Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of Establishing Just and Reasonable Rates for Local Exchange Carriers	WC Docket No. 07-135

REPLY COMMENTS OF VERIZON
IN RESPONSE TO NOTICE OF PROPOSED RULEMAKING

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The record in this proceeding establishes that traffic pumping is a classic arbitrage scam perpetrated by rural rate-of-return ILECs and CLECs. The Commission has already taken significant steps to limit the impact of ILEC traffic pumping. The Commission should complete the job by adopting the reforms proposed in Verizon's Comments in order to put an end to these illegitimate practices by rural ILECs once and for all. Even more urgently, swift Commission action is needed to limit the impact of CLEC traffic pumping. In the wake of the Commission's heightened scrutiny of ILEC traffic pumping, those schemes have largely shifted from ILECs to purported rural CLECs. CLEC traffic pumping is exploding and now accounts for the majority of traffic pumping minutes billed to Verizon and other IXCs. Absent prompt Commission action, CLEC traffic pumping will continue growing exponentially.

The record in this proceeding establishes further that traffic pumping is a discrete issue involving arbitrage scams that requires swift Commission action. Contrary to some parties' claims, traffic pumping does not implicate any broader questions of intercarrier compensation reform. Similarly, there is no reason, as some parties claim, for the Commission to delay action that would end these scams. A regulatory solution, targeted specifically at reducing incentives to engage in these scams, is therefore a more efficient means of addressing this form of arbitrage.

DISCUSSION

I. THE COMMISSION SHOULD ADDRESS THE FAST-GROWING PROBLEM OF TRAFFIC PUMPING CLECS IMMEDIATELY

The Commission's first priority in this proceeding should be to act immediately to put a stop to traffic pumping by CLECs. As AT&T's Comments make clear (at 11-12), as a result of this Commission's action in suspending access tariffs filed by ILEC traffic pumpers, CLECs now account for three-quarters of the traffic pumping minutes billed to AT&T. Verizon's experience has been similar: since July 2007, CLECs have accounted for more than 75 percent of the traffic pumping minutes billed to Verizon. Contrary to the views expressed by some parties, *see*, *e.g.*, All American Telephone et al. Comments at 3, the evidence is that CLECs now are creating the majority of traffic pumping minutes.

In this regard, as the Commission noted in the *NPRM*,[1] a CLEC has "the same incentive to stimulate access traffic as does an incumbent LEC." *NPRM* ¶ 34. Moreover, unlike an ILEC, a CLEC can be established in a very short time and can choose to serve only a small number of customers. As Qwest's Comments note, at least one free chat line provider has established its own purported CLEC in order to engage in these traffic pumping schemes. *See* Qwest Comments at 10 (citing All American Telephone Company, a CLEC in Nevada and Utah that shares ownership with Joy Communications, a chat line provider). Similarly, some owners of rural ILECs that were formerly engaged in traffic pumping have simply moved their traffic pumping scheme over to an affiliated entity that they claim acts as a CLEC. *See* AT&T

[1] Notice of Proposed Rulemaking, *Establishing Just and Reasonable Rates for Local Exchange Carriers*, 22 FCC Rcd 17989 (2007) ("*NPRM*").

Comments at 11 n.14 (citing new CLECs engaged in traffic pumping apparently related to Beehive Telephone Company); Qwest Comments at 9 (citing Tekstar Communications, Inc., a rural CLEC under common ownership with six rural ILECs in Minnesota, and Northern Valley Communications, a traffic pumping CLEC that has the same board of directors and management as James Valley Cooperative, a South Dakota ILEC). These types of improper attempts to evade the Commission's rules will continue absent prompt action by this Commission to stop traffic pumping by CLECs.

As with rural rate-of-return ILECs, this Commission never intended to allow CLECs to collect windfall returns through switched access tariffs. To the contrary, the Commission's chief goal in adopting the *CLEC Access Charge Order*[2] was to "eliminate regulatory arbitrage opportunities . . . with respect to tariffed CLEC access services" by "more closely . . . align[ing] tariffed CLEC access rates with those of the incumbent LECs." *CLEC Access Charge Order* ¶ 3. The Commission should take prompt action to stop these CLEC traffic pumping scams to vindicate the Commission's long-stated intent to "eliminate" arbitrage opportunities in this area.

In particular, the Commission must act to address two related rules that currently create incentives for CLEC traffic pumping schemes. First, if they meet certain conditions, CLECs operating only in a rural area served by a price-cap LEC with statewide operations can (and do) claim to meet the "rural exemption," and thereby benchmark their access rates at the highest rate band of the NECA access tariff. *See* 47 C.F.R. § 61.26. Second, CLECs that operate only in an area served by a rural rate-of-return ILEC can benchmark their access rates to the rural ILEC's tariffed rates. *See id.*

[2] Seventh Report and Order and Further Notice of Proposed Rulemaking, *Access Charge Reform*, 16 FCC Rcd 9923 (2001) ("*CLEC Access Charge Order*").

Recent experience demonstrates that, instead of supporting competition in rural areas, these rules have served almost exclusively to support traffic pumping scams. Indeed, in September 2007, CLECs engaged in traffic pumping represented *more than 90 percent* of the total amount billed to Verizon by "rural exemption" CLECs in that month. *See* Verizon Comments at 24. Some of these CLECs are serving no parties other than the ones with which they have kickback arrangements and appear to have been created solely for the purpose of traffic pumping. For example, more than 99 percent of the traffic Verizon currently sends to Aventure Communication Technology, an Iowa "rural exemption" CLEC that began operating in late 2006, is associated with just a handful of telephone numbers that Aventure has assigned to "free" conferencing and chat line services. *See id.* For Capital Telephone Inc., a South Dakota "rural exemption" CLEC that began operating in mid-2007, that number appears to be a full 100 percent. *See id*.

There is no reason to permit such abuses to continue. Accordingly, as proposed in Verizon's Comments, the Commission should immediately eliminate the rural exemption, which has been used almost exclusively to carry out the kind of arbitrage schemes the Commission sought to eliminate.

Alternatively, and at a minimum, the Commission should amend section 61.26 in the two respects proposed in Verizon's Comments. First, the rules would provide that CLECs will be disqualified from claiming the rural exemption if their traffic volume exceeds 350 minutes of use ("MOU") per line per month (excluding from their line counts any "lines" provided to a "customer" under an arrangement that can be expected to produce a net payment from the CLEC to its "customer") or a total of 1.3 million minutes per month. As Verizon's Comments explain (at 25-27), those trigger points are above the 95th percentile for MOU per line per month and

MOU per month for the very small NECA carriers to whom the rural CLECs are seeking to benchmark and are far above the median MOU for those NECA carriers. When supposedly rural CLECs have such heavy traffic volume, they have little in common with the small NECA ILECs and should not be permitted to benchmark to their rates. As with section 61.39 ILECs, where a CLEC reaches the volume trigger, the Commission should require that CLEC to file a revised tariff pursuant to section 61.26 without claiming the rural exemption.

Second, section 61.26 would be amended to require that, where a CLEC benchmarks to the rate of a competing rate-of-return ILEC, and the CLEC's monthly terminating access volumes exceed 400 MOU per line per month, the CLEC must benchmark its rates instead to the rates of the RBOC serving that state. As Verizon's Comments demonstrate (at 27-28), this limitation is appropriate because 400 MOU per line per month is a high volume for a supposedly rural, benchmarking CLEC. Adopting such a limit would prevent traffic pumping from shifting to these CLECs once the Commission takes corrective action as to the rural CLEC exemption.

II. ADDRESSING TRAFFIC PUMPING IMMEDIATELY AS A DISCRETE ISSUE IS APPROPRIATE AND WILL PROMOTE THE PUBLIC INTEREST

The Commission should act promptly to put in place needed safeguards for both CLECs and ILECs in this proceeding and not, as some parties suggest, await comprehensive intercarrier compensation reform.[3] Indeed, unless the Commission acts immediately as to *CLEC* traffic pumpers, its recent actions to limit this illicit behavior by rural ILECs will be largely meaningless,[4] as ILECs or third-party providers seeking to engage in traffic pumping will simply

[3] *See, e.g.*, Cbeyond/Integra Comments at 1-2; Chase Com et al. Comments at 6-7; Global Conference Partners Comments at 20.

[4] In addition to the recent actions of the Commission to curb traffic pumping, NECA, in its 2008 Modification of Average Schedules, WC Docket No. 07-290 (FCC filed Dec. 21, 2007), has proposed for the first time to define a "range within which the [average schedule] formulas accurately reflect costs as observed in [NECA's] study," *id*. at I-5; *see also NPRM* ¶¶ 25-26.

partner with CLECs or establish purported CLECs that are wholly or partly controlled by them. Indeed, abundant evidence, outlined above and in AT&T's Comments, demonstrates that these parties have already begun to do so in great numbers.

While it is understandable that parties benefiting from illegitimate traffic pumping schemes would want to delay changes to the rules that enable those schemes for as long as possible, the fact is that traffic pumping involves discrete issues that should be addressed now, and need not await general intercarrier compensation reform. Simply put, traffic pumping is a scam that leads to unjust and unreasonable rates and, in the case of CLECs, turns rules intended to permit rural competition into a vehicle for arbitrage. Such schemes are contrary to the public interest and the interests of consumers, and the Commission need not await broader reform to put in place safeguards that put an end to them. Addressing traffic pumping only through broader intercarrier compensation reform would only permit illegitimate and unlawful scams to continue without serving any public-interest purpose whatsoever.

Moreover, contrary to Comments suggesting otherwise,[5] traffic pumping is, at bottom, a discrete issue involving the tariffs filed by certain classes of carriers. Indeed, the *NPRM* makes clear that traffic pumping concerns whether "the current rules governing the *tariffing* of traffic-sensitive switched access services by [LECs] are ensuring that rates remain just and reasonable, as required by section 201(b) of the Communications Act." *NPRM* ¶ 1 (emphasis added). The Commission can adopt the tariffing regulations necessary to end these abuses now and need not let these scams continue pending the resolution of different, broader policy concerns. Similarly,

[5] *See, e.g.*, Chase Com et al. Comments at 6-7; Global Conference Partners Comments at 20; Leap Wireless Comments at 8 (all requesting that the Commission address traffic pumping as part of broader intercarrier compensation reform, ignoring the fact that traffic pumping is primarily a tariffing issue and *not* an intercarrier compensation issue).

the Commission should reject the requests to address phantom traffic and other alleged access avoidance schemes that bear no relationship to traffic pumping in this rulemaking proceeding.

III. NEW REGULATORY SAFEGUARDS ARE THE MOST EFFICIENT MEANS OF ADDRESSING TRAFFIC PUMPING

As the Commission has already indicated, the promulgation of new rules providing safeguards against traffic pumping is the most efficient approach for addressing traffic pumping. Traffic pumping implicates policy issues applicable to two classes of carriers: small rate-of-return ILECs and supposedly rural CLECs. Those issues are more efficiently addressed through a rulemaking adopting regulations for all members of those classes rather than through case-by-case decisions. As Verizon's Comments explain (at 13-20, 23-28), those rules should include, among other things, triggers for both ILECs and CLECs that require tariff refiling when specific demand thresholds are met.[6] Such general rules allow for a self-effectuating and effective method to end the unjust and unreasonable practices and rates at issue here. By contrast, if every IXC filed a complaint against each LEC suspected of traffic pumping, the Commission would have to adjudicate numerous complaints involving essentially the same schemes and facts. Such a process would be a significant drain on the Commission's resources.

Additionally, there are several critical factors that would significantly limit the effectiveness of the complaint process in this context. Absent new rules preventing traffic pumping conduct, rural ILECs and supposedly rural CLECs will continue to claim (wrongly) that their actions accord with existing requirements and are thus lawful. Moreover, as the recent

[6] AT&T has proposed triggers at somewhat higher levels than Verizon. *See* AT&T Comments at 28. While those triggers may be sufficient to capture the traffic pumping schemes that have been observed to date, they may not capture future traffic pumping and are, as AT&T acknowledges, well above any "natural" change in demand. *See id.*

Qwest Order shows,[7] even where an IXC can demonstrate that those arguments are incorrect, the tariffing rules granting a LEC's tariffed access rates "deemed lawful" status sometimes provide a significant obstacle to a § 208 complaint challenging the reasonableness of those rates.[8] The Comments suggesting that the Commission address traffic pumping through the complaint process ignore these limitations on the effectiveness of that process in this context.[9] Indeed, the Commission itself has explained that, although traffic pumping can "result in rates that are unjust and unreasonable," those rates might "be protected by the deemed lawful provision of the Act."[10] For this reason, if IXCs were to rely on the complaint process alone, a traffic pumping LEC may still be able to retain the revenue earned from its unjust and unreasonable practices, which in many cases is substantial.

IV. THE COMMISSION HAS AMPLE AUTHORITY TO REQUIRE A NEW TARIFF FILING WHEN DEMAND REACHES THE TRIGGER LEVEL

CenturyTel mistakenly argues (at 6-8) that the Commission's proposal to require ILECs and CLECs to file revised tariffs automatically in the event an ILEC or CLEC experiences a dramatic increase in demand (1) violates the "deemed lawful" provision of the Act, 47 U.S.C.

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[7] *See* Memorandum Opinion and Order, *Qwest Communications Corp. v. Farmers & Merchants Mut. Tel. Co.*, 22 FCC Rcd 17973, ¶ 27 (2007) ("*Qwest Order*") (concluding that Farmers & Merchants Mutual Telephone Company's access rates were unjust and unreasonable, but denying retroactive relief because those rates were "deemed lawful").

[8] *See* 47 U.S.C. § 204(a)(3); *see also CLEC Access Charge Order* ¶ 94 ("[W]e will conclusively presume that a CLEC's access rates are reasonable if they fall at or below the benchmark that we establish herein."); Eighth Report and Order and Fifth Order on Reconsideration, *Access Charge Reform*, 19 FCC Rcd 9108, ¶ 59 (2004) (explaining that, in the *CLEC Access Charge Order*, the Commission concluded that "a competitive LEC's access rates are presumed reasonable if they fall at or below the benchmark"). In the event that a LEC knowingly makes any required representation falsely, "deemed lawful" status does not apply. *See* Verizon Comments at 19.

[9] *See, e.g.*, CBeyond/Integra Comments at 6; Hypercube/McLeodUSA Comments at 10-11; Rural Independent Competitive Alliance Comments at 8; TelePacific Comments at 8.

[10] *See* Order Designating Issues for Investigation, *Investigation of Certain 2007 Annual Access Tariffs*, 22 FCC Rcd 16109, ¶ 15 (PPD 2007).

§ 204(a)(3), and the Commission's existing rules; and (2) denies carriers due process. *See also* Independent Telephone & Telecommunications Alliance Comments at 12-15 (same). Contrary to CenturyTel's contentions, the Commission has full authority to establish, by rulemaking, a measuring period for rate-of-return carriers that is different from the current two-year period, and to set the new measuring period based on a triggering event rather than as a discrete period of time. Moreover, in the event a carrier believes that the obligation to file a new tariff will be unreasonable in a particular instance, ample procedural avenues are available under both the Commission's rules and the proposed amendments to those rules for such a carrier to bring the matter before the Commission for hearing.

CenturyTel's first argument proceeds from the mistaken premise that the "deemed lawful" provision of the Act entitles carriers to charge the same rate in perpetuity, absent action by the Commission under § 205 or § 208 of the Act. *See* CenturyTel Comments at 6-7 (arguing that "rates remain lawful until and unless the Commission finds that the rates are unlawful pursuant to its other statutory processes, such as . . . Sections 205 or 208 of the Act"). In fact, requiring automatic tariff updates is a proper tool in ensuring just and reasonable rates, *see* 47 U.S.C. § 154(i), given that tariffed rates based on stale data lose their accuracy over time, *see* 47 C.F.R. § 61.43 (requiring price-cap carriers to file a new tariff on an annual basis); *id.* § 65.600 (requiring periodic rate-of-return reports). Indeed, if CenturyTel were correct (and it is not), the Commission's "two-year rate-of-return monitoring period," *see* CenturyTel Comments at 7 (citing 47 C.F.R. § 65.701), upon which CenturyTel purports to rely, would be just the sort of provision that would be impermissible: it requires carriers to update their tariff filings automatically every two years to ensure compliance with the prescribed rate of return. But the Commission can require tariff refiling every two years, and CenturyTel does not argue otherwise. The Commission's proposal here would simply replace that static two-year monitoring period with a different, but equally lawful, mechanism, adapted to solve a specific practical problem – namely, ILECs and CLECs charging rates that become unreasonable after a dramatic spike in demand. *Cf. Southwestern Bell Tel. Co. v. FCC*, 10 F.3d 892, 898 (D.C. Cir. 1993) (noting the "automatic adjustment[ ]" provisions of price-cap regulations based on fluctuation in certain exogenous costs). The Commission's proposed demand trigger concept represents a reasoned judgment that, in the event demand increases above a certain threshold, the cost and demand data used to set the tariffed rate will be sufficiently inaccurate compared with actual conditions to justify requiring the carrier to recalculate its tariff based on fresh cost and demand data. There is no legal barrier to the Commission acting based on that judgment.

Moreover, CenturyTel's contention (at 7) that "an automatic revision requirement" violates the Commission's existing rules overlooks the fact that the Commission is proceeding by proposed rulemaking here. The Commission is free to adopt *new* rules that modify – or even contradict – its existing rules so long as the new rules represent a permissible implementation of the Communications Act. *Cf. Chevron U.S.A. Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837, 863-64 (1984) ("An initial agency interpretation is not instantly carved in stone. On the contrary, the agency, to engage in informed rulemaking, must consider varying interpretations and the wisdom of its policy on a continuing basis.").

Finally, CenturyTel's argument (at 8) that the proposed rules might violate carriers' due process rights is without merit. As Verizon's Comments note (at 15), "[i]n the very unlikely event that a carrier experiences a sudden spike in demand that is, in fact, accompanied by a concomitant increase in costs (or, for example, where the demand increase was a result of a corporate merger, acquisition, or consolidation), that . . . carrier could petition the Commission for waiver of the obligation to file a revised tariff, and, in so doing, could provide an evidentiary showing that its increase in demand has, in fact, lead to a proportionate increase in costs." *See also* 47 C.F.R. § 1.3. Thus, the Commission's existing rules, consistent with due process requirements, offer potentially affected carriers ample "opportunity to be heard at a meaningful time and in a meaningful manner." *Mathews v. Eldridge*, 424 U.S. 319, 333 (1976) (internal quotation marks omitted).

V. THE APPROACHES CONTEMPLATED BY THE *NPRM* RAISE NO FIRST AMENDMENT CONCERNS

Contrary to the Comments of Chase Com, Fonepods, Inc., FreeConferenceCall.com, and HFT Corp. (collectively, "Chase Com"), the proposed revisions to the Commission's tariff rules do not implicate the First Amendment to the United States Constitution in any respect. Indeed, the real issue here is whether conference call and other similar providers, which are not themselves engaged in any speech, have the right to have their services subsidized by arbitrage scams. First Amendment law does not recognize any such right.

Chase Com is also wrong in asserting that this proceeding implicates end users' First Amendment interest in "talking to whom they please when they please." Chase Com et al. Comments at 10. No party to this proceeding has asked the Commission to outlaw or to restrict conference call or chat line services, nor is there any evidence that the Commission is considering something so outlandish. Instead, this proceeding solely involves routine issues relating to the unreasonable rates and practices of switched access providers. It assuredly does not involve regulation of speech, and the questions presented here thus implicate no First Amendment interest.

Nor is there any support for Chase Com's related suggestion that the corrective action proposed by the Commission is somehow an impermissible *content*-based regulation. *See id.*

at 11 (arguing that adopting the proposed rules would be "no different in principle than if [the Commission] had attempted to require one political commentator[ ] to pay a registration fee before appearing on television while exempting others from having to pay the registration fee"). As discussed above, the reforms proposed in these proceedings would not regulate speech, much less the particular content of the speech. Instead, these reforms would only regulate the practices and rates of rural rate-of-return ILECs that file tariffs under section 61.39 and of supposedly rural CLECs, regardless of whether conference call providers or chat lines were involved.[11] Thus, under the proposed reforms, providers would be free to continue to offer conference call and chat line services, and individuals could continue to use those services. *Cf. Chladek v. Verizon New York Inc.*, 96 F. App'x 19 (2d Cir. 2004) (affirming dismissal of First Amendment claim challenging order of New York Public Service Commission authorizing Verizon to remove from its tariff billing for "976" information service, because tariff regulation was content-neutral); *Hill v. Colorado*, 530 U.S. 703, 720 (2000) (even where, unlike this case, government is regulating speech, "government regulation of expressive activity is 'content neutral' if it is justified without reference to the content of regulated speech").[12]

[11] The First Amendment authorities Chase Com cites (at 10-11) in support of its Comments are inapposite. In *Simon & Schuster v. Members of New York State Crime Victims Board*, 502 U.S. 105 (1991), the Court struck down New York's "Son of Sam" law, which required that "an accused or convicted criminal's income from works describing his crime be deposited in an escrow account . . . [for the] victims of the crime and the criminal's other creditors." *Id.* at 108. There, the Court held that, because the law, on its face, was triggered based on the *content* of the speech in the work, it violated the First Amendment. The neutral rules proposed here, which merely seek to set reasonable tariffed rates, are not analogous in any sense. *Reno v. ACLU*, 521 U.S. 844 (1997), is similarly irrelevant. In that case, the Court addressed a First Amendment challenge to two provisions in the Communications Decency Act of 1996, which purported to regulate the transmission of "obscene or indecent" messages over the Internet. *Id*. at 858-59. Thus, as in *Simon & Schuster* – but unlike in the *NPRM* – the law at issue in *Reno* was content-based on its face. *Reno* thus has no application here.

[12] In this regard, the argument of Global Conference Partners (at 12-13) that call blocking violates the concept of "net neutrality" is irrelevant here, as the Commission has not proposed in

CONCLUSION

For the foregoing reasons, the Commission should resolve the issues in this proceeding in accordance with these Reply Comments and Verizon's previously filed Comments in this docket.

Respectfully submitted,

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the *NPRM* to allow call blocking, and Verizon does not block calls placed to access stimulation providers. Whatever the merit of discussing "net neutrality" in the context of broadband Internet access services and other services available on the public Internet, there is no reason to drag services offered over the PSTN into that debate.