



October 10, 2008

EX PARTE

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, SW
Portals II, Room TW-A325
Washington, DC 20554

Re: Developing a Unified Intercarrier Compensation Regime, CC Docket No. 01-92

Dear Ms. Dortch:

Pursuant to Commission rules, please include the attached letter in the docket of the above-referenced proceeding.

Sincerely,

A handwritten signature in black ink, appearing to read "David Cohen", written in a cursive style.

David Cohen
Vice President, Policy



October 10, 2008

Chairman Kevin J. Martin
Federal Communications Commission
445 12th Street SW
Washington, DC 20554

Commissioner Robert M. McDowell
Federal Communications Commission
445 12th Street SW
Washington, DC 20554

Commissioner Deborah T. Tate
Federal Communications Commission
445 12th Street SW
Washington, DC 20554

Commissioner Jonathan S. Adelstein
Federal Communications Commission
445 12th Street SW
Washington, DC 20554

Commissioner Michael J. Copps
Federal Communications Commission
445 12th Street SW
Washington, DC 20554

Dear Chairman Martin, Commissioners Copps, McDowell, Adelstein, and Tate:

Today's regulatory system governing how carriers compensate one another for calls traveling across the public switched network is badly in need of reform. Our members appreciate the Commission's renewed focus on comprehensive reform and achieving the consumer and broadband investment benefits that reform will bring. The reform that the Commission is working towards will require a comprehensive plan with broad consensus support. The Missoula Plan meets those needs, and provides the best platform for reform that sends the right pricing signals, substantially eliminates arbitrage and modernizes the social compact that underlies the provision of service in rural areas. We have worked to simplify and adapt the Missoula Plan to the current context of the debate, and believe that, as outlined in the attached document, the Plan provides the best roadmap to comprehensive reform.

The attached paper explains the key elements of the Missoula Plan in the context of the current debate. In essence, by greatly simplifying today's rate structure, appropriately shifting opportunities to recover revenues between carrier and consumer charges and a recovery fund collected through universal service contributions, the Plan provides the right framework for reform. A key element of that framework recognizes that not all carriers are similarly situated, and that a simple grouping into three tracks appropriately recognizes differences among them.

Ensuring greater fairness and stability of universal service funding by adopting a numbers-based contribution mechanism is an integral part of ensuring that comprehensive

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reform is pro-competition and pro-consumer. Solutions to remedy the problems of phantom traffic and traffic pumping must also be included in a reform package.

The current regulatory system governing carrier compensation is overdue for reform. We urge the Commission to take this opportunity to provide a more stable footing for the industry to move forward and meet the competitive challenges of providing new and better services to consumers.

Sincerely,

A handwritten signature in black ink, reading "Walter B. McCormick, Jr." in a cursive script.

Walter B. McCormick, Jr.



**FRAMEWORK FOR COMPREHENSIVE INTERCARRIER COMPENSATION
REFORM BASED ON THE MISSOULA PLAN**

October 10, 2008

I. The Missoula Plan's Tracks and Revenue Dials Provide the Right Analytical Tools for Commission Action

Two key aspects that emerge from the Missoula Plan's analytical work and consensus building are the need to recognize differences among carriers in terms of the economics of their serving territories, including regulatory burdens, and the need to appropriately balance revenue opportunities across potential revenue sources.

The three-track structure of the Missoula Plan should be included in any Commission order comprehensively reforming intercarrier compensation. There is no doubt that economies of scale and scope are a major factor in the cost structure of communications providers. So too is the density of the customers to which the providers offer service. The Commission has long recognized these concepts in its actions on compensation. For example, the last major restructuring of access charges in the CALLS plan adopted a three-track approach and set rates at \$.0055, \$.0065 and \$.0095 to recognize carriers' differing economics.

While unifying individual carrier rates, particularly terminating rates, for interstate access, intrastate access and reciprocal compensation is necessary to rationalize the system of intercarrier compensation, immediately unifying such rates across the wide spectrum of carriers is not only unnecessary but also would be harmful. Rebalancing rates to the levels suggested in the Missoula Plan, and eliminating the distinction between the various types of intercarrier traffic, represent a major step forward, one that will provide the correct economic signals while avoiding the introduction of potential new distortions. Simplifying and unifying compensation within the Missoula Plan framework also goes hand-in-hand with simplifying and unifying the regulatory framework for VoIP traffic that interconnects with the public switched telephone network ("PSTN"). As such, as part of this reform, VoIP traffic also would be subject to the same unified compensation as other traffic that terminates on the PSTN. This will provide clarity for VoIP and PSTN providers and eliminate a major source of dispute in the industry.

The USTelecom Framework retains the Missoula Plan track structure in simplified form because it generally reflects the right distinctions between providers in terms of cost structure. AT&T, Verizon and Qwest should continue to occupy Track 1, with the remaining, and much smaller, price cap carriers in Track 2, and all rate of return carriers and study areas in Track 3. Per the Missoula Plan all non-ILECs would be placed in Track 1. Changes in the industry since the submission of the Missoula Plan two years ago make these track distinctions even simpler and more clear cut. The conversion of Windstream, Consolidated, Puerto Rico and Frontier to price cap regulation, and the petition of Century/Tel for similar treatment place almost all mid-sized carriers in a similar position deserving of similar treatment.

The Missoula Plan identified four key revenue components involved in compensation reform: terminating rates, subscriber line charges, benchmark local service rates and an access restructure mechanism or “ARM.”¹ A recent AT&T submission illustrates these “dials” and their interdependence.² Proposals by ITTA, representing mid-sized carriers, and Verizon both utilized the dials approach. While neither of those proposals embraces the dial *settings* included in the Missoula Plan, the fact that both utilize the dials *framework* confirms that reform is best accomplished under the Missoula Plan analytical framework. Furthermore, their use of the dials facilitates analysis of each proposal and their suggested settings provide useful parameters for the Commission’s deliberations. As with the Missoula Plan, as well as the ITTA and Verizon filings, the rates shown below would be default rates.

II. The USTelecom Framework Retains the Missoula Plan Dial Settings Which Correctly Balance Key Interests

The Missoula Plan identified four key dials to adjust as part of compensation reform. These dials and the proper settings for them are discussed below.

- **Dial 1 -- Rates** – Regulatory arbitrage can be minimized with a default intercarrier rate structure that treats all traffic uniformly.³ Both the Verizon and ITTA proposals unify terminating intercarrier rates, thus both recognize and attempt to address the potential and actual arbitrage problems stemming from different rates charged for the carriage of traffic for which similar functions are performed. Today, telecommunications markets are disrupted by diverse intercarrier compensation regimes that assess different charges for the handling of traffic depending on the jurisdiction, customers or technologies involved in calls. This state of affairs produces arbitrage and intercarrier disputes. A key goal of intercarrier compensation reform should be to minimize arbitrage by adopting a more uniform rate structure, most importantly for traffic terminating on the PSTN, regardless of the identity of the service provider, the jurisdiction of the call, or the underlying technology with which the call was made. In particular, the terminating rates discussed below should specifically apply to VoIP traffic of any form terminating on the public switched network.⁴

¹ Although the name of the mechanism seems to imply that it only applies to revenues lost through reductions in access rates, under the Missoula Plan it applies to revenues lost through restructuring of all intercarrier charges which also includes potential reductions to reciprocal compensation charges in higher cost areas.

² See AT&T *ex parte* filing dated September 12, 2008, in CC Docket No. 01-92, WC Docket No. 05-337, CC Docket No. 96-45, WC Docket No. 99-68, WC Docket No. 07-135 on dials and relative affects of changing settings

³ Arbitrage schemes continue to multiply, as articulated in the *Petition of AT&T for Interim Declaratory Ruling and Limited Waivers*, WC Docket No. 08-152 filed July 17 2008, which listed several urgent specific problems with the current regime, and suggested piece-part solutions, including maintaining the current rules for ISP bound traffic, combating traffic pumping and adopting USTelecom’s proposal for addressing phantom traffic. USTelecom strongly endorses these solutions addressing particular forms of regulatory arbitrage. In particular, a remedy addressing phantom traffic will be a necessary part of any comprehensive reform proposal. While the rest of these solutions may still be relevant even with adoption of comprehensive intercarrier compensation reform, it is clear that effective comprehensive reform would minimize the opportunity for current and new schemes of regulatory arbitrage.

⁴ While the Missoula Plan also addressed originating rates, the USTelecom Framework does not. However, originating rates should be dealt with in a further notice promptly after adoption of a comprehensive intercarrier

The Missoula Plan accomplishes this key goal. Like the Missoula Plan, the USTelecom Framework recommends unifying intercarrier compensation termination rates as follows:

- Track 1 carriers: \$.0005 per MOU
- Track 2 carriers: \$.0080⁵ per MOU
- Track 3 carriers: The current interstate access rate level.

The Verizon proposal does not utilize this track approach, substituting a single nationwide termination rate for all providers. While the ITTA plan does adopt the track approach, it departs from the Missoula Plan's suggested rates. The track approach of the Missoula Plan, as well as the rates for each track, set the appropriate balance. As discussed below, the Missoula Plan rates include both end office switching and transport functions as appropriate. The Missoula and ITTA plans both recognize that costs vary by customer density and the geographic characteristics of each service area. Thus, they propose a higher default rate for Track 2 and use of current interstate access rates for Track 3 carriers.

Associated Interconnection Principles -- Simplified interconnection principles for defining transport would require sending carriers to deliver traffic to the terminating carrier's "Edge" through direct or indirect interconnection arrangements, with the sending carrier choosing the type of arrangement. The Edge for every carrier would be set at the tandem unless the terminating carrier has no tandem, in which case the Edge is the end office. This approach would allow an exception for local and EAS traffic sent by a rural carrier to a carrier with an Edge outside the rural carrier's service area. For such a carrier, the obligation is to deliver EAS traffic to a point on its service area boundary.

- **Dial 2 -- Subscriber Line Charge Cap Increases (at the conclusion of an appropriate transition)** – The Missoula Plan recommended Subscriber Line Charge (SLC) cap increases of \$3.50 for Track 1 providers and \$2.25 for Tracks 2 and 3. Verizon proposed \$4.00 SLC increases for residential and single line business subscribers and \$1.30 for multi-line business subscribers, while ITTA proposed \$2.25 SLC cap increases for all providers. The Missoula Plan SLC cap increases strikes the right balance between limiting the size of an access replacement mechanism while not placing an inordinate burden on subscribers in higher cost areas.
- **Dial 3 -- National benchmark** – The Missoula Plan includes a national benchmark which is \$25 for purposes of constraining the size of increases in the SLC caps but includes a \$20 lower-end adjustment which would be used to impute any difference between the \$20 adjustment and a carrier's calculation of its rates below it as a reduction to the access restructure mechanism. Thus, SLC increases would not be

compensation reform order addressing terminating rates. That further notice should carry forward the concepts of unifying rates and inclusion of a restructure mechanism.

⁵ Similar to the opportunity afforded to carriers in the CALLS plan, and consistent with the Missoula Plan, carriers should have an opportunity to submit a TELRIC cost study if the prescribed rates for Track 2 are non-compensatory.

required to the extent they would result in rates exceeding the \$25 dollar benchmark. The Verizon and ITTA proposal contain roughly similar approaches. The Verizon proposal includes a single benchmark suggested to be between \$22 and \$26 dollars for both purposes, and the ITTA proposal suggests a benchmark of \$20.76 excluding taxes and fees, solely to constrain increases in the SLC cap. Again, the Missoula Plan strikes the appropriate balance between the size of SLC increases and the size of the access restructure mechanism. It also has a more nuanced approach to the benchmark issue by addressing both legitimate purposes for a benchmark approach and utilizing levels appropriate to each.

- **Dial 4 -- Recovery Mechanism** –The Missoula Plan includes a recovery mechanism, as do the Verizon and ITTA filings, to create an opportunity for carriers to reduce terminating charges to recoup any remaining intercarrier compensation shortfall after companies move up to the new SLC caps to the extent allowed under the rules. Such a mechanism, called an access restructure mechanism or “ARM” in the Missoula Plan, is an appropriate way to comply with the Act by making implicit subsidies explicit and assuring carriers an opportunity to obtain the implicit subsidy revenue required to meet the additional costs imposed through carrier of last resort and other social obligations. As noted above in footnote 1, although the term “ARM” used in the Missoula Plan could be read to suggest that the recovery mechanism only applies to revenues lost through reduction in access rates, under the Missoula Plan it applies to revenues lost through restructuring of all intercarrier charges which also includes potential reductions to reciprocal compensation charges in higher cost areas. The Commission should likewise treat all intercarrier compensation, including reciprocal compensation, as eligible for ARM funding.

Companies receiving ARM funding should have maximum flexibility to match that funding to higher cost areas, including the same opportunity to geographically deaverage it as they have had under the prior rules for deaveraging other similar elements of universal service funding. Because the potential amount of ARM funding for some carriers may be substantial, if carriers have made one time elections regarding USF deaveraging, they should be afforded a fresh opportunity to make that election at the initiation of ARM funding.

Under the Missoula Plan, price cap companies would lose ARM funding with the loss of an access line. (Verizon proposes that the funding associated with a lost line be phased out over three years in equal increments.) The Commission has already tentatively concluded that access replacement funding, such as Interstate Access Support (IAS) and Interstate Common Line Support (ICLS), should not be provided to Competitive Eligible Telecommunications Carriers (CETCs). USTelecom concurs with the Commission’s conclusion and recommends that this conclusion be extended to the ARM.

III. Establishment of a Credible and Compensatory ARM is an Essential Element of Comprehensive Intercarrier Compensation Reform

Regulation must not stand between network owners and the opportunity to obtain fair compensation for the use of their networks. Thus, the Missoula Plan creates a restructure mechanism to provide an opportunity to replace intercarrier revenues reduced through reform of access and reciprocal compensation charges, to the extent that such revenues are not recovered through increased SLC rates. Similarly, Verizon states that “the Commission should create a stable, predictable access replacement mechanism to ensure that carriers ... have the opportunity to recover the revenues that have traditionally been collected through access charges.” ITTA’s proposal also contemplates such a mechanism for price cap as well as rate of return carriers, which it calls the “Alternative Recovery Mechanism.”

Creation of a credible, compensatory ARM is a necessary precursor to reform of intercarrier compensation. Telecommunications is a capital intensive business with massive amounts of long-term investment. Wireline carriers, as carriers of last resort, are obliged to sustain a certain level of investment. For example, borrowers from the government’s RUS telecom program have already made investments for which they owe the federal government billions of dollars in loan repayments. Public policy-makers are rightfully encouraging communications providers to increase the areas in which they provide broadband and enhance the speed and robustness of broadband services. All of these goals and obligations are at risk without a credible, stable ARM that provides carriers an opportunity to compete for the revenues previously available under regulatory compensation structures that helped fund an essential social compact to provide service in even the most rural areas. As long as the costs of serving as carriers of last resort and meeting other social obligations continue, making a credible and compensatory ARM available is a minimum step necessary for regulators to uphold their end of the bargain and to ensure continued availability of affordable telecommunications and information services in rural areas.⁶

IV. Action on Phantom Traffic, Access Pumping is a Necessary Component of Comprehensive Intercarrier Compensation Reform

While action on phantom traffic and traffic pumping are key parts of any broad reform proposal, in the event that broad reform cannot be implemented, the phantom traffic and access pumping solutions proposed by USTelecom should be put in place on a stand-alone basis.

- **Phantom traffic** is voice calls which are delivered to the terminating carrier that have incomplete, inaccurate or missing signaling data. This can result in the billing of access at a rate lower than the rate appropriate to the jurisdictionalization of the call would warrant, or the inability to bill for the call at all. Such disguise of the proper regulatory classification of traffic, generously characterized as arbitrage, disadvantages other carriers that adhere to the rules, and leads to higher than necessary rates for termination of intercarrier traffic. While unification of terminating rates would help resolve the

⁶ Additional targeted reforms of specific universal service distribution mechanisms were included in the Missoula Plan. Broad reform of universal service distributions has been proposed by the Joint Board and has been the subject of substantial recent comment.

problem of disguising the regulatory classification of traffic, it would not address questions concerning which carrier to bill. USTelecom has proposed a solution to the Commission which would greatly reduce the level of phantom traffic by putting in place some simple rules requiring the provision of call signaling information and providing for negotiated settlement of compensation issues.⁷ Our proposal enjoys broad support.⁸ The Missoula Plan recognized the issue of phantom traffic and recommended a solution. Regardless of the action taken by the Commission on comprehensive intercarrier compensation reform, the Commission should act promptly to adopt the USTelecom phantom traffic proposal.

- **Access pumping** is defined as a form of arbitrage in which a LEC artificially creates enormous increases (pumps) the volume of its traffic in an area with high access charges in order to reap windfall profits. This practice threatens the stability of the intercarrier compensation structure, and USTelecom has advocated speedy resolution of this problem.⁹ Particularly since most access pumping schemes have shifted to the CLEC portion of the industry and because CLEC access charges are not as closely regulated as those of ILECs, the Commission should address access pumping, particularly the rural CLEC access pumping, whether or not it adopts a comprehensive intercarrier compensation solution.
- **ISP Bound Traffic** rules provided a massive arbitrage opportunity that the Commission effectively remedied in a 2001 Order.¹⁰ Absent an order on the Core Petition for mandamus, the Commission's rules would be vacated and that opportunity for arbitrage would return with a vengeance. The Commission should adopt one or more of the legal theories available to it to maintain the current rules for ISP bound traffic. However, consistent with the Missoula Plan which classified all non-ILEC carriers as Track 1, there is no need to retain the mirroring provisions of the Order.¹¹

⁷ See USTelecom *ex parte* filing of February 12, 2008, in CC Docket No. 01-92, *Developing a Unified Intercarrier Compensation Regime*, in which USTelecom identified several reasonable steps that the Commission could and should take immediately to address industry concerns regarding unbillable traffic on the public switched telephone network.

⁸ USTelecom noted in its *ex parte* letter of May 8, 2008, in WC Docket No. 01-92, *Developing a Unified Intercarrier Compensation Regime*, that although there are differences from the USTelecom proposal in some details, all of the following parties (and more) have filed in support of improved call signaling rules: NECA, ITTA, CTIA, NCTA, NARUC, NuVox, XO Communications, One Communications, OPASTCO, Western Telecommunications Alliance, Qwest, The Rural Alliance, Alltel, Cavalier Communications, COMPTEL, GCI, iBasis, Pac-West Telecom, RCN Telecom, VON Coalition, Time Warner Telecom, T-Mobile, USA Datanet, Verizon, Alaska Telephone Association, Sprint/Nextel and Frontier.

⁹ See comments of USTelecom in WC Docket No. 07-135, *In the Matter of Establishing Just and Reasonable Rates for Local Exchange Carriers*, dated December 17, 2007 and Reply Comments of USTelecom dated January 16, 2008 in the same proceeding.

¹⁰ Order on Remand and Report and Order, *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, 16 FCC Rcd 9151 (2001).

¹¹ If however, the Commission decides not to undertake any comprehensive intercarrier compensation reform, and to simply address the ISP Remand Order, the Commission should retain the \$.0007 rate for ISP-bound traffic and the accompanying mirroring rules.

V. Expansion of the USF Contribution Base Facilitates and Is an Integral Part of Comprehensive Intercarrier Compensation Reform

Depending on the settings of the other three “dials,” the size of the ARM will vary. However, there is no doubt that it could add at least several hundred million dollars to the total of funds collected through the universal service contribution mechanism. Expansion of the USF contribution base thus facilitates and is an integral part of comprehensive intercarrier compensation reform.

The best way to expand the USF contribution base and ensure stability of both USF and the ARM is through implementation of a numbers-based approach for collection of funds. There is a broad consensus that the current system of assessing contributions for the universal service fund based on revenues is broken. A numbers-based system of contributions such as the “Direct Universal Service Fund Contribution Methodology” recently submitted to the Commission by AT&T and Verizon, would ensure a more stable USF base, provide simplicity and consistency to consumers, more fairly distribute the contribution burden among providers regardless of technology or platform, and significantly reduce administrative expenses and burdens for the FCC, USAC and contributors.¹² While details continue to be discussed to achieve the greatest level of competitive parity, the mechanism proposed by AT&T and Verizon creates an excellent opportunity for the Commission to act promptly to stabilize the USF contribution system, consistent with the input of affected groups.

The current contribution methodology is outmoded. Today bundled offerings including local and long distance, state and interstate services, and telecommunications services as well as information services make the distinctions required by the current system difficult and confusing. The resulting contribution factor has varied significantly from quarter to quarter and has continued to trend upward at a significant rate.

In contrast, a numbers-based system will be far easier for customers to understand and for providers and regulators to administer and to audit. And residential and lifeline customers actually fare better under this proposal than under the current system. The numbers-based plan will also result in a more stable customer charge and will broaden the base of contributors by capturing all providers of interconnected voice services regardless of technology.

VI. Conclusion

The current regulatory system governing carrier compensation is overdue for reform. We urge the Commission to take this opportunity to provide a more stable footing for the industry to move forward and meet the competitive challenges of providing new and better services to consumers.

¹² See letter from Walter McCormick, dated September 25, 2008, *In the Matter of Universal Service Contribution Methodology*, WC Docket No. 06-122; *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45 to Chairman Martin endorsing a numbers-based Universal Service Fund contributions methodology.