State of Florida

Public Service Commission

CAPITAL CIRCLE OFFICE CENTER ● 2540 SHUMARD OAK BOULEVARD
TALLAHASSEE, FLORIDA 32399-0850

-M-E-M-O-R-A-N-D-U-M-

DATE: AUGUST 8, 2002

TO: DIRECTOR, DIVISION OF THE COMMISSION CLERK & ADMINISTRATIVE SERVICES (BAYÓ)

FROM: DIVISION OF COMPETITIVE MARKETS & ENFORCEMENT (BLOOM, SIMMONS) SAS KAB
OFFICE OF GENERAL COUNSEL (BANKS, DODSON, KEATING) FRB

RE: DOCKET NO. 000075-TP - INVESTIGATION INTO APPROPRIATE METHODS TO COMPENSATE CARRIERS FOR EXCHANGE OF TRAFFIC SUBJECT TO SECTION 251 OF THE TELECOMMUNICATIONS ACT OF 1996.

AGENDA: AUGUST 20, 2002 - REGULAR AGENDA - POST-HEARING DECISION - PARTICIPATION IS LIMITED TO COMMISSIONERS AND STAFF

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\CMP\WP\000075.RCM

CASE BACKGROUND

On January 21, 2000, this docket was established to investigate the appropriate methods to compensate carriers for exchange of traffic subject to Section 251 of the Telecommunications Act of 1996 (the Act). An administrative hearing regarding issues delineated for Phase I of this docket was conducted on March 7 - 8, 2001. In accordance with Order No. PSC-00-2229-PCO-TP, issued November 22, 2000, as modified by Order No. PSC-01-0863-PCO-TP, issued April 5, 2001, post-hearing briefs were filed on April 18, 2001. Thereafter, on April 19, 2001, the Federal Communications Commission (FCC) released its decision in FCC Dockets Nos. 96-98 and 99-68 on matters regarding intercarrier compensation for telecommunications traffic to Internet Service Providers that had been remanded to the FCC for further determination by the Court of Appeals for the District of Columbia Circuit. On April 27, 2001, Order No. PSC-01-1036-PCO-TP was issued requiring all parties in this proceeding to file supplemental post-hearing briefs addressing the decision of the FCC in Dockets Nos. 96-98 and 99-68 (FCC Order) within 10 days of the issuance of the FCC's Order memorializing the April 19, 2001, decision. On that same day, the FCC Order was memorialized in Docket Nos. 96-98 and 99-68.

On May 2, 2001, AT&T Communications of the Southern States, Inc., TCG of South Florida, Global NAPS, Inc., MediaOne Florida Telecommunications, Inc., Time Warner Telecom of Florida, LP, Florida Cable Telecommunications Association, Inc., Allegiance Telecom of Florida, Inc. and the Florida Competitive Carriers Association (collectively "Joint Movants") filed a Joint Motion for Extension of Time to File Supplemental Post Hearing Brief. Order No. PSC-01-1094-PCO-TP, issued May 8, 2001, was issued granting the Joint Movants' Motion for Extension of Time.

On March 27, 2002, the parties filed a Joint Stipulation, suggesting the Commission defer action on the issues raised in Phase I of this docket. In support of this proposal, the parties stated that on April 27, 2001, the FCC issued its ruling in the case of Implementation of the Local Compensation Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98, Intercarrier Compensation for ISP-Bound Traffic, CC Docket No. 99-68, Order on Remand and Report and Order (*ISP Remand Order*), FCC 01-131. The parties asserted that the *ISP Remand Order* established certain nationally applicable rules regarding intercarrier compensation for ISP-bound traffic. Therein, the parties contended that the FCC had asserted jurisdiction over ISP-bound traffic and hence, this Commission should decline to issue a ruling on the issues in Phase I, which addresses reciprocal compensation for ISP-bound traffic. The parties asserted that although the *ISP Remand Order* is under court review, it had not been stayed and was, therefore, binding.

On May 7, 2002, the Commission issued Order No. PSC-02-0634-AS-TP, approving the Joint Stipulation, but leaving open the docket pending the resolution of issues to be addressed in Phase II of this proceeding. A hearing was conducted on July 5, 2001, concerning the Phase II issues dealing with non-ISP reciprocal compensation matters.

On December 5, 2001, the Commission held a special agenda conference to consider issues designated for resolution in Phase II of this docket (Issues 10-19). At the special agenda conference, the Commission reached decisions on Issues 10, 12, 14, 15, 16, and 18, and deferred decisions on Issues 13 and 17, and set the deferred issues for hearing. The Commission's decisions on Issues 10, 12, 14, 15, 16, 18, and 19 were not memorialized in an order pending final decisions on Issues 13 and 17, for which staff was directed to schedule a one-day hearing to gather more evidence. A prehearing conference was held April 19, 2002, on the two issues that comprise Phase IIA. At the prehearing, it was determined that testimony previously filed in Phase II of this proceeding would be refiled for informational purposes, and the witnesses sponsoring testimony for Phase II would not be susceptible to cross-examination. A hearing was conducted on May 8, 2002. To avoid potential confusion that may result from duplicative page references, transcript citations using Phase II testimony in the recommendation are prefaced with the initials "TR." Testimony in Phase IIA, filed specifically to address issues for which the Commission sought further discussion by the parties, is prefaced by the letters "TRa."

This recommendation deals with Issue 13, the definition of a local calling area, and Issue 17, a default compensation mechanism for traffic subject to Section 251 of the Act.

DISCUSSION OF ISSUES

ISSUE 13: How should a "local calling area" be defined, for purposes of determining the applicability of reciprocal compensation?

a) What is the Commission's jurisdiction in this matter?

b) Should the Commission establish a default definition of local calling area for the purpose of intercarrier compensation, to apply in the event parties cannot reach a negotiated agreement?

c) If so, should the default definition of a local calling area for purposes of intercarrier compensation be: 1) LATA-wide local calling, 2)based upon the originating carrier's retail local calling area, or 3) some other default definition/mechanism?

PRIMARY RECOMMENDATION: The local calling area should be defined through negotiations between the parties. While staff believes the Commission has jurisdiction to define local calling areas, staff does not believe a compelling case can be made to exercise the Commission's jurisdiction to designate a default in the event negotiations are unproductive. **(BLOOM, KEATING)**

ALTERNATIVE RECOMMENDATION: Alternative staff believes that the Commission has jurisdiction to define local calling areas, and recommends that the originating carrier's retail local calling area be used as the default local calling area for purposes of reciprocal compensation. **(SIMMONS, BANKS)**

POSITIONS OF THE PARTIES:

ALLTEL:

a) No. The Commission does not have authority in Florida to expand the ILEC's "local calling areas" for the purpose of determining the applicability of reciprocal compensation.

b) No. Interconnecting companies do not have the authority in Florida to negotiate away or expand the ILEC's "local calling areas" for the purpose of determining the applicability of reciprocal compensation.

c) The local calling area should be defined as the retail local calling area of the ILEC for the purposes of reciprocal compensation.

<u>BELLSOUTH:</u>

a) The Commission has jurisdiction under the FCC's Local Competition First Report and Order to determine geographic areas for reciprocal compensation purposes. However, whatever geographic area the Commission establishes must not conflict with Florida law.

b) No. Based on BellSouth's experience, a default definition of local calling area for the purposes of reciprocal compensation is not necessary because this issue has not been highly contested or arbitrated.

c) The Commission should adopt as the default definition the originating party's local calling area, if it finds that such a proposal is administratively manageable. If the Commission determines that the originating party's local calling area is not manageable, then the default definition should be the ILEC's local calling area.

<u>SPRINT:</u> Pursuant to the authority delegated by the FCC, the Commission should establish a default local calling area consistent with the Commission's authority under Florida law. The ILEC's tariffed local calling scope should define the appropriate local calling scope for reciprocal compensation purposes for wireline carriers.

<u>VERIZON:</u>

a) The Commission cannot define the entire LATA as the local calling area for reciprocal compensation purposes, because it lacks the authority to modify access charges and because it would violate the state and federal requirements for all carriers to contribute their fair share for universal service support.

b) Negotiation should continue to be the primary means of defining the local calling area for reciprocal compensation purposes. Adoption of a default approach in the event negotiations prove unsuccessful will be beneficial only if the Commission makes clear that the default is the ILEC's tariffed local calling area.

c) If the Commission adopts a default local calling area definition, it should be the ILEC's tariffed local calling areas. This is the only approach that is lawful, competitively neutral and consistent with universal service objectives.

AT&T: a) The Commission has jurisdiction to define its local calling area for determining the applicability of reciprocal compensation pursuant to Section 251(b)(5) of the Act, and the Florida Supreme Court ruling in Florida Interexchange Carriers v. Beard, 624 So.2d 248 (Fla. 1993)

b) Yes. The Commission should establish a default definition of local calling area for the purpose of intercarrier compensation in the event the parties cannot reach a negotiated agreement.

c) The default definition of local calling for purposes of intercarrier compensation should be LATA-wide calling.

FCTA/TIME WARNER:

Restructuring local calling zones can be addressed independently in this proceeding for intercarrier compensation purposes, and any adverse impact on universal service is speculative and can be addressed in a separate proceeding.

FDN: The FCC directed states to determine if reciprocal compensation or access applies for traffic exchanged between LECs whose local service areas are not the same. The Florida Statutes direct the Commission to establish fair, reasonable and nondiscriminatory interconnection terms and to exercise its exclusive jurisdiction to encourage and promote competition.

US LEC:

a) Sections 251 and 252 of the Act grant the Commission jurisdiction to define a "local calling area" for the purposes of determining the applicability of reciprocal compensation.

b) In the event parties cannot reach a negotiated agreement, the Commission should establish a default definition of local calling area for the purpose of intercarrier compensation.

c) LATA-wide local calling should be the default definition of local calling area for purposes of intercarrier compensation.

PARTIES' ARGUMENTS:

Commission jurisdiction

On the issue before the Commission of how local calling areas should be defined for determining the applicability of reciprocal compensation, the ALEC parties believe the Commission has explicit authority to make such decisions while ILEC parties offer differing responses.

In its brief, AT&T contends the FCC gave state commissions express authority to define local calling areas in its 1996 Local Competition Order (In the Matter of Implementation of the Local Competition Act of 1996, Order FCC 96-325) at ¶1035, which reads in part:

> With the exception of traffic to or from a CMRS network, state commissions have the authority to determine what geographic areas should be considered "local areas" for the purpose of applying reciprocal compensation obligations under Section 251(b)(5), consistent with the

> state commissions' historical practice of defining local service areas for wireline LECs. Traffic originating or terminating outside of the applicable local area would be subject to interstate and intrastate access charges. We expect the states to determine whether intrastate transport and termination of traffic between competing LECs, where a portion of their local service areas are not the same, should be governed by Section 251(b)(5)'s reciprocal compensation obligations or whether intrastate access charges should apply to the portions of their local service areas that are different. (AT&T BR at 3)

AT&T also believes the Florida Supreme Court determined the Commission has statutory authority to determine local calling areas based on its ruling in Florida Interexchange Carriers v. Beard, 624 So.2d 248, 251 (Fla. 1993), when it ruled, "The exclusive jurisdiction in section 364.01 to regulate telecommunications gives the [Florida Public Service] Commission the authority to determine local routes." (AT&T BR at 3)

In its brief, FDN asserts the Commission has jurisdiction to determine local calling areas based on FCC 96-325, ¶1035, (FDN BR at 3), as does US LEC (US LEC BR at 3)

Among the ILECs, there appear to be diverse views on whether the Commission has authority to define local calling areas for reciprocal compensation purposes. ALLTEL does not believe the Commission has jurisdiction (ALLTEL BR at 2); BellSouth believes the Commission has some latitude, providing that the Commission's decision does not conflict with Section 364.16(3)(a), Florida Statutes (BST BR at 4); Sprint appears to agree the Commission has jurisdiction to determine local calling areas consistent with appropriate state laws but believes the applicable state law is very limiting (Sprint BR at 4); and while Verizon's brief does not address directly the issue of jurisdiction for defining local calling areas, Verizon apparently believes the Commission cannot define an entire LATA as a local calling area. (Verizon BR at 4)

ALLTEL appears to rely on Section 364.16(3)(a), Florida Statutes, arguing this section precludes the Commission from defining a LATA as a default local calling area. The specific language referred to by ALLTEL in its brief reads, "No local exchange telecommunications company or alternative local exchange telecommunications company shall knowingly deliver traffic, for which terminating access service charges would otherwise apply, through a local interconnection arrangement without paying the appropriate charges for such terminating access service." (ALLTEL BR at 5) ALLTEL reasons this language prohibits the Commission from determining that all calls within a LATA may be considered local. ALLTEL subsequently argues the Commission "should reject efforts to establish the LATAs in Florida as the default 'local calling area' for reciprocal compensation purposes." (ALLTEL BR at 5)

ALLTEL also appears to rely on the testimony of BellSouth witness Shiroishi and Verizon witness Trimble to argue the use of a LATA as a local calling area would reduce ILEC revenues. (ALLTEL BR at 3-4) Witnesses Shiroishi and Trimble postulate that if all calls in a LATA were considered local, ILECs, as carriers of last resort, would experience a reduction in revenues because access charges would be replaced by reciprocal compensation payments. These revenue reductions would potentially undermine the state's implicit support for universal service (TRa 38; TRa 100-101) because it would leave the ILECs with no means of recovering the revenue losses. (ALLTEL BR at 4) ALLTEL witness Busbee testifies the net financial loss to ALLTEL if exchange access was redefined as reciprocal compensation would be $700,000. (TR 209)

In its brief, ALLTEL states, there are two reasons why it would lose money if intrastate intraLATA toll exchange routes were converted to reciprocal compensation: "First, the current price regulation system in Florida limits the ability of the Commission to grant a local rate increase. To the best of ALLTEL's knowledge, only one company (TDS/Quincy Telephone) has requested a local rate increase under the 'changed circumstances' provisions in Section 364.051(4); however, that effort was voluntarily dismissed." ALLTEL continues, "Second, to the best of ALLTEL's knowledge, no Florida ILEC has ever petitioned the FPSC to establish an explicit interim universal service mechanism." (ALLTEL BR at 4) ALLTEL does not offer an interpretation of the Commission's jurisdiction to determine local calling areas based on FCC 96-325, ¶1035.

BellSouth appears to believe the Commission can define a default local calling area for the purpose of reciprocal compensation, but the Commission is required by the FCC to do so consistent with this Commission's historical practice of defining local service areas for wireline local exchange companies. Similar to ALLTEL, BellSouth argues a default local calling area established by this Commission cannot conflict with Section 364.16(3)(a), Florida Statutes. (BST BR at 4)

In this context, BellSouth argues, the Commission ruled in a 1997 case (Petition for Arbitration of Dispute with BellSouth Telecommunications, Inc. Regarding Call Forwarding, by Telenet of South Florida, Inc., Order No. PSC-97-0462-FOF-TP) that while an ALEC may have a retail local calling area different from that of an ILEC, the ALEC must pay applicable access charges pursuant to Section 364.16(3)(a). (BST BR at 4)

BellSouth also argues that a change in local calling areas that reduces access revenues is tantamount to an implicit reduction in access rates, something BellSouth argues the Commission is barred from implementing under Section 364.163, Florida Statutes. (BST BR at 5)

Sprint also argues that the provisions of Section 364.163, Florida Statutes, prohibit the Commission from reducing access rates, and "The expansion of the local calling scope for reciprocal compensation purposes affects access charge rates in a manner not contemplated by the statute." (Sprint BR at 5-6) In addition, Sprint contends Section 364.02, Florida Statutes, which defines basic local telecommunications service, recognizes local calling areas of ILECs in the way the local calling areas existed on the date the ILEC elected price regulation. (Sprint BR at 4)

Verizon does not address directly the issue of the Commission's jurisdiction to define local calling areas, arguing instead that the Commission cannot define a LATA as a local calling area because it lacks the authority to modify access charges and because such a decision would violate federal and state requirements that all carriers contribute to universal service support. (Verizon BR at 4)

In its brief, FDN contends dependence on Section 364.163, Florida Statutes, in this proceeding is misplaced. "The Commission will not find anywhere in Section 364.163 or all of Chapter 364 a provision that either specifically or by implication preserves all in-LATA calls to the access regime rather than reciprocal compensation. Section 364.163 does not address the preservation of access revenues or revenue sources or the preservation of any calling areas or call routes to the access regime." (FDN BR at 5)

Similarly, FDN's brief dismisses ILEC concerns that Section 364.16(3)(a) precludes the Commission from considering a LATA as a default local calling area. "The plain meaning of 364.16(3)(a) is to prohibit any LEC from knowingly disguising access traffic as local, such as by stripping off call identifying information and/or by routing interLATA traffic over local trunks. This section does not provide that ILEC local calling areas control intercarrier payment schemes; and no misapplied rules of statutory construction can contort it enough to make it so provide." (FDN BR at 7)

Should the Commission adopt a default?

On the issue of whether the Commission should establish a default local calling area in the event parties to a negotiation are unable to reach agreement, the parties offer divergent views.

BellSouth witness Shiroishi testifies establishing a default is not necessary:

> It has not been BellSouth's experience that this issue is one that requires the Commission to establish a default definition. While many other issues surrounding intercarrier compensation (e.g., whether or not reciprocal compensation is owed for ISP-bound traffic, payment for transport when calls are transported outside of the local calling area, how virtual NXX traffic should be compensated, etc.) have been highly contested and arbitrated, this specific issue has not. BellSouth has entered into interconnection agreements that address this issue in a variety of ways.

Witness Shiroishi believes the best means of addressing the issue of which party's local calling area governs is to evaluate the traffic patterns of each party and to develop terms and conditions amenable to both through negotiation. (TRa 21)

Witness Shiroishi testifies current agreements between BellSouth and ALECs allow the competitors to establish their own local calling areas for retail purposes. Once the ALEC's local calling area is established for retail purposes, witness Shiroishi asserts, "The parties then agree upon and put in the interconnection agreement, how they will determine what is 'local' for intercarrier compensation purposes." (TRa 24)

AT&T witness Cain espouses a different view than BellSouth witness Shiroishi on the need for the Commission to establish a default local calling area. "Although the Commission should continue to encourage negotiation, the Commission also should establish a policy that requires a LATA-wide local calling area for intercarrier compensation purposes if the parties cannot reach agreement by negotiation. The Commission should not define local calling areas for retail purposes nor should it establish local calling areas based on current ILEC practices, which would force ALECs to mirror ILEC local calling areas. Competition cannot thrive if the monopoly incumbents control the marketplace in this manner." (TRa 215)

In its brief, Sprint states that while private negotiations are the preferred method of arriving at a definition of local calling areas, "unlike BellSouth, Sprint has found the issue of the appropriate local calling scope applicable to reciprocal compensation to be a contentious issue in its interconnection agreement negotiations." For this reason, Sprint advocates adoption of a default by the Commission to "facilitate resolution of interconnection negotiations between the parties." (Sprint BR at 3)

Verizon states in its brief that negotiation should be the primary means of defining local calling areas, but if negotiations fail, the ILEC's tariffed local calling areas should be the default. (Verizon BR at 4)

FDN witness McCluskey, whose testimony was subsequently adopted by FDN witness Warren, testifies the Commission should consider adoption of a "reasonable default mechanism" to promote efficiencies in negotiations, administration, and arbitration of interconnection agreements. (TRa 264)

In its brief, FDN argues that adoption of a default that is fair and reasonable for both parties is a goal that may not be achievable, given the disparate interests of the parties. For that reason, FDN asserts in its brief, "the pivotal factor that should influence the Commission when setting a default is the Commission's regulatory goals. The default definition of local calling area for the instant purposes should therefore achieve the goals the Commission is charged by the Legislature with achieving. Promoting competition is the goal that must take precedence . . ." (FDN BR at 8-9)

AT&T advocates the adoption of a default local calling area in its brief, stating, "A default definition of local calling area would serve the dual purpose of assisting carriers in negotiating their local calling area in their agreements as the carriers would know the parameters of the default mechanism, and would result in a consistent statewide default definition of a local calling for the purpose of intercarrier compensation." (AT&T BR at 4)

<u>What form should a default local calling area assume, if adopted?</u>

The question of what the default should be if the Commission chooses to establish one, elicits differing answers from the ILECs and two distinct proposals from the ALEC witnesses.

ALLTEL witness Busbee testifies the local calling area should be defined as the retail local calling area of the ILEC for reciprocal compensation purposes. (TRa 207) In support of this belief, witness Busbee cites local service guidelines developed by the Public Utility Commission of Ohio (Case No. 95-845-TP-COI, p.27), which use the incumbent's local calling area, including extended area service (EAS) routes, as the "demarcation for the differentiating local and toll call types for the purpose of traffic termination compensation." (TRa 207) The same guidelines are cited by BellSouth. (BST BR at 7)

BellSouth argues in its brief that if a default is deemed prudent, the originating party's local calling area should serve as the default definition if the Commission determines this proposal is administratively manageable. If, however, the Commission finds using the originating party's local calling area as a default is not viable from an administrative perspective, the default should be the ILEC's local calling area. (BST BR at 6)

BellSouth witness Shiroishi testifies a default local calling area is unnecessary because an ALEC can define its own local calling area for retail purposes, obviating the need for a regulatory solution. "Today, all of BellSouth's interconnection agreements with ALECs allow the ALEC to set its own local calling area for retail purposes. The Parties then agree upon, and put in the interconnection agreement, how they will determine what is 'local' for intercarrier compensation purposes." The determination of what traffic is or is not local is accomplished through billing factors, according to witness Shiroishi. (TRa 24)

Verizon witness Trimble argues the use of an originating party's local calling area is not feasible:

> A simple example will prove the unacceptable nature of this proposal. Tampa and Sarasota are not in the same Commission-approved Verizon local calling area. But under the originating carrier scenario, they could be in the same local calling area of an ALEC. In that situation, when a Verizon Tampa subscriber calls an ALEC's Sarasota subscriber, Verizon would be required to pay the ALEC access to terminate the call. However, under this hypothetical situation, when an ALEC costumer in Sarasota calls a Verizon customer in Tampa, the ALEC avoids paying Verizon's terminating access charges and instead pays only the lower reciprocal compensation rate. Thus, for identical calls between Tampa and Sarasota, the ALEC would collect a higher rate for calls from Verizon customers, but pay a lower rate for calls originated by its customers. The inequity of basing intercarrier compensation on the originating carrier's local calling area is obvious. (TRa 98)

Witness Trimble advocates adoption of the ILEC's local calling areas as a default local calling area.

Sprint witness Ward concurs with Verizon witness Trimble that using an originating caller's local calling area results in inequities in compensatory schemes among carriers. Witness Ward testifies, "It is critical to recognize the inequitable competitive environment that is created when the originating carrier's local calling area determines the intercarrier compensation between carriers. The result of this approach would allow ALECs to pay lower reciprocal compensation rates for their traffic terminated within the LATA by ILECs (assuming the ALEC defines the LATA as the local calling area for retail purposes) while ILECs are forced to change their LCAs or to pay ALECs higher access rates for terminating ILEC-originated traffic." (TRa 184-185)

Sprint's preferred solution is to adopt the local calling areas of the incumbent as the default for reciprocal compensation purposes. In its brief, Sprint argues that using an entire LATA as a local calling area would discriminate against IXCs, which would pay access rates to complete calls, which are higher than the reciprocal compensation rates ALECs would pay to complete calls.

In addition, Sprint contends, it would experience economic hardship if an originating carrier's local calling area is used because it would be forced to reconfigure its billing system to recognize the differing rate structures applicable to individual companies. (Sprint BR at 15) Sprint witness Ward estimates the conversion of intrastate, intraLATA access charges to reciprocal compensation would cost the company $14 million. (EXH 10, Attachment 1)

AT&T witness Cain evinces little sympathy for Sprint's claims of disparate treatment and financial losses, which he believes would affect all carriers:

> ILECs and ALECs are affected the same way: both sacrifice switched access revenue in exchange for lower costs of traffic termination. Each is free to respond to this change in its revenue/cost structure as it sees fit (e.g., reduced rates to customers, calling plans that are easier to understand, etc.). On the other hand, IXCs that are not in the local telecommunications business might indeed face erosion in their competitive position. That erosion can be traced to its source in the irrational layers of non-cost-based prices that pervade intercarrier compensation . . . . Furthermore, to the extent that ALECs and ILECs reach LATA-wide local reciprocal compensation agreements, that erosion is likely to happen regardless of the Commission's action in this proceeding. (TRa 234)

The use of the existing ILEC local calling areas avoids disparate rate structures, expenses, is competitively neutral and preserves the existing implicit mechanism for supporting universal service obligations, according to Sprint. For these reasons, Sprint recommends using the ILEC local calling areas as a default for reciprocal compensation purposes. (Sprint BR at 16)

Sprint witness Ward references a 1999 decision by the Public Utilities Commission of Nevada (Order Adopting Revised Arbitration Decision, April 12, 1999, Docket No. 98-10015) between Nevada Bell and Advanced Telecom Group. Witness Ward testifies the result of the Nevada commission's decision was to establish that reciprocal compensation obligations apply to traffic that originates and terminates within a Nevada Bell local calling area. "Thus, the Nevada Commission has determined that the ILEC's local calling area is the basis for determining whether reciprocal compensation is due or not." (TRa 176)

Witness Ward also cites a decision by the Texas Public Utilities Commission (Proceeding to Examine Reciprocal Compensation Pursuant to Section 252 of the Federal Telecommunications Act of 1996, Docket No. 21982) in which the commission "reaffirms its previous determination that reciprocal compensation arrangements apply to calls that originate from and terminate to an end-user within a mandatory single or multi-exchange local calling area . . ." in support of using the ILEC's local calling areas. (TRa 176)

Verizon witness Trimble believes "The only rational way to define local calling area for reciprocal compensation purposes is by reference to the ILEC's tariffed local calling areas." (TRa 142) In the event the Commission elects to create a default option, witness Trimble testifies, the Commission should consider four criteria to guide its deliberations: (1) competitive neutrality; (2) avoid undermining the advancement and preservation of universal service; (3) be administratively easy to implement; and (4) focus on the end user. (TRa 88)

Because of the economic disparities that would result from having the originating caller's network be the basis for intercarrier compensation, witness Trimble testifies, this approach cannot be considered competitively neutral. (TRa 98) Similarly, witness Trimble argues, use of a LATA-wide calling regime for reciprocal compensation disadvantages IXCs because it would apply different compensation rules to the same type of call. (TRa 91)

Verizon witness Trimble testifies LATA-wide calling for reciprocal compensation purposes is intrinsically biased toward ALECs to the disadvantage of ILECs and interexchange carriers (IXCs). "Under the LATA-wide approach, all intraLATA calls handled jointly by ALECs and ILECs would be termed 'local' and subject to reciprocal compensation. But, an intraLATA call that involves an IXC would still be subject to access compensation rules. The ILECs would, likewise, be subject to access compensation rules when they handle toll calls for their presubscribed customers because Florida law requires them to impute access costs into their intraLATA toll rates. Applying different intercarrier compensation rules to the same type of calls could give the ALECs a significant, artificial competitive advantage in pricing their intraLATA calls (regardless of whether they call them local calls or toll calls) versus pricing based on the cost structures that the IXC and the ILEC (through imputation) face." (TRa 91-92)

Witness Trimble asserts that using LATA-wide calling as a default would diminish revenues available to support universal service. Witness Trimble's premise is that basic local residential rates are subsidized by revenues from other services, such as access charges. Use of the LATA as a local calling area for wholesale purposes will reduce revenues gleaned from access charges, which would reduce the subsidy flows for basic local rates. (TRa 90)

Witness Trimble testifies "There is no explicit universal service fund in Florida, so all state support for universal service is generated implicitly within the ILEC's rate structures - whether through switched access, toll, or other rate elements. Paying reciprocal compensation rates for what have always been designated as access traffic allows the ALECs to take implicit universal service support flows out of the system - contrary to Congress' expressed intention for all carriers to equitably contribute to preservation and advancement of universal service." (TRa 101-102)

Witness Trimble acknowledges, however, that Section 364.051(4), Florida Statutes, allows a carrier to petition the Commission for an increase in basic local service rates if it experiences an unforeseen decrease in revenues. (TRa 148)

Quantifying the financial impact of a decision to use a LATA as a default for reciprocal compensation is complicated, according to witness Trimble, "because the answer requires several assumptions about what unintended future consequences will follow from a change in determining how intercarrier compensation is assessed." (TRa 107) In response to a staff discovery request, Verizon witness Trimble provided a proprietary estimate of potential revenue losses of converting intraLATA traffic to reciprocal compensation. (EXH 15)

Witness Trimble speculates end users may not benefit from a LATA-wide local calling area for reciprocal compensation purposes. "In fact, ALECs excused from paying access charges could well pocket the money they save and continue to assess toll charges to their end users." (TRa 133-34)

In its brief, Verizon asserts a number of states have considered and rejected the concept of applying reciprocal compensation for calls that do not originate and terminate in the ILEC local calling area. These states include Connecticut (DPUC Investigation of the Payment of Mutual Compensation for Local Calls Carried Over Foreign Exchange Service, Docket No. 01-01-29); Illinois (TDS Metrocom, Inc., Petition for Arbitration of Interconnection Rates, Terms, and Conditions and Related Arrangements with Illinois Bell Telephone Co., Docket No. 01-0338); the previously referenced Texas PUC decision; South Carolina (Petition of Adelphia Business Solutions of South Carolina, Inc., for Arbitration of an Interconnection Agreement with BellSouth Telecommunications, Inc., Docket No. 2000-516-C); Tennessee (Petition for Arbitration of the Interconnection Agreement with BellSouth Telecommunications, Inc. and Intermedia Communications, Inc., Docket No. 99-00948); Georgia (Generic Proceeding of Point of Interconnection and Virtual FX Issues, Docket No. 13542-U); and Missouri (Application of AT&T Communications of the Southwest, Inc., TCG St. Louis, Inc., and TCG Kansas City, Inc., for Compulsory Arbitration of Unresolved Issues with Southwestern Bell Telephone Company, Case No. TO-2001-455). (Verizon BR at 29)

AT&T witness Cain argues, however, that compelling ALECs to base compensation on the ILECs' local calling areas ignores two problems:

> Adoption of the incumbent local exchange carrier's local calling area suffers from two afflictions. First, it would preserve and perpetuate the complexities plaguing the industry. The ILEC's local calling area is yet another artificial boundary that few outside of this proceeding understand. Second, as a default, it would hold ALECs and consumers hostage to the calling plans of the incumbent local exchange carrier. Although it is true that ALECs are free to define their own retail local calling areas, that freedom is constrained by the costs the ALEC must incur. One of those costs is intercarrier compensation. If the ALEC must pay the ILEC switched access for some calls within the LATA, and reciprocal compensation for others, the ALEC's LATA-wide local calling areas will turn out to be either unprofitable or uncompetitive, or both. (TRa 229)

The unprofitability would result because the rates for switched access generally exceed rates for reciprocal compensation, witness Cain testifies, meaning ALECs would have a difficult time competing against ILECs. This leaves an ALEC with an alternative of duplicating the ILEC's local calling areas, which he believes means fewer consumer choices. (TRa 230)

If the Commission adopts LATA-wide calling as a default, witness Cain asserts, "the Commission will be taking a small but significant step towards eliminating an anticompetitive environment for ALECs. Florida consumers will benefit from the Commission's move towards simplifying intercarrier compensation and eliminating a layer of confusion." (TRa 230)

Witness Cain believes establishing a LATA-wide calling area for reciprocal compensation offers the benefits of administrative ease and enhanced competition:

> A LATA-wide calling area would simplify retail call rating as well as intercarrier billing of reciprocal compensation. All intraLATA calls would be treated the same for reciprocal compensation purposes, with each minute billed the same way. Additionally, a clear "fallback" policy statement while encouraging negotiation also would tend to reduce the number of issues that must be arbitrated.
>
> Establishing the LATA as the calling area also will enhance competition by allowing ALECs to offer their customers local calling arrangements that may vary from those offered by the ILEC. Establishing the current ILEC calling areas as the default, on the other hand, will force ALECs to mirror those areas, to the detriment of competition. (TRa 218)

Witness Cain testifies LATA-wide calling will result in compensation among carriers that is simple and fair. "Every minute is compensated based on the same rate when the call originates and terminates within the same LATA. A LATA-wide local calling area results in the elimination of intraLATA toll charges for various paths that a call takes and eliminates the need to input different rates for those calls. Instead, a call is rated the same no matter what dialing pattern is used and is more easily managed in billing systems." (TRa 219-220)

In its brief, AT&T contends continued dependence on the ILEC's retail local calling area disadvantages ALECs, thereby stifling an ALEC's ability to compete with an ILEC. (AT&T BR at 7) "If the Commission were to adopt the ILEC's position, ALECs would not be able to offer their customers local calling areas other than the ILEC's without paying the ILEC the artificially high originating switched access charges" for calls that an ALEC terminates in the ALEC's extended local calling area. The end result, according to AT&T's brief, is that, "Such a compensation regime would stifle competition and increase the ILEC's formidable competitive advantages." (AT&T BR at 7)

Witness Cain dismisses Verizon witness Trimble's arguments regarding threats to universal service funding as "tired." (TRa 231) Witness Cain testifies:

> When an ILEC such as Verizon elected price regulation, it gave up the right to a guaranteed level of revenue. One hopes that they understood that at the time. Furthermore, in the years leading up to the 1996 Telecommunications Act, and ever since, enlightened universal service policy has been based on the fundamental premise that subsidies should be explicit, not hidden in the prices carriers or customers pay for their services. That certainly seems to be the premise underlying Section 364.025 of the Florida statutes. The statute provides Verizon, BellSouth and Sprint the opportunity to ask the PSC for explicit universal service support. It is my understanding that no ILEC has done so. (TRa 231-232)

Witness Cain is also critical of Verizon witness Trimble and Sprint witness Ward's assertions that adoption of a LATA-wide local calling area lacks competitive neutrality because it disadvantages ILECs and IXCs. "ILECs and ALECs are affected the same way: both sacrifice access revenue in exchange for lower costs of traffic termination. Each is free to respond to this change in its revenue/cost structure as it sees fit (e.g., reduced rates to customers, calling plans that are easier to understand, etc.)." (TRa 234) Witness Cain concedes IXCs may see some erosion of their competitive position as a result of LATA-wide local calling areas, but he testifies this would be attributable to "irrational layers of non-cost-based prices that pervade intercarrier compensation." (TRa 234)

Overall, witness Cain testifies, the reduction in costs that would result from LATA-wide local calling would give carriers greater flexibility to respond to consumer demand, which he believes fosters greater competition. (TRa 235)

FDN witness Warren offers a variation on the use of the LATA as a default local calling area. FDN proposes the default local calling area be the LATA when the originating carrier hands off LATA-wide calls at the ILEC tandem serving the geographic location of the end user, or, if the call originator chooses, at the end office serving the call recipient. (TRa 264)

Witness Warren testifies FDN believes local calling areas create artificial pricing boundaries and should be rejected for intercarrier purposes. "The cost for intrastate access in Florida is prohibitively high, so the cost to the originating carrier for terminating access calls precludes the originating carrier from lowering retail prices for all intraLATA calls." (TRa 264) If, however, the originating caller's carrier agrees to deliver the call either to the tandem or the end office serving the call recipient, the effect would "minimize controversy over cost and call routing and delivery issues compared to other plans" and promote facilities-based and intraLATA retail price competition. (TRa 265)

BellSouth witness Shiroishi criticizes FDN's proposal as "vague" and non-compliant with FCC rules. "The FCC has long held that the jurisdiction of a call is determined by the end points of such call." Even if the FDN proposal were compliant with FCC rules, witness Shiroishi testifies, she remains skeptical that any billing system could determine the appropriate rate (access or reciprocal compensation)for a call, based on the point at which a call arrives at a tandem switch or an end office. (TRa 34)

Witness Shiroishi is also critical of Level 3 witness Gates' recommendation that a local calling area be determined by comparing the NXX codes of the calling number and the called number. (TR 766) Witness Shiroishi points out that the Commission rejected this methodology of determining compensation for virtual NXX/foreign exchange traffic at the December 5, 2001, Agenda Conference on Issue 15 of this docket. (TRa 33)

PRIMARY STAFF ANALYSIS:

Jurisdiction

Staff believes that the Commission is authorized to address this issue by Sections 364.01(4)(b), 364.01(4)(g), and 364.01(4)(i), Florida Statutes, whereby the Commission is directed to:

> (b) Encourage competition through the flexible regulatory treatment among providers of telecommunications services in order to ensure the availability of the widest possible range of consumer choice in the provision of all telecommunications services.
>
> (g) Ensure that all providers of telecommunications services are treated fairly, by preventing anticompetitive behavior and eliminating unnecessary regulatory restraint.
>
> (i) Continue its historical role as a surrogate for competition for monopoly services provided by local exchange telecommunications companies.

In particular, staff believes that subsection (b), as set forth above, is pertinent in view of the arguments that the definition of what the local calling scope should be for purposes of intercarrier compensation will directly impact "the availability of the widest possible range of consumer choice" in the provision of basic local telecommunications services by ALECs.

As argued by AT&T, staff believes that this interpretation is supported by the Florida Supreme Court's decision in Florida Interexchange Carriers v. Beard, 624 So.2d 248, 251 (Fla. 1993), wherein the Court stated that, "The exclusive jurisdiction in section 364.01 to regulate telecommunications gives the Commission the authority to determine local routes." Staff acknowledges that this decision was prior to the 1995 changes to Chapter 364. Nevertheless, staff believes that the general grants of authority set forth in Section 364.01 authorize the Commission to address the specific issue presented in this case in the same manner as those provisions interpreted by the Court in the Florida Interexchange Carriers v. Beard case.

Staff also acknowledges that this authority is not limitless, and that Sections 364.16(3)(a), Florida Statutes, and 364.163, Florida Statutes, restrict the Commission's authority in the area of access charges. However, as argued by FDN, neither of these provisions address the issue of actually defining the local calling scope. These provisions only address the Commission's authority with regard to access charges once the local calling scope has been defined.

Furthermore, as a matter of statutory construction, one should always begin by looking at the plain language of the statutes. In this instance, staff believes that Section 364.01, Florida Statutes, is clear in authorizing the Commission to act with regard to this issue.[1] However, even if it is determined that the statutory provisions at issue are less than clear, staff believes that applying standard rules of statutory construction results in the same conclusion that the Commission is authorized to act with regard to defining the local calling area for purposes of intercarrier compensation. Specifically, when interpreting a statutory provision(s) that is not clear, one should always attempt to read provisions in a manner that would not create conflict between competing provisions, or such that conflicting statutes are construed to give both statutes an area of operation. City of Punta Gorda v. McSmith, Inc., 294 So.2d 27 (Fla. 2d DCA 1974). See also Order No. PSC-99-0744-FOF-EI, issued April 19, 1999, in Docket No. 980693-EI. In this instance, staff believes Sections 364.01(4)(b), (g) and (i) and Sections 364.163 and 364.16(3)(a), Florida Statutes, can and should be read in a manner that does not conflict and gives each statutory provision an area of operation. The provisions of Section 364.01, Florida Statutes, should be read to authorize the Commission to act to define the local calling area where necessary to ensure the widest range of consumer choice and to eliminate barriers to competition, but once that calling area is defined, the Commission's authority is limited by the specific statutory provisions applicable to access charges, Section 364.163, and Section 364.16(3)(a), Florida Statutes. To date, the local calling area for purposes of intercarrier compensation has not been

[1] "When the language of a statute is unambiguous and conveys a clear and ordinary meaning, there is no need to resort to other rules of statutory construction; the plain language of the statute must be given effect." Starr Tyme, Inc. v. Cohen, 659 So.2d 1064, 1067 (Fla. 1995). If it is determined that the statute on its face is ambiguous or unclear, then one would resort to the other rules of statutory construction. See Id. "Only when a statute is doubtful in meaning should matters extrinsic to the statute be considered in construing the language employed by the Legislature." Capers v. State, 678 So.2d 330, 332 (Fla. 1996). See Order No. PSC-02-1265-PCO-WS.

defined, which is why the issue is now before the Commission in this case. Therefore, staff believes that the Commission may act to address the issue before it.

In addition, it appears the ILEC parties are failing to distinguish between access rates and access revenues. It is clear from the plain language of Section 364.163, Florida Statutes, that the Legislature has reserved for itself the authority to determine access charge rates. What is not clear from the ILECs' briefs is how Section 364.163 governs access charge revenues. Staff does not believe a decision by this Commission to establish LATAs as a default local calling area translates into rate-setting. While the parties appear to agree that using LATAs as default local calling areas would reduce access charge revenues, revenues and rates are distinct entities in intercarrier compensation schemes and under the law.

BellSouth cites a Commission decision in the Telenet order (Order No. PSC-97-0462-FOF-TP) that upheld the proposition that an ALEC with a retail local calling area different than that of the ILEC's retail must pay access charges pursuant to Section 364.16(3)(a), Florida Statutes. Staff notes, however, the Telenet order was issued in 1997 on an issue involving call forwarding. Given that the Telenet order addressed a specific issue in an arbitration proceeding, staff appreciates its conclusions but does not believe that decision has precedential value in the instant proceeding.

Furthermore, FCC 96-325, ¶1035 appears unequivocal in granting authority to state commissions to determine what geographic areas should be considered "local areas" for the purpose of applying reciprocal compensation obligations under Section 251(b)(5) of the Act. ILEC parties offer nothing to dispute what appears to be a clear delegation of authority from the FCC to state commissions to make determinations as to the geographic parameters of a local calling area.

In summary, staff does not believe any party to this proceeding has provided evidence or testimony based in fact or law that would prohibit this Commission from defining a local calling area - including defining a LATA as a local calling area - for purposes of reciprocal compensation.

Adoption of a default

All the parties express the view that negotiations are the preferred method of dispute resolution. A number of parties, however, advocate adoption of a default in the event negotiations are unfruitful.

BellSouth witness Shiroishi testifies the issue of defining local calling areas for interconnection agreements has not been contentious and need not be addressed by the Commission (TRa 21). BellSouth's brief emphasizes that its experience in negotiating agreements with ALECs does not compel a need to adopt a default at this time. (BST BR at 6)

Sprint asserts in its brief that the Commission should establish a default because the issue of local calling scope has proven "contentious" in its negotiations with ALECs. (Sprint, BR at 3) Verizon espouses the view that if the Commission adopts a default, the default should be the ILEC's retail calling area. (Verizon BR at 4) Both FDN and AT&T advocate the adoption of a default, although their proposed solutions differ from those of the ILECs and from each other.

Other than stating preferences, the parties devote little testimony or argument to the issue of whether the Commission should adopt a default, directing their energies instead to what the default should be in the event the Commission elects to establish a default. It appears from the testimony and the briefs that those parties advocating a default do so to create a definitive endpoint to unsuccessful negotiations.

It would appear that the perceived need for a default local calling area is contingent on the extent to which the Commission believes such a default is necessary or desirable. AT&T witness Cain (TRa 219) and FDN witness Warren (TRa 264) testify a default - particularly one recommended in their testimony - is necessary to spur competition. Verizon witness Trimble (TRa 98), BellSouth witness Shiroishi (TRa 34), Sprint witness Ward (TRa 182), and ALLTEL witness Busbee (TRa 208) contend a default is not desirable because of the potential negative consequences that would stem from a change in the status quo.

Structure of a default

In the event the Commission elects to establish a default local calling area, the parties offer four options. ALLTEL, Verizon and Sprint advocate using the ILEC's retail local calling area if parties are unable to negotiate an agreement. BellSouth recommends using the originating carrier's local calling area if this approach is administratively feasible and if this option is not viable, to use the ILEC's retail local calling area.

AT&T recommends establishing the LATA as the default local calling area, and FDN recommends the default be the LATA providing the originating carrier transports the call to the access tandem serving the end user and charges retail rates for intraLATA calls that are not toll rates.

Use of the ILEC's Retail Local Calling Areas

The ILEC parties contend the use of existing retail local calling areas provides simplicity (Verizon BR at 24), competitive neutrality (Sprint BR at 12), avoids arbitrage opportunities (BST BR at 9), preserves the existing universal service support (Sprint BR at 8), and is consistent with the findings of other state commissions (Verizon BR at 29).

Verizon witness Trimble contends the existing system, which defines reciprocal compensation obligations based on ILEC-tariffed local calling areas, "has the advantage because it has worked well over the years and it is easier to maintain an existing, proven system than to implement and administer a new one." (TRa 103)

AT&T witness Cain counters the "unique geography" of the telecommunications industry involving local calling areas, extended calling areas, LATAs and - in the case of wireless carriers - major trading areas (MTAs) creates costs that new entrants incur to provide service to customers. (TRa 228) Applying the ILEC retail local calling areas, which AT&T argues in its brief predate the Act (AT&T BR at 7), works to restrict consumer choice and result in higher rates for consumers. (TRa 230)

FDN witness Warren concurs that the ILECs' local service areas create "artificial retail pricing boundaries and should not dictate whether a call is access for intercarrier purposes." (TRa 264)

While Verizon apparently believes the use of an ILEC's retail local calling area as the basis for determining compensation is simple, (Verizon BR at 24), staff concludes that the issue of simplicity appears to be in the eye of the beholder. AT&T witness Cain (TRa 228) and FDN witness Warren (TRa 264) testify the use of ILEC retail local calling areas is hardly a simple solution because it creates artificial price barriers and stifles competitive offerings.

A similar conclusion can be reached on the issue of competitive neutrality, in staff's view. Verizon witness Trimble testifies the existing system of basing compensation on ILEC retail local calling areas treats all parties - ILECs, ALECs and IXCs - the same. A call that remains within a retail local calling area is subject to reciprocal compensation while a call that crosses a retail local calling area boundary is subject to access charges. (TRa 91)

AT&T witness Cain (TRa 229) and FDN witness Ward (TRa 265) believe the dependence on ILEC retail local calling areas tilts the competitive playing field toward ILECs and effectively bars ALECs from making competitive offerings different from those provided by the ILECs.

Staff is leery of the competitive neutrality argument advanced by witness Trimble. BellSouth witness Ruscilli acknowledges the ILEC retail local calling areas were delineated, "well before the Act and the envision [sic] of competition." (TR 209) Thus it would seem paradoxical to assume neutrality in a competitive market paradigm will result from the imposition of a compensation structure that is geographically rooted in monopoly era regulation.

BellSouth witness Shiroishi raises the specter of arbitrage opportunities resulting from a change in the existing local calling area structure. Witness Shiroishi testifies "Now that we are in a more competitive environment where many ALECs are IXCs and vice versa, many IXCs are also ALECs, if we go to a LATA-wide local definition which has no delineation, you have an opportunity for IXCs to try to masquerade that true interexchange traffic as local through the use of, in some instances, even perhaps stripping off ANI or CPN and terminating that to the ILEC or any other LEC as though it were local." (TRa 45)

Subsequently in her testimony, witness Shiroishi indicates BellSouth has experienced no difficulties with wireless carriers, who, because of their differing calling plans, work cooperatively with BellSouth to determine which of their calls are interMTA or intraMTA. (TRa 56)

ILEC parties in this proceeding deal extensively with the potential threat to universal service support if a system is adopted that reduces access revenues. Verizon witness Trimble testifies that because access charges are profitable for ILECs, they implicitly subsidize basic local rates, thus furthering universal service. (TRa 149) Witness Trimble acknowledges access revenues are one of a number of universal service support mechanisms for ILECs and that Florida law gives an ILEC the right to petition the Commission for a change in the interim mechanism. (TRa 148)

In a similar vein, BellSouth witness Shiroishi testifies that BellSouth has lost intraLATA access revenues each month since the advent of wireless service. (TRa 57) AT&T notes in its brief that despite these losses, "Nonetheless, BellSouth has never petitioned the Commission pursuant to Section 364.025(3), F.S., for a change in its universal service support mechanism based upon the decrease of monthly minutes of intraLATA toll traffic due to competition from wireless carriers." (AT&T BR at 10)

In its brief, Verizon cites decisions by a number of state commissions that have "refused to apply reciprocal compensation to such calls that do not originate and terminate in the same ILEC local calling area." (Verizon BR at 28-29)

Staff notes that of the decisions cited in Verizon's brief, those from the states of Connecticut, Illinois, South Carolina, Georgia, and Missouri were focused on the issue of foreign exchange or virtual NXX service, which this Commission addressed in Issue 15 of this docket in December 2001. Staff sees no reason to reargue those issues in this phase of the docket.

Verizon also cites guidelines issued by the Ohio Public Utilities Commission which found the ILEC's local calling areas were to be used as the basis for differentiating local calls from toll calls. (Verizon BR at 30) Staff points out that this decision was reached by the Ohio Commission in 1995, prior to passage of the

Act, rendering its applicability questionable for use in a competitive market proceeding.

Finally, Verizon cites decisions reached by the Texas and Nevada commissions. The Nevada commission ruled in an arbitration previously referenced in this recommendation that "reciprocal compensation obligations should apply to traffic that originates and terminates within state-defined local calling areas." (TRa 176)

The Texas Public Utilities Commission determined, "Consequently, the Commission declines to adopt AT&T's LATA-wide proposal because it has ramifications on rates for other types of calls, such as intraLATA toll calls, that are beyond the scope of this proceeding." (TRa 176)

Regarding the Nevada case, staff believes the limited circumstances of an arbitration between parties instructive, but hardly precedential in a generic proceeding of this nature. As for the Texas decision, it appears to staff that the Texas commission chose not to accept AT&T's proposal because the AT&T proposal was beyond the scope of the proceeding. A decision not to rule by a state commission does not appear to support either side in this dispute.

Use of an Originating Carrier's Retail Local Calling Area

BellSouth witness Shiroishi believes using an originating carrier's local calling area is technically feasible, but also appears to acknowledge potential administrative concerns. (TRa 22) Witness Shiroishi testifies:

> BellSouth's position is that, for purposes of determining the applicability of reciprocal compensation, a "local calling area" can be defined as mutually agreed to by the parties and pursuant to the terms and conditions contained in the parties' negotiated interconnection agreement with the originating Party's local calling area determining the intercarrier compensation between the parties. BellSouth currently has the arrangement described above in many of its interconnection agreements, and is able to implement such arrangement [sic] through the use of billing factors. These factors allow the originating carrier to report to the

> terminating carrier the percent of usage that is interstate, intrastate, and local. (TRa 22)

Witness Shiroishi testifies that while BellSouth believes its plan is feasible, BellSouth, "does understand the concerns raised as to the implementation of different calling areas." (TRa 22)

These concerns are articulated by Sprint witness Ward, who believes, "it would be administratively burdensome for all carriers, not just ILECs, to change their billing systems to maintain the varying local calling areas of each ALEC." (TRa 185)

Verizon witness Trimble concurs that the use of an originating carrier's local calling area to determine compensation obligations is administratively infeasible. (TRa 100) Witness Trimble testifies, "Each ALEC may have its own originating local calling area, or may have multiple local calling options; given their regulatory freedoms, these ALECs may change their calling areas any time virtually at will. Not only the ILECs - but every ALEC - would have to attempt to track these changes and build and maintain billing tables to implement each local calling area and associated reciprocal compensation application. Administration is even further complicated if one assume [sic] that local calling areas may extend within or beyond LATA, or even state boundaries." (TRa 100)

In its brief, FDN relies on BellSouth witness Shiroishi's testimony that billing factors can be used to jurisdictionalize traffic, providing an indication of the viability of using the originating carrier's local calling area as the basis for reciprocal compensation. (FDN BR at 16) FDN does not address in its brief the administrative and cost issues raised by Verizon witness Trimble and Sprint witness Ward.

Data on the potential cost to reconfigure billing systems is not in the record of this proceeding. It appears reasonable to staff, based on the testimony, however, that some costs would be incurred to implement proposals using the originating carrier's retail local calling area for reciprocal compensation purposes.

Use of the LATA as the Local Calling Area

AT&T and US LEC of Florida argue for the adoption of the LATA as a default local calling area between ILECs and ALECs when parties are unable to negotiate an agreement. Staff notes that US LEC did not present witnesses or testimony in this phase of the proceeding, basing its post-hearing arguments on testimony filed in Phase II of this docket.

AT&T witness Cain testifies the benefits of using a LATA as a local calling area are administrative ease and enhanced competition. Witness Cain testifies "A LATA-wide calling area would simplify retail call rating as well as intercarrier billing of reciprocal compensation. All intraLATA calls would be treated the same for reciprocal compensation purposes, with each minute billed the same way." (TRa 218) Witness Cain also believes a LATA-wide local calling area would simplify billing systems, requiring only the re-rating of calls to a single-per-minute rate within a LATA regardless of dialing pattern. (TRa 220)

A modicum of support for the ALEC position may be found in the testimony of BellSouth witness Ruscilli, who, when asked if administrative efficiencies could be realized by having a single LATA-wide definition of a local calling area, answered, "I imagine there could be some." (TR 214)

Witness Cain contends establishing the LATA as the local calling area will enhance competition by allowing ALECs to offer consumers calling plans distinct from those offered by ILECs. (TRa 218)

In its brief, AT&T contends BellSouth already offers LATA-wide local calling in interconnection agreements with AT&T, Level 3 Communications, ALLTEL Florida, US LEC of Florida and Time Warner Telecom of Florida. (AT&T BR at 11) The existence of these agreements, AT&T argues, illustrates "the absurdity of BellSouth's position that LATA-wide local calling violates Section 364.16(3)(a)..."

The issue of whether or not BellSouth offers LATA-wide local calling for purposes of reciprocal compensation is a source of conflicting testimony by BellSouth witnesses in distinct phases of this docket.

In Phase II of this docket, BellSouth witness Ruscilli engaged in the following dialogue with staff counsel:

> Q. Now, BellSouth has entered into some agreements with carriers for a LATA-wide calling area, is that correct?
>
> A. For reciprocal compensation purposes, yes.
>
> Q. Well, would BellSouth object if this Commission were to determine that for purposes of reciprocal compensation a local calling area should be defined as a LATA-wide area?
>
> A. Well, no, I don't really think we would be able to object, simply because the provisions of the Act, I think it is 252(i), indicates that when we establish an agreement with a carrier, other carriers can opt into that agreement if they so choose. You know, subject to making sure they take the same terms and conditions. So we have done it once, so it is open to any carrier that wants to do it. There is not a need for the Commission to order it. (TR 213)

In the current Phase II(a) of this proceeding, BellSouth witness Shiroishi appears to dispute the testimony of witness Ruscilli when she testifies:

> BellSouth has entered into agreements that expand what is considered local traffic for reciprocal compensation purposes; however, in those agreements switched access is specifically exempted from being considered as local traffic. The AT&T/BellSouth Agreement which AT&T references does NOT make all calls which originate and terminate in the LATA local for reciprocal compensation purposes. The agreement clearly excludes switched access from the local traffic definition (See Attachment 3, Section 5.3.1.1 of the Interconnection Agreement). (TRa 33)

In its brief, BellSouth references witness Shiroishi's testimony quoted above and concludes that "BellSouth does not have any current agreements that implement the LATA-wide local definition that the ALECs are proposing in this docket." (BST BR at 11)

Staff finds the apparent contradiction between the testimony of the two BellSouth witnesses disconcerting. That BellSouth fails in its brief to make any effort to reconcile the conflicting statements leaves staff with a record marked by a glaring inconsistency on a disputed issue of fact.

FDN asserts that the LATA should be the default, but to overcome controversy over cost issues, transport obligations should be addressed by requiring the originating carrier to bring its traffic to the tandem serving the end user. In this way, FDN witness Warren argues, transport obligations are met and facilities-based competition is promoted. (TRa 264-265)

FDN takes the position that the LATA should be the default local calling area, provided the originating carrier transports its originated traffic to the access tandem serving the end user in the LATA and the originating carrier charges retail rates for in-LATA calls that are not toll rates.

In its brief, FDN argues that if a carrier of intraLATA calls could hand off its originated traffic without being charged intraLATA access charges by a terminating carrier, the "complex local calling areas could be erased, the barrier of access costs would be removed, price competition for calls between all of the cities within the LATA would flourish." (FDN BR at 12)

Verizon witness Trimble testifies that while he lauds the prospect of requiring an ALEC to deliver its traffic at least as far as the ILEC tandem serving the end user, FDN's proposal with its LATA-wide implications is , "just another attempt to circumvent the established intraLATA access regime, and is thus unacceptable." (TRa 124)

The ILEC parties to this docket offer a number of objections to AT&T's proposal, which are discussed above in this recommendation. Those objections, in summary, are: AT&T's proposal is not competitively neutral (Sprint BR at 12); AT&T's proposal creates arbitrage opportunities (BST BR at 9); AT&T's proposal threatens universal service support and could lead to an increase in local service rates (Sprint BR at 9); and AT&T's proposal is inconsistent with the findings reached by other state commissions (Verizon BR at 9).

In addition, the four ILEC parties to this docket filed estimates of losses they anticipate would be incurred if revenue gained from intraLATA access charges were converted to reciprocal compensation payments at currently approved rates. ALLTEL estimates it would lose $700,000 annually, and Sprint estimates its losses by its ILEC, IXC and ALEC would be $14 million annually. BellSouth and Verizon filed comparable figures but did so under claims of confidentiality.

Staff notes that its initial recommendation in Phase II of this proceeding proposed that negotiations between parties should be the basis for defining local calling areas for reciprocal compensation purposes and, in the event the negotiations failed, the local calling area be defined as all calls that originate and terminate in a LATA.

At its special agenda conference on December 5, 2001, the Commission directed staff to solicit further testimony from the parties after expressing concerns in two areas: First, the Commission questioned whether a default to LATA-wide calling would unfairly give leverage to ALECs in negotiations, thereby creating a disincentive to negotiate; Second, there was concern over the potential for unintended consequences - particularly in the intraLATA toll market - that could result from establishing LATA-wide calling as a default.

Taking the second point first, staff is unpersuaded by ILEC testimony that arbitrage opportunities will result from a default to LATA-wide calling, as claimed by BellSouth witness Shiroishi. Staff finds it significant that witness Shiroishi acknowledges BellSouth's reliance on the integrity of wireless carriers in reporting to BellSouth whether calls are interMTA or intraMTA in nature for compensation purposes. There is nothing in the record to suggest a similar system could not be used in a LATA-wide calling regime. Witness Shiroishi testifies this system has functioned without incident with wireless carriers, leading staff to believe the concern regarding arbitrage opportunities is wholly speculative.

Verizon witness Trimble's concern over universal service obligations, echoed by BellSouth witness Shiroishi, ALLTEL witness Busbee and Sprint witness Ward, seems incomplete. While two of the parties filed public projections of anticipated losses from converting access revenues to reciprocal compensation revenues and two parties filed confidential projections, none of the parties indicated the relative scale of the projected losses. In other words, no party stated whether the projected losses would compel the respective ILEC to petition the Commission for a change in the interim universal service mechanism pursuant to Section 364.025(3), Florida Statutes.

Witness Shiroishi's testimony that BellSouth has seen a monthly erosion of intraLATA minutes attributable to the proliferation of wireless calling plans with expanded calling areas without a collateral petition under Section 364.025(3), Florida Statutes, would appear not to support the ILEC's universal service concerns.

As noted earlier in this recommendation, staff finds little in the decisions by other states cited by the ILEC parties that is dispositive in this matter.

Staff is concerned with the impact on the intraLATA toll markets that would result from adoption of the ALEC's proposals. As offered by AT&T witness Cain, in a LATA-wide calling regime, ALECs and ILECs would exchange all traffic in a LATA and compensate each other on the basis of reciprocal compensation rates. An IXC, however, would continue to be required to pay originating access and terminating access to the respective LEC, essentially creating a separate, more costly form of intraLATA toll service. AT&T witness Cain offers no remedy for this disparity, suggesting instead that erosion of the IXC's competitive position is inevitable and attributable to layers of non-cost-based prices in the access charge regime. Whether or not witness Cain's projection that economic Darwinism will consume IXCs providing intraLATA toll service is accurate, staff believes this possibility deserves notice as a potential consequence of LATA-wide local calling.

On the issue of providing leverage in negotiations, given the ALEC's advocacy of LATA-wide local calling and the ILEC's opposition to LATA-wide local calling, it would appear that setting LATA-wide local calling as the default would provide ALECs with a disincentive to negotiate. This appears to staff to be counterproductive if the preference is to have a business solution, as opposed to a regulatory solution, to industry disputes.

CONCLUSION: Primary staff believes the consequences of adopting any of the proposals advocated by the parties in this proceeding as a default has the potential to create a "one step forward and two steps back," effect. Continued use of the legacy retail local calling areas as the basis for wholesale compensation preserves the ILECs' role as arbiters of call jurisdiction, but financially disadvantages ALECs by stifling competitive calling plan options, thereby limiting consumer choices. Adoption of the LATA as a default local calling area provides ALECs with reduced wholesale costs - and theoretically greater competitive flexibility - while costing ILECs millions in lost access charge revenues and potentially decimating the IXCs' place in the intraLATA toll market. A default based on the originating carrier's retail local calling area promises the ultimate in calling plan flexibility but may require investment in reconfiguring billing systems and could lead to a market in which the direction of a call determines its jurisdiction for compensation purposes.

Given that each option presented appears to generate adverse consequences if adopted as a default by the Commission, staff shares concerns expressed by the parties that the carrier advantaged by the default will have a disincentive to negotiate. Thus, it would appear that adoption of any of the defaults presented here would predispose the parties toward regulatory solutions as opposed to negotiated business solutions. Conversely, parties negotiating with the knowledge that the Commission has a range of options available to it which one or both parties find onerous, may provide the incentive to reach a negotiated agreement.

Therefore, staff recommends the local calling area should be defined through negotiations between the parties. While staff believes the Commission has explicit jurisdiction to define local calling areas, staff does not believe a compelling case can be made to exercise the Commission's jurisdiction to designate a default in the event negotiations are unproductive.

ALTERNATIVE STAFF ANALYSIS:

Consistent with the Primary Staff Analysis, alternative staff believes that the Commission does have the jurisdiction to establish a default local calling area for purposes of reciprocal compensation. In addition, alternative staff agrees with the concerns expressed in the Primary Staff Analysis related to using either the ILEC's retail local calling area or the LATA as a wholesale local calling area. These two options, while administratively attractive, seem to suffer from a lack of competitive neutrality.

Using the ILEC's retail local calling area appears to effectively preclude an ALEC from offering more expansive calling scopes. Although an ALEC may define its retail local calling area as it sees fit, this decision is constrained by the cost of intercarrier compensation. An ALEC would be hard pressed to offer local calling in situations where the form of intercarrier compensation is access charges, due to the unattractive economics.

A LATA-wide wholesale calling regime appears to discriminate against IXCs. While ALECs and ILECs would exchange all traffic in a LATA at reciprocal compensation rates, IXCs would continue to pay originating and terminating access charges for carrying traffic over some of the same routes.

If the Commission sets a default local calling area, staff believes it is important that the default be as competitively neutral as possible. A default which is defined in accordance with the ILECs' preference for their existing retail local calling areas or the ALECs' preference for LATA-wide local calling may create a disincentive to negotiate. Adopting either of these two options would seem counterproductive, as it could chill negotiations and lead to one-sided outcomes.

At the same time, alternative staff believes it is important that the Commission establish a default local calling area for purposes of reciprocal compensation. This issue is becoming too commonplace in arbitration cases filed with this Commission, and some finality is important in order to avoid litigating this issue multiple times.

One approach to defining the wholesale local calling area which receives less attention from the parties is to use the originating carrier's retail local calling area. BellSouth witness Shiroishi actually supports this approach and believes that such a plan is "administratively manageable," while acknowledging that there may be some concerns. (TRa 22) In addition, she testifies that "BellSouth currently has the arrangement . . . in many of its interconnection agreements." (Shiroishi TRa 22) Of the options presented, alternative staff believes this approach is more competitively neutral than the others.

Verizon witness Trimble and Sprint witness Ward believe that BellSouth's proposal is administratively complex and illogical on the basis that wholesale compensation should not vary depending on the direction of a call. (Trimble TRa 97-100, Ward TRa 184-185) With respect to the administrative issues, Verizon witness Trimble speaks to the need to "build and maintain billing tables to implement each local calling area." (TRa 100) Sprint witness Ward expresses concern about carriers having "to change their billing systems to maintain the varying local calling areas of each ALEC." (TRa 185) Alternative staff notes, however, that BellSouth witness Shiroishi explains that her company has implemented this approach through the use of billing factors. She states that these factors "allow the originating carrier to report to the terminating carrier the percent of usage that is interstate, intrastate, and local." (Shiroishi TRa 22) The testimony suggests that a system based on the originating carrier's retail local calling area could be implemented in one of two ways. The Verizon and Sprint witnesses seem to envision a method whereby the various local calling areas would be coded into their billing systems, while the BellSouth witness describes a method based on billing factors, which would not necessitate such extensive coding. Consequently, alternative staff believes that using the originating carrier's retail local calling area for wholesale purposes need not be as complicated to implement as the Verizon and Sprint witnesses would lead the Commission to believe.

The second complaint, that wholesale compensation should not vary depending on the direction of the call, is more thought-provoking since directional differences in compensation appear to be anomalous and inequitable. While alternative staff believes that such a plan may result in directional differences initially, we question whether these differences will be sustainable over time. As carriers experiment with different retail local calling areas, market forces will eventually determine which plans are most viable, and more uniformity will emerge as a result. In the short run, it is important to encourage experimentation, and this plan accomplishes that objective.

In conclusion, alternative staff believes that the Commission should establish a default local calling area for purposes of reciprocal compensation. This issue appears with enough frequency that a default definition is needed for the sake of efficiency. A default should be as competitively neutral as possible, thereby encouraging negotiation and development of business solutions. On this basis, alternative staff recommends that the originating carrier's retail local calling area be used as the default local calling area for purposes of reciprocal compensation.

ISSUE 17: Should the Commission establish compensation mechanisms governing the transport and delivery or termination of traffic subject to Section 251 of the Act to be used in the absence of the parties reaching an agreement or negotiating a compensation mechanism? If so, what should be the mechanism?

a) Does the Commission have jurisdiction to establish bill and keep?

b) What is the potential financial impact, if any, on ILECs and ALECs of bill and keep arrangements?

c) If the Commission imposes bill and keep as a default mechanism, will the Commission need to define generically "roughly balanced?" If so, how should the Commission define "roughly balanced?"

d) What potential advantages or disadvantages would result from the imposition of bill and keep arrangements as a default mechanism, particularly in comparison to other mechanisms already presented in Phase II of this docket?

RECOMMENDATION: No. Staff does not recommend the imposition of a single compensation mechanism governing the transport and delivery or termination of traffic subject to Section 251 of the Act to be used in the absence of the parties negotiating a compensation mechanism. While staff believes the Commission has the jurisdiction to establish bill-and-keep subject to either a determination or a presumption that traffic between carriers is roughly balanced, the record of this proceeding does not support such a determination and argues against a presumption of balance. Should the Commission determine that the imposition of a bill-and-keep default is desirable, staff recommends the Commission define roughly balanced to mean the traffic imbalance is less than 10 percent between carriers over a three-month period. **(BLOOM)**

POSITIONS OF THE PARTIES:

BELLSOUTH:

a) Yes. Under the FCC rules, the Commission has the authority to establish bill and keep arrangements.

b) Bill-and-keep will allow carriers to recover their costs from end users rather than through subsidiaries [sic] received from other carriers.

c) Not necessarily. The Commission could presume that traffic is roughly balanced subject to a carrier rebutting such a presumption.

d) There are several potential advantages that may result from the adoption of bill-and-keep for local usage.

SPRINT:

Sprint's traffic analysis shows that traffic is generally not roughly balanced between Sprint and individual ALECs in Florida. Therefore, Sprint believes there is little benefit in the Commission adopting a presumption that traffic is roughly balanced and establishing bill and keep as the default mechanism for reciprocal compensation in Florida.

VERIZON:

No. The Commission should defer ruling until the FCC has completed its *Unified Intercarrier Compensation Rulemaking*, in which the FCC is considering the same issue identified here.

a) Yes.

b) It is impossible to give a generic answer about the potential financial impact of bill and keep on ILECs and ALECs; impacts can only be calculated for specific carrier pairs. In any event, negative financial impact will be prevented by an out-of-balance traffic condition.

c) Adoption of a standard for "roughly balanced" is advisable. Verizon suggests defining traffic as roughly balanced if the imbalance is less the 10% in any 3-month period.

d) A bill-and-keep approach may offer benefits in terms of ease of administration and less need for regulatory intervention, but it must include network architecture conditions and an out-of-balance standard to avoid creating new arbitrage and gaming opportunities.

AT&T:

a) Yes, the Commission has jurisdiction to establish bill-and-keep, if local traffic between the carriers is roughly balanced.

b) A bill-and-keep arrangement would cause major adverse financial impact on ALECs without a concomitant reduction in administrative costs.

c) Yes, if the Commission imposes bill-and-keep as a default mechanism, it will need to define generically, "roughly balanced." Traffic should be considered "roughly balanced" when the difference between the amounts of traffic terminated by each carrier is almost insignificant.

d) Bill-and-keep has many potential disadvantages as it preserves objectionable aspects of the existing patchwork of compensation.

FCTA, TIME WARNER:

Yes. The Commission should continue its policy of requiring reciprocal compensation for the local traffic (i.e., non-ISP-bound traffic) that remains under its jurisdiction. The Commission's current rules require that symmetrical rates, based upon the ILEC's Commission-approved unbundled network element rates, serve as the default reciprocal compensation mechanism.

a) The Commission has jurisdiction to establish bill-and-keep for non-ISP-bound local traffic under certain circumstances. The Commission can establish bill-and-keep if neither carrier has rebutted the presumption of symmetrical rates and if the flow of traffic between the carriers' networks is approximately equal.

b) ILECs should receive a substantial stream of cash flow, because they no longer have the obligation to compensate the ALECs for terminating calls that are originated on their networks. ALECs will not recover the revenue earned for transporting and terminating the local traffic that is originated by the ILECs' customers.

c) Yes. Non-ISP-bound local traffic must be measured for "roughly balanced" traffic loads. A percentage or dollar threshold could be established where an obligation to compensate the interconnecting carrier would arise when the net minutes-of-use for terminating traffic exceeded the threshold.

d) Several disadvantages would result from the imposition of a bill-and-keep arrangement. There would be market uncertainty, and new administrative and marketing costs will be borne by ILECs and ALECs. Bill-and-keep is also likely to promote regulatory gamesmanship and enhancement of the superior bargaining power of the ILECs.

FDN:

Yes. A fair and reasonable default mechanism would promote efficiencies in negotiations, administration and arbitration of interconnection matters. The default should be as FDN proposes in subparts below.

a) Yes, aside from state law authority under Sections 364.16 and 364.162 to establish fair, reasonable and nondiscriminatory terms for interconnection, 47 C.F.R. 51.713 grants the Commission authority to establish bill and keep arrangements and to presume traffic exchanges are roughly in balance.

b) Assuming the traffic balance/volume and transport conditions FDN proposes in subparts below are approved and a succinct mechanism is in place, LEC expenses for monitoring, billing and collection of intercarrier compensation could be reduced, and LECs may be able to reallocate resources to end-user focused, competitive activities.

c) Yes. On a per LATA basis, "roughly balanced" should mean there is a 10% or less variation in the volume of traffic exchanged between carriers over a reasonable period. Bill and keep should also apply where traffic exchanged does not meet a threshold minimum.

d) Disadvantages to a bill and keep regime would only result where traffic is not over a minimum threshold and/or not roughly in balance or where there are unfair or unreasonable rules on interconnection architecture.

US LEC:

a) Pursuant to FCC Rule 51.713(b), the Commission may impose bill-and-keep arrangements if the amount of telecommunications traffic from one network to the other is roughly balanced with the amount of local telecommunications traffic flowing in the opposite direction, and is expected to remain so.

b) A bill-and-keep arrangement would have a significant negative financial impact on ALECs as the cost-causer (originating caller) would not be responsible for the cost of transporting and terminating the call.

c) The Commission will need to define generically "roughly balanced" if the Commission imposes bill-and-keep as a default mechanism.

d) Bill-and-keep only offers any advantage to carriers when the exchange of local traffic is statistically balanced.

PARTIES' ARGUMENTS: There appears to be consensus among the parties on two subissues for which testimony and evidence was solicited: The parties agree the Commission has jurisdiction to establish bill-and-keep, although differing views are expressed as to whether the Commission should adopt bill-and-keep as a default; and the parities concur that if the Commission adopts bill-and-keep as a default compensation mechanism, the Commission should define generically the term "roughly balanced."

The parties do not agree that the Commission should establish a compensation mechanism in the event parties fail to reach agreement, and there is diversity of opinion on the potential financial impact of establishing a bill-and-keep regime for those carriers that cannot successfully negotiate an agreement. In addition, there is broad disagreement over the perceived advantages and disadvantages of a bill-and-keep default mechanism.

AT&T witness Cain testifies the imposition of a bill-and-keep regime for reciprocal compensation would be detrimental to ALECs and consumers. (TRa 222-223) "Bill and keep shifts the burden of recovering the cost of the call from the originator of the call to the recipient of the call. People who make very few calls or those who subscribe to phone service primarily for safety reasons (i.e., to make calls in an emergency) would likely see their phone rates increase. Customers that make a large number of calls (e.g., telemarketers) would likely see their rates decline." (TRa 223)

Witness Cain does not appear to believe a bill-and-keep system provides benefits to competitive carriers. "Bill and keep preserves objectionable aspects of the existing patchwork of compensation. As a default mechanism, bill and keep would discourage good-faith negotiations between the ILECs and ALECs. The party that expects to originate more traffic than it terminates would have every incentive to dig its heels in, knowing that the default mechanism will govern." (TRa 222)

AT&T witness Cain also predicts negative financial consequences for ALECs under bill-and-keep:

> Bill and keep will cause a major adverse financial impact without a concomitant reduction in administrative costs. ALECs in particular will lose a source of income that is necessary to cover the cost for transporting and terminating calls originating on the ILEC's network. As outbound calls would surely increase under a bill and keep regime, the pricing signals used to charge end user customers would have to change dramatically in order to pay for the costs of running the network. Under current traffic patterns, ILECs would reap a considerable windfall, able to terminate their local traffic to the ALECs for free. (TRa 224)

FCTA witness Barta shares the view expressed by AT&T witness Cain that bill-and-keep will deprive ALECs of one means of recovering costs. "The shift to a bill and keep arrangement will not relieve the ALEC of the responsibility to terminate the call that the ILEC's customer originates. More importantly, the shift to a bill and keep arrangement does not mean the ALEC's cost of terminating the traffic that has been originated on the ILEC's network has decreased or disappears simply because there is no explicit compensation for the carriage of traffic between the carriers." (TRa 247)

Witness Barta also expresses concern that a bill-and-keep default mechanism provides a disincentive for ILECs to negotiate:

> BellSouth and Verizon overwhelmingly support the move to a bill and keep regime. Based upon these dominant firms' preference for a bill and keep arrangement, the Commission's proposed default mechanism would cast a certain chill on the give and take that typically characterizes arms-length negotiations. Indeed, it is highly likely that the incumbent LECs will be tough "negotiators," secure in the knowledge that a bill and keep regime is the ultimate regulatory remedy to resolve any impasse between the parties. (TRa 244)

Witness Barta believes that while bill-and-keep arrangements may have the advantage of reducing transaction costs for interconnecting carriers, a bill-and-keep regime will cause greater administrative and marketing costs, in addition to fostering market uncertainty owing to the unknown financial consequences that ALECs may face. (TRa 243) Witness Barta does not provide estimates of the additional administrative and marketing costs he testifies would result from bill-and-keep.

Witnesses Cain and Barta allege a bill-and-keep system will encourage regulatory arbitrage. AT&T witness Cain testifies "bill and keep would create new opportunities for both regulatory arbitrage and monopoly abuse by encouraging carriers to seek out customers who make more calls than they receive (e.g., telemarketers, stockbrokers)." (TRa 222-223)

FCTA witness Barta believes bill and keep will not only encourage regulatory arbitrage, but will influence network decisions:

> Under a bill and keep arrangement, carriers will search for ways to unload the traffic originating on their networks as quickly as possible and to accept terminating traffic as late as possible. For instance, the strategic placement of central offices further out in the network can affect a carrier's costs under bill and keep regardless of whether it represents efficient design practices. In addition, the concern over regulatory arbitrage may shift carriers seeking an imbalance in terminating traffic to one where carriers target large

> net originators of traffic. Not only may bill and keep influence the carrier to base its network strategy upon concerns for regulatory treatment rather than concerns for the most economically efficient configuration, such an arrangement may invite new opportunities for regulatory arbitrage. (TRa 253)

Witness Barta does not elaborate on what form "new opportunities for regulatory arbitrage" will assume.

FDN witness Warren believes bill-and-keep arrangements are "inherently equitable" in situations where traffic volumes are roughly equal. Witness Warren defines roughly equal as meaning that the terminating local traffic volumes delivered by the respective parties are within 10 percent. (TRa 268) Witness Warren believes that if traffic is not in balance, a default symmetrical measurable rate should be established on a LATA-wide basis when a minimum traffic volume of more than 499,999 minutes of use is reached. Witness Warren testifies, "In my opinion, the administrative burden and resources required for reciprocal compensation billing and collection is not justified for minutes below that [proposed] threshold." (TRa 268)

A bill and keep system, witness Warren believes, minimizes the billing and collection obligations of the participating carriers, allowing carriers to devote resources to end-user focused, competitive activities. (TRa 269)

In its brief, US LEC argues "the potential disadvantages of bill-and-keep far outweigh the possible benefit of lower carrier transaction costs. Bill-and-keep would foster market uncertainty as its financial impact on ALECs remains unknown until a bill-and-keep regime is in effect. Bill-and-keep could also potentially spawn new incentives to engage in regulatory gamesmanship as carriers attempt to design their network to dispose of traffic originating on their networks quickly and to accept terminating traffic as late as possible." (US LEC BR at 11)

Sprint witness Hunsucker argues against the implementation of a standard for "roughly balanced" in the context of a bill-and-keep regime. Witness Hunsucker testifies that because the Commission must either determine or presume telecommunications traffic between carriers is roughly balanced in order to establish bill-and-keep, (TRa 194) and because evidence submitted does not support such a determination or presumption, (TRa 199) a definition of "roughly balanced" for a bill-and-keep default mechanism should not be established. (TRa 194)

Witness Hunsucker bases his argument on 47 C.F.R. §51.713(b) and (c), which read as follows:

> (b) A state commission may impose bill-and-keep arrangements if the state commission determines that the amount of local telecommunications traffic from one network to the other is roughly balanced with the amount of local telecommunications traffic flowing in the opposite direction, and is expected to remain so, and no showing has been made pursuant to §51.711(b).
>
> (c) Nothing in this section precludes a state commission from presuming that the amount of local telecommunications traffic from one network to the other is roughly balanced with the amount of telecommunications traffic flowing in the opposite direction and is expected to remains so, unless a party rebuts such a presumption.

In Exhibit 3, witness Hunsucker provides an analysis of traffic flows between Sprint and 26 ALECs in Florida. In the exhibit, witness Hunsucker indicates that Sprint exchanged approximately 6.1 billion minutes of traffic with ALECs in Florida in 2001, based on annualized traffic volumes for the first quarter of the year. Of the total amount of traffic exchanged, witness Hunsucker testifies, Sprint originated about 5.8 billion of those total minutes. (EXH 3, MRH-1) This equates to an aggregate traffic ratio of approximately 17 to 1, witness Hunsucker testifies, meaning Sprint is responsible for paying to terminate 17 minutes of traffic for each minute of traffic it is paid to terminate. (TR 198)

In an effort to separate dial-up ISP traffic from his analysis, witness Hunsucker testifies he adopted a rebuttable presumption from the FCC's Order on Remand and Report and Order, ¶8 (FCC 01-131, April 27, 2001). In its order, the FCC found:

> In order to limit disputes and costly measures to identify ISP-bound traffic, we adopt a rebuttable presumption that traffic exchanged between LECs that exceeds a 3:1 ratio of terminating to originating traffic

> is ISP-bound traffic subject to the compensation mechanism set forth in this Order.

Witness Hunsucker testifies that by eliminating traffic volume relationships in excess of the FCC's 3:1 rebuttable presumption, he concludes Sprint exchanged 1.1 billion minutes of non-ISP traffic in 2001 at a ratio of 1.94 to 1. (EXH 3, MRH-2) Witness Hunsucker adds that while he developed an overall ratio between Sprint and the ALECs with whom Sprint exchanges traffic, he does not believe the ratio can be the basis for a determination of whether traffic is roughly balanced. Citing 47 C.F.R. Rule 51.713(b), witness Hunsucker testifies the rule, "requires the state commission to make a determination on the amount of traffic 'from one network to the other'. Sprint believes that this requires a state commission to make a determination on the basis of traffic flows between two specific carriers and that it is not appropriate to make a determination on any aggregated basis, e.g., total ILEC to ALEC traffic." (TRa 197)

Witness Hunsucker declines to offer a definition of what would constitute a situation in which traffic volumes are roughly balanced and concludes:

> There is little evidence that the traffic flows between Sprint and ALECs in Florida is "roughly balanced." For this reason, if the Commission were to adopt a definition of "roughly balanced," it would be Sprint's position that individual carriers would file with the Commission to rebut the presumption. Sprint would file when it is in its best interests and connecting carriers would file when it is in their best interests. For this reason, adoption of a definition of "roughly balanced" would provide little, if any, benefit to the industry and would potentially place a greater workload on the Commission to review all the rebuttable pleadings that would result. (TRa 200)

Witness Hunsucker also expresses doubt that a bill-and-keep regime would net significant cost savings for Sprint. While acknowledging possible reductions in billing and collection costs associated with reciprocal compensation, witness Hunsucker testifies, "a portion of the costs associated with this function are sunk, in that there were significant modification costs incurred on the front end to implement billing for reciprocal compensation." (TRa 201) Witness

Hunsucker also testifies that Sprint's billing system was developed to include demand for all 18 states in which the company operates and that removing one state would do little to eliminate billing system maintenance costs. (TRa 201)

Sprint witness Hunsucker also notes that Sprint elected to opt in to the FCC's interim compensation regime effective February 1, 2002. (TRa 196) In its brief, Sprint argues that its decision to accept the interim compensation regime is significant:

> The ISP remand Order, addressing the appropriate intercarrier compensation for ISP-bound traffic, has altered the effect of any decision by this Commission to implement bill and keep as a default mechanism for reciprocal compensation. The order has eliminated ISP-bound traffic from the mix of 251(b)(5) traffic, but requires ILECs who elect the FCC compensation scheme for ISP-bound traffic to apply the same rate to reciprocal compensation for 251(b)(5) traffic as they apply to ISP-bound traffic. This requirement supercedes any compensation mechanism this Commission may adopt. (Sprint BR at 22)

Verizon witness Trimble believes the Commission should retain the record it has developed in this docket but defer any ruling on a compensation mechanism pending the outcome of the FCC's Notice of Proposed Rulemaking (In the Matter of Developing a Unified Intercarrier Compensation Regime, CC Docket No. 01-92, FCC 01-132, April 27, 2001). Witness Trimble testifies he recommends a deferral on compensation,"to avoid potentially conflicting rulings and subsequent revisions to the state scheme . . ." (TRa 112)

If, however, the Commission decides to adopt a default, witness Trimble offers conditional support for a bill-and-keep system:

> Any bill-and-keep proposal must, among other components, continue to require efficient direct trunking. Absent specific requirements, originating carriers may impose network inefficiencies, costs, and significant switch augmentation requirements on terminating carriers because there is no longer a price incentive to deliver traffic to the point of switching nearest the terminating end user. For example, absent requirements or incentives,

> originating ALECs could deliver terminating traffic to the ILEC tandem, quickly exhausting tandem switching and transport facilities with local traffic volumes and causing resulting congestion, blocking, and facilities expense.
>
> One solution would be to apply bill-and-keep only at the point of switching nearest the terminating end user (for example, the serving end office in a traditional ILEC network). Another solution may be a more comprehensive interconnection architecture standard establishing common interconnection point locations that do not unfairly benefit one class of carriers at the expense of another by requiring the originating carrier to deliver allegedly "local" traffic to distant interconnection points. (TRa 113-114)

Witness Trimble acknowledges that if the Commission adopts a bill-and-keep approach that is not consistent with his recommendations on architecture and interconnection points, there may be benefits nonetheless. One such benefit, witness Trimble testifies, would be a need for less regulatory intervention. (TRa 115) Witness Trimble is unable to quantify transaction costs that might be avoided under a bill-and-keep regime, although he testifies he believes there would be some savings. (TRa 115)

Should the Commission adopt a bill-and-keep approach, witness Trimble recommends "roughly balanced" be defined as carriers' traffic volumes being within 10 percent of each other during any three-month period. Witness Trimble notes this threshold has been adopted in Verizon's interconnection agreement with AT&T. (TRa 111) Verizon indicates in discovery that the 10 percent provision has been adopted by 58 other ALECs. (EXH 10, p.2)

Witness Trimble eschews FCTA witness Barta's testimony that a bill-and-keep system would allow ILECs to exercise superior bargaining power (TRa 244), contending "there is no evidence supporting Mr. Barta's statement that adoption of a B&K mechanism will give the ILECs a bargaining advantage." (TRa 138) Similarly, witness Trimble dismisses AT&T witness Cain's testimony that bill-and-keep will create incentives for "regulatory arbitrage and monopoly abuse." (TRa 222-223) Witness Trimble testifies, "Mr. Cain offers no factual explanation as to what form of monopoly abuse that could possibly result from an appropriately designed B&K mechanism . . ." (TRa 139)

In response to a discovery request by staff, Verizon filed data reflecting minutes of traffic exchanged with ALECs. (EXH 15) Because the information was filed with a request for confidentiality, staff cannot discuss specifics of the filing. Staff would note, however, that the balance of traffic between Verizon and the ALECs listed in the discovery response is generally consistent with the imbalances provided by Sprint and BellSouth.

BellSouth witness Shiroishi testifies the Commission has the authority to establish a bill-and-keep intercarrier compensation mechanism in this proceeding, based on FCC rules. (TRa 28) In order to do so, witness Shiroishi believes the Commission can presume non-ISP traffic between ILECs and ALECs is roughly balanced subject to a party rebutting the presumption. (TRa 29)

To make such a presumption, witness Shiroishi advocates for a definition of roughly balanced that applies the 3:1 ratio employed by the FCC in Order FCC 01-131:

> The FCC made a determination in it's [sic] Order on Remand and Report and Order in CC Docket 99-68 released April 27, 2001 ("ISP Order on Remand") that traffic above a 3:1 ratio of originating to terminating traffic would be considered ISP-bound traffic. Following this already established precedent, this Commission should find that traffic below a 3:1 ratio of originating to terminating traffic is "roughly balanced." (TRa 29)

If a party wanted to challenge the presumption that its traffic was roughly balanced, witness Shiroishi testifies, the party would make a showing to the Commission because the local traffic is subject to Commission jurisdiction. (TRa 29-30)

In its brief, AT&T describes witness Shiroishi's recommendation on the issue of roughly balanced as a "profound misreading of the FCC's *ISP Remand Order*." (AT&T BR at 16) AT&T argues in its brief that if the Commission finds that all traffic below a 3:1 ratio of originating to terminating traffic is roughly balanced, "every ALEC in Florida would be forced to terminate all of BellSouth's local traffic for free; even if that ALEC terminates three times the BellSouth traffic that it originates and sends to BellSouth." (AT&T BR at 17)

AT&T witness Cain testifies, "BellSouth jumps to the incredible conclusion that all traffic that is not ISP traffic must be in balance. So, according to BellSouth, traffic patterns that are out of balance by as much as 50% (i.e., 75% minus 25%) are actually 'in balance.' That is an extremely 'rough' definition of 'roughly in balance.'" (TRa 236)

Sprint, in its brief, describes BellSouth's position on roughly balanced as "creative." (Sprint BR at 19) While Sprint concurs that the FCC intends for all traffic above a ratio of 3:1 be presumed to be ISP-bound, Sprint disagrees with BellSouth's analysis that concludes all traffic below a 3:1 ratio should be considered roughly balanced for intercarrier compensation purposes. (Sprint BR at 19)

BellSouth filed originating and terminating traffic volumes for 62 ALECs from the first quarter of 2001 in the discovery phase of this proceeding. BellSouth's filing indicates that of the 28 carriers with whom BellSouth originates and terminates traffic, an overall ratio of 1.67 to 1 exists, meaning BellSouth originates 1.67 minutes of traffic to ALECs for each minute of traffic it terminates from ALECs. (EXH 12, Item 3, Exhibit C)

Witness Shiroishi testifies BellSouth has a number of current interconnection agreements in place in Florida that provide for bill-and-keep arrangements for non-ISP traffic, including agreements with Sprint, Covad, CRG International, Knology, Atlantic.net, Allegiance, and Hart. According to witness Shiroishi, "Such contracts state that per minute-of-use elements for local calls that originate from one Party and terminate to the other Party shall be compensated as bill-and-keep." (TRa 30)

ANALYSIS: In the previous phase of this proceeding, staff recommended the Commission adopt as a default the compensation mechanisms outlined in 47 C.F.R., Part 51, Subpart H, *Reciprocal Compensation for Transport and Termination of Local Telecommunications Traffic*. Staff further recommended that the applicable default rates be those established by the Commission in Docket No. 990649-TP.

In this phase of the docket, the parties were again asked whether the Commission should establish a default compensation mechanism and, if so, what the default mechanism should be. In addition, the Commission sought an expanded record on the impacts of bill-and-keep as a default, with an emphasis on traffic flows between ILECs and ALECs, and the policy ramifications of presuming traffic volumes are roughly balanced as a precursor to the imposition of bill-and-keep.

As noted at the outset, the parties agree the Commission has authority to establish bill-and-keep, though not on whether the Commission should adopt bill-and-keep as a default. In addition, the parties agree that in order to impose bill-and-keep, a definition of what constitutes "roughly balanced" traffic is necessary, although what the definition should be elicits some dissent. The potential financial impact on the parties of a bill-and-keep system and the potential advantages and disadvantages of bill-and-keep draw contrary responses from the parties.

BellSouth advocates adoption of a bill-and-keep default, a presumption by the Commission that traffic between carriers is "roughly balanced," and a definition of "roughly balanced" that would include all traffic below a threshold of 3:1. (TRa 29) Staff agrees with BellSouth that according to the provision of 47 C.F.R. Rule 51.713(c) the Commission can presume traffic between carriers is roughly balanced and that such a presumption is rebuttable. (BST BR at 15-16) Staff finds no support, however, for BellSouth's proposal that a 3:1 ratio constitutes a rough balance between carriers. As pointed out by Sprint in its brief (Sprint BR at 19), the FCC's use of a 3:1 presumption is intended to determine whether traffic is ISP-bound or local for compensation purposes (FCC 01-131, ¶8). Staff believes that to presume that traffic is roughly balanced when one carrier terminates 50 percent more traffic than it originates is, as AT&T witness Cain points out, "an extremely 'rough' definition of roughly balanced." (TRa 236)

By comparison, Verizon (Verizon BR at 32) and FDN (FDN BR at 19) recommend that a difference of 10 percent or less during any three-month period for traffic be considered "roughly balanced." AT&T recommends the difference between traffic exchanged should be "almost insignificant" (AT&T BR at 15), and FCTA and Time Warner argue against "large traffic imbalances." (FCTA/Time Warner BR at 13)

FDN witness Warren supports bill-and-keep in situations where an originating carrier hands off its call as far as the ILEC tandem serving the geographic location of the end user, and the traffic balance between two carriers is within 10 percent. (TRa 267)

Essentially, FDN argues, one condition for bill-and-keep should be the incorporation of its recommendation for a default local calling area, which staff has previously addressed and found lacking in Issue 13 of this recommendation. While staff appreciates FDN's effort to sustain consistency on the issues for resolution in this phase of the proceeding, the merits of establishing local calling areas and the method by which compensation is determined were deemed to be separate considerations.

FDN's recommendation that "roughly balanced" be defined as occurring when originating and terminating local traffic flows between two carriers are within 10 percent appears to be reasonable and enjoys explicit support from Verizon and implicit support from FCTA and Time Warner. (Verizon BR at 38; FCTA/Time Warner BR at 13)

FDN's recommended imposition of a minimum traffic volume of 500,000 minutes of use per month as a condition for a default symmetrical rate, appears ill-advised. Traffic flow data filed by BellSouth witness Shiroishi indicates 28 of the 62 ALECs with whom BellSouth reports exchanging traffic do not reflect traffic volumes of 499,999 minutes per month. (EXH 12, Item 3, Exhibit C) Similar data filed by Sprint witness Hunsucker shows two of the 26 ALECs with whom Sprint exchanges traffic do not reflect traffic volumes of 499,999 minutes per month. (EXH 3, MRH-1). Staff sees no reason to recommend a traffic volume standard that would interfere with the relationships among carriers or work to exclude carriers from participating in a bill-and-keep regime if the carriers determine such an arrangement is to their advantage.

In summary, it does not appear that FDN's vision of a bill-and-keep system predicated on the adoption of its local calling area default and the imposition of traffic volume standards for triggering compensation mechanisms reflects an awareness of the ramifications of its recommendation on other carriers. Staff cannot, therefore, recommend its adoption.

No other parties to this docket recommend adoption of a bill-and-keep default mechanism. Sprint witness Hunsucker and all other ALEC witnesses other than FDN oppose adoption of a bill-and-keep default on a number of grounds. Verizon witness Trimble advises restraint in the presence of the FCC's Notice of Proposed Rulemaking (*Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, FCC 01-132), which he testifies will consider all compensation schemes, including bill-and-keep.

Among the arguments raised in opposition to adoption of bill-and-keep are those of creating regulatory arbitrage opportunities, a dispute over whether savings will accrue to carriers engaged in bill-and-keep systems, projected losses by ALECs from loss of compensation for transporting and terminating ILEC traffic, and a debate over whether the adoption of bill-and-keep will lead to more or less regulatory intervention.

On the issue raised by Verizon witness Trimble - of holding matters in abeyance until the FCC completes a comprehensive review of intercarrier compensation - staff finds little merit. In fact, the FCC itself rejected a similar argument advanced by ALECs in FCC 01-131, ¶94:

> Some CLECs take this argument one step further. Whatever the merits of bill and keep or other reforms to intercarrier compensation, they say, any such reform should be undertaken only in the context of a comprehensive review of *all* intercarrier compensation regimes, including the interstate access charge regime. First, we reject the notion that it is inappropriate to remedy some troubling aspects of intercarrier compensation until we are ready to solve all such problems.

Staff acknowledges witness Trimble's concern that a policy decision in this docket may be subject to subsequent revisions by the adoption of a federal standard should the two conflict. Staff cannot recommend rejection of a bill-and-keep default, however, solely because the FCC may deliver an ultimate solution at an unspecified future date. Instead, staff believes, its recommendation must be based on the relative merits or shortcomings advanced by the parties in the record of this proceeding.

AT&T witness Cain testifies he believes the adoption of a bill-and-keep default mechanism will encourage regulatory arbitrage by causing carriers to seek out customers who originate more calls than they receive, such as telemarketers. (TRa 222-223) This view is shared by US LEC. (US LEC BR at 11) Verizon witness Trimble sees no merit in AT&T witness Cain's assertion and contends it is not based in fact. (TRa 139) Similarly, witness Trimble testifies (TRa 138), there is no evidence to support FCTA witness Barta's belief that bill-and-keep offers ILECs superior bargaining power in negotiations. (TRa 244)

Staff concurs with witness Trimble's observation that no factual evidence exists in the record to support claims that adoption of a bill-and-keep default will unfairly advantage ILECs in negotiations or lead to regulatory arbitrage opportunities. In addition, staff notes the ALEC witness' assertions may be deflected by the testimony of BellSouth witness Shiroishi, who lists a number of ALECs that have entered into bill-and-keep relationships with BellSouth and for which no evidence of coercion or arbitrage exists. (TRa 30)

The issue of whether a bill-and-keep default mechanism offers savings to carriers by eliminating transaction costs is one on which the parties do not agree.

Sprint witness Hunsucker testifies significant investment in Sprint's 18-state billing system has already been made, and a switch to bill-and-keep in one of those states will do little to alter the cost to maintain the system. (TRa 201)

Verizon witness Trimble believes some transaction costs would be avoided with bill-and-keep and some savings could be realized (TRa 115). FDN witness Warren testifies that bill-and-keep would minimize billing and collection costs and would allow ALECs to refocus resources on competitive activities. (TRa 269)

FCTA witness Barta does not dispute that some transaction costs would be avoided under a bill-and-keep system. Witness Barta believes, however, other costs, such as administrative and marketing costs, would rise under bill-and-keep. (TRa 243)

Staff believes the testimony on the issue of whether savings will inure to carriers under a bill-and-keep system is inconclusive. No party provides figures to support their contentions, and staff notes that efforts during the discovery phase of this proceeding to quantify the increased or decreased costs from adoption of a bill-and-keep regime yielded no specifics from the parties. Staff also notes that those carriers favoring adoption of a bill-and-keep default mechanism project cost savings while those opposing adoption of bill-and-keep as a default contend such a system will result in a net increase in costs. In the absence of data to support any of the positions assumed by the parties, staff cannot fully evaluate the respective claims.

Some of the ALEC parties testify conversion to a default bill-and-keep system will create financial losses, which they contend will result if they are not compensated for terminating the traffic of an interconnecting carrier.

AT&T witness Cain believes a default bill-and-keep system will adversely affect ALECs because they will remain responsible for transporting and terminating calls but will receive no compensation for performing these functions. (TRa 224) FCTA witness Barta shares this view. (TRa 247) Neither witness provides estimates or evidence in support of projected losses.

Indirect support for witness Cain and witness Barta's beliefs that ALECs may experience some financial losses by changing from reciprocal compensation to bill-and-keep may lie in the testimony of Sprint witness Hunsucker, who calculates Sprint would realize net gains of approximately $325,000 annually at current traffic volumes under a bill-and-keep system. Witness Hunsucker explains this is the amount Sprint would no longer pay to interconnected carriers that terminate Sprint's non-ISP traffic. (TRa 199)

Staff believes that while Sprint witness Hunsucker's analysis may corroborate the contentions of AT&T witness Cain and FCTA witness Barta, the analysis is difficult to place into perspective. As witness Hunsucker points out, Sprint elected to opt-in to the FCC's interim compensation regime and for that reason, is bound to exchange reciprocal compensation traffic at a rate of $.001 per minute. No other ILEC witness in this proceeding testified that their company opted-in to the FCC's interim compensation regime. For this reason, it is unknown what net gains, if any, would be realized by other ILECs if comparable analyses were performed.

The parties also debate the issue of regulatory intervention, specifically whether adoption of a bill-and-keep default mechanism will lead to a greater or lesser role for the Commission.

Sprint witness Hunsucker anticipates more regulatory intervention. Witness Hunsucker reasons that the imposition of bill-and-keep must be based on either a determination that traffic is roughly balanced or a presumption that traffic is roughly balanced, subject to rebuttal by a carrier. Because Sprint's data show traffic is not in balance, the Commission would have to presume subject to rebuttal that traffic is roughly balanced. This would open the door to rebuttal pleadings, potentially placing a greater workload on the Commission. (TRa 200)

AT&T witness Cain predicts a default bill-and-keep system will discourage good-faith negotiations because a party that expects to originate more traffic than it terminates would have no incentive to negotiate. (TRa 222) FCTA witness Barta mirrors this belief, testifying that ILECs, as originators of greater traffic volumes than ALECs, will have no incentive to negotiate because they will be "secure in the knowledge" that a bill-and-keep regime is the default. (TRa 244)

BellSouth witness Shiroishi appears ambivalent on this point. Witness Shiroishi testifies a bill-and-keep default would eliminate the need to address the "highly contentious" issue of compensation at the tandem interconnection rate, but could lead to disputes over traffic jurisdiction, whether traffic is roughly balanced, and "other tangential issues." (TRa 30)

Verizon witness Trimble expects less need for regulatory intervention except for disputes involving whether traffic is in balance. (TRa 115) FDN witness Warren shares the belief that less regulatory intervention would result from a bill-and-keep default "as long as the definition and terms of the bill and keep default are adequately specified by the Commission." (TRa 269)

CONCLUSION: Staff does not believe any of the parties make a compelling case for regulatory intervention in the form of adopting bill-and-keep as a default compensation mechanism.

The two proponents of bill-and-keep as a default mechanism - BellSouth and FDN - do not address potential revenue losses ALECs allege will result. Further, staff believes implementing

BellSouth's recommended presumption that traffic volumes below a 3:1 ratio be considered "roughly balanced" for a bill-and-keep default mechanism will lead to a round of regulatory proceedings by ALECs wishing to rebut the presumption. Staff is unpersuaded that the prescriptive approach proposed by FDN's minutes-of-use threshold for triggering a default symmetrical measurable rate mechanism is warranted.

Staff is unpersuaded by arguments that a bill-and-keep default will spawn regulatory arbitrage opportunities and finds claims of increased or decreased costs resulting from bill-and-keep vague and irreconcilable given the testimony. There appears to be some substantiation for the belief that a default bill-and-keep mechanism will enhance the financial positions of ILECs at the expense of ALECs, although the extent to which this would impact the overall competitive market is unclear based on the record. It does appear that given the traffic imbalances that exist between ILECs and ALECs, presuming that traffic is roughly balanced and imposing a bill-and-keep default will create, at least initially, a demand for regulatory intervention. None of these issues alone, or taken together, lead staff to its conclusion however.

Most persuasive to staff is a record reflecting that bill-and-keep arrangements exist between carriers that have determined the approach best suits their needs. Conversely, the record indicates a number of carriers continue to bill each other for reciprocal compensation. The simultaneous existence of both compensation schemes in the market leads staff to conclude that the parties involved in intercarrier relationships are best suited to determine what compensation mechanism is appropriate according to their unique circumstances.

Staff, therefore, does not recommend the imposition of a single compensation mechanism governing the transport and delivery or termination of traffic subject to Section 251 of the Act, to be used in the absence of the parties negotiating a compensation mechanism. While staff believes the Commission has jurisdiction to establish a bill-and-keep default mechanism subject to either a determination or a presumption that traffic between carriers is roughly balanced, the record of this proceeding does not support such a determination and argues against a presumption of balance. Should the Commission determine that the imposition of a bill-and-keep default system is desirable, staff recommends the Commission define roughly balanced to mean the traffic imbalance is less than 10 percent between parties in any three-month period.

ISSUE 19a: Should this docket be closed?

RECOMMENDATION: Yes. This docket should be closed upon the expiration of the time to file a motion for reconsideration or an appeal since no further action is required by the Commission. **(BANKS)**

STAFF ANALYSIS: This docket should be closed upon the expiration of the time to file a motion for reconsideration or an appeal since no further action is required by the Commission.