Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
Lifeline and Link Up	)	WC Docket No. 03-109
Universal Service Contribution Methodology	)	WC Docket No. 06-122
Numbering Resource Optimization	)	CC Docket No. 99-200
Implementation of the Local Competition Provisions in the Telecommunications Act of 1996	)	CC Docket No. 96-98
Developing a Unified Intercarrier Compensation Regime	)	CC Docket No. 01-92
Intercarrier Compensation for ISP-Bound Traffic	)	CC Docket No. 99-68
IP-Enabled Services	)	WC Docket No. 04-36

COMMENTS OF THE TELECOM INVESTORS

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Dated: November 26, 2008

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INTRODUCTION AND SUMMARY

The Telecom Investors are a group of investment firms that, since enactment of the Telecommunications Act of 1996 ("Act"), collectively have invested several billion dollars in companies that compete with incumbent cable and telecommunications companies. The past twelve years have been challenging for the Telecom Investors and their contemporaries, given the boom and bust experience of the industry and the unsettled nature of the underlying regulatory scheme. In spite of this, the Telecom Investors have generally been confident throughout that time that the Commission has been committed to furthering competition in the telecommunications industry in some fashion or another. That confidence, and the confidence of investors in the Commission's commitment to maintaining regulatory stability to foster new investment in competitive providers of telecommunications services is again challenged by the NPRM's proposals to tilt the intercarrier compensation field in favor of the two largest vertically integrated companies in the sector at the expense of smaller competitive entrants.

This regulatory shift is not only contrary to the Act and the purposes for which the Act was created, but it is unsound as matter of economics for the Commission to stifle investment at such a precarious time in the national economy. The loss of investment will decrease, if not eliminate, innovation that relies on capital investment. Because the Commission has recognized that innovation — the "provision of new technologies and services to the public" — best serves the public interest, a reduction in the level of innovation is contrary to the public interest and grounds to reject the radical proposals in the NPRM.[1]

Sound economic principles require that the reciprocal compensation regime provide competitors and their investors with the proper economic signals that will encourage efficient

[1] *See Time Warner Entertainment Co. and US West Communications, Inc.,* 8 FCC Rcd 7106, 7107-8 (1993).

investment choices. Setting a price far below a carrier's actual costs for terminating traffic will create economic distortions and inefficient investment and entry decisions. Nonetheless, the proposed regulatory scheme would force smaller competitors to price their traffic termination service at close to zero, based on the theory that the costs for large vertically integrated companies such as AT&T and Verizon can be used to determine the maximum price competitors charge for terminating other carriers' traffic. But the Commission has previously rejected the concept that costs for terminating traffic is *de minimis*.[2] Likewise the Commission has acknowledged the danger of adopting a structure built around such an invalid assumption.[3] The current proposals include no reasoned explanation for reversing these prior findings.

Adoption of a below-cost rate would create new arbitrage opportunities as carriers seek out customers with disproportionate amounts of outbound traffic. In addition, mandating a below-cost rate would discourage the facilities investment that is necessary for carriers to bring more advanced broadband services to a wider swath of customers because carriers would be unable to recover the full costs of providing facilities-based service.

The Commission has already been warned that its radical reform proposals threaten to further undermine the already fragile state of investor confidence in the telecom sector. As investment analysts Balhoff & Williams and Raymond James & Associates indicated, this radical shift would have dire consequences on the climate for investment across the sector.[4] The

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[2] *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98, First Report and Order, 11 FCC Rcd 15499, 16013 (1996) ("*Local Competition Order*"), at ¶ 1112.

[3] *Id.*

[4] *Ex Parte* Letter from Michael Balhoff, CFA, to Marlene H. Dortch, Secretary, FCC, Docket Nos. 01-92, 99-68, 96-45 and 05-337, at Slide 3 (filed Oct. 28, 2008) ("*Balhoff Analysis*"); "Intercarrier Compensation Reform: Potential Impact From an FCC Order" by Frank G. Louthan IV, Mark DeRussy and Jason Fraser at Raymond James & Associates, Inc., at 3, *attached to Ex Parte* Letter from Joshua Seidemann, Vice President Regulatory Affairs,

key to successful intercarrier compensation reform lies in the Commission's ability to "signal that a reformed system is fair and stable, not arbitrary and politicized."[5] Yet the plan proposed so clearly favors AT&T and Verizon at the expense of the rest of the industry, the only signal provided is that the system is not fair. This will retard investment in an economic climate where investors are already reluctant to part with their money.

It is axiomatic that regulatory stability and predictability are critical to promoting new investment. The analysts agree that "reforms that reduce stability and predictability will precipitate an even more severe reaction to sources of capital in a way that is harmful to customers, policy, the system, and investors."[6] Moreover, the consequences of the Commission's radical surgery would have a cascading effect on investment in the entire sector. As Raymond James analyst Frank Louthan explains, the impact on carriers would be "swift and negative."[7] And the damage would quickly spread to other firms in the sector.[8] The result would be "lower investment, even lower revenue and lower [free cash flow]." As Mr. Balhoff explains "if reforms are not grounded in an understanding of economic realities, the likely outcome is harm—potentially serious harm."[9]

Rather than comment on all of the issues set forth in the three draft items, the Telecom Investors focus on those issues that pose the greatest threat to the stability needed to encourage further investment in competition. The Telecom Investors caution the Commission against taking

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Independent Telephone & Telecommunications Alliance to Marlene H. Dortch, Secretary, FCC, Docket Nos. 01-92, 96-45, and 05-337 (filed Oct. 28, 2008) ("*Louthan Analysis*").

5 *Balhoff Analysis* at 3.

6 *Id.*.

7 *Louthan Analysis* at 3.

8 *Id.*

9 *Balhoff Analysis* at 10.

actions that threaten the regulatory stability and favorable investment climate the sector has enjoyed the last few years. While the Commission should tackle the problems presented by the unchecked growth in the universal service fund, and simplify the byzantine and outdated intercarrier compensation scheme, it should not casually abandon those principles that have proven to work. For instance, the Commission's proposal to abandon the use of the TELRIC pricing methodology for pricing terminating charges is illogical. The states and carriers have over a decade of experience working with the TELRIC standard and have already adopted cost based compensation rates predicated on this principle. The U.S. Supreme Court has affirmed the Commission's use of the TELRIC standard. To invite years of litigation and resulting instability is a solution in search of a problem. The issues of concern to the Commission, namely the arbitrage and intercarrier compensation disputes, are due to the differences between TELRIC compensation rates and higher access charges, not the level of the TELRIC rates set by state commissions.

In addition, the Commission should maintain its existing interconnection rules that have been in place for over a decade. Competitors have constructed networks and developed business practices to work with the RBOCs on exchanging traffic under these arrangements. A shift to new rules will unfairly add costs to competitors' operations and jeopardize the existing interconnection facilities already in place. Similarly, the Commission must forcefully explain that any classification of IP/PSTN traffic does not in any way abrogate the rights of carriers under § 251 and § 252. And finally, any reform of the USF contribution methodology must not discriminate against small businesses that are the engine of innovation and growth in the American economy.

I. A New Approach to Intercarrier Compensation (V.B.2.)

A. Terminating Rates Should Vary by Company Rather than a Statewide Average Rate

The Commission should require states to establish terminating rates on a company-by-company basis, not a statewide basis.[10] Enormous differences exist among service providers due to the provision of different services, geography, and other operational characteristics. A uniform state-based rate cannot reflect these real market distinctions and will certainly benefit the RBOCs which have denser networks that serve more customers.[11] As a result of their monopoly status, the RBOCs can spread the cost of terminating traffic across a broader customer base. CLECs can not. Thus, statewide rates benefit the RBOCs and force CLECs to charge rates that are dramatically lower than their own costs placing them at competitive disadvantage. This obviously tilts the playing field further to the RBOCs advantage.

For example, a recent QSI Consulting study finds that CLECs typically deploy a distributed network architecture that is significantly different from an RBOC network architecture.[12] Under a distributed architecture, the provider substitutes longer transport routes for switching nodes and outside plant facilities, while providing origination and termination services throughout large geographic areas roughly comparable in size to areas served, for

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[10] *See, e.g.*, *Ex Parte* Letter from John Heitmann, Counsel to Nuvox, to Marlene H. Dortch, Secretary, FCC, Docket No. 01-92, at 1-2 (filed Oct. 2, 2008) ("*Nuvox/QSI Analysis Letter*"); *Ex Parte* Letter from Tamar E. Finn, Counsel to PAETEC, to Marlene H. Dortch, Secretary, FCC, Docket No. 01-92, at 1 (filed Oct. 17, 2008) (advocating that intercarrier compensation rates should be based on an *individual carrier's* forward looking costs) ("*PAETEC Letter").*

[11] *See* "Exchange Access Rates for Competitive Local Exchange Carriers, A Basis for Economically Rational Pricing Policies," at 34, *attached to PAETEC Letter*; *See also Ex Parte* Letter from John Heitmann, Counsel to Cavalier Telephone, to Marlene H. Dortch, Secretary, FCC, Docket No. 01-92, at 1-2 (filed Oct. 24, 2008) ("*Cavalier Letter*").

[12] *See* Declaration of August H. Ankum, Ph.D. and Olesya Denney, Ph.D., at ¶ 17, *attached to Cavalier Letter*.

example, by RBOC tandem switches (which aggregate traffic from the RBOC's end office switches).[13] The typical CLEC uses one switch for the same area in which the RBOC has many switches, because the CLEC can expect to serve only a fraction of all the customers in the area. CLECs therefore generally deploy switches that provide a *combined* Class 5 (end office) and Class 4 (tandem) functionality.[14] This network architecture minimizes the amount of switching and central office investment required to serve a more dispersed customer base. On the other hand, it requires additional investments in transport and collocation.[15] Given the traffic-sensitive costs associated with these investments, the typical CLEC network architecture has higher traffic sensitive costs of intercarrier traffic, which should be recognized in terminating intercarrier compensation rates.[16] Given the variables inherent in network design between CLECs, RBOCs and other service providers, the Commission should require states to undertake a carrier-specific review for purposes of terminating rates, not a state-wide approach, which would have the result of ignoring CLEC network architecture and over-emphasize large RBOC economies of scale.

The resulting rates from such a statewide review would most likely not permit smaller competitors, with less dense customer bases, to recoup the cost of terminating traffic from their terminating rate. Instead a statewide rate would likely preclude competitors from recovering their costs and would reduce their ability to attract capital to their networks.

B. The Commission Should Promote Stability and Maintain its Existing Single Point of Interconnection Rules.

The NPRM proposes that at the end of the ten year transition to a uniform terminating rate, it would enforce new default rules regarding where on the network the new uniform

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[13] *See id.*

[14] *See id.* at ¶ 20.

[15] *See id.* at ¶¶ 20-21.

[16] *See id.*

terminating rate would apply. These new default rules, or "edge" rules would supplant the existing framework that allows CLECs to establish one interconnection point per LATA. Under the "edge" rules the RBOC could designate each of its tandem switches in a LATA as an "edge." CLECs would then be obligated to pay additional transport costs plus the unified terminating rate to complete their customers' calls to the RBOC's end users.

Using the single point of interconnection rules, at the end of the Commission's proposed 10 year transition to a unified rate, a CLEC terminating a call to an RBOC would deliver the call to its point of interconnection and pay the unified terminating rate. As Proposals A & C recognize, "[t]he reciprocal compensation rules currently require the calling party's LEC to compensate the called party's LEC for the additional costs associated with transporting a call subject to section 251(b)(5) *from the carriers' interconnection point to the called party's end office*, and for the additional costs of terminating the call to the called party."[17]

But most RBOCs have more than one tandem per LATA and have for years tried to impose a multiple point of interconnection regime on CLECs. The "edge" rules do just that as they would allow the RBOC to designate multiple tandems in a LATA as "edges." Unless a CLEC had a physical interconnection point at each tandem, under the "edge" rules, the RBOC is permitted to charge a dedicated transport charge in addition to the unified terminating rate. This would, in effect, require CLECs to undertake the significant expense of establishing a separate point of interconnection at each RBOC tandem or pay additional transport charges.

Abandoning the single point of interconnection rule in favor of the "edge" rules set forth in the NPRM, will significantly increase costs and place competitive carriers at a significant

[17] Proposal A, n.444; Proposal C, n.435 (emphasis added). *See also* 47 C.F.R. § 51.701(c) ("transport is the transmission and any necessary tandem switching of telecommunications traffic subject to section 251(b)(5) of the Act from the interconnection point between the two carriers to the terminating carrier's end office switch…").

disadvantage. Again the Commission's proposals seek to tread into calm waters that have been well settled for years. The existing certainty and stability of the single point of interconnection rule has allowed competitors to build distributed networks that serve broad geographic markets. Instead of investing large sums of capital in redundant connections to RBOC tandems, CLEC have invested in their own transport and building collocation. Requiring CLECs to adopt the RBOCs' preferred interconnection architecture, and connect at multiple points within the LATA, would drastically increase CLECs' costs making it hard to attract capital and would strand the substantial investments already made in reliance on the single point of interconnection structure. Changing these rules, even if such changes do not occur for another 10 years, threatens the stability investors require and thus jeopardizes future investment.

In addition to raising CLECs costs, the network edge rule is inconsistent with the plain language of the Act. Section 251(c)(2) requires RBOCs to provide interconnection at any technically feasible point requested by CLECs. Proposals A & C[18] ignore Congress' choice to place this obligation on RBOCs. Instead, as initially described by Verizon, these proposals grant the terminating carrier (without reference to its status as an ILEC or a CLEC) the right to demand "at least one [point of interconnection ('POI')] per LATA" and up to as many POIs as the terminating carrier may desire, so long as it does not exceed the number of ILEC tandems in that LATA.[19] The Proposals suggest that they are not inconsistent with the Act and attempt to distinguish a single physical POI from multiple financial POIs.[20] To the contrary, as the Chief of the Wireline Competition Bureau has explained, a proposal to establish a single POI in each

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[18] *See* Proposal A, ¶ 275; Proposal C, ¶ 270.

[19] *Ex Parte* Letter from Susanne A. Guyer, Verizon, to Chairman Martin, *et al*., CC Dockets Nos. 01-92 and 96-45, at 1-2 (filed Sept. 12, 2008).

[20] *See* Proposal A, n.726; Proposal C, n. 717.

LATA "more closely conforms to the Commission's current rules" than a proposal to transfer financial responsibility through multiple virtual POIs throughout a LATA.[21] The current rules recognize and account for differences in RBOC and CLEC network technologies to prevent conferring a competitive advantage on incumbent networks.[22] The edge proposal does just the opposite; it confers a regulatory advantage on RBOC networks. The Proposals offer no principled reason why the Section 251(b)(5) rate should apply at the point of interconnection and cover all transport and termination functions from the POI to the end user for the ten year transition period but then be abandoned when all traffic is unified at a single 251(b)(5) rate. Adopting the edge proposal would reverse the existing framework on which competitors have relied, without the adequate justification required by law and unnecessarily jeopardizing the ability of competitors to compete with the largest RBOC networks and attract capital necessary to continue growing and innovating.[23]

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[21] *Petition of Worldcom, Inc. Pursuant to Section 252(e)(5) of the Communications Act for Preemption of the Jurisdiction of the Virginia State Corporation Commission Regarding Interconnection Disputes with Verizon Virginia Inc. and for Expedited Arbitration*, CC Dockets Nos. 00-218, 00-249, and 00-251, Memorandum Opinion and Order, 17 FCC Rcd 27039, 27063-65, ¶¶ 51-53 (Wireline Comp. Bureau 2002). The Commission declined to address in at least one other proceeding the question of whether so-called financial interconnection points could satisfy the requirements of the Act. *See Application by Verizon Virginia Inc., Verizon Long Distance Virginia Inc., Verizon Enterprise Solutions Virginia Inc., Verizon Global Networks, Inc., and Verizon Select Services of Virginia Inc. for Authorization to Provide In-Region, InterLATA Services in Virginia*, WC Docket No. 02-214, Memorandum Opinion and Order, 17 FCC Rcd 21880, 21977, ¶ 173 (2002) (finding that Verizon had satisfied its interconnection obligations by entering into at least one interconnection agreement that did not mandate multiple points of interconnection for financial responsibility purposes).

[22] *See e.g., Local Competition Order* at ¶ 202.

[23] "[A]n agency choosing to alter its regulatory course 'must supply a reasoned analysis indicating that its prior policies and standards are being deliberately changed, not casually ignored.'" *Action for Children's Television v. FCC*, 821 F.2d 741, 745 (D.C. Cir. 1987) (quoting *Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 852 (D.C. Cir.1970)).

C. The Commission Should Clarify that Classification of IP-PSTN Services As Information Services Does Not Affect LEC Section 251 and 252 Rights and Duties

If the FCC classifies IP-based *services* that touch the PSTN as an information service, it must clarify that LECs' Section 251 and 252 obligations continue to apply.[24] The RBOCs should not be permitted to avoid their obligations under the Act's market opening provisions simply by migrating customers to IP enabled services. Action on this issue is critical to provide the regulatory certainty to investors that continued investment in competitive facilities will not be undermined as services migrate to IP networks. Without such certainty, and without the requested clarification investors will be unlikely to inject capital into such competitive networks.

Consistent with the Commission's emphasis on technology neutral implementation of the Act, a provider's selection of IP based technology to serve a customer should have no bearing on the fundamental interconnection rights and duties associated with the telecommunications input used by the information service to exchange calls with the public network. As the Commission recognizes, by definition an information service includes an underlying "telecommunications" component. Therefore, an RBOC cannot escape its obligation to exchange traffic with other carriers because it moves its voice customers to fixed VoIP services. The Act opened local markets to competition; Congress could not have intended for this achievement to be nullified by an RBOCs choice to migrate their voice customers to information services.

[24] *See Ex Parte* Letter from Russell M. Blau, Counsel to Covad and PAETEC, to Marlene H. Dortch, Secretary, FCC, Docket No. 01-92, Covad Communications Ex Parte Presentation, at Attachment 2 (PAETEC Attachment) (filed Oct. 28, 2008); *Ex Parte* Letter from 360networks(USA), Inc., *et al.* to Kevin Martin, Chairman, FCC, Docket Nos. 01-92 and 04-36 (filed Sept. 29, 2008); *Ex Parte* Letter from Thomas Jones, Counsel for tw telecom, *et al.*, to Marlene H. Dortch, Secretary, FCC, Docket Nos. 05-337, 99-68, 04-36, 01-92 and 96-45 (filed Oct. 24, 2008).

The Commission therefore should re-affirm the *Time Warner Order*[25]and explain that it applies to all carriers. Failure to do so would encourage RBOCs to dispute their Section 251 and 252 obligations with respect to CLECs that provide telecommunications service to VoIP and other information service providers.[26] The classification of VoIP as an information service poses other challenges for competitors. For instance, without further clarification, RBOCs may argue that CLECs are not entitled to 251(a) and (b) rights *to reach the RBOC's VoIP customers*. The legal rationale for mandating interconnection even for with *RBOC* VoIP customers subject to Sections 251(a) & (b) is plain. Even where the LEC is the provider of the information service, some telecommunications must underly that information service. This "telecommunications" enables the Commission "to bring IP/PSTN traffic within the section 251(b)(5) framework."[27] If the Commission fails to address this problem it threatens to undermine the entire competitive framework established in the Act and drive all investment from the competitive sector. Even pure facilities based competitors require the ability to terminate their end users' traffic to end user of other customers. That is the primary purpose of the mandatory interconnection requirements enacted in the 1996 Act. Allowing carriers to refuse to terminate traffic based on the use of IP technology is fundamentally at odds with the core mission of the act and the Commission principle of a technology neutral interpretation of the Act's text.

Failure to clarify these issues will result in endless litigation and disputes that would undermine the market opening provisions of the 1996 Act that have stimulated significant

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[25] *Time Warner Cable Request for Declaratory Ruling*, Memorandum Opinion and Order, 22 FCC Rcd 3513 (2007) ("*Time Warner Order*").

[26] *See, e.g., Petition for Declaratory Ruling Whether Voice over Internet Protocol Services Are Entitled to the Interconnection Rights of Telecommunications Carriers*, Petition for Declaratory Ruling (filed April 11, 2008).

[27] Proposal A, ¶ 218 & n.564; Proposal C, ¶ 213 n. 555.

investment. Investors will not provide new capital unless and until the legal uncertainty is resolved. The 1996 Act was designed not only to open local markets to competition, but also to spur advances in network technologies. As the industry shifts from circuit-switched to managed packet networks, incumbents cannot rely on this transition to escape the market opening obligations of Sections 251 and 252.

II. Additional Costs Standard (V.B.4.)

A. TELRIC Should Not Be Replaced With an Incremental Cost Standard

The Commission should not replace the TELRIC standard with an incremental cost methodology. A number of competitors have submitted record evidence demonstrating that a CLEC's additional costs of terminating telecommunications traffic (regardless of whether it is local, intrastate long distance, interstate long distance, ISP-bound, IP-PSTN, or PSTN-IP) are often many times higher than $0.0007.[28] For instance, as the QSI Consulting study found, "a rate equal to $0.0007 would fall far short of properly compensating Nuvox for the capital it has deployed and the expenses it incurs in transporting and switching voice-related services."[29] And any order that requires CLECs to provide below-cost termination services to IXCs and shift the un-recovered costs of IXC traffic termination to their local end user customers violates the Act.[30] Further, AT&T and Verizon's costs for terminating traffic cannot reasonably be relied upon as evidence of the true industry costs of terminating telecommunications traffic due to their size and economies of scale.[31] "[E]ven the largest, most efficient CLECs trail substantially behind AT&T

[28] *See* Declaration of Michael Starkey, at ¶ 8, *attached to Ex Parte* Letter from John Heitmann, Counsel to Nuvox, to Marlene H. Dortch, Secretary, FCC, Docket No. 01-92 (filed Oct. 2, 2008) ("*Starkey Analysis*"). *See, e.g., Nuvox/QSI Analysis Letter,* at 1-2, *PAETEC Letter* at 1; *See also Cavalier Letter*, at 1-2 .

[29] *See Starkey Analysis*, at ¶ 8.

[30] *PAETEC Letter*, at 2.

and Verizon with respect to economies of scale required to produce per-minute-of-use costs anywhere near the $0.0007 figure proposed by certain parties in this proceeding."[32]

B. The Commission Lacks Statutory Authority to Dictate the Results of a State Commission 252(d)(2) Cost Proceeding

In addition to suffering from a lack of rational economic analysis and poor public policy, Proposals A & C go well beyond the boundaries of adopting a cost methodology and are unlikely to survive judicial review. Because the Proposals specify the inputs state commissions must use and dictate the resulting rate, they run afoul of the same statutory limitations that doomed the proxy prices established in the *Local Competition Order*.[33]

Federal law restricts how far the Commission can go in establishing a pricing methodology, and the Proposals clearly cross that line.[34] By requiring state commissions to use the forward-looking network design of softswitches and fiber transport,[35] and threatening to set the rate if the state commission proceeding does not result in a rate close to zero,[36] the Proposals

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[31] *See id.* at 3.

[32] *Id.*

[33] The United States Court of Appeals for the Eighth Circuit, upon remand from the U.S. Supreme Court, vacated the Commission's default proxy prices, relying upon the Supreme Court's determination that the Commission's role was limited to resolving "general methodological issues," finding that "[s]etting specific prices goes beyond the [Commission's] authority to design a pricing methodology," and concluding that such an approach would "intrude[] on the states' right to set the actual rates." *Iowa Utils. Bd. v. FCC*, 219 F.3d 744, 757 (8th Cir. 2000), *aff'd in part and rev'd in part, Verizon Comm's, Inc. v. FCC*, 535 U.S. 467 (2002), and *vacated in part*, *Iowa Utils. Bd. v. FCC*, 301 F.3d 957 (8th Cir. 2002).

[34] *AT&T v. Iowa Utils. Bd.*, 525 U.S. 366, 384 (1999).

[35] *See* Proposal A, ¶ 272; Proposal C, ¶ 267 ("We offer further guidance regarding specific aspects of these cost studies. First, these cost studies must use the least cost, most efficient network technology. We find that the least cost, most efficient switch today is a softswitch. We further find that the least cost, most efficient technology for transport is fiber optic cable. We observe that, when carriers deploy fiber, they typically deploy capacity significantly in excess of current needs.").

[36] Proposal A, ¶ 215; Proposal C, ¶ 215.

do not allow the state commissions to "determin[e] the concrete result." As drafted, the Proposals put the states in the position of doing little more than ratifying the Commission's rate-setting mandate. This is flatly prohibited under the Act.[37]

The Eighth Circuit, in confirming the Commission's authority to resolve "general methodological issues,"[38] cited the Commission's explanation of its TELRIC pricing standard as "a methodology for state commissions to use in completing the 'critical and complex task of determining the economic costs of an efficient telephone network.'"[39] Thus, as the Eighth Circuit ultimately determined, "it is the state commission's role to exercise its discretion in establishing rates."[40] Because the Proposals limit state commission discretion to choose inputs and are contrary to the principles by which this Commission defended TELRIC nearly a decade ago, they run significant risk of failure on appeal.[41]

III. REFORM OF UNIVERSAL SERVICE CONTRIBUTIONS (IV.)

A. Contribution Assessment Methodology for Business Services (IV.B.3.)

1. Hybrid Numbers and Connection Fees Would be Discriminatory and Inequitable to Small Businesses

The Telecom Investors oppose a hybrid numbers/connection system with disproportionately high connection fees for small business services. Under the USF methodology included in Proposal B, carriers would be required to contribute:

- $0.85/month per number (residential & business, including wireless)

[37] *Iowa Utils. Bd. v. FCC*, 301 F.3d 957 (8th Cir. 2002).

[38] *Iowa Utils. Bd. v. FCC*, 219 F.3d at 757.

[39] *Id*. at 756 (quoting Reply Brief of the Federal Petitioners, Cases Nos. 97-826, *et al*. United States Supreme Court, at 7).

[40] *Id*. at 757 (citation omitted).

[41] *See also Federal Power Comm'n v. Hope Natural Gas Co.*, 302 U.S. 591, 602 (1944) (contrasting the "method employed" with the "result reached" in setting "just and reasonable" rates).

- $5.00/month per Business Connection, up to 64 kbps
- $35.00/month per Business Connection, above 64 kbps
- Mobile services are not "Assessable Connections"[42]

This would be catastrophic for small businesses that are a significant base of customers for competitive entrants. For example, assume a small business uses one DSL line at $70.00 per month. Today, the USF contribution for that line would be approximately $8.05 (11.5% of the $70 monthly service charge). Under Proposal B, however, the USF contribution for that line would be $35 (and a total charge of $105 per month), resulting in a USF contribution increase of approximately 335%, and a total cost increase of 34.5% (from $78.05 to$105). The effective universal service contribution rate for that DSL line under Proposal B would be 50%.[43] Whether a small business uses a DSL service, or an integrated T-1 service that delivers voice, data, and Internet access services, the results are the same.[44] Small businesses will bear the brunt of USF funding under Proposal B.

Such a drastic rate increase, and resulting effective contribution rate, would be unlawful under the Act. Section 254(d) of the Act requires that the Commission establish universal service contributions on an "equitable and nondiscriminatory basis." Proposal B is inequitable to the extent that a small business purchasing a DSL connection would pay the same as an enterprise customer that utilizes a DS3 Internet connection.[45] Further, it is discriminatory, as it would

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[42] *See* Proposal B, ¶¶ 81-82.

[43] *See, e.g., Ex Parte* Letter from Russell M. Blau, Counsel to Covad and PAETEC, to Marlene H. Dortch, Secretary, FCC, Docket No. 01-92, at Covad Communications Ex Parte Presentation (filed Oct. 28, 2008).

[44] *See generally Ex Parte* Letter from Stephen W. Crawford, General Counsel and Senior Vice President, Alpheus Communications, L.P., to Marlene H. Dortch, Secretary, FCC, Docket Nos. 06-122 & 96-45 (filed Oct. 228, 2008); *Ex Parte* Letter from Mary C. Albert, COMPTEL, to Marlene H. Dortch, Secretary, FCC, Docket No. 06-122 & 96-45 (filed Oct. 22, 2008).

[45] *See id.*

require wireline and fixed wireless connections to pay contributions, but would not require contributions from mobile wireless connections, including broadband.[46] Finally, massive (50%) rate increases for small businesses are poor public policy generally, but especially so in these troubled economic times. A 35% cost increase for DSL would force many businesses off the Internet. Proposal B would impact approximately 4.8 million business broadband users[47] to the tune of a $1 to 1.5 billion per year cost increase. Such a dramatic rate increase for small businesses would be unfair, discriminatory, inequitable and contrary to the Act. Such a drastic shift of USF burdens on these customers is likely to drive them away from the more robust and innovative services they receive from competitive entrants. Of course the Commission wants to encourage more access to broadband and not less which would be the result of this proposal.

CONCLUSION

For the aforementioned reasons, the Telecom Investors urge the Commission not to adopt any reforms to intercarrier compensation or universal service that jeopardize the regulatory stability necessary to encourage further investment in competitive telecommunications networks and to ensure that any such reforms are implemented in a competitively neutral and fair manner.

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[46] *See id.*

[47] *See FCC, Trends in Telephone Service,* Table 2.2 (Total Advanced Service Lines) and Table 2.4 (Residential Advanced Service Lines), August 2008 (data as of June, 2007), *available at*: http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-284932A1.pdf.

Respectfully submitted,

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Dated: November 26, 2008