STATE MEMBERS
of the
FEDERAL STATE JOINT BOARD ON SEPARATIONS
1101 VERMONT AVENUE, N.W. SUITE 200
WASHINGTON, D.C. 20005

October 18, 2008

NOTICE OF WRITTEN EX PARTE PRESENTATION (47 C.F.R. § 1.1204(10))

The Honorable Kevin Martin, Chairman
The Honorable Deborah Taylor Tate, Commissioner
The Honorable Michael Copps, Commissioner
The Honorable Jonathan Adelstein, Commissioner
The Honorable Robert McDowell, Commissioner

Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Re: ***In the Matter of Petition of AT&T Inc. for Interim Declaratory Ruling and Limited Waivers Regarding Access Charges and the ESP Exemption,***
CC Docket No. 08-152
In the Matter of IP-Enabled Services,
WC Docket No. 04-36
In the Matter of Developing a Unified Intercarrier Compensation Regime,
CC Docket No. 01-92
In the Matter of Universal Service Contribution Methodology,
WC Docket No. 06-122
In the Matter of Petition for Declaratory Ruling Filed by CTIA,
WT Docket No. 05-194
In the Matter of Jurisdictional Separations & Referral to the Federal-State Joint Board, **CC Docket No. 80-286**

Commissioners,

On September 12, 2008, Verizon filed[1] with the Federal Communications Commission (FCC) an intercarrier compensation reform proposal.[2] Seven days later Verizon provided a white

[1] *September 12, 2008 Letter from Verizon's Susan A. Guyer to FCC Commissioners Martin, Tate, McDowell, Copps and Adelstein*, filed in the proceedings captioned: *In the Matters of Developing a Unified Intercarrier Compensation Regime,* CC Docket No. 01-92, and *Federal-State Joint Board on Universal Service,* CC Docket No. 96-45, (*Verizon Letter*). [Available at <http://fjallfoss.fcc.gov/prod/ecfs/retrieve.cgi?native_or_pdf=pdf&id_document=6520067814>]

[2] The Verizon proposal had a variety of features, including the concept that the FCC would preempt the jurisdictional authority of state commissions so as to implement a uniform, national terminating rate of $.0007 per minute that would be charged for intercarrier compensation by all carriers for all traffic, absent negotiation of a commercial agreement offering a different rate. The proposal included a transition to the $.0007 rate over a period of three years. Carriers would have an

paper outlining legal arguments and factual assertions in support of its proposal.[3] Verizon asserted that providers are unable to distinguish between intrastate and interstate traffic, or between purely circuit switched and IP traffic, and therefore "all traffic that is routed on the PSTN can no longer be reliably separated and treated differently and is therefore inseverable for jurisdictional purposes."[4] Verizon also alleged that the FCC had legal authority to adopt the comprehensive intercarrier compensation reform contemplated in its proposal.[5] Verizon has directly raised the issue of jurisdictional separations in its filings and as a result, we believe a response from the state members of the Separations Joint Board is both necessary and appropriate.

Verizon advances the concept that federal preemption of state jurisdictional authority is justified by a lack of ability to differentiate between local, state, federal, and IP traffic. Verizon argues that if nomadic VoIP and wireless services are increasing in volume, economically inseverable from other traffic, and not subject to the state's economic jurisdiction,[6] then it must also be concluded that "*all* traffic routed over the PSTN is inseverable for jurisdictional purposes."[7] We believe neither point is factually accurate or supported by any record evidence. At a minimum circuit based networks and non-nomadic VoIP continue to be generally distinguishable between the intrastate and interstate jurisdictions, with some exceptions. This is demonstrated by the fact that carriers annually charge substantial amounts of interstate and intrastate access charge fees and continue to bill customers for retail services by jurisdiction. Further, we disagree with and oppose the concept that the FCC should base fundamental changes affecting state preemption and jurisdictional separations on a speculative projection of network evolution and the possibility that some time in the future the majority of traffic will become jurisdictionally inseverable.

We note that Verizon misquotes the FCC decision in Vonage when alleging that all Voice over Internet Propocol traffic is inseverable.[8] The existence of an IP component somewhere along the communications path does not necessarily make the call's jurisdiction difficult to determine. States continue to have authority over fixed origin, traditional local, state access, and intrastate long distance services and possible other intrastate services that may employ an IP transmission component. This authority remains intact unless successfully preempted at the federal level.[9] Such has not occurred, contrary to Verizon's assertions. As each jurisdiction retains authority, jurisdictional separations remain an important policy.

---

opportunity to recover "lost revenues" associated with its proposal through higher retail local rates, higher Subscriber Line Charge (SLC) rate caps, and a new federal Replacement Mechanism universal service fund. *Verizon Letter* at 3-4.

3 *September 19, 2008 Letter from Verizon's Donna Epps to Marlene Dortch FCC Secretary* with attached Memorandum captioned: "*The Commission has Legal Authority to Adopt a Single, Default Rate for All Traffic Routed on the PSTN*" filed in the proceedings captioned: *In the Matters of Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, *and Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, (*Verizon White Paper*), [Available at <http://fjallfoss.fcc.gov/prod/ecfs/retrieve.cgi?native_or_pdf=pdf&id_document=6520169702>]

4 *Verizon White Paper* at 2, (emphasis added).

5 *Verizon White Paper* at 5-29.

6 *Verizon White Paper* at 5-7, 15.

7 *Verizon White Paper* at 4, 10 (emphasis added).

8 Memorandum Opinion and Order, *Vonage Holdings Corp. Petition for Declaratory Ruling Concerning an Order of the Minn. Pub. Utils. Commission,* 19 FCC Rcd 22404 (2004) (*Vonage Order*). The *Vonage Order* concluded that Vonage's "DigitalVoice" service and not generically all intrastate services that may have an IP component could not be separated into interstate and state components. *Vonage Order* at 1.

9 The U.S. Court of Appeals, 8th Circuit in its review of the *Vonage order* stated that "We conclude that the NYPSC's challenge to the FCC's order is not ripe for review. The order only suggests the FCC, if faced with the precise issue, would

Verizon also argues that federal objectives addressing arbitrage and fraud support its proposal. Jurisdictional fraud in one form or another has occurred for years and in and of itself does not warrant preemption. The FCC has adequate enforcement authority to deal with such situations.[10] For example, to the extent that jurisdictional fraud has led to "phantom traffic" or arbitrage, the FCC could require proper labeling of calls. This is a far less intrusive method of addressing fraud and arbitrage concerns than outright preemption of each state's jurisdictional authority over intrastate communications as preserved by under 47 U.S.C. 152(b). We further note that should the FCC require location information for E-911 purposes, this would likely provide at least one method to further identify the jurisdictional nature of calls.[11]

Verizon argues that preemption and effective disregard of separations are warranted to advance important federal objectives, including encouraging efficient investment and use of limited resources.[12] We disagree that the proposed preemption will advance these objectives. Specifically Verizon proposes to set rates that are divorced from costs and separations outcomes. Rates that are divorced from costs will distort competitive markets, send false price signals and lead to uneconomic investment decisions, contrary to all the goals that Verizon purports to advance.[13] Rates that are divorced from costs lead to potential cross-subsidy and market distortions. Rates that are divorced from costs cannot be shown to advance any reasonable federal objective.

Under the Verizon proposal, the traditional jurisdictional cost assignment methodologies under Part 36 are ignored in favor of a $.0007 per minute termination rate, and other changes potentially affecting interstate SLC, the federal universal service fund and local rates. Verizon specifically disregards conventional Part 36 cost allocation procedures and proposes that a new formula for "switched access revenue requirement" be created for rate of return LECs.[14] Such fundamental effects on jurisdictional separations must be reviewed by the Separations Joint Board.

Verizon does not address whether its proposal, as it may affect jurisdictional separations, is contrary to the Supreme Court's instructions in *Smith v. Illinois* regarding appropriate cost assignments.[15] The Supreme Court concluded:

---

preempt fixed VoIP services. Nonetheless, the order does not purport to actually do so and until that day comes it is only a mere prediction." See, *Minnesota Public Utilities Commission v. FCC*, 483 F.3d 570 (8th Cir. 2007) paragraph 48.

[10] For example, in 2005 the FCC rejected an AT&T assertion that its prepaid calling card service was an "enhanced" service, and any call using AT&T's "enhanced" prepaid calling card platform was jurisdictionally interstate, allowing the carrier to avoid payment of state access charges and federal universal service contributions. WC Docket No. 03-133, WC Docket No. 05-68, *Order and Notice of Proposed Rulemaking*, FCC 05-41, released February 23, 2005, at paragraphs 6, 7, 28, and 31.

[11] Verizon also argues that carriers routinely incorrectly bill intrastate access charges or reciprocal compensation charge for jurisdictionally interstate calls. This would suggest that Verizon knows and has itself applied a means for determining the jurisdictional nature of traffic, contrary to its allegations. *Verizon White Paper* at 11.

[12] *Verizon White Paper* at 21.

[13] *Verizon White Paper* at 4.

[14] *Verizon Letter* Appendix at 8-9. Under this proposal the revenue requirement "is the sum of its [the ILEC's] interstate switched access revenue requirement, …its base period intrastate switched access revenue, and base period reciprocal compensation revenue net of reciprocal compensation expenses."

[15] *Smith v. Illinois Bell Tel. Co.*, 282 U.S. 133, 148 (1930).

> The separation of the intrastate and interstate property, revenues and expenses of the company is important not simply as a theoretical allocation to two branches of the business. It is essential to the appropriate recognition of the competent governmental authority in each field of regulation . . . . [T]he validity of the order of the [Illinois] state commission can be suitably tested only by an appropriate determination of the value of the property employed in the intrastate business and of the compensation receivable for the intrastate service under the rates prescribed. <u>While the difficulty in making an exact apportionment of the property is apparent, and extreme nicety is not required, only reasonable measures being essential</u> *it is quite another matter to ignore altogether the actual uses to which the property is put*. <u>It is obvious that, unless an apportionment is made, the intrastate service to which the exchange property is allocated will bear an undue burden to what extent is a matter of controversy</u>.[16]

The above court ruling should not be ignored in light of generalized arguments of potential harm if states continue to regulate intrastate rates.[17]

Some form of jurisdictional separations is necessary because ILECs like Verizon use real, tangible network assets in order to provide various telecommunications and information products and services to their end user and carrier customers.[18] These real assets take the form of facilities, plant, equipment, hardware, software, etc. Verizon's proposal ignores the functional use, nature, and actual investment in plant in favor of its proposed method of compensation. Without consideration of costs of all carriers[19] that would be affected by the Verizon proposal, there is no assurance that Verizon's method is compatible with a reasonable allocation of costs to the state and federal jurisdictions. Even in the current "intermodal competition" legal and regulatory paradigm, ILECs need to recover the costs of their investments in their networks, absent regulatory disallowances or other mitigating circumstances. In this case, to fail to jurisdictionally separate ILEC costs and expenses is to violate the Supreme Court's decision in Smith v. Illinois Bell.

We also note that part of Verizon's proposal preserves "full recovery" by rate of return companies. However the existing separations processes are sorely in need of reform and it cannot be assumed that existing revenues are necessarily reasonable in light of the long-standing jurisdictional separations freeze. It is possible, perhaps likely, that any inequities in intercarrier rates are partly the result of inappropriate separations policies requiring reform.

As a last point, to the extent the FCC determines it will preempt state access charge rate policies, separations changes must occur to ensure that jurisdictional cost assignments are consistent with rate setting authority. States should not be both preempted in setting rates for a service, yet responsible for the cost recovery for that service.

---

16 <u>Id</u>., (emphasis added).

17 *Verizon White paper* at 19-25.

18 ILECs at times assert that they should not be subject to jurisdictional separations requirements because that puts them at a competitive disadvantage with other non-ILEC competitors – e.g., CLEC wireline, cable, and wireless providers. However, we are unaware of any ILEC permanently waiving its right to pursue confiscation claims against a state commission if it believes that its regulated intrastate rates are "too low." Thus, the need for some form of separations remains, at least to the extent a state commission retains some form of regulatory ratemaking authority and the commission is subject to confiscation claims.

19 While primarily only ILECs are subject to separations, all carriers may be affected by the Verizon proposal to the extent the proposal fails to adequately consider their costs but requires their use of a fixed, national rate for termination.

If you have any questions about the positions outlined above, please do not hesitate to contact any of the undersigned or Brad Ramsay at 202.898.2207 or jramsay@naruc.org.

Sincerely,

/s/ Mark K. Johnson, Commissioner

The Honorable Mark K. Johnson
State Chairman, Federal State Joint Board on Separations
Commissioner, Regulatory Commission of Alaska
1016 West 6th Ave., Suite 400
Anchorage, Alaska 99501

/s/ John D. Burke, Esq.

The Honorable John D. Burke
Commissioner, Federal State Federal State Joint Board on Separations
Vermont Public Service Board
112 State Street, Drawer 20
Montpelier, Vermont 05620-2701

/s/ Steve Kolbeck, Commissioner

The Honorable Steve Kolbeck
Commissioner, Federal State Joint Board on Separations
South Dakota Public Utilities Commission
State Capitol
500 East Capitol Avenue
Pierre, SD 57501-5070

/s/ Anthony Palermino, Commissioner

The Honorable Anthony Palermino
Commissioner, Federal State Joint Board on Separations
Connecticut Department of Public Utility Control 10 Franklin Square
New Britain, CT 06051