under the Plan. As the Commission acknowledged in its *2005 Further Notice*, ILECs have market power in the provision of transit service and transit service is increasingly important to competitive carriers.[6] It is necessary therefore to tightly regulate ILEC tandem service rates so that ILECs do not have the opportunity to use them as a means of raising rivals' costs.[7] Indeed, AT&T has implicitly

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[5] *See* FCC, "RBOC Applications to Provide In-region, InterLATA Services Under § 271," *at* http://www.fcc.gov/Bureaus/Common_Carrier/in-region_applications/ (last visited Oct. 24, 2006).

[6] *See Developing a Unified Intercarrier Compensation Regime*, Further Notice of Proposed Rulemaking, 20 FCC Rcd 4685, ¶ 125 (2005) ("*2005 Further Notice*") ("The record suggests that the availability of transit service is increasingly critical to establishing indirect interconnection – a form of interconnection explicitly recognized and supported by the Act…Without the continued availability of transit service, carriers that are indirectly interconnected may have no efficient means by which to route traffic between their respective networks.").

[7] *See* TWTC *et al.* Comments, at 45-46 (filed May 23, 2005).

conceded this point by agreeing to cap its tandem transit rates in proposed conditions for the AT&T-BellSouth merger.[8]

Despite the ILECs' clear market power, the Missoula Plan grants a considerable amount of discretion to ILECs in setting transit rates. The Plan allows tandem transit rates to be determined "commercially," limited only by a high cap of $0.0025 per minute which increases with inflation after four years. *See* Missoula Plan at 51. The Missoula Plan does not subject ILECs to the negotiation and arbitration obligations for tandem transit commercial agreements, essentially calling a free-for-all on tandem transit rates. None of these provisions are appropriate in light of the ILECs' established market power over transit services.

III. The Subsidy And Cost Recovery Mechanisms In The Plan Would Introduce New Inefficiencies.

There are numerous problems with the subsidy and recovery mechanisms proposed in the Missoula Plan. *First*, and most fundamentally, the recovery mechanisms are simply too large. As consumer groups have explained, the recovery mechanisms in the Plan set the "make whole" transfer payments at a higher level than the projected revenue shortfall due to reductions in intercarrier payments. According to the Plan's own estimates, end-users will pay *more* ($6.9 billion)[9] in increased SLCs and subsidy payments after the Plan than would be achieved through intercarrier payment reductions ($6 billion). *See* Missoula Plan at 100. In essence, then, the Plan serves as a wealth transfer from end-users, CLECs and wireless carriers to ILECs. This is bad

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[8] *See* Letter from Peter J. Schildkraut, Counsel for AT&T Corp., to Marlene H. Dortch, Secretary, FCC, Attachment at 5, WC Dkt. No. 06-74 (filed Oct. 13, 2006).

[9] The Plan predicts a $4.7 billion increase in SLCs (*see* Missoula Plan at 100), $1.5 billion for the new Restructure Mechanism (*see* Missoula Plan Introduction at 13), $.2 billion for the new Early Adopter Fund (*see id.* n. 12), a $.3 billon increase in the High Cost fund (*see id),* and a $.2 billion increase in the Low Income Fund (*see id*.).

policy, and indeed, the Plan's proponents have not, and could not, justify such an outcome. Whatever the merits of making smaller and rural carriers whole through the new, pseudo-USF funds created to by the Plan, they do not apply to largest ILECs, including Verizon, BellSouth, AT&T and Qwest. These carriers are hugely profitable and do not need subsidies when intercarrier payments are modestly reduced. Moreover, there is no guarantee that the savings from reduced intercarrier payments will be passed through to consumers in the form of lower prices.

More significantly, most ILECs and especially the RBOCs[10] have already begun investing in new packet-based services that will, through the natural operation of the market, reduce the pool of available access charge revenues over time. For example, BellSouth has planned a fiber upgrade to its network that will reach 75 percent of BellSouth's households by the end of 2009. [11] AT&T has announced the availability of broadband services via fiber, satellite, WiMax, and other fixed wireless services via its so-called Project Lightspeed. AT&T also plans to deploy 40,000 miles of new fiber with the goal of bringing fiber-based services to 19 million households by the end of 2008.[12] Verizon's Fios service is expected to reach 6

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[10] Smaller rural ILECs have also begun deploying fiber. *See Annual Assessment of the Status of Video Competition in the Market for the Delivery of Video Programming,* Twelfth Annual Report, 21 FCC 362, ¶¶ 125, 204 (2006) (describing the commitment to deploying video services over fiber of smaller ILECs, *e.g.*, Cincinnati Bell, CenturyTel, Citizens Telephone Company, SureWest, the Rural Telephone Service Company, Hawaiian Telecom, and Cavalier Telephone).

[11] BellSouth Corp., Annual Report, at 17 (Form 10-K) (Feb. 28, 2006).

[12] *See* Press Release, AT&T Corp., AT&T Initiatives Expand Availability of Advanced Communications Technologies (May 6, 2006) *at* http://att.sbc.com/gen/press-room?pid=4800&cdvn=news&newsarticleid=22272.

million households by the end of 2006, covering 20 percent of the ILEC's residential customer base.[13]

And these RBOCs are already realizing substantial profits from these investments, easily compensating for any loss in access payments that they may face. According to AT&T, the revenue derived from the ILECs' advanced services more than doubles the revenue from switched access services. As AT&T stated in its Annual Report, "[w]e have found that when customers add broadband to a basic package, they are 40 percent less likely to switch to another provider, and average revenue per customer jumps nearly 120 percent."[14] It would make little sense for the ratepayers to subsidize the ILECs' already profitable business decisions.

Overall, the Plan constitutes a 32 percent increase in USF and USF-type funding from $7 billion per year to over $9 billion leading to a concomitant increase in the USF contribution factor.[15] Such a high contribution level may approach the point at which the USF charges imposed upon end-users actually threaten the goal of universal service. As the Fifth Circuit has explained, "excessive funding may itself violate the sufficiency requirements of the Act." This is because "universal service is funded by a general pool subsidized by all telecommunications providers -- and thus indirectly by customers -- excess subsidization in some cases may detract from universal service by causing rates unnecessarily to rise, thereby pricing some consumers out of the market."[16]

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[13] *See* Verizon Communications, Inc., Annual Report, at 7 (Form 10-K) (Mar. 14, 2006).

[14] AT&T, Inc., Annual Report (Form 10-K) at 10 (Mar. 1, 2006).

[15] Edwin Rosenberg *et al.*, *Commission Briefing Paper, Intercarrier Compensation and the Missoula Plan*, The National Regulatory Research Institute at 76 (October 2006).

[16] *Alenco Communications Inc. v. FCC*, 201 F.3d 608, 620 (5th Cir. 2001).

Proponents of the Plan are likely to argue that the recovery mechanisms are not too large since the Plan reduces Restructure Mechanism payments in proportion to any line loss experienced by the ILEC during the duration of the Plan. While it is true that the Plan takes into account the loss of access lines for Track 1 carriers,[17] it does *not* take into account the substantial effect of wireless substitution,[18] the ILECs' increasing sale of bundled local and long distance products and the winding-down of a stand-alone long distance market on the average access revenue that ILECs will receive on each remaining line.

The amount of money lost by ILECs through reductions in access charges not recovered through SLC increases and which may be obtained through the Restructure Mechanism is called the "access shift." At the beginning of the Plan, a Track 1 carrier determines the "access shift per line" (the amount of money that may be recovered per line) by dividing the total estimated access shift by the number of lines served by the carrier at *the beginning of the Plan*. Regardless of any decreases in revenue per line over the period of the Plan, "A Track 1 carrier's Access Shift Per Line will remain the same for the life of the Plan." Missoula Plan at 65. In other words, under the Plan, if an ILEC loses 10 percent of its lines over the life of the Plan, its receipts from the Restructure Fund also decrease by 10 percent. However, the fact that the remaining 90 percent of the carrier's lines will produce lower revenue per line at the end of the Plan than at the beginning of the Plan will have *no effect* on the amount of subsidy received by the ILEC. The recovery mechanism therefore overcompensates the ILEC recipients. This will distort the

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[17] *See* Missoula Plan at 68. The Plan provides, without adequate justification, that certain Track 2 carriers will not lose the revenue associated with their lines until Step 4. *See id.* at 73.

[18] The FCC has found that many customers are using their wireless phones for long distance service in lieu wireline-based long distance services. *See Verizon Communications Inc. and MCI, Inc. Applications for Approval of Transfer of Control*, Memorandum Opinion and Order, 20 FCC Rcd 18433, ¶ 93-95 (2005). Indeed, the FCC noted a report showing that over 60 percent of long distance calls are now made over wireless phones. *See id.* n. 288.

ILECs' incentives to innovate and provide lower-priced services, and they will target their business strategy towards merely retaining access lines. More fundamentally, such compensation is yet another wealth transfer from competitors to ILECs.

It is especially egregious that ILECs face no reduction in the per-line support payment because much of the revenue loss per line is the result of increased wireless long distance usage. This increase in wireless usage is largely the result of the *RBOCs' own wireless subsidiaries.* In this sense, RBOCs will be able to achieve double recovery--once through the Restructure Mechanism and once through increased wireless revenue.

Second, the design of the Restructure Mechanism appears not to comply with the sound principle that subsidy funds should be portable. Accordingly, the Plan can be read to require that CLECs contribute to a fund to make ILECs whole while CLECs themselves are not able to draw from the fund. This is especially incoherent where a competitor offers service in the same area as an ILEC that may draw from the fund. In this situation, the competitor likely incurs the same costs as the ILEC and therefore should be able to receive funding from the same sources as the ILEC with which it is competing.

Third, neither the Early Adopter Fund nor the Restructure Mechanism provide any incentive for states to rebalance ILECs' residential retail rates to reasonable levels. If either fund were established, it would make more sense to make these funds available only to carriers and states with respect to those states that already have or agree to rebalance their residential retail rates.[19] Indeed, in the absence of local rate rebalancing, in those states and areas of states where

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[19] The Plan introduction does note that "The Missoula Plan supporters are committing resources to work with State Commissioners to help size the Early Adopter Fund and to determine how that Fund should work when States have rebalanced access rates through State funds, local rate increases, and/or new line items." *See id.* n. 27. Nevertheless, rebalancing of rates is not a requirement to receive monies from the Early Adopter Fund, nor is it a stated purpose of the

local rates are set well below cost, CLECs providing residential services and wireless carriers are put at a substantial disadvantage with respect to the incumbent if they cannot obtain access to universal service funding. In such a scenario, CLECs are placed in the untenable situation of either meeting the ILEC's rates and not recovering their costs or charging the market-based rate for service and never obtaining any customers. Moreover, rate rebalancing should be accomplished through benchmarking, where carriers would only receive funds to offset their loss of interstate and intrastate access if local rates are at or near a particular benchmark rate. Similar schemes have been proposed in extensive detail in the prior round of comments in this docket.[20] Such an approach would both level the playing field among all carriers and reduce the need for large, additional subsidy funds.

IV. The Plan Leaves ILECs Free To Recover Reductions In Intercarrier Compensation In A Manner That Would Harm Competition In The Business Market

The manner in which the drafters of the Missoula Plan have structured SLC rates raises substantial potential for ILEC abuse. While it is true that carriers should be permitted to cover their costs to the extent possible directly from end-users, appropriate constraints must be placed on the manner in which ILECs can recover these costs. The Plan does not include such

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Fund. *See id.* at 74. States may receive money simply if they certify that the money is being used to compensate "carriers for access rate reductions made prior to the Plan's adoption." *See id.*

[20] For example, the Alliance for Rational Intercarrier Compensation (ARIC) proposed setting a local rate benchmark range based around the "national average urban-single line local residential rate" which, at the time of the Plan's submission, was $14.61. *See* Intercarrier Compensation Reform Plan of the Alliance for Rational Intercarrier Compensation at 64, WC Dkt. No. 01-92 (filed Oct. 25, 2004). To the extent that increased end-user rates did not fall within the benchmark, they were unable to obtain a subsidy under ARIC's Plan. *See id.* at 73-74. The Joint Commenters do not endorse any part of ARIC's Plan, but merely note that ARIC attempted to tie access to subsidy funding to rate rebalancing, while the Missoula Plan does not even attempt to do so.

constraints. Accordingly, if the Plan were enacted as is, ILECs would have the ability to charge unreasonably high rates to some customers and to engage in strategic pricing to exclude entrants seeking to serve other customers. The Commission must not allow the incumbents to recover intercarrier compensation revenue currently associated with one product or geographic market from another product or geographic market.

Unfortunately, the manner in which the Missoula Plan structures its SLC charges violates these principles and should be rejected. *First*, the SLC geographic de-averaging permitted at the outset of the Plan will permit substantial abuse. The Plan permits SLCs to be de-averaged into four "pricing zones" in each state. *See* Missoula Plan at 24. This will permit ILECs to levy higher SLCs in non-competitive areas, subject to the cap,(generally rural areas) while lowering SLCs in more competitive areas (generally urban areas) to meet competition. Moreover, in the absence of any competitive showing, this restriction will be lifted at Step 4 (*see id.* at 25), permitting complete geographic de-averaging and inviting substantial abuse,.

Second, the Plan permits the ILECs to divide their product markets into so many fine categories and apply individual SLCs to each category, that any product market restrictions on pricing flexibility become meaningless. For example, without defining the term, the Plan permits de-averaging based on "customer class." *See id.* 24. This ambiguous term could lead to any number of undesirable outcomes. The ILEC could define a "customer class" as those living outside of major urban centers who order only single residential lines. Such customers are likely to face little competition and the ILEC could charge these customers a higher SLC. The Plan also permits de-averaging based on "purchase choice" or the particular bundle of services purchased. *See id.* Such a requirement could lead to discrimination based on certain tying arrangements. For example, if a particular, and desirable service package (for example, a package including DSL) is only available from the ILEC, then that package could be subject to an high SLC. Moreover, to the extent that carriers use contract tariffs for business and residential customers, any restrictions on SLC de-averaging could largely be circumvented; the SLC constraints do not apply to contract tariffs. *See id.* at 25. Varying the term or volume of a particular contract or offer only slightly would permit additional flexibility.

Third, in a purported attempt to prevent cross-subsidization between product markets, the Plan restricts SLC flexibility between the "mass market" service category and the "enterprise service category."[21] This means that decreases in SLC rates in the more competitive business markets cannot be made up by increases in SLC rates in less competitive residential markets. For no apparent reason, and in the absence of any competitive showing, this restriction is lifted in Step 5 of the Plan, (*see id.* at 22) opening the door to ILEC abuse and cross-subsidies between mass and enterprise markets.

The absurdity of the Plan's SLC scheme is illustrated by the manner in which it sets the SLC caps for the carriers in each track. Track 1 carriers can raise their SLCs up to $10 and then beyond in accordance with inflation. By contrast, the higher cost Track 2 carriers can raise their multi-line SLCs to $10 and their remaining SLCs to $8.75. The highest cost Track 3 carriers can only raise their multi-line SLCs to $9.20 and their remaining SLCs also to $8.75. Neither Track 1 nor Track 2 carriers can raise their SLCs to inflation after the final step. *See id.* at 20. Thus, the highest cost carriers are able to recover the least costs while the lowest cost carriers can recover the most.

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[21] The *Plan* proposes to divide the common line pricing flexibility basket (as defined in 47 C.F.R. § 61.42(d)(1)) into two categories: mass market (comprising primary residential, non-primary residential, and single-line business) and enterprise (multi-line businesses). *See id.* at 21-22.

V. The Interconnection Rules Set Forth In The Plan Are Unnecessary And Affirmatively Harmful

The Missoula Plan represents another attempt to modify network interconnection rules unnecessarily, particularly when they are now becoming relatively stable and predictable. The interconnection rules in the Plan suffer from several basic flaws.

First, the network interconnection architecture rules proposed in the Plan are unnecessary to the implementation of the intercarrier compensation rates proposed by the Plan. Unlike the Intercarrier Compensation Forum ("ICF") proposal, which included a similar "edge" proposal because of its purported relationship with the unified rates proposed in that proposal, the Plan does not (as explained) result in uniform rates for all carriers. Absent even this dubious rationale, there is not even a pretext that the proposed changes in network architecture are somehow necessary to achieve changes in rates.

In any event, there is serious doubt that any purported rationale could justify including wholesale changes in the rules governing network interconnection as part of intercarrier compensation reform. The proposed network modifications included in the ICF proposal encountered substantial resistance. Competitors and incumbents alike argued in favor of maintaining existing network interconnection arrangements. As parties explained in that context, modifying arrangements that have already been negotiated by parties would only introduce additional inefficiencies into the intercarrier compensation system.[22] As several parties also

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[22] CMRS, RLEC, and CLEC commenters argued that requiring multiple points of interconnection, as outlined by proposed network modification schemes and current network interconnection "agreements," would force competitors to duplicate ILEC networks unnecessarily, given the advanced technology deployed by CLECs and CMRS providers and the dearth of RBOC interconnections points in rural areas. *See* XO Comments at 23 (filed May 23, 2005) ("XO Comments"); Dobson, *et al*. Comments at 4 (filed May 23, 2005) ("Dobson Comments"); TDS Comments at 28-30 (filed May 23, 2005); Pac-West, *et al*. Comments at 40

demonstrated, a complex, new set of interconnection rules is unnecessary and could be harmful.[23] Deploying the suggested edge network Plans and other alternatives would require substantial effort and investment from all parties.[24] Additionally, a modified interconnection system could simply create new opportunities for arbitrage and other market distortions.[25] Several commenters also correctly observed that proposals that limit a competitor's ability to choose the point at which it interconnects with the incumbent network likely violate Section 251(c)(2).[26] Rather than embark on the quixotic effort of re-building the network interconnection scheme, the Commission should work within the existing rules, clarifying the application of the rules to be more consistent with the Act's intent. *See* Rural Alliance Comments at 12; XO Comments at 20-21.

Second, the Missoula Plan's edge network proposal in combination with the modifications to the transport rules would result in arbitrary and unjustifiable wealth transfers

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(filed May 23, 2005) ("On its face, the ICF Plan is discriminatory against CLECs and CMRS carriers.").

[23] *See* Rural Alliance Comments at 12 (filed May 23, 2005) ("Rural Alliance Comments"); Pac-West, *et al.* Comments at 28, 40 (filed May 23, 2005).

[24] Verizon Comments at 29-33 (filed May 23, 2005) ("Verizon Comments").

[25] *See* Verizon Comments at 30-32; KMC, *et al.* Comments at 39-41 (filed May 23, 2005) ("KMC Comments").

[26] *See* Cox Comments at 18 (filed May 23, 2005) ("Nothing in Section 251(c)(2) supports denying interconnection at a technically feasible point that is otherwise required by subsection B."); Rural Alliance Comments at 19-20 (stating that CBICC's Plan illegally suggests designated points of interconnection); Dobson Comments at 3-4 (stating "[u]nhappily, these rules are often honored in the breach. ILECs large and small generally require interconnection at multiple points in each LATA."); Allied National Paging Association Comments at 6-7; KMC Comments at 47-53 (stating that "any effort to modify network interconnection rules to implement the ICF's network interconnection Plan would violate the Act, well-established Commission rules, and the Commission's stated policy objectives.").

from CLECs to ILECs. The Missoula Plan requires that carriers designate edges on their networks, at which they must permit other carriers to physically interconnect. *See* Missoula Plan at 41. Carriers assume the financial obligations for transport to deliver originating non-access traffic to the terminating carrier's edge regardless of the actual interconnection arrangement between the carriers. *See id.* at 42. As a result, a competitive carrier choosing an alternate point of interconnection is faced with the untenable choice between an inefficient point of interconnection or paying the cost of what is essentially unused transport (*i.e.*, transport to the designated edge that is not in fact used because the carriers have chosen to interconnect at a location other than the edge). To make matters worse, the Plan does not clearly define the manner in which even Track 1 carriers define the edge, thus increasing the likelihood of disputes and the overall costs associated with exchanging traffic.

The proposed interconnection and transport rules create especially serious problems where CLECs must interconnect with Track 2 or Track 3 ILECs. Today, CLECs and rural ILECs generally each bear financial responsibility for delivering local traffic originating on their networks to the other carrier's network. Moreover, the CLEC's financial responsibility today generally only extends to delivering traffic to a single point in the rural ILEC's network. The Missoula Plan, in contrast, requires that CLECs bear the financial responsibility of transmitting traffic that originates and terminates on the CLEC's network to and from a rural ILEC's edge. *See id.* at 33-35. The Plan also allows a rural ILEC to define its network edge as any end office. *See id. at 46*. Thus, the Plan would impose upon CLECs two new substantial expenses when exchanging local traffic with rural ILEC: (1) the cost of transmitting traffic that originates on the rural ILEC's network from multiple points on the rural ILEC's network to the CLEC's network (today, rural ILECs usually bear this financial responsibility); and (2) the cost of carrying traffic originating on the CLEC network to multiple rural ILEC end offices rather than (as is usually the case today) a single point on the rural ILEC's network. The result is essentially an arbitrary wealth transfer from CLECs (and their customers) to rural ILECs, again without any underlying public policy rationale.

Moreover, the problem is even worse than that because requiring carriers to deliver traffic to rural ILEC end offices would likely force a competitive carrier to purchase transport from a Track 1 ILEC. This is because it would be impossible to build facilities for such a small amount of traffic and no competitive supply of transport is likely to be available. But, as explained, the tandem rates set in the Plan are extremely high. Thus, the interconnection arrangements between CLECs and rural ILECs also result in a further arbitrary wealth transfer from CLECs to ILECs from which the CLEC would be forced to purchase tandem transit service. It is clear therefore that the interconnection architecture rules in the Plan should be rejected as unnecessary and harmful.

VI. The Missoula Plan Inexplicably And Inappropriately Proposes New Rules For Special Access

In addition to all of its other problems, the Missoula Plan unnecessarily and inexplicably appears to propose additional pricing flexibility for special access as a portion of its incentive regulation plan for rate-of-return carriers. The apparent purpose of the incentive plan is to move rate-of-return carriers closer to a price cap model and "replace cost-based rate-of-return revenue formulas with per-line revenue formulas that allow participating carriers to realize financial gains from increased efficiency." *Id.* at 80-82. But the incentive plan is entirely tangential to intercarrier compensation reform, and the Commission should not risk further complicating the special access proceeding[27] at the cost of accomplishing a minor and unjustified goal.

The Plan also permits revenue recovery for a "mid-course correction" loss of special access revenues for Track 2 carriers. No other explanation is provided as to why such a correction would be necessary. Missoula Plan at 83. Given the current debate on the astronomical rates of returns for special access,[28] the Commission should re-set expectations for special access revenues in the special access rulemaking (or merger) proceedings first, before providing any carriers with the right to recover lost revenues for special access.

VII. Rather Than Adopt The Missoula Plan, The Commission Should Take Targeted Action To Address The Most Pressing Problems Associated With Intercarrier Compensation Today.

While the Missoula Plan suffers from numerous fatal flaws, this does not mean that the Commission has no ability to address problems associated with intercarrier compensation reform. At the very least, the Commission could take certain pragmatic, targeted steps to address glaring problems with the current regime.

For example, the Commission should consider setting uniform, cost-based terminating rates under its Section 251(b)(5) authority. Setting unified terminating rates would be extremely beneficial and taking this step is far less legally risky than setting originating rates. Additionally, the Commission should consider adopting the Missoula Plan's recommendation to apply access

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[27] *See* S*pecial Access Rates for Price Cap Local Exchange Carriers et al.*, Order and Notice of Proposed Rulemaking, 20 FCC Rcd 1994 (2005).

[28] *See* Reply Declaration of Susan M. Gately at 6, attached to Reply Comments of the Ad Hoc Telecommunications Users Group, WC Dkt. No. 06-74 (filed Jun. 20, 2006) ("As of year end 2005, the rates of return on the special access category for the RBOCs was as follows: Verizon - 41.6%, AT&T - 91.7%, Qwest - 109.4% and BellSouth - 13 98.3%. The average across all four RBOCs was an awe-inspiring 67.8%.").

charges to IP-based telephony, using telephone numbers to identify proxy end-user locations. *See* Missoula Plan at 25. Providing clarity on this issue would again advance consumer welfare by reducing the number of intercarrier disputes. The Commission should also adopt appropriate measures for revising the universal service contribution methodology.

Phantom traffic is clearly an issue that ILECs and CLECs alike face,[29] and a uniform set of carrier-signaling rules would ameliorate this problem even though the incentives for arbitrage remain. The proposal in the Missoula Plan offers a basis for discussion, although it does not address all aspects of the phantom traffic problem and still risks assigning incorrect terminating charges to the wrong carrier. A focused Commission effort on this subject would permit consensus on this issue that affects carriers across the competitive spectrum.

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[29] *See* Letter from Thomas Jones, Counsel for Cbeyond Communications, LLC, to Marlene H. Dortch, Secretary, FCC (filed Aug. 31, 2005); Letter from Eric Einhorn, Executive Director - Federal Regulatory, SBC, to Marlene H. Dortch, Secretary, FCC, (filed Aug. 11, 2005).

VIII. Conclusion

For the reasons explained herein, the Commission should reject the Missoula Plan and should instead take more targeted steps to address the obvious and fixable problems with the current regime.

Respectfully submitted,

/s/Thomas Jones

Thomas Jones
Jonathan Lechter
Grace Koh*
WILLKIE FARR & GALLAGHER LLP
1875 K Street, N.W.
Washington, D.C. 20006
(202) 303-1000

ATTORNEYS FOR
TIME WARNER TELECOM INC.,
CBEYOND, INC. AND XSPEDIUS
COMMUNICATIONS, LLC

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*Admitted only in New York.