

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

In the Matter of)	
)	
The Ad Hoc Coalition of International Telecommunications Companies' Petition)	WC Docket No. 06-122
For Declaratory Regarding)	
Universal Service Fund Contributions)	

COMMENTS OF IDT TELECOM, INC.

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I. INTRODUCTION

In its *Petition*,¹ the Ad Hoc Coalition requests that the Commission declare revenue from the sale of prepaid calling cards to distributors and other wholesalers not be treated as end-user revenue. IDT Telecom, Inc. (“IDT”) supports this request. In fact, IDT’s corporate parent, IDT Corporation, requested the Commission in April 2006 make a similar finding and a response to the company’s request remains outstanding.² Indeed, much of IDT’s comments below restate IDT Corporation’s previously-submitted position on this issue. The Ad Hoc Coalition also requests that the Commission clarify that prepaid calling card revenue be reported in a manner consistent with GAAP, rather than based on the face value of prepaid calling cards. Subject to the clarifications provided below, IDT supports this request as well. Finally, the Ad Hoc Coalition requests that if the Commission does not issue a Declaratory Ruling, it should initiate a Rulemaking Proceeding. For the reasons stated below, IDT asserts that a Declaratory Ruling stating that the existing policy of treating the sale of prepaid calling cards to distributors and other wholesalers as end user revenues was not determined in a manner consistent with the Administrative Procedure Act (“APA”) is the only proper outcome. Any prospective changes to this policy would need to be accomplished in a manner consistent with the APA.

¹ The Ad Hoc Coalition of International Telecommunications Companies’ Petition For Declaratory Regarding Universal Service Fund Contributions, WC Docket No. 06-122 (February 12, 2009) (“*Petition*”).

² Request for Review of Decision by the Universal Service Administrator by IDT Corporation, USAC Audit Report No. CR2005CP005; CC Docket No. 96-45 (April 10, 2006).

II. LEGAL BACKGROUND

In its *First Report and Order*, the Commission adopted specific regulations regarding the assessment of, and contribution to, the USF.³ In the *First Report and Order*, the Commission ruled that a USF surcharge shall be assessed on end user telecommunications revenues only.⁴ The Commission concluded that:

[USF] contributions will be based on revenues derived from end users for telecommunications and telecommunications service, or “retail revenues”...End user revenues would also include revenues derived from other carriers *when such carriers utilize telecommunications services for their own internal uses* because such carriers would be end users for those services. This methodology is both competitively neutral and relatively easy to administer.⁵

The Commission also noted that “[b]asing contributions on end user telecommunications revenues eliminates this potential economic distortion because contributions will be assessed at the end user level, not at the wholesale and end user level... regardless of how the services are provided, their contributions will be assessed only on revenue derived from end users.”⁶ Similarly, the Commission’s USF regulations clearly provide that “every telecommunications carrier that provides interstate telecommunications services...shall contribute” to USF on the basis of its “interstate and international *end user* telecommunications revenues.”⁷

³ See *In re Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, *Report and Order*, 12 FCC Rcd 8776 (1997) (“*First Report and Order*”).

⁴ *Id.* at ¶ 843.

⁵ *Id.* at ¶ 844 (emphasis added).

⁶ *Id.* at ¶ 850.

⁷ 47 C.F.R. § 54.706(a) (emphasis added).

Nowhere in the regulations that govern universal service or in the underlying order is the term “end user” defined.⁸ As a result, term “end user” should be afforded its ordinary and customary meaning. Newton’s Telecom Dictionary defines end user as “[a]ny individual, association, corporation, government agency, or entity other than an IXC that subscribes to interstate service provided by an Exchange Carrier and does not resell it to others.”⁹ Such a definition is also consistent with the common understanding of an end user in ordinary parlance.

Furthermore, the Commission has specifically identified the limited examples where sales of telecommunications services to non-end users would be included in the universal service support contribution base, even though these sales are not sales to end users.¹⁰ Such reseller revenues that are treated as end user revenues include revenues from (i) sales to resellers that claim exemption from universal service contribution requirements under the *de minimus* exception, (ii) sales to system integrators that receive less than five percent of their revenue from telecommunications, and (iii) sales to broadcasters.¹¹ These specific examples are identified in the underlying *First Report and Order*, and are mirrored in the Form 499-A instructions.¹² By contrast, the reporting of sales to calling card distributors is not identified as such an exception either in the rules or the *First Report and Order*. Thus, sales of prepaid calling cards should only be treated

⁸ See 47 C.F.R. § 54.1 *et seq.*

⁹ Newton’s Telecom Dictionary (20th Ed.) at 301.

¹⁰ See *First Report and Order* at ¶¶ 281, 284, 298.

¹¹ *Id.*

¹² Form 499-A, Instructions at 16. The original reporting form, the Form 457, also included this language.

as “end user” sales only when they are truly sales to “end users” under the ordinary and customary meaning.

Yet, in the 2000 version of FCC Form 499-A, there is a specific line for prepaid calling card revenue that includes “card sales to customers and non-carrier distributors.”¹³ The instructions for this line provide that such revenue includes “revenues from pre-paid calling cards provided either to customers or to retail establishments” and that “[a]ll prepaid card revenues are classified as end user revenues.”¹⁴ The treatment of the sale of a calling card to distributors or retail sales outlets thus became, for the first time with the creation of the reporting Forms (either the original Form 457 or the Form 499-A), synonymous with the sale of a card to a consumer who actually uses the telecommunications service.

II. ARGUMENT

A. **Assessing USF Contributions on the Basis of Wholesale Revenue Violates the Administrative Procedure Act Because the Form 499-A’s Instructions Were Not Promulgated With Proper Notice and Comment.**

The instructions to the Form 499-A, originally included as an attachment to a Commission Order¹⁵ differ so significantly from the Commission’s underlying precedent and rules that it constitutes a separate substantive ruling distinct from the *First Report and Order*. Since the instructions implement, interpret, and prescribe the Commission's

¹³ FCC Form 499-A at line 411 (Feb. 2000). By contrast, the original Form 457 which was attached to the First Report and Order, did not include this language, rather, it only included a statement that calling card sales should include sales to users or retail establishments.

¹⁴ Instructions to FCC Form 499-A at 17 (Feb. 2000).

¹⁵ See Changes to the Board of Directors of the National Exchange Carrier Association, Inc.; Federal-State Joint Board on Universal Service, *Report and Order and Second Order on Reconsideration*, 12 FCC Rcd. 18400, 18498 (1997) (“NECA Order”). The original instructions were attached as Appendix A to the *NECA Order*.

policy with respect to the definition of end user revenue and also set forth the rights, duties, and obligations of contributors to the universal service support mechanisms, these instructions operate as a substantive rule under the APA.¹⁶ Indeed, it is IDT's experience that during audits of carriers' FCC Form 499-A, auditors from USAC refer primarily to the instructions on the Form as the basis for their decisions rather than the actual rules. Such reliance indicates that USAC uses these instructions as substantive rules rather than as merely interpretative clarifications of the Commission's regulations.

As a result, the Commission was required to provide appropriate notice to the public and afford any interested persons an opportunity to comment before the instructions were promulgated.¹⁷ By merely releasing the Form 499-A without going through the rigors of the APA, the Commission failed to put all aggrieved parties on reasonable notice of the instructions' content. Rather, the Commission merely attached the original draft of the instructions to a legally and conceptually distinct rulemaking proposal without any substantive discussion of the instructions and without inviting public comment on the instructions.¹⁸ For the instructions to be valid and binding upon contributors to USF, they must have been subject to the notice and comment procedures as set forth in the APA. Plainly put, the instructions were never subjected to the required procedures.

After publication of these instructions without the appropriate notice and comment, the Commission further declined to address the responsive comments in later

¹⁶ See 5 U.S.C. §§ 551(4), 552(a)(1)(D); *GMC v. Ruckelshaus*, 742 F.2d 1561, 1565 (D.C. Cir. 1984).

¹⁷ 5 U.S.C. § 553 (b)-(c). It should be noted that the only opportunity to comment ever provided on the instructions was for the limited purpose of addressing the Form's compliance with the Paperwork Reduction Act. See *NECA Order*, Appendix A at 18498.

¹⁸ See *NECA Order* at ¶ 80.

proceedings.¹⁹ The Commission has stated its broad application of the term end user in a report to the Congress on the state of universal service support implementation.²⁰ In the report, the Commission indicated that it includes telecommunications revenues in the universal service support mechanisms contribution base, “unless the associated services are provided to an entity that incorporates them into services that should generate their own universal service contributions.”²¹ The Commission has acknowledged the fact that it failed to raise the end user/reseller issue in the underlying Notice of Proposed Rulemaking.²²

It is axiomatic that federal regulations cannot be changed without the proper notice and comment required under the APA.²³ The absence of the appropriate notice and comment procedures in this instance renders the instructions to Form 499-A invalid. As discussed above, the Commission established in the *First Report and Order* that only sales to end users would be subject to USF. Yet, when the instructions to the Form 499-A were published, there was a different substantive rule established which is in direct conflict with the governing federal USF regulations. There can be no question that the change in the meaning of the term end user for the purposes of sales of prepaid calling cards substantively altered the way IDT would be required to report its services on the

¹⁹ In re 1998 Biennial Regulatory Review – Streamlined Contributor Reporting Requirements Associated with Administration of Telecommunications Relay Services, North American Numbering Plan, Local Number Portability, and Universal Service Support Mechanisms, CC Docket No. 98-171, *Report and Order*, 14 FCC Rcd. 16602 (1999) at ¶26. (“*July 1999 Order*”).

²⁰ In re Federal-State Joint Board on Universal Service, *Report to Congress*, CC Docket No. 96-45, (Apr. 10, 1998).

²¹ *Id.* at n.133

²² *See July 1999 Order* at ¶ 26.

²³ 5 U.S.C. § 551-553(c).

Form 499-A, and consequently, contribute to USF. As such, the instructions are unlawful and unenforceable for want of notice and comment.

It is clear from reading the governing USF regulations (aside from the invalid Form 499-A instructions) that revenue from calling card sales to distributors and resellers is not end user revenue, and thus may not be included in a carrier's USF contribution base. Rather, this revenue is more properly categorized as wholesale revenue and thus should not serve as the basis for USF contribution calculated based on end user revenues. As virtually all of IDT's prepaid calling cards are sold through a distributor rather than directly to the public, IDT's calling card sales are almost exclusively wholesale, not retail, revenue.

B. Even if the Instructions to Form 499-A are Deemed Interpretative Rules and Thus Immune from the APA's Notice and Comment Requirements, the Instructions are Still Invalid Because They Conflict with the Commission's USF Regulations That Impose USF Contributions Only On End User Revenues.

If the instructions to Form 499-A are deemed to be merely "interpretative" rules rather than "substantive" rules, in which case notice and comment are not required, the Form 499-A's instructions are still invalid because they clearly conflict with the Commission's regulations providing that USF contributions will be assessed on the basis of end user revenues.²⁴ In fact, The FCC Form 499-A essentially admits that it is only interpretative, and thus without binding force. The instructions to Form 499-A contains various disclaimers that the Commission's regulations and orders take precedence over the Form. For example, the instructions state that "[t]hese instructions contain an explanation of which carriers must contribute to particular mechanisms... but filers

²⁴ 47 C.F.R. § 54.706(b).

should consult the specific rules that govern contributions for each of the mechanisms.”²⁵

The instructions further state that “[f]ilers should consult the Commission’s rules and orders to determine whether they must contribute to one or more of the mechanisms.”²⁶

Compared to the Commission’s rules, the instructions to FCC Form 499-A expand the definition of end user revenue. Such disclaimers are an admission that instructions are inferior and subject to the Commission’s regulations and precedent.

In the *First Report and Order*, and in its Part 54 regulations governing USF, the Commission did not specifically define “end user,” thus relying on the ordinary and customary meaning. However, as outlined above, it is clear from the *First Report and Order* that the Commission made a distinct delineation between end user revenues and wholesaler revenue in the contribution methodology for the USF. Despite the clear and unambiguous language in the governing regulation regarding the term “end user”, the instructions to Form 499-A unlawfully redefine the USF contribution base to include revenue from any customer who is not a contributor to the USF, including someone who is, by common parlance, a reseller or distributor.²⁷ The instruction’s definition of “end user” is at odds with the common understanding of the definition of end user. Applying the common meaning of “end user” to prepaid calling card sales results in a determination that such sales made to distributors or resellers are not made to “end users.”

²⁵ Instructions to Form 499-A at 4.

²⁶ *Id.* at 30, n.38.

²⁷ Form 499-A, Instructions at 19. Originally, this instruction appeared in the predecessor Form 457. *See*, FCC Public Notice (rel. Aug. 4, 1997), 62 Fed. Reg. 43165 (Aug. 12, 1997) (announcing OMB approval of the Form).

In reviewing such rules, a court will defer to an agency's interpretation of its ambiguous regulation,²⁸ but will not defer to such interpretation if the regulation is unambiguous.²⁹ There is nothing ambiguous about the definition of "end user," as demonstrated by the Commission's consideration in the *First Report and Order* that USF contributions should not be based on total sales, but rather, based only on end user sales. Indeed, in so doing, the Commission consciously and directly considered the definition of end user to be so unambiguous, that nowhere in either the *First Report and Order* or in subsequent decisions, did the Commission ever specifically address the definition of "end user."

This failure to define "end user" is understandable, as the meaning cannot reasonably be understood to refer to anything other than the actual final purchaser and user of a telecommunications service. In fact, within the same Form 499-A instructions, prepaid calling providers are instructed to report revenue based on the amount actually paid by the consumer (typically the face value of the card), and not, by contrast, the price paid by the distributor or the retail outlet (priced at a wholesale discount).³⁰ This conflict within the same instructions indicates the absurdity of defining a distributor as an end user for USF reporting and contribution purposes. If the distributor was truly the end user, then the reporting would be done based on the revenue received from the

²⁸ *Auer v. Robbins*, 519 U.S. 452, 461 (1997); *see also Bowles v. Seminole Rock & Sand Co.*, 325 U.S. 410, 413-14 (1945).

²⁹ *Christensen v. Harris County*, 529 U.S. 576, 588 (2000). The Supreme Court held that *Auer* deference is warranted only when the language of the regulation is ambiguous, otherwise to defer to the agency's interpretation would be to permit the agency, under the guise of interpreting a regulation, to create *de facto* a new regulation. *See id.*

³⁰ Form 499-A, Instructions at 22. The instructions for Line 411 specifically state that "[g]ross billed revenues should represent the amounts actually paid by customers and not the amounts paid by distributors or retailers..."

distributor, not the ultimate price paid by the consumer. This anomaly can be easily rectified by simply applying the proper, common sense definition of end user as contemplated in the Commission's regulations and the underlying Orders rather than the instructions from the Form 499-A.

C. Prepaid Calling Card Providers Should Be Allowed to Report Revenue Consistent with GAAP.

The Ad Hoc Coalition also requests that calling card providers be allowed to report revenue from the sale of calling cards based on revenue received, *i.e.*, in a manner consistent with GAAP, rather than the revenue "received" based on the face value of its prepaid calling cards. IDT believes this request, for the purpose of determining end-user revenue subject to USF, is something of a red herring for the below-stated reasons, although to the degree the request is relevant, IDT supports it.

Most of the discounted sales of prepaid calling cards are done within the context of the sale of cards to distributors. Based on the arguments presented above and by the Ad Hoc Coalition, revenue from the sale of prepaid calling cards to distributors is not subject to the USF. Therefore, acknowledging that reported revenue should be based on the amount billed to a wholesaler/reseller, rather than on the face value of a prepaid calling card will not have any impact on the prepaid calling card provider's USF contribution: the primary impact will be on simplifying the reporting carrier's reporting process.

Obviously, addressing the reporting of revenue from the sale of pre-paid calling cards to end users is critical; as such reporting *will* have an impact on contributions to the Fund. Generally, there are fewer discounts involved in the sale of prepaid calling cards to end users, but, to the degree the face value of a card differs from the charge imposed

upon an end user, prepaid calling card provider should be able to reduce that difference should be reflected in the provider's reportable end-user revenue. For example, if an IXC refunds \$1.00 for every \$10.00 of international toll service purchased from a presubscribed end user, the IXC can report on its 499-A a net \$9.00. If a PPCC provider chooses to sell a calling card with a face value of \$10.00 to an end user for \$9.00, the provider should be afforded the same opportunity as the IXC to report its actual revenue.

But while IDT agrees that the GAAP methodology should be available to prepaid calling card providers, we do not support that it be mandatory. Because prepaid calling card providers may have wholesale and retail calling card businesses and different business models for the sale of their cards, it may be difficult for some providers to account for all the different models in their reporting. Therefore, IDT recommends that the Commission should clarify that revenue from the sale of prepaid calling cards *may* be reported using a methodology consistent with GAAP or, in the alternative, using a methodology that will not result in less revenue being reported than would otherwise be reporting using GAAP. If subject to an audit, it would be the responsibility of the prepaid calling card provider to demonstrate, upon request, that its methodology results in an amount reported that is equal to or greater than the amount that would be reported under GAAP.

III. CONCLUSION

In light of the foregoing reasons, IDT respectfully requests that the Commission clarify that revenues from the sale of prepaid calling cards to distributors and other wholesalers are not end user revenues and should not be included in the base used to compute universal service contributions. Any changes to this policy should be done prospectively only, and in a manner consistent with the APA. The Commission should also clarify that revenue from the sale of prepaid calling cards may be reported in a manner consistent with GAAP or, in the alternative, in accordance with a methodology that results in an amount reported that is equal to or greater than the amount that would be reported under GAAP.

Respectfully submitted,

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