EXHIBIT 1

3-2500-15076-2
MPUC P5733,421/IC-02-1372

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS
FOR THE MINNESOTA PUBLIC UTILITIES COMMISSION

In the Matter of the Petition of Level 3 Communications, LLC, for Arbitration to Resolve Issues Relating to an Interconnection Agreement with Qwest Communications

ARBITRATOR'S RECOMMENDED DECISION

Administrative Law Judge Kathleen D. Sheehy arbitrated this matter on October 10, 2002. The record closed on October 21, 2002, upon receipt of the briefs.

The following persons appeared for the evidentiary hearing:

Mary Rose Hughes, Esq., Perkins Coie, 607 14th Street NW, Washington, DC 20005, and Joan C. Peterson, Esq., Qwest Corporation, 200 South Fifth Street, Room 395, Minneapolis, Minnesota 55402, appeared for Qwest Corporation (Qwest).

Gregory Merz, Esq., Gray, Plant, Mooty, Mooty & Bennett, 33 South Sixth Street, Suite 3400, Minneapolis, Minnesota 55402, and Gregory Rogers, Esq., Level 3 Communications, LLC, 1025 El Dorado Boulevard, Broomfield, Colorado 80021, appeared for Level 3 Communications (Level 3).

Linda Jensen, Esq., Assistant Attorney General, 525 Park Street, Suite 200, St. Paul, Minnesota 55103-2106, appeared for the Department of Commerce (the Department).

Kevin O'Grady appeared for the staff of the Minnesota Public Utilities Commission (the Commission).

PROCEDURAL HISTORY

Level 3 is a local exchange carrier[1] under the Telecommunications Act of 1996 and is authorized by the Commission to provide local exchange service in

[1] The term "local exchange carrier" means any person that is engaged in the provision of telephone exchange service or exchange access. *See* 47 U.S.C. § 153(44).

Minnesota.[2] On March 6, 2002, Level 3 served Qwest with a request to negotiate an interconnection agreement. Having reached agreement on all but one issue, Level 3 requested arbitration of the remaining issue on August 13, 2002, the 160th day of negotiations. Qwest filed its response on September 9, 2002. On September 10, 2002, the Commission referred the matter to the Office of Administrative Hearings for arbitration by an Administrative Law Judge. The prehearing conference took place on September 13, 2002, and the evidentiary hearing took place on October 10, 2002.

Pursuant to the Commission's Order Assigning Arbitrator[3] and the Prehearing Order[4] in this case, the Arbitrator's Recommended Decision is due November 1, 2002; exceptions to the Arbitrator's Recommended Decision are due by November 11, 2002; and the final Commission decision is due December 6, 2002.

ISSUE

Should Level 3 be required to pay for trunks and facilities on the Qwest network used by Qwest to handle calls placed by its end users?

The arbitrator concludes that Level 3 is not responsible for the recurring costs of originating traffic on Qwest's side of the network, and that traffic originating on Qwest's network that is bound for Internet Service Providers (ISPs) should not be excluded from the relative-use calculation agreed to by the parties to determine the appropriate charges for interconnection facilities (direct trunk transport and entrance facilities). The language proposed by Level 3 should be incorporated into the parties' interconnection agreement.

Background and Positions of the Negotiating Parties

Under the proposed interconnection agreement, all traffic to be exchanged between Level 3 and Qwest is ISP-bound traffic.[5] This traffic is originated on Qwest's network by Qwest end users who call ISPs served by Level 3, and it travels over Qwest's local facilities, in the same manner as other local calls placed by Qwest customers, to the point of interconnection at Qwest's tandem switch in Minneapolis.[6] From there, Level 3 transports the traffic to its ISP customers. Qwest agrees that it is obligated to interconnect with Level 3 under the Telecommunications Act of 1996, even though all traffic sent to Level 3 from Qwest's network is bound for an ISP.[7]

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[2] *In the Matter of the Application of Level 3 Communications, LLC to Provide Local Exchange Telecommunications Services in the State of Minnesota*, MPUC Docket No. P-5733/NA-98-1905 (authority granted June 9, 1999).
[3] Order Assigning Arbitrator, September 10, 2002.
[4] Prehearing Order, September 16, 2002.
[5] Tr. at 38.
[6] Tr. at 24-25.
[7] Tr. at 27-28.

Level 3 and Qwest have agreed that the financial responsibility for interconnection facilities should be based upon each party's relative use of the facilities, and they have agreed that relative use will be determined by the amount of traffic that each party originates over those facilities.[8] Under the proposed interconnection agreement, Level 3 would order LIS trunks to various communities, and Level 3 would pay the nonrecurring charge necessary to "turn up" the trunks.[9] The relative use calculation would be applied to the monthly recurring charges billed to Level 3, against which Qwest would apply a credit for any traffic originated by Qwest that is terminated to Level 3.[10]

Qwest and Level 3 disagree about whether ISP-bound traffic should be included in this calculation of relative use. Qwest wishes to exclude it from the relative use calculation; Level 3 wishes to include it. Because Level 3 provides local exchange service exclusively to ISPs and will originate no traffic on its side of the network to be terminated on Qwest's side of the network, *exclusion* of ISP-bound traffic from the relative use calculation would mean that Qwest would apply no credit to the monthly bills and that Level 3 would be solely responsible for the recurring costs of the interconnection facilities that allow Qwest's customers to reach Level 3's network; conversely, *inclusion* of ISP-bound traffic in the calculation would mean that Qwest would be solely responsible for those recurring costs.

In support of its position, Qwest relies on 47 C.F.R. § 51.709(b), the FCC regulation concerning rate structure for transport and termination of telecommunications traffic, and the FCC's *ISP Remand Order,*[11] concerning reciprocal compensation for ISP-bound traffic. Because the FCC has excluded ISP-bound traffic from the reciprocal compensation obligations of 47 U.S.C. § 251(b)(5), Qwest contends that this traffic must also be excluded from relative use calculations that determine compensation for interconnection facilities.

Level 3 contends that § 51.709(b) is not applicable to this issue because it addresses only the financial responsibility for traffic originated by the interconnecting carrier and sent back to be terminated on Qwest's network (as opposed to responsibility for traffic that Qwest originates); it further contends that the reciprocal compensation issues addressed in the *ISP Remand Order* concern the rates for transport and termination of traffic that has passed the point of interconnection (as opposed to the costs of interconnection facilities on

[8] The facilities at issue are interconnection trunks (which Qwest calls LIS trunks) that bring traffic from Qwest end users to Qwest's access tandem, and the entrance facility that connects Level 3 to the access tandem.

[9] Level 3 does not dispute the payment of this nonrecurring charge.

[10] Tr. at 23, 39-41; *see also* Ex. 2 at 9.

[11] Order on Remand and Report and Order, *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, Intercarrier Compensation for ISP-Bound Traffic*, CC Dkt. Nos. 96-98 & 99-68, FCC-01-131 (rel. Apr. 27, 2001), *remanded sub nom.*, *WorldCom, Inc. v. FCC*, 288 F.3d 429 (D.C. Cir. 2002) (*ISP Remand Order*).

Qwest's side of the network). In support of its position that Qwest is responsible for the facilities on Qwest's side of the network, Level 3 relies on 47 C.F.R. § 51.703(b), which prohibits LECs from charging other carriers for traffic that originates on the LEC's network, and the FCC's order in *TSR Wireless.*[12]

Decision and Rationale

The positions advanced by the parties relate to two different obligations under the Telecommunications Act of 1996: (1) the obligation to interconnect with other carriers; and (2) the obligation to pay reciprocal compensation for the transport and termination of calls that originate on one carrier's network and terminate on another carrier's network.[13] Pursuant to 47 U.S.C. § 251(a)(1), a carrier has an obligation to interconnect directly or indirectly with the facilities of other telecommunications carriers. It is this obligation that ensures that the customers of one carrier will be able to make calls to, and receive calls from, the customers of another carrier. Pursuant to 47 U.S.C. § 251(b)(5), a carrier has an obligation to establish "reciprocal compensation arrangements for the transport and termination of telecommunications." This obligation arises when the originating party and the terminating party are served by different carriers.

Under the Act, each carrier has different responsibilities for the costs associated with carrying these calls, depending on whether the carrier is originating or terminating the call. The originating carrier, which (as between these parties) is always Qwest, is obligated to carry the call to the point of interconnection between the two carriers' networks. Until relatively recently, it was very clear that 47 C.F.R. § 51.703(b) provided the general principle applicable to financial responsibility for originating traffic:

> A LEC may not assess charges on any other telecommunications carrier for telecommunications traffic that originates on the LEC's network.

Thus, as a general rule, Qwest would be responsible for routing traffic from its customer to the point of interconnection with Level 3.

In *TSR Wireless v. U S WEST*, the FCC addressed the issue of responsibility for interconnection facilities in resolving a dispute between several incumbent LECs and five different one-way paging companies. In that case, the ILECs made the same argument that Qwest makes here, that because the traffic is one-way from ILEC end users to the paging companies

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[12] Memorandum Opinion and Order, *In the Matter of TSR Wireless, LLC, v. U S West Communications, Inc., 15 FCC Rcd at 1116 (June 21, 2000), aff'd sub nom., Qwest Corp. v. FCC*, 252 F.3d 462 (D.C. Cir. 2001) (*TSR Wireless).*

[13] "Interconnection" is the linking of two networks for the mutual exchange of traffic. The FCC has determined that this term does not include the transport and termination of traffic. *See* 47 C.F.R. § 51.5.

should be solely responsible for the costs of interconnection. The FCC rejected this argument, determining first that § 51.703(b) prohibits not only charges for traffic itself, but also prohibits charges for the facilities used to deliver LEC-originated traffic:

> Since the traffic must be delivered over facilities, charging carriers for facilities used to deliver traffic results in those carriers paying for LEC-originated traffic and would be inconsistent with the rules. Moreover, [the *First Local Competition Order*] requires a carrier to pay for dedicated facilities only to the extent it uses those facilities to deliver traffic that it originates.[14]

In addition, the FCC made clear that any costs an ILEC incurs to bring traffic to the point of interconnection are to be absorbed by the ILEC:

> The *Local Competition Order* requires a carrier to pay the cost of facilities used to deliver traffic originated by that carrier to the network of its co-carrier, who then terminates that traffic and bills the originating carrier for termination compensation. In essence, the originating carrier holds itself out as being capable of transmitting a telephone call to any end user, and is responsible for paying the cost of delivering the call to the network of the co-carrier who will then terminate the call. **Under the Commission's regulations, the cost of the facilities used to deliver this traffic is the originating carrier's responsibility, because these facilities are part of the originating carrier's network. The originating carrier recovers the costs of these facilities through the rates it charges its own customers for making calls.** This regime represents "rules of the road" under which all carriers operate, and which make it possible for one company's customer to call any other customer even if that customer is served by another telephone company.[15]

The source of the relative use calculation contained in the proposed interconnection agreement between Qwest and Level 3 is 47 C.F.R. § 51.709(b). The regulation provides, in relevant part, as follows:

> The rate of a carrier providing transmission facilities dedicated to the transmission of traffic between two carriers' networks shall recover only the costs of the proportion of that trunk capacity used by an interconnecting carrier to send traffic that will terminate on the providing carrier's network.[16]

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[14] *TSR Wireless* at ¶ 25.
[15] *Id.* at ¶ 34 (emphasis added).
[16] 47 C.F.R. § 51.709(b).

By its express terms, this regulation applies to traffic that is originated by the interconnecting carrier and is sent back to the providing carrier, in this case Qwest, to be terminated on the providing carrier's network. It makes clear that an interconnecting carrier must pay proportionately for interconnection trunks *to the extent that it uses them to send traffic that it originates back to Qwest's side of the network*. When the interconnecting carrier sends no traffic back to Qwest, there is no FCC regulation that would obligate the interconnecting carrier to pay anything for the interconnection facilities. Rather, that cost would be considered, under § 51.703(b), to be the originating carrier's responsibility.

Once traffic is handed over from an ILEC to the interconnecting carrier at the point of interconnection, or from the interconnecting carrier to the ILEC, the rules concerning reciprocal compensation come into play. Reciprocal compensation is an arrangement between two carriers in which each carrier receives compensation from the other "for the transport and termination on each carrier's network facilities" of telecommunications traffic that originates on the network facilities of the other carrier.[17] These functions take place on the terminating, as opposed to the originating, side of the point of interconnection. Rates for transport and termination generally must be based on cost per minute of use, or may be handled by bill-and-keep arrangements (in which neither of the interconnecting carriers charges the other for the termination of traffic that originates on the other carrier's network).[18]

Qwest contends that the relative use rule, as amended by the FCC in its most recent decision concerning ISP-bound traffic, requires that ISP-bound traffic be excluded from the relative use calculation to determine financial responsibility for interconnection facilities. The FCC has struggled mightily with the issue of reciprocal compensation for ISP-bound traffic. Initially, the FCC excluded ISP calls from the reach of § 251(b)(5) on the theory that they were not "local." It reached this conclusion by applying its "end-to-end" jurisdictional analysis, traditionally employed in determining whether a call is jurisdictionally interstate or not. On appeal, the D.C. Circuit Court of Appeals held that the FCC had failed to explain why the jurisdictional analysis was relevant to deciding whether reciprocal compensation rules apply to ISP traffic under the 1996 Act. The D.C. Circuit vacated and remanded the order.[19]

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[17] 47 C.F.R. § 51.701(e). "Transport" is the transmission and any necessary tandem switching of telecommunications traffic "from the interconnection point between the two carriers to the terminating carrier's end office switch that directly serves the called party. *Id.* § 51.701(c). "Termination" is the switching of telecommunications traffic "at the terminating carrier's end office switch, or equivalent facility, and delivery of such traffic to the called party's premises." *Id.* § 51.701(d).

[18] *See generally* 47 C.F. R. § 51.705-711; § 51.713(a).

[19] *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, Intercarrier Compensation for ISP-Bound Traffic*, 14 FCC Rcd 3689 (1999) (*ISP Order*), *vacated and remanded sub. nom., Bell Atlantic Tel. Cos. v. FCC*, 206 F.3d 1, 5, 8 (D.C. Cir. 2000).

On remand, the FCC again reached the conclusion that the compensation between two LECs involved in delivering ISP-bound traffic should not be governed by the reciprocal compensation provisions of § 251(b)(5). This decision rested on its conclusion that ISP-bound traffic is "information access" under 47 U.S.C. § 251(g), which the FCC interpreted as a "carve-out" provision exempting this traffic from reciprocal compensation obligations under § 251(b).[20] Because the FCC determined that it had jurisdictional authority to regulate the interstate access services that LECs provide to connect callers with interstate carriers or ISPs, the FCC fashioned an interim compensation regime, involving rate caps and bill-and-keep, until further rulemaking was completed. In so doing, the Commission concluded that because it was now exercising its § 201 authority to determine intercarrier compensation for ISP-bound traffic, "state commissions will no longer have authority to address this issue."[21] The FCC then amended its definition of "telecommunications traffic" for purposes of the reciprocal compensation rules to eliminate the references to "local" traffic and to expressly exclude the interstate or intrastate exchange access, information access, or exchange services referenced in § 251(g).[22]

On appeal the D.C. Circuit held that § 251(g) provides no basis for the Commission's action, and remanded the case to the Commission for further proceedings.[23] In the Court's view, "[b]ecause we can't yet know the legal basis for the Commission's ultimate rules, or even what those rules may prove to be, we have no meaningful context in which to assess these explicitly transitional measures." The Court did not vacate the order because many of the petitioners favored the bill-and-keep regime set forth therein and because of the likelihood that the Commission would have authority to elect such a system, "(perhaps under §§ 251(b)(5) and 252(d)(B)(i))."[24] So although state commissions can no longer rely on the legal rationale that ISP traffic is "information access" that is exempt from the reciprocal compensation rules, they are left with the amended rules, including § 51.703(b), which now exclude "information access" from the definition of "telecommunications traffic."

Qwest argues that because the FCC has exempted ISP-bound traffic from reciprocal compensation obligations, the *ISP Remand Order* must also be read to require that this traffic be excluded from the relative use calculation to apportion costs of interconnection. The arbitrator cannot accept this conclusion. Nothing in the text of the *ISP Remand Order* suggests that it applies to any functions other than transport and termination on the terminating side of the point of interconnection. Furthermore, although § 709(a) uses the term "telecommunications traffic," the relative use rule (§ 709(b)) does not; it uses only

[20] *ISP Remand Order* at ¶¶ 33-34.
[21] *Id.* at ¶ 82. Qwest has not disputed the MPUC's jurisdiction to resolve this dispute over the costs of interconnection, although it maintains that the reciprocal compensation rules control the result.
[22] *See* 47 C.F.R. § 51.701(b).
[23] *WorldCom, Inc. v. FCC*, 288 F.3d 429.
[24] *Id.*

the term "traffic." Qwest contends that the term "traffic" in 709(b) should be read as "telecommunications traffic," which by definition excludes ISP-bound traffic. Based on basic principles of statutory construction, the ALJ does not believe the regulation should be read this way.[25]

Even if the word "telecommunications" were to be read into § 709(b), however, it does not mean that it requires the exclusion of ISP-bound traffic from the relative use calculation as proposed by Qwest. First, as noted above, the rule apportions the cost of interconnection trunking based on the amount of traffic originated by the interconnecting carrier, not based on the amount of traffic originated by the providing carrier. Qwest essentially wants to apply the relative use rule in reverse. Second, even if the word "telecommunications" were to be read into the section, it would simply mean that § 709(b) is inapplicable to transmission facilities dedicated to ISP-bound traffic, and in the absence of some sort of interim compensation regime comparable to that developed for reciprocal compensation the regulations would provide no answer to the question of how the recurring costs of interconnection facilities should be apportioned, if at all.

Qwest also contends that, even if § 709(b) does not control the issue, the policy reasons supporting the FCC's *ISP Remand Order* support the same result. The FCC was concerned about preventing regulatory arbitrage, meaning that interconnecting carriers should not have an economic incentive to seek out customers with high volumes of incoming traffic that will generate high reciprocal compensation payments from an ILEC.[26] Reciprocal compensation is paid on a per-minute basis; the costs of interconnection trunking and entrance facilities are charged on a flat-rated basis.[27] A carrier serving an ISP cannot generate more revenue from an ILEC by increasing traffic volume. Accordingly, the policy considerations applicable to reciprocal compensation have no place in apportioning the costs of interconnection.

Level 3 correctly maintains that the *ISP Remand Order* concerned what a terminating carrier might charge an originating carrier for transport and termination, and that it was not concerned with the originating carrier's obligation to take traffic over its own network to a point of interconnection. Specifically, Level 3 points to a footnote in the Order providing as follows:

> This interim regime affects only the intercarrier compensation (i.e., the rates) applicable to the delivery of ISP-bound traffic. It does not alter carriers' other obligations under Part 51 rules, 47 C.F.R. Part

[25] With respect to defined terms, when Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion. *Barnhart v. Sigmon Coal Co.*, 534 U.S. 438 (2002) (citations omitted).
[26] *ISP Remand Order* at ¶¶ 68-70.
[27] Tr. at 76.

51, or existing interconnection agreements, such as obligations to transport traffic to points of interconnection.[28]

This footnote supports Level 3's argument that, despite the change in the rates for reciprocal compensation for ISP-bound traffic, the *ISP Remand Order* does not alter an ILEC's obligation under § 51.703(b) to transport this traffic to the point of interconnection.

Before the *ISP Remand Order*, the law was clear that Level 3's position on apportioning the costs of interconnection is correct. It is certainly not accurate to assert, as Qwest does, that the FCC "conclusively determined" in the *ISP Remand Order* that ISP-bound traffic is not properly included in the relative use calculation.[29] The Order does not refer to § 709(b) at all. Given the uncertainty in the application of § 703(b) as a result of the *ISP Remand Order's* amendment of the definition of telecommunications traffic, and the subsequent remand by the D.C. Circuit, it is not so clear that there is at this time any controlling authority on this issue.

The Arbitrator recommends that Level 3's contract language be accepted for several reasons. First, there is no suggestion in the text or the rationale of the *ISP Remand Order* that the FCC intended to change the rules concerning costs of interconnection, as opposed to reciprocal compensation for ISP-bound traffic. In addition, as agreed by the parties and as required by the *ISP Remand Order,* bill-and-keep applies to call termination and delivery costs, because Qwest and Level 3 exchanged no traffic before the date of the Order.[30] It is consistent with the *ISP Remand Order*, the D.C. Circuit's decision to remand in *WorldCom v. FCC*, and the *TSR Wireless Order* to apply what is essentially bill-and-keep to the costs of interconnection for ISP-bound traffic.[31] Furthermore, the Administrative Law Judge is not persuaded by the reasoning of other state commissions in Colorado, Washington, and Oregon that have accepted Qwest's arguments. The Arizona Commission's decision in favor of Level 3 is the only one cited that recognizes the distinction between interconnection and reciprocal compensation.

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[28] *ISP Remand Order* at ¶ 82 n. 149.

[29] Qwest's Post-hearing Brief at 3. Qwest further contends that the Hobbs Act precludes any challenge to or deviation from the FCC's requirements concerning relative use and ISP-bound traffic. *Id.* at 11-12. Level 3 is not challenging either the validity of or recommending any deviation from the FCC's regulations and orders on these issues in an "impermissible collateral attack."

[30] *ISP Remand Order* at ¶ 81.

[31] Both the FCC and Qwest have advocated moving toward bill-and-keep for all traffic exchanged by telecommunications carriers. *See, e.g., ISP Remand Order* at ¶ 83 (there is a strong possibility that the FCC's rulemaking proceeding may result in the adoption of a "full bill and keep regime" for ISP-bound traffic); Ex. 4 at Ex. 2 (Qwest has proposed to the FCC that originating carriers should be responsible for paying the cost of facilities to transport traffic to other carriers).

Finally, as illustrated by the Department during the hearing, an ISP served by Qwest that is connected to an end office in the Minneapolis-St. Paul local calling area has access to each of the end offices, and each of the Qwest customers served by each of those end offices, without bearing the cost of facilities that connect the end offices.[32] According to Qwest, the cost of those facilities is included in the local calling rate. In contrast, Level 3 would be required to bear the recurring cost of trunking to each end office in order for its ISP customers to provide service to end users served by those end offices.[33] Qwest's proposal would have an adverse competitive effect on Level 3 and potentially other CLECs, because it would make it more expensive for them to serve ISP customers than it would be for Qwest to serve ISP customers. There is nothing in the statute, the FCC's regulations, or the *ISP Remand Order* that would support this result.

RECOMMENDATION

The Arbitrator respectfully recommends that the Minnesota Public Utilities Commission order that the interconnection agreement between Qwest and Level 3 contain the terms recommended by Level 3 in this proceeding.

Dated this __ day of November, 2002

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KATHLEEN D. SHEEHY
Administrative Law Judge

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[32] Tr. at 61-62, 72; Ex. 3. Qwest calls these trunks "interoffice trunks within the local calling area," whereas it calls the trunks that Level 3 would use "LIS trunks."
[33] Tr. at 73.