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RECORDS AND
REPORTING

April 18, 2001

Mrs. Blanca S. Bayó
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Florida Public Service Commission
2540 Shumard Oak Boulevard
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Re: **000075-TP (Generic ISP) (Phase I)**

Dear Ms. Bayó:

Enclosed is an original and fifteen copies of BellSouth Telecommunications, Inc.'s Brief of the Evidence, which we ask that you file in the captioned docket.

A copy of this letter is enclosed. Please mark it to indicate that the original was filed and return the copy to me. Copies have been served to the parties shown on the attached Certificate of Service.

Sincerely,

E. Earl Edenfield, Jr.

E. Earl Edenfield, Jr. (KA)

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STATEMENT OF THE CASE

The Telecommunications Act of 1996 (“1996 Act”) requires interconnection negotiations between local exchange companies and new entrants. Under the Act, all local exchange carriers have a duty to establish reciprocal compensation arrangements for the transport and termination of telecommunications. 47 U.S.C. § 251(b)(5). As a matter of federal law, however, reciprocal compensation is owed only for the transport and termination of local traffic. This generic proceeding was instituted to determine whether the Florida Public Commission (“Commission”) has the authority to establish an inter-carrier compensation mechanism for Internet traffic routed through Internet Service Providers (“ISPs”) and if so, what should this compensation mechanism be. BellSouth Telecommunications, Inc. (“BellSouth”), Verizon Florida, Inc. (“Verizon”), Sprint Communications Company L.P. (“Sprint”), and numerous ALECs intervened in this proceeding to assert their position regarding the above question.

The hearing in this matter was held on March 7 and 8, 2001. At the hearing, BellSouth submitted the direct and rebuttal testimony of Beth Shiroishi and David Scollard and the rebuttal testimony of Dr. William Taylor. Verizon submitted the direct and rebuttal testimony of Edward C. Beauvais and Howard Lee Jones. Sprint submitted the direct and rebuttal testimony of Michael R. Hunsucker. E.spire submitted the testimony of James Falvey. The ALECs submitted the direct and rebuttal testimony of Lee L. Selwyn, and Staff submitted the direct testimony of Gregory D. Fogleman. This Brief of the Evidence is submitted in accordance with the post-hearing procedures set forth in the Commission’s Pre-Hearing Order (PSC-01-0422-PHO-TP) dated December 22, 2000 and Rule 25-22.056, Florida Administrative Code. A summary of BellSouth’s position on each issue to be resolved in this docket is set forth in the following pages and marked with a double asterisk.

STATEMENT OF BASIC POSITION

The Commission's goal in this generic proceeding is to resolve each issue consistent with the requirements of the Act and federal law, including the regulations prescribed by the Federal Communications Commission ("FCC"). The Commission should adopt BellSouth's positions on the issues in dispute. BellSouth's positions on these issues are reasonable and consistent with the 1996 Act and federal law.

STATEMENT OF POSITION ON THE ISSUES

ISSUE 1(a): Does the Commission have the jurisdiction to adopt an inter-carrier compensation mechanism for delivery of ISP-bound traffic?

ISSUE 1(b): If so, does the Commission have the jurisdiction to adopt such an inter-carrier compensation mechanism through a generic proceeding?

** The Commission does not have jurisdiction to adopt an inter-carrier compensation mechanism for ISP-bound traffic because this traffic is interstate. Notwithstanding, if the Commission finds that it has jurisdiction, the compensation mechanism should be established through a generic proceeding. **

DISCUSSION

The Commission does not have the jurisdiction to adopt an inter-carrier compensation mechanism for the delivery of ISP-bound traffic because the Commission does not have the authority to set compensation rates for interstate traffic.

A. The Commission does not have jurisdiction over interstate traffic, which includes ISP-bound traffic.

The 1996 Act grants the FCC jurisdiction over "all interstate and foreign communication by wire." 47 U.S.C. § 152(a); *see also*, Declaratory Ruling and Notice of Proposed Rule Making, Docket No. 96-98, *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996; Inter-Carrier Compensation for ISP-Bound Traffic*, FCC 99-38 (1999) ("Declaratory Ruling"), *vacated and remanded*, *Bell Atlantic Tel. Cos. v. FCC*, 206

F.3d 1 (D.C. Cir. 2000). Indeed, in its First report and Order, the FCC made it perfectly clear that reciprocal compensation rules do not apply to interstate or interLATA traffic such as interexchange traffic. (Tr. 599); First Report and Order, *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, FCC 96-325, Docket No. 96-98 at ¶ 1034 (First Report and Order) (Aug. 8, 1996). Consequently, pursuant to 47 C.F.R. § 51.701(9), this Commission only has the authority to establish rates for the transport and termination of local telecommunications traffic. See 47 C.F.R. § 51.709(a).¹ Local traffic is defined as “[t]elecommunications traffic between a LEC and a telecommunications carrier . . . that originates and terminates within a local service area established by the state commission.” 47 C.F.R. § 51.701(b)(1).

As a matter of federal law, ISP-bound calls are not local and thus the Commission does not have the authority to establish inter-carrier compensation rates for this type of traffic. To understand why ISP-bound calls are not local traffic, one must first understand the basic structure of an Internet communication. Most individuals obtain access to the Internet through an ISP. See Declaratory Ruling, FCC 99-38 at ¶ 4. When a person logs onto the Internet, he or she typically uses a modem to dial a seven or ten digit telephone number assigned to the ISP. *Id.* The call does not terminate at the ISP, however. (Tr. 590) Rather, the customer uses the ISP as a conduit for transmitting information to and receiving information from Internet sites located across the country and around the world. *Id.* (Tr. 590)

¹ 47 C.F.R. § 51.709(a) provides that: “In state proceedings, a state commission shall establish rates for the transport and termination of local telecommunications traffic that are structured consistently with the manner that carriers incur those costs, and consistently with the principles in §§ 51.507 and 51.509.”

In its Declaratory Ruling, the FCC confirmed that, under its prior precedent, ISP-bound calls do not terminate at an ISP's premises². The FCC explained that such calls "do not terminate at the ISP's local server . . . but continue to its ultimate destination." Declaratory Ruling at ¶ 12. The FCC further determined that, because such calls do not terminate locally, neither the 1996 Act nor its regulations require reciprocal compensation for ISP-bound calls:

[Section 251(b)(5) of the Act and our rules promulgated pursuant to that provision concerning inter-carrier compensation for interconnected *local* telecommunications traffic. We conclude in this Declaratory Ruling, however, that ISP-bound traffic is *non-local* interstate traffic. Thus, the reciprocal compensation requirements of section 251(b)(5) of the Act and . . . of the Commission's rules do not govern inter-carrier compensation for this traffic.

Id. at ¶ 26, n.87 (second emphasis added).

In March 2000, the D.C. Circuit vacated and remanded the Declaratory Ruling. *See Bell Atlantic Tel. Cos. v. FCC*, 206 F.3d 1 (D.C. Cir. 2000). The court did so, however, not because the FCC's decision was substantively incorrect, but rather for lack of sufficient explanation by the FCC. *Id.* at 9. Indeed, although some petitioners in that case asked the court to rule that ISP-bound traffic terminates at the ISP and is therefore subject to reciprocal compensation under Section 251(b)(5), the court did not do so. Instead, it concluded only that the FCC had insufficiently explained the aspects of its decision. *See id.* ("the Commission has not provided a satisfactory explanation why LECs that terminate calls to ISPs are not properly seen as

² Indeed, throughout the evolution of the Internet, the FCC repeatedly has asserted that ISP-bound traffic is interstate. (Tr. 591). For instance, since 1983, the FCC has exempted ISPs from the payment of certain interstate access charges. *Id.*; *see also*, *MTS/WATS Market Structure Order*, 97 FCC 2d at 715. Also, in the FCC's Notice of Proposed Rulemaking, *In the Matter of Amendments to Part 69 of the Commission's Rules Relating to Enhanced Service Providers*, CC Docket No. 87-215 (July 17, 1987), the FCC ruled that enhanced service providers, like ISPs, "use the local network to provider interstate services. (Tr. 591-92).

‘terminat[ing] . . . local telecommunications traffic,’ and why such traffic is ‘exchange access’ rather than ‘telephone exchange service’”) (alternation in original).

The court made clear that, with proper explanation, the FCC could again determine that neither the 1996 Act nor its regulations impose reciprocal compensation obligations for ISP-bound traffic. *See id.* FCC officials stated an intention to do just that the day the court announced its decision. *See Strickling Believes FCC Can Justify Recip Comp Ruling in Face of Remand*, TR Daily, Mar. 24, 2000.

Importantly, the D.C. Circuit’s vacatur of the Declaratory Ruling is not fatal to a finding that ISP-bound traffic is interstate. The Colorado Public Utilities Commission has found that ISP-bound traffic is interstate and thus not subject to reciprocal compensation after the D.C. Circuit rendered its decision in *Bell Atlantic*. *See Sprint Commun. Co., L.P.*, Col. Pub. Util. Comm’n, No. C00-479, Docket No. 00B-11T (May 5, 2000), 2000 WL 689363 at *2 (“Given that most Internet calls end at locations out of state, it appears that such calls are primarily interstate in nature.”); *see also, Sprint Commun. Co., L.P.*, Mass. Dept. Tele.& Energy, Decision T.E. 00-54 (Dec. 11, 2000), 2000 WL 3314667 *2 (affirming previous decisions finding that reciprocal compensation is not due for ISP-bound traffic because of its interstate nature). A similar conclusion would not be prohibited in Florida, as this Commission has never issued an order that specifies the jurisdictional nature of ISP-bound traffic. (Tr. 855)

Moreover, in an order issued after the Declaratory Ruling, which has not been challenged on appeal and is still good law, the FCC provided a detailed explanation to support its conclusion that ISP-bound traffic is “exchange access” and, therefore, “largely non-local for purposes of reciprocal compensation obligations of section 251(b)(5).” Order on Remand, *Deployment of*

Wireline Services Offering Advanced Telecommunications Capability, FCC 99-413, ¶¶ 36-38 (Remand Order).

As the FCC explained, “the service provided by the local exchange carrier to the ISP is ordinarily exchange access service [*i.e.*, not local service] because it enables the ISP to transport the communication initiated by the end-user subscriber located in one exchange to its *ultimate destination in another exchange*.” Remand Order at ¶ 35 (emphasis added). A LEC “provides access permitting the ISP to complete the transmission from its subscriber’s location to a destination in another exchange using the toll service is typically has purchased from [an] interexchange carrier.” *Id.* at ¶ 36. In sum, the FCC confirmed that ISP-bound traffic normally “originate[s] in one exchange and terminate[s] in another.” *Id.* at ¶ n.77.³

The fact that ISP-bound traffic is “exchange access” is further evidenced by the fact that BellSouth’s ADSL service offering was approved and filed by the FCC in BellSouth’s Tariff FCC Number 1. (Tr. 593) According to a FCC White Paper, “DSL is a high speed telecommunications service that offers consumers the ability to access data services at speeds of up to 50 times the traditional 56 kbps dial-up modem. The Commission concluded that DSL services were properly classified as interstate telecommunications services and should be tariffed at the federal level.” Jason Oxman, *The FCC and the Unregulation of the Internet*, at 25-26 (Office of Plans and Policy FCC, Working Paper Nov. 31, 1999). “Obviously, a call to cyberspace, either through a DSL connection or via an ISP, constitutes an interstate call under

³ The D.C. Circuit did not consider this explanation because the FCC “did not make this argument in the ruling under review.” *Bell Atlantic*, 206 F.3d at 9. Nonetheless, the D.C. Circuit noted that the statutory definitions of “exchange access” and “telephone exchange service” are sufficiently ambiguous that “any agency interpretation would be subject to judicial deference.” *Id.*

the FCC's jurisdiction." Thomas W. Bonnett, *Is ISP-Bound Traffic Local or Interstate?*, 53 Fed. Comm. L.J. 239, 273 (2001).

Simply put, the FCC has historically treated ISP-bound and similar traffic as being interstate in nature. Consequently, the Commission does not have the jurisdiction or authority to establish a recovery mechanism for ISP-bound traffic.

B. State commissions do not have the authority to establish an inter-carrier compensation mechanism for ISP-bound traffic.⁴

Sprint, and probably the other ALECs, have or will argue that the Declaratory Ruling empowered the Commission to establish an inter-carrier recovery mechanism for ISP-bound traffic in this proceeding. (*See* Tr. 410) In that case, the FCC held that, although it found that ISP-bound traffic was largely interstate, "neither the statute nor our rules prohibit a state commission from concluding in an arbitration that reciprocal compensation is appropriate in certain instances not addressed by section 251(b)(5), so long as there is no conflict with governing federal law." Declaratory Ruling at ¶ 26. Consequently, the FCC concluded that "in the absence of a federal rule, state commissions have the authority under section 252 of the Act to determine inter-carrier compensation for ISP-bound traffic." *Id.* at n.87.

As admitted by Sprint witness Hunsucker, however, the D.C. Circuit vacated the Declaratory Ruling in its entirety. (Tr. 410) Thus, as a matter of law, the FCC's grant of power to state commissions to establish a compensation mechanism for ISP-bound traffic in the absence of a federal mechanism is no longer valid.⁵

⁴ The following discussion addresses Chairman Jacob's request that the parties brief the issue of the Commission's authority to establish a reciprocal compensation policy outside of a specific arbitration proceeding. (Tr. 904).

⁵ The D.C. Circuit's vacatur of the Declaratory Ruling is more significant for the FCC's finding that state commissions can determine inter-carrier compensation for ISP-bound traffic than it is for its finding that ISP-bound

Without this express authority, state commissions cannot establish such a mechanism in an arbitration proceeding or otherwise because, as stated above, ISP-bound traffic constitutes interstate traffic. As a result, establishing an inter-carrier compensation mechanism for the delivery of ISP-bound traffic would violate federal law and thus be prohibited.⁶ *See* 47 U.S.C. § 152(a); *see e.g.*, Declaratory Ruling at ¶ 25. This does not mean that state commissions cannot address the issue of ISP-bound traffic in an arbitration proceeding under the 1996 Act. *See* First Report and Order at ¶ 84 (the state’s authority over interconnection agreements pursuant to Section 252 “extends to both interstate and intrastate matters.”). To the contrary, it only means that any order must be consistent with federal law. *See e.g.*, Declaratory Ruling at ¶ 25; *see also*, Bonnett, *supra* at 16 (“If there remain “two hands on the steering wheel,” then the FCC’s firm grip clearly dominates.”). Thus, if a carrier seeks reciprocal compensation for ISP-bound traffic in an arbitration, the Commission has two options: (1) it can refuse to hear the issue because it is without authority to require the payment of reciprocal compensation for ISP-bound traffic; or (2) address the issue in accordance with federal law and find that reciprocal compensation is not owed for ISP-bound traffic because such traffic is interstate in nature.

traffic is largely interstate. This is so because, before and after the Declaratory Ruling, the FCC has treated ISP-bound or similar traffic as being interstate in nature. *See* Declaratory Ruling at ¶ 26 n.88 (“As noted, in other contexts, we have directed the states to treat such traffic as local.”); Remand Order at ¶¶ 35-38. In contrast, prior to the Declaratory Ruling, state commissions were not expressly authorized by the FCC to establish an inter-carrier compensation mechanism for ISP-bound traffic.

⁶ In addition, no state statute authorizes the Commission to establish an inter-carrier compensation mechanism for ISP-bound traffic. Even if such a statute existed, it would be contrary to federal law and thus prohibited.

Much emphasis has been placed upon one passage in the D.C. Circuit's vacatur of the Declaratory Ruling.⁷ In its conclusion, the court held that it vacated the Declaratory Ruling because the FCC did not adequately explain its classification of ISP-bound traffic as "exchange access." *Bell Atlantic Tel. Cos.*, 206 F.3d at 8. The court then stated that "in the interim our vacatur of the Commission's ruling leaves the incumbents free to seek relief from state-authorized compensation that they believe to be wrongfully imposed." *Id.* Sprint and probably the other ALECs have or will attempt to argue that this one passage somehow resurrects the Declaratory Ruling as it related to authorizing state commissions to establish an inter-carrier compensation mechanism for ISP-bound traffic. (*See* Tr. 381-82; 412-14)

To interpret this passage in such a manner would be to ignore the undisputed fact that the D.C. Circuit vacated the Declaratory Ruling in its entirety. If the court truly intended to preserve the FCC's express determination that state commissions can establish inter-carrier compensation mechanisms for ISP-bound traffic, it could have simply vacated the Declaratory Ruling in part, which it did not do.

The most logical interpretation of this passage is that the court recognized that its vacatur would cause the state of the law to be somewhat unsettled and that, whether authorized or not, state commissions would be forced to address the issue of a compensation mechanism for ISP-bound traffic in arbitration proceedings. By making this statement, the court ensured ILECs that, until the FCC issued its order on remand, they could appeal any state-authorized compensation mechanism they believed to be wrongfully imposed. This recognition should not be construed as an express finding by the D.C. Circuit that state commissions are authorized to establish an

⁷ The following discussion addresses Commissioner Jaber's specific request that the parties brief the effect of the last paragraph of the D.C. Circuit's vacatur on the Commission's authority to establish an inter-carrier compensation

inter-carrier compensation mechanism for ISP-bound traffic in an arbitration proceeding or otherwise.

In sum, because ISP-bound traffic is interstate, state commissions do not have the jurisdiction or are authorized to establish an inter-carrier compensation mechanism for ISP-bound traffic.

For the reasons expressed above, the Commission does not have the jurisdiction to adopt an inter-carrier compensation mechanism for the delivery of ISP-bound traffic. However, if the Commission determines that it has such jurisdiction, then a generic proceeding is the proper forum to address the issue.

ISSUE 2: Is delivery of ISP-bound traffic subject to compensation under Section 251 of the Telecommunications Act of 1996?

** No. Because the Act only requires reciprocal compensation for the delivery of local traffic, ISP-bound traffic is not subject to compensation under Section 251 of the Act. **

DISCUSSION

The Act only requires reciprocal compensation for the delivery of local traffic. (Tr. 599) As made clear above, ISP-bound traffic is interstate and not local traffic. Thus, for the foregoing reasons, the delivery of ISP-bound traffic is not subject to compensation under Section 251 of the Act.

ISSUE 3: What actions should the Commission take, if any, with respect to establishing an appropriate compensation mechanism for ISP-bound traffic in light of current decisions and activities of the courts and the FCC?

** The Commission should not take any action because ISP-bound traffic is not subject to inter-carrier compensation under the 1996 Act and the FCC is expected to render a decision shortly. If the Commission does anything, it should adopt bill-and-keep. **

DISCUSSION

mechanism for ISP-bound traffic. (Tr. 904)

It is not appropriate for the Commission to take any action on this issue because inter-carrier compensation for ISP-bound traffic is not an obligation under Section 251 of the Act. (Tr. 601) At a minimum, the Commission should wait until the FCC renders its expected Order regarding this issue before spending resources developing a plan that may be rendered moot by an upcoming FCC decision. (*Id.* at 601-02). Indeed, espire witness, Falvey, admitted that the FCC will be making a decision “in the next couple of weeks, and [that] they [*sic*] want to put it away once and for all.” (Tr. 283) However, if the Commission feels that it must act at this time, then, as discussed more fully below, it should follow the lead of the Colorado and other state commissions, as well as the recommendation of this very Commission, and adopt a bill-and-keep mechanism for the delivery of ISP-bound traffic. *See Sprint Commun. Co., L.P.*, Col. Pub. Util. Comm’n, No. C00-479, Docket No. 00B-11T (May 5, 2000), 2000 WL 689363 at *2; (Tr. 888-890).

ISSUE 4: What policy considerations should inform the Commission’s decision in this docket?

**** The Commission should consider how this decision will affect competitive entry decisions by ALECs, cost recovery and the economics of the cost causation, the impact on residential customers, and the continued development of competition. ****

DISCUSSION

In deciding whether to implement a compensation mechanism for ISP-bound traffic in this proceeding, the Commission must consider a number of factors. Among those factors are: (1) the effects that such a decision will have on competitive market entry decisions by ALECs; (2) cost recovery and the economics of the cost causation; (3) the impact on residential customers; and (4) the continued development of competition. Each of these factors must be considered in light of the current economic reality that Commission-approved rates for basic

residential exchange service are set below their actual cost. This economic reality is exacerbated by the additional burden being placed on the ILECs to subsidize the ALECs through reciprocal compensation payments for ISP-bound traffic.

Taking the numbers proposed by ALEC witness Selwyn, the average residential customer will spend approximately 1500 minutes per month on the Internet. (Tr. 51) At the Commission-approved tandem switching rate of \$.00325 (Tr. 271), which the ALECs contend is appropriate, this equates to a reciprocal compensation liability for ISP-bound traffic of \$4.88 per month. When compared to the current rate for basic residential service of \$7.41 in rate group 12, the impact of reciprocal compensation for ISP-bound traffic is as obvious as it is significant. Equally important is the fact that basic rates for residential service were established long before the advent of the Internet and, therefore, did not contemplate that level of usage. (Tr. 604-05) In short, BellSouth is providing service at below cost based on rates that did not take Internet usage into consideration and, at the same time, is being asked to subsidize ALEC market entry. This scenario is causing skewed economic and competitive results.

It almost goes without saying that the goal of the 1996 Act was to create a competitive environment in both residential and business markets. ALECs, however, are not burdened with "carrier of last resort" responsibilities and can therefore focus on the more lucrative segments of the telecommunications market. (Tr. 625) Thus, the payment of reciprocal compensation for ISP-bound traffic has adversely affected competition in two ways. First, ALECs have chosen to not provide widespread competitive alternatives in the residential market, as reciprocal compensation liabilities will often exceed the revenue derived from providing the basic local service, which is itself already priced below cost. (Tr. 603) Second, ALECs have been drawn almost exclusively to the ISP segment of the business market because the ALECs not only

receive revenue from the ISPs for providing the requested services, they also receive reciprocal compensation payments from the ILECs that, in some instance, exceed the revenue derived from providing the underlying service to the ISPs. (Tr. 634) Further, the payment of reciprocal compensation for ISP-bound traffic discourages the deployment of any technology that does not generate reciprocal compensation, such as xDSL technologies. (Tr. 608) The Colorado Commission looked at these same policy considerations and ordered bill-and-keep instead of reciprocal compensation for the transport and termination of ISP-bound traffic. In coming to this conclusion, the Commission found that reciprocal compensation gave the ALECs an “unwarranted property right” and skewed the market:

While ISP calls appear to be interstate in nature, our conclusion is not necessarily based upon that. Even if this traffic were considered to be local in nature, the Commission still would not embrace reciprocal compensation with a positive rate. Such a scheme would, in our view, bestow upon Sprint an unwarranted property right, the exercise of which would result in decidedly one-sided compensation. In addition we find that reciprocal compensation would introduce a series of unwarranted distortions into the market. These include: (1) cross-subsidization of CLECs, ISPs, and Internet users by the ILEC’s customers who do not use the Internet; (2) excessive use of the Internet; (3) excessive entry into the market by CLECs specializing in ISP traffic mainly for the purpose of receiving compensation from the ILECs; and (4) disincentives for CLECs to offer either residential service or advanced services themselves. In short, we agree with US West that reciprocal compensation for ISP traffic would not improve overall social welfare; it would simply promote the welfare of some at the expense of others.

Sprint Commun. Co., L.P., Col. Pub. Util. Comm’n, No. C00-479, Docket No. 00B-11T (May 5, 2000), 2000 WL 689363 at *2.

These same policy concerns and market distortions apply with equal force in Florida. Indeed, Staff witness Fogleman admitted that ALECs in Florida are targeting ISPs as customers to obtain reciprocal compensation under the current rate scheme and that reciprocal compensation for ISP-bound traffic benefits ALECs over ILECs. (Tr. 877-88)

From an economic perspective, the payment of reciprocal compensation for ISP-bound traffic is inconsistent with basic cost causation and recovery principles. In the context of an Internet call, the end user accessing the Internet is a customer of the ISP. As noted by witness Shiroishi, “[t]he ISP bills the customer separately and when the customer has a problem with their Internet access service he calls the ISP. The fact that the end user is the ILEC’s customer for local service does not change the fact that the same end user is the ISP’s customer for access to the Internet. The end user is no more the ILEC’s customer on Internet calls than it is the ILEC’s customer for interLATA long distance calls.” (Tr. 604) Likewise, the ALEC is compensated by its customer who in this instance is the ISP that buys services (such as PRIs) from the ALEC’s tariffs. (*Id.*) As basic local exchange rates were not designed to cover the added reciprocal compensation costs associated with Internet usage, the ILEC becomes the only entity in this transaction that is not compensated. (*Id.*) Thus, the payment of reciprocal compensation for ISP-bound traffic is wrong not only from a competitive perspective, but an economic one as well.

But for the FCC’s access charge exemption to ISPs, the best solution would be to treat ISP-bound traffic in the same manner as other interLATA traffic and require the payment of originating and terminating access. (Tr. 821) Under that scenario, every entity involved in the Internet call would be compensated. As that solution is not available, the next best solution is a bill-and-keep mechanism. (Tr. 826) Although not every entity involved in the completion of an Internet call is compensated under a bill-and-keep mechanism (mainly the ILEC), such a mechanism will stop the subsidy that has resulted from the ALEC being double-paid by both the ISP and the ILEC. (Tr. 626)

In addition to those discussed above, there are other advantages to establishing a bill-and-keep mechanism for ISP-bound traffic. As noted by Staff witness Fogelman, bill-and-keep eliminates the need for billing and the costs associated with monitoring traffic and reduces the ability of carriers to target customers solely for expected reciprocal compensation revenues. (Tr. 861-62) The prerequisites to establishing a bill-and-keep mechanism are found in FCC Rule 51.713, which allow a state commission to establish a bill-and-keep mechanism when *local* traffic is “roughly balanced.” (Tr. 622-23) The rule goes on to provide that a state commission can presume that traffic is balanced in the absence of that presumption being rebutted by another party. (See, 51.713 (c)) As discussed in the previous issues, ISP-bound traffic is exchange access (interstate) traffic. Therefore, the limitations of FCC Rule 51.713 are not applicable in this instance. Even if the Commission were to determine that ISP-bound traffic is local traffic, there is no guidance on how to define the “in balance” requirement. For instance, the Commission could determine that a majority of the carriers operating in Florida have balanced traffic and therefore traffic in Florida is roughly in balance. Likewise, the Commission could look at the balance of traffic that would result from the implementation of a bill-and-keep mechanism over a three-year period and conclude that over that period of time traffic will be roughly balanced. While presumably some carriers will have an imbalance of traffic when considering ISP-bound traffic, no such showing was made by any carrier in this proceeding.

In conclusion, while bill-and-keep may result in a number of ALECs having to revise their competitive strategy in the short term, such a mechanism will result in more widespread competition in the residential and business markets. There are many carriers, however, that have been able to compete in Florida without targeting ISPs and should be indifferent to a bill-and-keep mechanism for ISP-bound traffic.

ISSUE 5: Is the Commission required to set a cost-based mechanism for delivery of ISP-bound traffic?

** No, not required. However, if the Commission establishes a compensation mechanism other than bill-and-keep, it should be cost-based and reflect the cost actually incurred for delivering ISP-bound traffic, not the cost of terminating a local call. **

DISCUSSION

Although for different reasons, the Parties appear to be in general agreement that if the Commission establishes an ISP-bound traffic cost recovery mechanism, the rates should be cost-based. BellSouth contends that ISP-bound traffic is jurisdictionally interstate and therefore outside of the pricing requirements of §252(d) of the 1996 Act. (Tr. 605) Notwithstanding, if the Commission establishes a cost recovery mechanism for ISP-bound traffic (and the mechanism is something other than bill-and-keep), the mechanism should be cost-based. Further, the rate should be based on the actual cost incurred by the carrier who serves the ISP, not on the cost to terminate a local call. (Tr. 606)

ISSUE 6: What factors should the Commission consider in setting the compensation mechanisms for delivery of ISP-bound traffic?

** If the Commission establishes a compensation mechanism for ISP-bound traffic other than bill-and-keep, the Commission should consider the characteristics of ISP-bound calls as distinguished from local calls, including call length and the cost of network equipment. **

DISCUSSION

As discussed in Issue 4 above, if the Commission determines that it has the jurisdiction to establish a compensation mechanism for ISP-bound traffic, that mechanism should be bill-and-keep. Under a bill-and-keep mechanism, the ALEC is compensated by the ISP and the ISP is, in turn, compensated by the end-user customer. Thus, there are no uncompensated costs to be recovered and no work to be done by the Commission in the form of developing and implementing rates.

If instead, this Commission considers a per minute of use (“MOU”) compensation arrangement, at a minimum it should consider the characteristics of ISP-bound calls as distinguished from local calls. At a minimum the following factors would need to be considered: call duration, cost of equipment, and call set-up cost differences for originating end office switching and subsequent end office switching. (Tr. 609; 626)

Typically, reciprocal compensation billing consists of separate charges for end office and/or tandem switching and common transport. When BellSouth conducted the cost studies for these elements, it did not consider a mix of local calls along with non-local, long-duration ISP-bound calls when arriving at the average length of a call, which is an important factor in determining the appropriate per MOU rate for ISP-bound traffic. (Tr. 610) As noted by witness Shiroishi:

Switching costs have two major components – call set-up costs and call duration costs. Call set-up costs occur irrespective of how long the call actually lasts. Conversely, call duration costs are specifically related to how long the call actually lasts. On average, a local call is approximately three minutes long. Obviously, the call duration for an Internet call is substantially longer than for a local call.

(*Id.*) Thus, the existing per minute rates for local switching, if applied to ISP-bound traffic, would greatly overstate the amount of compensation.

Additionally, the existing rates for end office switching were established for unbundled local switching, which contemplate the originating switch of a call. With ISP-bound traffic, the switch would never be the originating switch, but the switch that directly serves the ISP. Thus, the call set-up involved in the originating switch is more complex (and ultimately more expensive) than the call set-up on subsequent end office switches. (Tr. 625)

The costs for traditional reciprocal compensation also take into account conventional switching equipment used in an ILEC's network for conventional voice traffic. As noted by witness Shiroishi, ALECs that have ISPs as a target market have the luxury of not having to utilize these conventional switching technologies:

With new technologies, a LEC can deploy scaled-down switches, often referred to as "softswitches." These switches do not have all the features and functionalities of a traditional switch, but are instead designed exclusively to funnel dial-up traffic to ISPs. The cost of these "softswitches" is dramatically less than conventional switches. Examples include the Nortel CVX 1800 and Level 3's network. Level 3 boasts that by using Cisco routers for data and Lucent softswitches for voice, it expects to "reap capital savings between 40% and 60%, and operational savings 'that may be even greater.'" (Footnote omitted)

(Tr. 611) In conclusion, there are a number of cost differentials that the Commission will need to consider if the Commission decides to set a per MOU compensation mechanism for ISP-bound traffic.

ISSUE 7: Should inter-carrier compensation for delivery of ISP-bound traffic be limited to carrier and ISP arrangements involving circuit-switched technologies?

**** Yes. Non-circuit-switched connections should not be included as no switching costs are incurred and, therefore, there is no switching compensation at issue. ****

DISCUSSION

To the extent that the Commission requires inter-carrier compensation for delivery of ISP-bound traffic, that compensation should be limited to carrier and ISP arrangements involving circuit-switched technologies (also known as "dial-up"). The issue of the treatment of non-circuit-switched technologies, such as IP telephony, is to be addressed in Phase II of this docket. Further, as non-circuit-switched connections (such as xDSL) are dedicated facilities and do not require switching, BellSouth is at a loss to understand for which elements the ALEC would seek compensation. (Tr. 612)

ISSUE 8: Should ISP-bound traffic be separated from non-ISP bound traffic for purposes of assessing any reciprocal compensation payments? If so, how?

**** Yes. Reciprocal compensation should not be paid for ISP-bound traffic, which is jurisdictionally interstate. To separate the traffic, the billing LEC should provide the billed LEC a list of ISP telephone numbers used in calculating the charges on the bill. ****

DISCUSSION

The Commission should develop a plan for separating ISP-bound traffic from non-ISP-bound regardless of whether the Commission decides to establish a specific compensation mechanism for ISP-bound traffic. For example, if the Commission reaches the conclusion that it does not have the jurisdiction to require compensation for ISP-bound traffic, there still needs to be a mechanism to separate the ISP-bound (interstate) traffic from the non-ISP-bound (local) traffic. That way, there is no risk of a LEC paying reciprocal compensation, as required under the 1996 Act for local traffic, for ISP-bound traffic.

Likewise, if the Commission establishes a compensation mechanism for the delivery of ISP-bound traffic that sets different rates for ISP-bound and non-ISP-bound traffic, there still needs to be a mechanism in place to differentiate the traffic. Only if the Commission sets an identical rate for ISP-bound and non-ISP-bound traffic would the need for a mechanism to differentiate the traffic be obviated. Therefore, the Commission should implement a mechanism to differentiate ISP-bound and non-ISP-bound traffic consistent with the mechanism currently used by BellSouth.

In September 1997, BellSouth implemented a procedure to separate ISP-bound traffic from non-ISP-bound traffic. As part of the procedure, BellSouth searches the Internet and creates a list of all telephone numbers that potentially are being used by ISPs for dial up access to the ISP. These telephone numbers are dialed to verify that the tones returned are consistent with

those used for ISP access. The verified numbers are then added to a database accessed by CABS.⁸ (Tr. 132) Updates to the database are made periodically as new information becomes available so that numbers can be added or removed as appropriate. (Tr. 133)

Each day, as CABS is processing the switch recordings used to bill usage charges for calls originating from the ALEC's end users, the ISP numbers included in the database are matched against the telephone numbers in the switch recordings. If the matching process identifies a call which is bound for one of the identified numbers it is marked as an ISP call and is treated as such in the billing system. (Tr. 132-33)

In order to more accurately populate the database, the billing LEC should be required to provide the billed LEC a list of the ISP numbers used in calculating the charges on the bill. That way, the billed company would be able to use its own switch records to verify that the appropriate charges have been calculated. (Tr. 133-34)

Sprint contends that developing a database for ISP telephone numbers is impractical and potentially violates confidentiality rights of the end-user. (Tr. 378) What Sprint fails to acknowledge is that there are several examples in the industry today where LECs report line level information and make that information accessible to other local service providers. (Tr. 136) As noted by Mr. Scollard:

The database supporting third number and calling card calling is an example that has been in place for decades. Local service providers update the database with telephone numbers authorized to be billed for such calls. As calls are placed, the toll carrier accesses the database and verifies that the call can be completed and billed. In another example, the establishment of processes to support Local Number Portability (LNP) provides for LECs serving a given ported number to report that number for inclusion in the regional LNP database. This process is an extremely important part of the overall LNP service. With the information stored

⁸ CABS is a BellSouth billing system that processes call usage records and bills the applicable rate elements to the ALEC or other interconnecting carrier based on whether the call is local, intra-LATA toll or inter-LATA. (Tr. 132)

in the database each LEC can then determine who is providing local service to the end user since the telephone number no longer provides enough information to make that determination. More recently, the Ordering and Billing Forum (OBF), the group consisting of ILECS, ALECs, IXCs and other participants responsible for developing solutions to billing issues in the telecommunications industry, has completed the requirements for a database which will house telephone numbers of end users being provided local service via an unbundled switch port. This information is needed by ILECs, ALECs and interexchange companies so that each will know who is to be billing whom for reciprocal compensation and access charges.

(*Id.*) Sprint's concerns about the disclosure of confidential end-user information are equally misplaced. As Mr. Scollard testified, "[f]irst, the database described above would not contain any end user information at all. There would be no customer name or address or any other identifying information maintained in the database. Second, as is the case with the LNP database and the newly developed UNE line-level database, the industry participants could be required to agree to use the stored information only for the intended purpose. That is, those carriers with access to the data must only use it for the purpose of creating and verifying intercarrier bills."

(Tr. 138)

There is no reason why the Commission could not require each LEC to develop a database similar to that currently used by BellSouth to identify telephone numbers serving ISPs. Because ISPs are in the better position to know which of their telephone numbers are being used to provide Internet access, the ISPs should be responsible for providing those numbers to the LEC providing the service.

ISSUE 9: Should the Commission establish compensation mechanisms for delivery of ISP-bound traffic to be used in the absence of the parties reaching an agreement or negotiating a compensation mechanism? If so, what should be the mechanisms?

**** No. The Commission lacks jurisdiction to establish such a mechanism. However, if such a mechanism is established it should be bill-and-keep and only applicable when parties cannot reach an agreement on a compensation arrangement mechanism. ****

DISCUSSION

The Parties appear to be in general agreement that if the Commission establishes an ISP-bound traffic cost recovery mechanism, that said mechanism should be used as the default mechanism only when the Parties are unable to reach an agreement through negotiations. The dispute surrounding this issue is whether the Commission should establish a compensation mechanism in the first instance and, if so, what that mechanism should be. As discussed in the previous issues, ISP-bound traffic is access service. Thus, the determination of the appropriate compensation mechanism for ISP-bound traffic is an issue to be decided by the FCC, not this Commission. If the Commission, however, decides to establish a compensation mechanism for delivery of ISP-bound traffic, said mechanism should be a bill and keep mechanism. (Tr. 613)

CONCLUSION

BellSouth respectfully submits that the Commission lacks the jurisdiction to consider the issues raised in this proceeding. Thus, the Commission should defer any action until after the FCC issues a decision on the jurisdictional nature of ISP traffic and clarifies the role of the state commissions. If the Commission is determined to proceed, however, it should implement a bill-and-keep mechanism for the exchange of ISP traffic. Such a mechanism would: (1) encourage competition across the entire Florida telecommunications market, not just the limited business Internet Service Provider niche market, and (2) eliminate the discriminatory subsidy currently being paid by BellSouth to the ALECs.

Respectfully submitted this 18th day of April 2001.

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