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. 65-45**
	)	
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	)	**CC Docket No. 96-98**
Act of 1996	)	
	)	
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 EMBARQ

Embarq Local Operating Companies
By its Attorneys:

David C. Bartlett
Jeffrey S. Lanning
John E. Benedict
701 Pennsylvania Ave., NW
Suite 820
Washington, DC 20004
202-393-1516

November 26, 2008

TABLE OF CONTENTS

I.	INTRODUCTION AND SUMMARY			1
II.	EMBARQ SUPPORTS REALISTIC REFORM.			5
III.	REFORM OF HIGH COST UNIVERSAL SERVICE SUPPORT.			8
	A.	Embarq Has Offered a Better Approach for Targeted Universal Service Support.		8
	B.	The Commission's Proposals Would Unfairly and Unreasonably Force ILECs to Cross-Subsidize High-Cost Customers.		10
	C.	The Commission's Rationale for USF Reverse Auctions is Flawed.		12
	D.	The Commission's Suggestion that Dividend-Paying Carriers Warrant Less Universal Service Support is Unreasonable.		14
IV.	REFORM OF UNIVERSAL SERVICE CONTRIBUTIONS.			17
V.	REFORM OF INTERCARRIER COMPENSATION.			19
	A.	Commission Must Reaffirm its Long-Standing End-to-End Analysis.		19
	B.	The Commission's Intercarrier Compensation Reform Proposal.		22
		1.	A Few Targeted Improvements Can Produce Significant Benefits.	22
		2.	Rate Unification by Local Carriers Within Study Areas Makes Sense; a Single, Industry-Wide Rate Does Not.	23
		3.	Rate Disparities for Voice Traffic Between Technologies Stifle Broadband Development and Investment.	25
		4.	Recovery of Displaced Revenues is a Vital Component of Any Intercarrier Compensation Reform Plan; Recovery Mechanisms Must be Sufficient and Reliable.	25
		5.	The Proposed Rate of $0.0007 Per Minute is Arbitrary and Unlawful.	26

C.	Legal Authority.		27
	1.	The Proposed Rules Reflect an Unlawful Abdication of the Commission's Statutory Obligations Under Section 254(g).	28
	2.	The Act Does Not Give the Commission Authority to Broadly Preempt State Regulatory Authority Over Intrastate Traffic.	29
	3.	The Commission Lacks Jurisdiction Over Intrastate Traffic.	35
	4.	The Commission Cannot Lawfully Conclude that IP/PSTN Traffic is an "Enhanced Service."	35
D.	Additional Costs Standard.		42
	1.	The Proposed Order is Wrong to Suggest the TELRIC Cost Standard Has Been a Failure on Reciprocal Compensation Traffic.	43
	2.	The Proposed Incremental Cost Methodology is Unreasonable, Because It Leaves Recovery of Legitimate Costs in Jeopardy.	44
	3.	It is Premature to Propose Use of Soft Switch Technology as the Technology for Cost Purposes.	49
E.	Implementation -- Direction to the States.		51
	1.	The Commission's Default Network Edge Rule on Direct and Indirect Interconnection Contradicts Section 251.	51
	2.	A Decision on Symmetry Rules Is Premature.	51
	3.	Existing Agreements Should Be Orderly Transitioned to Any New Rules.	52
F.	Implementation -- Revenue Recovery Opportunities.		53
	1.	Excessive Reliance on SLCs is Inappropriate for Access Recovery.	53
	2.	Universal Service Support Should Not be Denied Because a Carrier Earns Profits in Other, Unregulated Lines of Business.	54

	G.	Measures to Ensure Proper Billing.		55
		1.	Phantom Traffic Reform is a Necessary Component of Intercarrier Compensation Reform.	55
		2.	The Commission Needs to Act to Reduce the Problem of Phantom Traffic to Enable Proper Billing.	56
		3.	Financial Obligations Must be Reasonably Balanced Between Tandem Owners and Carriers Using Tandem Services.	58
VI.	FURTHER NOTICE OF PROPOSED RULEMAKING.			62
	A.	Universal Service Further Notice.		62
	B.	Intercarrier Compensation Further Notice.		64
		1.	The Commission Should Not Establish Default Transit Rates, but Should Direct Users and Providers to Negotiate Agreements for Transit Services.	64
		2.	Providing Transit Services is Not a Statutory Obligation.	65
		3.	The Commission Should Affirm that Competitive Carriers are Financially Liable for Traffic Exchanged Indirectly with a Rural Carrier.	65
VII.	CONCLUSION			66

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. 65-45**
	)	
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 EMBARQ

I. INTRODUCTION AND SUMMARY

Embarq respectfully provides these comments on the recently-released *Order on Remand and Report and Order and Further Notice of Proposed Rulemaking* (FNPRM) in the above-captioned dockets.[1] Embarq agrees with the Commission's statements that the

[1] Public Notice, DA 08-2486 (rel. Nov. 12, 2008); *Order on Remand and Report and Order and Further Notice of Proposed Rulemaking,* FCC 08-262 (rel. Nov. 5, 2008)

broadband era is here.[2] It also agrees with Commissioner Copps when he asks two key questions:

> [D]oes America at the beginning of the 21st century become technologically stagnant or the leader of the Digital Age? For me the answer to that question depends in some significant measure upon whether we succeed in bringing high speed, high-value broadband … to all Americans … rural as well as urban folks….[3]

Embarq fully supports the continued expansion of broadband services. It is very concerned that the proposals as outlined in Appendices A, B, and C ("the proposed order") would not only frustrate the expansion of broadband services, but would also place existing rural network integrity at risk and threaten to ultimately cripple or even bankrupt carriers serving rural areas.

Despite the Commission's statement that "Congress's vision has been largely realized,"[4] the promise of the Telecommunications Act of 1996[5] is incomplete for many rural Americans. Rural customers are still waiting for explicit funding to replace the vast amounts of lost implicit support that has been eroded by competition in urban and suburban areas over the last twelve years. The Commission has an obligation to provide

---

("FNPRM"). *See 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 03-109); *Universal Service Contribution Methodology* (WC Docket No. 06-122); *Number Resource Optimization* (CC Docket 99-200); *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996* (CC Docket 96-98); *Developing a Unified Intercarrier Compensation Regime* (CC Docket No. 01-92); *Intercarrier Compensation for IP-Enabled Services* (CC Docket No. 99-68); *IP-Enabled Services* (Docket No. 04-36).

[2] FNPRM at App. A ¶ 19, App. C ¶ 19.

[3] Remarks of Commissioner Michael J. Copps, Pike & Fischer's Broadband Policy Summit IV, Washington, DC (June 12, 2008), available at http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-282890A1.pdf.

[4] FNPRM at App. A ¶ 2, App. C ¶ 2.

[5] Pub. L. No. 104-104, 110 Stat. 56.

this explicit funding. Millions of urban and suburban customers enjoy the benefits of competition. However, this competition has eroded the implicit support relied upon by rural Americans, effectively funding the benefits of competition at their expense. Such a result is inequitable and, unless offset by comparable revenue opportunities, it is also a violation of the Communications Act.

Accordingly, the proposed order would be counterproductive. It further reduces implicit support and fails to assure the additional funding required to provide government-mandated, below-cost service in high-cost rural areas. This would represent an abdication of the Commission's responsibilities under section 254 of the Communications Act.[6] Moreover, the proposed order is profoundly unfair to mid-sized price cap carriers serving rural areas, like Embarq. It will directly harm millions of rural consumers by denying them broadband services and placing their existing service offerings and reliability at-risk.

Beyond being counterproductive and contrary to the interests of consumers, the proposed order is likely to be reversed and remanded. The proposed order exceeds the Commission's jurisdiction and legal authority by a wide measure. It disregards inconvenient facts and precedent and ignores the statutorily recognized interests of states and the Joint Boards. All in all, the proposed order's approach to high cost universal service reform and intercarrier compensation restructuring is arbitrary and capricious in many ways, and cannot be expected to withstand appeal.

---

[6] 47 U.S.C. § 254.

Embarq agrees reforms are necessary. It has supported the Missoula Plan,[7] worked with other industry segments, consumer groups, and regulators to find solutions, and, most recently, it has worked with ITTA and USTelecom on workable proposals that have broad industry support. Clearly, the proposed order must be revised to produce the proper funding, economic incentives, and regulatory oversight necessary to meet statutory obligations and to produce the desired reform outcome.

Accordingly, Embarq opposes the proposed order as currently written or, more specifically, Appendices A, B, and C to the FNPRM.[8] Further, Embarq believes it is clear the additional cost standard utilized under section 252(d)(2) of the Act[9] should remain the existing, proven TELRIC standard. The incremental cost methodology proposed in the draft order is unreasonable, under-compensates local carriers, will discourage investment, and frustrate universal service goals.[10] Finally, the terminating rate for section 251(b)(5)[11] traffic should be set by each operating company, not set as a single statewide rate.[12]

---

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

[8] FNPRM at ¶ 40.

[9] 47 U.S.C. § 252(d)(2).

[10] FNPRM at ¶ 41.

[11] 47 U.S.C. § 251(b)(5).

[12] FNPRM at ¶ 41.

II. EMBARQ SUPPORTS REALISTIC REFORM.

The Joint Statement of Commissioners Michael J. Copps, Jonathan S. Adelstein, Deborah Taylor Tate, and Robert M. McDowell issued with the FNPRM represents significant agreement, not just among those four Commissioners but also with the principal goals and framework put forth by Chairman Kevin J. Martin. This should provide important guidance, perhaps even a roadmap for Commission action on comprehensive reform of intercarrier compensation and universal service support to high-cost areas.

The four Commissioners issued a joint statement, in which they wrote:

> While we do not pre-judge any of the proposals set forth therein, we do believe that there is a tentative but growing measure of consensus on a number of issues.… We would appreciate stakeholders' attention to these issues of concern and consideration of whether modifications along these lines to the attached proposals are warranted.

The issues upon which the four Commissioners appear to agree are:

(a) Moving intrastate access rates to interstate access levels over a reasonable period of time;

(b) Not unduly burdening consumers with increases in their rates untethered to reductions in access charges;

(c) Addressing phantom traffic and traffic stimulation;

(d) Implementing an alternative cost recovery mechanism in certain circumstances;

(e) Eliminating the identical support rule and moving over time towards support based on a company's own costs;

(f) Emphasizing the importance of broadband to the future of universal service; and

(g) Clarifying the implementation of the Alaska Native regions and tribal lands exception to the CETC cap adopted on May 1, 2008, and the need for special consideration for such areas.

These principles are based in sound policy choices and, as the four Commissioners stated, nearly everyone can agree about the steps they identify. Certainly, some parties would desire greater benefits to accrue to their benefit, but no one can deny that the four commissioners have identified a package that represents substantial progress when compared with the current environment. For example, simply taking the first step of reducing intrastate access rates to interstate access levels will cut intercarrier compensation expense in Embarq study areas by over 50%.

Embarq and other mid-size incumbent local exchange carriers ("ILECs") are particularly impacted by intercarrier compensation reform as they typically serve mostly rural, high-cost areas and historically have been compensated for this public service through implicit support in access charges (both at the federal and the state level). Moreover, mid-size ILECs typically realize less benefit from access charge reductions, as they are not integrated with large purchasers of access services, such as interexchange carriers ("IXCs") or commercial mobile radio service ("CMRS") providers. As mentioned above, Embarq and other mid-size ILECs have several substantial disagreements with the policies and decisions in the proposed order. These areas of disagreement are described in subsequent sections of these comments.

Embarq and other mid-sized ILECs have taken the guidance of the four Commissioners and the Chairman of the Commission, and they have worked actively within other carriers and industry segments to develop proposals that could modify the proposed order to make it workable and achieve positive and substantial intercarrier compensation reform, which is a goal Embarq and mid-size ILECs share with most of the industry, regulators, and consumer groups.

Two proposals in particular appear promising based on the work that has been done so far—ones being put together by the United States Telecom Association ("USTelecom") and the Independent Telephone and Telecommunications Alliance ("ITTA"). It is expected that both proposals will be filed with the Commission as a part of this round of comments, and Embarq anticipates supporting both of them.

Embarq anticipates, based on the work that has been done within the associations, that the USTelecom and ITTA proposals will be very similar. At their core, they both strongly reflect the guidance in the Joint Statement by the four Commissioners. They also work within the framework of the proposed order rather than seeking to abandon the good work that has gone into that effort. Accordingly, Embarq anticipates that it will support both proposals and urge the Commission to adopt either one or to do something else that contains the same common elements. Those common elements, which the Commission should adopt as modifications to the proposed order are:

1. Reduce intrastate access rates to company-specific interstate rate levels (either actual rates or target rates set pursuant to price cap regulation) over a three-year period;

2. Permit ILECs (which are subject to both rate regulation and carrier-of-last-resort obligations to serve high-cost areas) to increase residential subscriber line charges ("SLCs") by as much as $0.50 per year ($1.50 total), and business SLCs by $0.77 per year ($2.30 total), to offset intrastate access revenue reductions;

3. Permit ILECs to recover access reductions (net of SLC increases) through increased support from the appropriate federal access replacement mechanism (Interstate Access Support or "IAS" for price-cap regulated ILECs and Interstate Common Line Support or "ICLS" for rate-of-return regulated ILECs);

4. Commence a further rulemaking proceeding and referral to the Federal-State Joint Board on Universal Service to determine the next steps toward unifying rates for all terminating traffic, evaluating the appropriate cost standard for such traffic, and providing appropriate

replacement mechanisms to offset further reductions in access revenue (and reciprocal compensation revenue should such reductions be ordered as well);

5. Require parity in the treatment of voice traffic such that all voice traffic, including calls originated with or terminated with Internet Protocol, pay the same charges based on jurisdiction (i.e., local, intrastate access, or interstate access);

6. Establish clear rules regarding signaling obligations and other measures to reduce phantom traffic, such as the USTelecom proposal; and

7. Take steps to reform the distribution of federal high-cost support in price-cap study areas to calculate and distribute such support more granularly so that support is targeted more appropriately to truly high-cost areas rather than requiring customers in the low-cost (and often competitive) parts of study areas to subsidize customers in the high-cost parts of study areas.

If the Commission makes these modifications, it will achieve substantial reform to the benefit of all consumers, including those living in rural areas, and we will all long look back on this as major accomplishment. On the other hand, if the proposed order is adopted as written, intercarrier compensation reform will not be remembered fondly because of the range of significant policy and legal problems associated with it.

III. REFORM OF HIGH COST UNIVERSAL SERVICE SUPPORT (FNPRM ¶¶ 4-59).

A. Embarq Has Offered a Better Approach for Targeted Universal Service Support.

Embarq supports the dual goals contained in the universal service proposals outlined in each of the appendices to the FNPRM. Those goals — promoting the deployment of broadband services while controlling the overall size of the fund — are the same two goals that led Embarq to propose its Broadband Carrier of Last Resort Solution ("BCS") on September 18, 2008.[13]

In the BCS proposal, current support dollars were re-calculated and re-distributed on a targeted basis, and carriers receiving those dollars were required to provide broadband service to the majority of customers in the supported areas. On its surface, Embarq's BCS proposal might appear similar to the proposals contained in Appendix A and Appendix C. Under the BCS proposal, receipt of federal support dollars is contingent on increased broadband deployment. However, there are significant differences between the two approaches, and those differences ultimately render the proposals in Appendix A and Appendix B not only unworkable, but contrary to the specific requirements contained in section 254 of the Act.

The existing mechanism for distributing federal Universal Service Fund ("USF") dollars has created a situation where current federal funding is insufficient. Specifically, the use of study area averaging has created and exacerbated this insufficiency. As correctly described in Embarq's comments filed on April 17, 2008, the current mechanism perpetuates monopoly-era assumptions regarding cross-subsidization, and propagates the myth that companies can rely on revenues earned in low-cost areas to offset costs incurred in high-cost areas. The Commission itself, in previous orders in this docket, has acknowledged that these cross-subsidies are unsustainable in a competitive market.

---

[13] *See* Letter from David Bartlett (Embarq) to Marlene Dortch (FCC), *High Cost Universal Service Support*, WC Docket No. 05-337, *Federal State Joint Board on Universal Service*, CC Docket No. 96-98 (filed Sept. 18, 2008).

B. The Commission's Proposals Would Unfairly and Unreasonably Force ILECs to Cross-Subsidize High-Cost Customers.

The proposals outlined in Appendix A and Appendix C maintain the reliance on these unsustainable cross-subsidies by using existing levels of support as a starting point. The proposals argue that in order for a company to continue to receive its current level of funding—an amount that is already insufficient for many companies—the company must provide broadband service to all of the customers in its serving areas within five years. The incongruity of this requirement is obvious. Since current support amounts are insufficient for the existing list of supported services, they can only be more insufficient when additional services are added to the list.[14] This is all the more remarkable given that the Commission has not determined that broadband is to be classified as a supported service under section 254.

The magnitude by which support becomes even more insufficient, in the face of the Commission's proposed broadband obligation, is enormous. Embarq has estimated that the initial costs to deploy broadband to every one of the customers in its serving territory would be, collectively, more than twenty times the amount of high-cost support the company receives on an annual basis. And since the Commission's proposals do not allow for the use of satellite technology to meet this requirement, there is no potentially lower cost alternative available.

[14] Embarq's BCS proposal avoided this problem by increasing the amount of support available to carriers in exchange for increasing the carriers' obligations. These increased support amounts were dollars that were "freed up" by the elimination of wireless access replacement support, consistent with the Commission's tentative conclusion in its earlier FNPRM. *See High Cost Universal Service Support*, WC Docket No. 05-337, *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Notice of Proposed Rulemaking, FCC 08-4 (rel. Jan. 29, 2008).

In addition, those costs reflect only initial deployment of capital. It has been well-documented that the recurring costs associated with broadband service — particularly the costs of backhaul across long stretches of rural network — are often prohibitive even if the initial deployment costs might be manageable in an area. The proposals contained in Appendix A and Appendix C ignore the consequences of these additional recurring costs.

Embarq acknowledges and agrees with many of the specific points cited in the proposals as the incentive for increased broadband deployment. Universal service is indeed "an evolving level of telecommunications services," and broadband is necessary to ensure that "our Nation remains competitive and continues to create business and job growth."[15] In addition, it is correct that the broadband subscription rate tends to be lower in rural regions.[16] However, while these facts may justify some form of intervention on the part of the Commission with regard to broadband, they do not justify the specific obligation outlined in Appendix A and Appendix C. The obligation to provide broadband with no additional support dollars amounts to nothing more than an unfunded mandate. It is inconsistent with Commission precedent, and the proposed order does not explain why. The Commission does not have authority to "condition" the receipt of high-cost dollars -- including support for which carrier currently qualify -- on carriers' complying with this unfunded mandate.

Additionally, the proposed order erroneously concludes that "making an offering of broadband Internet access service a condition of receiving universal service high-cost support can bring this critical service to the remainder of Americans who await its

---

[15] FNPRM at App. A ¶¶ 21, 22 and App. C ¶¶ 21, 22.

[16] *Id.* at App. A ¶¶ 23 and App. C ¶ 23.

deployment."[17] Such a conclusion would make sense if the benefits of complying with the unfunded mandate exceeded the cost; in other words, if what a company would lose by not offering broadband (its current USF receipts) was greater than the cost of meeting the requirement. However, in most cases it is likely — as is the case for Embarq — that the cost of complying with the mandate so greatly exceeds the benefit that it would be a breach of fiduciary duty for Embarq's management even to attempt to comply. As a result, the Commission will have failed in its efforts with regard to broadband and with regard to its obligation to create a sufficient mechanism to ensure the provision of the existing list of supported services.

C. The Commission's Rationale for USF Reverse Auctions is Flawed.

The proposals outlined in Appendix A and Appendix C show that in areas where incumbent LECs are unable to meet the broadband commitment a "reverse auction" would be conducted.[18] The purpose of this auction would be to award high-cost support to a bidder — other than the incumbent — that ostensibly would commit to assume carrier of last resort obligations and also promise to offer broadband throughout the study area. However, it is important to note that the proposed order's justification for the use of auctions falls apart under examination.

The proposed order argues that a support mechanism based on cost or a cost model provides no incentive for an ETC to provide the supported services at the minimum possible cost.[19] It argues further that an auction mechanism is appropriate because the winning bid should approach the minimum level of support required "to

[17] *Id.*

[18] *Id.* at App. A ¶ 31, App. C. ¶ 31.

[19] *Id.* at App. A ¶ 33, App. C ¶ 33.

achieve our universal service goals." The first flawed assumption in this argument is that the proposed broadband obligation has the effect of *expanding* "our universal service goals" to include heretofore unsupported services, while the establishing of a reserve price at current funding levels prevents the amount of available support from *expanding* to cover the costs of providing this additional service.

In essence, the proposed order seems to be operating under the assumption that an auction mechanism will reveal that there is some other provider, somewhere, that is capable of offering ubiquitous broadband in the most rural, high-cost regions of the nation, for less support than an ILEC requires to provide ubiquitous voice service. If this assumption were correct, this provider would have long ago stepped forward as a C-ETC, since voice is simply one application on a broadband network, and such a provider could have easily been receiving USF support equal to the incumbent's support all along.

The second flawed assumption in the proposed order's justification for auctions is the notion that current support mechanisms do not provide adequate incentives for carriers to operate efficiently, and that an auction mechanism would provide this incentive. As outlined in detail in Embarq's BCS filing, there is a significant difference between carriers that operate under price cap regulation and carriers that operate under rate of return regulation. Regardless of the way the federal USF mechanism is structured, price cap carriers have every incentive to operate as efficiently as possible since it is only through their increased efficiency that they are able to earn an economic return. Price cap carriers have a fiduciary duty to achieve maximum levels of efficiency, even if the existing federal USF mechanisms are based on costs or cost models. This is why it is logically appropriate to establish *different* support mechanisms for price cap and rate of return carriers, which was the foundation of Embarq's proposed BCS plan.

The third flawed assumption is manifest in the proposed order's proposals, when it describes the (hypothetical) transition from supporting an ILEC to supporting another carrier that "wins" an auction.[20] In this paragraph, the proposed order notes that the winning bidder would take on the carrier of last resort obligations imposed at both the state and federal levels, and that the "losing" ILEC would be relieved of those same obligations. The first problem with this assumption is that it is unclear whether the Commission has the authority to relieve a carrier of COLR obligations that are imposed at the state level, particularly when many carriers are designated (at the state level) as public utilities. The second problem with this assumption is one of stranded investment. Because ILECs have been *required* to spend decades and billions of dollars building and operating ubiquitous networks, carrier-of-last-resort "relief" for much of the ILEC's serving territory is illusory. Having already incurred the cost of putting the network in place, the incumbent is hardly in a position to walk away from its investment even if granted such "relief."

D. The Commission's Suggestion that Dividend-Paying Carriers Warrant Less Universal Service Support is Unreasonable.

The proposed order includes a discussion about the fact that certain carriers -- specifically price cap carriers, including Embarq -- pay dividends to their shareholders.[21] The Commission also notes that certain commenters have identified this as a "concern" to be weighed carefully when evaluating the need for universal service support. Embarq

[20] *E.g.,* FNPRM at App. C ¶ 41.

[21] *Id.* at App. A ¶¶ 312-314, 324, App. C ¶¶ 307-09, 319.

welcomes the opportunity to point out that such "concerns" demonstrate a serious misunderstanding of the role that dividends play in capital markets.[22] Such "concerns" are often based on a misperception that because a company pays dividends to its shareholders, somehow it does not need universal service support.

In any publicly traded company, part of the cost of doing business is the cost associated with providing a reasonable return to investors. Indeed, in the Commission's own high-cost model, the Synthesis Model (also referred to as HCPM), a reasonable return is built into the cost calculation. For equity investors, that return can either come in the form of an increase in the value of shares (i.e., capital appreciation) or it can come through dividend payments. Otherwise, it could come in the form of a stock buy-back, in which the value of shares increases through the reduction in the number of outstanding shares.

Generally, capital appreciation is the type of return associated with growth companies. If the company faces numerous growth opportunities, earnings are best utilized by reinvestment them in the firm to take advantage of such opportunities, and the increased stock price will reflect the expected earnings of these new growth projects. Alternately, dividend payments and stock buy-backs are characteristic of ILECs, given their companies typically may face declining growth opportunities. The dividends paid to shareholders are an integral -- and necessary -- part of the process by which these firms

---

[22] Embarq, a publicly held company, pays a reasonable dividend typical for carriers in its class. Its typical dividend is roughly comparable to that paid by other carriers, including larger, integrated carriers. At the same time, Embarq actually receives comparatively little universal service support. It is a rural carrier in 17 of the 18 states in which it operates, with low line densities in nearly all of its study areas. Yet high-cost universal service support (including high cost loop support, LSS, and IAS) accounts for *less than 2%* of its regulated revenues.

obtain investor capital. Accordingly, the proposed order's focus on dividends as some type of evidence that universal service support is not needed is misplaced, and can produce unintended policy outcomes with damaging results.

To understand why this focus is misplaced, one need only ask the question: If companies had used the very same earnings to buy back shares of stock, rather than pay dividends to shareholders, would the Commission view this as evidence of a lack of need? Most likely it would not, yet the impact would be basically the same with regard to equity investors. If the company had used the same earnings to undertake new lines of business or new non-regulated projects that had nothing to do with the supported services, rather than pay dividends to shareholders, would the Commission have viewed this as evidence of a lack of need? Again, most likely it would not. This underscores how unreasonable it is for the proposed order to suggest that carriers paying dividends should receive less universal service support.

Simply stated, the existence of dividends does not negate the need for universal service support. Rather, it is evidence that even with the receipt of universal service support, many rural regions remain uneconomic to serve. Carriers, particular ILECs facing line loss, must rely on dividends to secure capital necessary to invest in their networks and provide service in these areas. Reducing access to universal service support to dividend-paying companies would be unreasonable and counterproductive. It would serve only to reduce investment and discourage broadband deployment, especially in rural areas.

IV. REFORM OF UNIVERSAL SERVICE CONTRIBUTIONS. (FNPRM ¶¶ 88-151).

The proposed order suggests that a new telephone numbers-based methodology be adopted for determining the appropriate universal service fund assessment on carrier's residential services. It also proposes that providers of business services should contribute to universal service on a connections basis, and it seeks comment on the implementation of that methodology. However, pending implementation of that methodology, the proposed order would continue assessing providers of business services on the basis of interstate and international revenues.[23]

Embarq acknowledges the record support for the assertion that the current system of contributions to the universal service fund is broken. Comprehensive reform of universal service is served by addressing the decrease in contributions from the current revenue-based system. However, reform of the contribution system is a secondary concern relative to the need for reform to address the insufficient and faulty distribution of universal service support. This small aspect of the comprehensive reform proposal will simply be immaterial to carriers like Embarq if other negative aspects of the proposed order were adopted.

Although the proposed order provides some support for numbers-based contributions for residential services, there are some curious weaknesses in that support. One apparent rationale provided is that "the amount of North American Numbering Plan (NANP) numbers in use has shown steady, stable growth, providing a fairly constant basis for estimating universal service support amounts."[24] This also suggests the

---

[23] FNPRM at App. C ¶ 88.

[24] *Id.* at App. A ¶ 110, App. B ¶ 57. App. C. ¶ 106.

proposed order may be relying on continuing growth in contributions by changing to a numbers-based approach.

Elsewhere, however, the proposed order asserts that assessing universal service contributions based on residential telephone numbers will promote number conservation,[25] suggesting that growth in numbers would then be less steady and perhaps less predictable, which is counter to the rationale provided earlier. Finally, there is no support provided at all for the decision to assess the specific amount of $1.00 per number. Such an amount may not be overly burdensome, may be consistent and predictable, and may even have other favorable attributes as suggested by the proposed order in Appendices A and C.[26] But so does the $0.85 per line amount that Appendix B proposes as the per-number contribution.[27] While it is understandable that $1.00 will produce a higher level of contribution to the fund than would $0.85, so would $1.50, and the proposed order has not provided any support for a specific per-number contribution amount. These troubling weaknesses in the support for a numbers-based contribution system only exacerbate the problems and legal infirmities with other parts of the comprehensive reform proposal.

If the Commission does adopt a numbers-based contribution mechanism, then Embarq fully supports the proposed order's position that any exemptions should be kept to a minimum. Exceptions, whether for a particular provider or to a particular category of end users would complicate the administration of this new mechanism, and would

---

[25] *Id.* at App. A ¶ 111, App. B ¶ 58, App. C. ¶ 107.

[26] *Id.* at App. A ¶¶ 110, 112, App. C. ¶¶ 106, 108.

[27] *Id.* at App. B ¶ 52.

unfairly favor certain groups. The proposed order makes these same findings.[28] Embarq particularly supports the decision to not grant an unfair exemption to wireless family plans. Overall, the proposed order's conclusion that the Commission should not grant the myriad of requested exemptions[29] is wholly in keeping with the sound policy rationale behind expanding the contribution base, which is that services that benefit from access to the public network should contribute to the support of that network.

Consequently, Embarq supports the approach of Appendix C to not grant an exemption for stand-alone voice mail providers, in contrast to the approach of Appendix A, which would grant such an exemption. Finally, Embarq supports the exemption for numbers assigned to Lifeline customers.[30] An exemption for Lifeline customers is justified not only on the basis that relieving Lifeline customers from regulatory assessments will foster universal service, but such an approach is also consistent with Embarq's view that universal service support mechanisms need to be more targeted, both geographically and, in the case of Lifeline customers, economically.

V. REFORM OF INTERCARRIER COMPENSATION (FNPRM ¶¶ 152-338).

A. The Commission Must Reaffirm its Long-Standing End-to-End Analysis.

The proposed order ignores that the Commission has consistently held that the physical end points of a call (as opposed to the calling and called numbers) establish the proper jurisdiction for intercarrier compensation (i.e., the historical end-to-end analysis). Embarq believes that any intercarrier compensation reform order established by the

---

[28] *Id.* at App. A ¶ 140, App. B ¶ 89, App. C. ¶ 136.

[29] *Id.* at A ¶ 143-46, App. B ¶ 91-94, App. C ¶¶ 138-41.

[30] *Id.* at A ¶ 142, App. B ¶ 90, App. C ¶ 137.

Commission must reaffirm the use of physical endpoints as the appropriate manner in which traffic jurisdiction is determined.

For years, some carriers have been masking the true jurisdiction of calls by assigning local numbers to end users who are physically located outside the local calling area of the originating caller. This number assignment scheme creates a "double hit" to the originating carrier by "flipping" the intercarrier compensation arrangement. The carrier ultimately provides an inter-exchange service without incurring access charges; and also generates terminating compensation revenue from the originating carrier through its "locally dialed" calls.

Some examples are ISP-bound traffic where the server is located outside of the local calling area, otherwise known in the industry as Virtual NXX traffic. Yet another growing example of this locally dialed inter-exchange traffic occurs with the use of local platforms. Embarq has identified CLECs who are aggressively marketing and selling these Local Platform/Local DID services. In this situation, the originating end user dials a local number owned by the CLEC, but is then prompted to enter a secondary number or PIN, which causes the call to eventually terminate interexchange, interstate or even internationally. While this is clearly an interexchange call subject to originating access based on the physical endpoints of the call, to the originating carrier, the call appears "local" by nature of the numbers dialed. Therefore, it causes a doubly unfair effect on the originating carrier, which loses the originating access revenues and likely pays a terminating compensation rate to the CLEC. One CLEC website advertises their DID service which *"aggregates incoming local calls from multiple rate centers across* *multiple LATAs into a single point of access"* and *"is a flexible solution for providing customers with access to nationwide local telephone numbers."*

While much of the discussion surrounding the need for a phantom traffic solution focuses on the terminating revenue erosion, Embarq believes that such number assignment practice, without paying access charge, represents a different type of arbitrage. This type of arbitrage is eroding ILECs' *originating* access streams and also represent a burdensome, growing expense to ILECs. The Commission, therefore, must not allow carriers to redefine the jurisdiction of calls based on the calling and called numbers. The result has been a continued (and growing) arbitrage of the intercarrier compensation system to the advantage of some CLECs and to the detriment of ILECs.

There is often a flawed belief that a unified rate concept will make this issue of properly establishing traffic jurisdictional a moot issue. However, this is simply not accurate. Affirming the proper method for determining jurisdiction of a call establishes which carrier "writes the check". In other words, is the call subject to originating access (i.e. the call physically originates and terminates in different local calling areas) or is the call subject to a terminating revenue stream (i.e. the call physically originates and terminates within the same local calling area)? Any intercarrier compensation reform proposal must reinforce the long-standing end-to-end analysis which properly establishes intercarrier compensation based upon the physical end points of a call.

B. The Commission's Intercarrier Compensation Reform Proposal.

1. A Few Targeted Improvements Can Produce Significant Benefits.

Intercarrier compensation reform is not an all-or-nothing proposition. A few simple steps will produce substantial improvements. Contrary to the Commission's statement that "only comprehensive reform can address the fundamental challenges,"[31] the record is full of examples of less than comprehensive reform that has yielded significant public policy benefits. In 2000, the FCC's *CALLS Order* reduced interstate switched access rates and provided reliable and sufficient retail rate and universal service fund revenue recovery mechanisms for price-cap ILECs.[32] It took similar action in its 2003 *MAG Order* to reduce the interstate switched access rates of rate-of-return ILECs and provide similar revenue recovery mechanisms. The Commission should take similar action in this proceeding to unify intrastate and interstate switched access rates, with adequate revenue recovery mechanisms.[33]

---

[31] FNPRM at App. A, ¶ 2; FNPRM at App. C, ¶ 2.

[32] *Deployment of Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Low-Volume Long Distance Users, Federal-State Joint Board on Universal Service,* Sixth Report and Order in CC Docket Nos. 96-262 and 94-1, and Report and Order in CC Docket No. 99-249, and Eleventh Report and Order in CC Docket No. 96-56, 15 FCC Rcd 12962 (2002), *aff'd in relevant part by Texas Office of Pub. Util. Counsel v. FCC*, 265 F.3d 313 (5th Cir. 2001) ("*CALLS Order*").

[33] *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Fifteenth Report and Order, *Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation*, CC Docket No. 98-77, Report and Order, *Prescribing the Authorized Rate of Return From Interstate Services of Local Exchange Carriers*, CC Docket No. 98-166, Report and Order, 16 FCC Rcd 19613 (2001) *(MAG Order), recon. in part, Multi-Association Group (MAG) Plan for Regulation of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, CC Docket No. 00-256, First Order on Reconsideration, *Federal-State Joint Board on Universal Service*, CC Docket 96-45, Twenty-Fourth Order on Reconsideration, 17 FCC Rcd 5635 (2002), *amended on recon., Multi-Association Group (MAG) Plan for Regulation of Non-Price*

Many examples of targeted improvements also can be found at the state level. The general scenario is where a state reduces intrastate switched access rates, and provides opportunities for revenue recovery in the form of retail rate increases and establishment and implementation of an adequate state universal service fund. Embarq has participated in such reform in the states of South Carolina, Pennsylvania, Texas, Nebraska, and Wyoming. Florida, Indiana, Ohio and Missouri have also reformed the intercarrier compensation system and allowed for offsetting retail rate increases. Embarq notes that although some states have opted to reduce rates to interstate levels, others have stopped short, opting only to reduce the rate differential between the respective jurisdictions.

Each of these reform efforts recognized the need to replace lost implicit support, at both the state and federal levels. As competition continues to be ever more pervasive, recovery of lost implicit support is needed more now than ever before. Broadband expansion and continued investment in reliable rural networks are dependent on reliable support mechanisms.

Cap Incumbent Local Exchange Carriers and Interexchange Carriers, CC Docket No. 00-256, Federal-State Joint Board on Universal Service, CC Docket 96-45, Third Order on Reconsideration, 18 FCC Rcd 10284 (2003). *See also Multi-Association Group (MAG) Plan for Regulation of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers; Federal-State Joint Board on Universal Service*, CC Docket Nos. 00-256, 96-45, Report and Order and Second Further Notice of Proposed Rulemaking, 19 FCC Rcd 4122 (2004).

2. Rate Unification by Local Carriers Within Study Areas Makes Sense; a Single, Industry-Wide Rate Does Not.

Embarq supports the concept of unified switched access rates and its benefits in terms of reduced arbitrage and phantom traffic.[34] However, Embarq disagrees with the assertion made by the proposed order that this is a function of above-cost rates.[35] More commonly, arbitrage is a function of simply seeking the lowest rate for traffic termination. Arbitrage is driven by an analysis of relative rates, with little basis in absolute costs.

The Commission's *CLEC Access Charge Order*[36] is evidence of this fact. The order significantly reduced arbitrage by unifying CLEC switched access rates at the rate level of the corresponding ILEC. The determination of absolute cost was not a primary consideration in the proceeding and the Commission's order increased equity between competitors. Embarq supports proposals to unify intrastate and interstate switched access rates over a reasonable period of time, assuming that provisions are made for reliable

---

[34] *See* Petition for Waiver of Embarq Local Operating Companies of Sections 61.3 and 61.44-61.48 of the Commission's Rules, and any Associated Rules Necessary to Permit it to Unify Switched Access Charges Between Interstate and Intrastate Jurisdictions, WC Docket No. 08-160 (filed Aug. 1, 2008).

[35] "We have seen numerous competitors exploit arbitrage opportunities created by a patchwork of above-cost intercarrier compensation rates." FNPRM at ¶ 39, App. A ¶ 2, App. C ¶ 2.

[36] *Access Charge Reform, Reform of Access Charges Imposed by Competitive Local Exchange Carriers*, CC Docket No. 96-262, Seventh Report and Order, 16 FCC Rcd 9923 (2001) ("*CLEC Access Charge Order*"), *recon.*, *Access Charge Reform, Reform of Access Charges Imposed by Competitive Local Exchange Carriers, Petition of Z-Tel Communications Inc. For Temporary Waiver of Commission Rule 61.26(d) to Facilitate Deployment of Competitive Service in Certain Metropolitan Statistical Areas*, CC Docket No. 96-262, CCB/CPD File No. 01-19, Eighth Report and Order and Fifth Order on Reconsideration, 19 FCC Rcd 9108 (2004) ("*CLEC Access Charge Recon. Order*").

revenue recovery mechanisms. If the Commission were to take such action, Embarq requests that it extend its *CLEC Access Charge Order* to intrastate switched access rates.

Embarq supports a future NPRM to determine how the industry should proceed to achieve the ultimate unification of switched access and local reciprocal compensation rates. Properly implemented, switched access rate unification will go a long way toward achieving the ultimate goal of rate unification and will shift substantial revenues out of the intercarrier compensation system. Doing so, however, will shift substantial revenues out of the intercarrier compensation system, putting additional pressure on retail rates and the federal Universal Service Fund to replace these revenues. Accordingly, it is prudent to provide a phase-in period of several years to effectuate switched access rate unification and its impacts prior to determining the appropriate next steps. Embarq welcomes a future NPRM to determine the nature and timing of additional steps.

3. Rate Disparities for Voice Traffic Between Technologies Stifle Broadband Development and Investment.

Contrary to the proposed order's statement[37] that legacy regulatory regimes pose an obstacle to the transition to an all-IP broadband world, it is the disparity in rates between technologies that is largely responsible. Consumers in urban areas now have many broadband options; the Commission has largely realized broadband availability goals in those areas. Accordingly, now the policy objective needs to focus on expanding broadband availability for rural consumers. An intercarrier compensation system that provides for free or low-priced IP-PSTN terminations will only serve to deprive carriers serving rural areas of the revenues necessary to continue to expand broadband services.

[37] FNPRM at App. A ¶ 189, App. C ¶ 184.

4. Recovery of Displaced Revenues is a Vital Component of Any Intercarrier Compensation Reform Plan; Recovery Mechanisms Must be Sufficient and Reliable.

As prior Commission orders and the actions of many states recognize, the establishment of a sufficient, reliable revenue recovery mechanism is a vital component of any intercarrier compensation reform plan that reduces intercarrier compensation revenues. As the proposed order fails to establish a sufficient, reliable recovery mechanism for price-cap ILECs, it reflects its own outdated, "pre-1996 worldview."[38]

It is commonly understood that pervasive competition serves as a governor on retail rates. This fact is highly touted in many urban and suburban areas by competitors. The Commission could hypothetically permit unlimited retail rate increases to permit recovery of lost intercarrier compensation revenues. However, these revenues would not be realized due to competitive pressures. Competition has eroded implicit support relied on by rural carriers and the consumers they serve. Therefore, modest retail rate increases must be coupled with another access recovery mechanism as a result of intercarrier compensation reductions. Furthermore, it is just and equitable for the Commission to require competitive carriers to contribute to a recovery mechanism of sufficient size to recover displaced revenues and permit broadband to continue to be built in rural America.

5. The Proposed Rate of $0.0007 Per Minute is Arbitrary and Unlawful.

The proposed order would cap all intercarrier compensation at the current reciprocal compensation rate of $0.0007 per minute for all traffic and virtually all carriers. Setting a uniform rate for all carriers and all states, without an access recovery mechanism, is arbitrary, unreasonable, and unfair. It ignores the differences among

---

[38] *Id.* at App. A ¶ 228, App. C ¶ 223.

carriers, their networks, their locations, and their operating costs. A uniform rate, or rate cap, set at so low a level denies carriers like Embarq the opportunity to recover their costs.

The only way to harmonize all rates while simultaneously complying with section 252(d)(2)'s mandate and the requirements of sections 201 and 202 is to reaffirm the current TELRIC cost standard.[39] The TELRIC standard satisfies the requirements of sections 201 and 202, because it covers economic costs while satisfying section 252(d)(2). The Supreme Court has already affirmed that TELRIC is a lawful methodology under section 252(d), as well as section 251(c)(3),[40] and "a reasonable policy."[41]

The proposed order abruptly re-interprets the statute to require rates at incremental cost may not comply with section 252(d)(2), and it surely violates sections 201 and 202. Sections 201 and 202 require cost-based rate-making, and they require the Commission to explain any deviation from it. The proposed order fails to explain how and why it can set a rate, much less a uniform rate cap for all carriers and virtually all states, without any regard to those carriers' actual network costs. The proposed order's arbitrary $0.0007 rate cap would not withstand appellate scrutiny.

The proposed order's focus on incremental costs, moreover, is itself unreasonable. If one applied incremental cost analysis to all network costs, no carrier would ever recover its costs. The proposed order appears determined simply to ignore costs, and to

[39] 47 U.S.C. §§ 201, 202, 252(d)(2).

[40] 47 U.S.C. §§ 251(c)(3).

[41] *Verizon Communications, Inc. v. FCC,* 535 U.S. 467, 523 (2002).

drive intercarrier compensation rates to zero. The Commission lacks authority to impose such a policy.

C. Legal Authority (¶¶ FNPRM 202-230).

In its restructuring of intercarrier compensation, the proposed order has repeatedly overreached the Commission's legal authority. The Commission is not free to ignore the limits of its authority, nor to adopt arbitrary rules simply because it seeks a particular policy result. It is ironic that the proposed order claims authority to impose dramatic intercarrier compensation reform "by electing to partner with the states,"[42] when it actually seeks to usurp their authority over intrastate traffic.

1. The Proposed Rules Reflect an Unlawful Abdication of the Commission's Statutory Obligations Under Section 254(g).

One striking feature of the proposed order's treatment of intercarrier compensation is its failure to comply with the Commission's obligations under section 254(g). The statute directs the Commission to ensure that the rates charged to subscribers in rural and high cost areas are affordable and comparable to those in low-cost, urban areas. Section 254(g) also directs the Commission to maintain to state-wide geographically averaged rates by service providers.

The legal analysis set out in the proposed orders does not even mention this statutory provision. This oversight signals the Commission's complete abdication of the principles underlying section 254(g),[43] as well as the Commission's obligation to ensure its rules advance these principles. This provision may matter little to some commenters, but it is of critical importance to consumers in high-cost and rural areas, including the

[42] FNPRM at App. A ¶ 207, App. C ¶ 202.

[43] 47 U.S.C. § 254(g).

many rural areas that Embarq serves.[44] The Commission lacks legal authority to adopt rules, such as those outlined in the proposed order, that fail to meet these requirements.

Furthermore, the Commission's implementation of high-cost support has yet to pass judicial scrutiny, and its high-cost support mechanism for non-rural areas has been remanded twice. The Commission cannot lawfully "freeze" the current universal service fund, but must correct the flaws in the universal service support system. The proposed order, however, would only compound the errors, and it would leave the Commission even farther from compliance with the section 254 mandate. Indeed, the proposed order offers no rational basis for concluding that it is meeting that statutory mandate.

2. The Act Does Not Give the Commission Authority to Broadly Preempt State Regulatory Authority Over Intrastate Traffic.

The proposed order relies too heavily on its assumption that the 1996 Act preempted state authority. It is true that Congress preempted some state authority, but only to a point. The Act did not give the Commission *carte blanche* to preempt the states, and it did not give the Commission authority to regulate rates for intrastate traffic.

The proposed order bases its claim on the premise that section 251(b)(5) applies to all traffic. In more than twelve years since the 1996 Act's passage, the Commission has never reached such a conclusion before. On the contrary, in the *Local Competition First Report and Order*, the Commission instead recognized that section 251(b)(5) is limited to local traffic.[45] While the 1996 Act may not indeed be a "model of clarity,"

---

[44] Embarq is a rural telephone company, as defined by the Act, in 17 of 18 states in which it provides service. It is non-rural only in Nevada, where it serves the Las Vegas metropolitan area.

[45] *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996 and Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers*, CC Docket Nos. 96-98, 95-185, First Report and Order,

section 251(b)(5) cannot be fairly used to justify the proposed order's uniform intercarrier compensation regime.

The proposed order emphasizes that section 251(b)(5) does not itself use the term "local." But it does not need to. After all, section 251(b) is itself clearly limited to "local exchange carriers." Section 251(b)(5) is addressed to "*reciprocal* compensation arrangements," which plainly involves the two-way exchange of roughly balanced, local traffic. And by its terms, those arrangements are "for the transport and termination of telecommunications." The proposed order has improperly extended section 251(b)(5) reciprocal compensation obligations to all traffic, including ISP-bound traffic that is obviously not "reciprocal" and obviously not "terminating," and which the Commission has otherwise found is predominately interstate in character. The absence of the term "local" in section 251(b)(5) does not entitle the Commission to ignore the fundamental elements of that section. And it does not entitle the Commission to usurp the states' authority over intrastate traffic. The proposed order's misuse of section 251(b)(5) would be arbitrary and capricious.

The proposed order, moreover, does not explain how the Commission has the authority to sweep all traffic into its unified, single-rate federal regime, at the expense of state authority. The proposed order would preempt state authority, but the proposed order includes no conflict preemption analysis. Indeed, the proposed order has not even claimed that there is a conflict, which is the prerequisite for any preemption analysis. The only policy justification for a unified rate is regulatory arbitrage. Yet, although the proposed order notes the problem of regulatory arbitrage, it does not suggest that such

---

11 FCC Rcd 15499 (1996) (subsequent history omitted) ("*Local Competition First Report and Order*").

regulatory abuse is a basis -- let alone a sufficient basis -- for preempting the states. Instead, the proposed order unilaterally set a proposed rate for intrastate traffic in violation of section 2(b) of the 1996 Act,[46] and with no regard for the legitimate and statutorily recognized role of the state commissions.

The proposed order also would unlawfully bypass both the Federal-State Joint Board on Universal Service and the Federal State Joint Board on Separations. The Joint Board on Universal Service has undeniable jurisdiction over these issues and undeniable concern over the implicit subsidies that still provide the foundation for universal service, protecting investment in the PSTN and the availability of comparable service and rates for rural consumers. The Federal State Joint Board on Separations also has undeniable interest in the impact of such proposals on the important jurisdictional accounting issues within its area of oversight. These boards reflect the Act's determination to preserve state authority, even while coordinating policy. The Commission is not free to ignore them or their important roles in developing intercarrier compensation policy.

The proposed order's reliance on *Bell Atlantic v. FCC*[47] is misplaced. The proposed order reads too much into the D.C. Circuit's decision to justify its proposed unified rate for all traffic. The proposed orders focus unreasonably on one small aspect of the opinion, suggesting that an ISP-bound call is "dialed locally." Embarq believes this court dicta is unlikely to stand further court scrutiny, even within the D.C. Circuit itself. And while the FNPRM repeatedly claims that the D.C. Circuit has not questioned the proposed order's conclusion that ISP-bound traffic is interstate,[48] this is a serious

---

[46] 47 U.S.C. § 152(b).

[47] *Bell Atlantic Tel. Cos. v. FCC,* 206 F.3d 1 (D.C. Cir. 2000).

[48] *E.g.,* FNPRM at App. A ¶¶ 180, 182, 234, App. C ¶¶ 175, 177, 229.

overstatement. In *Bell Atlantic*, the court vacated and remanded, after finding that "the Commission has not provided a satisfactory explanation why LECs that terminate calls to ISPs are not properly seen as 'terminat[ing] ... local telecommunications traffic,' and why such traffic is 'exchange access; rather than 'telephone exchange service.''"[49]

Similarly, in *WorldCom, Inc. v. FCC*,[50] after finding the Commission's statutory rationale insufficient, the court stated, "as in *Bell Atlantic*, we do not decide whether handling calls to ISPs constitutes 'telephone exchange service,' or 'exchange access' (as those terms are defined in the Act ... or neither, or whether those terms cover the universe to which such calls might belong. Nor do we decide the scope of the 'telecommunications' covered by § 251(b)(5)." It seems inconceivable that the Commission could assert that the D.C. Circuit has somehow accepted the Commission's argument claim that ISP-bound traffic is jurisdictionally interstate.

As applied here, the proposed order's reading of *Bell Atlantic* requires viewing ISP-bound traffic as two calls. ISP-bound traffic does not terminate locally. Although the end user may dial in to a local number to receive access to their Internet service provider, the same is true when a long distance subscriber dials 10-10-XXX to reach his interexchange carrier. By this flawed rationale, even 1+ calling involves a locally-dialed call to the IXC's POP, using "1" effectively as speed dial, although that number is stored at the local exchange carrier's equipment and not on the caller's CPE. In each of these examples, however, the actual end-to-end routing (i.e., physical end points) of the call shows it is clearly non-local.

---

[49] *Bell Atlantic*, 206 F.3d at 9.

[50] *WorldCom Inc. v. FCC*, 288 F.3d 429 at 424 (D.C. Cir. 2002).

The Commission has never before adopted such a two-call finding, and doing so now would be unreasonable and unsustainable. The proposed order is unreasonable in basing its proposed rules on a single aspect of the *Bell Atlantic* decision. The court never would have envisioned its statement on this issue as providing the basis for turning a decade of telecommunications law on its head.

The proposed order is similarly wrong to claim jurisdiction over intrastate rates, and power to preempt state regulatory authority, based on the history of CMRS and information services. The regulatory history of these services, and the limited preemption that have been extended to them, is fundamentally different from the proposed order's attempt to preempt intrastate authority over intrastate services.

With CMRS services, the Commission was acting based on express statutory provisions. Congress recognized the need to limit state authority over the provision of wireless services, and tailored the Act accordingly. Preemption of state authority was and is limited. States were preempted from regulating *services*, not from regulating *traffic* from those services. Indeed, the Commission itself has never regulated the rates charged by CMRS carriers on the traffic that they originate. Yet that is precisely what the proposed order would do for all wireline traffic nationwide.

The *Pulver.com Order*, also cited in the proposed order, addressed only retail service regulation.[51] The Commission did not, in that order, pretend to have authority to preempt state jurisdiction over the underlying traffic itself. The *AT&T Order* likewise

---

[51] FNPRM at App. A ¶ 208, App. C ¶ 203, *citing Petition for Declaratory Ruling that Pulver.com's Free World Dialup is Neither Telecommunications nor a Telecommunications Service*, WC Docket No. 03-45, Memorandum Order and Opinion, 19 FCC Rcd 3307 (2004) ("*Pulver.com Order*").

did not address jurisdiction over traffic.[52] On the contrary, the *AT&T Order* found that there was no net protocol conversion when IP was introduced in the middle of the call path, and consequently there was not even any retail service preemption applicable to such traffic. The Commission must recognize the very real limits of its jurisdiction and its legal authority. Just because it may have authority -- even exclusive authority -- to regulate a particular service on a retail basis does not give the Commission authority to regulate traffic to and from such services.

The Commission simply does not have jurisdiction under section 251(b)(5) or section 252(d)(2) to set prices. That, however, is exactly what the proposed order would have the Commission doing. The proposed order directs states to set a uniform interim reciprocal compensation rate at a level lower than the current interstate access rate, and reduce the intrastate access, interstate access and reciprocal compensation rate to that interim rate over a period of time. In so doing, the Commission would have robbed the states of their authority under section 252(d)(2) to determine the just and reasonable rates for transport and termination of interstate traffic. In *Iowa Utilities Board v. FCC*,[53] the Eighth Circuit properly vacated the Commission's rules setting proxy reciprocal compensation rates, finding that even setting "upper limits higher than which rates set by the state commission shall not go" unlawfully usurped "the states' rights to set the actual rates."

---

[52] FNPRM at App. A ¶ 208, App. C ¶ 203, citing *Petition for Declaratory Ruling that AT&T's Phone-to-Phone IP Telephony Services are Exempt from Access Charges*, WC Docket No. 02-361, Order, 19 FCC Rcd 7457 (2004) ("*AT&T Order*").

[53] *Iowa Utils. Bd. v. FCC*, 219 F.3d 744 at 756-57 (8th Cir. 2000).

3. The Commission Lacks Jurisdiction Over Intrastate Traffic.

The Commission cannot lawfully claim jurisdiction over rates for intrastate traffic. The proposed order, by claiming jurisdiction and authority over intrastate rates, are unlawful. They exceed the Commission's authority, because it does not have jurisdiction over intrastate rates.

The distinctions between interstate and intrastate traffic and federal and state authority are replete throughout the Act. Section 2(b) of the 1996 Act directs the Commission to recognize its lack of authority over intrastate services and rates. The proposed order's usurpation of jurisdiction over intrastate rates is also a clear violation of section 2(b) of the Act, which establishes that "nothing in this Act shall be construed to apply or to give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communications service by wire or radio of any carrier...." The Commission is not free to ignore the separation of jurisdiction between intrastate and interstate, and it is not free to ignore the limits of its jurisdictional authority.

4. The Commission Cannot Lawfully Conclude that IP/PSTN Traffic is an "Enhanced Service."

The proposed order would "classify as 'information services' those services that originate calls on IP networks and terminate them on circuit-switched networks," or vice-versa.[54] In a single short paragraph, the proposed order announces that IP-enabled services are "enhanced services" or "information services." It bases that finding on the mistaken assumption that "[s]uch traffic involves a net protocol conversion between end-

[54] FNPRM at App. A. ¶ 209, App. C ¶ 204.

users, and thus constitutes an 'enhanced' or 'information service.'"[55] The proposed order uses this mistaken finding as an excuse to claim that all "authority to impose economic regulation with respect to IP/PSTN traffic rests exclusively with this Commission."[56]

It is unreasonable and arbitrary for the Commission to claim that IP/PSTN traffic is an enhanced service. The proposed order does not describe the supposed "net protocol conversion" between end users on an IP/PSTN call, but a footnote hints that this "conversion" occurs when the call passes through "computers that transform the circuit switched voice signal into IP packets, and vice versa, and perform associated signaling, control and address functions."[57] But this is not a net protocol change between *end users.* This is a voice call between two telephones. The statutory definition specifically excludes from "information services" any capabilities used for the "management, control or operation of a telecommunications system or the management of a telecommunications service."[58] The Commission has previously found that the definition expressly excludes "conversions taking place solely within the carrier's network to facilitate provisions of a basic network service" -- like phone-to-phone voice services contacting the PSTN -- and "result in no net conversion to the end user."[59] Routing a call through a gateway that

---

[55] *Id.*

[56] *Id.* at App. A ¶ 208, App. C ¶ 203.

[57] *Id. at* ¶ 209 n.520, App. C ¶ 204 n.535.

[58] 47 U.S.C. § 153(20). The proposed order acknowledges the exception in a footnote and dismisses it as inapplicable and irrelevant, but does not explain how or why. FNPRM at App. A ¶ 210 n.521, App. C ¶ 205 n.536.

[59] *AT&T Order*, 19 FCC Rcd 7457 at ¶¶ 4, 7. *See also Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as Amended,* CC Docket No. 96-149, Order on Reconsideration, 12 FCC Rcd 2297 at ¶ 2 (1997) (subsequent history omitted) ("*Non-Accounting Safeguards Recon. Order*").

converts it to or from IP format is an "internetworking" conversion that the Commission has found to be a telecommunications service, not an information service.[60]

The proposed order gives no reasoning for its new finding, and it furthers its error by concluding "that IP/PSTN services are not mere changes to the underlying technology used for 'existing' basic services, but are entirely new services with characteristics in many ways distinct from pre-existing telephone services."[61] The proposed order offers no explanation whatsoever as to how these services are "entirely new." It ignores the record to the contrary, it ignores the statutory definitions of "information service" and "telecommunications service,"[62] and it even ignores the Commission's own precedent.[63]

---

[60] *Id.* at ¶¶ 11, 12.

[61] FNPRM at App. A ¶ 209, App. C ¶ 204.

[62] 47 U.S.C. §§153(43), 153(46).

[63] *See, e.g., Deployment of Wireline Services Offering Advanced Telecommunications Capability*, CC Docket No. 98-147, Memorandum Opinion and Order and Notice of Proposed Rulemaking, 13 FCC 24011 at ¶ 35 (1998) (footnotes omitted):

> The Commission has repeated held that specific packet-switched services are "basic services," that is to say, pure transmission services. xDSL and packet switching are simply transmission technologies. *To the extent that an advanced service does no more than transport information of the user's choosing between or among user-specified points, with change in the form or content of the information of the information as sent and received, it is "telecommunications,"* as defined by the Act. Moreover, to the extent that such a service is offered for a fee directly to the public, it is a "telecommunications service."

See also Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as Amended, Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, CC Docket No. 96-149, First Report and Order and Further Notice of Proposed Rulemaking, 11 FCC Rcd 21905 at ¶ 106 (1996) ("*Non-Accounting Safeguards Order*") (noting that if *the user* sees no protocol conversion on the service level, it is a "telecommunications service" regardless of whether protocol processing takes place internal to the call); *Amendment of Section 64.702 of the Commission's Rules and Regulations (Computer III -- Phase II),* CC Docket No.

IP/PSTN voice calls have always been subject to access charges. Part 69 of the Commission's rules[64] has never conditioned the obligation of a carrier to pay access based on the technology used by that carrier, and it has never contained an exemption for IP-enabled voice services. The ESP Exemption was adopted as a narrow exception to the Commission's deliberately broad access charge regime.[65] It applies only when an enhanced or information service provider allows its *own subscribers* to obtain access to the ISP's own information services. It does not apply when a service provider uses the PSTN to place a voice call between end users.

The Commission has recognized that, unlike true information service providers, interconnected voice over Internet protocol ("VoIP") providers use the PSTN in the same way and for the same purposes as more traditional phone-to-phone service providers, and impose the same costs and burdens on the PSTN.[66] The Commission has recognized that interconnected VoIP services are substitutes for ordinary voice telephone services.[67] The

---

85-229, Report and Order, 2 FCC Rcd 3072 at ¶¶64-71 (1987) (same), *vacated on other grounds*, *California v. FCC*, 905 F.2d 1217 (9th Cir. 1990).

[64] 47 C.F.R. §§ 69.1, et seq.

[65] *MTS and WATS Market Structure*, CC Docket No. 78-72, Order on Reconsideration, 97 FCC 2d 682 (1983), *modified on further recon.*, 97 FCC 2d 834 (1983), *aff'd in part and remanded in part*, *Nat'l Ass'n of Regulatory Util. Commissioners v. FCC*, 737 F.2d 1095 (D.C. Cir. 1984) ("*Access Charge Recon. Order*"). The ESP Exemption was maintained and extended in *Amendment of Part 69 of the Commission's Rules Relating to Enhanced Service Providers*, Notice of Proposed Rulemaking, 2 FCC Rcd 4305 (1987) ("*ESP NPRM*"); *Amendments of Part 69 of the Commission's Rules Relating to Enhanced Service Providers*, Order, 3 FCC Rcd 2631 at ¶¶ 2, 18, n.51 (1988) ("*ESP Order*"); *Access Charge Reform*, First Report and Order, 12 FCC Rcd 15982 at ¶ 343 (1997), *pet. for rev. denied, Southwestern Bell Tel. Co. v. FCC,* 153 F.3d 523 (8th Cir. 1998) ("*Access Charge Reform Order*").

[66] *Access Charge Reform,* 12 FCC Rcd 15982 at ¶¶ 343, 346.

[67] *Universal Service Contribution Methodology,* WC Docket Nos. 06-122, 04-36, CC Docket Nos. 96-45, 98-171, 90-571, 92-237, 99-200, 95-116, 98-170, Report and Order and Notice of Proposed Rulemaking, 21 FCC Rcd 7518 at ¶¶ 35, 43 (2006), *aff'd*

Commission has previously found, appropriately, that the "cost of the PSTN should be borne equitably among those that use it in similar ways,"[68] rather than giving an artificial competitive advantage to one group of service providers based on technology used in originating a call.[69] The Eighth Circuit upheld the ESP Exemption based on that critical distinction, pointing out that enhanced services "do not utilize LEC services and facilities in the same way or for the same purposes as other customers who are assessed per-minute interstate access charges."[70]

Finding IP/PSTN traffic is "enhanced services" or "information services" is plainly inconsistent with the long-standing practice of technological neutrality. There is no reasonable justification for a distinction between interconnected VoIP technology, and the Commission has previously recognized that phone-to-phone voice communications should be regulated in the same manner regardless of technology. The Commission has recognized that interconnected VoIP services, such as cable telephony, are indistinguishable from more traditional voice services provided by telecommunications carriers. Both enable subscribers to use a phone, dial a number assigned from the North America Numbering Plan, and engage in real-time voice conversations. The Commission

in relevant part sub nom. Vonage Holdings v. FCC, 487 F.3d 1232 (D.C. Cir. 2007). *See also IP-Enabled Services*, First Report and Order and Notice of Proposed Rulemaking, 20 FCC Rcd 10245 at ¶ 23 (2005) (*VoIP 911 Order*), *aff'd sub nom. Nuvio Corp. v. FCC*, 473 F.3d 302 (D.C. Cir. 2006) (emphasizing that consumers expect interconnected VoIP services to work much "like a 'regular telephone'"); *VoIP CALEA Order*, 20 FCC Rcd 14989 (2006), *aff'd, American Council on Educ. v. FCC*, 451 F.3d 226 (D.C. Cir. 2006) (applying CALEA compliance requirements).

[68] *Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92; *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45; *IP Enabled Services*, WC Docket No 04-36, Notice of Proposed Rulemaking, 19 FCC Rcd 4863 at ¶ 61 (2004) ("*IP Enabled Services NPRM*").

[69] *USF Contribution Order* at ¶ 43.

[70] *Southwestern Bell*, 153 F.3d. at 542.

has recognized that interconnected VoIP providers (and cable companies in particular) market their services as a direct substitute for the voice services of telecommunications carriers.

The proposed order gives no reasoned explanation for such a substantial departure from its prior findings and precedent. Allowing interconnected VoIP providers, such as cable companies, to be exempt from the intercarrier compensation regime would result in extremely disparate financial treatment of the two voice services. It cannot be justified and would violate the Equal Protection, Due Process, Takings, and Commerce clauses of the United States Constitution, as well as being an arbitrary and capricious classification under the Administrative Procedure Act[71] and the Communications Act.

Moreover, the proposed order ignores that only carriers have a right to interconnect with local exchange carriers under section 251. The Commission allowed genuine ESPs a limited exemption from its access charge rules, precisely because they are not carriers and do not use the PSTN in the way carriers do. Interconnected VoIP services, in contrast, are just IP-originated substitutes for more traditional voice services. Indeed, as the proposed order itself recognizes,[72] all carriers are increasingly introducing IP technology in their networks, just as carriers previously introduced digital technology in place of analog. IP-originated calls reach the PSTN in TDM format, and today's networks have no systems capable of distinguishing IP-originated calls from any other ordinary calls. The Commission noted in 1983 that the use of digital loops would include

---

[71] U.S. Const. art. I, § 8, amends. V, XIV; 5 U.S.C. §§ 551, et seq.; 47 U.S.C. §§ 151, et seq.

[72] FNPRM at App. A ¶ 2, App. C ¶ 2. The FNPRM also recognizes that "IP technologies will be used to deliver the predominant share of voice and data traffic within a few years." *Id.* at App. A ¶ 260, App. C ¶ 255.

"a net protocol conversion within the network," and found that although "[t]his could be thought of as invoking the definition of enhanced service, ... *the service itself would remain a switched message service otherwise unchanged except for the characteristics of the electrical interface*."[73] Clearly, the introduction of new technology does not change a service provider's status from a telecommunications services provider to an information services provider, and it does not create some new class of services that entitles the Commission to usurp state regulatory authority over intrastate traffic. The Commission cannot ignore its own precedent, and finding IP/PSTN traffic is "enhanced services" would be arbitrary and capricious.

Curiously, the Commission has no need to attempt to classify -- or more accurately, to re-classify -- IP/PSTN service as an "information service" in order to implement intercarrier compensation reform. The Commission can fashion rules that would apply to the transport and termination of such services without violating its own precedent and putting its order on a path to vacatur and remand. In addressing intercarrier compensation reform, the Commission should be taking steps to reduce ambiguity and disputes, not adding to them.[74]

---

[73] *Communications Protocols Under Section 64.702 of the Commission's Rules and Regulations,* Memorandum Opinion, Order, and Statement of Principles, 95 FCC 2d 584 at ¶ 16 (1983) (emphasis in original). *See Non-Accounting Safeguards Order,* 11 FCC Rcd 21905 at ¶ 106.

[74] For that reason, the Commission should grant Embarq's separately-pending petition, which asks the Commission to forbear from any application of the ESP Exemption to IP-to-PSTN voice traffic, to the extent any party claims it may apply. Alternatively, the Commission could resolve the same issue by a declaratory ruling that the ESP Exemption has never applied to such traffic. *See* Petition of the Embarq Local Operating Companies For Limited Forbearance Under 47 U.S.C. § 160(c) from Enforcement of Rule 69.5(a), 47 U.S.C. § 251(b), and Commission Orders on the ESP Exemption, WC Docket No. 08-8 (filed Jan. 11, 2008). The Commission likewise should grant the parallel petition filed by Frontier. Petition of the Frontier Local Operating

D. The Additional Costs Standard (¶¶ FNPRM 231-263).

The proposed order also seeks comment on two important items that determine the price of terminating intercarrier compensation. The first item is the cost standard used to determine rates for all terminating traffic including reciprocal compensation, intrastate switched access, and interstate switched access. The proposed order redefines the Commission's current definition of "additional cost" to one based on an approach established by Gerald Faulhaber in his 1975 paper on cross-subsidization.[75] Embarq will refer to this new "additional cost" standard as Faulhaber Incremental Cost Methodology ("FICM").

As described in detail below, the FICM methodology is inappropriate. The Total-Element Long-Run Incremental ("TELRIC") standard, which includes an incremental component plus a reasonable allocation of forward-looking common costs, remains the appropriate costing methodology for establishing the cost to terminate traffic on a carrier's network.

The second item in question is how to average the final price for terminating traffic. The proposed order would adopt a new method for averaging the price of termination. Current intercarrier compensation rates are carrier-specific, as well as state-

Companies for Limited Forbearance Under 47 U.S.C. § 160(c) from Enforcement of Rule 69.5(a), 47 U.S.C. § 251(b), and Commission Orders on the ESP Exemption, WC Docket No. 08-8 (filed Sept. 30, 2008). It should deny the forbearance petition filed by Feature Group IP, for the reasons set out in the Embarq's opposition. *See* Opposition of Embarq, Feature Group IP Petition for Forbearance Pursuant to 47 U.S.C. § 160(c) from Enforcement of 47 U.S.C. § 251(g), Rule 51.701(a)(1), and Rule 69.5(b), WC Docket No. 07-256 (filed Feb. 19, 2008).

[75] FNPRM at App. A ¶ 248, App. C ¶ 243.

specific. The proposed order would adopt a method using a single statewide average rate for all carriers within a state.[76]

Additionally, the proposed order suggests that the proper technology to be used to calculate switching for voice traffic is soft switch technology, as opposed to TDM switch technology.[77] Embarq believes that it is premature to propose the use of soft switch technology for cost purposes. Soft switch technology is first-generation and is not widely deployed. Consequently, it does not properly reflect the cost characteristics of the current switch network. In total, the proposed cost methodology shift from the TELRIC standard to the FICM methodology, combined with establishing a single terminating rate for all carriers leaves the recovery of legitimate network costs in jeopardy. In addition, reliance on soft-switch technology inappropriately assumes certain efficiencies that carriers may or may not actually realize.

1. The Proposed Order is Wrong to Suggest the TELRIC Cost Standard Has Been a Failure on Reciprocal Compensation Traffic.

The proposed order asserts that the TELRIC standard, which had been applied only to section 251(b)(5) traffic, has failed. It argues that pricing failures allowed certain carriers to collect "above-cost reciprocal compensation payments" by targeting customers in order to become net recipients of reciprocal compensation.[78] While it is true that some carriers (i.e., some CLECs) have received large volumes of terminating compensation by targeting customers who terminate one-way traffic, it is critical to understand that the underlying TELRIC cost methodology did not cause this situation. Carrier-specific

76 *Id.* at App. A ¶ 274, App. C ¶ 269.

77 *Id.* at App. A ¶ 261, App. C ¶ 256.

78 *Id.* at App. C ¶ 234.

TELRIC rates for ISP dial-up service were never developed thus the averaged rates applied did allow for over-recovery of that specific service.

The TELRIC standard is an appropriate methodology for calculating the cost of a product or service for multi-service firms. When properly developed and applied to each carrier's specific cost characteristics, TELRIC does not produce above-cost results or cross-subsidization of products; it allows for the proper recovery of the economic cost of equipment and resources which are needed to provide telecommunication services.

The new methodology proposed by the Commission to measure "Additional Cost" is Incremental Cost as it was defined by Faulhaber in his 1975 paper. Under the FICM, common costs are removed when pricing termination rates, therefore the recovery of these costs associated with terminating traffic on a carrier's network are in limbo. By removing any contribution toward common costs from the "additional cost" standard, the proposed order would require that other services recover *more* than a reasonable allocation of common costs.

Embarq endorses the continued use of the forward-looking cost methodology, TELRIC. An examination of the components that are needed to provide the termination of a call shows that the model functions reasonably well. The called party service provider terminates a call from the originating carrier's switch through a trunk port, the call is then examined by the switch processor, the switch determines the call path, the switch then forwards the call to the proper line gateway and line card which allows the call to traverse the last-mile of the network connecting to the called customer. In order to recover the economic cost of providing this service a portion of the cost of each component needed to provide the call must be accounted for as well as items such as land

& building, power, overheads and common cost. By mandating that carriers ignore any of these real-world costs of terminating traffic, the Commission would be improperly imposing a requirement to terminate traffic below cost.

2. The Proposed Incremental Cost Methodology is Unreasonable, Because It Leaves Recovery of Legitimate Costs in Jeopardy.

The TELRIC standard for calculating the cost for switched termination services includes forward-looking allocated costs of all switch components, power, land & building, overheads and other common costs. The FICM methodology for terminating traffic would narrowly define the allocation of the switch component to an undefined usage-sensitive subset of costs, eliminate any allocation of power, land & buildings, overheads, and common costs. The affect of this narrow allocation requires all other switching services to carry the burden of costs ignored by the FICM methodology.

The result of using the proposed cost methodology for terminating rates would be failure to recover the full economic cost of furnishing a switch. In addition, the proposed standard would fail to allow for recovery of the necessary common costs that company must incur to ensure the service. This causes two very real problems. First, it pushes the entire cost of the switch to the called party. Second, the terminating LEC would no longer receive the revenue needed to fund replacement capital used to invest in new technologies.

The proposed order discusses this issue — the failure of the FICM to allow for recovery of total costs.[79] It suggests that a multi-part pricing regime could result in total cost recovery by incorporating a fixed monthly fee along with a variable usage fee. Economic theory does indicate that such a two-part pricing mechanism can produce

---

[79] *Id.* at App. C, ¶ 247.

efficient results in some cases. However, the proposed order — in arguing that the variable usage component should be priced based on FICM — gives no indication of how the fixed monthly fee would be recovered, or from whom it would be recovered. If the implication is that such a fixed fee would be recovered from end-users, the effect of this would be to place a disproportionate share of common costs on those users. And there is no economic justification as to why it is either desirable or efficient to have end-users to pay a greater share of common costs just so carriers sending terminating traffic can pay a smaller share of common costs.

In addition, the proposed order reaffirms "that the long-run incremental cost rather than short-run incremental cost is the appropriate cost concept."[80] It then proposes the use of the FICM, a methodology that is characteristically a short-run approach. In the long-run, all costs are variable. In the short-run, certain costs are fixed, and only costs that change with small increments of volume are considered. Therefore, prices based on short-run costs dictate that a carrier could never recover its fixed costs. FICM recovers incremental cost based on only the additional cost of implementing a new product. Therefore, it does not recover the fixed costs attributed to the new product.

If the Commission were to adopt a short-run cost methodology, the cost of the embedded network may be more appropriate than a forward-looking network design.[81] The question should be asked: Under what circumstances would the FICM definition of additional cost be developed for pricing purposes? The answer: Only in the short-run would a firm price at this level of cost; and that is likely because the firm has the ability to recover the ignored cost through other pricing mechanisms.

---

[80] *Id.* at App. C, ¶ 240.

[81] *Id.* at App. C, ¶ 238.

Again, the proposed order asserts that TELRIC methodology for reciprocal compensation has not led to rates that accurately reflect cost.[82] The *application* of the methodology is at issue, not the validity of the TELRIC methodology. Based on this faulty conclusion, the proposed additional cost standard could drive undesirable market outcomes. Interconnecting carriers may be incented by the artificially low terminating rates to move traffic to tandem facilities rather than use dedicated transport circuits to the end office. For intrastate and interstate switched access, the existing rate structure applies cost directly to the cost causer with a rate structure for each network element consisting of end office, common transport and tandem switch cost element. The new proposed cost methodology could cause carriers to disconnect dedicated end-office circuits and route all traffic to tandem switch locations. The movement of traffic from dedicated transport facilities to tandem connections could cause a large increase in trunk hardware and could potentially lead to tandem exhaust.

With regard to the proposal to establish a single, state-wide rate, there are two fundamental problems with the proposed order. (1) It fails to recognize the large disparate cost characteristics present for each individual carrier and (2) it fails to recognize the inherent subsidies in high level averages. The proposed order concludes that the cost characteristics of Alaska and Hawaii[83] are unique. A similar argument could be made for other remote areas (i.e., rural ILECs). High-level averaging of multiple carriers' costs may result in certain carriers not fully recovering costs for this very important service.

---

[82] *Id.* at App. C, ¶ 234.

[83] FNPRM at App. C, ¶ 186.

Setting rates at an average requires that some level of subsidy exists for the product or service. When the individual data points vary widely from the average, the subsidy can be large for the upper outlying points. By establishing rates at the lowest possible level of de-averaging, the need for support in each geographic area is lessened. The ability to de-average costs by carrier, by state, and across multiple rate elements is possible with desktop computer processing. Billing systems are already established to bill at these numerous geographic levels and across numerous elements (e.g., switched, transit minutes of use, tandem minutes of use). For these reasons, establishing rates based on the characteristics of each LEC within a state, rather than a single all-carrier statewide average rate, would be the right approach to develop terminating intercarrier compensation rates. If the broader definition of "one rate per state" were accepted this would lead to an over-recovery of costs by the larger carriers serving urban areas.

The primary drivers of costs associated with switching equipment have always been call volumes, minutes of use, and user connections. Urban areas benefit from high capacity switches which carry a lower cost per minute of use. If a statewide average rate were accepted those carriers which mostly serve urban areas would over-recover their termination costs while the rural carriers would under-recover their termination costs. This would in effect, create a subsidy of terminating traffic for urban LECs by rural carriers, the same rural LECs that are already burdened by serving high-cost areas.

The 1996 Act did not contemplate costs to be developed by averaging together all carriers. Section 252(c)(2)(A) provides that "a state commission shall not consider the terms and conditions for reciprocal compensation to be just and reasonable unless:
(i) such terms and conditions provide for the mutual and reciprocal recovery by each

carrier of costs associated with the transport and termination on each carrier's network facilities of calls that originate on the network facilities of the other carrier."[84] Costs vary substantially across carriers and vary across geographic areas for each carrier. For example, Embarq has found that switching and transport costs can vary by more than three times the company's overall average.

The continued use of a unique, single rate by operating company, by state, is appropriate and preferable to Embarq. Concerns that carriers could abuse this system would be eliminated if all companies, including CLECs, were required to provide cost justification of their terminating rates. Having the Commission impose one rate on all carriers, regardless of profile, is unreasonable.

3. It is Premature to Propose Use of Soft Switch Technology as the Technology for Cost Purposes.

Carrier-grade soft switch technology has not been widely accepted or deployed outside urban areas. Several technical issues arise when using soft switch technology, such as, security and quality of service. These technical issues will impact costs, and therefore must be explored before a wholesale adoption of soft switch technology is used to set forward-looking rates.

A common misconception is that a soft switch can easily replace a circuit switch; a properly configured soft switch will consist of more network elements than just the soft switch alone. The fully configured soft switch complex would include the soft switch processor, IP switches, routers, firewall, session border controller and media gateways. The proposed order mistakenly assumes one can simply remove a circuit switch and replace it with a soft switch. That assumption is an over-simplification.

[84] 47 U.S.C. § 252(c)(2)(A).

Another common misconception is that a soft switch is not traffic-sensitive. The reality is a soft switch is more sensitive to traffic volumes as it continuously sends voice packets throughout the duration of the call. The deployment of a soft switch as mentioned above would require the addition of several network components all of which are sensitive to traffic volumes and result in significant additional costs.

The transport network itself would have to be upgraded if carriers moved to soft switch architecture. Not only would more traffic be placed on the data network, which would require more resources, every element in the data network would have to be upgraded to provide redundancy, security, and to handle quality of service requirements.

The proposed order's guidance related to the assumed deployment of soft switch architecture is premature.[85] Although, Embarq does deploy soft switch technology it is driven by end-to-end IP applications which are used by a small subset of business customers. Embarq's soft switch architecture is not utilized on a ubiquitous basis or even in all states. All special deployments have been economically justified. Therefore, the existing TDM-based switching architecture should continue to be utilized when determining TELRIC-based cost for the foreseeable future, especially in rural areas.

Additionally, it is surprising that the proposed order would dictate a very particular switch technology, such as soft switch, when the 1996 Act states flatly that "the Commission is not authorized to engage in rate proceedings to establish with particularity the additional cost of transporting and terminating call."[86] Extreme "particularity," such as dictating an assumed soft switch technology as a costing standard, would be a significant error.

---

[85] *Id.* at App. A ¶ 266, App. C ¶ 261.

[86] 47 U.S.C. § 252(d)(2)(B)(ii).

E. Implementation -- Direction to the States (¶¶ FNPRM 264-288).

1. The Commission's Default Network Edge Rule on Direct and Indirect Interconnection Contradicts Section 251.

The proposed order establishes default rules regarding the network "edge" which, by the Commission's own terms, are intended to simply define functions governed by a uniform terminating rate, and not to require changes to physical points of interconnection.[87] Some of these defaults, however, appear to contradict established principles under section 251. Specifically, the Commission proposes that "[t]he calling party service provider may at its sole discretion choose whether to interconnect directly or indirectly with the called party service provider."[88] Under section 251, the party being interconnected with, *i.e.*, the called party, gets to choose whether interconnection is direct or indirect.[89] Under the Order, however, the calling party gets to choose whether interconnection is direct or indirect. Not only does this default rule represent a change from current practice, but also appears to mandate changes to interconnection between parties not intended by the Commission.[90] If the proposed order intends to change current conventions, it must be explicit and explain why it is doing so.

2. A Decision on Symmetry Rules is Premature.

The proposed order imposes a symmetrical uniform reciprocal compensation rate in all cases once the final uniform rate becomes effective.[91] These rules would not become effective until the end of the 10-year transition period established in the proposed

---

[87] FNPRM at App. A ¶ 275, App. C ¶ 270.

[88] *Id.*

[89] *See, e.g.*, *Local Competition First Report and Order*, 11 FCC Rcd 15499 at ¶ 997.

[90] FNPRM at App. A ¶ 275, App. C ¶ 270.

[91] FNPRM at App. A ¶ 281, App. C ¶ 276.

order. It is premature, however, for the Commission to adopt such absolute rules. With the pace of innovation, it is unclear how traffic and networks may change in the future. Symmetrical rates only make sense when there is symmetrical and balanced traffic, which is not always the case in the real world. ISP traffic, for example, is not symmetrical, and it is unclear what the balance of traffic will be ten years from now, when any proposed symmetry rules would take effect.

Rather than imposing a rigid standard now that would not be applicable until so far in the future, it would be more appropriate for the Commission either to establish a rebuttable presumption of symmetry or to defer changes to these rules until later in the transition period.

3. Existing Agreements Should Be Orderly Transitioned to Any New Rules.

Embarq supports an orderly transition of existing interconnection and commercial agreements to new rules. Embarq believes that invoking a change-of-law under existing interconnection agreements is appropriate and would facilitate an orderly transition. For agreements in "evergreen" status or lacking a change of law provision, the section 252 process is a reasonable process to update those agreements to reflect the new regime envisioned by the proposed order.[92] With respect to commercial agreements, enabling parties to invoke change-of-law terms rather than abrogating agreements is appropriate and promotes an orderly transition given that these agreements are generally the products of arms-length negotiation between sophisticated parties.[93]

[92] *Id.* at App. A ¶ 292, App. C ¶ 287.

[93] *Id.* at App. A ¶ 293, App. C ¶ 288.

F. Implementation -- Revenue Recovery Opportunities (¶¶ FNPRM 289-321).

1. Excessive Reliance on SLCs is Inappropriate for Access Recovery.

The proposed order would raise price-cap carriers' subscriber line charges ("SLCs") to offset some of the loss of intercarrier compensation revenue. Relying on SLC increases, however, is an unreasonable approach to intercarrier compensation reform.

The effect of SLCs is to impose on an ILEC's customers the costs of its COLR obligation. SLCs force customers in low-cost service areas to subsidize service to high-cost areas. They also are inherently anti-competitive, putting ILECs at an unfair and artificial competitive disadvantage against other service providers who do not have a COLR obligation. Under the proposed order, ILECs alone remain compelled to serve high-cost customers under COLR, and they are expected to increase rates to their customers and further disadvantage themselves in the competitive marketplace. Such a policy is unfair and unreasonable, and ultimately unsustainable. The competitive distortion grows only more serious over time, because cable companies and other competitors focus their marketing and investment in areas that are low cost to serve, leaving high-cost areas to the incumbents. The Commission is aware that ILECs are rapidly losing access lines in low cost areas to competitors.[94] The proposed order, however, ignores the impact of such a policy.

[94] Embarq's access lines have declined 20% since December 31, 2005, chiefly due to competition from cable telephony, but also to growing wireless substitution and "over-the-top" VoIP services.

2. Universal Service Support Should Not be Denied Because a Carrier Earns Profits in Other, Unregulated Lines of Business.

The proposed order would deny supplemental IAS to price cap carriers unless they are unable to earn a normal profit when looking at *all* of their lines of business, including unregulated offerings in competitive markets. In effect, therefore, the proposed order unreasonably would require price-cap regulated ILECs to subsidize their below-cost regulated activities with revenue from their competitive businesses.

This requirement is inherently arbitrary and capricious, and it is entirely inconsistent with Commission precedent. The Commission has long recognized that competition is superior to regulation in ensuring just and reasonable rates and preventing any over-earning. It makes no sense to require carriers to use revenues from competitive markets to subsidize regulated activities. Indeed, it is wholly inconsistent with the direction of decades of Commission regulation, which has sought to ensure that profits from regulated activities are not used to subsidize competitive activities.

The Commission has found that it is not permissible for firms to subsidize regulated services with revenue from competitive services. The Commission should not depart, and cannot reasonably depart, from this long-standing conclusion. Forcing price-cap carriers, but not rate-of-return carriers, to subject themselves to losses on unregulated lines of business is arbitrary and capricious. There is no policy justification for treating the two classes of carrier separately with regard to their respective unregulated activities. Different regulation of their local telecommunications offerings does not offer the requisite nexus to the unregulated activities. Moreover, if the Commission were to require price-cap carriers to lose money on regulated activities and subsidize those regulated activities with revenue from unregulated activities, it would likely violate the takings clause of the Constitution.

The Commission must afford regulated carriers -- including those subject to price cap regulation -- a reasonable opportunity to make a normal profit. It cannot avoid this responsibility by compelling the regulated firm to cross-subsidize its regulated activity with revenue from unregulated activities and businesses.

G. Measures to Ensure Proper Billing (¶¶ FNPRM 332-338).

1. Phantom Traffic Reform is a Necessary Component of Intercarrier Compensation Reform.

Embarq is both a tandem owner and an ILEC that subtends foreign ILEC tandems in many of the states in which it operates.[95] As a tandem owner, Embarq creates and distributes call detail records to subtending carriers to facilitate intercarrier compensation. But as a subtending carrier, Embarq relies upon call detail records generated by the larger ILEC tandem owners that it subtends. As a result of this network architecture, Embarq exchanges traffic both directly and indirectly with competitive carriers (e.g., CLEC and CMRS carriers). Although Embarq prefers to exchange traffic on direct trunks with competitive carriers, many carriers refuse to establish direct network connections with mid-sized and rural ILECs such as Embarq. Instead, CLECs and CMRS carriers chose to route the traffic through an intermediary transit provider.

Because many of the issues surrounding unidentified/phantom traffic occur with the exchange of indirect traffic, Embarq has allocated significant resources to reducing the indirect traffic volumes it exchanges with competitive carriers. However, Embarq

[95] 88% of Embarq's access lines subtend its own tandems, while the remaining 12% are served by tandems owned by other providers.

typically faces tremendous resistance during negotiations with CMRS carriers and CLECs to establish direct trunking, even when Embarq agrees to permit indirect traffic routing for specified levels of traffic that do not exceed a usage threshold. In fact, even when Embarq has its own tandem within the LATA where traffic is exchanged, Embarq finds itself exchanging traffic indirectly with competitive carriers, causing the traffic to flow through two tandems owned by two separate ILECs. [96]

2. The Commission Needs to Act to Reduce the Problem of Phantom Traffic to Enable Proper Billing.

There appears to be growing industry consensus regarding the need for rules and guidelines to reduce the substantial amounts of unidentified traffic that terminates on carriers' networks (i.e., phantom traffic). Embarq applauds the proposed order for taking an initial step to reduce these large volumes of unidentified, and therefore, unbillable minutes. These unbilled minutes permit originating carriers to unjustly enrich themselves at the expense of other carriers.

Embarq supports the Commission's effort to establish rules to facilitate the transfer of critical call signaling information necessary to permit the terminating carrier to bill the correct intercarrier compensation rate to the appropriate carrier. Consistent with prior filings in this proceeding, Embarq reiterates its support of the USTelecom Phantom Traffic Proposal,[97] which seeks to resolve the tremendous volumes of minutes that are

---

[96] One example of this double tandem situation occurs in MN. Embarq owns the Osseo, MN tandem, but a larger Qwest tandem resides within the same LATA. Embarq is currently exchanging *all* traffic with a large nationwide CMRS carrier on an indirect basis through the Qwest tandem. Despite the fact that traffic volumes exchanged between Embarq and this CMRS carrier exceed 2 million minutes per month, the CMRS carrier has failed to establish a direct connection to Embarq's tandem.

[97] *See, e.g.,* Letter from Glenn Reynolds (USTelecom) to Marlene Dortch (FCC) at Att. pp. 9-14, WC Docket No. 01-92 (Feb. 12, 2008).

terminating on carriers' networks without sufficient information to bill the proper carrier at the proper rates, depriving these carriers of just compensation and unfairly distorting telecommunications markets.

Embarq agrees with the importance of issuing clear call-signaling obligations and believes that the rules should be equally applicable to all carriers. *All* traffic, including VoIP traffic, should be bound by the signaling rules adopted by the Commission to facilitate proper billing.

The proposed order, however, has not gone far enough to resolve the problems associated with traffic lacking sufficient information to permit proper billing. The remaining USTelecom principles must be addressed and implemented in order to fully resolve phantom traffic concerns. In fact, the additional USTelecom principles are necessary for carriers to realize the full value of newly adopted signaling rules. For example, simply having knowledge of *which carrier* originated traffic from the signaling information and/or the call detail records is not sufficient for a terminating ILEC unless it has the ability to initiate negotiations to establish the terms and conditions under which the traffic is to be exchanged and billed. Accordingly, the *T-Mobile* decision[98] must be extended to provide a mechanism for ILECs to invoke the 251/252 negotiation/arbitration timeline and process with CLECs with which they exchange traffic.

In addition, carriers should not be allowed to route traffic for the purpose of disguising the identity of the financially responsible provider or the traffic's originating

---

[98] *Developing a Unified Intercarrier Compensation Regime; T-Mobile et al. Petition for Declaratory Ruling Regarding Incumbent LEC Wireless Termination Tariffs*, 20 FCC Rcd 4855 (2005).

jurisdiction. The USTelecom principles attempt to mitigate this type of routing behavior, as such routing practices would be deemed an unreasonable practice.

3. Financial Obligations Must be Reasonably Balanced Between Tandem Owners and Carriers Using Tandem Services.

Embarq fully supports the USTelecom's call for a rule that requires tandem owners to transmit, unaltered, signaling information in the call signaling stream. Specifically, Embarq supports the indisputably sensible principle set out by USTelecom:

- "Every provider to transmit, without alteration, except where not feasible with network technology deployed at the time the call was originated, or where PSTN industry standards would dictate otherwise, the telephone number information that it receives from another provider in signaling."[99]

The Commission, however, must not and cannot fairly or rationally impose financially burdensome responsibilities on transit providers. Embarq is sympathetic to rural ILECs who receive a substantial percentage of their traffic through an intermediary tandem owner and also understands that many rural ILECs have been terminating traffic on their networks for no compensation. The proposed order has plainly overreached, however, by requiring tandem owners to essentially be placed in a "banker role" by requiring them to pay the subtending carrier's highest rate and bear the burden of collecting from carriers upstream in the call signaling path. Such rules will establish unintended, new opportunities for terminating carriers to simply bill the intermediate tandem owners for traffic that is uncollectable for reasons other than simply being "unidentified" due to lack of CPN in the signaling stream.

---

[99] Letter from Glenn Reynolds (USTelecom) to Marlene Dortch (FCC) at Att. 8-15, WC Docket No. 01-92 (Feb. 12, 2008) at Att. p. 10.

For instance, many CLECs and CMRS carriers prefer to not negotiate interconnection agreements with rural ILECs and establish network connections. Given that the Commission has not extended the *T-Mobile Order* to CLECs, rural ILECs have experienced difficulty bringing many competitive carriers to the negotiation table to establish the terms and conditions governing the exchange of their traffic as the competitive carriers benefit from the lack of an agreement. Therefore, much of this traffic has been terminated on the small ILEC network for no compensation.

The rules must clearly state that tandem owners cannot be held liable in this instance. New disputes will likely arise as subtending carriers and tandem owners will disagree on the "sufficient" nature of the information provided, generating new disputes. While tandem owners must play a role in cooperating with terminating carriers to ultimately allow terminating carrier to bill originating carriers, allowing intermediate tandem owners to be "default" billed forces the tandem owners to spend resources in disputes with originating carriers or risk substantial financial losses. The proposed order appears to "expressly permit service providers subject to this charge to pass it along to the service provider that delivered that applicable traffic to them," but Embarq believes it to be unlikely that tandem owners will be able to easily collect for this traffic.

An additional concern pertains to requiring tandem owners to distribute call detail records to all carriers in the downstream call path.[100] This new obligation will likely be costly for tandem owners to implement. The current standard industry practice is for tandem owners to create and distribute call detail records to the ultimate terminating carrier, but not to all carriers in the downstream call path, such as other tandem owners.

[100] FNPRM at App. A ¶ 337 n.875, App. C ¶ 333 n.870.

It is not efficient from a network perspective for calls to be routed through multiple tandems. Secondary tandem owners would never be involved in a call path, and Embarq believes this problem of double-tandeming could be largely avoided, if competitive carriers were required to establish trunking to all ILEC tandems in each LATA. In other words, there would be no need to require initial tandem owners to pass call detail records to subsequent tandem owners in a call path.

It is generally accepted throughout the industry that double-tandemed traffic significantly increases the volume of unidentified traffic. It is unclear whether the proposed order's new rules regarding tandem owner responsibilities allow the second tandem owner in the call path to "default" bill a transit fee to the initial tandem owner if it does not pass a call detail record to the subsequent tandem owner to identify the originating carrier to ensure proper billing. While Embarq disagrees with the concept of "default" billing a tandem owner, a Commission rule allowing financial obligations to fall to a tandem owner must make clear the terminating carrier cannot "default" bill the second tandem owner in the call path. The second tandem owner in the call path does not generate the call detail record and will not have any ability to influence the information ultimately received by the terminating carrier.

As mentioned above, several critical aspects of USTelecom's proposal must be ordered by the Commission to realize the desired public policy impacts of an improved phantom traffic reform solution. While reforming intercarrier compensation rates and reducing current rate disparities will reduce incentives to disguise traffic jurisdictions, the necessary transitions implemented by the Commission prior to reaching rate uniformity allow carriers to continue to find ways to mask traffic and pay unjust lower intercarrier compensation rates than is proper.

Therefore, it is critical that the Commission implement a rule that would deem it an unreasonable practice for a provider to route traffic for the purpose of disguising the identity of the financially responsible provider or the traffic's originating jurisdiction. Embarq continues to police arbitrage traffic and identify ways in which carriers are routing traffic in a manner that is intended to disguise the traffic's actual jurisdiction. Currently, Embarq has millions of dollars in dispute as a result of carriers' attempts to mask the accurate jurisdiction of a call. Some examples of the arbitrage Embarq has identified include:

- Routing non-local traffic subject to terminating access charges over local interconnection trunks to avoid the access charges and pay lower reciprocal compensation rates or even bill and keep as commingling disparate traffic bypasses the capability of carrier systems ability to detect and properly bill in an automated fashion;

- Routing traffic that originates and terminates within the same traffic out of the state or even internationally with the intent avoiding intrastate access charges by failing to provide accurate call detail record information;

- Routing wireless traffic over CLEC interconnection trunks to avoid paying the wireless rates and instead benefit from the CLEC's negotiated bill-and-keep compensation arrangement (wireless ICAs typically do not include such bill and keep provisions); and

- Routing traffic to a tandem not serving the called NPA/NXX to avoid transit charges from the second tandem transit provider in the call path as call detail record information is lost after hitting the initial tandem.

In addition, the Commission's *T-Mobile Order* expressed a desire for ILECs and CMRS carriers to negotiate agreements to govern the terms and conditions of the traffic exchanged between their networks. This same rationale must also be applied to CLECs and is one of the key aspects of the USTelecom proposal. In order for terminating ILECs to attain full value of new signaling rules identifying the originating carrier, it is necessary for the ILEC to execute an agreement with originating CLECs. Some CLECs currently benefit financially by not having an agreement, so they prefer not to enter into the section 251/252 process to achieve an agreement.

Like many rural ILECs, Embarq has identified CLECs terminating indirect traffic on its network without an interconnection agreement in place. Although in some instances the originating CLEC has agreed to enter into an interconnection agreement, many choose to be unresponsive to negotiation requests. Many CLECs continue to leverage the *T-Mobile Order* as support for "stiff-arming" an ILEC request to negotiate, which allows CLECs to continue to avoid compensating the terminating ILEC. See the attached letter from one CLEC unwilling to negotiate with Embarq and citing the *T-Mobile Order* as a rationale for its actions.[101]

VI. FURTHER NOTICE OF PROPOSED RULEMAKING (FNPRM ¶¶ 339-End).

A. Universal Service Further Notice (¶¶ FNPRM 339-341).

The FNPRM seeks comment on "an appropriate universal service mechanism (or mechanisms) focused on the deployment and maintenance of advanced mobile wireless services in high-cost and rural areas."[102] As discussed above, Embarq has proposed a plan for providing sufficient and targeted support for high-cost, rural regions. Embarq's "Broadband Carrier of Last Resort Solution," filed September 18, 2008, laid out the competitively neutral mechanism by which carriers other than incumbent carriers — and, specifically, wireless carriers — would be able to receive funding for serving high-cost areas.

---

[101] A copy of the letter, dated June 1, 2006, is attached to these comments.

[102] FNPRM at App. C ¶ 339.

In the BCS proposal, all recipients of funding (wireline or wireless carriers) are eligible for specific, targeted support on a wire-center-by-wire-center basis if the carrier agrees to provide advanced service to 85% of the customer locations within the supported area within a five year period. This advanced service must be provided using the carrier's own network, and this obligation is in addition to the obligation to provide the current supported service to all customers in the wire center.

Unlike the Commission's proposal described in Appendix A and Appendix C, the BCS proposal is both sufficient and predictable, because the amount of support available to wireless carriers (and wireline carriers) in these areas is re-calculated at a more granular level than a study area. Consequently, there are areas that would receive funding under the BCS proposal that receive no high cost support today. As described in the BCS filing itself, however, this is accomplished without an increase to the overall size of the fund.

By obligating wireless carriers to expand their networks throughout the wire center, and by requiring wireless carriers to offer advanced services to 85% of the customers in each supported wire center, the BCS proposal achieves the very goals outlined in the FNPRM. Wireless carriers are encouraged to deploy and maintain advanced wireless services in areas that may currently be underserved. And by offering sufficient support to these wireless carriers without increasing the overall fund, it resolves the Commission's concerns about fund growth and the overall size of the fund.

B. Intercarrier Compensation Further Notice (¶¶ FNPRM 343-346).

1. The Commission Should Not Establish Default Transit Rates, but Should Direct Users and Providers to Negotiate Agreements for Transit Services.

The Commission seeks comment about whether it should establish a default transit rate for transit services provided for indirectly interconnected carriers. The Commission should not establish default transit rates, and Embarq believes firmly that the most appropriate rate for transit services is established through a negotiation process between the tandem transit provider and the user of transit services.

A negotiated rate is necessary to allow transit providers and users the opportunity to negotiate mutually beneficial rates. A default rate fails to account for the numerous factors that cause transit costs to vary and, accordingly, would fail to result in rates that are more closely aligned with costs. A couple of the major factors influencing costs include the location of the tandem switch (urban vs. rural areas) and the utilization level of the tandem switch providing the intermediary service. As a largely rural ILEC that provides transit services across many of its states, Embarq believes that any default transit rate established by the Commission would very likely be far too low to cover the network costs associated with providing the transit service in the majority of the rural markets served by Embarq. The costs Embarq incurs to provide transit services vary greatly from the costs incurred by larger, urban RBOC tandem owners and a default rate would likely not account for the significant and very real cost differences between rural and urban markets. A default rate is highly unlikely to be able to account for these differences and would harm rural tandem owners.

2. Providing Transit Services is Not a Statutory Obligation.

The Commission should affirm that the provision of transit services is not a statutory obligation. Accordingly, these services need not be provided at a cost-based rate. Rather, the rates, terms and conditions for transit services should be negotiated as part of a commercial transit agreement. Given that competition for transit services exists in most urban and suburban territories and is increasing, buyers of transit services have real and growing alternatives for the provision of transit services. One such competitive alternative in the transit market is Neutral Tandem. Neutral Tandem provides competitive transit services to over 70 wireless, CLEC, cable and VoIP providers. Embarq's tandem serving areas overlap Neutral Tandem's markets throughout Florida and the Las Vegas, NV market, as well as extensive coverage in Ohio, and some parts of Pennsylvania, and Indiana. In addition, Neutral Tandem's website lists Embarq's Kansas and Missouri rural markets as "Planned for Development."

Combined with the Phantom Traffic solution in Appendix C where tandem owners are placed in the role of the "banker" to be responsible to pay subtending carriers without assurance of collecting from originating carriers, the prospect of a default rate is daunting. Tandem owners will be placed in the position of facing increased risk and costs without the ability to increase prices to offset these new factors. Such a result is contrary to sound business practices and would produce a bad public policy outcome.

3. The Commission Should Affirm that Competitive Carriers are Financially Liable for Traffic Exchanged Indirectly with a Rural Carrier.

Transit services are provided by tandem owners to allow carriers to connect their networks indirectly. It is the tandem owner that facilitates this indirectly exchanged traffic. In situations where a mid-sized or rural ILEC is one of the indirectly interconnected carriers, it is, in most cases, a competitive carrier, such as CLEC or CMRS carrier, that made a deliberate business decision to not establish the direct connection with the ILEC network.

The competitive carrier is voluntarily entering into this business arrangement. It will have reviewed other alternatives, and chosen to exchange traffic indirectly via the transit provider network. The Commission should affirmatively state that the competitive carrier is liable for the transit charges for indirect traffic exchanged in both directions with a rural carrier.

VII. CONCLUSION

Embarq supports comprehensive reform of universal service and intercarrier compensation. However, the proposed order is counterproductive for broadband deployment, destructive to investment, harmful to rural consumers, unfair to many carriers, and likely to be reversed. Embarq has been working with industry, consumer groups, and the Commission to develop a sensible and viable reform approach based on modifications to the proposed order. Proposals by ITTA and USTelecom appear particularly promising, based on the work that has been done so far. Embarq anticipates supporting both of them.

Respectfully submitted,

EMBARQ CORPORATION

By:________________________

David C. Bartlett
Jeffrey S. Lanning
John E. Benedict
701 Pennsylvania Ave., NW, Suite 820
Washington, DC 20004
(202) 393-1516

November 26, 2008