BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

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| QWEST CORPORATION<br><br>Complainant,<br><br>v.<br><br>LEVEL 3 COMMUNICATIONS, LLC, PAC-WEST TELECOMM, INC., NORTHWEST TELEPHONE, INC., TCG SEATTLE, ELECTRIC LIGHTWAVE, INC., ADVANCED TELECOM, INC. d/b/a ESCHELON TELECOM, INC., FOCAL COMMUNICATIONS CORPORATION, GLOBAL CROSSING LOCAL SERVICES, INC., and MCI WORLDCOM COMMUNICATIONS, INC.<br><br>Respondents. | DOCKET NO. UT-063038 |

**REPLY BRIEF**
**ON BEHALF OF COMMISSION STAFF**

**June 29, 2007**

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# I. INTRODUCTION

1 In this complaint case, Qwest has sought relief against various named competitive local exchange carriers (CLECs). The relief Qwest seeks includes, *inter alia*, a prohibition against the provisioning of service using virtual NXX arrangements. Such arrangements cause Qwest to transport intrastate interexchange traffic to CLEC interconnection points at its own expense and to pay reciprocal compensation when a Qwest customer calls a CLEC customer served through a VNXX arrangement.

2 Staff recommends that the Commission prohibit VNXX for uses other than dial-up Internet access service and VoIP telephony. The Commission is authorized by RCW 80.36.140 to determine, upon complaint, the reasonable and proper practices to be observed by telecommunications companies.

3 With respect to services that afford dial-up Internet service providers (ISPs) with local number presence, the Commission should allow VNXX only under the following conditions: CLECs must enter into agreements for the exchange of ISP-bound VNXX traffic that relieve Qwest of the obligation to pay reciprocal compensation on that traffic and of the expense of local interconnection facilities to the extent those facilities are used to transport VNXX traffic to the CLEC's point of interconnection.

4 The Commission should reserve for separate determination questions related to proper routing and compensation for VoIP calls.

5 This brief responds to various arguments in the parties' opening briefs in opposition to Staff's proposed resolution.

## II. "VNXX" LEGAL ISSUES

### A. COCAG and Other Industry Guidelines.

#### 1. Extent to which guidelines are binding on the Commission.

6 Many of the parties misinterpret Staff's argument to be that the COCAG is binding on the Commission. The COCAG is relevant to this proceeding not because it binds the Commission, but because it reflects industry practice and the regulatory *status quo* in the absence of any contrary policy announced by an appropriate regulatory authority, such as this commission.[1]

#### 2. Industry guidelines and geographic issues in connection with numbers and number assignments.

7 The CLEC parties make two arguments with regard to whether the various cited standards and legal authorities[2] reflect an underlying requirement or expectation that, in order to be "local" for inter-carrier compensation, a call must be between parties physically located within the same local calling area.

8 The most extreme version of the first argument is Level 3's statement that "the definition of 'local calling area' . . . is devoid of any geographical underpinnings."[3] A somewhat more moderate formulation of this argument is TCG's statement that "the definition of local calling area makes no reference to the physical location of the calling or called parties or even to an 'exchange' for that matter."[4] Similarly, the Joint CLECs say that none of the statutory provisions or Commission rules cited by Qwest or Staff "include any reference to, much less restriction on, the physical location of the parties to a "local" call.[5]

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[1] *See* Staff Opening Br. at pp. 9, 10.
[2] COCAG paragraph 2.14, RCW 80.36.230, WAC 480-120-265, WAC 480-120-021, 47 U.S.C. Sec. 251(g).
[3] Level 3 Br. at 11.
[4] TCG Br. at 7.
[5] Joint CLEC Br. at 6.

Staff submits that these arguments go too far, and if accepted by the Commission, would erase any distinction between local and interexchange traffic, between local exchange carriers and interexchange carriers, and between the access charge and reciprocal compensation regimes.

9 The second CLEC argument regarding geographic local calling areas is focused on the specific problem of foreign exchange (FX) service. The Joint CLECs, for example, point out that if the cited statutes and rules do restrict local calls to parties physically located in the same local calling area, then Qwest's FX service would also be prohibited.[6] FX admittedly is an exception to the general rule that a call is local only when its endpoints are within the same geographic local calling area. FX service has been allowed because the customer pays for a private line—its own dedicated facility—to carry calls from the switch in the customer's chosen local calling area to the customer's distant location. The conditions under which CLECs should be able to offer a service that affords this functionality have become the focal point of this case. Staff addresses this issue in section III.A (Foreign Exchange Service), below.

**3. Exceptions/Industry Practices.**

10 CLECs point to various Internet telephony services, including a Qwest provided VoIP service, through which a customer can obtain a telephone numbers associated with a rate center of the customer's choosing.[7] As Staff stated in its opening brief,[8] it appears that the assignment of geographic telephone numbers to nomadic VoIP providers is an FCC-authorized exception to the COCAG and to any contrary state regulation. VoIP number

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[6] *Id.* at 7.
[7] Level 3 Br. at 7, 8.
[8] Staff Opening Br. at 27.

assignment has limited relevance to this case because the FCC's decisions do not apply to VNXX service and both CLECs and Qwest are providing telephone numbers to providers of IP voice service.

**B. <u>Washington State Statutes, Rules, Orders, Tariffs.</u>**

*11* The Joint CLECs assert that the Commission's decisions, including the decision in the AT&T/Qwest arbitration (UT-033035) "are fundamentally at odds with the notion that 'VNXX' provisioning of FX service is unlawful."[9] Unfortunately, the word "unlawful" has generated more heat than light. A better formulation of Staff's position is that VNXX provisioning—to the extent that its inequities for purposes of intercarrier compensation are not addressed—is inconsistent with good competition policy, and threatens to subvert the intrastate access charge regime. Staff's position is consistent with relevant Commission precedent.

*12* The AT&T/Qwest arbitration[10] is the only case in which the Commission has been confronted with the question of whether VNXX calls may be treated as local *under state law and policy.* As discussed below, other Commission orders that dealt with VNXX were based on an interpretation of the FCC's *ISP Remand Order* that the Federal District Court recently found to be in error (namely that the FCC intended for all ISP-bound traffic is subject to the same compensation scheme, regardless of whether it is within or between local calling areas). The District Court's order requires the Commission to reconsider the treatment of ISP-bound VNXX traffic in terms of *state* law and policy and not on the premise that the FCC decided the matter in its *ISP Remand Order.* Thus, the AT&T/Qwest arbitration order moves front and center as the relevant Commission precedent.

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[9] Joint CLEC Br. at 8.
[10] *In re AT&T Communications of the Pacific Northwest and TCG Seattle*, UT-033035.

13 In the AT&T/Qwest arbitration, AT&T took an above-board approach to implementing VNXX. It did so by proposing, in its interconnection agreement with Qwest, to define "local traffic" based only on the NPA/NXX of the calling and called parties, and not on the parties' physical location as proposed by Qwest. AT&T's proposed definition would have opened the way for VNXX provisioning and would have obligated Qwest to pay reciprocal compensation on VNXX traffic. As the Commission then correctly concluded, AT&T's proposal would have required a departure from existing state policy—a policy which Staff submits is reflected in the COCAG, and embodied in the various rules and tariffs discussed in Staff's opening brief.

14 While it may be permissible for CLECs to provide an FX-like service using VNXX, and even desirable from a competition policy standpoint, CLECs may not do so without first proposing some equitable alternative to reciprocal compensation (such as bill-and-keep) for VNXX traffic. The Commission rejected AT&T's proposed definition, but expressed sympathy for allowing CLECs to provide an FX-like service *under some limitations designed to address the arbitrator's concerns*:

> We note, however, the Arbitrator's discussion of his concerns that adopting Qwest's alternative leaves open the door to disputes if Qwest tries to use this definition to frustrate an effort by AT&T to offer services that are functionally equivalent, from a customer perspective, to Qwest's FX service and local-number-presence service for ISP bound traffic.
>
> We approve of the Arbitrator's efforts to encourage the parties to avoid such potential disputes by further negotiation, if necessary, to ensure implementation of their Interconnection Agreement in a manner consistent with the pro-competitive principles discussed in the Arbitrator's Report. We emphasize that those principles are stated as dicta. They suggest options for implementation (*e.g.,* agreement to bill-and-keep compensation; FX functionality for inbound calls only), but they do not bind the parties to

> specific arrangements, nor do they bind us if we must ultimately resolve a dispute over implementation.[11]

The arbitrator's analysis, referred to here by the Commission, went to the heart of the VNXX intercarrier compensation problem. The arbitrator also came to the conclusion that staff believes best resolves this complex dispute:

> While AT&T, in the interest of promoting competition, must be allowed to offer services that are functionally equivalent to existing services offered by Qwest, such as FX and ISP local number presence, insistence that Qwest pay reciprocal compensation for such services is inappropriate. The FCC's *ISP Remand Order* does not preempt state jurisdiction to determine the appropriate intercarrier compensation scheme for FX functionality provided via virtual NXX, but it is strongly suggestive of what is appropriate given that FX service and ISP local number provisioning both result in a hybrid form of traffic; traffic that is neither clearly local, nor clearly interexchange, and that is largely one-way traffic. Such traffic should be compensated on a bill-and-keep basis.[12]

TCG Seattle states that, "[i]n response to this guidance, Qwest and TCG Seattle are exchanging all local-rated traffic, including voice and ISP-bound VNXX traffic, on a bill-and-keep basis under their current approved interconnection agreement."[13]

*15* Level 3's brief in a number of places[14] creates the impression that the Commission has addressed the VNXX intercarrier compensation question more often than it actually has. Level 3 cites an inapposite 2001 U.S. West Order[15] and cites not only the final decision in the Pac-West complaint—which for all practical purposes was the same as Level 3's complaint in UT-053036, in UT-053039, but also the recommended decision, as if it were separate authority. On the other hand, Level 3 fails to mention the AT&T/Qwest

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[11] *In re AT&T Communications of the Pacific Northwest and TCG Seattle*, UT-033035, Final Order Affirming Arbitrator's Report and Decision Approving Interconnection Agreement, ¶¶ 15-16, Feb. 6, 2004.
[12] *In re AT&T Communications of the Pacific Northwest and TCG Seattle*, UT-033035, Order 4, Arbitrator's Report, ¶ 35, Dec. 1, 2004.
[13] TCG Br. at 9.
[14] Level 3 Br. at 13, 16.
[15] *See* Level 3 Br. at 13, fn. 48.

arbitration, discussed above, that specifically considered arguments regarding CLEC's ability to provide a type of FX service through the assignment of NPA/NXXs not associated with the called party's location.

*16* The Commission made its first formal decision with regard to VNXX traffic in a 2003 Level 3/Century Tel arbitration order.[16] In that order, it concluded that VNXX ISP-bound traffic is the same as other ISP-bound traffic for intercarrier compensation purposes on the theory that this is what the FCC intended in the *ISP Remand Order*. The Commission next decided the 2004 AT&T/Qwest arbitration, rejecting AT&T's definition of "local" traffic based solely on NPA/NXX of the calling and called parties and adopting, with reservations, Qwest's definition of a local call as originating and terminating within the same local calling area. Finally, in 2006 the Commission decided two parallel complaints brought by Pac-West and Level 3 against Qwest in nearly identical simultaneous orders.[17] The Commission decided both the 2003 Level 3/CenturyTel case and later Level 3 and Pac-West complaint cases against Qwest on an interpretation of the *ISP Remand Order* that was reversed by the Federal District Court.[18] In those decisions, the Commission also expressly reserved to a later complaint—*this complaint*—"whether VNXX arrangements generally, are appropriate or within the law."[19]

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[16] *In the Matter of the Petition for Arbitration of an Interconnection Agreement Between Level 3 Communications, LLC, and CenturyTel of Washington, Inc.*, Docket UT-023043, Seventh Supp. Order: Affirming Arbitrator's Report and Decision, at page 4 (February 28, 2003).

[17] *Level 3 Communications, LLC v. Qwest Corportation,* Docket No. UT-053039, Order No. 05, para. 39, 40 (February 10, 2006); *Pac-West Telecomm, Inc. v. Qwest Corporation,* Docket No. UT-053036, Order No. 05 (February 10, 2006).

[18] *Qwest Corp. v. Washington Utilities and Transportation Commission,* 2007 WL 1071956, __ F.Supp.2d __ (April 19, 2007).

[19] *Level 3 Communications, LLC v. Qwest Corportation,* Docket No. UT-053039, Order No. 05, para. 39, 40 (February 10, 2006); *Pac-West Telecomm, Inc. v. Qwest Corporation,* Docket No. UT-053036, Order No. 05, para. 42, 43 (February 10, 2006).

17 Curiously, Level 3 asserts that "the Commission has consistently held, without exception, that ISP-bound traffic should be subject to the same compensation regime as voice traffic."[20] What makes this puzzling is that there is no dispute that ISP-bound traffic that terminates within the calling party's local calling area should be subject to the same compensation regime as voice traffic. Rather, the question is whether ISP-bound traffic terminating at the equipment of an ISP physically outside the caller's local calling area is to be treated as local for intercarrier compensation. It is also unclear how to square Level 3's assertion with the statement of its own witness, Dr. Blackmon, that ISP bound traffic may be treated differently from voice traffic for purposes of access charges.[21]

**C. <u>Interconnection Agreements.</u>**

18 Level 3 argues that reciprocal compensation is not barred by its (or its affiliate, Broadwing's) existing interconnection agreements with Qwest because neither of the agreements "define, describe or address 'VNXX' traffic."[22] Likewise, the Joint CLECs say that the "FCC … prescribed a rate of $.0007 per minute for terminating ISP-Bound traffic. In the absence of an interconnection agreement to the contrary, therefore, Qwest is responsible for compensating calls that originate on Qwest's network – including calls to CLEC 'VNXX' FX customers – at the FCC rate for ISP-bound traffic and at the cost-based rates the Commission has established for all other Section 251(b)(5) traffic."[23]

19 The CLECs assertion would be true only if this Commission had classified VNXX calls as local under state law, but it has not. The Commission rejected AT&T's language that would have classified traffic as local based solely on the NPA/NXXs of the calling and

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[20] Level 3 Br. at 13.
[21] Blackmon, Exh. No. 401T, 15:25 -16:9.
[22] Level 3 Br. at 17.
[23] Joint CLEC Br. at 20, 21.

called parties, rather than based on the parties' physical location.[24] For the reasons Staff has described, VNXX is inconsistent with industry standards for number assignment as well as state policies, reflected in rule, regarding the distinction between local and toll traffic and the geographic nature of local calling areas. Thus, an interconnection agreement's silence on the subject of VNXX should not be construed as permission. Nonetheless, Staff believes there are valid policy reasons to allow VNXX for ISP-bound traffic under a bill-and-keep regime until the FCC addresses the matter.

*20* Regardless of the interpretation of existing interconnection agreements, the parties should be required to amend their interconnection agreements, if necessary, to comply with the Commission's decision in this case.

**D. <u>FCC/Federal Court/ Other State Commission decisions.</u>**

**1. Telecom Act.**

*21* Level 3 argues that Section 251(b)(5) of the Act[25] requires payment of reciprocal compensation on "FX-like traffic" (Level 3's term for VNXX).[26] This is the same argument that was rejected by the District Court[27] as well as by Ninth, Second and First Circuits.[28]

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[24] *In re AT&T Communications of the Pacific Northwest and TCG Seattle,* UT-033035, Final Order Affirming Arbitrator's Report and Decision Approving Interconnection Agreement, ¶¶ 15-16, Feb. 6, 2004.
[25] 47 U.S.C. § 251(b)(5).
[26] Level 3 Br. at 19-21.
[27] *Qwest Corp. v. Washington Utilities and Transportation Commission,* 2007 WL 1071956, pp. 9, 10, __ F.Supp.2d __ (April 19, 2007).
[28] *Global NAPs Inc. v. Verizon New England, Inc.,* 444 F.3d 59, 73-74 (1st Cir. 2006) ("The issue that necessitated FCC action in the ... *ISP Remand Order* was whether reciprocal compensation obligations apply to the delivery of calls from one LEC's end-user customer to an ISP *in the same local calling area* that is served by a competing LEC.") (internal quotations omitted; emphasis added); *Global NAPs Inc. v. Verizon New England, Inc.,* 454 F.3d 91, 99 (2nd Cir. 2006) ("The ultimate conclusion of the *[ISP] Remand Order* was that ISP bound traffic *within a single calling area* is not subject to reciprocal compensation."); *id.* ("Although the *[ISP] Remand Order* states explicitly that ISPs are exempt from reciprocal compensation for intra-local calling area calls, it sheds little light on inter-local calling area calls or access fees."); *WorldCom, Inc. v. F.C.C.,* 288 F.3d 429, 430 (D.C. Cir. 2002) (explaining that, in the *ISP Remand Order* the FCC "held that under § 251(g) of the Act it was authorized to 'carve out' from § 251(b)(5) calls made to [ISPs] located *within the caller's local calling area*") (emphasis added); *Verizon California, Inc. v. Peevey,* 462 F.3d 1142, 1159 (9th Cir. 2006) (noting that the *ISP Remand Order* "had no effect on the collection of charges by ILECs for originating

22 Similarly, Level 3 describes various "rules of the road"–such as a local exchange carrier's obligation to establish reciprocal compensation arrangements—that it claims apply to all *"locally dialed"* ISP traffic originating from Qwest's local exchange customers.[29] Of course the whole issue in this case is whether the rules pertaining to the exchange of local traffic should apply to traffic that is not in fact local, but merely "locally dialed." Therefore, Level 3's recitation of rules that apply to local interconnection simply misses the mark of the disputed issue.

**2. FCC Orders.**

**a. ISP Remand Order.**

23 Level 3 continues to argue that the ISP Remand Order "repudiated the 'local' distinction for determining the scope of Section 251(b)(5) intercarrier [reciprocal] compensation obligations,[30] and that the FCC knew of VNXX before the ISP Remand Order and therefore impliedly decided that ILECs owed some form of compensation for VNXX ISP-bound traffic.[31] These arguments were expressly rejected by the Federal District Court in the case to which Level 3 was a party. The argument is foreclosed by the Court's order.[32]

24 Similarly, the Joint CLECs argue that "ISP-bound traffic is governed by section 251(b)(5) and associated FCC rules, including the rules requiring reciprocal compensation."[33] To the extent that the Joint CLECs are asserting that *non-local* ISP-bound

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interexchange ISP-bound traffic ... [a]s this issue was not before the FCC when it crafted the *ISP Remand Order* ").

[29] Level 3 Br. at 21- 23.

[30] Level 3 Br. at 26-27.

[31] *Id.* at 27-28.

[32] *Qwest v. WUTC,* 2007 WL 1071956, *8 ("The WUTC's first interpretation error was its apparent reading of the *ISP Remand Order* as completely eliminating the distinction between "local" and "non-local" traffic. The defendants cling to this analysis, arguing that the *ISP Remand Order's* sweeping rejection of the local/non-local dichotomy is further evidence that the FCC's new compensation scheme applies to *all* ISP-bound traffic . . . The Court disagrees.")

[33] Joint CLECs Br. at 10.

traffic is subject to section 251(b)(5)'s reciprocal compensation requirements, their argument is also inconsistent with the decision of the Federal District Court, the Ninth Circuit's *Peevey* decision, and the First and Second Circuits' *Global NAPs I and II* decisions.[34] Pac-West made these same arguments to the federal district court to no avail. The federal courts have held that states are free to treat VNXX traffic as they see fit for purposes of intercarrier compensation because *it is interexchange traffic* and therefore not subject to section 251(b)(5).[35]

**b. Core Forbearance Order.**

25 Level 3 argues that the FCC, in its Core Forbearance Order, decided that its concerns regarding the arbitrage resulting from CLECs' receipt of terminating reciprocal compensation for ISP traffic had decreased and were now outweighed by the public interest in creating a uniform compensation scheme.[36]

26 In both the ISP Remand Order and the Core Forbearance Order, the FCC was addressing *local* ISP-bound traffic, not VNXX ISP-bound traffic.[37] As numerous federal courts have concluded, the FCC never intended to preempt the application of intrastate access charges to VNXX ISP-bound traffic. States retain authority to set compensation rates for inter-local calling area ISP-bound calls. The FCC only expressly considered the situation in which ISP equipment is located in each local calling area in which the ISP's customers are located.[38] VNXX allows CLECs to reduce costs by having centrally located

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[34] *See* Staff Opening Br. at 26; footnote 28, supra.
[35] *Id.*
[36] Level 3 Br. at 29; b*ut see Core Forbearance Order,* 19 F.C.C.R. at 20186 ¶¶ 18-19 (stressing that "the rate caps and mirroring rule remain necessary to prevent regulatory arbitrage and promote efficient investment in telecommunications services and facilities").
[37] *See* Staff Opening Br. at 26.
[38] *Id.*

ISP equipment. Therefore the Core Forebearance Order, like the ISP Remand Order, does not resolve the VNXX issue.

**c. <u>Other FCC orders.</u>**

**3. Federal Court Decisions.**

27 The Joint CLECs assert that the Ninth Circuit in *Peevey* "upheld the position that the Joint CLECs have taken in this case – that 'VNXX' provisioning of FX service is permissible and the traffic delivered to CLECs for termination to customers of this service is subject to reciprocal compensation."[39] Level 3's brief likewise appears to suggest that the Ninth Circuit, in *Peevey*, decided *as a matter of federal law* that the classification of call local depends solely on the NPA-NXXs of the calling and called parties, and that, *as a matter of federal law* reciprocal compensation is owed for transport and termination of "FX-like traffic."[40] That is not the case. Rather, the court upheld California's state law determination that reciprocal compensation should apply to such calls.[41]

28 More significantly, the court also upheld California's determination that VNXX calls are interexchange and therefore not covered by the *ISP Remand Order*. Consequently, the Court rejected Pac-West's argument that the Telecom Act and the FCC's rules pertaining to reciprocal compensation apply to VNXX traffic and upheld California's carrier origination charge (collected by the originating ILEC from the terminating CLEC).[42] The Court therefore distinguished cases cited in that case by Pac-West as dealing with "traffic that

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[39] Joint CLEC Br. at 11.
[40] Level 3 Br. at 30.
[41] 462 F.3d 1142, 1158.
[42] *Id.* at 1157, 58 ("Here, the CPUC applied its *own* balancing test in determining as a matter of fair compensation policy that VNXX traffic is subject to reciprocal compensation as "local" traffic; it did not make that determination under the *Telecommunications Act* or the *FCC's* rules for reciprocal compensation. Rather, the CPUC determined that VNXX traffic is interexchange traffic that is *not* subject to the FCC's reciprocal compensation rules.")

originated and terminated in the same calling area" that was "deemed local for purposes of federal law."[43]

29 This Commission should likewise determine, consistent with the AT&T/Qwest arbitration order, that VNXX traffic is interexchange. To the extent that the Commission wishes to require a form of intercarrier compensation to that traffic other than at the *ISP Remand Order's* reciprocal compensation cap of $.0007 per minute, it may do so pursuant to its authority to establish rates and practices for intrastate exchange access service.

**4. VoIP Preemption/ESP Exemption.**

30 Staff addresses VoIP issues in Section II.A.3, above.

**5. Other State Commission Decisions.**

31 The Joint CLECs express their approval of the Oregon PUC's resolution of the VNXX dispute. According to the Joint CLECs, the Oregon Commission "has long precluded all LECs from offering FX service but recently created an exception to that ban for FX service provided to ISPs as long as the LEC terminates traffic to those ISPs on a bill and keep basis."[44] The only distinction between the way the Joint CLECs describe the Oregon decision and Staff's recommendation in this case is that, under the Oregon approach, in the rare event that a CLEC customer calls a Qwest FX ISP customer, the CLEC would not be required to pay reciprocal compensation. Another result if this Commission were to adopt the Oregon approach, is that ILECs and CLECs alike would have to abandon FX service for non-ISP customers, regardless of how they provide the service.

32 One way to address the Joint CLEC's competitive neutrality concern would be to relieve CLECs of the obligation to pay reciprocal compensation when their customer

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[43] *Id.*
[44] Joint CLEC Br. at 12.

originates a call to an ILEC FX customer. However, as a practical matter, such a provision would probably have little effect because there is no evidence that CLECs serve the kinds of residential customers who make the dial-up Internet calls. In addition, prohibiting ILEC FX service for non-ISP customers, which has existed for decades, would be disruptive to the few customers that do rely on Qwest's FX service. Staff believes that there are reasonably inexpensive ways for CLECs to offer ordinary (non-ISP) FX service, without resort to VNXX arrangements, in those local calling areas where the CLEC actually has facilities and serves customers.[45]

*33* The Joint CLECs also express approval of the California PUC's approach to VNXX,[46] though again, they mention only the fact that California requires the payment of reciprocal compensation on VNXX traffic and not the fact that the CLEC must pay the originating ILEC an offsetting call origination charge for transporting the call.[47] Staff believes that the California approach, while analytically correct from the standpoint of requiring the CLEC to pay for the transport it receives from the ILEC, does not achieve the competitive neutrality that it takes as its benchmark. This is because it allows the CLEC to purchase its transport from the ILEC at TELRIC rates for shared transport, while the ILEC's FX customer has to pay much higher retail private line rates for the same functionality.[48] On the totality of the considerations, Staff believes it is preferable to require the CLEC to bear the TELRIC rate for the transport facilities (by allowing Qwest to exclude VNXX traffic

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[45] Staff Opening Br. at 6, 33-34.
[46] Joint CLEC Br. at 12.
[47] *Re Pacific Bell Telephone Company*, California Public Utilities Commission, Application 02-03-059, Decision 03-05-031, 2003 WL 21212003, pp. 4, 5 (May 8, 2003); *In the Matter of Verizon California, Inc. (U-10021-C) Petition for Arbitration with Pac-West Telecomm, Inc. (U5266-C) Pursuant to Section 252(b) of the Telecommunications Act of 1996*, California Public Utilities Commission, Application 02-06-024, Decision 03-05-075, pp. 7, 8 (May 22, 2003).
[48] 2003 WL 21212003, at * 7 (Cal. P.U.C. May 8, 2003); Cal. PUC Decision 02-06-076 at 28 (July 5, 2002) http://www.cpuc.ca.gov/word_pdf/FINAL_DECISION/17122.pdf ; Brotherson, Exh. No. 24T, 5:4 – 5:12.

from the relative use factor for the interconnection facilities), and to reduce the reciprocal compensation rate on VNXX ISP-bound traffic to zero (*i.e.*, bill-and-keep).

*34* Finally, in its brief, ELI advocates for this Commission to follow the New Hampshire Commission's approach to VNXX.[49] The New Hampshire Commission allows VNXX for ISP-bound traffic subject to the use of a special statewide "information access NXX."[50] However, New Hampshire appears to have declined to decide the compensation applicable to such traffic, stating "[i]ntercarrier compensation, i.e., terminating access, originating access, and reciprocal compensation, for this traffic will be governed by the FCC."[51] As for *voice* VNXX service, which the New Hampshire commission terms "CLEC FX," the CLECs are only allowed to provide the service to the extent that they have a "local nexus" in the local calling area from which they seek to offer the service.[52] But if a company could meet the local nexus requirement, it could also provide FX service in the manner described by Mr. Williamson at relatively modest expense.[53] The more significant difference between the New Hampshire approach and Staff proposal here is that Staff would require the CLEC to provision a private line in the same manner that Qwest provides FX service rather than obtaining the transport for free from Qwest.[54] The private line requirement is necessary because it is what defines FX service. It is also necessary for competitively neutrality because Qwest is only required to haul traffic to CLECs'

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[49] ELI Br. at 14-16.
[50] *Investigation as to Whether Certain Calls are Local,* DT 00-223, *Independent Telephone Companies and Competitive Local Exchange Carriers – Local Calling Areas,* DT 00-054, New Hampshire Public Utilities Commission, Final Order, Order No. 24,080, pp. 53-54 (October 28, 2002).
[51] *Id.* at 55.
[52] *Id.* at 56, 57; In deciding on the treatment of VNXX traffic, the New Hampshire Commission stated "[w]e note that our ruling applies to ISP-bound data traffic not to Internet telephony. Inasmuch as the issue of Internet telephone [i.e., VoIP] has not been brought before us, we decline to rule on it at this time." *Id.* at 55.
[53] *See* Staff Opening Br. at 33, 34.
[54] *See* ELI Br. at 15, 16.

interconnection points at its own expense on the presumption that the CLEC meets the quid pro quo of hauling the call back to the local calling area from which the call originated.[55] That is not the case with the type of VNXX that ELI describes. Rather, as with all VNXX, the call terminates at or near the CLEC's interconnection point.[56]

## III. VNXX RELATIONSHIP TO OTHER SERVICES

### A. Foreign Exchange Service.

35 One the CLEC's main themes is that VNXX is "functionally equivalent" to Qwest's FX service, including the FX arrangement that Qwest's affiliate, QCC, uses to provide Wholesale Dial.[57] Staff agrees, but if VNXX is to be allowed in the interest of fair competition in the market for FX services, the question remains as to what the appropriate intercarrier compensation should be for that traffic.

36 Imagining what might constitute competitive neutrality between Qwest and the CLECs is difficult because ILEC and CLEC networks are nowhere near equal in size and reach and CLECs are in many respects dependent on Qwest. The CLECs argue that their networks are more technologically advanced and that is why they are able to provide an FX-like service without using private line transport, as Qwest does. They suggest that VNXX should be allowed, and reciprocal compensation should apply to VNXX traffic, because their superior FX technology is winning out in the competitive market. Level 3 says that CLECs have leveraged technological advances so they do not need to use additional switching and dedicated transport to provide FX functionality.[58] Similarly, ELI argues that

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[55] 2003 WL 21212003, at * 3, 4 (Cal. P.U.C. May 8, 2003).
[56] ELI Br. at 19:9-11.
[57] Joint CLEC Br. at 13; Level 3 Br. at 35.
[58] Level 3 Br. at 36; Level 3 also argues that Qwest's proposal of a "physical presence" requirement for CLEC FX services would "penalize the CLEC for deploying a more advanced network." *Id.* at 24.

CLECs "use more modern methods which provide a functionally equivalent service for customers which utilizes fewer resources."[59]

37 But in the context of VNXX, the only thing Level 3 and other CLECs have "leveraged" is the regulatory requirement that Qwest must transport calls across local calling area boundaries for delivery to a centralized points of interconnection. CLECs are able to provide "FX-like" VNXX service only to customers (usually the CLEC itself acting as a wholesale ISP) that happen to be physically located immediately next to the CLEC's single switch. The reason it is unnecessary for either the CLEC or its customer to provide transport is because Qwest is obligated as a *regulatory* matter to aggregate traffic from its customers to that location for delivery to the CLEC (under the arrangement called "single point of presence" or "SPOP").[60] And because of the one-way nature of ISP-bound traffic, after application of the relative use factor to the local interconnection facilities, Qwest ends up paying the full cost of transporting the call from the distant local calling area to the CLEC's single switching and Internet access facility.[61]

38 Some of the CLECs who focus on the ISP niche appear to have no interest in ever building out facilities to provide local phone service to customers who are located outside of the local calling area where their point of interconnection is located. They express resentment at Staff's suggestion that in order to provide voice FX service they might need to have some equipment in the local calling area where they purport to be providing *local* service. Their resentment is misplaced. As the California Commission stated in requiring

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[59] ELI Br. at 1.

[60] Brotherson, Exh. No. 24T, 6, 7.

[61] *See* 47 C.F.R. § 54.709(b); Note, however, that this and other FCC interconnection rules only apply to local and not interexchange traffic such as VNXX. *Verizon California, Inc. v. Peevey,* 462 F.3d 1142, 1158 (2006). Therefore, this Commission is free to exclude VNXX traffic from the relative use factor as a matter of fair competition policy.

CLECs to pay ILECs for the cost of transporting VNXX calls from origination to the point of interconnection:

> The policies of this Commission and the Telecom Act precisely intends for carriers to invest in facilities based on the innovation incentives inherent in an openly competitive market. We refrain from creating an incentive that distorts marketplace investments by requiring incumbents either to either subsidize its competitors or shift costs to local exchange customers for inter-exchange traffic that is destined beyond the origination rate center. Such policy would encourage CLECs to become providers of termination facilities, to collect reciprocal compensation and thereby avoid investment in multiple points of interconnection, switching, and transport, and result in less network redundancy than facilities based competition economics would otherwise dictate.

SPOP makes sense when a CLEC actually bears a cost, which is symmetrical with that of the ILEC, of hauling calls over transport facilities that it owns or leases from CLEC customers located in distant local calling areas to the point of interconnection that it shares with the incumbent. SPOP does not make sense when the CLEC decides to make a business of taking incoming traffic from the incumbent and then immediately terminating it to an Internet gateway that is located at or near the single point of interconnection. The California Commission discusses this at length in its decisions.[62]

*39* This seems to be one of the reasons the New Hampshire commission imposed a requirement that in order to provide "FX-like" VNXX service using numbers associated with a particular local calling area, a CLEC has to have at least one customer physically

[62] E.g., 2003 WL 21212003, at *3, 4 ("The Commission is deciding prior arbitration agreements concluded that CLECs would be absolved from paying the costs associated with transport from origination to the point of interconnection on the condition that the . . . traffic was returned and terminated within the rate area where the local call originated. For foreign exchange type of service, where the traffic doe not return to the originating rate center, such traffic would be subject to transport charges. . . . The rationale supporting the premise of the ILEC not having to pay for transport [and consequently requiring the CLEC to do so] for [for foreign exchange type VNXX calls] was based on a quid pro quo that the CLEC bears the cost of returning the traffic from its point of interconnection to the local calling rate center.")

located in that local calling area.[63] This "local nexus" requirement ensures some minimal investment on the part of the CLEC to provide actual local service. Similarly, it is why the California Commission, while it required the ILEC to pay reciprocal compensation on VNXX traffic, also required the CLEC to pay the ILEC an offsetting call origination charge to compensate the ILEC for transporting the call.[64] And it is the reason why many state commissions simply prohibit VNXX.[65]

40 Level 3 says that if the Commission decides that a CLEC must have some kind of "local presence" (e.g., a switch, portion of a switch, or a channel bank) in order to offer FX service, the Commission "should find that the CLEC local interconnection transport (e.g., DEOT/DTT trunks), establishes a 'local' presence in the local calling area. This CLEC trunk is the functional equivalent of the private line in ILEC FX and other ILEC FX-like services."

41 The most obvious fallacy of this argument is that, after the application of the relative use factor, because Level 3 terminates almost all of the traffic carried over its local

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[63] *Investigation as to Whether Certain Calls are Local*, DT 00-223, *Independent Telephone Companies and Competitive Local Exchange Carriers – Local Calling Areas*, DT 00-054, New Hampshire Public Utilities Commission, Final Order, Order No. 24,080, p. 56 (October 28, 2002) ("Going forward, a CLEC may offer FX-like service for non-ISP bound traffic only when it is providing service to at least one customer physically located in the exchange from which the FX service is requested. For this purpose, the CLEC must be providing local dial tone via its own facilities, over and EEL arrangement or by using UNE loops.")

[64] *Re Pacific Bell Telephone Company*, California Public Utilities Commission, Application 02-03-059, Decision 03-05-031, 2003 WL 21212003, pp. 4, 5 (May 8, 2003); *In the Matter of Verizon California, Inc. (U-1002l-C) Petition for Arbitration with Pac-West Telecomm, Inc. (U5266-C) Pursuant to Section 252(b) of the Telecommunications Act of 1996*, California Public Utilities Commission, Application 02-06-024, Decision 03-05-075, pp. 7, 8 (May 22, 2003).

[65] *See, e.g., Global NAPs, Inc. v. Verizon New England, Inc.*, 454 F.3d 91, 101 (2006) ("[A]lthough virtual NXX and FX share some similarities, there is one fundamental difference: retail customers using FX service purchase a foreign exchange line, paying the costs both of installation of the line and of transportation of bulk traffic between the two points of communication. Virtual NXX customers, on the other hand, do not purchase any lines or pay transportation costs, but rely on the terminating carrier to provide the service without cost. [Prohibiting] virtual NXX does not necessarily prevent users from obtaining nongeographically correlated numbers; the ban simply requires that someone pay Verizon for use of its infrastructure.")

interconnection facilities with Qwest, Level 3 does not pay anything for the DEOT/DTT trunk—Qwest picks up the entire cost. Therefore, neither Level 3 the CLEC, nor Level 3 the wholesale ISP, nor Level 3's ISP customers pay the cost of transporting the VNXX call to Level 3's switch. By contrast, QCC, as a retail customer of Qwest, must pay for PRI service in each LCA where it wishes to receive local calls (pursuant to the longstanding ESP exemption) and for a private line to transport the call to its location.[66]

42 The Joint CLECs point out that when a CLEC customer calls a Qwest FX customer, the CLEC has to pay Qwest reciprocal compensation (and consequently, receives no originating access).[67] They then argue that "[i]f a CLEC is obligated to pay Qwest reciprocal compensation for [calls made by a CLEC customer to a Qwest FX customer], there is no reasoned basis for Qwest to compensate the CLEC for calls to the CLEC's FX customers, regardless of how the CLEC provisions that service."[68]

43 First, there is no evidence that CLECs like Level 3 and Pac-West actually serve any residential customers who reach their ISP by dialing up an ISP served over Qwest's wholesale dial service. Qwest overwhelmingly serves the consumers who use dial-up services. Therefore, this is a purely hypothetical argument.

44 Second, the important point, as noted previously, is that a Qwest FX customer (such as QCC when it is providing wholesale dial to ISPs) has to pay for retail private line transport from every local calling area to its server or modem bank location. By contrast, neither the CLEC nor its VNXX customer (under the CLEC's proposal) has to pay anything for transport—Qwest must absorb the cost. Qwest doesn't have the ability to require

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[66] Linse, Tr. at 136:24 – 138:14; Brotherson, Exh. No. 24T, 4, 5.
[67] Joint CLECs Br. at 14.
[68] Joint CLEC Br. at 15.

another carrier to haul calls from end-users of ISP dial-up service for free to a centrally located server.

45 Staff proposes that the Commission allow CLECs to use VNXX arrangements for ISP-bound traffic, without the need to place switching facilities in local calling areas. Qwest would be relieved, however, of the portion of the expense of the local interconnection facilities that are used to originate ISP-bound VNXX calls (the equivalent of FX private line transport), and of the obligation to pay reciprocal compensation on those calls (for which it would otherwise be receiving originating access charges).

**B. <u>800 Service.</u>**

46 Level 3 and other CLECs distinguish 800 service from VNXX by describing technical differences in the way the service is provided.[69] Staff's point is simply that the services are functionally equivalent, yet with 800 service there is no misassignment of geographic telephone numbers and no toll bypass. Ironically, Level 3 makes the same kind of "functional equivalency" argument with respect to Qwest's FX service, but then focuses, in the case of 800 service, on the technical aspects of how the service is provided in order to distinguish it from VNXX.

**C. <u>Market Expansion Line/Remote Call Forwarding Services.</u>**

47 Level 3 and the Joint CLECs assert that remote call forwarding is functionally equivalent to VNXX. They say that when a CLEC customer calls a MEL customer with a local call, and the call is then forwarded (as a second, long distance call carried by an interexchange carrier, which the MEL customer pays for), the CLEC does not get

[69] Level 3 Br. at 37-38.

originating access charges[70] but instead pays reciprocal compensation (assuming the first call is local).

48 While this is true, remote call forwarding in fact involves two calls, and if one of those calls is an interexchange call, it must be handed off to an interexchange carrier and access charges apply. There is no toll avoidance. The reason reciprocal compensation applies to the first call is because it is truly a local call.[71] If a CLEC were to attempt to use this service as a way of providing VNXX, as suggested in the brief of the Joint CLECs[72] it would be objectionable for the same reason as VNXX—namely, it would result in Qwest bearing an uncompensated cost of transporting the call to the distant local calling area and the failure of anyone to pay access charges.

**D. One Flex Service.**

49 One Flex is a VoIP service. Intercarrier compensation for the PSTN leg of a VoIP call was addressed by the Commission in UT-063006.[73] Issues surrounding VoIP are outside of the scope of this proceeding.

**E. Other Services.**

50 N/A.

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[70] Level 3 Br. at 39.

[71] Staff Opening Br. at 35.

[72] at 18.

[73] In the Matter of the Petition of Level 3 Communications, LLC, Docket No. UT-063006, Order 12, Final Order, at 11, 12 (June 7, 2007).

## IV. VNXX POLICY CONSIDERATIONS

### A. Cost Issues.

51 The Joint CLECs correctly observe that the parties disagree about how cost causation should be determined in the context of VNXX. In addition to asserting the legal theory that Section 251(b)(5) requires Qwest to pay them reciprocal compensation for terminating VNXX traffic, Level 3 and the Joint CLECs also advance the *economic* theory that Qwest should compensate the CLECs for the costs they incur in terminating VNXX calls. Level 3 asserts that "[c]ost causation analysis in the industry is based on the concept of 'calling party pays.' . . . A Qwest customer causes a cost when he or she dials an ISP or when he or she dials another business; Qwest is [sic.] proposing to make other businesses pay for the costs of the calls they receive, and the Commission should not single out ISPs as Qwest suggests."[74]

52 The only WUTC "precedent" that Level 3 can point to as articulating its preferred cost causation theory is a 1999 letter (prior to the *ISP Remand Order*) from the Commission to the FCC that concerned ISP-bound traffic, but not VNXX traffic.[75] The actual Commission decisions cited by Level 3 merely relied on the *legal theory* that the *ISP Remand Order* requires a form of reciprocal compensation for all ISP-bound traffic, regardless of whether it is local or interexchange.[76] As noted above, that theory was rejected by the Federal District Court.

[74] Level 3 Br. at 43, 44.
[75] Level 3 Br. at 44.
[76] *Id.*

53 Even if the ISP-bound calls at issue here were indisputably local, rather than interexchange, the CLEC's argument would still fail because it depends on a cost-causation theory that the FCC found to be flawed in the ISP Remand Order:

> [W]e now believe that the Commission's concerns [in earlier decisions] about economic inefficiencies associated with bill and keep missed the mark, particularly as applied to ISP-bound traffic. The [FCC in an earlier decision] appears to have assumed, at least implicitly, that the calling party was the sole cost causer of the call, and it may have overstated any incentives that a bill and keep regime creates to target customers that primarily originate traffic. A carrier must provide originating switching functions and must recover the costs of those functions from the originating end-user, not from other carriers. Originating traffic thus lacks the same opportunity for cost-shifting that reciprocal compensation provides with respect to serving customers with disproportionately incoming traffic. Indeed, it has become apparent that the obligation to pay reciprocal compensation to interconnecting carriers may give rise to uneconomic incentives. As the current controversy about ISP-bound traffic demonstrates, reciprocal compensation encourages carriers to overuse competing carriers' *origination* facilities by seeking customers that *receive* high volumes of traffic.
>
> We believe that a bill and keep regime for ISP-bound traffic may eliminate these incentives and concomitant opportunity for regulatory arbitrage by forcing carriers to look only to their ISP customers, rather than to other carriers, for cost recovery. As a result, the rates paid by ISPs and, consequently, their customers should better reflect the costs of services to which they subscribe. Potential subscribers should receive more accurate price signals, and the market should reward efficient providers.[77]

The FCC's economic analysis supports bill-and-keep for *local* ISP-bound traffic, but the FCC stopped short of imposing a zero rate not based on its economic analysis, but in order not to upset the expectations of those CLECs who serve ISPs by enabling true local dial-up ISP calls.[78] That FCC's concern about the CLECs' dependency on reciprocal compensation should not extend to VNXX, where CLECs are able to provide ISP dial-up access much more cheaply. TCG Seattle—which exchanges VNXX traffic with Qwest under a bill-and-

[77] Order on Remand and Report and Order, FCC 01-131, ¶ 73 (April 27, 2001).
[78] *Id.* at ¶ 77.

keep arrangement—observes in its brief, ". . . CLECs' provision of VNXX service has allowed ISPs to concentrate modem equipment in a centrally located manner, rather than distributed in every local calling area. ISPs have been able to pass the cost efficiencies from this centralization on to users of their dial-up service."[79] Because VNXX affords such savings to CLECs as compared with locating modem banks in each local calling area, there is no reason why bill-and-keep should not prevail.

*54* Additionally, VNXX traffic is fundamentally interexchange traffic and would otherwise result in an inflow of originating access to the ILEC rather than an outflow of reciprocal compensation. WITA argues that if VNXX is allowed, the transport cost should be borne by the CLEC, since it is the CLEC that gains the benefit of avoiding access charges.[80] And as the California Commission explained, if the rationale for allowing VNXX is to put CLECs on an equal footing with ILECs in the provision of FX service, the CLECs need to compensate the ILEC for the cost of transporting the call from the distant local calling area to the CLEC's point of interconnection.[81] Staff believes this is the correct analysis. However, rather than requiring the ILEC to pay reciprocal compensation and the CLEC to pay an offsetting carrier origination charge (which California set at the TELRIC rate for shared transport), Staff believes that simply reducing reciprocal compensation to zero (bill-and-keep), is more administratively simple. (Moreover, as stated in Section II.D.5 (Other State Commission Decisions) above, the TELRIC rate for shared transport is still not competitively neutral as Qwest must provision a dedicated private line to its FX customer.)

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[79] TCG Br. at 14.
[80] WITA Br. at 6.
[81] 2003 WL 21212003, at * 3, 4 (Cal. P.U.C. May 8, 2003).

55 The Joint CLECs argue it is not true that reciprocal compensation for VNXX traffic puts upward pressure on Qwest's local service rates because there is no study to show this and Qwest rates haven't increased since 1998.[82] Staff's point was simply that when Qwest pays reciprocal compensation rather than receiving originating access payments, it has less revenue. This proposition requires no empirical support. Whether that translates immediately into a need for a local service rate increase is irrelevant.

56 ELI argues that "it does not use a single point of presence that would require Qwest to haul ELI's traffic around the State."[83] It is perhaps for this reason that ELI favors the New Hampshire commission's allowance of VNXX for voice calls subject to a "local nexus" requirement in a given local calling area.[84] If it is true that ELI is situated differently than other CLECs with respect to the transport costs that its VNXX service imposes on Qwest (which Staff is not convinced it is), then ELI should be allowed an interconnection agreement with Qwest that acknowledges that fact.

57 Staff is proposing that the Commission prohibit VNXX for voice service. Staff has suggested, however, that CLECs need not locate a full switch in a local calling area from which they wish to offer foreign exchange service, but could place remote subscriber loop carrier equipment or a channel bank as a means of providing dial tone from that local calling area. Level 3 attacks this on the grounds that it would require what Level 3 calls "zig-zag" or "triple transport." The Joint CLECs say that "Staff proposes that a CLEC collocate in the Qwest serving wire center and deploy excess transport so that a call from a Qwest customer and a CLEC FX customer would travel from the Qwest wire center to the CLEC switch,

[82] Joint CLECs Br. at 22.
[83] ELI Br. at 16.
[84] ELI Br. at 15.

then back to the Qwest wire center, then back to CLEC switch location and on to the customer."[85] The joint CLECs assert there is no regulatory requirement for this.[86]

58 As explained in Staff's opening brief, companies who wish to compete in the market for local exchange services have been afforded the opportunity to do so without locating a switch within every local calling area where they wish to provide service.[87] Instead, they may place a single switch in a LATA to which the ILEC is obligated to haul the calls originated on its network. The CLEC must then bear the cost of hauling the call back to its customer in the distant local calling area. Thus, CLECs tend to have high transport costs, but this is a cheaper alternative than locating an expensive switching in every local calling area where the CLEC wants to provide local phone service. Thus, under ordinary circumstances, there exists what Level 3 might term "double transport."[88] The third leg of the "triple transport," to which Level 3 refers, mirrors the private line transport that any customer of Qwest's FX service must pay for in order to receive local service within the exchange it chooses. Unless a CLEC is providing dial-up ISP service through centralized server in each LATA, then it would only be a coincidence that the customer served over the private line was located immediately next to the CLEC's switch. A typical non-ISP FX customer might just as likely be a tire shop in Tacoma wishing to make and receive local calls from customers in Olympia, and so the private line would run from the channel bank or subscriber loop carrier equipment in Olympia to the customer's location in Tacoma. In such a case, the CLEC would have no choice but to use a private line. The "triple transport" argument is a rhetorical distraction.

[85] Joint CLEC Br. at 16.
[86] *Id.*
[87] Staff Opening Br. at 2, 3.
[88] *See* ELI Br. at p. 18:11—19:2 ("While the call takes a seemingly circuitous route, it is actually more efficient for ELI to provide local service this way.")

## B. Impact on Access Regime/Impact on Competition.

59 Joint CLECs argue that VNXX is not toll bypass because it is the only way for a CLEC with a single switch per LATA to provide an FX service, and because customers will not make long distance calls to the Internet.[89] As stated previously, Staff's proposal would allow VNXX for ISP-bound traffic, however, the CLECs should not receive reciprocal compensation on such traffic and Qwest should not bear the transport costs.

60 Level 3 says that there is no evidence that VNXX imposes any cost on Qwest in addition to what a local call would impose.[90] Staff agrees with this, but a VNXX call *is not a local call*, and to the extent that it is allowed on the theory that it is a competitive substitute for ILEC FX services provided to ISPs, it is inequitable for Qwest to have to bear the expense of transport. There also is no cost-causation or cost-recovery theory to support the payment of reciprocal compensation on such calls. Bill-and-keep is preferable because of the perverse incentives created by requiring reciprocal compensation on one-way ISP-bound traffic. Because of the savings CLECs enjoy as a result of having only one server per LATA, instead of within each local calling area, the FCC's concerns about CLECs' dependence on some level of reciprocal compensation should not apply.

61 Level 3 says that there is no history of using access charges on ISP-bound calls to subsidize other phone service rates. *Id.* Staff does not disagree with the notion that access charges were devised before dial-up ISP traffic existed. WITA, however, asserts that this is not true in the case of rural incumbent local exchange carriers for whom a substantial change to the access charge regime occurred in 2000.[91] While WITA may raise a valid point, it is

[89] Joint CLECs Br. 23.
[90] Level 3 Br. at 45, 46.
[91] WITA Br. at 8, 9.

necessary to balance the disparate interests of many parties with regard to this issue. ILEC foreign exchange service has long existed and has long been an exception to the payment of access charges on inter-local-calling area calls. Qwest has come to utilize FX-like arrangements with its affiliate QCC to provide ISP local number presence services—lawfully in Staff's view. Staff's proposal seeks to preserve a more equitable form of competition in that market—a market that appears to be declining market as a result of the growing popularity and deployment of broadband facilities. By limiting the use of VNXX to dial-up ISP traffic, Staff's proposal seeks to prevent further erosion of access charges revenues to the WITA's members.

### C. **Consumer Impact.**

*62* Level 3 misconstrues Staff's recommendation, suggesting that Staff would require what Level 3 terms "triple-transport" *for ISP-bound traffic.*[92] Similarly, the Joint CLECs assert that competition in local-number-presence service for ISPs would suffer if VNXX were prohibited.[93] Staff is not recommending a prohibition on ISP-bound VNXX calls. Rather, Staff is recommending allowing VNXX arrangements for ISP-bound traffic, subject to bill-and-keep. Thus, Staff is not recommending that CLECs utilizing VNXX for ISP-bound traffic make any changes to their networks, but merely that Qwest not be required to pay reciprocal compensation on those ISP-bound calls. Bill-and-keep is the rule in many jurisdictions where Level 3 competes, including Colorado,[94] and has been agreed to voluntarily by at least two CLECs in this state. Staff does not believe it is reasonable to

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[92] Level 3 Br. at 50.
[93] Joint CLEC Br. at 24, 25.
[94] Greene, Tr. 607:10-25.

anticipate that competitors will disappear from the market as a result of the proposed adjustment in compensation for ISP-bound VNXX traffic.

*63* If a CLEC wishes to offer *voice* foreign exchange service, however, it would have to do so by way of equipment located in the local calling area. All the evidence suggests that CLECs are offering very little voice "FX" service and Level 3 is offering none. It may be appropriate for the Commission to allow for grandfathering of existing voice customers served over VNXX or to provide for a transition period to the type of engineering described by Staff. The Commission could direct the parties to address this in any ICA amendments necessary to comply with a commission order prohibiting VNXX arrangements for non-ISP customers.

### D. Impact on Independent ILECs.

*64* Staff addresses the impact on Independent ILECs in Sec. IV.B. (Impact on Access Regime) above.

### E. Other Public Policy Considerations.

*65* Level 3 says that Staff may not rely on the FCC's rationale for applying bill-and-keep to ISP-bound traffic, which the FCC stated in the ISP Remand Order, because it has been repudiated by the Core Forebearance Order and the Missoula Plan.[95]

*66* Level 3 is simply wrong that the Core Forebearance Order repudiated bill-and-keep for ISP Bound traffic. Rather, the Order merely removed the new market restrictions and growth caps that had been announced in the *ISP Remand Order*.[96] While the FCC did state a preference for uniform compensation for ISP-bound traffic, the ISP-bound traffic to which

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[95] Level 3 Br. at 52.
[96] *See* Staff Opening Br. at 25.

it is referring must be interpreted as *local* ISP-bound traffic only.[97] As numerous court have now concluded, the FCC did not intend for its $.0007 compensation scheme to override the intrastate access charge regime that applies to ISP-bound calls between local calling areas.[98]

67 The outcome of the FCC's intercarrier compensation NPRM remains unknown. Thus, the *ISP Remand Order* still provides the most thorough analysis from the FCC regarding the arbitrage problems related to ISP-bound traffic. The fact that VNXX traffic is not even local ISP traffic, but is in fact interexchange traffic on which Qwest would ordinarily receive access charges further supports the proposal that Qwest at least should not be required to pay terminating compensation on such calls.

68 A further question is whether Qwest should be apportioned the cost of local interconnection service facilities that is attributable to VNXX traffic originated on Qwest's network. In the Commission's recent June 7, 2007, Final Order in docket UT-063006 the Commission stated it would refrain from deciding how to apply a relative use factor until the issues of classification and compensation for VNXX traffic have been resolved.[99]

69 Level 3 states that the Commission previously held, in UT-023042, Third Supp. Order at 7 (Nov. 27, 2002), that FCC rules "apportion[] the cost of interconnection trunking based on the amount of traffic *originated* by the interconnecting carrier." Level 3 then says that accepting Qwest's argument that it should not be apportioned the facility costs (under the relative use factor) of ISP-bound VNXX traffic would "'charge Level 3 for calls originating with Qwest's customers and terminating on Level 3's network,' in violation of FCC rules." The Commission order cited by Level 3 dealt with 47 C.F.R. Sec. 51.709(b).

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[97] *See Qwest v. WUTC*, 2007 WL 1071957, p. 11, 12.
[98] Staff Opening Br. at 26.
[99] Paragraphs 19 and 22.

In the cited WUTC order, the Commission was not specifically addressing *VNXX* ISP-bound traffic, but ISP-bound traffic generally, which would have been presumed to be terminating within a local calling area (and not at ISP equipment located outside the caller's local calling area as is the case with VNXX). To the extent that Level 3 is asserting that VNXX traffic is "local" traffic within the meaning of the FCC's rule (or more specifically, traffic for which the FCC has required reciprocal compensation), that argument is inconsistent with the Ninth Circuit's decision in *Verizon California, Inc. v. Peevey.*[100] The FCC's rules do not apply to VNXX ISP-bound traffic because such traffic is interexchange and does not come within the FCC's interconnection rules except to the extent that a state decides, as a matter of state law and policy, that it can and should be addressed in a local interconnection agreement. For reasons discussed elsewhere in this brief, the Commission should require CLECs to pay for the cost of interconnection facilities attributable to ISP-bound VNXX traffic.

## V. STAFF PROPOSAL

70 Most of the parties' criticisms of Staff's proposal are addressed in other portions of this brief. For example, the Joint CLECs say Staff's proposal is discriminatory because it would relieve Qwest of paying reciprocal compensation on Qwest originated/CLEC terminated VNXX calls, but would not relieve CLECs of paying reciprocal compensation on CLEC originated calls to Qwest FX customers.[101] Staff addresses this argument in Section III.A (Foreign Exchange Service), above. The Joint CLECs also argue that Staff's proposal is discriminatory because it would allow Qwest to offer FX service to non-ISP customers, but would not allow CLECs to do so.[102] Staff addresses this argument in Section IV.A

[100] 462 F.3d 1142, 1159 (2006).
[101] Joint CLEC Br. at 26.
[102] Joint CLEC Br. at 26.

(Cost Issues). The Joint CLECs argue that Staff's proposal fails to provide any justification for denying CLECs compensation for terminating calls to their VNXX customer when "CLECs continue to incur switching costs to terminate that traffic, just as Qwest incurs switching costs to terminate calls to its FX customers."[103] This argument is also addressed in Section IV.A (Cost Issues). Finally, Level 3 says that requiring it to mimic the incumbent's network and employ "zig-zag" transport would be discriminatory.[104] This too, is dealt with in Section IV.A (Cost Issues).

71 One criticism not addressed elsewhere arises from an apparent misunderstanding of Staff's proposal. Level 3 seems to believe that Staff is recommending that the Commission require a change in the handling of VoIP traffic. That is not the case. The proper routing and compensation for VoIP traffic is an issue in the arbitration just concluded between Level 3 and Qwest in docket UT-063006. It is not Staff's recommendation to require, in this proceeding, any change in the way any carrier handles the PSTN leg of a VoIP call, the use of numbering resources for VoIP, or intercarrier compensation for VoIP calls. Therefore, the Joint CLECs' assertion that Staff's proposal would prohibit CLECs (but not Qwest) from providing FX service to VoIP customers is also unfounded.

72 Level 3 and the Joint CLECs criticize Staff's "reliance" on findings of the New Hampshire commission staff for Staff's proposal that VNXX should be prohibited for ordinary voice services.[105] Staff's proposal to prohibit VNXX for ordinary voice calling does not require any "evidence" because it is based on the legal classification of calls between customers in different local calling areas as interexchange.

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[103] Joint CLEC Br. at 27.
[104] Level 3 Br. at 53.
[105] Level 3 Br. at 51, 52; Joint CLEC Br. at 27.

73 While TCG Seattle agrees with Staff that public policy supports allowing CLECs to use VNXX arrangements to provide ISP-bound service subject to bill-and-keep, it would oppose Staff's proposal to prohibit VNXX that is "functionally equivalent" to Qwest's FX service.[106] TCG asserts that a "better approach would be to allow VNXX for voice services and handle individual CLEC abuses, if any occur, through the existing complaint processes." Staff's point, however, is that there is no circumstance, absent a *bona fide* foreign exchange arrangement, under which such a call would not be classified as interexchange and therefore toll bypass. No evidence is required that companies are using VNXX for ordinary voice service to know that it should be prohibited. The considerations that support allowing VNXX for ISP-bound traffic are absent in the case of voice traffic. The New Hampshire study simply shows there are entities that stand ready to take full advantage of the toll bypass opportunity that voice VNXX would provide. This record also provides the example of LATA-wide "local" calling.[107]

74 Level 3 makes the legal argument that, under Staff's proposal, if it wishes to receive reciprocal compensation for VNXX calls, it would have to duplicate the network of the existing carrier and that this would represent a barrier to entry that violates Sec. 253 of the Act.[108] Level 3 also says that bill-and-keep for VNXX would violate Sec. 252's various requirements applicable to the exchange of local (as opposed to interexchange) traffic. These arguments are plainly invalid, as three federal circuit courts of appeal, including the Ninth Circuit, have upheld against CLEC challenge state commission orders prohibiting VNXX outright, or requiring CLECs to pay the ILEC for the cost of transporting the call

[106] TCG Br. at 15-17.
[107] *See* Staff Opening Br. at 46, 47.
[108] Level 3 Br. at 54.

from the distant local calling area. The latter does not violate Sec. 252's reciprocal compensation requirement or related rules because the traffic in question is interexchange and, as such, not subject to Sec. 252.[109]

75 Finally, Advanced Telecom, Inc. (ATI) states in its brief that Staff's proposal does not belong in this complaint proceeding because several CLECs and at least one ILEC (Verizon) and other companies and customers would presumably be subject to the change and will have no notice "that this Complaint proceeding against a few CLECs, had morphed into a rate-setting proceeding for reciprocal compensation for ISP traffic."[110] ATI states that if the Commission concludes that VNXX should not be banned, "then a proceeding should be conducted to determine what, if any, changes should be made to the compensation scheme for such traffic."[111] Staff is not asserting that the Commission's order in this case should be binding on any carrier not a party to this case. Staff agrees it could not be, though it may have *precedential* effect in later cases.

76 It should be remembered that WITA tried to initiate an industry-wide declaratory ruling, but Level 3 refused to participate and therefore prevented the matter from going forward.[112] There is nothing wrong with Qwest proceeding to resolve matters related to VNXX on a company-by-company complaint basis, or a multi-party complaint such as this. Many states have addressed these matters in company-specific proceedings rather than rulemaking. This Commission invited Qwest to bring this complaint to address the appropriateness of VNXX arrangements generally, and the Commission has authority under

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[109] *See* Staff Opening Br. at 26.
[110] ATI Br. at 13.
[111] *Id.*
[112] *See* Staff Opening Br. at 17, 18.

RCW 80.36.140 to determine, upon complaint, the reasonable and proper practices to be observed by telecommunications companies.

77 Similarly, the Joint CLECs argue that if "Qwest, Staff, or another party seeks establishment of a new law, the proper recourse is either to the legislature of to request that the Commission initiate a rulemaking to address whether and the extent to which any local exchange carrier ("LEC") should be permitted to assign telephone numbers to customers who are not physically located in the local calling areas to which those numbers are rated."[113] Legislation is not required to implement what Staff proposes. This Commission has authority to prescribe exchange area boundaries, to prescribe practices of telecommunications carriers, and to fix rates for intrastate exchange access service.

## VI. QWEST/MCI VERIZON ACCESS SETTLEMENT

### A. Standards for Approval of Negotiated ICA.

78 The standards for approval of negotiated interconnection agreements have been accurately stated by other parties.

### B. Terms and Conditions.

79 If the Commission accepts Staff's proposal to prohibit VNXX for voice traffic, Verizon Access will have to comply, regardless of whether it amends the language of its interconnection agreement with Qwest.

80 Verizon Access objects to Staff's proposed prohibition on VNXX for voice traffic, stating that "if either party had concerns about the potential impact the amendment could have on toll bypass, that would have been addressed as part of the negotiation of the

[113] Joint CLEC Br. at 4.

business interests between Qwest and Verizon Access."[114] The problem with this argument is that it ignores the interest of the Independent CLECs who were not party to the negotiations and who arguably would lose toll revenue if voice VNXX were allowed.

81 Verizon Access also argues that "there is no evidence in the record that toll bypass with regard to voice VNXX is even an issue."[115] Like other CLECs, Verizon Access says Staff relies on a study about New Hampshire and statement that there is no reason to believe that the situation in New Hampshire is different than New Hampshire. As stated above, the error of this argument is that no evidence is required to prohibit this form of toll bypass. To the extent that carriers do use VNXX for voice traffic, it results in less money going to access charges that support universal service. It would be one thing if there were no clear causal link between voice VNXX and lost access charge revenue. Staff's point is that voice VNXX is by definition toll bypass. The arguments in favor of permitting VNXX are only compelling with regard to ISP-bound traffic.

## VII. CARRIER-SPECIFIC ISSUES

### A. Level 3/Broadwing Counterclaim.

82 N/A.

### B. Global Crossing Counterclaim.

83 N/A.

### C. Other Carriers (Listed Individually).

84 N/A.

[114] Verizon Access Br. at 6.
[115] Verizon Access Br. at 7.

## VIII. CONCLUSION/RECOMMENDATIONS

*85* For the reasons stated above, the Commission should prohibit VNXX for uses other than dial-up Internet access service and VoIP telephony. The Commission is authorized by RCW 80.36.140 to determine, upon complaint, the reasonable and proper practices to be observed by telecommunications companies.

*86* As a condition of continuing to use VNXX arrangement for ISP-bound traffic, the Commission should require CLECs to enter into agreements that relieve Qwest of the obligation to pay reciprocal compensation on that traffic and of the expense of local interconnection facilities to the extent those facilities are used to transport VNXX traffic to the CLEC's point of interconnection.

*87* The Commission should reserve for separate determination questions related to proper routing and compensation for VoIP calls.

DATED this 29th day of June, 2007.

Respectfully submitted,

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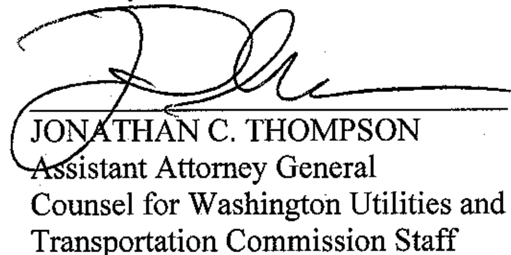

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