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

In the Matter of	)	
	)	
Connect America Fund	)	WC Docket No. 10-90
	)	
A National Broadband Plan for Our Future	)	GN Docket No. 09-51
	)	
Establishing Just and Reasonable Rates for Local Exchange Carriers	)	WC Docket No. 07-135
	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337
	)	
Developing an Unified Intercarrier Compensation Regime	)	CC Docket No. 01-92
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	
Lifeline and Link-Up	)	WC Docket No. 03-109

COMMENTS OF XO COMMUNICATIONS, LLC

Brad E. Mutschelknaus
Edward A. Yorkgitis, Jr.
Denise Smith
Kelley Drye & Warren LLP
3050 K Street, NW – Ste. 400
Washington, DC 2007
202-342-8500
Counsel to XO Communications, LLC

Heather B. Gold
Lisa R. Youngers
Teresa K. Gaugler
XO Communications
13865 Sunrise Valley Drive
Herndon, Virginia 20171

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COMMENTS OF XO COMMUNICATIONS, LLC

XO Communications, LLC ("XO"), through counsel, hereby provides its Comments in response to the Notice of Proposed Rulemaking and Further Notice of Proposed Rulemaking (the "*Notice*" or "*NPRM*") issued by the Federal Communications Commission (the "FCC" or "Commission") in the above-captioned proceeding on February 9, 2011. Separate comment cycles were established with respect to issues discussed in Section XV of the Notice, and XO previously filed comments regarding the issues raised therein. These Comments respond to the request for comment on the remaining matters raised in the *Notice*.[1]

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[1] *In re: Connect America Fund; A National Broadband Plan for Our Future; Establishing Just and Reasonable Rates for Local Exchange Carriers; High-Cost Universal Service Support; Developing an United Intercarrier Compensation Regime; Federal-State Joint Board on Universal Service; Lifeline and Link-Up,*

Introduction and Summary

The Commission is well aware of the myriad flaws in the current intercarrier compensation system, in particular that the current rules create arbitrage opportunities and hinder deployment of IP networks. The Commission should strive to accomplish National Broadband Plan goals with policies that shift the focus from circuit-switched networks to broadband infrastructure. Therefore, XO urges the Commission develop strong IP interconnection policies in conjunction with the reform of intercarrier compensation. In particular, XO submits a proposal for IP interconnection – the exchange of traffic between carriers in an IP format – and intercarrier compensation reform that would create incentives to migrate to all-IP networks while still permitting an appropriate transition from legacy TDM traffic exchange. Critically, the Commission should develop policies for IP interconnection that apply regardless of the technology used by each carrier to serve its end users.

While XO supports the general objectives of the Commission's proposals to unify and reduce TDM intercarrier compensation rates, XO does not believe that the Commission's proposals would truly modernize its rules, reduce waste and inefficiency, and establish market-driven and incentive-based policies for IP deployment. The current intercarrier compensation rate structures and interconnection policies are burdensome and inefficient, and maintenance of TDM interconnection facilities frustrates the rapid deployment of IP services to end users.

Notice of Proposed Rulemaking and Further Notice of Proposed Rulemaking, FCC 11-13 (Feb. 9, 2011) ("*NPRM*").

XO urges the Commission to confirm that Section 251 interconnection rights and obligations exist for IP interconnection as well as TDM interconnection. In particular, section 251(c)(2) obligates ILECs to provide interconnection to any requesting telecommunications carrier at any technically feasible point within the LEC's network under just, reasonable, and nondiscriminatory rates and terms. These interconnection obligations are neither specific to any particular technology nor targeted to apply only to legacy TDM networks that existed at the time the Telecommunications Act was passed. Therefore IP interconnection clearly must be provided by all carriers for the exchange of telecommunications traffic, regardless of the network on which it originated or technology used to serve the parties at either end of the call.

The Commission can and should encourage broadband investment through development of appropriate rate structures and policies regarding TDM and IP networks. By quickly removing subsidies from rates for TDM-based interconnection arrangements, the Commission would remove the appeal for carriers to maintain such networks and interconnection arrangements since they are inherently more expensive to operate than IP networks. Moreover, by adopting an IP rate structure that permits originating (or intermediate) carriers to immediately incur lower termination costs than those for TDM interconnection, the Commission would create market-based incentives for carriers to deploy IP further into their networks.

XO supports the Commission establishing a pricing methodology under section 251(b)(5) that explicitly supersedes section 251(g) and provides a glide path for reduction of TDM rates. Furthermore, XO supports the Commission's proposal to first reduce intrastate access charges to interstate levels and then to transition those rates to reciprocal compensation levels or lower within five years. As discussed more fully below, XO firmly believes that the best way to achieve the NBP's goals to encourage, rather than deter, investment in IP networks is to eliminate TDM interconnection and termination rates after a reasonable transition to IP interconnection, which XO believes can also be achieved within five years.

Saddling IP-to-IP interconnection arrangements with legacy intercarrier compensation applicable to TDM-based interconnection would continue to impede the progress of IP deployment. Thus, the Commission should immediately adopt lower rates for IP-to-IP exchange of traffic, rather than prioritizing parity of rates among different types of traffic exchange and interconnection. XO proposes that roughly-balanced traffic volumes exchanged between carriers on via IP-to-IP interconnection should be terminated on a bill-and-keep basis. For out of balance traffic volumes, however, XO recommends that the Commission adopt a tiered flat rate structure that closely approximates the additional costs incurred in terminating out-of-balance traffic.

The full benefits of IP technology cannot be realized while carriers must continue to maintain TDM interconnection and access circuits at each of the ILEC tandems and/or end offices throughout the country, rather than in a handful of locations as is common under IP peering arrangements. Therefore, XO urges the Commission to adopt its proposal to require carriers to offer and use IP interconnection for the exchange of all traffic within five years. Once IP interconnection arrangements are in place, no terminating carrier should be permitted to require conversion to a particular format for exchanging traffic, regardless of the technology used to serve any particular end users. Thus, during the transition period, each originating (or intermediate) carrier would have the option to determine whether to deliver traffic via a TDM POI or IP POI and would pay according to the corresponding intercarrier compensation regime. After a transition period, all carriers should be required to exchange traffic in an IP format, and terminating carriers should be permitted to refuse to accept traffic via TDM interconnection arrangements where IP interconnection is available. By setting a date certain when carriers may realize the full benefit of terminating traffic on their IP networks without incurring costs of conversion, the Commission would strongly encourage carriers to quickly deploy IP networks.

There is broad agreement that the interstate Universal Service Fund ("USF") program has grown uncontrollably over the past dozen years even while the contribution base has been shrinking, leading to a tripling of the contribution factor over that period. The appetite for ever more subsidy support has been insatiable, and the system is fast approaching the breaking point. The instant *Notice* seeks to reform only the distribution side with no consideration for corrections on the contribution side. XO submits that reform of the USF must be comprehensive, addressing *both the contribution and distribution* sides of the fund. Otherwise, the prospect for over-commitment to subsidy programs remains.

Reform of universal service on the distribution side must begin with the immediate imposition of a "*hard cap*" on the High Cost Program at current levels. As Commissioner McDowell suggests, the Commission should adopt and implement a plan to *reduce* the size of this program over time. XO urges the adoption of the following reforms without delay: the reimbursement rate for High Cost Loop Support must be reduced substantially; a ceiling should be established for Interstate Common Line

Support at $250 per line monthly to end abusive claims for subsidies; and the Local Switching Support subsidy should be rapidly phased out. In addition, the Interstate Access Support ("IAS") program should be ended immediately. Created in 2000 expressly as an interim program as part of a five-year transition plan, the IAS is no longer needed to ensure the availability of rural voice service on reasonable terms. Finally, the "identical support" rule for ETCs should be eliminated immediately, which should reduce the High Cost Fund by $1.1 billion, monies which should not be shifted to the new Connect America Fund ("CAF") as proposed in the *Notice*. In many areas, USF support is paid to multiple ETCs on an "identical support" basis, burdening consumers with supporting unnecessary duplicative services.

The High Cost funds should be redirected to the CAF and, thus, toward the most efficient, capable, and forward-looking IP-based technologies in unserved and underserved areas. Where providers do not offer these IP-based services because their networks have not completed the migration from circuit-switched operations, consumers of services in those areas will suffer relative to those that have IP-based services. Because the evolution toward IP-networks and the services they support is the clear industry trend, Universal Service support recipients should be required to invest toward the future rather than further entrenching the circuit-switched networks of the past. Firm milestones should be set to complete the transition entirely to the CAF with the minimum delay.

CAF funding should be distributed through the use of competitive bidding or reverse auctions to a single provider in any given area and on a technology-neutral basis. The reverse auction model has been used successfully in a number of state universal services program and in other countries of the world. CAF should immediately replace any existing voice support attributable to the service area related to the winning bid. The Commission must ensure that ILECs and other recipients of current high cost funding do not continue receiving High Cost support for voice-only networks.

Finally, reform should abandon assurances of revenue neutrality, as any mechanism that guarantees compensation for lost revenue would preserves today's uneconomic and anticompetitive subsidies in just a different set of clothes. XO submits that providers desiring an opportunity to preserve complete or partial revenue neutrality should look no further than their own end users. Specifically, the Commission should remove the current caps on the interstate Subscriber Line Charge ("SLC") and allow market forces to establish how much "lost revenue" can be recovered. Such deregulation should be the sole means of lost revenue recovery available to carriers.

I. INTERCARRIER COMPENSATION REFORM SHOULD STRIVE TO ACCOMPLISH NATIONAL BROADBAND PLAN GOALS WITH POLICIES THAT SHIFT THE FOCUS FROM CIRCUIT-SWITCHED NETWORKS TO BROADBAND INFRASTRUCTURE.

The Commission is well aware of the myriad flaws in the current intercarrier compensation system.[2] Of utmost importance to XO is the fact that the current system does little to encourage carriers to invest in Internet protocol ("IP") interconnection facilities, which "has the compounding effect of forcing interconnecting carriers to also retain legacy [time-division multiplexing ("TDM")] network architecture to accommodate the exchange of traffic."[3] The Commission aptly stated in the *NPRM* that "[t]he wildly varying and disparate rates within the intercarrier compensation system

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2 *Id.*, ¶ 495.

3 *Id.*, ¶ 506.

create arbitrage opportunities and introduce layers of regulatory complexity and associated costs, which hinder deployment of IP networks."[4] Although the Commission has been contemplating intercarrier compensation reform for over a decade, the rate of technological change has outpaced the Commission's consideration of the issue. XO believes that the Commission even now is too focused in the *NPRM* on reforming and maintaining policies for interconnection of circuit-switched-based TDM networks. Instead, the time is ripe for the Commission to reform the intercarrier compensation system with forward-looking policies that focus on IP, rather than TDM, networks in order to create proper incentives to spur additional broadband deployment.

During the development of the National Broadband Plan ("NBP"), the Commission recognized that broadband is no longer simply another optional or supplemental service, but rather is becoming the backbone over which many consumers access their voice, data, and video services in an integrated manner.[5] With this in mind, the NBP recommended consideration of "actions [the Commission] could take to encourage transitions to IP-to-IP interconnection where that is the most efficient approach."[6] The Commission clearly understands the strong connection between the intercarrier compensation ("ICC") system and the development of IP networks:

> Because providers' [ICC] rates are above cost, the current system creates disincentives to migrate to all IP-based networks. For example, to retain ICC revenues, carriers may require an interconnecting carrier to convert Voice over Internet Protocol (VoIP) calls to time-division

[4] *Id.*, ¶ 496.

[5] Comment Sought on Transition from Circuit-Switched Network to All-IP Network, NBP Public Notice # 25, GN Docket Nos. 09-47, 09-51, and 09-137, DA 09-2517 (rel. Dec. 1, 2009) ("NBP PN # 25").

[6] *Connecting America: The National Broadband Plan,* Recommendation 4.10 (Mar. 16, 2010) ("National Broadband Plan").

> multiplexing in order to collect intercarrier compensation revenue. While this may be in the short-term interest of a carrier seeking to retain ICC revenues, it actually hinders the transformation of America's networks to broadband.[7]

XO urges the Commission to connect these dots by developing strong IP interconnection policies in conjunction with the reform of intercarrier compensation. In particular, XO submits a proposal for IP interconnection – the exchange of traffic between carriers in an IP format – and intercarrier compensation reform that would create incentives to migrate to all-IP networks while still permitting an appropriate transition from legacy TDM traffic exchange.

A. Intercarrier Compensation and Interconnection Policies Based on TDM Networks Are Outdated and Inefficient And Therefore Must Be Reformed.

The Commission believes that its proposals to reform and reduce TDM rates "will: (1) modernize [its] rules to make affordable broadband available to all Americans and reduce waste and inefficiency by taking steps to curb arbitrage; (2) promote fiscal responsibility; (3) require accountability; [and] (4) transition to market-driven and incentive-based policies."[8] While XO supports the general objectives of the Commission's proposals to unify and reduce TDM intercarrier compensation rates, XO does not believe that the Commission's proposals would truly modernize its rules, reduce waste and inefficiency, and establish market-driven and incentive-based policies for IP deployment. Although the Commission's proposals will reduce waste by curbing arbitrage opportunities, they do not create the necessary framework for overcoming the inefficiencies in TDM networks themselves by promoting all-IP networks in their place.

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7 National Broadband Plan, Chapter 8.

8 *NPRM*, ¶ 490.

Without clear strong policies regarding IP interconnection, XO submits that slowly reducing TDM rates to reciprocal compensation levels, or even to zero, over a ten year period will do little to further spur carriers to deploy IP interconnection facilities.

The current intercarrier compensation rate structures and interconnection policies require burdensome, costly and unnecessary overhead in engineering design, network planning, mediation and billing.[9] Under the current interconnected network design (and unless competitive carriers are directly interconnected), competitive carriers must maintain multiple interconnected circuits with either the incumbent LEC end office switch or tandem switch for the jurisdictional segregation of traffic. This patchwork of interconnected circuits was developed primarily to support the ability of terminating carriers to assess varying rates based almost solely on the originating technology (wireline or wireless) and location (creating local versus intrastate or interstate toll calls) of the calling party. There is no operational benefit to such segregation of traffic, and the maintenance of duplicative circuits merely to support intercarrier compensation arrangements is wasteful and inefficient.

Furthermore, maintenance of TDM interconnection facilities frustrates the rapid deployment of IP services to end users. Absent an alternative agreement, competitive carriers are currently required to convert IP-originated traffic to TDM format in order to deliver it to the ILEC or other terminating carrier. This costly conversion continues to chill the deployment of IP-enabled services to the fullest extent. Deployment of IP-based services to business customers may continue to grow where a carrier can realize the cost benefits of IP transport and termination for traffic that remains on its own IP network or

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[9] *Id.*, ¶ 502.

can be terminated on another IP network without conversion. However, the full potential for IP-enabled services, particularly to residential users, will not be realized until providers serving those customers can reduce termination costs by interconnecting on an IP basis rather than being forced to convert each and every call placed by that customer to a TDM format before delivering it for termination to the PSTN.

Critically, the Commission should develop policies for IP interconnection that apply regardless of the technology used by each carrier to serve its end users. In other words, carriers should exchange traffic in an IP format, whether it was originated or will terminate in IP or in a TDM format. The Commission recognized that "the transition to IP can result in cost savings, including reductions in circuit costs, switch costs, space needs, and utility costs, as well as the elimination of other signaling overhead."[10] Moreover, IP-based points of interconnection ("POIs") can serve a larger geographic area than current TDM POIs, thereby reducing the costs of interconnection. Thus, IP networks provide more efficient and lower cost transport and exchange of all types of traffic, but especially for IP-originated services because the costs of converting traffic to TDM format are avoided. Furthermore, a reduced IP termination rate structure should immediately apply in order to provide incentives for carriers to exchange traffic in IP format and therefore deploy IP technology further into their networks.

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[10] *Id.*, ¶ 506.

B. The Commission Should Declare All Intercarrier Compensation Rates To Be Regulated Under Section 251(b)(5) With States Exercising Their Roles Pursuant To Section 252.

While the Commission has proposed two approaches to coordination with the states to reform intercarrier compensation,[11] XO believes there is only one methodology that would appropriately address intercarrier compensation on a going-forward basis: regulating all traffic under the reciprocal compensation framework of section 251(b)(5). XO agrees that section 251(g) created a carve-out to maintain the then-existing access charge regime until such time as the Commission adopts rules to supersede all access charge obligations preserved by section 251(g), including intrastate access requirements.[12] XO supports the Commission superseding those obligations by applying section 251(b)(5) to all telecommunications traffic (intrastate, interstate, reciprocal compensation, and wireless).[13]

The Commission posits that maintaining the current regulatory categories of intercarrier compensation and asserting its clear jurisdiction over interstate services while relying on the states to initiate reform of intrastate access charges might lead to fewer disputes and litigation. However, XO urges the Commission to recognize that there is a high likelihood of litigation regardless of the methodology it chooses to implement

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11 *Id.*, ¶ 491.

12 47 U.S.C. § 251(g). *NPRM*, ¶ 514.

13 *NPRM*, ¶ 512-13. The Commission has already determined that LEC-CMRS mutual compensation arrangements under the Commission's rule 20.11 fall within the scope of section 251(b)(5). As XO discussed in its comments filed regarding Section XV of the *NPRM*, the Commission should modify section 20.11(e) to require CMRS providers to negotiate with CLECs as well as ILECs, in order to provide consistent treatment for intercarrier compensation purposes. ILECs should not be granted the right to collect interim compensation or demand negotiation while CLECs are left with no recourse with a CMRS provider short of litigation.

intercarrier compensation reform, and not to be swayed by some parties' reservations regarding its legal authority to adopt reform policies that impact traditionally intrastate services. The future of telecommunications will be provided over IP networks, which by their nature do not distinguish between interstate and intrastate services. Consumers no longer bother with distinctions between interstate and intrastate services because they purchase all-distance plans with a single provider. In fact, consumers today think about telecommunications globally because they are able to readily communicate with friends and family all over the world, and the antiquated intercarrier compensation regime should not continue to view telecommunications in ways of the past.

The Commission should focus on the outcome that best meets its national goals because this will provide the greatest stability and certainty regarding the reform.[14] XO does not believe that utilizing the current regulatory categories is the most efficient means of overhauling the intercarrier compensation regime. The dramatic reform that is necessary is unlikely to occur if reliant on the completion of individual state proceedings that may or may not conform to the Commission's goals. Even with the best of intentions, there is no guarantee that each state will reach the same conclusions regarding access reform and transitions, such that a patchwork of intercarrier compensation rates could remain indefinitely, creating additional unintended arbitrage opportunities.[15] While it is possible that the Commission could establish a backstop to impose its federal regime where states either choose not, or are unable, to enact intrastate access reform,[16] XO urges the Commission not to venture down any path that would further delay

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14 *Id.* ,¶ 537.

15 *Id*.

16 *Id.*, ¶ 548.

comprehensive reform of the current system. Consumers and the industry cannot and should not withstand additional delay in decreasing costs, especially if the Commission intends to ensure more widespread broadband deployment.

Moreover, there is no reason to distinguish between types of termination services based on the origination point of the call.[17] Maintaining different regulatory treatment for these services perpetuates carrier expectations that higher rates should continue and higher revenue is justified. For this reason the Commission should terminate the access regime carve out created by section 251(g) and declare that all origination and termination services shall be regulated under section 251(b)(5) and Commission-adopted rules to implement that section.[18] The Commission should approach this proceeding with a forward-thinking mentality that focuses on networks of the future rather than maintaining networks, subsidies, and regulatory regimes developed decades ago. Providers are fast developing new services, and the intercarrier compensation regime should encourage that movement, rather than hinder it.

Thus, XO supports the Commission's adoption of a pricing methodology under sections 251 and 252 and establishment of a glide path to reducing intercarrier compensation rates for *all traffic*, including traffic currently subject to intrastate access charge regimes. Furthermore, XO agrees that section 201(b) provides the Commission

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[17] The rationale for maintaining separate rate structures for these services has been the continuance of subsidies included in access rates that Congress did not intend to be imposed on the exchange of local traffic in the advent of local competition. The Commission's charge in the Act has been to establish an effective universal service program so that all subsidies in access rates can be eliminated, thereby reducing those rates to cost.

[18] XO concurs with the Commission's interpretation that section 251(b)(5) permits regulation of originating access charges as well as termination services since the functionality of these services is essentially the same. *NPRM*, ¶ 517.

with authority to regulate telecommunications traffic that today is subject to intrastate access rates in order to accomplish its federal policies.[19] Because the existence of disparate (higher) intrastate rates creates opportunities for arbitrage and deters investment from broadband networks in favor of maintaining TDM switches and collecting switched access revenues, XO believes the Commission has clear legal authority and policy justifications for adopting principles and rules to address the transition from intrastate access charges to Section 251(b)(5) compensation for such traffic. XO does not believe the Commission should defer to the states to determine the transition from intrastate access rates in each state.[20]

C. The Commission Should Confirm That Section 251 Requires All Carriers To Provide IP-based Interconnection, Regardless of The Technology Used By The Terminating Carrier To Serve End Users.

Although some ILECs may contest the legal and policy justifications for Commission-mandated and regulated IP interconnection, the Commission clearly has authority to confirm that Section 251 interconnection rights and obligations exist for IP interconnection as well as TDM interconnection.[21] In adopting its resolution regarding IP

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19 47 U.S.C. § 201(b). *NPRM*, ¶ 515.

20 However, the Commission may decide that state commissions retain flexibility to address petitions from smaller carriers under section 251(f)(2). 47 U.S.C. § 251(f)(2). Nonetheless, the Commission should adopt guidelines for a state commission to follow when deciding whether to permit suspension or modification of the Commission's policies under section 251(f)(2), so that there is no confusion or inconsistency among the states, as well as with carriers, regarding the special circumstances that may justify a limited modification or suspension of the Commission's rules. *NPRM* , ¶ 550-52. Under no circumstances should the Commission permit a state to permanently or indefinitely suspend the Commission's intercarrier compensation or IP interconnection policies.

21 *See Deployment of Wireline Services Offering Advanced Telecommunications Capability*, FCC 99-413, CC Docket No. 98-147, Order on Remand (finding that obligations of sections 251(b) and (c) apply to the exchange of advanced serviced traffic); *see also Deployment of Wireline Services Offering Advanced*

interconnection in 2008, the National Association of Regulatory Utility Commissioners ("NARUC") sought to preserve "telecommunications carriers' interconnection rights and traffic exchange obligations, under Sections 251 and 252, in a technologically neutral manner."[22] Section 251(a)(1) of the Communications Act of 1934 (the "Act") requires all telecommunications carriers to interconnect with the facilities and equipment of other telecommunications carriers.[23] As NARUC recognized, "[t]he Act, in its imposition of interconnection requirements is technologically neutral and does not distinguish between circuit switched facilities and other network facilities that may be used to exchange voice telecommunications traffic."[24] The importance of interconnection was highlighted in the NBP: "For competition to thrive, the principle of interconnection—in which customers of one service provider can communicate with customers of another—needs to be maintained."[25] Thus, these telecommunications carriers must be required under section 251(a)(1) to interconnect their IP networks with the IP networks of other telecommunications carriers to exchange telecommunications traffic.

Telecommunications Capability, CC Docket No. 98-147, Memorandum Opinion and Order and Notice of Proposed Rulemaking, 13 FCC Rcd 24011, 24035-36 (1998) (finding that incumbent LECs are subject to the obligations imposed by section 251 in connection with the offering of advanced services that employ packet-switching or other specific technologies such as digital subscriber line (xDSL) technologies).

[22] *Resolution Regarding the Interconnection of New Voice Telecommunications Services Networks*, Sponsored by the Committee on Telecommunications and Adopted by the NARUC Board of Directors July 23, 2008 ("NARUC IP Interconnection Resolution").

[23] 47 U.S.C. § 251(a)(1).

[24] *See* NARUC IP Interconnection Resolution.

[25] National Broadband Plan, Recommendation 4.10.

Moreover, section 251(c)(2) further obligates ILECs to provide interconnection to any requesting telecommunications carrier at any technically feasible point within the LEC's network under just, reasonable, and nondiscriminatory rates and terms.[26] These interconnection obligations are neither specific to any particular technology nor targeted to apply only to legacy TDM networks that existed at the time the Telecommunications Act was passed. Therefore IP interconnection clearly must be provided by all carriers for the exchange of telecommunications traffic, regardless of the network on which it originated or technology used to serve the parties at either end of the call.

II. THE INTERCARRIER COMPENSATION RATE STRUCTURE MUST BE REFORMED TO PROVIDE PROPER INCENTIVES FOR IP INVESTMENT.

The Commission can and should encourage broadband investment through development of appropriate rate structures and policies regarding TDM and IP networks. By quickly removing subsidies from rates for TDM-based interconnection arrangements, the Commission would remove the appeal for carriers to maintain such networks and interconnection arrangements since they are inherently more expensive to operate than IP networks. Moreover, by adopting an IP rate structure that permits originating (or intermediate) carriers to immediately incur lower termination costs than those for TDM interconnection, the Commission would create market-based incentives for carriers to

[26] The intercarrier compensation regime applies to carrier-to-carrier interconnection and compensation arrangements, not to unbundling requirements for last mile facilities or to end user services. Because many broadband services are offered over unbundled last-mile copper facilities, revised regulation of carrier-level functions of interconnection, transport and termination are distinct from classification of the retail-level services relying on such functions. The wholesale functions of interconnection, transport and termination are telecommunications services that are entitled to interconnection rights whether or not the retail service is an information service.

deploy IP further into their networks.

A. The Commission Should Remove Subsidies and Adopt a Unified Rate Structure For All Traffic Exchanged On A TDM-Basis.

The Commission seeks comment on both the end game and the transition glide path that should apply to traffic exchanged on a TDM basis. Since there is no cost justification for varying rate levels for the termination of TDM traffic, the Commission's ultimate goal should be to establish a unified rate structure that applies to all carriers and all types and jurisdictions of traffic terminated on a TDM basis. XO supports the Commission establishing a pricing methodology under section 251(b)(5) that explicitly supersedes section 251(g) and provides a glide path for reduction of intrastate and interstate access rates to reciprocal compensation levels or lower within five years.[27] XO recognizes that the NBP suggested a ten-year transition as does the Commission in the *NPRM*.[28] However, such reductions were also proposed ten years ago and then again in 2008. Consequently, the industry has had plenty of opportunity to prepare for such reductions and adjust business plans accordingly.

Similarly, state commissions have had fair warning and considerable opportunity to address reductions in intrastate access charges. The Commission need not cater to those states that have not chosen to review and reform rates yet. Instead, the Commission should develop a transition plan applicable to all states, giving the states opportunity to

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[27] XO supports further cost-based reductions in TDM intercarrier compensation rates below reciprocal compensation rates. In particular, TELRIC rules may need to be refreshed and a new round of state commission rate-setting proceedings may be required to recognize the cost efficiency of IP-interconnection. However, as discussed below regarding compensation rates for traffic exchanged on an IP-basis, XO has concerns about unintended arbitrage opportunities where a bill-and-keep regime is adopted without any consideration of traffic imbalances.

[28] *See* National Broadband Plan, Section 8, at 148. *NPRM*, n.804.

review the impacts and address state-specific issues, such as state USF and rate rebalancing, as necessary.

XO supports the Commission's proposal to first reduce intrastate access charges to interstate levels and then to transition those rates to reciprocal compensation levels or lower. During this transition, interstate access rates for rate-of-return carriers should be capped so that they do not continue to increase and thereby distort the transition.[29] XO does not believe the Commission should simultaneously reduce reciprocal compensation and interstate access rates at the outset of the transition because such reductions would perpetuate rate disparities throughout the transition. Instead the Commission should unify all rates at reciprocal compensation levels under its authority to adopt a regulatory framework to implement Section 251(b)(5) and then further reduce the unified rate.[30] Opportunities for arbitrage exist primarily where different rate levels exist; therefore, XO believes that the best policy is to reduce disparity as quickly as possible during the transition.

Individually negotiated arrangements are always preferable in order to address unique interconnection arrangements between parties. Therefore, XO believes that the Commission should adopt a default glide path under Section 251(b)(5) for rate reductions but permit carriers to negotiate alternate arrangements.[31] Importantly, the Commission must adopt default rules that would apply in the absence of an agreement to prevent carriers from refusing to negotiate interconnection or traffic exchange agreements to avoid paying any intercarrier compensation.

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[29] *NPRM*, ¶ 557.

[30] *Id.*, ¶ 553.

[31] *Id.*, ¶ 554.

As discussed more fully below, XO firmly believes that the best way to achieve the NBP's goals to encourage, rather than deter, investment in IP networks is to eliminate TDM interconnection and termination rates after a reasonable transition to IP interconnection, which XO believes can also be achieved within five years. While section 252(d)(2)(A) requires that transport and termination rates provide for the mutual and reciprocal recovery of network costs, the Commission may (and should) immediately establish an IP termination rate structure different from the TDM termination rates. In particular, the commission may establish certain rate structures in order to encourage or discourage certain market behavior.[32] Given its strong preference for encouraging broadband deployment, the Commission should adopt rate structures that best drive that result. By immediately both establishing a lower rate for IP termination as well as confirming that terminating carriers must interconnect and accept traffic on an IP basis, the Commission will establish clear incentives for carriers to move to IP networks at the outset.

B. The Commission Should Not Burden IP-to-IP Interconnection Arrangements With Legacy TDM Rate Structure But Instead Should Establish a Rate Structure Applicable To All Telecommunications Traffic Exchanged On An IP Basis.

The NBP recognized that the "current [intercarrier compensation] system is not sustainable in an all-broadband Internet Protocol (IP) world where payments for the exchange of IP traffic are not based on per-minute charges, but instead are typically

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[32] For example, the Commission determined that while ISP-bound traffic falls under the reciprocal compensation regime in section 251(b)(5), it would establish a different rate in order to discourage arbitrage opportunities. Order on Remand and Report and Order and Further Notice of Proposed Rulemaking, 24 FCC Rcd 6475 ,6495, ¶ 28 (2008) ("*2008 ISP Remand Order*"); *see also* Order on Remand and Report and Order, 16 FCC Rcd 9151, 9171–72, ¶ 44 (2001) ("*ISP Remand Order*").

based on charges for the amount of bandwidth consumed per month."[33] It further underscored the importance of crafting an intercarrier compensation framework that creates the proper incentives for carriers to invest in new broadband technologies.[34] Indeed, two years ago the Commission found that "[b]ecause carriers…can receive significant revenues from charging above-cost rates to terminate telecommunications traffic, they have a reduced incentive to upgrade their networks to the most efficient technology or negotiate interconnection agreements that are designed to accommodate the efficient exchange of IP traffic…."[35] Similarly, the Commission has concluded in this proceeding that the current system is actually hindering progress toward all-IP networks, and "creates the perverse incentive to maintain and invest in legacy, circuit-switched-based, time-division multiplexing (TDM) networks to collect intercarrier compensation revenue…."[36]

Clearly, saddling IP-to-IP interconnection arrangements with the same legacy intercarrier compensation that might apply when legacy TDM-based interconnection is used would be just such a significant impediment to progress. Thus, the Commission should immediately adopt lower rates for IP-to-IP exchange of traffic, rather than prioritizing parity of rates among different types of traffic exchange and interconnection. XO proposes that roughly-balanced traffic volumes exchanged between carriers on via IP-to-IP interconnection should be terminated on a bill-and-keep basis. For out of balance traffic volumes, XO recommends that the Commission adopt a tiered flat rate

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33 National Broadband Plan at 142.

34 *Id.*

35 *2008 ISP Remand Order*, ¶ 189.

36 *NPRM*, ¶ 506.

structure that closely approximates the additional costs incurred in terminating out of balance traffic. The differentiation between TDM termination rates and IP termination rates that XO advocates would *not* introduce yet another uneconomic arbitrage opportunity; on the contrary, such a differentiation is intended to make sure that rates properly reflect how costs are incurred. As the Commission has correctly recognized, policy can "play a role in providing a glide path for all industry players [in other communications transitions], enabling more efficient planning and adjustment over the course of the transition."[37] Thus, the Commission should adopt policies here to encourage the widespread transition to more efficient IP interconnection arrangements.

4. <u>Where Carriers Interconnect on an IP-to-IP Basis And Traffic Volumes Are Roughly In Balance, Each Party Should Terminate Traffic Using a Bill-and-Keep Methodology.</u>

When carriers interconnect on an IP-to-IP basis, they exchange voice and all other types of traffic simply by transferring packets back and forth. Unlike the TDM-based interconnection, there is no need to occupy an entire circuit in a circuit-switched network for the duration of the call. When completing voice traffic over an IP network, per minute charges for service do not reflect the manner in which termination costs are incurred.[38] Indeed, by creating a mismatch between the way costs are incurred and how customers are charged, per minute charges create a distortion by denying users of the economic efficiencies introduced by soft-switches and IP transport.

[37] NBP PN # 25.

[38] As explained below, XO does propose to use minutes of use in calculating a tiered system of flat-rated termination charges that would apply to out-of-balance traffic volumes because XO believes this provides an appropriate proxy for bandwidth costs incurred in terminating traffic on an IP network.

Fortunately, there are market-based arrangements showing how carriers that interconnect on an all IP-basis compensate one another for completing each other's traffic in the absence of the distortions caused by legacy regulatory frameworks. With respect to the public Internet, so-called "Tier 1 Peers" generally exchange packets on a "bill-and-keep" basis where traffic volumes exchanged between the carriers are roughly in balance. Payment is "in kind" in the sense that each party agrees to terminate the traffic of the other party by providing service without charge. When Internet "peering" is requested by a provider that is not expected to deliver a volume of traffic which is roughly "in balance" with the traffic coming in the other direction, rates are negotiated as required to reasonably compensate the provider that is required to terminate a disproportionate volume of Internet traffic. While not entirely problem-free, to be sure, this system has worked reasonably well for a decade, and clearly has allowed for the explosive growth of public Internet capacity and connectivity.

XO recommends that the Commission largely replicate the successful public Internet model with respect to voice telecommunications traffic exchanged on an IP basis. Therefore, the Commission should adopt rules establishing that, unless parties agree otherwise, the traffic exchanged through IP interconnection arrangements shall be terminated on a bill-and-keep basis when the traffic volumes are reasonably balanced – using MOUs as a proxy exchanged in each direction – in both directions.

Authority to adopt a default bill-and-keep regime lies in section 252(d)(2)(B)(i) of the Act which expressly authorizes regulatory "arrangements that afford the mutual recovery of costs through the offsetting of reciprocal obligations, including arrangements that waive mutual recovery (such as bill-and-keep arrangements)."[39] Furthermore, section 201(b) grants the Commission authority to "prescribe rules and regulations as may be necessary in the public interest to carry out the provisions of [the] Act."[40] Thus, while the Commission has yet to do so, nothing prevents it from *requiring* bill-and-keep arrangements in particular circumstances, given its general authority to adopt rules that implement sections 251(b) and 251(c). Indeed, the Supreme Court has already recognized the Commission's authority to mandate the pricing standard applicable to "mutual and reciprocal recovery by each carrier of costs" under section 252(d)(2), in considering the Commission's imposition of the total long run incremental cost standard on such cost recovery.[41] That statutory language empowers the Commission to impose a bill-and-keep regime as an intercarrier compensation mechanism, *provided* that the Commission can be reasonably confident that it allows for a "mutual recovery of costs."[42] XO submits that limiting the mandatory use of bill-and-keep to situations where traffic volumes exchanged are *reasonably balanced,* meets this criteria since it is reasonable to presume that each party will incur approximately the same cost in terminating traffic for the other party, and thus mutual recovery of costs is assured.

5. Traffic Balance Should Be Calculated Based On All Voice Telecommunications Traffic Exchanged Between Two Directly Interconnected Carriers.

IP interconnection is a one-to-one relationship between two carriers that are directly interconnected. Therefore, XO proposes that the balance of traffic should be

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39 47 U.S.C. § 252(d)(2)(B)(i).

40 47 U.S.C. § 201(b).

41 47 C.F.R. § 51.705(a)(1).

42 *See, id.*

calculated based on the total volumes of voice telecommunications traffic directly exchanged between those two carriers, regardless of the carrier or network where the traffic originated. In other words, whether one carrier provided wholesale or transit services for a third party would be irrelevant to the arrangement, and all traffic exchanged would be calculated into the balance regardless. Some of the current intercarrier compensation rules create opportunities for wholesale or transit providers to game the system by receiving payment from third parties for transiting traffic but then refusing to pay either access charges or reciprocal compensation to the terminating carrier because they claim not to be responsible for those payments. By simplifying the compensation arrangement to apply between two directly interconnected carriers, the problems associated with the "middle-man" and phantom traffic would be eliminated. Each carrier has direct visibility into the traffic volumes it is both delivering and receiving from the other carrier. Consequently, there is little opportunity for dispute.

Importantly, XO suggests that (unless the parties agree otherwise) bill-and-keep arrangements be used in connection with the termination of *all* PSTN traffic exchanged via IP interconnection, even if one of the parties elects to ultimately convert the traffic to TDM and terminate it using circuit switching. The purpose is to allow the parties to realize the economic benefits of deploying an all-IP network, and even provide an incentive for carriers to move as quickly as possible to migrate to IP-based interconnection. Once parties have interconnected on an IP-basis, it is clear that they have the ability to deploy and use efficient soft-switching if they choose to do so. TELRIC principles allow carriers to recover only the reasonable additional cost of forward-looking technology, and there can be no denying that soft-switches are the forward-looking technology used in IP networks, not legacy circuit switches. XO does not suggest that carriers should be barred from converting traffic to TDM and using legacy circuit switches for termination. However, they should not be permitted to charge legacy TDM rates calculated on the basis of antiquated technology when they elect to do so. This formulation allows carriers to retire legacy circuit switches according to their own business needs, but eliminates any incentive to retain circuit switching simply to charge unduly high intercarrier compensation rates. Thus, parties that invest in an all-IP network can reap the attendant economic and technical benefits, and providers that have hybrid IP-TDM networks will have an incentive to migrate to all-IP networks as swiftly as possible.

Therefore, XO proposes that an appropriate definition of "in-balance" would be no more than a 20 percent difference in the telecommunications traffic terminated by each carrier in any given calendar quarter.[43] Thus, the exchange of traffic would be considered in-balance if neither of the two carriers terminated more than 60% of the total volume of traffic exchanged between the carriers during that quarter, which is a common ratio in reciprocal compensation arrangements.

6. <u>Out-of-Balance Traffic Exchanged On An IP Basis Should Be Subject To A Tiered Cost-Based Rate Structure To Ensure Recovery of Costs And Reduce Arbitrage Opportunities.</u>

Although it might be tempting for the Commission to simplify matters by requiring that *all* traffic exchanged on an IP-to-IP basis be terminated on a bill-and-keep basis, regardless of traffic balances, such an approach would not be either economically

[43] XO anticipates that carriers may negotiate to include the exchange of voice and data traffic under one agreement, but the Commission need not address those arrangements except to ensure that nothing prohibits carriers from combining voice and data traffic under the same agreement.

rational or legally sustainable. XO shares the Commission's desire to eliminate uneconomic per-minute termination charges. However, the Commission's rules must appreciate that termination costs do exist even in an IP network. XO believes that eliminating all termination charges may lead to other unintended and unforeseen arbitrage opportunities where one carrier overuses another carrier's terminating network without consequence.

While the Commission may have determined that both the called and calling party benefit from participating in a call and should therefore share the costs,[44] as a policy matter, the Commission should avoid adopting rules that might be exploited by one carrier to the disadvantage of another. Because the calling party is still in control of initiating the call and there is a high likelihood of call completion once it has been initiated because most consumers using some form of automated answering service. With the Commission's rules prohibiting carriers from blocking traffic, there is no valid way for a terminating carrier to reject incoming calls in order to reduce its termination costs. With no regulatory backstop to permit the terminating carrier to assess terminating charges on the originating (or intermediate) carrier if balances are dramatically out of balance, the terminating carrier may have no recourse to recover its reasonable costs of providing a service to the originating (or intermediate) carrier.

Therefore, XO submits that a low, cost-based tiered rate structure would be administratively simple, eliminate complicated billing, and remove any incentives for arbitrage business plans. Traffic volumes are already measured in the normal course of business, even in IP networks, so quarterly traffic balances would be simple to calculate

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44 *NPRM* , ¶ 525.

and verify. If one carrier terminated more than 60% of the total quarterly volume, using minutes of use as a proxy, that carrier would be permitted to assess a flat termination charge to the other carrier. The Commission has already determined that $.0007 is an appropriate per-minute termination rate for ISP-bound traffic.[45] Although the costs of operating an IP network are incurred on a packet or bandwidth basis, rather than a per-minute basis, XO believes this per-minute rate can be used as a proxy for the costs of additional bandwidth necessary to transport and terminate out-of-balance traffic. Therefore, XO proposes that an out-of-balance carrier would be assessed $700 for each up to one million minutes of use ("MOU") out of balance: $700 = Up to 1 million MOU out of balance, $1400 = Over 1 million and up to 2 million MOU out of balance, $2100 = Over 2 million and up to 3 million MOU out of balance, etc.

Assessment on a flat rate more properly reflects the way in which additional costs of bandwidth capacity are incurred by the terminating carrier and would discourage uneconomic overuse of the terminating carrier's network. Moreover, low cost-based flat charges based on a tiered structure would not create arbitrage opportunities for terminating carriers to inflate their terminating traffic volumes. Therefore, XO proposes that the Commission adopt a default tiered flat rate structure for termination of out-of balance traffic exchanged on an IP-basis.

III. THE COMMISSION SHOULD IMMEDIATELY ADOPT POLICIES TO ENSURE WIDESPREAD TRANSITION TO IP INTERCONNECTION AND EXCHANGE OF VOICE TELECOMMUNICATIONS TRAFFIC.

XO is already embarked on an aggressive program to migrate to an all-IP network, and establishing IP-to-IP interconnection arrangements with other carriers is a

45 *2008 ISP Remand Order*, ¶ 29; *ISP Remand Order*, ¶ 78.

critical component of XO's plan. XO has already invested substantial sums in implementing IP interconnection arrangements with a number of other major carriers, but to realize the true cost benefits of an all-IP network, IP interconnection must be widespread throughout the industry. When carriers such as XO invest as required to offer the efficiencies of an all-IP network to the public, both such carriers and their customers should be able to realize the benefits by availing themselves of an intercarrier compensation system that properly reflects the economics of IP-based interconnection.

The Commission recognizes that "the long-term approach to intercarrier compensation reform also must be consistent with the exchange of traffic on an IP-to-IP basis."[46] Therefore, XO urges the Commission to adopt strong interconnection policies in this proceeding that will ensure widespread IP-to-IP interconnection in the industry. Moreover, the Commission is aware that the transition to all-IP networks for every carrier will be stalled unless and until all carriers are pressed to adopt IP interconnection as the standard means of exchanging traffic or to incur their own costs of converting traffic between IP and TDM formats.[47] In a nutshell, the interconnected nature of telecommunications networks creates an all-or-nothing proposition for carriers, and there is inherent tension between a carrier's desire to deploy evolving IP-enabled services that consumers demand and its efforts to manage and reduce operating costs, particularly for transporting and terminating traffic. For a carrier like XO that has deployed a nationwide IP network, the full benefits of IP technology cannot be realized while XO must continue to maintain TDM interconnection and access circuits at each of the ILEC tandems and/or end offices throughout the country, rather than in a handful of locations as is common

[46] *NPRM*, ¶ 527.

[47] *NPRM*, ¶ 506 (citations omitted).

under IP peering arrangements.

While developing the NBP, the Commission considered the "appropriate policy framework to facilitate and respond to the market-led transition in technology and services, from the circuit switched PSTN system to an IP-based communications world."[48] The Commission there sought comment on "the scope and breadth of the policy issues associated with this transition" to all-IP networks. In particular, the Commission sought "to understand which policies and regulatory structures may facilitate, and which may hinder, the efficient migration to an all IP world."[49] The Commission should understand that the most relevant consideration in determining the appropriate timing of the transition to all-IP interconnection is the amount of overall IP capacity now operating, not how many end users subscribe to IP-based voice services. "It is estimated that 90% of the interLATA PSTN has been replaced by IP technology, and 60% of the intraLATA PSTN as well."[50] Moreover, any carrier (including small/rural LECs) that offers ISP service already connects (either directly or indirectly) in an IP format to exchange Internet traffic. There has been widespread industry support for the Commission to adopt policies regarding IP interconnection,[51] and the Commission should not delay any further adoption of such policies.

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48 NBP PN # 25.

49 *Id.* at 1.

50 CompTel et al. Comments on NBP PN # 25, GN Docket No. 09-51, Attachment A at 1 (filed Dec. 21, 2009) (citing Presentation of Carl Ford, Vice President, Crossfire Media, to National Association of Regulatory Utility Commissioners, Staff Telecommunications Subcommittee, February 14, 2009).

51 *See e.g.,* AT&T Comments on NBP PN # 25, GN Docket No. 09-51 (filed Dec. 21, 2009); CompTel et al. Comments on NBP PN # 25 , GN Docket No. 09-51 (filed Dec. 21, 2009); Sprint Comments on NBP PN # 25 , GN Docket No. 09-51 (filed Dec. 21, 2009).

Last year, XO presented a proposal for intercarrier compensation reform that focused on developing strong policies for IP Interconnection. In that proposal, XO recommended that the Commission require every telecommunications carrier to provide IP-based carrier-to-carrier interconnection (directly or indirectly) within 5 years, regardless of the technology the carrier uses to provide services to its end users. Such carrier-to-carrier IP interconnection can and is occurring now, where IP-transport facilities exist, even if end users are directly served by circuit-switched TDM technology.

At the outset the Commission must confirm that every carrier has the obligation to interconnect on an IP basis (either directly or indirectly) with the networks of other carriers and pay the costs of transporting traffic to the IP POI. Any carrier may negotiate a market-based arrangement with a third party to fulfill its interconnection obligation, either through IP transit to the IP POI or to convert traffic to TDM format for purposes of traffic exchange as necessary. XO recommends that the Commission expressly eliminate LATA and other jurisdictional traffic boundaries for traffic exchanged on an IP basis. As discussed above, there is no cost justification for designating and segregating traffic based on arbitrary jurisdictional boundaries. Furthermore, the Commission should establish a policy of no more than one default IP POI in each state, but should encourage the development of regional POIs for more efficient interconnection. While individually negotiated IP interconnection and traffic exchange arrangements should be encouraged, federal rules are necessary in the event negotiations stall. Therefore, the provisions of section 251 and 252 would apply absent a voluntarily negotiated agreement.

Once IP interconnection arrangements are in place,[52] no terminating carrier should be permitted to require conversion to a particular format for exchanging traffic, regardless of the technology used to serve any particular end users. Thus, during the transition period, each originating (or intermediate) carrier would have the option to determine whether to deliver traffic via a TDM POI or IP POI and would pay according to the corresponding intercarrier compensation regime. If a carrier chose to continue delivering traffic to the TDM POI, it would continue to pay higher intercarrier compensation rates. However, because the IP termination rate would be immediately set to lower rates as discussed above, the originating (or intermediate) carrier would have the incentive to deliver traffic in an IP format, and therefore to deploy IP networks to end users in order to avoid the costs of converting from TDM to IP on the originating side of the call. Additionally, because the costs of any IP-TDM conversion necessary would be borne by the terminating carrier, these terminating carriers will have increased incentive to retire TDM switching facilities and deploy IP networks facilities all the way to end users as the traffic volumes delivered via IP interconnection arrangements increase.

After a transition period, which XO recommends should be accomplished within

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[52] The Commission may establish a reasonable ramp-up period, which should be no longer than 12 to 18 months, to permit carriers the opportunity to negotiate and implement IP interconnection arrangements. Certain industry standards should be developed to smooth the transition to a uniform all-IP interconnection regime, such as development of ENUM databases to facilitate efficient IP routing, technical standards for ensuring voice quality, and regional standard IP POI locations. However, this should not delay the first stage of implementation since carriers are already implementing IP interconnection arrangements for the exchange of voice traffic. *See also* Letter from Kathleen O'Brien Ham, Vice President, Federal Regulatory Affairs, T-Mobile USA, Inc. and Charles W. McKee, Vice President, Government Affairs, Federal and State Regulatory, Sprint Nextel Corp., to Marlene H. Dortch, Secretary, FCC, CC Docket No. 01-92, at 4 (filed Jan. 21, 2011).

five years, all carriers should be required to exchange traffic in an IP format. During the transition, terminating carriers have an obligation to accept traffic in either IP or TDM format, but after a transition, terminating carriers should be permitted to refuse to accept traffic via TDM interconnection arrangements where IP interconnection is available. In this way, an originating (or intermediate) carrier would then be required to bear the costs of conversion from TDM to IP if that carrier has not migrated to an IP network. By setting a date certain when carriers may realize the full benefit of terminating traffic on their IP networks without incurring costs of conversion, the Commission would strongly encourage carriers to quickly deploy IP networks.

XO urges the Commission to adopt the foregoing proposal to require carriers to offer and use IP interconnection for the exchange of all traffic within five years. While it may take many years before all circuit-switched technology is removed from the telecommunications networks, there is no reason to delay beginning the migration to all-IP networks, particularly where carriers have already deployed IP transport facilities. If the Commission decides not to adopt this proposal as a whole at this time, XO urges the Commission to begin the transition to IP networks at least by confirming that section 251 requires telecommunications carriers that have deployed an IP network and facilities to interconnect on an IP basis and accept traffic delivered in an IP format.

IV. THE COMMISSION SHOULD NOT UNDERTAKE REFORM OF THE USF DISTRIBUTION SYSTEM PRIOR TO COMPLETING REFORM OF THE USF CONTRIBUTION FRAMEWORK.

Over the past decade, the Universal Service Fund ("USF") program has grown exponentially and uncontrollably with ever-increasing demand for fund support requiring an equal increase in contributions even while the contribution base has been shrinking. Annual USF expenditures have nearly quadrupled since the program was established only a dozen years ago. Total USF outlays this year will amount to nearly $9 billion as compared to only $2.3 billion in 1998.[53] The expanding fund has required increased contributions, and from 2000 to 2011, the USF contribution factor has nearly tripled, rising from a low of 5.3% in 2000 to a high of 15.5% for the first quarter of this year.[54] This increased burden clearly was unintended; no one can seriously contend that Congress in 1996 believed that it was enacting what would become a 15% telecommunications sales tax in 2010. In XO's experience, this "tax" on telecommunications consumers has reached the breaking point. End users are unwilling to pay more in terms of USF-related surcharges.

The exorbitant increase in the contribution factor is the direct result of increased demands on the distribution side of the fund, drawing from a shrinking contribution base. Whether from traditional incumbent LEC ("ILEC") recipients or new competitive Eligible Telecommunications Carrier ("ETC") claimants of USF funding, the appetite for ever more subsidy support has been insatiable. The problem has been exacerbated by policy decisions of the Commission to reclassify many previously assessable telecommunications services into non-assessable information services. Moreover, both carriers and their customers increasingly are substituting information services for telecommunications services, thereby reducing USF assessments. Thus, while demand for scarce USF funding has increased steadily, the USF contribution base has stagnated or

53 *NPRM*, Separate Statement of Commissioner Meredith Atwell Baker.

54 Public Notice, Proposed Third Quarter 2000 Universal Service Contribution Factor, DA 00-1272 (June 9, 2002); Public Notice, Proposed First Quarter 2011 Universal Service Contribution Factor, DA 10-2344 (Dec. 13, 2010).

shrunk.[55] As XO has commented previously, the Commission desperately needs to shore up the USF contribution base, and substantially reduce the USF contribution factor, by expanding the base of telecommunications-related revenue that is subject to USF assessment.[56]

Despite obvious problems on the contribution side of the USF, the instant *NPRM* seeks to reform only the distribution side with no apparent consideration for how such distribution needs will be funded.[57] Any reform of the USF must be comprehensive, addressing *both the contribution and distribution* sides of the fund. Otherwise, only one half of the current whipsaw will be addressed, even should future growth be capped. As Commissioner McDowell aptly noted regarding the instant proceeding:

> I have long advocated for *comprehensive* reform of the entire universal service and intercarrier compensation regimes. It's like fixing a watch; it is impossible to tinker with one component of the mechanism without affecting all of its parts at the same time. Today, the Commission is choosing to take the piecemeal route again by not addressing the contribution mechanism at the same time.[58]

While the Commission considers restructuring the USF to subsidize broadband deployment, the Commission *must at the same time* determine whether and how sufficient funds can be raised – without unfairly burdening any particular categories of

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55 *See, e.g.*, Universal Service Monitoring Report (2010), CC Docket No. 98-202, Table 1.1 ("2010 Monitoring Report").

56 *See, e.g.*, Letter from Brad E. Mutschelknaus, Kelley Drye & Warren, LLP, Counsel to XO Communications, LLC, to Marlene H. Dortch, WC Docket. Nos. 05-337, 06-122 and GN Docket No. 09-51 (Sept. 17, 2010).

57 *NPRM*, ¶¶ 18-32.

58 *NPRM*, Separate Statement of Commissioner Robert M. McDowell (emphasis in the original).

carriers – to support the altered funding requirements.[59] Adding broadband services and facilities to the funding pool will only further burden the USF and the limited pool of contributors. If the Commission does not address reform of the contribution side of the USF, concurrently with reform of the distribution side, the likely result will be an over-commitment to subsidy programs. Simply put, however well intended, the overwhelming temptation will be to promise support for new programs without also making the hard decision to reduce current obligations. A better approach would be to first decide how much money can be raised without placing undue burdens on customers that pay into the USF, and then decide the eligible uses for the available funding.

V. HIGH COST SUPPORT SHOULD BE CAPPED AT CURRENT LEVELS.

A. The Scale of the High Cost Fund Has Far Eclipsed What Was Envisioned By the Framers of the 1996 Act.

As noted above, the cost of USF has exploded uncontrollably. The time for discipline and restraint in USF expenditures has long passed. Not surprisingly, the demand for subsidies by ILECs and competitive CETCs alike is insatiable. It is far more appetizing for eligible entities to receive a subsidy from competitors via the High Cost Program than charge economic rates to their own customers or reduce expenses to operate more efficiently. High cost funds also enable many ILECs to prop up their share prices by paying extraordinarily high dividends.[60] Any serious USF reform effort must start with the imposition of a *"hard cap*" on the size of high cost funding at current

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[59] *See, e.g., NPRM*, ¶ 18. *See, also, e.g.*, National Broadband Plan, Recommendation 8.10.

[60] Although USF funding is not directed at dividend support, the simple fact is that dollars, once received, are fungible and High Cost support provides the free cash flow required for many small and mid-sized LECs to fund extraordinary dividend pay-out ratios – ranging from 7-9% on common stock for Windstream, Frontier and CenturyLink, for example.

levels.[61] Anything less than a strict freeze on the current size of the program will only lead to further abuse as there will be no end to the excuses from both rural LECs ("RLECs") and ETCs that are addicted to subsidy flows in attempts to rationalize more funding. On the contrary, these companies need to be weaned off their USF "habit." Not only should a hard cap be instituted, but, as Commissioner McDowell suggests, the Commission should establish a policy of actually *reducing* the size of the fund over time.[62]

B. Reform of the High Cost Program Should be Implemented Immediately.

The current High Cost Program is poorly conceived and wasteful. XO commends the Commission on its proposals for reform of the program to be implemented beginning in 2012, and urges their adoption. Specifically, *first*, the three components of the High Cost Program that are directed to support of rate-of-return ILECs promote inefficient operation and investment, and therefore must be restructured quickly. By rewarding unnecessary investment, the current reimbursement formula for High Cost Loop Support ("HCLS") encourages gold-plating. The reimbursement rate must be reduced substantially. Further, the lack of any ceiling on the amount of HCLS and Interstate Common Line Support ("ICLS") that any individual ILEC may receive has led to some outlier RLECs pocketing truly shocking amounts of USF subsidy payments,[63] and

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61 Since the telecommunications industry is generally a declining cost business, it would not be necessary to adjust the cap based on an inflation factor.

62 *See NPRM*, Separate Statement of Commissioner Robert M. McDowell.

63 Some small RLECs have claimed as much as $23,000 per line annually in HCLS. Requiring such extraordinary subsidy flow is both unfair to customers that pay into the USF and is a severe disincentive to consolidation and expense reductions that could improve efficiency. *See NPRM*, ¶ 210.

imposing an absolute cap of $250 per line monthly of support is required to end abusive claims. Further, in an era when low cost softswitches are displacing expensive circuit-switches, the Local Switching Support ("LSS") subsidy simply provides an incentive for recipients to maintain inefficient technology. The LSS program should be quickly phased out.

Second, the Interstate Access Support ("IAS") program should be ended immediately. It is highly questionable whether the large price-cap ILECs that primarily benefit from the program ever needed or were deserving of this subsidy flow. However, in any event, it was created in 2000 expressly as an interim program and as part of a five-year transition plan.[64] The transition period has long since expired, and there is scant evidence that IAS is required any longer to ensure the availability of rural voice service on reasonable terms.

Third, the "identical support" rule for ETCs should be eliminated immediately. The identical support rule is incredibly wasteful. ETCs receive support as a per-line, dollar-for-dollar match of ILEC support, regardless of the ETCs' actual costs or needs. Since most ETCs are wireless carriers, their costs of service are not readily comparable to those incurred by wireline ILECs. Moreover, in many areas, USF support is paid to four or more ETCs on an "identical support" basis, thereby requiring consumers to pay not only for overly costly services, but unnecessarily duplicative ones as well. The High-Cost program was created to ensure that rural consumers would have access to a

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[64] *See Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers; Low-Volume Long-Distance Users; Federal-State Joint Board on Universal Service*, 15 FCC Rcd 12962, ¶ 185 (2000) ("Interstate Access Support Order"), *aff'd in part, rev'd in part, and remanded in part*, *Texas Office of Public Util. Counsel et al. v. FCC*, 265 F.3d 313 (5th Cir. 2001).

reasonably-priced voice service, not to fund the entry of multiple mobile wireless competitors in the same market. The Commission should seize this opportunity to reduce the size of the High Cost Fund by $1.1 billion by eradicating the identical support rule effective at the end of this year (and correspondingly reducing the USF assessment factor by a significant amount). The resulting reduction in Universal Service spending should redound immediately to consumers by decreasing their overall USF burden. That burden should not be preserved by shifting these revenues to the new Connect America Fund ("CAF") as proposed in the *Notice*.[65]

VI. HIGH COST FUNDS CAN BE REDIRECTED TO SUPPORT BROADBAND DEPLOYMENT, BUT VOICE-ONLY SUPPORT MUST BE PHASED OUT CONCOMITANTLY.

A. Refocusing High Cost Support to Make Broadband Affordable Is Sensible.

Throughout the *NPRM*, the Commission recognizes that telecommunications networks have been and continue to evolve toward all-IP (Internet Protocol) networks.[66] IP-based networks have distinct advantages over the circuit-based networks they are replacing. As a general matter, IP-networks offer multiple applications over a single platform while still supporting voice offerings, the latter which have been the principal focus of high cost support to date. Carriers deploying newer IP-technologies can capitalize on operational simplicity, reduced costs of service, and flexible provision of diverse services over the same platform, such as unified communications, cloud services, and interactive video applications far beyond voice and data connectivity. In the coming years, there will be more personalized services, personalized applications, and the

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65 *See, e.g.*, *NPRM*, ¶ 18.

66 *See, e.g., NPRM* , ¶¶ 40, 41, 103, 156, 191, 528, 532, 561, and 609.

increased embrace of a Gigabit lifestyle at home and in the office. Where providers cannot offer these services because the networks have not completed the migration to IP, consumers of services in those areas will suffer relative to those that have such services.

The USF has a vital role to play in ensuring that the United States does not evolve into a nation of advanced communications "haves" with large pockets of "have nots." As explained above, the Commission should adopt a "hard cap" on high cost funding under the current programs. Equally important, those funds should be redirected as quickly as possible to subsidize the deployment of broadband over IP-based networks, rather than the entrenchment of circuit-switched voice systems. The demand for advanced IP-services has far outpaced the transformation of the nation's networks to IP-based solutions, especially in rural and other high cost areas.

Today's Universal Service system had its roots in the mid-1990s when circuit-switched services heavily predominated. The existing funding programs were not developed to support broadband, with the exception of special programs, such as funding for advanced technologies for schools and libraries. Nonetheless, Congress, in adopting Section 254 of the Act, directed the Joint Board and the Commission to "preserve and advance universal service" on principles which include making available access to "advanced telecommunications and information services . . . in all regions of the Nation."[67]

Because the evolution toward IP-networks is the clear trend for telecommunications networks as a whole now and for the foreseeable future, those

[67] 47 U.S.C. § 254(b)(2). *See also* 47 U.S.C. § 254(b)(3) ("reasonably comparable to those services provided in urban areas . . . at rates reasonably comparable to the rates charges for similar services in urban areas").

providers that receive Universal Service support should be using these funds to invest toward the future rather than further entrenching the circuit-switched networks of the past in underserved areas. The Commission's rules governing Universal Service must be restructured to redirect funds toward the most efficient, capable, and forward looking technologies in underserved areas. Only in this manner will the objectives of bringing, "on a reasonable and timely basis," "advanced telecommunications capability to all Americans" progress toward reality.[68]

XO strongly supports the establishment of a new Connect America Fund, as proposed in the *NPRM*, to both close the gap of broadband availability in underserved areas and also to provide ongoing support for broadband networks.[69] Without a redirection of high cost funds to broadband networks, through the CAF, consumers in some regions of the country will not have access to both advanced telecommunications and information services that are "reasonably comparable to those services provided in urban areas . . . at rates reasonably comparable to the rates charges for similar services in urban areas."[70]

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68 *See* 47 U.S.C. § 706(a). *See also* 47 U.S.C. § 254(b)(2) ("Access to advanced telecommunications and information services should be provided in all regions of the Nation.")

69 *NPRM* , ¶ 157. The Commission should not pursue methods, as suggested by the National Broadband Plan, to accelerate broadband deployment by using public funding outside the Universal Service contribution-distribution framework to provide funding to the CAF, even in part. See National Broadband Plan, Recommendation 8.15, at 151. Methods such as these – rather than expediting the transition from the High Cost program to the CAF – would only serve to further entrench current High Cost funding recipients and their all-voice, circuit switched networks, as well as create new problems in funding universal service when Congressionally provided public funding for the CAF expires. Rather, the Commission should rely wholly on transitioning High Cost program funds to fuel the CAF program.

70 *See* 47 U.S.C. § 254(b)(3).

XO understands that the Commission may not find it reasonable to impose a flash cut in all areas in order to support only broadband networks rather than circuit-switched networks. The Commission is rightly concerned to "minimize regulatory uncertainty for investment."[71] But the Commission should adopt a prompt transition and quickly move to identify current high cost funds that can be promptly migrated to the CAF because continued USF support for voice-only, circuit-switched networks merely creates, in many cases, an incentive for recipient network providers to delay the migration to all-IP networks, with their attendant benefits.[72] Firm milestones should be set to complete the transition entirely to the CAF with the minimum delay. The Commission noted, presciently, over twenty years ago that "rate of return [regulation] does not provide sufficient incentives for broad innovations in the way firms do business."[73] In much the same way, today's high cost funding under the current Universal Service Fund does not encourage, as a general matter, innovation or deployment of broadband.[74] Further, investors and service providers have been aware, or should have been aware, for quite some time that the Commission is likely to transition to a restructured universal service

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71 National Broadband Plan, Section 8.3., at 141.

72 This is especially true where incumbents are experiencing competition within some portion of their territories. *See* National Broadband Plan, Recommendation 8.6, at 147.

73 *Policies and Rules Concerning Rates for Dominant Carriers*, 5 FCC Rcd 6786, 6790 (1990) *aff'd Nat'l Rural Telecom Ass'n v. FCC*, 988 F.2d 174 (D.C. Cir. 1993). While the National Broadband Plan suggested an outside deadline of 2020 for transition from the High Cost program to the CAF, XO submits both that this date should be moved up and that intermediate milestones should be set along the way to ensure concrete progress toward that goal. *See* National Broadband Plan, Recommendation 8.13, at 150.

74 Moving rate of return carriers to incentive regulation would be welcome, but it would not replace the benefits of and need for an expeditious transition from the High Cost Fund to the CAF as soon as possible, as XO argues herein.

program that end subsidies for voice-only networks. The acclimation to a new regulatory regime cannot be reasonably described as unexpected. Moreover, as long as the funds are not made available in direct support of broadband networks, other providers that may be willing to step in and deploy such networks in competition with existing providers with a modest funding subsidy (under reverse auctions which XO advocates below) may be deprived of the opportunity while reduction of the High Cost Fund is slowed.

B. Broadband Connect American Funding Should Be Awarded Through the Use of a "Reverse Auction" Process.

There is a growing swell of support for using a competitive bidding process – or reverse auctions, as they are commonly described – to distribute High Cost funds. As an initial matter, it should be recognized that competitive bidding processes are "the standard way the government typically procures any good or service."[75] In 2008, the Commission itself proposed the use of reverse auctions to determine the recipients of high cost funding disbursements.[76] A growing number of state USF funds and foreign countries already are using reverse auctions to distribute universal service funding.[77]

The benefits of reverse auctions are several. *First*, reverse auctions are the most economically efficient means of determining both the minimally required subsidy amount

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[75] Scott Wallsten, "Reverse Auctions and Universal Telecommunications Service: Lessons from Global Experience," April 2008 (Technology Policy Institute) at 3-4 ("Wallsten").

[76] *High-Cost Universal Service Support, Federal-State Joint Board on Universal Service*, WC Docket No. 05-337, CC Docket No. 96-45, Notice of Proposed Rulemaking, 23 FCC Rcd 1495 (2008) ("Reverse Auction Notice").

[77] *See, e.g.*, National Broadband Plan, Section 8.3., at 140 and nn. 30 and 31 (describing state use of reverse auctions); Irene S. Wu, "Maximum Impact for Minimum Subsidy: Reverse Auctions for Universal Service in Chile and Australia," October 2010, revised Nov. 15, 2010 (FCC Staff Working Paper 2); *Wallsten, generally* (reviewing reverse auctions processes and results in Australia, Chile, Colombia, India, Nepal, and Peru).

and the identity of the most deserving recipient. If carriers compete against each other for support in a given area, the resulting "market" can be expected to identify the provider that will support the program at the lowest cost. The ideal subsidy would be equal to the smallest difference between the price at which a company would be willing to provide a service and the investment that is required to render the service. Subsidy programs based on costs-of-service do not readily produce this result because the recipient of funds has an incentive to maximize the subsidy. *Second*, reverse auctions can encourage new competitors to enter a service market, potentially increasing competition overall in the nation's marketplace and spurring innovation. Other methods of fund distribution tend to favor established players over new entrants. *Third*, reverse auctions are more transparent than today's disbursement process. The method of selection – the competitive bid process itself – is plain for the public and all participants to see. *Fourth*, reverse auctions can lead to the delivery of universal service funds more quickly than other methods, once the governmental agency responsible for distribution identifies the service area and the requisite services.[78] *Finally*, and most importantly, when programs are awarded to the lowest bidder, the burden on other consumers is minimized.

In light of the many benefits of reverse auctions, and their potential to help speed a reduction in the total amount of universal service funding at the national level, XO supports the Commission's proposal to use reverse auctions to distribute high cost funds in lieu of the current system. Because of the clear benefits of reverse auctions, the

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78 Similarly, when the United States moved from comparative hearings to spectrum auctions to assign radio licenses, the Commission cited the speed of implementation offered by auctions. *See, e.g.*, *In re: Implementation of Section 309(j) of the Communications Act - Competitive Bidding*, 9 FCC Rcd 2348, ¶ 52 (1994).

Commission should move as rapidly as possible to using the competitive bidding process to allocate *all* CAF funds, not just the first phase CAF funds as suggested in the *NPRM*.[79]

As noted above, reverse auctions have the potential to increase competition and to promote new entrants. To maximize the pro-competitive potential of reverse auctions, the CAF should be awarded on a technology-neutral basis. Recent trends show that broadband is being provided almost equally extensively on both a mobile and wireline basis, so companies should be entitled to bid in reverse auctions regardless of the technology to be used to fulfill the project.[80] This will help ensure that the lowest possible bid is obtained,[81] maximizing efficiency, and also is the best chance to spur innovation in broadband services for the area to be served using the subsidy.[82]

As stated earlier, High Cost Support should be discontinued for circuit-switched networks. Additionally, XO agrees with the Commission that, to ensure that as many unserved areas as possible receive the benefit of broadband, all-IP networks as quickly as possible, there should be only one recipient of CAF support in any given area.[83] As the Commission noted in its *Reverse Auctions Notice*, there should be only one provider receiving funding in underserved high-cost areas because supporting multiple providers

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79 *NPRM*, ¶¶ 94, n.159.

80 Any exceptions to technology-neutrality should be rare and could be addressed by the Commission on a case-by-case basis.

81 *See Reverse Auction Notice*, 23 FCC Rcd 1495, 1501, ¶ 11 ("If a sufficient number of bidders compete in the auction, the winning bid might be close to the minimum level of subsidy required to achieve the desired universal service goals.").

82 The Commission noted in the *Reverse Auction Notice* that, as of 2008, many wireless carriers were already ETCs receiving Universal Service disbursements in high cost areas. *Reverse Auction Notice*, 23 FCC Rcd 1495, 1500, ¶ 10.

83 *NPRM*, ¶ 268 ("to maximize the reach of available funds, support would be available to, at most, one provider in any given unserved area").

in an area where there is difficulty establishing a business case for even a single provider simply makes no sense.[84] Subsidizing only one provider per area will help ensure that the funds are not only available to benefit potentially as many consumers as possible, but it will also lay the groundwork for reduction of the overall fund as soon as practical. XO noted above that in many areas, multiple providers receive funding from the High Cost Fund, increasing the monies needed to subsidize service in a given area. The same mistake should not be made as high cost funding is transitioned to the CAF.

As CAF funding is implemented in a given area, the Commission should ensure that ILECs and other recipients of current high cost funding cannot "double dip." ILECs and current recipients of USF should, along with any other provider, be able to compete for CAF funds. However, if a current recipient is the successful bidder in a given area, CAF should immediately replace any existing voice support attributable to the service area related to the winning bid. Similarly, if one or more current recipients of high cost funding is unsuccessful in its bid for CAF money, it, or they, must immediately relinquish any existing universal service support for that area. Only in this way can the Commission ensure that implementation of the CAF does not increase overall universal service funding from present levels.

VII. ANY "RECOVERY MECHANISM" MUST BE COMPETITIVELY NEUTRAL.

The Commission seeks comment on whether and how to structure a recovery mechanism as part of its access charge reform plan. As the Commission observes, there is no need that "recovery needs to be revenue neutral" given that carriers have a variety

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84 *Reverse Auction Notice*, 23 FCC Rcd 1495, 1500, ¶ 10; *see also* National Broadband Plan, Recommendation 8.2, at 145 (same).

of regulated and non-regulated revenue sources available to them to make-up revenue losses.[85] However, the key is that any recovery mechanism be competitively neutral, and not provide one class of carriers an artificial regulatory advantage over any other set of service providers.

A. The Commission Should Facilitate Cost Recovery from the End Users of Adversely Affected Carriers.

One of the major objectives of this proceeding is to end the distortions that are caused when carriers are required to pay amounts to one another based on factors other than the direct cost of service. Such above-cost revenue flows amount to a subsidization of some carriers by their competitors. Inevitably, the recipients of such subsidy make uneconomic decisions intended primarily to preserve their subsidy payments. Subsidies also provide an unfair advantage to recipients and impede the ability of the subsidy payors to compete effectively.

The Commissions asks whether it has any legal or policy obligation regarding a recovery mechanism.[86] From a legal perspective, the Commission need only permit carriers "adequate cost recovery," as noted in the National Broadband Plan.[87] Neither this Commission nor any State has any obligation to maintain revenues streams for carriers that are not rooted in a cost basis. The Commission pointed to the fact that existing intercarrier compensation revenue may represent up to 30 percent of some carriers' regulated revenues while questioning in the *NPRM* whether to consider a

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85 *NPRM,* ¶ 568.

86 *Id*.

87 National Broadband Plan at 148.

recovery mechanism based on current intercarrier compensation revenue.[88] XO urges the Commission, however, to focus on cost recovery, not simply on replacing reduced intercarrier compensation revenues.[89] There is no legal or policy justification for compensating carriers for a reduction in this revenue without tying such recovery to the costs incurred by the carrier. Carriers must be required to consider whether they can support business plans predominantly, if not exclusively, on revenues from customers, not by subsidizing costs through a recovery mechanism based on inflated intercarrier compensation rates. The solution, therefore, is to ensure that any recovery comes from charges collected from the end users of the adversely affected carriers.

Fortunately, the Commission already has an efficient mechanism in place to enable carriers to recover lost interstate access charge revenues and costs from end users that benefit from the access services involved. The interstate Subscriber Line Charge ("SLC") is a flat-rated charge that is designed to recover part of the interstate portion of the local loop from end users. The use of the SLC can simply be expanded to allow LECs to recover revenues lost to access reform or additional costs as well. Currently, SLCs charged by ILECs are subject to an absolute cap that varies between primary residential/single line business ($6.50), non-primary residential lines ($7.00), or multi-line businesses ($9.20). XO suggests that the SLC cap be deregulated and allow market forces establish how much "lost revenue" can be recovered.[90] Alternatively, XO supports

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88 *NPRM,* ¶ 567.

89 *Id.,* ¶ 492.

90 *See* National Broadband Plan at 149.

the proposal included in the *2008 Order and ICC/USF FNPRM* to increase the residential SLC by $1.50 and the multi-line business SLC by $2.30.[91]

Using a deregulated SLC increase as the *exclusive means* to implement a recovery mechanism offers five advantages. First, it imposes cost recovery for local network facilities only on the cost-causers, consistent with sound economic principles. Second, it enables market forces to determine the amount of lost revenue actually recovered. Third, a deregulated SLC eliminates the problem of cross-subsidy between competing carriers. Fourth, since all LECs would be able to increase their SLCs, it permits all LECs an equal chance to recover their lost access revenues. Finally, since neither the government nor any other third party has to administer the plan, recovering lost revenue through SLC charges to end users is much simpler to implement and administer than any other alternative.

B. Any One-Sided Replacement Fund is Fundamentally Unfair and Anticompetitive.

The Commission must not repeat the mistake of the State of Michigan which recently created a mechanism that permits ILECs to achieve revenue neutrality at the expense of their competitors. Legislation adopted in 2009 required all LECs to reduce their intrastate access charge rates to interstate levels, and created a restructuring fund that LECs could dip into to replace any lost revenue. While *all* carriers must contribute to the Michigan restructuring fund, only ILECs are entitled to claim reimbursement from

91 *See, High-Cost Universal Service Support; Universal Service Contribution Methodology; Developing a Unified Intercarrier Compensation Regime; et* al, 24 FCC Rcd 6475, 6828-29, App. C, ¶ 293, 6630, App. A, ¶ 298 (2008).

it. CLECs have rightfully asked the Commission to preempt the Michigan plan.[92] By requiring CLECs to contribute to a fund which benefits only their ILEC competitors, the Michigan plan violates one of Section 254's core "principles," namely that contributions to universal service be "equitable and nondiscriminatory."[93] CLECs pay into the fund, and then ILECs draw from it in order to keep rates below market levels – prices that CLECs must then attempt to match without the benefit of the same subsidy. It is hard to conceive of something more anticompetitive.

Thus, if the Commission chooses to adopt a special Recovery Mechanism (which it should not), it is critical that *all* LECs that lose revenue due to implementation of access charge reform have *equal rights and opportunity* to claim reimbursement from such fund. An all-ILEC – or all rate-of-return ILEC – slush fund, whether explicitly or practically, would create an intolerably unequal playing field, and place the competitors of the ILECs at an inherently unfair market disadvantage created solely by regulatory fiat. That is an outcome that must be avoided at all costs.

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92 *In the Matter of ACD Telecom, Inc. Joint Petition for Expedited Declaratory Ruling that the State of Michigan's Statute 2009 PA 182 is Preempted Under Sections 253 and 254 of the Communications Act*, WC Docket No. 10-45 (filed Feb. 9, 2010).

93 47 U.S.C. § 254(b)(4).

CONCLUSION

For the forgoing reasons, XO respectfully requests that the Commission reform its intercarrier compensation and universal service rules and adopt strong, clear IP interconnection policies in a manner consistent with the proposals contained herein.

Sincerely,

Brad E. Mutschelknaus
Edward A. Yorkgitis, Jr.
Denise Smith
Kelley Drye & Warren LLP
3050 K Street, NW – Ste. 400
Washington, DC 2007
202-342-8500
Counsel to XO Communications, LLC

Heather B. Gold
Lisa R. Youngers
Teresa K. Gaugler
XO Communications
13865 Sunrise Valley Drive
Herndon, Virginia 20171

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