State of Florida

Public Service Commission

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

DATE: DECEMBER 9, 1999

TO: DIRECTOR, DIVISION OF RECORDS AND REPORTING (BAYÓ)

FROM: DIVISION OF COMMUNICATIONS (FAVORS, HINTON, BROWN, BARRETT)
DIVISION OF LEGAL SERVICES (FORDHAM)
DIVISION OF POLICY ANALYSIS & INTERGOVERNMENTAL LIAISON (CLARK-WATTS)

RE: DOCKET NO. 990691-TP - PETITION OF ICG TELECOM GROUP, INC. FOR ARBITRATION OF UNRESOLVED ISSUES IN INTERCONNECTION NEGOTIATIONS WITH BELLSOUTH TELECOMMUNICATIONS, INC.

AGENDA: 12/21/99 - REGULAR AGENDA - POST HEARING DECISION - PARTICIPATION IS LIMITED TO COMMISSIONERS AND STAFF

CRITICAL DATES: THE PARTIES HAVE AGREED TO NOT BE BOUND BY THE STATUTORY TIME LIMIT IN SECTION 252(b)(4)(C),

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: I:\PSC\CMU\WP\990691.RCM

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CASE BACKGROUND

On October 27, 1997, this Commission approved a one-year agreement between ICG Telecom Group, Inc. (ICG), and BellSouth Telecommunications, Inc. (BellSouth), providing for interconnection services. That agreement expired on October 27, 1998, but the parties mutually agreed to extend it pending finalization of a successor agreement. Negotiations for a successor agreement failed, and on May 27, 1999, ICG filed a Petition for Arbitration, seeking the assistance of the Commission in resolving the remaining issues. The Petition enumerated a total of twenty-five issues. Since the petition was filed, however, ten of those issues have been resolved and withdrawn by the parties. At the Prehearing Conference, BellSouth's Motion to Remove Issues From Arbitration was granted, and nine additional issues were removed from consideration.

An administrative hearing was held on October 7, 1999. The following is staff's recommendation on the remaining issues of this arbitration.

DISCUSSION OF ISSUES

ISSUE 1: Until the FCC and the FPSC adopt a rule with prospective application, should dial-up access to the Internet through Internet Service Providers (ISPs) be treated as if it were a local call for purposes of reciprocal compensation?

PRIMARY RECOMMENDATION: Yes. Until the FCC and the FPSC adopt a rule with prospective application, dial-up access to the Internet through Internet Service Providers (ISPs) should be treated as if it were a local call for purposes of reciprocal compensation. **(BARRETT)**

ALTERNATIVE RECOMMENDATION: Staff recommends that the parties should continue to operate under the terms of their current contract until the FCC issues its final ruling on whether reciprocal compensation is due for ISP-bound traffic because the FCC has retained jurisdiction over this traffic. **(BARRETT)**

POSITION OF PARTIES

ICG: Yes. The FCC has clearly determined that, until its rule takes effect on a prospective basis, state commissions may determine that reciprocal compensation should be paid for ISP traffic; moreover, it has stated its view that state commissions have an obligation to require ILECs to compensate ALECs for ISP traffic. Physical and policy reasons compel the result that BellSouth provide reciprocal compensation for calls to ISPs at a rate that reflects the network functions ICG performs in delivering traffic to all customers, including ISPs.

BELLSOUTH:

No. The FCC's recent Declaratory Ruling in CC Docket Nos. 96-98 and 99-68, released on February 26, 1999, confirmed unequivocally that traffic bound for the Internet through ISP's ("ISP-bound traffic") is interstate in nature, not local. Under the provisions of the 1996 Act and FCC rules, only local traffic is subject to reciprocal compensation obligation. Thus, reciprocal compensation is clearly not applicable to ISP-bound traffic. In addition to being contrary to the law, treating ISP-bound traffic as local for

reciprocal compensation purposes is contrary to sound public policy.

The issue in this proceeding is vastly different from prior ISP decisions rendered by the Commission, which were based on findings that the parties intended to pay reciprocal compensation for ISP-bound traffic. In this proceeding, there is absolutely no doubt that BellSouth does not intend to pay reciprocal compensation for ISP-bound traffic.

The FCC made clear that any inter-carrier compensation mechanism for ISP-bound traffic is outside of the scope of 251(b)(5), as such traffic is interstate, not local. *See* FCC Declaratory Ruling, at FN 87. Thus, this issue is not proper for 252 arbitration. Notwithstanding, BellSouth proposed an interim mechanism for ISP-bound traffic pending the FCC's issuance of a final order in its inter-carrier compensation docket.

PRIMARY STAFF ANALYSIS: This issue focuses on whether ISP traffic should be treated as "local" for purposes of the parties' Interconnection Agreement and for the payment of reciprocal compensation. More specifically, this issue seeks to determine whether or not, when an end user of one party calls an ISP that is an end user of the other party, the party that serves the customer originating the call should pay reciprocal compensation to the other party which serves the ISP. Section 251 (b)(5) of the Telecommunications Act of 1996 obligates all local exchange carriers "to establish reciprocal compensation arrangements for the transport and termination of telecommunications." The FCC further clarified in its Local Competition Order "that section 251(b)(5) reciprocal compensation obligations should apply only to traffic that originates and terminates within a local area." (FCC 96-325, ¶1034) Therefore, if ISP-bound traffic is defined as "local traffic" for purposes of the parties' Interconnection Agreement, reciprocal compensation would necessarily apply.

Arguments

ICG asserts that the FCC has confirmed the state commissions' authority to arbitrate the matter, has ruled repeatedly that such traffic must be treated as 'local' for regulatory purposes, and that ISP-bound traffic requires compensation, whether through a reciprocal or an alternative arrangement. (ICG BR 2) ICG witness Starkey declares that reciprocal compensation is appropriate for ISP-bound traffic, stating, "it is simply good public policy, as well as economically rational, to require payment for terminating

this traffic." (TR 124) The witness further asserts that, quite simply, ICG wants to be paid for carrying BellSouth's traffic regardless of whether it terminates to a residential, business, or an ISP customer served by their network. (TR 168) He further states that ICG incurs costs which do not differ between customer types when their network is accessed from a BellSouth end user, and contends that the exact same call path and facilities are employed for an ISP-bound call as for a call to a residential or business customer. (TR 168) The witness argues that BellSouth only wants to provide compensation for a subset of the local traffic by excluding the ISP-bound traffic, even though the costs to the ICG network would be exactly the same. Therefore, the witness argues that the same level of compensation should be paid for ISP-bound calls as for non ISP-bound calls. (Starkey TR 169) The witness argues that "if there is neither a technical or economic distinction between the two types of [local] calls. . . they should not be treated differently in terms of compensation." (Starkey TR 170) He summarizes by stating, "this simply isn't equitable, economically efficient, or in the public interest." (Starkey TR 169)

Witness Starkey asserts that the FCC's declaratory ruling suggests that they [the FCC] have and continue to treat ISP-bound traffic as local for the purposes of compensation. He references paragraphs 23 and 25 of FCC Order 99-38, which indicate that state commissions may arbitrate this issue and find, as the FCC has, that ISP-bound traffic should be treated as local traffic. (Starkey TR 170)

ICG witness Schonhaut states that ALECs, including ICG, provide new and innovative services to ISPs and other technologically demanding customers, which is a market the ILECs have "ignored." (TR 226) Furthermore, she states that absent the reciprocal compensation due for a significant amount of traffic that ICG terminates, ICG would be forced to raise rates, absorb its costs, or even decline to serve ISPs altogether, which endangers the competition that is critical to fostering the development of the public switched telephone network (PSTN) to meet the needs of all consumers. (TR 227, 236)

BellSouth witness Varner responds that reciprocal compensation is not applicable for ISP-bound traffic, and claims that payment therefor is inconsistent with the law and is not sound public policy. (TR 312) The witness asserts that reciprocal compensation is only applicable for the termination of <u>local</u> traffic on either parties' network, citing the FCC's determination that "ISP-bound traffic is non-local interstate traffic." (Varner, TR 315-316) Witness Varner argues that no part of an ISP-bound communication

terminates at the facilities of an ISP. (TR 317) He asserts that "once it is understood that ISP traffic 'terminates' only at distant websites . . . it is, therefore, evident that these calls are not local." (TR 317)

Witness Varner believes that carriers are entitled to be compensated appropriately based on the use of their network to transport and deliver traffic. (TR 312) He also states that payment of reciprocal compensation for ISP-bound traffic subsidizes the prices an ALEC charges an ISP. (TR 337)

BellSouth believes that "any interim inter-carrier compensation mechanism adopted by state commissions is outside the provisions of Section 251(b)(5) of the Act, because ISP traffic is interstate in nature, not local." (BST BR 4, Varner TR 316) He emphasizes that a final ruling from the FCC to govern inter-carrier compensation for ISP-bound traffic will be forthcoming, upon conclusion of the Notice of Proposed Rulemaking comment period. Witness Varner states that "the FCC has, will retain, and will exercise jurisdiction over this traffic." (TR 313) He asserts that BellSouth's position is supported by the FCC's findings and Orders. (TR 317)

Staff's Analysis

Each party to this docket has cited passages from the FCC's Declaratory Ruling Order 99-38 in CC Docket No. 96-98, issued on February 26, 1999 (hereafter, FCC 99-38), which also encompasses the Notice of Proposed Rulemaking in CC Docket 99-68. FCC 99-38 provides the foundation for the argument and interpretation of the issues of ISP-bound traffic and the applicability of reciprocal compensation, if any. (EXH 1)

The FCC concluded that the traffic generated by calls that access the Internet through ISPs, though usually dialed by the end user on a local basis, are not purely local, finding that:

> . . .ISP-bound traffic is jurisdictionally mixed and appears to be largely interstate. This conclusion, however, does not in itself determine whether reciprocal compensation is due in any particular instance. . .In the absence, to date, of a federal rule regarding the appropriate inter-carrier compensation for this traffic, we therefore conclude that parties should be bound by their existing interconnection agreements, as interpreted by state commissions. (FCC 99-38, ¶1)

Staff notes, however, that the FCC 99-38 Order acknowledges many aspects of ISP-bound traffic that are unique. Foremost, the Internet itself is not a single destination, but rather, it is a "network of interconnected computers enabling millions of people to communicate with one another and to access vast amounts of information from around the world." (¶3) Also, the FCC asserts that the "communications at issue here do not terminate at the ISPs local server, . . . but continues to the ultimate destination . . . often located in another state." (¶12) Additionally, FCC 99-38 states that "an Internet communication does not necessarily have a point of 'termination' in the traditional sense." (¶18) The FCC's jurisdictional analysis considered the end-to-end nature of the communications (¶11), and regarded ISP-bound traffic to be a "continuous transmission from the end user to the distant Internet site." (¶13)

In terms of addressing the inter-carrier compensation for delivery of ISP-bound traffic, the FCC 99-38 Order again states that no rule governs the issue of inter-carrier compensation for ISP-bound traffic, and:

> . . . in the absence of such a rule, parties may voluntarily include this traffic within the scope of their interconnection agreements under sections 251 and 252 of the Act, even if these statutory provisions do not apply as a matter of law. Where parties have agreed to include this traffic within their section 251 and 252 interconnection agreements, they are bound by those agreements, as interpreted and enforced by the state commissions. (FCC 99-38, ¶22)

Staff contends that the regulatory framework for reciprocal compensation is found in Section 251(b)(5) of the Act, which addresses inter-carrier compensation "for the transport and termination of telecommunications." Under a separate Order, the FCC's Local Competition Order, the FCC interpreted the language in §251(b)(5)in a limited fashion, such that the provision now should apply *"for the transport and termination of local telecommunications traffic."* (FCC 99-38, ¶7) The FCC acknowledges, however, that "Enhanced Service Providers (ESPs), including ISPs, use interstate access services, . . . and has exempted ESPs from certain interstate access charges." (FCC 99-38, ¶5) Pursuant to this exemption, the ESPs are treated as end-users for purposes of assessing access charges, and are permitted to purchase their links to the PSTN through *intra*state business tariffs, rather than

*inter*state access tariffs. The FCC asserts that "retaining the ESP exemption would avoid disrupting the still-evolving information services industry and advance the goals of the 1996 Act . . .", and again affirm their regulatory obligations by treating ISP-bound traffic as though it were local. (FCC 99-38 ¶5)

The FCC directed the states to treat ISP traffic as if it were local, by permitting ISPs to purchase their links to the PSTN through local business tariffs. (FCC 99-38, ¶9) In a common arrangement, ISPs purchase analog and digital business lines from a local exchange company, lines that allow unlimited incoming calls for which the ISPs own customers may dial-in to access the Internet. The ISP pays a flat monthly fee to the local exchange provider for the business lines, and "combines computer processing, information storage, protocol conversion, and routing with transmission to enable users to access Internet content and services." (FCC 99-38, ¶4) The end-user, in addition to paying for their ordinary telephone service, usually pays the ISP a flat, monthly fee for this Internet access.

Conclusion

Staff agrees with ICG's assertions that, until a definitive rule is adopted, the FCC will allow state commissions to rule on the issue of reciprocal compensation of ISP-bound traffic, pursuant to Sections 251 and 252 of the Act. Staff also agrees with ICG's claim that reciprocal compensation is appropriate for all types of local traffic, including ISP-bound traffic, as all types of local traffic contribute to the economic costs of ICG's network. We are not persuaded by with BellSouth's assertion that reciprocal compensation is not the appropriate inter-carrier compensation mechanism for ISP-bound traffic. Until the FCC and the FPSC adopt a rule with prospective application, dial-up access to the Internet through ISPs should be treated as if it were a local call for purposes of reciprocal compensation between BellSouth and ICG.

In addition we agree with ICG's argument that the 'cost causer' should bear the reciprocal, proportional responsibility for the delivery of calls to and from their own network. We also agree with ICG witness Starkey's statement that the elimination of reciprocal compensation for traffic to ISPs would not be equitable, economically efficient, or in the public interest. However, staff notes that ICG does not yet have a network in Florida, and absent a network in Florida, the companies will not be subject to reciprocal compensation obligations until such time that ICG develops their Florida network.

For these reasons, staff recommends that until the FCC and the FPSC adopt a rule with prospective application, dial-up access to the Internet through ISPs should be treated as if it were a local call for purposes of reciprocal compensation between BellSouth and ICG.

ALTERNATIVE STAFF ANALYSIS: Staff's alternative position was based upon the FPSC's approach taken in its recent decision in Order No. PSC-99-2009-FOF-TP, issued on October 14, 1999, in Docket No. 990149-TP, the Petition by MediaOne Florida Telecommunications, Inc. for arbitration of an interconnection agreement with BellSouth Telecommunications, Inc. (See EXH-1) In the MediaOne/BellSouth arbitration, the issue itself was framed somewhat differently than in this docket, but the assertions are distinctly similar, particularly with respect to BellSouth's position. (BST BR. p.4)

BellSouth supports this Commission's recent decision in the MediaOne/BellSouth arbitration (See EXH-1, Order No. PSC-2009-FOF-TP, issued on October 14, 1999, in Docket No. 990149-TP) in which the FPSC decided to maintain the status quo pending the FCC's decision with respect to adopting a compensation mechanism. (TR 44)

The root of the problem in determining whether ISP-bound traffic is local and whether reciprocal compensation is due, stems from the FCC's treatment of this traffic. The FCC admittedly has treated ISP-bound traffic as though it were local traffic. The FCC has exempted ISPs from paying access charges. In its Declaratory Ruling it stated:

> Although the Commission has recognized that enhanced service providers (ESPs), including ISPs, use interstate access services, since 1983 it has exempted ESPs from the payment of certain interstate access charges. (FCC 99-38, ¶5)(EXH 1)

The FCC explains that the exemption was adopted at the inception of the interstate access charge regime to protect certain users of access services, such as ESPs, that had been paying the generally much lower business service rates from the rate shock that would result from immediate imposition of carrier access charges. (FCC 99-38, at fn. 10) The FCC continues to allow ESPs to purchase their links to the PSTN through intrastate business tariffs rather than through interstate access tariffs. In addition, incumbent LEC expenses and revenues associated with ISP-bound traffic traditionally have been characterized as intrastate for separations purposes.

The FCC has realized the problems that its treatment of this traffic has caused throughout the country. It stated:

> Until now, however, it has been unclear whether or how the access charge regime or reciprocal compensation applies when two interconnecting carriers deliver traffic to an ISP. . . . As a result, and because the Commission had not addressed inter-carrier compensation under these circumstances, parties negotiating interconnection agreements and the state commissions charged with interpreting them were left to determine as a matter of first impression how interconnecting carriers should be compensated for delivering traffic to ISPs, leading to the present dispute. (FCC 99-38, ¶9)

The FCC issued a Declaratory Ruling concluding that ISP-bound traffic is jurisdictionally mixed and appears to be largely interstate. (FCC 99-38, ¶1) However, the FCC stated that it currently has no rule governing inter-carrier compensation for ISP-bound traffic, but believes that adopting such a rule to govern prospective compensation would serve the public interest. (FCC 99-38, ¶28) To this end, the FCC has issued a Notice of Proposed Rulemaking seeking comments on two proposals for a rule. In the meantime, the FCC has left it to state commissions to determine whether reciprocal compensation is due for this traffic.

Alternate staff agrees that the FCC has claimed jurisdiction over this traffic and will ultimately adopt a final rule on this matter. The FCC stated:

> We emphasize that the Commission's decision to treat ISPs as end users for access charge purposes and, hence, to treat ISP-bound traffic as local, does not affect the Commission's ability to exercise jurisdiction over such traffic. (FCC 99-38, ¶16)

Further, as mentioned earlier, the FCC does intend to adopt a final rule to govern inter-carrier compensation for ISP-bound traffic. Therefore, any decision the Commission makes will only be an interim decision. However, in Order No. PSC-99-2009-FOF-TP, issued on October 14, 1999, in Docket No. 990149-TP, the MediaOne and BellSouth arbitration, this Commission ruled that the parties should continue to operate under their current contract pending a

decision by the FCC. Staff believes this approach is reasonable in view of the uncertainty over this issue. As such, alternate staff also recommends that the parties should continue to operate under the terms of their current contract until the FCC issues its final ruling on whether ISP-bound traffic should be defined as local or whether reciprocal compensation is due for this traffic.

Conclusion

Alternate staff recommends that the parties should continue to operate under the terms of their current contract until the FCC issues its final ruling on whether ISP-bound traffic should be defined as local or whether reciprocal compensation is due for this traffic. Any decision this Commission makes presumably will be preempted if it is not consistent with the FCC's final rule.

ISSUE 2: Should the following packet-switching capabilities be made available as UNEs:

a) user-to-network interface (UNI) at 56 kbps, 64 kbps, 128 kbps, 256 kbps, 384 kbps, 1.544 Mbps and 44.736 Mbps.

b) network-to-network interface (NNI) at 56 kbps, 64 kbps, 1.544 Mbps and 44.736 Mbps

c) data link control identifiers ("DLCIs") at committed information rates ("CIRs") of 0 kbps, 8 kbps, 9.6 kbps, 16 kbps, 19.2 kbps, 28 kbps, 32 kbps, 56 kbps, 64 kbps, 128 kbps, 192 kbps, 256 kbps, 320 kbps, 384 kbps, 448 kbps, 512 kbps, 576 kbps, 640 kbps, 704 kbps, 768 kbps, 832 kbps, 896 kbps, 960 kbps, 1.024 Mbps, 1.088 Mbps, 1.152 Mbps, 1.216 Mbps, 1.280 Mbps, 1.344 Mbps, 1.408 Mbps, 1.472 Mbps, 1.536 Mbps, 1.544 Mbps, 3.088 Mbps, 4.632 Mbps, 6.176 Mbps, 7.720 Mbps, 9.264 Mbps, 10.808 Mbps, 12.350 Mbps, 13.896 Mbps, 15.440 Mbps, 16.984 Mbps, 18.528 Mbps and 20.072 Mbps.

RECOMMENDATION: No. The packet-switching capabilities ICG has requested should not be provided as UNEs. However, BellSouth has agreed to provide these packet-switching capabilities to ICG; therefore, the parties should negotiate the price. Staff also recommends that the evidence of record is insufficient to determine whether interoffice transport should be provided as a UNE; therefore, it should not be provided as a UNE. **(FAVORS)**

POSITIONS OF THE PARTIES

ICG: Yes. It now appears that BellSouth will provide packet-switching capabilities as UNEs as an interim measure until the FCC's decision on remand is published. However, BellSouth wants to provide them at "modified" TELRIC rates. BellSouth should be required to provide these capabilities as UNEs at TELRIC rates, including the capability to connect at TELRIC rates a BellSouth central office where ICG is collocated (but which does not have a BellSouth frame relay packet switch) with a BellSouth central office that does have a BellSouth frame relay packet switch.

BELLSOUTH:

With certain exception, BellSouth agrees to comply with ICG's request until the FCC issues a final non-appealable order on Rule 51.319. Moreover, until a recent (August 25, 1999) pre-hearing conference before the Tennessee Regulatory Authority, BellSouth believed that this issue was settled regionally, subject only to ICG's review of BellSouth's rates in each state. BellSouth's understanding was based upon agreements reached in a mediation conference in Montgomery, Alabama, held on August 10, 1999. While BellSouth acknowledges that ICG raised collocation questions relating to this issue during that mediation, the parties settled the issue in its entirety in Alabama.

BellSouth opposes ICG's attempt to broaden Issue 2 to include a collocation issue related to packet-switching. Section 252(b)(2) of the 1996 Act requires the petitioner (in this case ICG) to state the unresolved issues in the Arbitration Petition. In addition, 252(b)(4) limits the Commission's consideration of 252 arbitration issues to those "set forth in the petition and in the response..." The packet-switching issue raised by ICG in the Arbitration Petition is limited strictly to whether BellSouth is required to provide packet-switching capabilities as a UNE. To allow ICG to change and expand this issue would be a violation of the requirements of the 1996 Act and would prejudice BellSouth's right to a fair arbitration.

STAFF ANALYSIS:

The issue before the Commission is to determine whether the packet-switching capabilities that ICG is requesting from BellSouth should be provided as unbundled network elements (UNEs). There is no dispute as to whether BellSouth will provide these capabilities as BellSouth has agreed to do so.

Arguments

ICG witness Holdridge states that frame relay service employs a special switch to send data rapidly. (TR 102) Witness Holdridge further states that "consistent with the innovation it has always shown in providing new services to its customers, ICG requires various packet switching UNEs to provide competitive advanced services to its customers." (TR 85) He also states:

> ICG would like to be able to purchase from BellSouth, either in part(s) or in whole, and not limited to, the packet assembler/disassembler (PAD), the customer access circuit, any circuit link(s) between the customer serving central office and the central office in which the frame relay switch is located, and the frame relay switch port, as required per customer application. (TR 84-85)

Witness Holdridge further states that ICG requires a network to network interface (NNI) at speeds ranging from 56 kbps to 44.736 Mbps and data link control identifiers (DLCI) that provide committed information rates (CIRs) between 0 kbps and 20.072 Mbps so that ICG can efficiently utilize the UNEs and NNIs for competitive product offerings. (TR 85)

Witness Holdridge argues that packet-switching capabilities should be available as UNEs to ensure that the prices charged to ICG for these capabilities are TELRIC-based. (TR 86)

BellSouth witness Varner states:

> The FCC's Unbundled Network Element ("UNE") Rule 51.319 (Specific unbundling requirements) has been vacated and is being readdressed by the FCC. Until that time, which will probably be several months, there is no minimum list of UNEs that BellSouth is required to offer. There are numerous capabilities that competitive local exchange carriers ("CLECs") have requested from BellSouth. As an interim measure, BellSouth is proposing to provide those capabilities although, technically, they are not UNEs, until the FCC's new rules become final. Because the required list of UNEs is unknown, it would not be appropriate to require application of FCC rules that apply to UNEs to these capabilities during this interim period. When the FCC rules become finalized, BellSouth should be permitted to modify the list of capabilities that it will offer in the interim to conform to the FCC's rules. (TR 301-302)

Witness Varner also states that "BellSouth will continue to offer any individual UNE currently offered until Rule 51.319 is resolved." (TR 308)

In regard to the packet-switching capabilities that ICG has requested, BellSouth witness Varner contends:

> It is BellSouth's understanding that ICG is requesting that BellSouth unbundle its existing tariffed Packet Switching Frame Relay Service. Subject to the conditions stated in my testimony, BellSouth has agreed to do that. (TR 341)

ICG witness Holdridge also requests that BellSouth unbundle its interoffice transport facilities. He states:

> Under its proposal, BellSouth would provide end user access to frame relay service as a UNE only when the customer is directly served out of the same central office housing the BellSouth frame relay switch, or when the ICG customer premise is served out of a BellSouth central office in which ICG has an established collocation site. This means BellSouth decides where packet switching is available. If the ICG customer premise is served out of a BellSouth central office that has no frame relay switch, and ICG has no collocation site established in that central office, it will be necessary for ICG to purchase transport from that central office to the frame relay switch. (TR 102-103)

Witness Holdridge further states that if ICG is required to pay BellSouth tariff rates for frame relay, end user access, and interoffice transport, ICG will not be able to offer to the public a competitively priced frame relay product. (TR 103)

BellSouth offered no testimony on interoffice transport as a UNE.

Staff's Analysis

Staff reiterates that the issue is not whether BellSouth will provide the packet-switching capabilities that ICG has requested, but whether these capabilities will be provided as UNEs. According

to 47 CFR part 51 Subpart F-Pricing of Elements, certain pricing rules apply to unbundled network elements, interconnection, and methods of obtaining access to unbundled elements, including physical collocation and virtual collocation. Specifically, §51.503(b) reads:

> An incumbent LEC's rates for each element it offers shall comply with the rate structure rules set forth in §§51.507 and 51.509, and shall be established, at the election of the state commission-
>
> (1) Pursuant to the forward-looking economic cost-based pricing methodology set forth in §§51.505 and 51.511; or
>
> (2)Consistent with the proxy ceilings and ranges set forth in §51.513.

Therefore, the real issue before the Commission is how the prices for the packet-switching capabilities should be set. The list of unbundled network elements that an incumbent LEC must provide to requesting telecommunications carriers was provided in FCC Rule §51.319. However, this rule was vacated by the United States Supreme Court and remanded back to the FCC. The FCC has recently issued its Order on this rule; however, the Order was not issued until after the hearing in this case was held. The FCC did issue a press release prior to the actual Order that was entered as evidence, but staff notes that the press release itself is subject to modification and is not legally binding.

Staff points out that packet-switching capabilities were not a part of the original list of UNEs contained in Rule §51.319, which was vacated. However, the FCC did address packet-switching capabilities as a UNE in its First Report and Order. It stated:

> At this time, we decline to find, as requested by AT&T and MCI, that incumbent LEC's packet switches should be identified as network elements. Because so few parties commented on the packet switches in connection with section 251(c)(3), the record is insufficient for us to decide whether packet switches should be defined as a separate network element. We will continue to review and revise our rules, but at present, we do not adopt a national rule for the unbundling of packet switches. (FCC 96-325, ¶427)

Further, the FCC did mention packet switching in its press release regarding the new list of UNEs. Specifically, it stated:

> Packet Switching. Incumbent LECs are not required to unbundle packet switching, except in the limited circumstance in which a requesting carrier is unable to install its Digital Subscriber Line Access Multiplexer (DSLAM) at the incumbent LEC's remote terminal, and the incumbent LEC provides packet switching for its own use. Packet switching involves the routing of individual data message units based on address or other routing information and includes the necessary electronics (e.g., DSLAMs). (TR 110-111)

Staff again must note that the information contained in the FCC's press release is not legally binding, and is not dispositive by itself of the issue. Nonetheless, staff points out that the press release does indicate that the new Rule §51.319 will not require incumbent LECs to unbundle its packet-switching capabilities except in a very narrow and limited instance. Staff does not believe that ICG's argument that innovation and competition necessitate TELRIC-based pricing of packet-switching capabilities sufficiently demonstrates that these capabilities are intended under the Act to be provided as UNEs. ICG has only argued its value to ICG's own business plan. Therefore, the evidence of record indicates that packet-switching capabilities are not UNEs. However, BellSouth has agreed to provide these capabilities to ICG; therefore, the parties should negotiate a price.

Neither party has presented much evidence regarding the interoffice transport that would be used to connect central offices where a frame relay switch does not exist and ICG is not physically collocated. ICG states that this element should be provided as a UNE. ICG witness Holdridge states that if ICG must pay special access for interoffice transport, it will not be able to offer a competitively priced frame relay product. (TR 103) BellSouth did not present any evidence on this topic. This evidence is insufficient for staff to make a recommendation. Staff is even unaware if ICG seeks shared or dedicated interoffice transport. Therefore, staff recommends that the evidence is insufficient for the Commission to determine that the interoffice transport that ICG seeks is a UNE.

Conclusion

The evidence of record does not indicate that BellSouth should provide packet-switching capabilities as UNEs. The original list of UNEs contained in FCC Rule 51.319, even though currently vacated, did not list packet-switching capabilities as UNEs. Further, the evidence of record seems to suggest that packet-switching capabilities will also not be made a part of the new list of UNEs. Therefore, staff recommends that the packet-switching capabilities ICG has requested should not be provided as UNEs. However, BellSouth has agreed to provide the packet-switching capabilities to ICG, therefore, the parties should negotiate the price.

Staff also recommends that the evidence of record is insufficient to determine if interoffice transport should be provided as a UNE; therefore, staff recommends that it should not be provided as a UNE.

ISSUE 3: Under the Telecommunications Act of 1996, should "Enhanced Extended Link" Loops (EELs) be made available to ICG in the interconnection agreement as UNEs?

RECOMMENDATION: No. Enhanced Extended Link Loops (EELs) should not be made available to ICG in the interconnection agreement as UNEs. However, BellSouth has agreed to provide EELs to ICG; therefore, the parties should negotiate the price for the EEL. **(FAVORS)**

POSITIONS OF THE PARTIES

ICG: Yes. BellSouth has refused to provide the EEL to ICG on a UNE basis. ICG needs the ability to obtain the unbundled elements that comprise the services its customers seek at TELRIC-based rates. BellSouth's provision of the EEL at retail prices would undercut ICG's ability to offer services to its customers. Further, provision of the EEL on a UNE basis will obviate the need for ICG to incur the exorbitant expense of collocating at each central office from which it hopes to serve customers. Availability of the EEL will also free up valuable collocation space.

BELLSOUTH:

No. First, because the Supreme Court vacated the FCC's Rule 47 C.F.R. Section 51.319, neither loops, ports, nor transport have been defined by the FCC as UNEs that BellSouth must provide. Second, even if loops, ports and transport are defined as UNEs, BellSouth is only obligated to provide combinations of those elements where they are currently combined in BellSouth's network. Notwithstanding, BellSouth is willing to provide the EEL combination through commercial agreement.

Because BellSouth is not required to combine network elements for ALECs under the 1996 Act, the issue of applicable rates for such network combinations is not properly the subject of arbitration. To the extent the Commission concludes otherwise, or determines to establish rates for network elements that are currently combined in BellSouth's network, the Commission should do so in the context of the UNE generic proceeding (Dkt. 990649-TP) rather than an arbitration involving one ALEC. Thus, this issue is not appropriate for arbitration.

STAFF ANALYSIS:

The issue before the Commission is to determine whether BellSouth should provide the Enhanced Extended Link loop (EEL) to ICG as an unbundled network element (UNE). There is no dispute as to whether BellSouth will provide the EEL to ICG. BellSouth has agreed to do so. The dispute is whether the EEL will be provided as a UNE.

The EEL is a combination of a loop and dedicated transport that connects a customer to an ALEC point of presence. The EEL would in effect "extend" the customer's loop from one BellSouth central office in which an ALEC is not physically collocated, to another BellSouth central office where the ALEC is physically collocated.

Arguments

ICG witness Holdridge states that by using the EEL, if an ICG customer is served out of Central Office A, yet the ICG collocation site is in Central Office B, ICG can get from Central Office A to the ICG collocation site in Central Office B at a TELRIC rate. (TR 86) Witness Holdridge also states that without the EEL, ICG would be forced to collocate in each and every BellSouth central office in which ICG finds a customer. (TR 98) He further states that "if a carrier is required to incur the large expense of collocation at every central office, then the expansion of facilities-based competition and related new products will be unduly slowed." (TR 98)

ICG would like to be able to obtain the EEL at TELRIC-based rates. ICG witness Holdridge states:

> BellSouth offered to provide the EEL capability to ICG through BellSouth's "Professional Services Agreement" at rates that appear to be substantially higher than they would be under TELRIC. By declining to provide the EEL as a UNE, BellSouth forces ICG to pay a higher rate for the EEL capability. (TR 86)

Witness Holdridge believes that BellSouth's provision of the EEL at retail prices significantly undercuts ICG's ability to introduce the innovative advanced services that ICG's customers want. (TR 86)

ICG witness Schonhaut states that the EEL "is an existing combination of unbundled network elements that exist within the BellSouth network. As such, BellSouth is required to provide the EEL to ICG at TELRIC-based prices." (TR 471)

BellSouth witness Varner counters, "ICG's request for an 'enhanced extended link' would require BellSouth to combine the loop and dedicated transport, a function that BellSouth is not required to perform." (TR 312) Witness Varner argues:

> In accordance with the FCC's Rule 51.315(a), BellSouth is obligated to provide unbundled network elements in a manner that allows requesting telecommunications carriers to combine them in order to provide a telecommunications service. Though requesting telecommunications carriers may combine unbundled elements in any manner they choose, BellSouth is not required to combine unbundled network elements for those carriers. (TR 303)

He further states:

> The Eighth Circuit vacated the FCC's rules that purported to impose such a requirement (§§51.315(c)-(f)). The Eighth Circuit's decision vacating these rules was not challenged by any party, and because those rules are not in effect, BellSouth is not required to combine network elements. However, BellSouth is willing to perform this function upon execution of a commercial agreement that is not subject to the requirements of the Act. (TR 303)

In regard to whether the EEL is an existing combination in BellSouth's network, witness Varner states:

> And the last point on this issue is that BellSouth must provide combinations of loops and transport only where they are currently combined. However, the definition of currently combined is not clear. Based on the FCC's action, we believe that the definition will be that the UNEs must already be in existence and providing service to a BellSouth end user when ICG requests them. That

> interpretation is correct. There are no currently combined UNEs that constitute an EEL. Therefore, ICG's claim that the EEL consists of currently combined UNEs is erroneous. (TR 383-384)

Staff Analysis

Staff reiterates that the issue is not whether BellSouth will provide the EEL to ICG, but whether the EEL will be provided as a UNE. According to 47 CFR, Part 51, Subpart F-Pricing of Elements, certain pricing rules apply to unbundled network elements, interconnection, and methods of obtaining access to unbundled elements, including physical collocation and virtual collocation. Specifically, §51.503(b) reads:

> An incumbent LEC's rates for each element it offers shall comply with the rate structure rules set forth in §§51.507 and 51.509, and shall be established, at the election of the state commission-
>
> (1) Pursuant to the forward-looking economic cost-based pricing methodology set forth in §§51.505 and 51.511; or
>
> (2)Consistent with the proxy ceilings and ranges set forth in §51.513.

Therefore, the real issue before the Commission is what the price should be for the EEL. The list of unbundled network elements that an incumbent LEC must provide to requesting telecommunications carriers was provided in FCC Rule §51.319. However, as stated in Issue 2, this rule was vacated by the United States Supreme Court and remanded back to the FCC. The FCC has issued its Order on this rule; however, it was not issued until after the hearing in this case was held. The FCC did issue a press release prior to the actual Order that was entered as evidence, but again staff notes that the press release is not legally binding. Nonetheless, staff would like to point out that the EEL was not listed as a mandatory UNE in the FCC press release.

BellSouth argues that in order to provide the EEL, it would have to combine the loop and dedicated transport for ICG, and it is not required to do that. Staff agrees that FCC Rules 51.315(c)-(f) regarding incumbent LEC provisioning of combinations were vacated by the Eighth Circuit and remain vacated. However, both parties recognized that reconsideration may be given to these rules. (Schonhaut TR 246, Varner TR 302) Nevertheless, at this time,

incumbent LECs are not required to combine network elements for other telecommunications carriers.

The other argument that ICG presented in support of the EEL being a UNE was that the EEL is a preexisting combination in BellSouth's network. FCC Rule 51.315(b) reads:

> Except upon request, an incumbent LEC shall not separate requested network elements that the incumbent currently combines.

Therefore, according to this rule, if the elements were currently combined in an incumbent's network, they must be provided in combined form to requesting carriers. This rule was vacated by the Eighth Circuit but reinstated by the Supreme Court.

While ICG argues that the EEL is a UNE combination that currently exists in BellSouth's network, staff does not believe that the evidence of record bears this out. In fact when ICG witness Schonhaut was asked if she knew for a fact that the EEL was currently combined in BellSouth's network, she replied "[w]ell, I believe that to be true." (TR 283) The EEL consists of a customer loop and dedicated transport. If a customer is served from one central office and is connected directly to that serving central office via the customer loop, there would normally be no need to be connected to a different central office via dedicated transport unless the customer has requested specific service(s) that would require such a connection (e.g., foreign exchange service or private line services). At best, it appears that such a combination would be the exception rather than the rule. Therefore, staff concludes that ICG's arguments are unpersuasive on this matter.

Staff would also point out that the EEL was not offered in the existing agreement between BellSouth and ICG. (TR 112) While staff understands the pricing benefit of having the EEL at TELRIC rates, staff notes that ICG has been providing service under its existing agreement without such pricing benefits.

Conclusion

ICG has not proven that the EEL must be provided as a UNE. Witness Schonhaut's arguments that the EEL is an existing combination in BellSouth's network are unsubstantiated and unpersuasive. Further, the state of the law currently does not require an incumbent LEC to combine network elements for requesting telecommunications carriers. Therefore, staff recommends that EELs

should not be made available to ICG in the interconnection agreement as UNEs. However, BellSouth has agreed to provide EELs to ICG; therefore, the parties should negotiate the price for the EEL.

ISSUE 4: Should volume and term discounts be available to ICG for UNEs?

RECOMMENDATION: No. There is insufficient evidence in the record to require BellSouth to provide volume and term discounts for Unbundled Network Elements (UNEs) to ICG. **(WATTS)**

POSITIONS OF THE PARTIES

ICG: Yes. ICG should receive the benefit of any reduced costs that BellSouth experiences from provisioning service either in high volumes within a specified period or for extended terms.

BELLSOUTH:

No. BellSouth should not be required to provide volume and term discounts for UNEs. Neither the 1996 Act nor any FCC order or rule require volume and term discount pricing. The UNE recurring rates that ICG pays are cost-based in accordance with the requirements of Section 252(d) and are derived using least-cost, forward looking technology consistent with the FCC's rules. Also, BellSouth's nonrecurring rates already reflect any economies involved when multiple UNEs are ordered and provisioned at the same time. To the extent the Commission decides to consider volume and term discounts for UNEs, the Commission should do so in the context of the UNE generic proceeding (Dkt. 990649-TP) rather than an arbitration involving one ALEC.

STAFF ANALYSIS:

The issue before the Commission is to determine whether BellSouth should be required to provide volume and term discount pricing for UNEs to ICG.

ARGUMENTS:

ICG witness Starkey states that ICG is seeking a commercial relationship similar to the type it has with its other suppliers, customers and business partners.(TR 156) He describes the arrangement sought as "a commitment to passing on cost savings associated with providing services in larger volume and commitments for longer term use of the BST network for carriers willing to commit themselves to volume and term purchases." (TR 156-157)

Witness Starkey begins by stating that he "partially" disagrees with BellSouth's contention that volume and term discount pricing is required by neither the Act nor an FCC order or rule. (TR 157) He points out that Section 252(d)(1) of the Act provides two primary criteria for the establishment of UNE prices. That section provides:

> Determinations of a State commission of the just and reasonable rate for the interconnection of facilities and equipment for purposes of subsection (c)(2) of section 251, and the just and reasonable rate for network elements for purposes of subsection (c)(3) of such section-
> (A) shall be-
> (i) based on the cost (determined without reference to a rate-of-return or other rate-based proceeding) of providing the interconnection or network element (whichever is applicable),
> and
> (ii) nondiscriminatory, and
> (B) may include a reasonable profit. (TR 157-158)

Witness Starkey also cites the FCC's Local Competition Order, FCC 96-325, at Paragraph 743:

> We conclude, as a general rule, that incumbent LECs' rates for interconnection and unbundled elements must recover costs in a manner that reflects the way they are incurred. This will conform to the 1996 Act's requirement that rates be cost-based, ensure requesting carriers have the right incentives to construct and use the public network facilities efficiently, and prevent incumbent LECs from inefficiently raising costs in order to deter entry. We note that this conclusion should facilitate competition on a reasonable and efficient basis by all firms in the industry by establishing prices for interconnection and unbundled elements based on costs similar to those incurred by the incumbents, which may be expected to reduce the regulatory burdens and economic impact of our decision for many parties, including both small entities seeking to enter the local exchange markets and small incumbent LECs. (TR 158-159)

Witness Starkey reasons that the requirement that rates be cost based and the FCC's subsequent interpretation that rates recover costs in the same manner in which they are incurred requires that BellSouth's UNE rates reflect any reductions resulting from volume or term purchases.(TR 160) Therefore, ICG believes offering carriers volume and term discounts is the most reasonable means of complying with this requirement.(TR 159)

For additional justification, witness Starkey next addresses the FCC's interpretation of the term "nondiscriminatory" as provided in Paragraph 315 of its Local Competition Order (EXH 1):

> The duty to provide unbundled network elements on "terms, and conditions that are just, reasonable, and nondiscriminatory" means, at a minimum, that whatever those terms and conditions are, they must be offered equally to all requesting carriers, and where applicable, they must be equal to the terms and conditions under which the incumbent LEC provisions such elements to itself. (TR 159-160)

Witness Starkey interprets this provision to mean that:

> ...if BST experiences any reductions in cost as a result of a carrier's purchase of unbundled elements in volume or as the result of the carrier's commitment to purchase those elements over a period of time, BST is required to reflect that cost reduction in a non-discriminatory [*sic*] fashion to the carrier purchasing those facilities. (TR 160)

He further states that otherwise, BellSouth would incur a lower cost per unit of providing UNEs than was reflected in the price charged to its competitors. Witness Starkey concludes that such practice would conflict with BellSouth's obligation to provide cost-based, nondiscriminatory rates. (TR 160)

Witness Starkey asserts that BellSouth's UNE prices are to be based on the TELRIC pricing methodology adopted by the FCC. He admits that the TELRIC methodology limits the extent of any cost savings that could result from larger volume purchases and term commitments. Specifically, witness Starkey states:

> The TELRIC methodology does require that prices for unbundled network elements reflect the economies of scale that are enjoyed by providing the'total element.' To a certain extent, this reduces the likelihood that as BST sells greater volumes of specific unbundled network elements, its TELRIC costs go down as a result of the economies of scale it experiences. This results from the fact that these economies of scale have, to some extent, already been accounted for in the derivation of TELRIC costs. (TR 160)

But witness Starkey then argues:

> However, there are a number of other areas where per-unit costs will undoubtedly fall with increases in volume purchases and commitments to longer purchase times and where the TELRIC methodology as applied does not account for such reductions. (TR 161)

In addition to his assertion, witness Starkey believes that one of the most important steps in developing a TELRIC study is the process of 'unitizing' network investments into costs attributable to individual UNEs.(TR 161) He refers to Paragraph 682 of the FCC's Local Competition Order (EXH 1)which provides:

> Per unit costs shall be derived from total costs using reasonably accurate 'fill factors' (estimates of the proportion of the facility that will be 'filled' with network usage); that is, the per unit cost associated with a particular element must be derived by dividing the total cost associated with the element by a reasonable projection of the actual usage of the element. (TR 161)

Witness Starkey uses an example in which he calculates an ILEC's per unit costs based on his understanding of the FCC's guidelines. In his first scenario, witness Starkey assumes an investment of $1,000 for a piece of equipment that can support 100 loops. He calculates that BellSouth would be able to attribute "far more than $10 to each unit (likely in the neighborhood of $20 based upon a 'fill factor' of 50% - i.e. $1,000/50)."(TR 161) In the next scenario, witness Starkey states:

> ...it is obvious that if ICG were willing to commit to 80 loops served by the particular piece of equipment described above and BST had developed its TELRIC costs based upon a 50% fill factor, BST's actual costs would fall on a per unit basis from $20 per loop ($1,000/50) to $12.50 per loop ($1,000/80).(TR 161-162)

From this analysis, witness Starkey concludes that "as the volume of UNE purchases increases, the 'actual fill' associated with the underlying BST equipment will rise, thereby altering the 'actual' usage by which total investments are allocated." He goes on to emphasize that as BellSouth's rates are set today without any volume or term discount, only BellSouth would enjoy whatever cost reductions are achieved. Witness Starkey concludes that this is in direct conflict with the FCC's mandates that UNE rates recover costs in the manner in which they are incurred and that the rates are to be nondiscriminatory. (TR 161-162)

BellSouth's witness Varner disputes witness Starkey's analysis and conclusions by stating that the analysis is flawed because witness Starkey assumes that "TELRIC prices were based on network costs as they <u>are</u> instead of what they are <u>projected to be.</u>" As an example, Witness Varner states that the claim that a volume commitment by ICG would increase plant utilization ignores the way the costs were developed; plant utilization in the study represents the Commission's view of plant utilization in the future. He further states that any impact of volume requested by ICG has already been included in this utilization percentage. (TR 366-367)

Regarding term discounts, Witness Starkey refers to Paragraph 687 of the FCC's Local Competition Order (EXH 1):

> As noted, we also agree that, as a matter of theory, an increase in risk due to entry into the market for local exchange service can increase a LEC's cost of capital. We believe that this increased risk can be partially mitigated, however, by offering term discounts, since long-term contracts can minimize the risk of stranded investment... (TR 163)

He further states that BellSouth "uses both volume and term discount structures pervasively in pricing its retail services and

has begun to employ these discounts with increasing frequency as local competitive alternatives increase." (TR 164)

Witness Varner admits that BellSouth offers volume and term discounts for tariff services and custom service arrangements. However, he explains that these discounts are neither to UNEs as ICG is proposing, nor are they applicable to all tariff services.(TR 454) According to witness Varner, some tariff services have volume or term contract arrangements and some do not. He further explains that such determination is dictated by the marketplace; these arrangements are generally found in situations where other providers offer a volume and term arrangement and BellSouth offers them as well in order to compete. (TR 454)

Witness Varner agrees with witness Starkey that in the retail world, the risk of stranded plant costs would be reduced by a term commitment.(TR 367) However, witness Varner also emphasizes that "none of the costs that a term commitment would reduce are included in TELRIC" and that "the impact of any reduction, even if it exists, is irrelevant with respect to UNE prices."(TR 367) Witness Varner also states that witness Starkey misses a major point in that retail prices typically exceed costs and that discounts due to term commitments reduce the level of contribution and not the level of costs. He concludes by stating that UNE prices do not include any contribution; thus, there is no basis for offering term discounts. (TR 367)

Witness Starkey disputes witness Varner's contention that there is no contribution in UNE prices. He states that "UNE prices set at TELRIC rates include an economic return, which is a return on the capital employed to provision those unbundled network elements." (TR 203) He reiterates his point that when BellSouth knows the number of units that will be sold from a given facility, "its risk associated with employing that capital is decreased." Witness Starkey concludes by stating that BellSouth's "economic return is likewise decreased and the price for unbundled network elements decreases, as well." (TR 203)

When asked to provide examples of costs included in TELRIC that would be reduced in a term commitment, witness Starkey states:

> I think I mentioned this in my -- I don't remember whether it is in my direct or rebuttal, but I talk about to the extent to which the risk associated with constructing facilities on BellSouth's behalf would

> certainly be lower if they knew that ICG, for instance, was going to purchase X number of units of capacity for a number or a year or a period of time. Based on that, they don't have to -- or BellSouth doesn't have to engineer its network attempting to forecast what that demand would be. It knows it already. The risk associated with its capital and placing its capital is much lower. In TELRIC cost studies one of the issues is what is the cost of capital associated with employing a network. Risk is a factor associated with the rate of the cost of capital that is included in the study. Less risk, the lower the rate of the cost of capital, the lower the unbundled network element rate. (TR 202)

Finally, when asked for examples using specific UNEs and associated costs demonstrating BellSouth's potential savings upon providing volume and term discounts, witness Starkey responds by referencing Order No. PSC-96-1579-FOF-TP. He states that in it, Ms. Caldwell, a BellSouth witness in Docket No. 960833-TP, suggests that TELRIC is comprised of both volume sensitive and volume insensitive costs. He further states that "Ms. Caldwell suggests that volume sensitive costs rise and fall with the level of volume that is purchased. Ms. Caldwell goes on to state that there are no volume insensitive costs in the costs associated with the loop." Witness Starkey states that this leads him to believe that all costs associated with BellSouth's loop are volume sensitive costs. Witness Starkey concludes that Ms. Caldwell's statement supports the position ICG is taking in this docket -- that "the larger the volume to which ICG is willing to commit, so should follow that the costs are lowered, as well." (TR 203-204)

STAFF'S ANALYSIS

Staff believes that the basis for ICG's request for volume and term discounts rests on the presumption that there will be cost savings associated with BellSouth's provision of such discounts. However, the record in this docket does not provide sufficient evidence that the Commission should require BellSouth to provide such discounts at this time.

ICG argues that if BellSouth experiences cost savings due to offering, e.g., a term plan, it is required to reflect such savings in its rates. However, the primary question to be answered is whether BellSouth will actually realize any cost savings by providing the requested volume and term discount arrangements. Although ICG provides a few mathematical scenarios demonstrating a potential reduction in costs for BellSouth, BellSouth contends that certain theoretical assumptions made in the analysis are inaccurate. Witness Varner emphasizes that witness Starkey does not understand the manner in which the cost studies were done. (TR 366-367) Staff believes that even if ICG is correct in its assumptions, the examples provided in this docket were still insufficient to prove that BellSouth will receive cost savings that may be passed on to ICG.

CONCLUSION

The record in this docket does not provide conclusive evidence regarding the existence of cost savings that will be achieved through offering volume and term discounts. No cost studies were filed, nor were any specific parts of previous studies filed with the Commission specifically referenced. Since there is no reliable evidence in the record in this proceeding that the provision of volume and term discount plans result in lower UNE costs, staff recommends denying ICG's request that volume and term discounts be made available for UNEs.

ISSUE 5: For purposes of reciprocal compensation, should ICG be compensated for end office, tandem, and transport elements of termination where ICG's switch serves a geographic area comparable to the area served by BellSouth's tandem switch?

RECOMMENDATION: No. The evidence of record does not show that ICG's switch will serve an area comparable to the area served by BellSouth's tandem switch. In addition, the evidence does not show that ICG's switch will perform the same functions as a BellSouth tandem switch. Therefore, staff recommends, for the purposes of reciprocal compensation, that ICG not be compensated for the tandem element of terminating calls on their network which originated on BellSouth's network. However, staff does recommend that ICG be compensated for the transport and end office elements of termination. **(HINTON)**

POSITIONS OF THE PARTIES

ICG: Yes. In Florida, ICG is in a start-up mode. In states in which ICG has an established business, it employs a network configuration in which its switch serves a geographical area comparable to that served by a tandem switch and it provides comparable functionality. As ICG grows its business in Florida, it intends to develop the type of network that typifies its approach to network design in other jurisdictions.

BELLSOUTH:

No. The appropriate rates for reciprocal compensation are the elemental rates for end office switching, tandem switching and common transport that are used to transport and terminate local traffic. If a call is not handled by a switch on a tandem basis, it is not appropriate to pay reciprocal compensation for the tandem switching function. BellSouth's position is consistent with the Commission's December 16, 1996 Order in the MFS/Sprint Arbitration (Order No. PSC-96-1532-FOF-TP), which was reaffirmed in the MCI/Sprint Arbitration in an Order dated April 14, 1997 (Order No. PSC-97-0294-FOF-TP).

STAFF ANALYSIS:

The issue before the Commission is to determine whether ICG Telecom Group, Inc. (ICG) is entitled to be compensated for end office, tandem, and transport elements of termination where ICG's switch serves a geographic area comparable to the area served by BellSouth Telecommunications, Inc.'s (BellSouth) tandem switch.

47 C.F.R. § 51.711 (Symmetrical reciprocal compensation) states:

> (3) Where the switch of a carrier other than an incumbent LEC serves a geographic area comparable to the area served by the incumbent LEC's tandem switch, the appropriate rate for the carrier other than an incumbent LEC is the incumbent LEC's tandem interconnection rate.

Arguments

ICG witness Starkey asserts that "BellSouth should pay ICG a reciprocal compensation rate based upon the recovery of tandem, transport and end office switching costs." (TR 505) Witness Starkey states that for an ALEC to qualify for the tandem termination rate, the FCC's First Report and Order, FCC 96-325, requires only that the ALEC's switch serve a geographic area comparable to that served by an ILEC tandem. (TR 150) Witness Starkey further states that "the FCC establishes that the LEC's tandem interconnection rate is the appropriate rate for an ALEC to receive if this single geographic criterion is met." (TR 506) In support, ICG witness Starkey quotes the FCC First Report and Order:

> 1090. We find that the "additional costs" incurred by a LEC when transporting and terminating a call that originated on a competing carrier's network are likely to vary depending upon whether tandem switching is involved. We, therefore, conclude that states may establish transport and termination rates in the arbitration process that vary according to whether the traffic is routed through a tandem switch or directly to an end-office switch. In such event, states shall also consider whether new technologies (e.g. fiber ring or wireless networks) perform functions similar to those performed by an incumbent LEC's tandem switch and thus, whether some or all calls terminating on the new entrant's network should be priced the same as the sum of transport and termination via the incumbent LEC's tandem switch. Where

> the interconnecting carrier's switch serves a geographic area comparable to that served by the incumbent LEC's tandem switch, the appropriate proxy for the interconnecting carrier's additional costs is the LEC tandem interconnection rate. (TR 505-506)

ICG states that "[i]n Florida, ICG is in a start-up mode. However, as it grows its business in Florida, ICG intends to develop the type of network - including the geographical coverage of its switches - that typifies its approach to network design in other jurisdictions." (Starkey TR 507) Witness Starkey states further that in states where ICG has established business, it employs a network with a switch that serves a geographic area comparable to that of a BellSouth tandem switch. (TR 506)

BellSouth witness Varner contends, "[a]t the present time ICG is not collocated in any BellSouth central office in Florida. Therefore, it is not possible to determine whether ICG's switch would actually serve a geographic area comparable to BellSouth's tandem." (TR 343) Witness Varner further argues that if ICG intends to provide service in Florida similar to how they are providing service in Alabama, then their switch will not serve a geographic area comparable to that served by BellSouth's tandem switch. (TR 343) Witness Varner states:

> ICG ignores the fact that BellSouth's Alabama tandem switch serves six central offices in addition to the two central offices ICG has chosen to serve. Obviously, the area served by BellSouth's tandem switch (eight central offices) is not comparable to the area ICG has elected to serve (two central offices). (TR 343)

ICG asserts that in addition to meeting the geographic criterion indicated in FCC 96-325, ¶1090, its network also performs similar functionality, which further qualifies them for reciprocal compensation at the tandem rate. (Starkey TR 150) Witness Starkey states that "[t]he advent of relatively inexpensive fiber transport facilities and the enormous capacity of today's switching platforms enable ALECs to now provide many of the same functions with a single switch that may be performed by at least two switches in the BST network." (TR 152) Although witness Starkey described ICG's network as having only one switch, he states this switch is a "class 4/class 5 switch, which is a tandem and end office switch combined and provides the functionality of both." (TR 201)

Witness Starkey explains:

> Tandem switches (what are commonly called Class 4 switches in the traditional AT&T hierarchy), generally aggregate toll traffic from a number of central office switches (Class 5 switches) for purposes of passing that traffic to the long distance network. The tandem switch is also a traditional focal point for other purposes as well, including the aggregation and processing of operator services traffic, routing traffic that is to be transferred between the trunk groups of two separate carriers and measuring the recording toll traffic detail for billing. While ILECs have traditionally employed two separate switches to accomplish these Class 4 and Class 5 functions, ICG's Lucent 5ESS platform performs all of these functions in addition to a number of others within the same switch. (TR 150)

In addition to requesting tandem termination rates, witness Starkey asserts that ICG should receive reciprocal compensation for costs incurred in addition to switching.(TR 152) Witness Starkey states that in addition to switching costs associated with identifying the appropriate termination point for a call originated on BellSouth's network, ICG transports these calls to the proper collocation point using its fiber network and identifies the proper unbundled loop to which the call must be completed. (TR 153) He argues that this process is no different than that used by BellSouth to terminate a similar call originated on ICG's network; therefore, ICG should be paid a combined rate equal to the rate ICG pays to BellSouth for terminating traffic based on the individual rate elements of tandem switching, transport and end office switching. (TR 153)

BellSouth witness Varner contends that ICG's Lucent 5ESS switch functions only as an end office switch. (TR 365) Witness Varner states that "ICG's switch is not providing a transport or tandem function, but is switching traffic through its end office for delivery of traffic from that switch to the called party's premises." (TR 365) BellSouth's position is that if a call is not handled by a switch on a tandem basis, it is not appropriate to pay reciprocal compensation for the tandem switching function. (Varner TR 342) Witness Varner further explains:

> A tandem switch connects one trunk to another trunk and is an intermediate switch or connection between an originating telephone call location and the final destination of the call. An end office switch is

> connected to a telephone subscriber and allows the call to be originated or terminated. If ICG's switch is an end-office switch, then it is handling calls that originate from or terminate to customers served by the local switch, and thus ICG's switch is not providing a tandem function. ICG is seeking to be compensated for the cost of equipment it does not own and for functionality it does not provide. (TR 343)

BellSouth witness Varner also argues that ICG does not provide transport between its switch and its collocations. Witness Varner contends the equipment used by ICG to collocate is a Subscriber Loop Carrier (SLC), which is part of loop technology and provides no switching functionality. (TR 344) He states that "ICG is only providing the termination function, which is not the same as transport from the ILEC tandem to end offices as ICG contends." (TR 344) Witness Varner further states:

> [t]ransport includes any flat rated dedicated services, tandem switching function and 'common' transport between the tandem switch and end office switch necessary to transport the call from the interconnection point to the end office. ICG's switch is not providing a common transport or tandem function, but is switching traffic through its end office for delivery of that traffic from that switch to the called party's premises. (TR 345)

BellSouth cites Florida Public Service Commission (FPSC) Orders as precedent for its assertion that since ICG's network does not perform tandem and transport functions, ICG is not entitled to reciprocal compensation at those rates. [Order No. PSC-96-1532-FOF-TP and PSC-97-0294-FOF-TP] (TR 365)

Staff's Analyses

Staff agrees that the evidence of record shows that ICG presently has no facilities (i.e., switches or transport facilities) in Florida. (TR 240) While ICG states that it will begin facilities-based service in Florida by fourth quarter 1999, the evidence of record does not show that its switch will serve a geographic area comparable to an area served by a BellSouth tandem switch. ICG simply states it is in "start-up mode" in Florida, but plans to develop the type of network in which its switch will serve a geographic area comparable to that of the BellSouth tandem. (Starkey TR 507) Because ICG currently does not have a network in place in Florida, staff cannot determine if ICG's network will, in

fact, serve a geographic area comparable to one that is served by a BellSouth tandem switch.

While 47 C.F.R. § 51.711 allows the FPSC to provide for reciprocal compensation at the tandem rate if the switch of a carrier other than an incumbent LEC serves a geographic area comparable to that served by the incumbent LEC's tandem switch, the evidence of record does not provide an adequate basis to determine that ICG's network will fulfill this "geographic criterion." In addition, in the MCI/Sprint arbitration Order issued April 14, 1997 [Order No. PSC-97-0294-FOF-TP], the FPSC concluded:

> We find that the Act does not intend for carriers such as MCI to be compensated for a function they do not perform. Even though MCI argues that its network performs "equivalent functionalities" as Sprint in terminating a call, MCI has not proven that it actually deploys both tandem and end office switches in its network. If these functions are not actually performed, then there cannot be a cost and a charge associated with them. Upon consideration, we therefore conclude that MCI is not entitled to compensation for transport and tandem switching unless it actually performs each function. (Order at p.10)(EXH 1)

Similarly, the evidence of record in this arbitration does not show that ICG will deploy both a tandem and end office switch in its network. In addition, since tandem switching is described by both parties as performing the function of transferring telecommunications between two trunks as an intermediate switch or connection, staff does not believe this function will or can be performed by ICG's single switch. As a result, staff cannot at this time recommend that ICG be compensated for the tandem element of termination.

Transport is defined in the FCC's Rules as:

> the transmission and any necessary tandem switching of local telecommunications traffic subject to section 251(b)(5) of the Act from the interconnection point between the two carriers to the terminating carrier's end office switch that directly serves the called party, or equivalent facility provided by a carrier other than an incumbent. (47 C.F.R. § 51.701(c))

This definition describes the transmission of local telecommunications from the point of interconnection to the end office of the terminating carrier. While the definition provides for "any necessary tandem switching," transport need not include tandem switching. As such, staff believes the record shows that the fiber network ICG intends to deploy will provide a transport and end office function. Therefore, staff recommends, for the purpose of reciprocal compensation, that ICG be compensated for the elements of transport and end office switching.

Conclusion

Staff believes the evidence of record does not support ICG's claim that its network serves a geographic area comparable to the area served by BellSouth's tandem switch. Therefore, staff recommends that ICG not be compensated for the tandem element of termination. However, staff believes it is appropriate for ICG to be compensated through reciprocal compensation for the transport and end office switching elements of termination.

ISSUE 6: **(A)** Should BellSouth be required to enter into a binding forecast of future traffic requirements for a specified period?

(B) If so, are they then required to provision the requisite network buildout and necessary support?

RECOMMENDATION: **(A)** No. BellSouth should not be required to enter into a binding forecast of future traffic requirements for a specified period with ICG. There is no such requirement in the Telecommunications Act of 1996 nor in any FCC Order or rule. **(B)** If the Commission approves staff's recommendation in Issue 6(A), BellSouth would not be required to provision the requisite network buildout and necessary support, because 6(B) would be rendered moot. **(BROWN)**

POSITIONS OF THE PARTIES

ICG: **(A)** Yes. ICG believes its traffic requirements will continue to grow. In order to support competition, by ensuring that the requisite capacity will be in place, BellSouth should be required to enter a binding forecast with ICG. BellSouth has nothing to lose in agreeing to a binding forecast because ICG will pay BellSouth for the increased capacity whether or not it actually uses it.

(B) ICG must have the requisite capacity on BellSouth's network as its traffic requirements grow in order to serve its customers. By entering a binding forecast, ICG commits to pay for the facilities; accordingly, BellSouth should be required to provision them.

BELLSOUTH:

(A) No. BellSouth is not required by the 1996 Act or any FCC order or rule to commit to a binding forecast with ICG or any ALEC.

(B) If BellSouth were to be required to enter into a binding forecast with ICG for ICG's traffic requirements, BellSouth would honor its contractual obligation. If BellSouth were required to enter into such binding forecast, however, BellSouth should remain free to determine the necessity for any network buildout or support or the manner in which such resources should be deployed. In addition, BellSouth should be permitted to

> reserve the right to challenge any ICG forecast ICG contends should be binding if BellSouth believes it would not be technically feasible for BellSouth to provision or support the forecasted requirements.

STAFF ANALYSIS:

The issue before the Commission is to determine whether BellSouth should be required to enter into a binding forecast for future traffic requirements for a specified period, and if so, should BellSouth be required to provision the requisite network buildout and necessary support. ICG witness Jenkins contends that such a requirement is necessary to ensure that BellSouth's network will be able to handle reasonably foreseeable traffic volumes and that any additional trunking be provided when deemed necessary. (TR 62) BellSouth witness Varner contends that there is no such obligation under the Telecommunications Act of 1996, or any FCC Order or rule to commit BellSouth to such an arrangement. (TR 349; 386) However, BellSouth has stated that it is willing to continue negotiating towards an acceptable arrangement. (TR 349)

Arguments:

ICG currently provides BellSouth with quarterly non-binding traffic forecasts to aid in planning for the growth of its (BellSouth's) network. ICG witness Jenkins states that the concern with the current arrangement, however, stems from the fact that BellSouth is under no obligation to respond to these forecasts. (TR 67) Witness Jenkins further states that as a result, BellSouth may still choose not to provision additional trunking even when the forecasts indicate additional trunking may be needed. (TR 61) Because of this concern, witness Jenkins proposes that "ICG is willing to commit to BellSouth for a specified volume of interconnection trunks as part of a binding forecast - whether or not ICG's traffic volume achieves the forecasted levels." (TR 61) Furthermore, if the traffic volume were to fall short of the forecasted level, ICG would pay BellSouth for the full cost of the unused trunks. (Jenkins TR 59, 66) Witness Jenkins claims that the binding forecast which they are proposing is a "win/win situation," involving no risk to BellSouth. (TR 61, 66)

In addition, witness Jenkins states that ICG is only seeking the option to require binding forecasts and even then, only in certain circumstances. (TR 62) He states:

> ICG would only use the binding forecast option where (i) it was confident of substantial additional growth and

(ii) it was concerned that, without a binding commitment by BellSouth to timely provision the necessary trunks, there would be an unacceptable risk of blockage of incoming calls to ICG's network.(TR 62)

Witness Jenkins believes that BellSouth has already agreed to provide binding forecasts in "at least one agreement."(TR 64) In support of his argument he cites a provision in the agreement between BellSouth and KMC Telecom (KMC) approved by the FPSC in Order No. PSC-97-0857-FOF-TP and PSC-98-0990-FOF-TP. The provision is as follows:

20.4 Binding Traffic Forecasts
Any Party that is required pursuant to this Agreement to provide a forecast (the "Forecast Provider") or the Party that is entitled pursuant to this Agreement to receive a forecast (the "Forecast Recipient") with respect to traffic and volume requirements for the services and Network Elements provided under this Agreement may request in addition to non-binding forecasts required by Section 20.3 that the other enter into negotiations to establish a forecast (a "Binding Forecast") that commits such Forecast Provider to purchase, and such Forecast Recipient to provide, a specified volume to be utilized as set forth in such Binding Forecast. The Forecast Provider and the Forecast Recipient shall negotiate the terms of such Binding Forecast in good faith and shall include in such Binding Forecast provisions regarding price, quantity, liability for failure to perform under a Binding Forecast and any other terms desired by such Forecast Provider and Forecast Recipient. Notwithstanding Section 31.0, the Parties agree that each forecast provided under this Section 20.4 shall be deemed "Proprietary Information" under Section 31.0. (emphasis added) (TR 63-64)

ICG witness Jenkins further states that "there is no reason similar language should not be included in the ICG agreement."(TR 64) However, witness Jenkins and BellSouth witness Varner note that BellSouth does not oppose including such language and has offered to make the same language applicable to ICG. (TR 68; TR 453)

BellSouth witness Varner believes that the Binding Traffic Forecasts provision (Section 20.4), referenced above, does not truly represent a binding forecast. Instead, it is an agreement to determine whether the parties could come up with a "binding forecast mechanism that we could agree to."(TR 453) Witness Varner

also states that the provision was "an agreement to negotiate, continue negotiating, and come up with an arrangement."(TR 453)

BellSouth witness Varner contends that the Telecommunications Act of 1996 does not impose any obligation to enter into binding forecasts. This position was affirmed by ICG witness Jenkins.(TR 65, 67, 68) When asked about legal and contractual requirements of providing a binding forecast, ICG witness Jenkins stated, "there is no requirement."(TR 68) Despite no requirement to do so, BellSouth is considering offering such an arrangement on a voluntary basis pending further analysis.(Varner TR 386) BellSouth witness Varner states, "it (Section 20.4) has turned out to be rather complicated to be able to do that and still fulfill our nondiscrimination obligations to other carriers."(TR 454) Witness Varner also states that BellSouth is willing to discuss the specifics of such an arrangement with ICG.(TR 349, 453)

Staff's Analysis:

Based on the evidence in the record, staff agrees that BellSouth is not required by the Act, FCC rule, FCC Order, or FPSC Order to enter into a binding forecast arrangement with ICG. Therefore, staff does not believe that BellSouth should be required to do so. As such, BellSouth should not be required to provide the requisite network buildout and necessary support to accommodate such a forecast.

ICG's argument relies, in large part, upon the language in the KMC/BellSouth agreement. Staff also notes that it does not believe that Section 20.4 of the KMC/BellSouth agreement requires the "binding forecast" that ICG is requesting. The language contained in that provision speaks only to a party's option to request that the other party begin negotiating towards establishing a binding forecast. ICG witness Jenkins recognizes this when he states that "Section 20.4 of the KMC agreement refers to -- requires that negotiations take place between the forecast provider and the forecast recipient."(TR 70) BellSouth has offered this provision to ICG and is willing to discuss the specifics of such an arrangement. Nevertheless, regardless of what is contained in the KMC/BellSouth agreement, that was a negotiated agreement between those two parties and has no precedential value in this case. It is not a basis for requiring BellSouth to enter into a binding forecast arrangement with ICG. However, if the parties so choose, they may negotiate such an arrangement.

ICG witness Jenkins describes an event where overflow situations resulted because trunks that had been ordered had not

been installed in time and no binding forecast existed.(TR 70-71) Witness Jenkins also states that it is anticipated that "the situation will only get worse as ICG's needs increase, and as we move into other large markets, such as Miami." (TR 71) Staff believes that BellSouth and ICG have an opportunity to avoid the situation described above by including language similar to the KMC provision in the new agreement. This should allow ICG to make its forecasted needs known to BellSouth and also provide a forum in which the parties could negotiate towards a mutually agreeable binding forecast arrangement. Staff reiterates that BellSouth has already offered to include the KMC provision in the new agreement with ICG, and to negotiate the details of such an arrangement. (TR 349; 453)

Conclusion:

Staff recommends that BellSouth not be required to enter into a binding forecast of future traffic requirements for a specified period with ICG. There is no such requirement in the Telecommunications Act of 1996 or in any FCC Order or rule. If the Commission approves staff's recommendation in Issue 6(A), BellSouth should not be required to provision the requisite network buildout and necessary support.

ISSUE 7: Should this docket be closed?

RECOMMENDATION: No, the parties should be required to submit a signed agreement that complies with the Commission's decisions in this docket for approval within 30 days of issuance of the Commission's order. This docket should remain open pending Commission approval of the final arbitration agreement in accordance with Section 252 of the Telecommunications Act of 1996. **(FORDHAM)**

STAFF ANALYSIS: The parties should be required to submit a signed agreement that complies with the Commission's decisions in this docket for approval within 30 days of issuance of the Commission's order. This docket should remain open pending Commission approval of the final arbitration agreement in accordance with Section 252 of the Telecommunications Act of 1996.