

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

_____)	
In the Matters of)	
)	
Petition for Declaratory Ruling Regarding)	
Access Charges by Certain Inserted)	
CLECs for CMRS-Originated Toll-Free)	
Calls)	
)	
Access Charge Reform)	CC Docket No. 96-262
)	
Developing a Unified Intercarrier)	WC Docket No. 01-92
Compensation Regime)	
_____)	

REPLY OF LEVEL 3 COMMUNICATIONS, LLC

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SUMMARY

Level 3’s petition questions the legality of kickbacks paid by certain “Inserted CLECs” to wireless carriers in connection with the delivery of toll-free wireless traffic. Not every CLEC that carries toll-free traffic from a wireless carrier to an IXC is an “Inserted CLEC” as defined in Level 3’s petition. The petition addresses only those CLECs that pay kickbacks to wireless carriers. In exchange for the kickback, a wireless carrier diverts its toll-free traffic to a particular CLEC, rather than sending that traffic to an IXC such as Level 3 through an ILEC or otherwise. The Inserted CLEC funds its kickbacks by levying originating access charges to IXCs that can be more than five times higher than those charged by ILECs under more traditional routing arrangements – that is, the arrangements that the wireless carrier would choose were it paying for this transit service. Level 3 seeks a determination as to whether these practices are lawful. If not, as Level 3 believes, they should be halted for all carriers; if so, Level 3 would like to know that it can engage in similar practices.

Hypercube Telecom, LLC (“Hypercube”), a proponent of kickback-driven access charges for wireless toll-free traffic, opposes Level 3’s petition. Although Hypercube claims to comply with the FCC’s CLEC access charge rules, it does not dispute that the access charges it bills Level 3 are many times in excess of the charges that would be billed by competing ILECs for identical services. Nor does it dispute that Inserted CLECs share the proceeds of their tariffed access charges with wireless carriers in exchange for the wireless carrier’s routing toll-free traffic through them. And it cannot dispute that kickback schemes distort the traffic routing choices of wireless providers, giving them a powerful financial incentive to route toll-free traffic through kickback-

paying Inserted CLECs rather than any other competing carrier. The plain purpose of the kickback is to affect these routing choices for toll-free traffic – where the originating caller has no customer relationship with the IXC and the IXC picks up the tab for choices made by others.

Hypercube concedes that Congress and the Commission prohibit wireless carriers from tariffing their own access charges – a deliberate and express policy choice that wireless access charges are governed solely by commercial agreements between the wireless carrier and the IXC. Yet by remitting access charges to the wireless carrier without any contractual agreement with the IXC, Inserted CLEC schemes evade the Congress’ and the Commission’s deliberate policy choice by doing indirectly that which they cannot do directly.

Hypercube raises a welter of conflicting, any-port-in-a-storm arguments. Primarily, Hypercube attacks Level 3’s petition on procedural grounds, arguing both that the problem identified in the petition is so general it requires a rulemaking and that it is so specific it requires a complaint. These criticisms cannot both be true, and in fact neither is true. The rules are already clear, and the conduct at issue involves a number of CLECs apart from Hypercube.

On the merits, Hypercube asserts not that the kickbacks are in any way useful or salutary, but that they have not previously been expressly declared unlawful. In doing so, Hypercube mischaracterizes both the state of the law and Level 3’s Petition.

- Hypercube concedes that Section 332(c)(3) prevents wireless carriers from filing intrastate access tariffs. There is thus no dispute that state tariffing of Hypercube’s access charges is prohibited by federal law if those

charges are deemed to be “charges by” CMRS carriers. Hypercube argues that kickbacks are nonetheless lawful because, although wireless carriers may not themselves demand access charges, “Hypercube’s tariffs and its invoiced access charges are for work that Hypercube – and no one else – performs.” But Level 3’s very argument was that Inserted CLECs and wireless carriers cannot elevate form over substance through kickback arrangements. Where there is a kickback (and only where there is a kickback), Inserted CLEC’s access charges are “charges by” CMRS carriers, and thus cannot be levied pursuant to state tariffs (which usually have higher rates than federal tariffs).

- Hypercube argues that, although the “same services” rule requires CLECs to limit their access charges to ILEC access charges, CLECs may nonetheless charge many times the ILEC rate because (among other things) the relevant Commission order employs a “benchmark” rather than a “hard cap.” But the relevant rule provides that “the rate for the access services provided *may not exceed* the rate charged by the competing ILEC for the same access services.” 47 C.F.R. §61.26(f) (emphasis added). Even if Hypercube were correct, moreover, surely the same services rule prohibits CLEC rates that are *quintuple* the ILEC’s.
- Hypercube argues that, although the Communications Act prohibits rebates, kickbacks are nonetheless permitted so long as the Inserted CLEC charges all *LXCs* the same originating access charges. But there are two types of potential discrimination from kickbacks. The first is among the

carriers and subscribers who choose to use the Inserted CLEC's network. The second is between IXCs that are assessed charges by tariff and those that are assessed charges through direct agreement. Even if the Inserted CLEC charges the same rate to all IXCs, Hypercube's comments do not speak to the first type of potential discrimination.

- Hypercube argues that, although the Communications Act prohibits rates that are the result of anticompetitive tying, kickbacks are nonetheless permitted because they encourage wireless carriers to choose “procompetitive” CLECs for transit. But where wireless carriers choose CLECs to handle toll-free traffic on the basis of kickbacks, this choice cannot be said to be “competitive.” The plain purpose of the Inserted CLEC scheme is to exercise the market power over originating access that is otherwise constrained by the Commission's requirement that wireless carriers obtain access charges only through commercial agreements with IXCs, rather than by tariff. Toll-free calls are particularly susceptible to this arbitrage scheme because there is no customer relationship between the IXC and the originating caller. The Inserted CLEC's exploitation of its ability to tariff is critical to effectuating the tying arrangement – and thus is unjust and unreasonable.

Level 3 does not have a generalized grievance with routing traffic through CLECs, or even with “double-tandem” routing (wireless carrier to CLEC to ILEC to IXC). Indeed, Level 3 offers a tandem routing service itself – but without kickbacks. Level 3 objects only when wireless carriers and Inserted CLECs intentionally divert

traffic for reasons *other than* efficient routing or interconnection – namely, to extract extra profits from captive IXCs and their customers. Level 3 objects to such practices both as an IXC that has to pay inflated origination access charges, and as a CLEC that must compete against unlawful practices.

The Communications Act and the Commission’s Rules prohibit the Inserted CLEC kickback schemes described in Level 3’s Petition. The Commission should grant Level 3’s petition. If, on the other hand, the Commission concludes that such practices are lawful, it should clarify this matter for all carriers, so that they can also employ these tactics.

Table of Contents

	PAGE
SUMMARY.....	i
I. Kickbacks Multiply Originating Access Charges For Toll-Free Wireless Traffic.....	2
II. The Commission Should Declare That Inserted CLEC Kickbacks Violate Existing Law.....	6
A. A Petition for Declaratory Ruling is an Appropriate Means of Questioning the Legality of the Practices of Inserted CLECs.....	6
B. Section 332(c)(3) of the Communications Act Preempts Inserted CLECs' Kickback-Driven Access Charges.....	9
C. The "Same Services" Requirement of Section 61.26(f) of the Commission's Rules Prohibits CLECs from Charging Access Charges Multiples of Those Charged by the Competing ILEC.....	11
D. Inserted CLEC Kickbacks May Violate the Anti-Discrimination Provisions of the Communications Act.....	14
E. Inserted CLEC Kickbacks are Unjust, Unreasonable, and Unlawful Practices Because they Facilitate an Unlawful Tying Arrangement.....	16
CONCLUSION.....	20

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REPLY OF LEVEL 3 COMMUNICATIONS, LLC

Level 3 Communications, LLC (“Level 3”) hereby submits this reply to the comments of Hypercube Telecom, LLC (“Hypercube”) opposing Level 3’s Petition for a Declaratory Ruling.

Level 3’s petition questions the legality of kickbacks paid by certain “Inserted CLECs” to wireless carriers.¹ Not every CLEC that carries toll-free traffic from a wireless carrier to an IXC is an “Inserted CLEC” as defined in Level 3’s petition. The petition addresses as “Inserted CLECs” only those that pay kickbacks to wireless carriers. In exchange for the kickback, a wireless carrier diverts toll-free wireless traffic to a particular CLEC rather than sending that traffic directly, whether through an ILEC or

¹ Level 3 Communications, LLC, Petition for a Declaratory Ruling (filed May 12, 2009) (“Petition”). The Commission subsequently placed the petition in CC Docket No. 96-262 and WC Docket No. 01-92.

otherwise. The Inserted CLEC funds its kickbacks by levying originating access charges to IXCs that can be more than five times higher than those paid under more traditional routing arrangements – *i.e.*, routing arrangements that would be chosen if the wireless carrier were actually paying for this transit service.

Hypercube Telecom, LLC (“Hypercube”) – a main proponent of kickbacks and the only commenter thus far in this proceeding – offers no efficiency-based justification for this practice.² Although Hypercube suggests that no one would ever use a CLEC without kickbacks if it were routing and interconnecting efficiently, that is not so.³ Level 3 certainly believes that CLECs can compete with each other and with the ILECs to provide transit efficiently without utilizing kickbacks. Hypercube also defends kickbacks on the ground that they are not expressly prohibited and attacks Level 3’s petition on procedural grounds. Hypercube’s procedural and substantive claims are meritless. The Commission should grant Level 3’s petition, and declare such kickbacks unlawful.

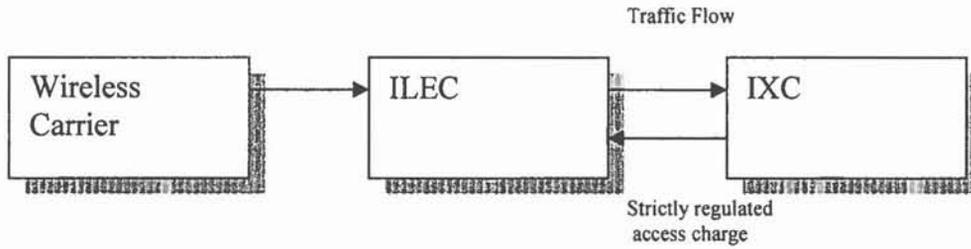
I. KICKBACKS MULTIPLY ORIGINATING ACCESS CHARGES FOR TOLL-FREE WIRELESS TRAFFIC.

Without Inserted CLECs charging unlawfully high originating access charges to fund kickbacks, determining originating access charges paid by long-distance carriers for toll-free wireless traffic would be straightforward. Wireless carriers sometimes deliver such traffic directly to long-distance carriers such as Level 3. More often, however, they route such traffic through ILEC “tandem transit” providers, who then deliver it to the IXC. Wireless carriers themselves cannot charge originating access charges directly to

² Comments of Hypercube Telecom, LLC in Opposition to Level 3 Communications, LLC’s May 12 Filing, CC Docket Nos. 96-262, 01-92 (filed May 22, 2009) (“Opp.”).

³ Opp. at 10.

an IXC unless it has a contract with that carrier.⁴ ILECs can charge originating access charges for the functions they provide in handling such traffic, but such charges are strictly regulated.⁵ Either way, originating access charges paid by the IXC for toll-free wireless traffic remain comparatively reasonable.



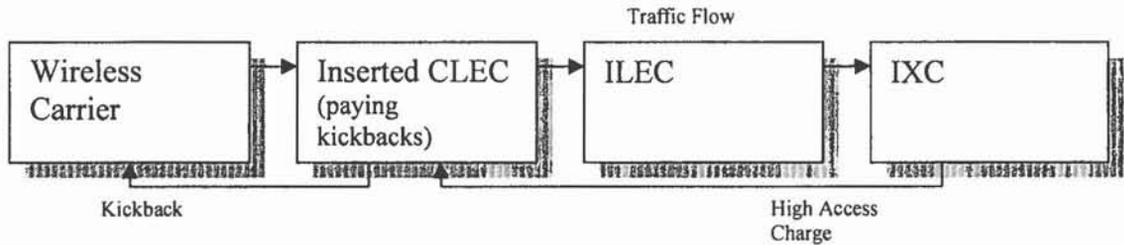
Historically, however, CLECs have been less heavily regulated than ILECs, and until the Commission and some states intervened, CLECs could charge significantly higher originating access charges.⁶ Some CLECs thus perceived an opportunity for enrichment: by offering to kick back a portion of the inflated access charges to wireless carriers (who cannot tariff access charges), a CLEC could induce wireless carriers to route long-distance traffic (particularly toll-free traffic) first to the CLEC and then to the IXC, rather than sending that same traffic directly to the IXC or routing it through the ILEC or a non-kickback-paying CLEC. Toll-free traffic is especially susceptible to this arrangement, because the originating caller (or the originating carrier in the case of a wholesale long distance arrangement) lacks any customer relationship with the IXC.

⁴ *Petitions of Sprint PCS and AT&T Corp., for Declaratory Ruling Regarding CMRS Access Charges*, 17 FCC Rcd. 13192, 13198 ¶ 12 (2002) (“*Sprint PCS*”) (stating that wireless carriers may only charge originating access charges “to the extent that a contract impose[d] a payment obligation” on an IXC).

⁵ *See, e.g.*, 47 C.F.R. §§ 61.28-61.58 and Part 69.

⁶ *Access Charge Reform, Reform of Access Charges Imposed by Competitive Local Exchange Carriers*, Seventh Report and Order and Further Notice of Proposed Rulemaking, 16 FCC Rcd. 9923 ¶ 8 (2001) (“*Seventh Report and Order*”).

Hypercube does not deny that, in this scenario, wireless carriers do not choose to route toll-free traffic through the kickback-paying CLECs for efficiency or other pro-competitive (rather than pro-competitor) purposes. Rather, they do so simply to receive the kickback.⁷



This practice permits the kickback-paying CLECs to capture a much greater share in the market for wireless-originated toll-free traffic than they would otherwise be able to obtain, at the expense of long-distance carriers. It distorts the choices of wireless providers, who have a powerful financial incentive to route traffic through Inserted CLECs rather than a competing ILEC or a CLEC that does not pay kickbacks. Instead of competing with ILECs and other CLECs on cost, quality, or reliability, the “Inserted CLEC” business model relies on pure regulatory arbitrage. Wireless carriers who have no real need for the Inserted CLEC’s services are *paid to use them* for the sole purpose of setting up a regulatory charade that grossly inflates the access charges to IXCs.

IXCs, meanwhile, are *required* by law to accept this traffic,⁸ a point Hypercube admits.⁹ Indeed, as Level 3 demonstrated in its petition, IXCs cannot even determine

⁷ Hypercube claims that the kickback *itself* is competitive. We discuss this in Part II.D. below.

⁸ *Seventh Report and Order* ¶ 97.

⁹ *Opp.* at 3.

which traffic is sent to them pursuant to a kickback scheme.¹⁰ Companies in Level 3's position are powerless to prevent Inserted CLECs from enriching themselves at the IXC's expense. Moreover, because Inserted CLECs can assess these inflated charges through tariffs, they can also inflate their demands in direct commercial arrangements – skewing the process of carrier-to-carrier negotiations. As the Commission recognized in its *Seventh Report and Order*, such circumstances permit CLECs to “impose high access rates without creating the incentive for the end user to shop for a lower-priced access provider.”¹¹

Level 3 does not have a generalized grievance with routing traffic through CLECs, or even with “double-tandem” routing (wireless carrier to CLEC to ILEC to IXC). Indeed, Level 3 offers such a service – but without kickbacks.¹² Level 3 objects only when wireless carriers and Inserted CLECs intentionally divert traffic for reasons *other than* efficient routing or interconnection – namely, to extract profits from long-distance carriers for toll-free traffic. For some CLECs, exploitation of the ability to levy higher tariffs than competing ILECs on intrastate traffic appears to be the only rationale for the existence of the carrier. Level 3 seeks Commission clarification that *this* kickback-driven activity – not the mere existence of CLECs in a call flow¹³ or the offering of tandem routing service – violates the Act and the Commission's rules.

¹⁰ Petition at 6.

¹¹ *Seventh Report and Order* ¶ 31.

¹² Accordingly, Level 3's transit services are not “Inserted CLEC” services for purposes of the Petition because Level 3 does not pay kickbacks. As discussed further below, it is the kickback that renders the Inserted CLEC's charges *de facto* charges by the wireless carrier, and thus both preempted by Section 332(c)(3) and “unjust and unreasonable.”

¹³ Hypercube also appears to believe that Level 3 asks the Commission to “adopt a new rule defining a class of carrier, apparently styled as an ‘Inserted CLEC.’” Opp. at 4. The nomenclature here is purely descriptive, however. What Level 3 seeks – as is abundantly clear from its Petition – is clarification

II. THE COMMISSION SHOULD DECLARE THAT INSERTED CLEC KICKBACKS VIOLATE EXISTING LAW.

Hypercube does not dispute that Inserted CLEC kickbacks can result in IXCs paying rates that are five times higher than the competing ILEC's for originating access charges for wireless-originated toll-free traffic. Nor does it advance efficiency-related justifications (*i.e.*, pro-competition, not just pro-competitor) for them. Rather, it attacks Level 3's petition on procedural grounds and argues that kickbacks are not unambiguously prohibited by existing law and precedent. Its procedural argument is meritless, and its substantive argument mischaracterizes both the state of the law and Level 3's Petition.

A. A Petition for Declaratory Ruling is an Appropriate Means of Questioning the Legality of the Practices of Inserted CLECs.

Hypercube spends most of its Opposition arguing procedural issues. It claims that a Petition for Declaratory Ruling is not the proper vehicle for determining that kickbacks are illegal. Instead, Hypercube argues that Level 3 should have sought a change in the Commission's rules and filed a complaint against Hypercube.¹⁴ These criticisms cannot both be true, and in fact neither is true.

A rulemaking is unnecessary because paying kickbacks to divert wireless-originated toll-free traffic for the purpose of assessing intrastate access charges or inflated interstate access rates violates multiple *existing* provisions of the Communications Act, the Commission's rules, and previous orders. Level 3's petition demonstrated that Inserted CLEC kickback schemes violate four provisions of the Communications Act and

that, in this context, kickbacks are illegal and that all kickback-driven charges are governed by federal CLEC access charge rules.

¹⁴ *E.g.*, Opp. at 8-11 (Level 3 should have sought new rules); *id.* at 8, 15 (Level 3 should have filed a complaint under section 208 of the Act).

the Commission's rules. None of these claims requires the Commission to issue new rules or modify precedent. For that reason, they are the appropriate subject of a petition seeking a declaratory ruling with retroactive effect.¹⁵

The three cases cited by Hypercube in its opposition do not suggest otherwise. Each suggests simply that declaratory rulings are inappropriate where a petitioner fails to identify rules that support its petition or merely disagrees with earlier rulings.¹⁶ Level 3 has not asserted any disagreement with prior decisions of the Commission – rather, it thinks those decisions support its view of the law. For that reason, a declaratory ruling is an appropriate means of seeking clarification of the legality of the practices of Inserted CLECs.

Nor is Level 3 *required* to file a Section 208 complaint. The *Eighth Report and Order* stated that an IXC “may” file a Section 208 complaint, not that it *must* do so.¹⁷ In any event, Level 3 does not assert that Hypercube alone engages in Inserted CLEC

¹⁵ See, e.g., *AT&T v. FCC*, 454 F.3d 329, 332 (D.C. Cir. 2006) (sustaining a declaratory ruling with retroactive effect where the petitioner seeks “new applications of existing law, clarifications, and additions”) (quoting *Verizon Tel. Cos. v. FCC*, 269 F.3d 1098, 1109 (D.C. Cir. 2001)).

¹⁶ *BellSouth's Petition for Declaratory Ruling or, Alternatively, Request for Limited Waiver of the CPE Rules to Provide Line Build Out (LBO) Functionality as a Component of Regulated Network Interface Connectors on Customer Premises*, 66 FCC Rcd. 3336 ¶ 26 (1991) (denying BellSouth's petition for a declaratory ruling on the ground that BellSouth “fail[ed] to identify any policy or Section . . . of the rules which would support” its claim); *The Public Service Commission of Maryland and Maryland People's Counsel Applications for Review of a Memorandum Opinion and Order By the Chief, Common Carrier Bureau Denying The Public Service Commission of Maryland Petition for Declaratory Ruling Regarding Billing and Collection Services; The Public Utilities Commission of New Hampshire Petition for Rule Making Regarding Billing and Collection Services*, 4 FCC Rcd. 4000 ¶ 30 (1989) (holding that a petition for a declaratory ruling is not appropriate if an interested party merely “believes an unambiguous Commission decision is incorrect”); *Federation of American Health Systems; Petition for Declaratory Ruling, or in the Alternative, Petition for Waiver*, 12 FCC Rcd. 2668 ¶ 11 (1997) (reaffirming that a declaratory ruling was inappropriate where the interested party merely disagreed with an unambiguous order, observing that it was “not inclined to issue a declaratory ruling on an issue that the Commission has fully addressed”).

¹⁷ *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*, Eighth Report and Order and Fifth Order on Reconsideration, 19 FCC Rcd. 9108 ¶ 72 (2004) (“Eighth Report and Order”).

kickback schemes – just as Level 3 is likely not the only victim of such schemes.¹⁸ While Hypercube is an outspoken proponent of kickbacks, it is likely not alone. The issues identified by Level 3 are national in scope.¹⁹ Moreover, the core issues raised in the petition are purely legal. While Level 3 could have – and may have to – file a complaint regarding Hypercube’s particular rates, its petition for declaratory ruling was a more appropriate way to raise the broader legal questions concerning kickback schemes.

Indeed, the Commission is the only body that can, in the first instance, rule definitively on the legal issues raised by this petition, as its reasonable construction of any ambiguous statutes or rules are entitled to deference by reviewing courts.²⁰ It should take this opportunity to remove any ambiguity regarding the legality of the payment of kickbacks by Inserted CLECs. This will avoid piecemeal litigation of the issues raised in the petition in state public utilities commissions and courts around the country.²¹

For similar reasons, the Commission should disregard Hypercube’s allegation that Level 3 filed its Petition to “disrupt” a complaint Hypercube filed with the California Public Utility Commission.²² In the first instance, Level 3 did not know of Hypercube’s

¹⁸ Litigation including other parties but raising similar issues has already begun in several courts around the country. See, e.g., *Hypercube, LLC and Hypercube Telecom, LLC v. Comtel Telecom Assets LP*, No. 3:08-cv-2298-B (N.D. Tex.), filed *sub nom. Hypercube, LLC and Hypercube Telecom, LLC v. Comtel Telecom Assets LP*, No. 1:08-CV-7428-LTS (S.D.N.Y. filed Aug. 21, 2008); see also *InterMetro Communications, Inc. v. MKC Data, LLC and HyperCube, LLC*, No. 2:07-cv-02820-DSF (C.D. Cal. filed Apr. 30, 2007) (involving similar claims brought by pre-paid calling card carrier).

¹⁹ See, e.g., “Request of MetroPCS Communications, Inc. for a Commission Public Notice Setting Public Comment Dates Regarding, Or In the Alternative, Motion for Extension of Time to Comment On, the Petition for Declaratory Ruling of Level 3 Communications, LLC,” filed May 22, 2009, at 2 (characterizing the questions raised here as “important and complex policy issues that impact numerous CLECs and CMRS carriers throughout the United States”).

²⁰ *Nat’l Cable & Telecomms. Ass’n v. Brand X Internet Servs.*, 545 U.S. 967 (2005).

²¹ For 2008 and 2009, Level 3 has disputed Hypercube’s bills in 43 states. In addition, as noted above, *supra* n. 18, there appears to be litigation pending between Hypercube and other carriers in at least two states.

²² E.g., Opp. at 1 (arguing that Level 3’s petition is a “sham designed to . . . disrupt Hypercube’s efforts to collect interstate and intrastate access charges long-owed by Level 3”).

California complaint when it filed its petition; a service copy of Hypercube's California complaint did not reach the designated service party until after Level 3 filed its petition, and that was the first Level 3 heard of the California filing. In any event, the Commission's consideration of the federal law issues presented by Level 3's petition cannot "disrupt" a State Commission action unless the State Commission decides that it is best to dismiss or hold its matter in abeyance pending resolution of the federal issues. Such primary jurisdiction or abeyance issues are matters best considered in the first instance by those tribunals.

B. Section 332(c)(3) of the Communications Act Preempts Inserted CLECs' Kickback-Driven Access Charges.

As Hypercube concedes, wireless carriers cannot tariff originating access charges for toll-free traffic, either at the FCC or before state commissions.²³ And the Commission has stated unambiguously that it will not construe its rules and policies to permit wireless carriers to do indirectly what they cannot do directly.²⁴ But that is precisely what occurs when Inserted CLECs impose tariffed access charges (both intrastate and interstate) for handling wireless-originated toll-free traffic and share the proceeds with wireless carriers. In its petition, Level 3 explained that access charges levied by an Inserted CLEC as a result of its contract with a wireless carrier and then kicked back to the wireless carrier are no less of a rate "charged by any commercial mobile service" than if the wireless

²³ See 47 U.S.C. § 332(c)(3) (stating that states may not regulate the "rates charged by any commercial mobile service").

²⁴ *Eighth Report and Order* 19 FCC Rcd. 9108, 9116 n.57.

carrier had levied the rate itself.²⁵ Level 3 argued that to hold otherwise would exalt form over substance.²⁶

In response, Hypercube asserts that wireless providers should be permitted to share in state tariffs because “Hypercube’s tariffs and its invoiced access charges are for work that Hypercube – and no one else – performs.”²⁷ Level 3 does not dispute that Hypercube performs work for which it charges access charges. The problem is that no one *needs* Hypercube to perform that work, and we know this to a moral certainty because instead of charging the wireless carrier for its services Hypercube actually *pays for the opportunity to insert itself into the call flow* for this toll-free traffic. The economics of the Inserted CLEC model are fundamentally indistinguishable from the economics of debt collection: wireless carriers who cannot collect access charges on their own retain an Inserted CLEC to collect access charges on their behalf, and the Inserted CLEC gets to keep a healthy portion of everything it collects. Since the effect of the arrangement is the same as if the access charges were levied directly by the wireless carrier, the legal treatment of the two situations should also be the same.

There is one and only one thing that Inserted CLECs do for wireless carriers that wireless carriers could not do for themselves: impose access charges by tariff. But when Inserted CLECS such as Hypercube are actually billing access charges *on behalf of* wireless carriers, and hiding this fact by filing a public tariff for their originating access service, this is plainly inconsistent with the Section 332(c)(3)’s preemption of state

²⁵ Petition at 11 (citing 47 U.S.C. § 332(c)(3)); *see also, e.g., Atlas Communications v. Okla. Corp. Comm’n*, 400 F.3d 1256, 1264 (10th Cir. 2005) (holding that wireless traffic does not lose its wireless character when it is handed off to a transit carrier).

²⁶ *Id.*

²⁷ Opp. at 12.

tariff's and the Commission's own mandatory detariffing of wireless carrier access services.

C. The “Same Services” Requirement of Section 61.26(f) of the Commission’s Rules Prohibits CLECs From Charging Access Charges Multiples of Those Charged by the Competing ILEC.

In its Petition, Level 3 argued that Inserted CLECs violate the “same services” requirement of the Commission’s rules when they charge quintuple the access charges of ILECs for wireless-originated toll-free traffic.²⁸ Hypercube, for its part, does not dispute that Section 61.26(f) of the Commission’s rules limits the cumulative average per minute charges that CLECs may permissibly assess for access services provided to end users whom they do not serve.²⁹

Hypercube instead offers a variety of unpersuasive arguments. First, it claims that all local exchange carriers “should charge only for those services that they provide.”³⁰ But Level 3 has never claimed that Inserted CLECs may not “charge . . . for those services that they provide.” It argues simply that the “same services” rule limits *how much* they may charge for originating access.

Hypercube next claims the *Eighth Report and Order* imposes a “benchmark,” rather than a “hard cap,” on originating access charges.³¹ The relevant rule, however, provides that “the rate for the access services provided *may not exceed* the rate charged by the competing ILEC for the same access services.”³² To the extent that Hypercube

²⁸ Petition at 12-15.

²⁹ 47 C.F.R. § 61.26(f).

³⁰ Opp. at 13 (quoting *Eighth Report and Order* ¶ 20); see also *id.* 5 (“Thus, access services associated with carrying 8YY traffic to the correct IXC have always been, and are now, fully compensable.”).

³¹ Opp. at 13.

³² 47 C.F.R. §61.26(f) (emphasis added).

perceives that a “benchmark” is somehow more permissive, the rule makes clear that CLECs are limited to the rate charged by the competing ILEC. Level 3 agrees that the CLEC has flexibility as to its rate structure and specific rates for each element, but the Commission’s rules are clear that the sum of those rates cannot exceed the ILEC’s for the same services.

Even if Hypercube were right, its argument is irrelevant. CLECs must calculate access charges “in a manner that *reasonably* approximates the competing incumbent LEC rate,”³³ and the rate charged by a CLEC is “reasonable” only if it “does not result in revenues that exceed those the competing incumbent LECs would receive from IXCs for access to [the CLEC’s] customers.”³⁴ Accordingly, CLECs cannot charge five times the ILEC rate.³⁵ This is not a close call – whether the metric used for comparison is a “hard cap,” a “benchmark,” or anything else. Indeed, the mere existence of the kickback scheme tells us all we need to know about how the two rates compare. A CLEC that pays kickbacks to originating wireless carriers has presumably set its access charges so high that it can perform all the same functions as the competing ILEC and have enough left over for the kickback. To pretend, as Hypercube does, that there might not be excessive access charges behind those kickbacks ignores reality.

Hypercube also mischaracterizes Level 3’s petition as arguing that CLEC access charges should be measured against the charges the IXC “may have paid the ILEC before

³³ *Eighth Report and Order* ¶ 21; *see id.* ¶ 48 (“If a competitive LEC charges a blended access rate other than a negotiated rate, such a rate must reasonably approximate the rate that an IXC would have paid to the competing incumbent LECs for access to the competitive LEC’s customers.”).

³⁴ *Id.*

³⁵ Petition at 8 (showing CLEC charges quintuple those of the corresponding ILEC charges).

the competing tandem provider entered the market.”³⁶ Level 3 has argued no such thing. The same services rule contemplates a comparison of the CLEC’s rates to the rates that apply when the competing ILEC performs the same functions, and Hypercube’s attempt to confuse the issue is a red herring.

Hypercube mischaracterizes the Commission’s orders in much the same way it mischaracterizes Level 3’s arguments. It is not true, for example, that “tariffed CLEC access charges for such services are ‘conclusively deemed reasonable’” in all circumstances.³⁷ While the Commission has established a conclusive presumption of reasonableness, that presumption applies *if and only if* the CLEC complies with the Commission’s “same services” benchmark.³⁸ A CLEC that charges access rates well in excess of the ILEC rate is not entitled to a conclusive presumption of reasonableness.

Likewise, it is not true that the Commission’s *Eighth Report and Order* exempted toll-free traffic from the “same services” requirement. Hypercube claims “the FCC held that it was ‘not necessary immediately to cap [CLEC] access rates for 8YY traffic at the rate of the competing [ILEC],’” and that “CLECs could ‘continue to charge the

³⁶ Opp. at 13.

³⁷ Opp. at 3.

³⁸ See *Seventh Report and Order* ¶ 60 (“CLEC access rates will be conclusively deemed reasonable *if they fall within the safe harbor that we have established.*”) (emphasis added). Hypercube also errs in its assertion that “Interexchange Carriers (‘IXCs’), such as Level 3, are obligated to purchase tariffed CLEC access services, including those related to toll-free calls made from wireless networks.” Opp. at 2 (citing *Seventh Report and Order* ¶¶ 90-97). The paragraphs cited by Hypercube address interconnection, not the payment of charges. Thus, the *Seventh Report and Order* held that a long-distance carrier “cannot refuse to provide service to an end user served by the CLEC without violating section 201 [of the Communications Act].” *Seventh Report and Order* ¶ 97 (emphasis added). The *Seventh Report and Order* does not hold, as Hypercube claims, that a long-distance carrier violates the Communications Act by accepting traffic from Inserted CLECs but refusing to pay access charges to the extent that they are unlawfully inflated. That is what Level 3 is doing here: it has suspended payments until its payments reach the amount it should have paid, after which it will resume payments at the correct rates. Subject to traffic flows, Level 3 expects it will have redeemed the overcharges and will begin remitting payments in October 2009.

previously established' rate.”³⁹ These quotes were from a Commission decision declining to decrease originating access charges for toll-free traffic at a rate faster than it decreased CLEC access charges for all other traffic. The Commission did not exempt toll-free traffic from the cap – in fact, its decision was predicated on the assumption that the CLEC would be charging rates that did not exceed the competing ILEC for the functions provided.⁴⁰

The Commission thus need not “reconsider past decisions” to conclude that Inserted CLECs violate the “same services” rule when they employ a kickback scheme to charge IXCs significantly more than is charged by ILECs.⁴¹ The Commission’s past decisions already prohibit the conduct described in Level 3’s petition.

D. Inserted CLEC Kickbacks May Violate the Anti-Discrimination Provisions of the Communications Act.

Level 3’s petition explained that the payment of kickbacks by Inserted CLECs violates the anti-discrimination principles set out in Sections 201 and 202 of the Communications Act. Those provisions forbid common carriers from making “any unjust or unreasonable discrimination in charges, practices, classifications, regulations, facilities, or services for or in connection with like communications service, directly or indirectly, by any means or device.”⁴² Level 3 argued that *if* Inserted CLECs such as

³⁹ Opp. at 5 (quoting *Eighth Report and Order* ¶ 69).

⁴⁰ *Eighth Report and Order* ¶ 72. We note that Hypercube was founded in 2005, the year after the *Eighth Report and Order*. To the extent Hypercube believes that the language in question grandfathered certain CLEC access charges, Hypercube would not have been eligible for any such grandfathering. In any event, the transition to the competing ILEC rate is long over.

⁴¹ Opp. at 8.

⁴² 47 U.S.C. § 202(a).

Hypercube offer kickbacks to some entities but not others, or if they offer higher kickbacks to some entities than others, they would violate these provisions.⁴³

In response, Hypercube claims that it is not discriminating *against Level 3*, noting that the Communications Act “precludes Hypercube from offering a rebate to *customers* that purchase Hypercube’s tariffed interstate switched access offering.” Even if Inserted CLECs charge all IXCs the same rate (which may not be the case for Hypercube), Inserted CLECs’ discrimination among IXCs is only one of two types of discrimination. Level 3’s petition claims that kickbacks to wireless carriers who route their toll-free originating traffic through an Inserted CLEC tend to discriminate against the Inserted CLEC’s real “customers” – the other carriers or subscribers who also originate traffic on the CLEC’s network but who do not receive the same kickbacks because they are not as useful in shaking down captive IXCs for exorbitant access charges from toll-free traffic.

Inserted CLECs engaging in kickback schemes do not “sell” anything to IXCs handling toll-free traffic, and IXCs thus cannot be thought of as their “customers.” Instead, as Hypercube’s own description of itself reveals, they sell “Toll Free Origination – Switching and transport service” to wireless carriers, among others, but not to IXCs.⁴⁴ From Hypercube’s own description, the price for this service is *negative*; Inserted CLECs can make so much money from inflating their access charges to IXCs like Level 3 for toll-free traffic that they can afford to *pay wireless carriers to use the CLEC’s network*

⁴³ See Petition at 23 (“*To the extent* the Inserted CLEC has non-CMRS end-user customers that are not paid a kickback, the payment of kickbacks to the CMRS customer constitutes direct price discrimination in favor of the CMRS carriers and against the Inserted CLEC’s other customers. *To the extent* that the Inserted CLEC strikes kickback deals with multiple CMRS carriers, there may well be price discrimination between those carriers, with some receiving higher kickbacks than others.”) (emphases added).

⁴⁴ Petition at 5.

and still have plenty left over for the CLEC to pocket.⁴⁵ Hypercube's attempt to describe wireless carriers as "vendors for inputs that support its offering" rather than "customers" of its tariffed service is therefore extremely misleading. The Inserted CLEC serves the wireless carrier who freely chooses to route its toll-free traffic that way, not the IXC who has no choice in the matter and would much prefer not to deal with the Inserted CLEC at all. Indeed, because these calls are routed from the Inserted CLEC to the IXC via the ILEC, the IXC will not know that the Inserted CLEC is even involved in the call routing until it receives a bill. Although it is the IXC that *pays* the Inserted CLEC, that is only because the law says that it must.

It may be that Hypercube pays the same kickback to all of its wireless (and non-wireless) customers, in which case there may not in fact be any discrimination by Hypercube (though the Inserted CLEC kickback arrangement would still be unlawful for the other reasons already discussed). But, as Level 3 has been at pains to stress, we seek a declaratory ruling not just on Hypercube's behavior, but on such kickback schemes more generally. To the extent an Inserted CLEC – whether Hypercube or another entity – offers kickbacks of ill-gotten access revenues to some users of its network but not to others, it is discriminating among users in violation of the Communications Act.

E. Inserted CLEC Kickbacks Are Unjust, Unreasonable, and Unlawful Practices Because They Facilitate an Unlawful Tying Arrangement.

Level 3's petition explained that the payment of kickbacks by Inserted CLECs violates Section 201(b) of the Communications Act by facilitating an unlawful tying arrangement.⁴⁶ Specifically, the Inserted CLEC uses kickbacks to tie a transit service that

⁴⁵ In Hypercube's case, it does not originate any traffic of its own: it has no end users.

⁴⁶ Petition at 15-19.

no one particularly needs to a product IXCs cannot do without: originating exchange access on customers' calls to toll-free numbers. This has the effect of forcing long-distance carriers to pay supracompetitive rates for the tied transit service, solely for the purpose of enriching Inserted CLECs and allowing wireless carriers to evade the regulations prohibiting them from tariffing access charges.

The Commission's mandatory detariffing of wireless services constrained wireless carriers' market power over originating access by requiring wireless carriers to negotiate arms' length agreements for the payment of access charges with IXCs. That policy is effective so long as wireless carriers deliver traffic directly to IXCs, and it is not subverted when the traffic transits through an ILEC or CLEC charging the same aggregate rates as the ILEC. But it is undermined if CLECs are permitted to negotiate kickback arrangements with wireless providers and to assess unlawfully high charges. In such circumstances, the tying of a competitive product with a non-competitive product for the purpose of generating monopoly rents is *per se* anticompetitive.⁴⁷

Hypercube does not dispute that an anticompetitive tying arrangement would be an unjust, unreasonable and unlawful practice. It denies, however, that such tying exists here. It first seems to argue that tying *cannot* occur with respect to "access charges . . . subject to the Commission's regulations [and] . . . PSC's regulations."⁴⁸ This is not right. Level 3 is forced to take Hypercube's tariffed service even when it does not want to receive such a service – which is the essence of a tie. The tie works because of the market power inherent in originating access for toll-free calls, and because Level 3

⁴⁷ See, e.g., *Eastman Kodak Co. v. Image Tech. Services*, 504 U.S. 451, 461 (1992).

⁴⁸ Opp. at 15.

cannot block Hypercube's traffic. Without the tariff, there would be no way to collect the high transit charges that fund the kickbacks.

Hypercube next suggests that there is a pro-competitive justification for the kickbacks, stating that CLECs will "oust" competitors for wireless traffic.⁴⁹ "Ousting" competitors is generally a good thing. But Level 3 has described a situation in which an Inserted CLEC is reestablishing market power over originating access for toll-free calls by using its own tariffs – market power that does not exist when the CMRS carrier must negotiate individually with the IXCs rather than having the Inserted CLEC use its tariff to compel charges. Ousting a lower priced competitor in favor of a higher priced one that uses its tariffs to exercise market power is anticompetitive, not "pro-competitive."

Hypercube also asserts that "a CMRS provider may charge carriers for access to the CMRS carrier's network pursuant to contract."⁵⁰ This is true only insofar as the contract is with an IXC, and not with an intermediary CLEC. As the FCC reiterated in the *Eighth Report and Order*, "the Commission has held that a CMRS carrier is entitled to collect access charges from an IXC only pursuant to a contract *with that IXC*."⁵¹ The Commission went on to explain, "If a CMRS carrier has no contract with an IXC, it follows that a competitive LEC has no right to collect access charges for the portion of the service provided by the CMRS provider."⁵² Indeed, Hypercube resurrects the argument that a wireless carrier may "collect access charges from an IXC if the CMRS provider has a contract with an intermediate competitive LEC" – an argument the

⁴⁹ *Id.*

⁵⁰ *Id.* at 14 (citing *Sprint PCS*, ¶ 12).

⁵¹ *Eighth Report and Order* ¶ 16 (citing *Sprint PCS*) (emphasis added).

⁵² *Id.*

Commission expressly rejected.⁵³ This demonstrates yet again that the real purpose of the Inserted CLEC scheme is to accomplish indirectly that which the Commission has already prohibited directly – which the Commission has already refused to permit.⁵⁴

⁵³ *Id.* at n. 57.

⁵⁴ *Id.* (“We will not interpret our rules or prior orders in a manner that allows CMRS carriers to do indirectly that which we have held they may not do directly.”).

CONCLUSION

Level 3's Petition describes a scenario in which Inserted CLECs use kickbacks to persuade wireless carriers to route traffic through them instead of the ILEC or other CLECs charging competitive rates. Inserted CLECs can afford to pay kickbacks because they charge originating access charges for toll-free wireless traffic many times higher than those permitted by law. This scenario is forbidden by multiple provisions of the Communications Act and this Commission's rules and past orders. For the reasons described above, and in Level 3's Petition, the Commission should declare that Inserted CLEC kickback schemes are unlawful.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Sarah Kate Wagner, certify that on this 1st day of June, 2009, I have caused a true and correct copy of the foregoing Reply to be served via first class mail, postage paid, upon:

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A handwritten signature in black ink, appearing to read "Sarah Kate Wagner", written over a horizontal line.