

State of Florida



Public Service Commission

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

DATE: August 7, 2007

TO: Office of Commission Clerk (Cole)

FROM: Division of Competitive Markets & Enforcement (Trueblood, Barrett, Lee, Ollila)
Office of the General Counsel (Tan, Teitzman)

RE: Docket No. 060767-TP – Petition of MCImetro Access Transmission Services LLC d/b/a Verizon Access Transmission Services for arbitration of disputes arising from negotiation of interconnection agreement with Embarq Florida, Inc.

AGENDA: 08/14/07 – Regular Agenda – Post-Hearing Decision – Participation is Limited to Commissioners and Staff

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: Carter

CRITICAL DATES: None

SPECIAL INSTRUCTIONS: None

FILE NAME AND LOCATION: S:\PSC\CMP\WP\060767.RCM.DOC

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Case Background

On November 27, 2006, MCImetro Access Transmission Services LLC d/b/a Verizon Access Transmission Services (Verizon Access) filed its Petition for Arbitration (Petition) of disputes arising from negotiation of an interconnection agreement (ICA) with Embarq Florida, Inc., (Embarq). On December 22, 2006, Embarq Florida, Inc., (Embarq) filed its Response to the Petition.

Docket No. 060767-TP was established in response to the petition filed by Verizon Access. The Order Establishing Procedure, Order No. PSC-07-0063-PCO-TP, issued on January 24, 2007, set forth the controlling dates for this matter. On April 9, 2007, the parties filed prehearing statements indicating that the parties had resolved two of the five outstanding issues through negotiation. An administrative hearing was held on May 3, 2007 to address the three remaining issues:

- Issue 1: What compensation should apply to virtual NXX Traffic under the Interconnection Agreement?
- Issue 4: When the Parties exchange traffic via Indirect Connection, if Verizon Access has not established direct end office trunking sixty days after reaching a DS1 level, should it be required to reimburse Embarq for any transit charges billed by an intermediary carrier for local traffic or ISP bound traffic originated by Embarq?
- Issue 5: What should apply to transit traffic under the parties' Interconnection Agreement?

Post-hearing briefs were filed on June 1, 2007. A recommendation was filed on July 19, 2007, addressing the three remaining issues. On July 26, 2007, Verizon Access filed a letter with the Commission Clerk notifying staff that the parties had resolved Issue 4 through negotiations. The joint letter stated that the Commission therefore does not need to vote on this issue.

At the July 31, 2007 agenda conference, the Commission voted to defer the recommendation to allow more time to consider additional information on Issue 1. Subsequent to the agenda conference, the analysis of the original recommendation for Issue 1 was revised to include additional information on the potential effects of parties' proposals on consumers and carriers and a set of three diagrams that illustrate a traditional local call, a traditional toll call, and a vNXX call. Issue 4 also was revised to strike through the entire issue since it has been resolved by the parties. This recommendation addresses the ~~three~~ two remaining issues that remain in dispute.

The Commission is vested with jurisdiction over this matter pursuant to Chapter 364.012(2), Florida Statutes, and Section 252 of the 1996 Telecommunications Act.

Discussion of Issues

Issue 1: What compensation should apply to virtual NXX Traffic under the Interconnection Agreement?

Recommendation: Staff recommends that the physical end points of a virtual NXX (vNXX) call determine the appropriate intercarrier compensation. If the physical end points of a vNXX call are within the local calling area, as defined in the parties' interconnection agreement, the call should be considered local for intercarrier compensation purposes. If one of the physical end points of the call is outside of the local calling area, the call should be considered interexchange and subject to originating access charges (billed by the carrier whose end user makes the vNXX call). (Ollila)

Position of the Parties

Verizon: Until the FCC decides the vNXX compensation issue in its ongoing rulemaking, the Commission should adopt for the parties' ICA the same kind of compensation approach carriers have negotiated in the absence of regulatory intervention, and that this Commission has approved for the BellSouth/Verizon ICA and many others.

Embarq: Consistent with Commission and FCC precedent, intercarrier compensation should be based on the physical location of the calling and called parties, not the NPA/NXXs. Any traffic that physically originates and terminates outside of Embarq's local calling area, including vNXX traffic, is interexchange traffic that is subject to access charges.

Staff Analysis: Virtual NXX (vNXX) service allows a CLEC's customer to obtain a telephone number in a local calling area (exchange) where it does not have a physical presence.¹ For an end user dialing the "virtual" number, the call appears to be local, even if the physical end point of the call is outside the end user's local calling area. A primary use of vNXX numbers is to provide local telephone numbers for dial-up Internet access. (Fox TR 41) In this proceeding, the parties agree that ISP-bound calls originated by Embarq customers are 100 percent or nearly 100 percent of vNXX calls. (EXH 3, p. 2; EXH 7, p. 69)

Issue 1 asks what compensation should apply for vNXX calls. As a point of reference, traditional non-vNXX calls between customers of an ILEC and a CLEC are compensated based on whether both physical end points of the call are in the local calling area (a local call). For example, if an ILEC's customer makes a local call to a CLEC's customer, the ILEC pays the CLEC to terminate (complete) the call. This charge is called reciprocal compensation under the Telecommunications Act of 1996, §251(b)(5). If the ILEC's customer makes a toll call to a CLEC's customer, the ILEC's customer incurs a toll charge, and the ILEC receives switched access charges. (Fox TR 42) The diagrams on the next page illustrate a traditional local call, a traditional toll call, and a vNXX call.

¹ NXX refers to the first three numbers of a seven-digit telephone number.

Diagram 1 - 1: Traditional Local Call

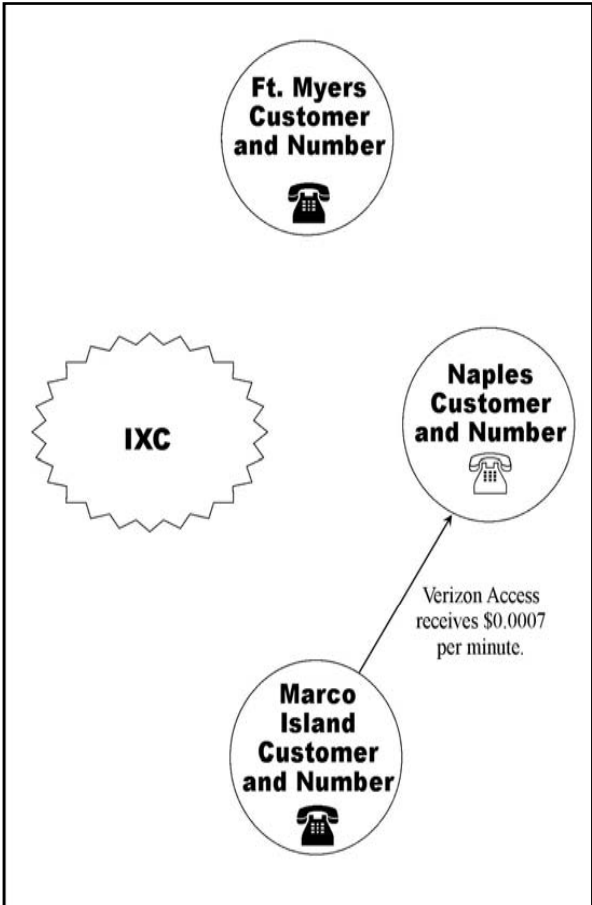


Diagram 1 - 2: Traditional Toll Call

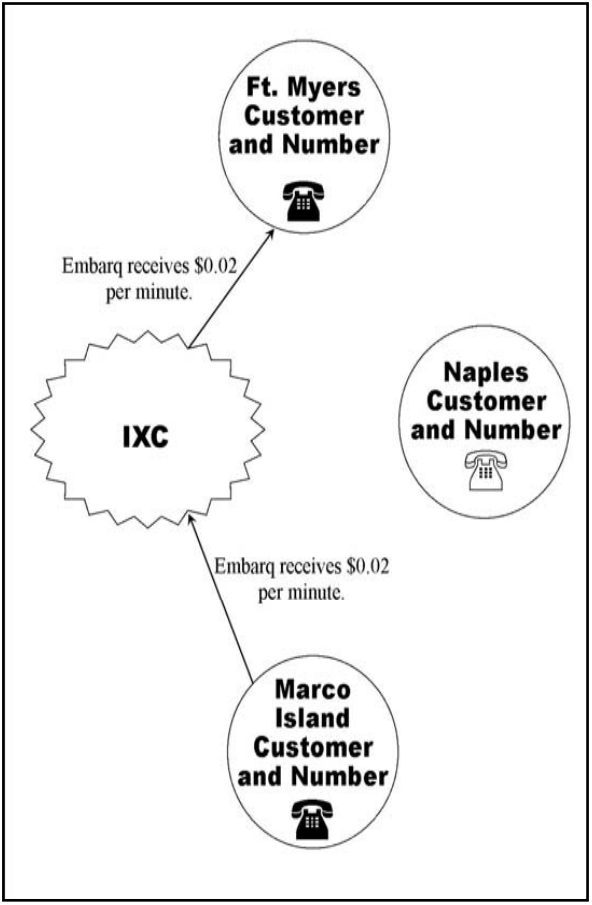
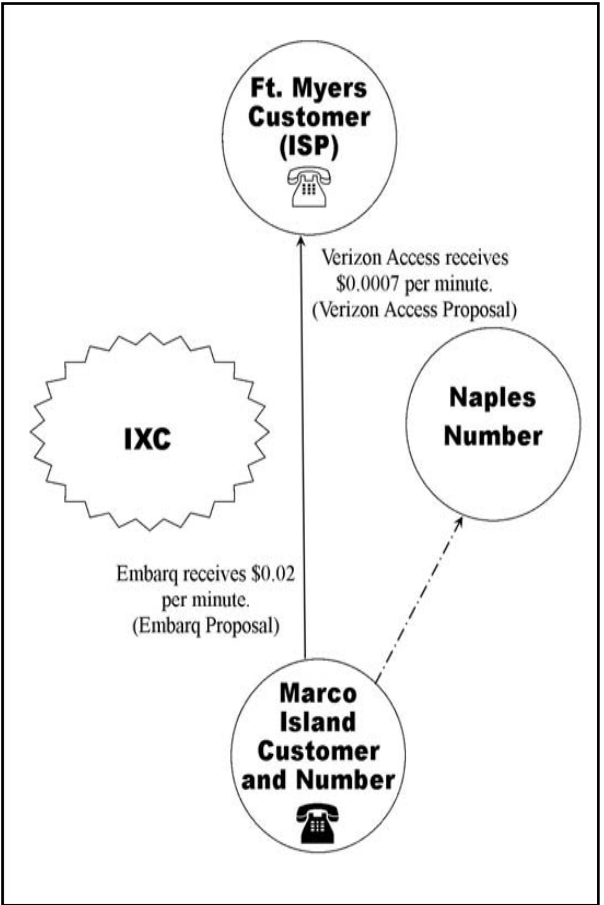




Diagram 1 - 3: vNXX Call



In Diagram 1, an Embarq customer in Marco Island makes a local call to a Verizon Access customer in Naples. Verizon Access receives \$0.0007 per minute from Embarq to terminate this call.

In Diagram 2, an Embarq customer in Marco Island makes an interexchange (toll) call to another Embarq customer in Ft. Myers using an interexchange carrier (IXC). Embarq receives \$0.02 per minute from the IXC for originating the call and \$0.02 per minute for terminating the call, a total of \$0.04 per minute.

In Diagram 3, an Embarq customer in Marco Island dials a local Naples number to reach his ISP, which is a Verizon Access customer. Although the call may appear local from the customer's perspective, in reality it is a vNXX call terminating in Ft. Myers. Verizon Access proposes that it receive \$0.0007 per minute from Embarq for this call. Embarq proposes that it receive \$0.02 per minute from Verizon Access for this call.

 Embarq Customer
 Verizon Access Customer

PARTIES' ARGUMENTS

Verizon Access' Proposal

Verizon Access witness Price devotes most of his testimony to explaining the history and network design of ILEC and CLEC networks, and how this has resulted in differing viewpoints on the appropriate compensation method for vNXX calls. (TR 10-16) According to witness Price, CLECs traditionally characterize all vNXX calls as local, while ILECs determine whether or not a vNXX call is local by using the physical end points of the call. (TR 15) Witness Price asserts that a traditional CLEC perspective would indicate that the CLEC receives reciprocal compensation for all vNXX calls because vNXX calls, by definition, are local. (TR 15) According to witness Price, the traditional ILEC perspective is that it should receive originating switched access charges for any vNXX call that is not local. (TR 15)

Verizon Access witness Price asserts that the FCC has expressed its intention to decide how vNXX calls should be compensated in its ongoing Intercarrier Compensation Rulemaking; however, as of the recommendation date, the FCC has not reached a decision. (TR 16) According to witness Price, any determination reached in a state arbitration should be considered interim until the FCC makes its decision, and the interconnection agreements should require rapid implementation of the FCC's decision. (TR 17) Staff notes that Embarq witness Fox asserts that the Commission has jurisdiction over non-local vNXX ISP-bound calls; therefore, the parties agree that the FPSC has the authority to determine the intercarrier compensation method for vNXX traffic. (TR 45-46)

The Verizon Access witness argues that the compensation method for vNXX calls should be addressed through "market-based solutions, rather than by resort to the usual, polarized win-lose paradigm of regulatory decision-making." (TR 17) Witness Price asserts that market-based solutions are the industry trend, and as evidence of that trend, he points to the vNXX compensation method recently agreed to by Verizon Access and BellSouth, and subsequently deemed approved by this Commission. According to witness Price, the Verizon Access-BellSouth method is what Verizon Access is proposing in this proceeding. (TR 17) Witness Price states that Verizon Access' proposal is similar to agreements reached by some large ILECs and CLECs, including Verizon Access and SBC (pre-merger with AT&T and BellSouth), Verizon and pre-merger MCI, Verizon and pre-merger AT&T, Verizon and Level 3, etc. (TR 18) According to witness Price, these multi-state agreements:

- Avoid the uncertainty of different outcomes in different states that may result from litigation;
- Eliminate multi-state carriers' billing and invoicing problems; and
- Allow the carriers "to appropriately weigh their own business interests." (TR 18)

Witness Price asserts that Verizon Access' market-based solution is a compromise whereby the CLEC receives compensation for handling vNXX calls originated by the ILEC, and in turn, the CLEC commits to accepting greater responsibility for transporting the traffic from the ILEC's end office. (TR 18) In Verizon Access' proposal, the rates it charges Embarq are determined on a per LATA basis, depending on whether its proposed condition is met within that LATA. Table 1 - 1 describes Verizon Access' compensation proposal as it applies to Embarq.

Table 1 - 1: Verizon Access' Proposal for vNXX Compensation

| | | | |
|--|---------------|--|---------------|
| <p>Condition: Embarq and Verizon Access have at least one point of interconnection (POI) for the exchange of traffic in each Embarq tandem serving area (within the LATA) where Verizon Access assigns telephone numbers to its customers.</p> <p>Embarq LATAs where the condition is met: The condition has been met in four LATAs: Pensacola (at Crestview and Fort Walton Beach), Gainesville (at Ocala), Orlando (at Winter Park), and Tallahassee (at Tallahassee) and partially met in one LATA (Fort Myers). In the Fort Myers LATA, Fort Myers has a direct connection and an order for a direct connection has been placed for Avon Park.</p> | | | |
| <p>LATA A – Condition Met</p> <p><u>Per Minute Rate Charged to Embarq</u></p> | | <p>LATA B – Condition NOT Met</p> <p><u>Per Minute Rate Charged to Embarq</u></p> | |
| ISP-Bound: | \$0.0007* | ISP-Bound: | Bill and keep |
| Voice: | Bill and keep | Voice: | Bill and keep |

*FCC's default rate for local ISP-bound traffic.

Source: TR 17-18; EXH 2, p. 17; EXH 6, p. 3; EXH 7, pp. 7-8

Embarq's Rebuttal to Verizon Access' Proposal

Embarq witness Fox asserts that a negotiated agreement involves give and take by both parties, and that Verizon Access has not provided substantive information to Embarq on the negotiating points and trade-off on specific issues, thus not allowing Embarq to judge the merits of Verizon Access' compromise solution. (TR 55)

Embarq witness Fox disagrees that Verizon Access' "compromise" provides anything meaningful to Embarq because Embarq still must transport the calls while Verizon Access "avoids" switching and transport costs. (TR 43) The Embarq witness argues that "demanding reciprocal compensation" only exacerbates the inequity. (TR 43)

Embarq witness Fox asserts that the physical end points of the call, whether it is a non-local, vNXX voice call or a non-local, vNXX ISP-bound call, determine the appropriate form of intercarrier compensation, i.e., reciprocal compensation or access charges. (TR 41) According to witness Fox, Embarq incurs the same network costs to deliver the non-local call to Verizon Access for a voice vNXX call or an ISP-bound vNXX call. (TR 43)

Embarq witness Fox further asserts that Verizon Access' "willingness" to provide transport (establish points of interconnection at each tandem serving area) is not a reasonable exchange for Embarq paying \$0.0007 per minute, thus treating all vNXX calls in the LATA as local. (TR 17, 56) Embarq argues that Verizon Access already must interconnect with Embarq if it wishes to receive Embarq's traffic. Verizon Access has already agreed to establish a minimum of one POI per LATA and to establish a direct end office trunk at an Embarq end office when the total traffic exchanged between Embarq and Verizon Access exceeds a DS1 equivalent at that end office. (TR 56) Therefore, Embarq argues, Verizon Access' offer to pay the costs of providing transport (by establishing one POI at each tandem serving area in a LATA where Verizon Access has customers) is "entirely self-serving." The offer, according to witness Fox,

does not fairly compensate Embarq for the “lost” access revenues Embarq would otherwise be due under “long-established regulatory principles.” (TR 56)

Embarq’s Proposal

Embarq proposes that it be compensated at originating access rates when its customers make vNXX calls that physically terminate outside of the customer’s local calling area. (Price TR 46) Embarq’s originating intrastate switched access charges are around \$0.02 per minute. (EXH 7, pp. 69-70) According to Embarq, terminating access rates would not apply to vNXX traffic. (EXH 3, p. 6) Typically, an interexchange or long distance carrier (IXC) is responsible for access payments to the originating and terminating carriers when end users make a toll call. However, when an Embarq customer makes a vNXX call to a Verizon Access customer, Verizon Access acts as both the IXC and the terminating carrier, thus removing the need for terminating access payments. (EXH 3, pp. 6-7)

Witness Fox asserts that with a vNXX code, CLECs can offer all their customers a locally-rated telephone number without establishing a physical presence. (TR 42) Without a vNXX number, according to witness Fox, the end user making the call would pay a toll charge, and the originating carrier would collect originating switched access. (TR 42) Witness Fox asserts that if a CLEC wants to provide a vNXX service, “it should not be at the originating ILEC’s expense.” (TR 42-43)

Witness Fox describes Embarq’s position as “reasonable” because the “historic end-to-end analysis confirms” that a call originating in a local calling area and terminating outside of that local calling area is not considered a local call for intercarrier compensation purposes. (TR 42) Witness Fox further asserts that if there were not a vNXX numbering “scheme,” the originating end user would incur a toll charge and the originating carrier would charge access to the terminating carrier. (TR 42)

According to witness Fox, two decisions by the Florida Public Service Commission (FPSC or Commission) support Embarq’s proposal that the physical end points of a call determine its compensation method. First, the FPSC decided in its generic reciprocal compensation proceeding (Generic Proceeding), that the physical end points of calls determine the compensation for non ISP-bound calls.² (TR 46) Second, the FPSC decided in an arbitration between FDN Communications and Embarq’s predecessor company, Sprint (FDN/Sprint Arbitration), that vNXX calls should be subject to access charges based on the end points of the calls.³ (TR 46)

In his testimony on Issue 1, witness Fox provides information on subjects that are not part of this issue, including how a CLEC assigns numbers outside the local calling area and number porting outside the assigned rate center. (TR 43-44) Witness Fox asserts that CLECs know they can “violate” the number portability rule. He avers that this “attempted cost-shifting is inequitable” and asserts that Embarq is entitled to collect switched access revenue. (TR 44) It is unclear to staff why witness Fox discusses the potential for a number portability rule violation by

² Order No. PSC-02-1248-FOF-TP in Docket No. 000075-TP.

³ Order No. PSC-06-0027-FOF-TP in Docket No. 041464-TP.

CLECs because 1) this topic is not an issue in this proceeding, and 2) in a discovery response, Embarq stated that it does not have knowledge as to whether or not Verizon Access is following the number portability rules. (EXH 3, p. 4)

Verizon Access' Rebuttal to Embarq's Proposal

Verizon Access witness Price asserts that Embarq witness Fox does not "correctly" understand Verizon Access' vNXX proposal because witness Fox describes Verizon Access' proposal as one that makes vNXX traffic subject to §251(b)(5) of the Telecommunications Act, thus requiring reciprocal compensation (the traditional CLEC proposal). (TR 27) Verizon Access witness Price asserts that Verizon Access has not argued that vNXX traffic is subject to §251(b)(5) of the Telecommunications Act. Witness Price also asserts that Verizon Access is not asking Embarq to pay reciprocal compensation for vNXX traffic. (TR 27-28)

According to witness Price, one of the "advantages" to Verizon Access' proposal is that it is not linked to specific legal definitions, thus avoiding the "usual" debates about the nature of vNXX traffic. (TR 28) Witness Price avers that Verizon Access' proposed compensation rate of \$0.0007 per minute is "several times" lower than the already agreed-upon reciprocal compensation rate. (TR 28)

Verizon Access witness Price asserts that Verizon Access' proposal "appropriately" balances ILEC and CLEC interests, contrary to Embarq witness Fox's testimony. (TR 29) Verizon Access witness Price avers that numerous "sophisticated" ILECs and CLECs have agreed to the "same kind" of solution as "compelling" evidence that ILEC and CLEC interests are appropriately balanced. (TR 29) According to witness Price, the Verizon ILEC in Florida has implemented similar agreements with CLECs such as KMC Data LLC, TelCove Investment LLC, Bright House Network Information Services, LLC, etc. (TR 29)

The Verizon Access witness argues that his approach addresses Embarq's concern about having to provide a "substantial" amount of transport because Verizon Access will receive no compensation where it does not have a POI in a tandem serving area. (TR 30) Witness Price asserts that in the arbitration between FDN and Embarq's predecessor company, Sprint, Sprint argued that establishing a POI at each tandem is the best approach to ensure a reasonable sharing of costs. (TR 30)

Witness Price reiterates that negotiated intercarrier compensation agreements are the industry trend and a better alternative to the "protracted, expensive" litigation long associated with vNXX compensation issues. (TR 30)

Verizon Access witness Price argues that prior Commission decisions in the Generic Proceeding and the FDN/Sprint Arbitration emphasize that the Commission has "explicitly" declined to mandate a specific intercarrier compensation mechanism for vNXX traffic. (TR 31) According to Verizon Access witness Price, Verizon Access is "not arguing that the law prohibits Embarq from doing this," that is, assessing access charges on interexchange vNXX calls. (EXH 7, p. 72) Rather, Verizon Access is "suggesting" that the Commission look to other carriers' agreements on this issue for guidance in the instant proceeding. (EXH 7, pp. 72-73)

Witness Price asserts that the Commission's policy favoring negotiation is consistent with Verizon Access' position and the industry trend that intercarrier compensation agreements are best negotiated by the parties. (TR 31) Verizon Access witness Price describes Embarq as "wedded" to the traditional ILEC view of compensation because it has refused to consider or acknowledge Verizon Access' compromise solution. (TR 31)

During his deposition, witness Price was asked, "You are saying if you had to pay access charges, you wouldn't have a virtual NXX for your ISP traffic, is that what you are saying?" He responded, "It is in the ballpark with what I'm saying." (EXH 7, p. 71) He explained his statement by saying that "you cannot take a volume of minutes that exist today where originating access charges are not paid and then assume that a Commission decision in favor of Embarq in this proceeding would result in that many minutes. . . . People will not use their computers in the same way if they would have to incur toll charges in order to reach their ISP." (EXH 7, p. 71)

ANALYSIS

Verizon Access argues that its proposal is a market-based compromise that enables Verizon Access to receive compensation for ISP-bound vNXX traffic if, and only if, it accepts greater responsibility for transporting traffic from Embarq's end office to its customer. (TR 17-18) Staff agrees with Embarq witness Fox's assertion that Verizon Access has not provided Embarq any "substantive" information on the negotiating points between Verizon Access and the other carriers that would permit Embarq to "judge the merits" of Verizon Access' proposal.⁴ Staff questions the relevancy of Verizon Access witness Price's discussion of the benefits of multi-state agreements to support a position for an issue that is in litigation.⁵ Staff notes that because Verizon Access has almost all of its required interconnection arrangements in place, Verizon Access' proposal results in exactly the same rate for non-local ISP-bound traffic as for local ISP-bound traffic (\$0.0007 per minute) in all but one Embarq LATA.

Verizon Access witness Price asserted in his deposition that if access charges were applied to interexchange vNXX calls, consumers would change the way they use computers. (EXH 7, p. 72) The witness assumed that application of access charges would translate into

⁴ In its brief, Embarq argues that Verizon Access' proposal is "conceptually no different from the 'pick and choose' right that the CLECs previously had under the Telecommunications Act of 1996." Under "pick and choose," CLECs could literally pick and choose different sections of different interconnection agreements. Embarq asserts that the Verizon ILECs "vigorously opposed pick and choose." The FCC eliminated pick and choose in 2004. (Embarq BR at 8-9) Verizon Access argues in its brief that nothing in the Commission's past decisions prevents the Commission from adopting Verizon Access' proposal. Verizon Access also argues that the Generic Proceeding and the FDN/Sprint Arbitration emphasize that the Commission has explicitly declined to mandate a particular intercarrier compensation mechanism for vNXX traffic. (Verizon Access BR at 8)

⁵ Verizon Access and Embarq recently litigated vNXX compensation in Ohio. On April 18, 2007, the Public Utilities Commission of Ohio (Ohio PUC) issued its Arbitration Award in its Verizon Access/Embarq proceeding. The Ohio PUC found that when an ISP-bound vNXX call originates or terminates outside Embarq's local calling area, the call is considered to be an interexchange call, and thus access charges apply. The Ohio PUC stated, "Given that an ILEC must perform the exact same functions when originating a voice vNXX call and an ISP-bound vNXX call, the Commission sees no reason to treat these two types of calls differently, absent FCC preemption." (EXH 6, p. 16)

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consumers having to pay toll charges to access the Internet, yet provided no evidence to support this inference.

The implementation of either Verizon Access' proposal or Embarq's proposal may affect consumers and carriers. Staff has analyzed both proposals with regard to any potential downstream impacts, although these impacts were not expressly addressed in the record.

Potential Effect of Verizon Access' Proposal on Consumers

Implementation of Verizon Access' proposal is likely to reduce Embarq's access charge revenue. During the deposition of the Verizon Access witness, the Embarq attorney asked the witness to assume an approximate access rate of \$0.02 per minute and approximately 75 million minutes per month. (EXH 7, pp. 69-70). Using the Embarq attorney's assumptions, Embarq's potential vNXX access revenue would be \$1.5 million per month. If Embarq instead were to seek to recoup this amount through rate increases in basic or nonbasic services, some or all of Embarq's end user customers might see rate increases in their local service.

Potential Effect of Verizon Access' Proposal on Carriers

If Verizon Access' proposal is implemented, it is likely to result in dissimilar rate treatment for Verizon Access and long distance carriers. How this occurs can be illustrated with an example. A Marco Island Embarq customer (customer) dials his ISP's "local" vNXX number (e.g., a Naples number). When the vNXX number physically terminates outside the customer's exchange, such as in Fort Myers, Embarq would pay Verizon Access \$0.0007 per minute. However, when the same customer calls a doctor's office in Fort Myers, the customer's long distance carrier (e.g., AT&T) would pay Embarq originating access of \$0.02 per minute and terminating access of \$0.02 per minute.

Potential Effect of Embarq's Proposal on Consumers

Any potential effects of Embarq's proposal would be limited to those Embarq local service customers who use dial-up Internet access where the ISP is a Verizon Access customer and where the physical end point of the vNXX number is outside the customer's local calling area. Whether these consumers see any effects depends on:

1. Whether Verizon Access can flow through the access charges it would be billed to its customers, the ISPs (e.g., if there are contracts and do the contracts permit flow-throughs).
2. If Verizon Access can flow through the charges, it must decide whether or not it will do so.
3. If Verizon Access decides to flow through the charges to the ISPs, then the ISPs need to decide whether or not they can flow through charges (many ISPs have nationwide rates).

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4. If the ISPs decide to flow through the charges, they need to decide how to do so (e.g., rate increase, rate surcharge, or addition of a per minute surcharge).

Finally, if the access charges are flowed through to the ISPs' end user customers, then the customers must decide what to do, e.g., pay the increase, search for another ISP, purchase broadband, if available, or disconnect service.

Potential Effect of Embarq's Proposal on Carriers

It appears likely that implementation of Embarq's proposal would result in consistent application of access charges between Verizon Access and the long distance carriers operating within the same LATA.

Prior Commission Decisions

The FPSC has rendered decisions on vNXX compensation in at least two prior proceedings, the Generic Proceeding and the FDN/Sprint Arbitration. At the time the Commission rendered its decision in the Generic Proceeding, state commissions were preempted by the FCC from addressing issues regarding ISP-bound traffic. Almost all of the vNXX traffic in this proceeding is ISP-bound; however, staff believes the order from the Generic Proceeding provides compelling guidance because it determined that the physical end points of a call determine the classification and thus the compensation of a call, regardless of whether the call is rated as local or toll for the end user. The Commission stated in part:

We believe that the classification of traffic as either local or toll has historically been, and should continue to be, determined based upon the end points of a particular call. We believe this is true regardless of whether a call is rated as local for the originating end user (e.g., 1-800 service is toll traffic even though the originating customer does not pay the toll charges). We acknowledge that an ILEC's costs in originating a virtual NXX call do not necessarily differ from the costs incurred originating a normal local call. However, we do not believe that a call is determined to be local or toll based upon the ILEC's costs in originating the call. In addition, we do not believe that the proper application of a particular intercarrier compensation mechanism is based upon the costs incurred by a carrier in delivering a call, but rather upon the jurisdiction of a call as being either local or long distance.⁶

In the FDN/Sprint Arbitration, both parties agreed that the end points of a call determine whether a call is local or not.⁷ FDN's issue in that arbitration was that any compensation should be reciprocal – that is, both FDN vNXX and Sprint's similar Foreign Exchange (FX) traffic should be compensated in the same manner without regard to whether a Sprint or FDN customer originated the call.⁸ In the FDN/Sprint Arbitration, vNXX service was described as typically

⁶ Order No. PSC-02-1248-FOF-TP in Docket No. 000075-TP at 30.

⁷ Order No. PSC-06-0027-FOF-TP in Docket No. 041464-TP at 37.

⁸ Id.

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used by a CLEC to connect its customer to dial-up Internet service.⁹ The Commission ordered the reciprocity language and concluded that the end points of a call determine the intercarrier compensation method.¹⁰ Staff believes that the FDN/Sprint Arbitration order also provides strong guidance even though the parties had agreed to the end points of a call as the determining factor in intercarrier compensation.¹¹

~~Staff is appreciative of Verizon Access' effort to craft a compromise on vNXX intercarrier compensation; however, staff believes that Verizon Access does not provide convincing evidence that vNXX intercarrier compensation should be determined without regard to the physical end points of a call. Staff believes that using the past Commission decisions as a guide, the physical end points of a vNXX call determine jurisdiction and thus the appropriate form of intercarrier compensation.~~

Summary

At first glance, the potential effect of Embarq's proposal on consumers appears to be confined to the subset of customers that use the ISPs with whom Verizon Access does business. Although it is unclear how large this group of customers is, these customers appear to have competitive options available to them if their ISP rates are increased, although none of those options may be appealing to them. Upon closer examination of Verizon Access' proposal though, more Embarq customers could be at risk for rate increases if Embarq decides to recoup what it might consider its foregone or "lost" access revenue. In considering which proposal is "better" for consumers, staff believes that when downstream effects cannot be known with certainty, the more conservative approach is to:

- Limit any changes in rates so that the potential for increases in local service rates is minimized; and
- Keep any potential rate increases for other services, such as dial-up Internet access, to as small a group as possible.

Due to the wide range of possible outcomes, the downstream effects on consumers of either proposal cannot be known with any degree of certainty; however, staff believes the potential impacts on Embarq's end users under Verizon Access' proposal is more disturbing because a larger group of consumers may see increases in local service rates.

The potential effect of Verizon Access' proposal on the long distance carriers carrying interexchange intraLATA traffic is troubling to staff because different carriers performing the same function, transporting and delivering traffic that terminates outside the exchange boundary, would be treated differently for intercarrier compensation purposes.

⁹ Id., at 36.

¹⁰ Id., at 38.

¹¹ According to its brief, Embarq "strongly disagrees" that the parties' agreement to physical end points determining the intercarrier compensation "renders the FDN decision inapplicable to the instant case." (Embarq BR at 4)

Verizon Access attempted to craft a compromise on vNXX intercarrier compensation; however, staff believes that Verizon Access' proposal may have far-reaching unintended consequences, affecting a much larger group of consumers and their local service rates, than Embarq's proposal. Staff is also concerned about the potentially dissimilar treatment between Verizon Access and long distance carriers with regard to intraLATA access charges. In sum, staff believes that Verizon Access does not provide convincing evidence that vNXX intercarrier compensation should be determined without regard to the physical end points of a call. Therefore, for this arbitration, staff believes that, using the past Commission decisions as a guide, the physical end points of a vNXX call is the most appropriate method to determine jurisdiction and thus the appropriate form of intercarrier compensation. If the physical end points of a vNXX call are within the local calling area, as defined in the parties' interconnection agreement, the call should be considered local for intercarrier compensation purposes. If one of the physical end points of the call is outside of the local calling area, the call should be considered interexchange and subject to originating access charges (billed by the carrier whose end user makes the vNXX call).

The Verizon Access witness argues that the Commission should adopt its proposal until the FCC renders a decision on intercarrier compensation. Embarq addressed this point in its brief, where it argues that because it is unclear if and when the FCC will address vNXX compensation, the Commission should resolve the issue without regard for possible FCC actions. (Embarq BR at 9) As it is unclear when the FCC will address vNXX intercarrier compensation, staff believes the Commission should resolve this issue here.

CONCLUSION

Staff recommends that the physical end points of a virtual NXX (vNXX) call determine the appropriate intercarrier compensation. If the physical end points of a vNXX call are within the local calling area, as defined in the parties' interconnection agreement, the call should be considered local for intercarrier compensation purposes. If one of the physical end points of the call is outside of the local calling area, the call should be considered interexchange and subject to originating access charges (billed by the carrier whose end user makes the vNXX call).

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Issue 4: ~~When the parties exchange traffic via indirect connection, if Verizon Access has not established direct end office trunking sixty days after reaching a DS1 level, should Verizon Access be required to reimburse Embarq for any transit charges billed by an intermediary carrier for local traffic or ISP-bound traffic originated by Embarq?~~

Recommendation: ~~No, although the language to implement direct end office trunks should, at a minimum:~~

- ~~▪ include a 90-day timeframe for establishing direct trunks;~~
- ~~▪ state that this timeframe is extendable if facility, equipment requirements, or related problems with the trunking order cause a delay that is attributable to Embarq;~~
- ~~▪ state that this timeframe is extendable if facility, equipment requirements, or related problems with the trunking order cause a delay that is attributable to a third party; and~~
- ~~▪ specify that the timeframe starts when all ordering requirements are fulfilled. (Barrett)~~

Position of the Parties

Verizon: ~~No. Verizon Access already agreed to establish direct trunks within the agreed-upon timeframe, and Embarq has shown no need for its unprecedented self-enforcing penalty. Verizon Access should not be forced to pay Embarq's transit bills, because Verizon Access alone cannot control the timeframe for establishing direct trunks.~~

Embarq: ~~Embarq's language requires Verizon Access to pay any transit charges incurred by Embarq if Verizon Access fails to establish direct connection within a certain time frame, as agreed to by the parties. This specific enforcement mechanism is designed to provide a reasonable incentive for Verizon Access to comply with the direct connection requirement.~~

Staff Analysis: ~~Embarq has proposed language that addresses the exchange of transit traffic, a portion of which involves the reimbursement of transit charges¹² under specific circumstances. Staff believes the reimbursement portion (of Embarq's proposed Section 61.2.4) is the main focus in Issue 4, although there are numerous related considerations developed in the parties' arguments.~~

PARTIES' ARGUMENTS

~~Verizon Access witness Price begins his argument by explaining the trunking options for transit traffic. He asserts that two carriers may agree to directly interconnect their networks, which is efficient from a traffic engineering perspective when a large volume of traffic is exchanged between the networks, but may not be when the traffic volumes are low. (TR 19; EXH 7, p. 101) In low volume scenarios, the viable alternative is to exchange traffic using a~~

¹²~~When indirect traffic flows from Embarq to Verizon Access, Embarq is the "originating carrier" and Verizon Access is the "terminating carrier." In a traditional compensation scheme, the originating carrier (Embarq, in this example) is the party that incurs transit charges. (TR 20, 58-59) Although the terminating carrier (Verizon Access) does not incur transit charges, staff notes that it could bill the originating carrier terminating charges.~~

~~third party with which each carrier has a direct connection, typically a transit provider. Witness Price states a DS1 level¹³ is an appropriate threshold to distinguish low and high traffic volumes. According to the witness, implementing a direct connection would eliminate the traffic flow to the transit carrier. (Price TR 20; EXH 7, pp. 30-31) In a discovery response that examined the relative traffic volumes between the parties, Embarq reports that none of its end offices routed a high volume of indirect traffic to Verizon Access.¹⁴(EXH 3, p. 8)~~

~~According to Verizon Access witness Price, the parties have agreed to the DS1 threshold for replacing indirect connections. (EXH 7, p. 28; EXH 2, p. 18; BR at 9) Once indirect traffic levels reach that threshold, Verizon Access is required to establish direct end office facilities within a specific timeframe. (EXH 7, p. 28; EXH 2, p. 18; EXH 6, p. 5; BR at 9) If direct trunking is not established, witness Price claims the language in Embarq's proposal permits Embarq to consider requiring Verizon Access to reimburse it for transit charges, which he strenuously challenges. He contends Embarq's proposal:~~

- ~~▪ holds his company responsible for delays over which Verizon Access has no control;~~
- ~~▪ is unprecedented as a provision in an interconnection agreement and may be contrary to FCC rule 51.703(b); and~~
- ~~▪ adds a secondary "dispute resolution process." (Price TR 21-22, 35-36; EXH 2, p. 18; EXH 7, pp. 104-105)~~

Delays and Third Party Responsibility

~~Verizon Access witness Price states that since the work effort to establish direct trunks is "a joint undertaking," no single party can or should control the process. (TR 22, 35) He claims that under the Embarq proposal, Embarq would have exclusive control over its contribution to the overall work effort, while at the same time holding Verizon Access to a stringent time requirement and the possible consequences for nonperformance. The witness contends that this is "patently unreasonable." (Price TR 22) According to the witness, this concern also applies to third parties, when such entities are working on his company's behalf. (Price TR 35)~~

~~Embarq argues that its proposed language is necessary as a "specific financial incentive" to encourage Verizon Access to meet its contractual obligation. (Fox TR 59) Witness Fox asserts that when indirect traffic flows from Embarq to Verizon Access, Embarq is the party that incurs the transit charges, and as a result, suffers when Verizon Access fails to establish a direct connection in a timely manner. (TR 59) The Embarq witness states that for qualifying traffic, his company may have to pay "twice" for each minute of traffic, once to Verizon Access for reciprocal compensation, and again to a transit provider. (Fox TR 47-48) The Verizon Access witness claims that Embarq's assertions are unsubstantiated. (Price TR 33-34)~~

¹³ According to witness Price, DS1 is a term used to describe a certain transmission level. It is typically thought of as 24 voice grade channels. In digital terms, DS1 and T-1 both operate at a transmission speed of 1.544 megabits per second. (EXH 7, p. 120)

¹⁴ Embarq studied usage data for January 2007.

~~In his deposition, witness Price claims an Embarq ordering process is also a factor in causing delays. He contends that a “customer profile” must be established before Embarq will accept orders for trunks, which he believes unnecessarily lengthens the time period for establishing such trunks. (EXH 7, pp. 27, 32, 65-66) He states, “the clock starts long before an order can even be placed for new trunking.” (EXH 7, p. 27) Embarq witness Fox answers this and other concerns. (TR 57; EXH 8, p. 14) He states that Embarq must accept the profile before the clock would start, and offers to develop language to specifically address that concern. (EXH 8, pp. 22, 61)~~

~~Embarq witness Fox claims that when facilities are available and there are no construction or extraordinary engineering concerns, Embarq can establish direct connections 14 days from the date an order is received. (TR 49) Witness Fox believes Embarq’s proposed language is clear in stating that Verizon Access will not be billed, nor will the “clock” start, for delays attributable to Embarq. (EXH 8, pp. 14-15, 23) He also addresses the topic of third-party responsibility in asserting that “Verizon Access will not incur the transit costs **when delays are not its fault.**” (Fox TR 49)(emphasis in original) According to witness Fox, the 90-day requirement is proposed in order “to make sure there is movement” in meeting the contractual obligations. (EXH 8, p. 15) He asserts that Embarq has been receptive to the concerns Verizon Access has raised with it, and points to its modified language proposal, which:~~

- ~~▪ has a 90-day window for action instead of 60;~~
- ~~▪ **allows the 90-day window to be extended “for an appropriate period” if the delay is attributable to Embarq;**~~
- ~~▪ **waives the reimbursement requirement if a delay is attributable to Embarq.** (Fox TR 48-49, 58) (emphasis in original)~~

Unprecedented in an Interconnection Agreement and Contrary to FCC rule

~~According to witness Price, the parties agree to the industry standard arrangement for transit billing whereby the transiting carrier bills the originating carrier (e.g., Verizon Access) for transiting the originating carrier’s traffic to another carrier (e.g., Embarq). (TR 19-20) The proposed language, however, departs from this because it contains a reimbursement mechanism that hinges upon the timing of establishing direct end-office facilities.¹⁵ He states those provisions do not exist in any other Embarq ICA. (EXH 7, p. 63; BR at 9-10) The witness claims~~

~~[The change] would require Verizon Access to pay all transiting charges, even those the transiting carrier charges Embarq for **handling Embarq’s own originated traffic.** If Embarq’s proposal is accepted, Verizon Access will, therefore, end up paying transit in **both** directions (to the third party for Verizon Access’s originating traffic and to Embarq for Verizon Access’s terminating traffic). (Price TR 20-21)(emphasis in original)~~

¹⁵ The wording of Issue 4 and the earliest proposal from Embarq state that the timeframe for establishing direct end-office facilities is sixty days; subsequent proposals have revised that timeframe to ninety days.

~~According to witness Price, there are numerous examples where CLECs have agreed to either implement direct interconnection or to pay the transit charges for traffic, but not do both. (EXH 7, pp. 29, 40; BR at 10)~~

~~In addition, witness Price believes Embarq's unprecedented proposal may be contrary to FCC rule 47 C.F.R. § 51.703(b), which restricts the extent to which an incumbent LEC (like Embarq) may charge other carriers for traffic originated on its network. (TR 21, 35-36) Although witness Price did not offer a language proposal, Verizon Access's response to staff Interrogatory 12(b) states that Issue 4 could be resolved by "deleting Embarq's proposed addition to Section 61.2.4 that would require Verizon [Access] to reimburse Embarq's transit charges." (EXH 2, p. 18) Embarq witness Fox contends that the concerns over the FCC rule are meritless. (TR 57) In its brief, Embarq states that Verizon Access "is misusing the rule" for its own purposes. (BR at 12)~~

~~According to Embarq witness Fox, Embarq made a small but significant change to its language proposal to highlight the distinction between its proposal and the FCC rule in question. An early iteration of Embarq's proposal states that Verizon Access "will reimburse Embarq for" transit charges, but the most recent version appears to have more latitude in stating "Embarq may require CLEC [Verizon Access] to reimburse Embarq for transit charges." (TR 48-49, 58; BR at 12)(emphasis in original) In its brief, Embarq makes the point that it is not "assessing" a direct charge on Verizon Access, which is squarely what FCC rule 47 C.F.R. § 51.703(b) addresses. (BR at 12) Embarq believes this is significant because an "assessment" is not the same thing as a "reimbursement." According to its brief, Embarq believes this distinction satisfies the allegations from Verizon Access that Embarq's reimbursement requirement violates the FCC rule. (BR at 12)~~

~~Embarq witness Fox soundly answers the claim from Verizon Access that this language is "unprecedented." (EXH 8, p. 16) He notes that this very issue was one of two that Embarq recently arbitrated with Verizon Access in Ohio.¹⁶ The witness states that the settlement in that venue "went in Embarq's favor," and that as of the date of his deposition in this case (April 25, 2007), the parties were finalizing contract language. (EXH 8, pp. 16-17)~~

Dispute Resolution Concerns

~~Witness Price states that general dispute resolution provisions give the parties an opportunity to resolve differences and are intended to apply to all aspects of the parties' obligations and responsibilities under the interconnection agreement, including this one. (TR 34; EXH 7, pp. 60, 83) He believes that Embarq's proposed language effectively adds a second dispute resolution process to address transit traffic exclusively. (Price TR 22, 32-33)~~

¹⁶ Petition of Verizon Access for Arbitration of an Interconnection Agreement with Embarq, Ohio PUC Case No. 06-1485 TP ARB ("Ohio case"). Florida is the second venue for these parties to arbitrate this issue. Staff notes that the language proposal in evidence here conforms to the Ohio arbitrator's decision. (EXH 6, p.5) In its brief, Verizon Access states that the "Ohio Order provides little meaningful guidance" for this Commission. (BR at 15) Staff agrees.

~~Witness Fox states that the Embarq proposal “supplements” the existing dispute resolution language and is necessary to provide a specific enforcement mechanism “for Verizon Access’s noncompliance.” (TR 59) According to Embarq’s witness, his company incurs transit expenses until direct connections are established, and without the time factor as a motivator, Verizon Access has very little economic incentive to timely establish the direct interconnection required by their agreement. (Fox TR 59; EXH 8, p. 15; BR at 11) In its brief, Embarq claims that if a dispute involving this subject matter came before the Commission pursuant to the conventional dispute resolution process, this body could make a finding, but would not have the jurisdiction to award monetary damages. (BR at 14) In his deposition, witness Fox was asked if Embarq had ever engaged the conventional dispute resolution process to address a failure to establish direct connections in a timely manner, and the response was negative. (EXH 8, p. 20) Witness Fox asserts that other options would be exhausted before the “very last resort” option of formal dispute resolution. (EXH 8, p. 22)~~

ANALYSIS

~~There appears to be no disagreement between the parties regarding the obligation of Verizon Access to establish a direct interconnection with Embarq’s end office for the mutual exchange of traffic once the specified traffic threshold is met. Staff believes the disagreement in Issue 4 is whether Embarq should be permitted to impose a specific incentive (or penalty) on Verizon Access with respect to the obligation.~~

~~From Embarq’s perspective, this issue is straightforward. The Embarq witness claims incentive language is there “to make sure there is movement” from Verizon Access in meeting its contractual obligations. (EXH 8, p. 15) Although Embarq describes its proposal as an “incentive” and Verizon Access describes it as a “penalty,” staff notes that the reimbursement requirement is only engaged when, or if: 1) indirect traffic has exceeded a DS1 level; 2) Verizon Access has not established a direct connection pursuant to its agreement to do so, and; 3) their reasoning for not doing so is due to something within Verizon Access’ control. (EXH 6, p. 5) Embarq believes its proposal provides “consequences to Verizon Access if it breaches its agreement to establish direct trunks.” (BR at 14) Witness Fox states that any amount Verizon Access would incur under the terms and conditions of Embarq’s proposed language “would be due solely to Verizon [Access]’s failure to comply with the terms of the ICA.” (Fox TR 57)~~

~~Staff notes that “time factors” were discussed extensively. Because the provisioning of direct end office trunks is a joint initiative, staff acknowledges that engineering and facilities-related concerns can impact the timeframe. Staff believes Embarq recognized this as well, by changing the timeline in its language proposal from 60 to 90 days. (Fox TR 48; EXH 7, p. 31) In his deposition, Verizon Access witness Price was asked about time factors, and instead of addressing Embarq’s current proposal (with a 90-day timeline), he instead expresses a concern about whether or not the language would, or could, make an accommodation for third party responsibility.¹⁷ (EXH 7, pp. 32-33) Because Embarq’s current proposal squarely addresses third party responsibility, staff believes the timeframe overall has become a less noteworthy concern~~

¹⁷ Embarq’s earlier proposal did not make an accommodation for third party responsibility, but the more recent one does.

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to Verizon Access. Significantly, staff points out that Embarq also added a provision that the 90-day timeline may be extended, if necessary. (EXH 6, p.5)

Staff believes another noteworthy change to the proposal was the clarification by Embarq regarding delays attributable to itself. Specifically, Embarq proposes that the reimbursement requirement be suspended if a provisioning delay greater than 90 days is attributable to Embarq. (EXH 6, p.5) Embarq also committed to add language to answer the "customer profile" concern identified by Verizon Access witness Price. (EXH 7, pp. 27, 32, 65-66) In his deposition, Embarq witness Fox agreed to include contract language that "the 90-day clock" would not start until that ordering requirement (for a "customer profile") was met. (EXH 8, p. 61)

According to Embarq's brief, the monies at issue represent "an appropriate measure of damages" for Verizon Access if it breached its commitment to establish direct end office facilities in the specified timeframe. (BR at 12) However, staff questions the need for Embarq to "build in" a specific remedy solely to address this aspect of its agreement with Verizon Access. First, staff notes that Embarq made broad, sweeping assertions regarding its experience with establishing direct end office facilities with other carriers; it did not offer evidence or documentation to substantiate a track record of difficulties with Verizon Access. (TR 47) Second, staff does not believe it is appropriate for Embarq to unilaterally decide what "an appropriate measure of damages" should be. Although Embarq acknowledges its obligation to pay the appropriate transit charges for *all* of its originated traffic, it contends that when it does so for DS1 and up volume levels, it is experiencing an "inequity of financial risk." (BR at 16) While it appears inequitable, staff does not agree it justifies its own remedy plan. Third, although the parties conceptually agree on the DS1 threshold, the data in evidence indicates that current traffic levels are lower than that. (EXH 3, p. 8; EXH 8, p. 51) Although Verizon Access expresses a concern about "spikes," or fluctuations in traffic volumes, Embarq conveys a willingness to make accommodations in that regard. (Price TR 22; Fox TR 58; Embarq BR at 14) Staff does not believe that a provision intended to address a "high volume" scenario is necessary when traffic volumes are well below that threshold. Even if the traffic volumes were higher, staff notes that Embarq has never pursued formal dispute resolution¹⁸ to expedite the construction of direct end office trunks. (EXH 8, pp. 19-22) Fourth, evidence demonstrates that Embarq and Verizon Access currently have a robust network of direct connections throughout Florida. According to a discovery response, only one area in Florida is not covered by such connections, but orders are pending to establish direct arrangements there. (EXH 2, p. 17; Verizon Access BR at 12)

Staff agrees with witness Price that a single dispute resolution provision should govern all aspects of the parties' obligations and responsibilities under the interconnection agreement, including this one. (Price TR 34; EXH 7, pp. 60, 83) Nonetheless, staff believes that the entire discussion about a specific remedy and dispute resolution is a moot point if all provisions between the parties are followed.

The final and perhaps most significant concern staff has is that a portion of Embarq's language may not comply with 47 C.F.R. §51.703(b). Staff believes Embarq's argument for its

¹⁸ Speaking generally, witness Fox claims Embarq would have extensive discussions with a carrier before it would pursue a formal resolution. (EXH 8, pp. 19-22)

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~~reimbursement requirement is flawed since the transit charges Embarq would like to have “reimbursed” were assessed on it as an originating carrier. Staff believes any further reassignment of such charges may violate rule 47 C.F.R. §51.703(b). That rule states:~~

~~§51.703 Reciprocal compensation obligations of LECs.~~

~~(b) A LEC may not assess charges on any other telecommunications carrier for telecommunications traffic that originates on the LEC’s network.~~

~~Although staff believes 47 C.F.R. §51.703(b) addresses reciprocal arrangements for the exchange of traffic, staff is concerned that Embarq’s reimbursement requirement may be a “back door” method of skirting this rule. Staff believes rule 47 C.F.R. §51.703(b) is clear on its face, and notes that the application of that rule was addressed in a recent Commission Order. (See Order No. PSC 06-0776 FOF TP, pp. 22-24) In that Order, the Commission ruled that an originating carrier is responsible for the payment of transit charges. Significantly, the Commission found that “any decision to the contrary would appear to conflict with 47 CFR 51.703(b), which prohibits a LEC from assessing charges on any other carrier for traffic originated on its network.” (Order No. PSC-06-0776-FOF-TP, p. 22)~~

~~In its brief, Verizon Access states that Embarq’s proposal is a “solution in search of a problem,” and staff agrees. (BR at 12) Although staff does not recommend that Embarq be permitted to require Verizon Access to reimburse it for any transit charges for traffic originated by Embarq, staff believes the language to implement direct end office trunks should include the conditions listed or identified in staff’s conclusion below.~~

CONCLUSION

~~Embarq should not be permitted to require Verizon Access to reimburse it for any transit charges billed by an intermediary carrier for local traffic or ISP-bound traffic originated by Embarq. Nonetheless, staff recommends that the language to address implementing direct end office trunks should, at a minimum:~~

- ~~▪ Include a 90-day timeframe for establishing direct trunks;~~
- ~~▪ state that this timeframe is extendable if facility, equipment requirements, or related problems with the trunking order cause a delay that is attributable to Embarq;~~
- ~~▪ state that this timeframe is extendable if facility, equipment requirements, or related problems with the trunking order cause a delay that is attributable to a third party; and~~
- ~~▪ specify that the timeframe starts when all ordering requirements are fulfilled.~~

Issue 5: What rate should apply to transit traffic under the parties' interconnection agreement?

Recommendation: Staff recommends a transit rate of \$0.003 per minute of use (MOU) should apply to transit traffic under the parties' interconnection agreement (ICA). (Lee)

Position of the Parties

Verizon: The Commission should set a reasonable transit rate based on the comprehensive, relevant range of data points Verizon Access presented. It should reject Embarq's proposed transit rate, which--at double the existing rate Verizon Access pays Embarq--is unreasonably high.

Embarq: The parties agree that transit service is not a §251 obligation. Embarq's proposed transit traffic rate of \$.005/MOU is a reasonable commercial, market-based rate. In addition, Embarq's proposed rate is consistent with prior Commission orders regarding the appropriate rate for transit traffic.

Staff Analysis: Carriers interconnect their networks either directly or indirectly.¹⁹ Direct interconnection is when carriers have dedicated facilities to physically connect their networks. However, when traffic volume levels are low, it is more cost effective for carriers to indirectly interconnect by way of an intermediary carrier or transit provider, to route and complete calls. (Price TR 19; Fox TR 47; EXH 7, p. 101) Transit traffic is traffic that originates on one carrier's network, traverses another carrier's network, and then terminates on the network of a third carrier.²⁰ (ICA, §1.112) Transit service is the delivery of transit traffic. (ICA, §1.111; Price TR 23; Fox TR 47)

The transit provider charges a fee to the originating carrier for the use of its network in switching the traffic to the terminating carrier; this fee is referred to as a transit charge. (EXH 7, pp. 101-102) Embarq agrees to provide transit service to deliver traffic originated by Verizon Access' end users to end users of another competitive local exchange carrier (CLEC), incumbent local exchange company (ILEC), interexchange carrier (IXC), or commercial mobile radio service (CMRS) provider as long as contract arrangements exist with all necessary parties. (ICA §68.2; Fox TR 47) In return Verizon Access agrees to pay Embarq a transit charge.

The dispute in this issue is the rate that Embarq should charge for transit service under the ICA. (Price TR 24; Fox TR 50) Verizon Access proposes a transit rate of \$0.002867 per minute of use (MOU), which equates to the sum of the FPSC-approved common transport and tandem switching rates for Embarq for reciprocal compensation. (Price TR 24) Embarq proposes a market-based transit rate of \$0.005 per MOU. (Price TR 24; Fox TR 50)

¹⁹ Indirect interconnection is explicitly recognized and supported in the Telecommunications Act of 1996 (Act). The FCC recognized in its intercarrier compensation rulemaking docket that carriers often rely on a transit provider. Without a transit provider, there would be no indirect interconnection. (Order No. FCC 05-33, released March 3, 2005, CC Docket No. 01-92, In Re: Developing a Unified Intercarrier Compensation Regime, Further Notice of Proposed Rulemaking (ICF FNPRM), ¶125; §251(a))

²⁰ Transit service allows smaller carriers to connect indirectly through a third-party provider, rather than establishing direct connections. (Price TR 19-20)

PARTIES' ARGUMENTS

Verizon Access and Embarq agree that the provisioning of transit service is not an obligation under the Telecommunications Act of 1996 (Act), and therefore the transit rate need not be cost-based.²¹ (Price TR 36; Fox TR 50-51) The parties acknowledge that neither the FCC nor the FPSC has established a pricing standard for transit service. (Price TR 36; Fox TR 50-51; Verizon Access BR at 17; EXH 7, p. 48)

Rate Proposals

As stated previously, Verizon Access witness Price proposes a transit rate of \$0.002867 per MOU, the sum of the common transport and tandem switching FPSC-approved TELRIC (Total Element Long-Run Incremental Cost) elements for Embarq for reciprocal compensation purposes. (TR 24) Embarq witness Fox proposes a transit rate of \$0.005 per MOU. (TR 50)

Verizon Access witness Price contends that Embarq's proposed transit rate is unreasonably high, more than double the transit rate in the parties' existing ICA. (TR 24, 36) Further, the witness opines that Embarq has not proven that its proposed transit rate is reasonable. (TR 36) Recognizing the lack of an established pricing standard, the witness believes that the following reference points indicate that Verizon Access' proposed transit rate is more reasonable than the rate Embarq proposes:

- The transit rate in the existing ICA is \$0.002045 per MOU.
- The analogous Embarq interstate access rate is \$0.002052 per MOU.
- The transit rates Verizon Access recently negotiated with BellSouth in Florida are \$0.0015 per MOU in 2007, \$0.0020 per MOU in 2008, and \$0.0025 per MOU thereafter.²² (TR 37; EXH 7, pp. 51-52)
- A \$0.002071 per MOU transit rate is included in the existing Verizon Florida Inc./Sprint ICA. (TR 24-25; TR 36-37; EXH 2, p. 21; EXH 5, p. 12; EXH 7, pp. 46, 56, 83, 90)
- Based on Neutral Tandem's²³ Florida price schedule, its tariffed transit rate is \$0.003102 per MOU, excluding transport. (TR 37; EXH 15, pp. 47-48; EXH 8, p. 47) Embarq assumes 10

²¹ Embarq witness Fox acknowledges that the FCC is addressing transit issues regarding whether carriers have a federal duty to provide transit service and the appropriate pricing standard for transit service in its intercarrier compensation rulemaking docket.

²² In the BellSouth transit docket, BellSouth's tariffed rate was rendered invalid; parties were directed to negotiate. (Order No. PSC-06-0776-FOF-TP, issued September 18, 2006, Docket No. 050119-TP 050125-TP, In Re: Joint Petition by TDS Telecom d/b/a TDS Telecom/Quincy Telephone; ALLTEL Florida, Inc.; Northeast Florida Telephone Company d/b/a NEFCOM; GTC, Inc. d/b/a GT Com; Smart City Telecommunications, LLC d/b/a Smart City Telecom; ITS Telecommunications Systems, Inc.; and Frontier Communications of the South, LLC ["Joint Petitioners"] Objecting to and Requesting Suspension and Cancellation of Proposed Transit, and Docket No. 050125-TP, In Re: Petition and Complaint for suspension and Cancellation of Transit Traffic Service Tariff no. FL2004-284 filed by BellSouth Telecommunications, Inc., by AT&T Communications of the Southern States, LLC, pp. 57-59. (BellSouth Transit Order))

²³ Neutral Tandem is an alternative transit provider operating in some parts of Florida.

miles of transport and 185,000 minutes to convert the transport charge to a per minute basis; witness Price counters that the assumed level of minutes for a T-1 facility should be 250,000.²⁴ Thus, witness Price believes that Embarq's calculation of \$0.0046425 per MOU, including transport, is artificially high. (EXH 7, p. 54; EXH 9, p. 7)

Embarq witness Fox asserts that Embarq's proposed market-based transit rate is reasonable. Embarq argues in its brief that Verizon Access has failed to demonstrate the applicability of its suggested reference points or reconcile its proposal to the market-based standard that Verizon Access agrees is applicable to transit service. (BR at 21) Embarq makes the following points in support of its proposed transit rate:

- 21²⁵ carriers in Florida have agreed to the \$.005 per MOU rate. (Fox TR 52-53)
- BellSouth's tariffed transit rate in South Carolina is \$.006 per MOU. (TR 52-53)
- Neutral Tandem has Georgia and Florida tariffs setting its transit rate at \$.0046425 per MOU, assuming 10 miles of transport. (TR 52)
- The FCC has not determined that transit service is a federal requirement. (TR 52)
- The FCC has not established a pricing standard for transit service but is allowing parties to negotiate market-based rates. (TR 50, 53)
- The FPSC has determined that the transit rate may be a commercial rate. (Fox TR 51-53)
- Embarq's interstate access rate should not be considered outside of the context of Embarq's entire interstate access rate structure and is therefore inappropriate to consider as a basis for a market-based transit rate. (Embarq BR at 21)
- It is not appropriate to tie the transit rate to Embarq's §251 reciprocal compensation rates when the FPSC determined in the BellSouth Transit Order that transit traffic is not a §251 obligation. (TR 60-61; EXH 8, pp. 24-25)
- Consideration of applying FPSC-approved TELRIC-based rates is wrong without consideration of other factors essential in establishing a market-based rate -- such as additional costs not covered by the TELRIC-based rates and the value-added component of Embarq's transit service. (BR at 21; EXH 3, pp. 11, 13; EXH 8, pp. 30-31)

²⁴ Verizon Access equates a traffic volume of 250,000 minutes to a T-1 transmission level. (EXH 7, p. 54) In digital terms, DS1 and T-1 both operate at a transmission speed of 1.54 megabits per second. (*Newton's Telecom Dictionary, 22nd Updated and Expanded Edition*. (CMP Books. 2006) There is no dispute between the parties that when traffic volumes exceed a T-1 threshold, direct interconnection will be established. (ICA § 61.1.5; EXH 7, pp. 31)

²⁵ Witness Fox initially identified 15 carriers that have agreed or adopted Embarq's proposed transit rate. The witness revised the number to 21, including an Embarq affiliate, as part of his response to a late-filed deposition exhibit. (EXH 8, p. 68)

- Embarq's proposed transit rate is consistent with the principles reflected in the staff recommendation in the BellSouth transit docket where staff's recommended upper bound of a "just and reasonable" rate equated to a multiple of 2.6 times BellSouth's FPSC-approved TELRIC rate elements. Embarq's rate is only 1.75 times its FPSC-approved TELRIC rate elements, considerably less than that suggested by staff and recognized by the FPSC as an upper limit of a just and reasonable market-based rate for BellSouth. (TR 60-61; EXH 3, pp. 9-10, 13; EXH 8, p. 41)
- Embarq's costs are higher than BellSouth's as demonstrated by the level of its TELRIC-approved Unbundled Network Element (UNE) rates. It is therefore reasonable for Embarq's transit rate to be higher than BellSouth's transit rate. (BR at 20; EXH 8, pp. 34-35, 45)

ANALYSIS

In the BellSouth Transit Order the FPSC recognized that transit arrangements are best established through negotiations. (BellSouth Transit Order, p. 44) In this proceeding, negotiations have failed, and the parties have asked that the FPSC establish a transit rate.

Rate Proposals

Both parties agree that the transit rate need not be cost-based. In responses to staff discovery, Embarq contends that the FPSC should focus on "staff's recommendation that BellSouth's market-based rate, which reflects the value-added services associated with providing an intermediary function, should be considered a 'just and reasonable' rate." (EXH 3, p. 13) Embarq claims that the staff recommendation in the BellSouth Transit docket set a maximum rate of \$0.0023 per MOU, which is "2.6 times BellSouth's Commission-approved rate elements." (Fox TR 60; EXH 3, p. 10) Embarq concludes that its proposed \$0.005 rate is reasonable under the logic of the BellSouth Transit Order because it is only 1.75 times its FPSC-approved TELRIC rates for tandem switching and common transport. (EXH 3, p. 10; EXH 8, p. 41)

Staff believes that Embarq's representation of the BellSouth Transit Order is misleading and does not lend support to the reasonableness of Embarq's transit rate. As acknowledged by Embarq witness Fox, the FPSC did not establish a transit rate for BellSouth, nor did it approve any pricing guidelines to establish an upper limit. (EXH 8, pp. 41-42, 58-59) Staff believes the BellSouth Transit Order speaks for itself.

1. CLECs agreeing to Embarq's proposed rate

In support of its proposed transit rate, Embarq has identified 102 CLECs with whom Embarq has an effective interconnection agreement: 21 CLECs have agreed to Embarq's proposed transit rate without arbitration or dispute, and 81 have negotiated cost-based transit rates ranging from \$0.002045 per MOU to \$0.002867 per MOU.²⁶ (Fox TR 52; EXH 3, pp. 12-13; EXH 6, pp. 7-9; EXH 8, pp. 45-49, 62-63) Embarq believes that the transit rate other

²⁶ Prior to May 2006 when Embarq was spun off from Sprint, there was a desire for a low transit rate because Sprint was paying more in transit rates than the local company was billing. Since the spin-off of the local company, Embarq, witness Fox explains there has been a change in policy and the company now contends that transit service should be at market-based rates. (EXH 8, pp. 36, 46-47)

competing carriers charge also ensures that its proposed rate is reasonable because options exist for transit service – direct connection or another transit provider.

Staff believes that a transit rate predicated on the fact that it is comparable to rates that some CLECs have negotiated, fails to support Embarq's allegation that its transit rate is market-based. Staff agrees with Verizon Access witness Price that negotiated rates reflect company-specific business needs and constraints and is not evidence, in and of itself, of a market rate. Staff observes that in a negotiation there is give and take on both sides based on the needs of the individual carriers negotiating. If a CLEC does not expect to originate much transit traffic, it seems logical that transit issues would not be of great import to it. Staff believes it is most telling that of the 102 CLEC agreements listed on Exhibit 6 that contain a transit rate, 25 were identified as terminating transit traffic in December 2006,²⁷ 10 of which terminated more than 250,000 minutes. Of those 10, only two were identified as having agreed to Embarq's proposed \$0.005 per MOU rate. (EXH 3, pp. 12-13; EXH 4; EXH 6, pp. 7-9; EXH 8, pp. 45-49, 68)

Embarq witness Fox and Verizon Access witness Price are generally aware of the existence of Neutral Tandem as an alternative transit provider in Florida, but do not know the extent to which it interconnects with Embarq. (EXH 7, p. 52; EXH 8, pp. 42-43) It would seem logical that if Neutral Tandem is truly a competitor to Embarq's transit service, Embarq would have proffered evidence to that fact. Embarq did not. Market-based rates are generally established based on negotiations between two parties where sufficient alternatives exist such that the purchaser has reasonably comparable bargaining power. (EXH 7, p. 52) That is not the case here; the record does not indicate any other competitive provider of transit service operating in Embarq's footprint. Given the lack of alternative providers, staff believes there is no transit service "market" from which to derive a market-based rate. For this reason, Embarq's negotiated transit rates does not lend support to the just and reasonableness of its proposed rate.

2. Other reference points

Both Verizon Access and Embarq offer other reference points in support of their respective proposals. Verizon Access contends that its reference points are all Florida-specific and therefore more relevant than a Georgia or South Carolina tariffed rate referenced by Embarq. (Price TR 37; EXH 7, pp. 81-82)

Verizon Access references the negotiated transit rates with BellSouth and also those negotiated between Verizon (the ILEC) and Sprint. Embarq characterizes these reference points as inappropriate, contending that Embarq's transit rate should be higher than BellSouth's or Verizon's. This contention is based on a cost-based rationale asserting that Embarq "provides transit services in less urban areas than the RBOCs²⁸ in Florida," so it is relatively more costly for Embarq to provide such services; and "per unit network cost for BellSouth is substantially lower than it is for Embarq." (EXH 3, p. 10; EXH 8, pp. 33-35, 44-45, 66-67) At the same time, however, Embarq readily admits that no testimony or evidence supporting the contention that transit service costs more in less urban areas has been provided, stating "mainly again because we don't think that this is a cost-based issue per-se." (EXH 8, pp. 45, 62, 66) It is disconcerting

²⁷ Staff notes that five CLECs terminated more than 2,000,000 minutes. Of those five, only one carrier is represented to have agreed to Embarq's transit rate.

²⁸ Regional Bell Operating Companies.

that Embarq claims that its costs justify a higher transit rate but then denies the relevance of its costs. Staff believes that Embarq's argument that its transit rate should be higher because its costs are higher is unsupported by the record. Moreover, staff believes that Embarq's arguments that costs are irrelevant directly contradicts its desire to use costs as a reason for a higher transit rate.

Recommended transit rate

Staff believes that, at a minimum, transit service is subject to the "just and reasonable" pricing standards of §201 and §202 of the Act.²⁹ While it can be argued that "just and reasonable" rates should be higher than TELRIC, staff believes that a rate almost 100% higher than TELRIC is a strained interpretation of "just and reasonable" with respect to transit service. Moreover, given that the FCC has found that interstate access rates are "just and reasonable," one could argue that a transit rate that is more than 150% higher than the comparable interstate proxy rates cannot be considered "just and reasonable." For the reasons stated above, staff does not believe that Embarq's proposed transit rate of \$0.005 per MOU is "just and reasonable" based on the record evidence. However, staff believes other options are supported by the record and available for the FPSC to consider.

Option A. FPSC-approved elemental rates (Verizon Access' proposal)

Embarq witness Fox testifies that transit service is comprised of tandem switching and common transport network element costs as well as a tandem intermediary cost (TIC). (EXH 8, pp. 28-29, 55) The TIC, explains the witness, is designed to capture other business costs associated with transit service, such as the cost of providing billing records, handling billing disputes, use of network resources, and product management. (EXH 3, pp. 10-11; EXH 8, pp. 28-31, 53) Witness Fox testifies that a "value-added" component, described as an intangible, should also be recognized in a transit rate. (EXH 8, pp. 55-56) Embarq argues that consideration of the TIC as well as the "value-added" component are essential in establishing a market-based rate for its transit service. (BR at 17, 18, 21) Embarq witness Fox concedes, however, that no analysis was performed to determine the amount of other business costs that needed to be recovered, and there was no attempt to quantify the "value-added" component. (EXH 8, pp. 29-32, 54-57) The reason given by the witness was that Embarq did not approach transiting as a cost issue. (EXH 8, pp. 29-30)

In the Joint CLEC Arbitration Order³⁰ the FPSC found that BellSouth was entitled to charge a TIC based on BellSouth's indications that it incurred certain costs associated with transit service that were not covered by its TELRIC rates. (Joint CLEC Arbitration Order pp. 51-53) Embarq's position is that it should be afforded this same action even though Embarq readily

²⁹ The pricing of network elements that are not subject to the unbundling standards in §251(d)(2) are generally priced utilizing the basic just, reasonable, and nondiscriminatory rate standards of §201 and §202 of the Act. At this time, transit has not been deemed to be a UNE.

³⁰ Order No. PSC-05-0975-FOF-TP, issued October 11, 2005, Docket No. 040130-TP, In Re: Joint petition by NewSouth Communications Corp., NuVox Communications, Inc., and Xspedius Communications, LLC, on behalf of its operating subsidiaries Xspedius Management Co. Switched Services, LLC and Xspedius Management Co. of Jacksonville, LLC, for arbitration of certain issues arising in negotiation of interconnection agreement with BellSouth Telecommunications. Inc. (Joint CLEC Arbitration Order).

admits it provided no record evidence for the TIC. Staff believes that if the transit rate is designed to recover certain costs, it should be important to analyze and quantify those costs to ensure they are being recovered. Embarq made no analysis of the costs and indeed did not provide any cost support for its proposed rate. (EXH 8, pp. 30-32) Embarq's only argument is that its proposed transit rate is applicable in a number of other states and is used system-wide as often as possible. (EXH 8, p. 31)

Nevertheless, staff believes there may be costs not recovered in the FPSC-approved elemental TELRIC rates that the TIC is intended to recover; the "added-value" appears to be an additional intangible component. The magnitude of the TIC and the "added-value" are unknown because Embarq did not provide any supporting cost data or analysis. As such, an available option is to exclude recognition of a TIC or "added-value" as being unsupported by the record, yielding a transit rate comprised of the tandem switching and common transport network element rates of \$0.002867 per MOU as Verizon Access proposed. Staff believes that the recently negotiated transit rate between Verizon Access and BellSouth in Florida of \$0.0015 in 2007, \$0.0020 in 2008, and \$0.0025 thereafter, lends reasonableness to this rate. Further, staff notes that Embarq witness Fox recognizes that the BellSouth negotiated transit rate is above-cost and along the lines of being market-based. (EXH 8, p. 44)

Option B. Interstate access rates

Embarq's interstate access tariff includes a transit rate of \$0.002052³¹ per MOU. Embarq argues that the use of interstate access rates should not be considered outside of the context of Embarq's entire interstate access rate structure and, therefore, are inappropriate to consider as a basis for a market-based transit rate. (BR at 21) Notwithstanding this, staff notes that while the interstate access rates are not necessarily market-based, they have been deemed by the FCC to be "just and reasonable." (EXH 7, pp. 55-56, 82-83) This being said, staff believes that there may be some additional business costs associated with provisioning transit service that are not recognized in the interstate access rate.

On balance, staff believes a \$0.003 per MOU transit rate is reasonable. Based on a "just and reasonable" interstate access rate and recognizing there may be additional business costs associated with the transit service, the result would likely approximate \$0.003 per MOU. The rate is also comparable to the existing FPSC-approved element rates and the recently negotiated BellSouth/Verizon Wireless transit rate that Embarq recognizes as being above-cost.

CONCLUSION

Staff recommends a transit rate of \$0.003 per minute of use (MOU) should apply to transit traffic under the parties' interconnection agreement (ICA).

³¹ Assumes 14 miles of transport. (EXH 7, pp. 56-57)

DOCKET NO. 060767-TP

DATE: August 7, 2007

Issue 6: Should this docket be closed?

Recommendation: No. This docket should remain open pending the submission of a properly executed conforming Agreement. Thereafter, it is recommended that staff review the Agreement and, if in compliance, administratively approve the Agreement and close the Docket. **(Tan)**

Staff Analysis: This docket should remain open pending the submission of a properly executed conforming Agreement. Thereafter, it is recommended that staff review the Agreement and, if in compliance, administratively approve the Agreement and close the docket.