

**Position of TelNet and Pac-West regarding
Intercarrier-Compensation for VNXX ISP-Bound traffic.**

January 18, 2006

The *ISP Remand Order* and related D.C. Circuit Court ruling established an intercarrier compensation mechanism for all ISP-bound traffic. The FCC did so under the framework of what is compensable under sections 251(b)(5) and 251(g) of the Act. As explained further below, this compensation regime by definition includes VNXX ISP Bound traffic. At the same time, the FCC also made clear that state commissions are preempted from implementing a different intercarrier compensation mechanism. (All cites are to the *ISP Remand Order*, unless specified otherwise.)

I. The ISP Remand Order’s Intercarrier Compensation Mechanism Applies to ISP Bound VNXX Traffic

Background

In the *ISP Remand Order*, the FCC found that it had previously “erred in focusing on the nature of the service (i.e., local or long distance)” when developing prior intercarrier compensation regimes. (¶ 26) Instead, the FCC found that intercarrier compensation regimes are governed by either section 251(b)(5) or section 251(g) of the Act. (¶ 30.) In essence, all traffic has to fall into one of these two buckets:

251(b)(5)

“Section 251(b)(5) imposes a duty on all local exchange carriers to ‘establish reciprocal compensation arrangements for the transport and termination of telecommunications.’ ” (¶ 31, footnote omitted.) Said differently, “Unless subject to further limitation, section 251(b)(5) would require reciprocal compensation for transport and termination of *all* telecommunications traffic, -- i.e., whenever a local exchange carrier exchanges telecommunication traffic with another carrier.” (¶ 32)

251(g) Carve Out

The FCC found, “that Congress explicitly exempts certain telecommunications services from the reciprocal compensation obligations” of section 251(b)(5). (¶ 32) Those services that are carved out of the reciprocal compensation provisions of subsection (b)(5) are set forth in section 251(g) of the Act and are “exchange access, information access, and exchange services for such access” provided to IXCs and information service providers. (¶ 32 and 24.) The services specified in Section 251(g) have one thing in common: they are all access service or service associate with access. (¶ 37) The focus now becomes determining which “traffic falls within subsection (g) and *not* the universe of traffic that falls within subsection (b)(5)” (¶ 34.)

The FCC ultimately determined that ISP-bound traffic is “information access” under the 251(g) carved out from 251(b). (¶ 42 and 44) In so doing, the FCC reiterated that it was

mistaken to have based its prior compensation decisions on the designation of a call as local or non-local. Basing reciprocal compensation obligation on the definition of “local calls”, however defined, overlooked the proper statutory test and interplay set out in sections 251(b)(5) and 251(g). The FCC further explained that the use of the term “local call” is ambiguous because it is not defined in statute. (¶ 45 and 26.)

The *ISP Remand Order* was subsequently appealed. See, D.C. Circuit Court of Appeals in *WorldCom v FCC*, 288 F. 3d 429 (2002). The D.C. Circuit Court found that ISP traffic did not fall under Section 251(g). The court narrowed the FCC’s reading of Section 251(g) and found that the section “appears to provide simply for the ‘continued enforcement’ of certain pre-Act regulatory ‘interconnection restrictions and obligations.’” (Emphasis added.) The court further stated that:

[A]s it seems uncontested--and the Commission declared in the Initial Order--that there had been no pre-Act obligation relating to intercarrier compensation for ISP-bound traffic. See Initial Order, 14 FCC Rcd at 3695, p 9; see also id. at 3690, p 1, 3707-3710, p p 28-36. The best the Commission can do on this score is to point to pre-existing LEC obligations to provide interstate access for ISPs. See, e.g., Remand Order, 16 FCC Rcd at 9164, p 27; In the Matter of MTS & WATS Market Structure, 97 F.C.C.2d 682, 711-15, p p 77-83 (1983). Indeed, the Commission does not even point to any pre-Act, federally created obligation for LECs to interconnect to each other for ISP-bound calls. And even if this hurdle were overcome, there would remain the fact that § 251(g) speaks only of services provided "to interexchange carriers and information service providers"; LECs' services to other LECs, even if en route to an ISP, are not "to" either an IXC or to an ISP.

The Court, however, did not vacate the *ISP Remand Order* or its intercarrier compensation regime as “there is plainly a non-trivial likelihood that the Commission has authority to elect such a system.” (*WorldCom v FCC*, last paragraph of ruling.) In essence, the D.C. Circuit Court ruling moved the FCC’s compensation regime from the 251(g) bucket to the 251(b)(5) bucket.

Discussion

The question before the workgroup at this juncture is whether ISP Bound VNXX traffic is subject to the intercarrier compensation mechanism set forth in the *ISP Remand Order*. The answer is yes. Using the bucket analogy, the D.C. Circuit Court has already determined that ISP Bound traffic does not fall under 251(g) as there was no pre-Act obligation for intercarrier compensation for such traffic. The same is true for ISP Bound VNXX traffic. Furthermore, the service of routing and terminating ISP VNXX call is not being provided to an IXC or ISP, which is another prerequisite for 251(g) traffic. The only other bucket ISP Bound VNXX traffic can fit is the default, section 251(b)(5) category under which the FCC, in its *ISP Remand Order*, has established a special compensation arrangement which applies to all such traffic, without exception.

II. The FCC has Preempted States from Imposing Alternative Inter-carrier Compensation Regimes for ISP Bound Traffic.

Background

In the *ISP Remand Order*, the FCC found that Section 251(i) of the Act provided it with the statutory authority under Section 201 to regulate ISP-bound traffic. (¶ 28) As part of its Section 201 analysis, the FCC reaffirmed its prior finding that ISP-bound traffic is properly classified as interstate based on the end-to-end analysis. (¶ 52 and 53)

Under its 201 authority, the FCC imposed a compensation mechanism which established relatively low per minute rates which transitioned down over a period of time, stopping short of bill and keep. (¶ 77) The current inter-carrier compensation rate for ISP bound traffic is .0007 per minute. (¶ 149.) Among other things, the FCC also imposed growth caps and new market restrictions on ISP traffic eligible for compensation. Those restrictions were later removed by the *Core Forbearance Order*.

The FCC stated that “[b]ecause we now exercise our authority under section 201 to determine the appropriate inter-carrier compensation for ISP-bound traffic, however, state commissions will no longer have authority to address this issue.” (¶ 82) The FCC further clarified that the rates it set are a cap and “have no effect to the extent that states have ordered LECs to exchange ISP-bound traffic” at a lower rate, or at bill and keep – noting the past tense of the word ordered. (¶ 80, emphasis added).

The D.C. Circuit Court of Appeals decision in *WorldCom v FCC*, did nothing to revise or vacate the FCC’s inter-carrier compensation scheme. As stated previously, the court did not vacate or alter the *ISP Remand Order’s* compensation mechanism as “there is plainly a non-trivial likelihood that the Commission has authority to elect such a system.” (*WorldCom v FCC*, last paragraph of ruling.)

Discussion

Based on the clear language of the *ISP Remand Order*, state commissions are preempted from imposing an inter-carrier compensation mechanism for ISP bound traffic that is different from that the FCC created. The only exception to this rule is if the state imposed a lower rate or bill and keep prior to the *ISP Remand Order*.

III. Other Decisions Relating to Inter-carrier Compensation for ISP Bound VNXX Traffic.

Starpower v Verizon South

In *Starpower v Verizon South*, rel’d November 7, 2003, involved a contractual dispute between Starpower and Verizon South regarding the payment of reciprocal compensation for ISP Bound VNXX traffic. While the contract at the center of the dispute predates the *ISP Remand Order* and the case does not address the compensation mechanism adopted

in that order, it does provide guidance as to how traffic has traditionally be determined to be interexchange access (251(g) traffic).

In the *Starpower Decision* the FCC held that the ICA negotiated between the parties required Verizon to pay reciprocal compensation on VNXX ISP-traffic. The Parties' ICA incorporated the treatment of such traffic under Verizon's tariff. The FCC relied upon various facts; (i) Verizon had engaged in "the very same conduct that it now alleges is unlawful" (*Starpower Decision* ¶14) and (ii) Verizon and the entire industry designated calls as "either local or toll by comparing the NPA-NXX codes of the calling and called parties" (*Starpower Decision* ¶ 17). Based on these facts, the FCC determined that VNXX ISP-bound traffic was "local" traffic under Verizon's tariff and consequently concluded that reciprocal compensation was due. (*Starpower Decision* ¶ 13)

Under the ISP Remand Order's framework, for traffic to be designated as 251(g) or exchange access, one of the determining factors would be the historical comparison of the NPA-NXX codes of the calling and called parties, as the *Starpower Decision* confirms. In the case of VNXX traffic, the NPA-NXX comparison would translate to traffic which has not been defined as exchange access. (Of course, ISP Bound VNXX traffic also fails the 251(g) test because it is not service being provided to and IXC's and ISPs.)

Core Forbearance

In the Core Forbearance Decision, FCC 04-241, Rel'd October 18, 2004, the FCC removed its growth cap on ISP bound traffic eligible for compensation. Similarly, the FCC also removed its restriction requiring carriers to exchange ISP bound traffic on a Bill and Keep basis for markets entered after the effective date of the *ISP Remand Order*. (¶ 20, 21, 23 and 24) The FCC lifted these restrictions for several reasons, but it did state that the restrictions were "no longer in the public interest", it was no longer concerned with "continued expansion of the arbitrage opportunity" and that a "policy favoring a unified compensation regime outweigh any remaining concerns about the growth of dial-up Internet Traffic. (¶ 20 and 21, footnote omitted)

IV Comments of Other Parties

CenturyTel asserts that the *ISP Remand Order* does not address VNXX ISP-bound traffic because ¶ 10 says: "As we noted in the Declaratory Ruling, an ISP's end-user customers typically access the Internet through an ISP server located in the same local calling area." (Emphasis is CenturyTel's). CenturyTel's elevation of this casual statement to a significant restriction of the scope of the *ISP Remand Order* is not supported. The statement is pulled from the background section of the ISP Remand Order in its discussion of a prior order which has since been vacated by the court of appeal. (¶ 10 and 16.) Furthermore, it is instructive to consider the FCC's actual statement in the *Declaratory Ruling* that the FCC was referring to in the *ISP Remand Order*. In the *Declaratory Ruling*, the FCC stated, "Under one typical arrangement, an ISP customer dials a seven-digit number to reach the ISP server in the same local calling area." (Emphasis added, 14 FCC Rcd 3691.) This language demonstrates that as early as 1999, the FCC was aware that there was more than one typical way that ISP customers could

reach the Internet, and that accessing an ISP server located in the same local calling area was just one of the typical arrangements. Certainly, if the FCC had intended to restrict its *ISP Remand Order* to one of the typical arrangements, it would have expressly defined that restriction in its Order.

V Conclusion

The FCC implemented an intercarrier compensation regime for ISP-Bound traffic based on sections 251(b)(5) and 251(g) of the Act, and independent of any designation of a call as local or non-local. The test for determining compensation is simple. If the traffic is not explicitly carved out by 251(g) as a pre-Act regime for exchange access, information access, and exchange services for such access provided to IXC's and information service providers, it must be considered 251(b)(5) traffic subject to reciprocal compensation. In the case of ISP bound traffic, which the FCC took exclusive jurisdiction of, it was ultimately determined that such traffic is 251(b) and subject to the compensation mechanism set forth in the *ISP Remand Order*. ISP bound VNXX traffic likewise is subject to the *ISP Remand Order*'s compensation plan as it is clearly not a service predating the Act or being provided to IXC's or information access services. Accordingly, the recommendation of this workgroup should be that VNXX traffic is subject to the FCC's compensation plan and that the state is preempted for altering that plan.