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September 7, 1999

Mrs. Blanca S. Bayó
Director, Division of Records and Reporting
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850

Re: Docket No. 990691-TP (ICG Arbitration)

Dear Ms. Bayó:

Enclosed is an original and fifteen copies of BellSouth Telecommunications, Inc.'s Rebuttal Testimony of Alphonso J. Varner, which we ask that you file in the captioned docket.

A copy of this letter is enclosed. Please mark it to indicate that the original was filed and return the copy to me. Copies have been served to the parties shown on the attached Certificate of Service.

Sincerely,

E. Earl Edenfield Jr.
E. Earl Edenfield, Jr. (BW)

cc: All Parties of Record
Nancy B. White
Marshall M. Criser III
R. Douglas Lackey

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CERTIFICATE OF SERVICE
Docket No. 990691-TP

I HEREBY CERTIFY that a true and correct copy of the foregoing was served via U.S. Mail this 7th day of September, 1999 to the following:

C. Lee Fordham
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Tallahassee, FL 32399-0850

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BELLSOUTH TELECOMMUNICATIONS, INC.

REBUTTAL TESTIMONY OF ALPHONSO J. VARNER

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 990691-TP

SEPTEMBER 7, 1999

Q. PLEASE STATE YOUR NAME, YOUR POSITION WITH BELLSOUTH TELECOMMUNICATIONS, INC. ("BELLSOUTH") AND YOUR BUSINESS ADDRESS.

A. My name is Alphonso J. Varner. I am employed by BellSouth as Senior Director for State Regulatory for the nine-state BellSouth region. My business address is 675 West Peachtree Street, Atlanta, Georgia 30375.

Q. HAVE YOU PREVIOUSLY FILED TESTIMONY IN THIS DOCKET?

A. Yes. I filed direct testimony and seven exhibits on August 2, 1999.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. My testimony rebuts portions of the direct testimony filed by ICG Telecom Group, Inc. ("ICG") witnesses Michael Starkey, Bruce Holdridge and Karen Notsund filed with the Florida Public Service Commission ("Commission") on August 2, 1999.

Q. ON PAGE 11, MR. STARKEY STATES THAT ISP-BOUND TRAFFIC IS FUNCTIONALLY NO DIFFERENT THAN OTHER TYPES OF TRAFFIC FOR WHICH BELLSOUTH HAS AGREED TO PROVIDE RECIPROCAL COMPENSATION. IS HE CORRECT?

A. No. Mr. Starkey is incorrect. Traffic bound for the Internet for Internet Service Providers ("ISP-bound traffic") is functionally equivalent to access traffic, not local traffic. As I stated in my direct testimony, only local traffic is subject to reciprocal compensation obligations. As previously confirmed by the Federal Communications Commission's ("FCC") Declaratory Ruling, ISP-bound traffic is jurisdictionally interstate; therefore, reciprocal compensation for ISP-bound traffic under Section 251 is not applicable.

Q. MR. STARKEY EXPLAINS ON PAGE 17 THAT CALLS DIRECTED TO ISPs ARE FUNCTIONALLY IDENTICAL TO LOCAL VOICE CALLS FOR WHICH BST HAS AGREED TO PAY TERMINATION CHARGES. DO YOU AGREE?

A. To the extent this statement is correct, the same could be said of a call to an interexchange carrier's ("IXC's") point of presence ("POP"). Mr. Starkey would agree that such calls to an IXC's POP are not subject to reciprocal compensation. It is not the technical use of the facilities that is relevant here, rather it is the nature of the traffic. Just like IXC traffic, ISP-bound traffic is originating access traffic.

Q. AT PAGE 8 OF HIS TESTIMONY, MR. STARKEY QUOTES FROM PARAGRAPH 25 OF THE FCC'S DECLARATORY RULING IN AN ATTEMPT TO SHOW THAT THIS COMMISSION SHOULD APPLY RECIPROCAL COMPENSATION TO ISP-BOUND TRAFFIC IN THE PARTIES' INTERCONNECTION AGREEMENT. PLEASE COMMENT.

A. Mr. Starkey's use of paragraph 25 is incorrect. The basis for paragraph 25 is to advise the state commission that, in the absence of a federal rule governing ISP-bound traffic, states may "at this point" determine how ISP traffic should be treated in interconnection agreements. In other words, to do so would not violate any federal rule "at this point." However in its NPRM, the FCC asked for comment from the parties as to whether it is proper for states to address ISP traffic in arbitration proceedings. BellSouth believes it is not within the states' authority to do so and the FCC lacks the power to vest that authority with the state commissions. In any event, the FCC notes that decisions by the states must be consistent with federal law and that states must comply with the FCC's rules when adopted.

In light of this instruction to the states, it is important to emphasize the FCC's position as stated in footnote 87 of its Declaratory Ruling: "We conclude in this Declaratory Ruling, however, that ISP-bound traffic is non-local interstate traffic. Thus, the reciprocal compensation requirements of section 251(b)(5) of the Act and Section 51, Subpart H (Reciprocal Compensation for Transport and Termination of Local Telecommunications Traffic) of the Commission's rules do not govern inter-carrier compensation for this traffic." The inescapable conclusion that this Commission must reach is that the FCC has exercised jurisdiction over ISP-bound traffic and footnote 87 states that ISP-bound traffic is not subject to reciprocal compensation. Instead, ISP-bound traffic will be subject to an inter-carrier compensation mechanism more appropriate to interstate access traffic.

Q. MR. STARKEY FURTHER QUOTES FROM PARAGRAPH 25 IN AN ATTEMPT TO SHOW THAT THE FCC WAS ENCOURAGING STATES TO APPLY RECIPROCAL COMPENSATION TO ISP-BOUND TRAFFIC. DO YOU AGREE?

A. No. The FCC is not at all encouraging the states to adopt reciprocal compensation for ISP-bound traffic in paragraph 25. Footnote 87 clearly demonstrates the fallacy of Mr. Starkey's conclusion. Instead, the FCC is simply explaining why it believes those states that ruled that reciprocal compensation is applicable to ISP-bound traffic could have done so. Paragraph 25 states in part, "[w]hile to date the Commission has not adopted a specific rule governing the matter, we do note that our policy of treating ISP-bound traffic as local for purposes of interstate access charges would, if applied in the separate context of reciprocal compensation, suggest that such compensation is due for that traffic." The rest of the Order, however, goes on to say conclusively that such a conclusion is inaccurate. The FCC was simply advising the states that it could understand how its failure to adopt a specific rule could be a reason that the states might not have fully understood the FCC's previous decisions that ESP/ISP traffic is access traffic.

Q. MR. STARKEY AT PAGE 16 IMPLIES THAT A CLEC WOULD NOT HAVE ANY COST RECOVERY ASSOCIATED WITH SERVING AN ISP PROVIDER IF NOT FOR THE RECIPROCAL COMPENSATION IT RECEIVES FROM ILECS. DO YOU AGREE?

A. No. ISPs are carriers. As carriers, ISPs obtain access services from their serving local exchange carrier ("LEC"). The rates ISPs pay their serving LEC covers the full charge for the service provided to them. When an IXC or an ISP purchases access service, it is the IXC or the ISP, not the end user, who is the customer of the LEC for that service. The revenue the LEC receives from the ISP for access services is the only means to recover the costs of delivering the traffic to the ISP. Any additional compensation would only serve to augment the revenues the LEC receives from its ISP customer at the expense of the originating LEC's end user customers. In other words, paying ICG reciprocal compensation for ISP-bound traffic would result in BellSouth's end user customers subsidizing ICG's operations. Indeed, the FCC has recognized that the source of revenue for transporting ISP-bound traffic is the charge that the ISP pays for the access service. Further compensation to the ISP-serving LEC is inappropriate and is not in the public interest.

If ICG is not recovering its cost from the ISPs it serves, it is likely that ICG is charging below cost rates to those ISPs. Apparently ICG's complaint is that it will no longer be able to charge below cost rates when the subsidy it received from BellSouth in the form of reciprocal compensation goes away. Obviously, such complaint provides no basis for continuing the subsidy. However, it does clearly show why such subsidies should not be established, because once they are established, they become difficult to remove.

It is difficult to empathize with ICG's situation. BellSouth has been an access service provider for ESPs and ISPs for years. Though BellSouth has been unable to collect the otherwise applicable switched access charges due to the FCC's exemption, BellSouth's source of cost recovery has been the business exchange service rates it charges ISPs.

Q. DOES MR. STARKEY CONTRADICT HIS OWN CLAIM THAT ALECs DO NOT RECOVER COSTS FROM ISPs?

A. Yes. Interestingly, Mr. Starkey directly contradicts his contention that alternative local exchange carriers ("ALECs") do not recover their costs from ISPs. The contradiction is found in the following comment at page 14: "Indeed, ISPs and other technologically reliant customer groups are, in many cases, providing the revenue and growth potential that will fund further ALEC expansion into other more traditional residential and business markets." If ALECs are not recovering their cost to provide service to ISPs, what is the source of the revenue to fund expansion? The revenue comes from ALECs like ICG soaking ILECs for inappropriate reciprocal compensation payments on non-local ISP-bound access traffic. The Commission should see this situation for what it is. ICG is asking this Commission to require BellSouth to fund ICG's business operations and expansion plans. Such a scheme creates a market distortion that should not be allowed to occur. If ICG's recommendation is adopted, ICG wins, ISPs win and BellSouth's end user customers lose and, ultimately, competition in the local exchange suffers. Reciprocal compensation for ISP-bound traffic sets up a win-win-lose situation, versus an appropriate inter-carrier compensation sharing mechanism, which establishes a win-win-win situation.

Q. AT PAGE 20, MR. STARKEY TAKES A DIFFERENT TACK, SETTING UP A HYPOTHETICAL SITUATION WHERE BELLSOUTH IS THE ONLY LOCAL PROVIDER AND SERVES ALL ISP CUSTOMERS. HE CONTENDS THAT FOR BELLSOUTH TO MEET THE INCREASED NETWORK REQUIREMENTS CAUSED BY ISPS, BELLSOUTH WOULD "UNDOUBTEDLY BE ASKING STATE COMMISSIONS AND THE FCC FOR RATE INCREASES TO RECOVER THOSE ADDITIONAL INVESTMENT COSTS." DO YOU AGREE?

A. No. BellSouth is not arguing that routing traffic through an ISP should be done for free. In Mr. Starkey's hypothetical case, BellSouth would be receiving revenues from the ISP for the access service. When ICG serves that ISP, a portion of those revenues should be used to compensate BellSouth for the costs incurred.

Q. MR. STARKEY STATES THAT BELLSOUTH SHOULD BE

"ECONOMICALLY INDIFFERENT AS TO WHETHER IT ITSELF INCURS THE COST TO TERMINATE THE CALL ON ITS OWN NETWORK OR WHETHER IT INCURS THAT COST THROUGH A RECIPROCAL COMPENSATION RATE PAID TO ICG". PLEASE RESPOND. (PAGES 11, 19-20)

A. Mr. Starkey leaves out one very important point. When BellSouth uses its own network to route calls to a BellSouth served ISP, it charges the ISP business exchange rates. It is not able to recover its cost from the end user that places the call. When an ALEC serves the ISP, only the ALEC receives revenues for the access service provided to the ISP. Although BellSouth incurs cost for delivering BellSouth end user calls to the ALEC, under reciprocal compensation BellSouth is unable to recover that cost. This is why it is so important that access service revenues, such as for ISP-bound traffic, be shared among the carriers that jointly provide the service. As I stated earlier, ICG should reimburse the originating carrier (BellSouth) for its cost of transporting the ISP-bound call to ICG's point of interconnection. Instead, ICG wants BellSouth to incur even more of the costs without receiving any of the compensation. This is a perversion of the entire access charge system that this Commission should not allow to occur.

Q. MR. STARKEY STATES ON PAGE 17 THAT IT IS A SIMPLE ECONOMIC REALITY THAT BOTH ISP CALLS AND OTHER CALLS GENERATE EQUAL COSTS THAT MUST BE RECOVERED BY THE RECIPROCAL COMPENSATION RATE PAID FOR THEIR CARRIAGE.

DO YOU AGREE?

A. No, this statement is wrong. Costs for calls directed to ISPs are to be recovered from the ISP, rather than the originating end user. Costs for local calls are recovered from the originating end user. This fact means that reciprocal compensation is inappropriate for ISP-bound calls. In the case of a call sent from BellSouth to an ISP served by ICG, ICG is the only carrier collecting revenue for the ISP-bound calls. In the case of a local call directed from a BellSouth end user to an ICG end user, BellSouth would be the only carrier collecting revenue. Mr. Starkey ignores this important point and claims that the only carrier collecting revenue for ISP-bound calls should receive more revenue.

Q. CONTRARY TO MR. STARKEY'S CONTENTION, WHY IS IT POOR PUBLIC POLICY TO REQUIRE THE PAYMENT OF RECIPROCAL COMPENSATION FOR ISP TRAFFIC? (PAGES 10-11)

A. In paragraph 33 of its ISP Declaratory Ruling, the FCC stated its desire that any inter-carrier compensation plan advance the FCC's "goals of ensuring the broadest possible entry of efficient new competitors, eliminating incentives for inefficient entry and irrational pricing schemes, and providing to consumers as rapidly as possible the benefits of competition and emerging technologies." In fact, payment of reciprocal compensation on ISP-bound traffic would be contrary to the FCC's stated goals for the following reasons:

- Reduces incentive to serve residence and business end user customers;

- Further subsidize ISPs;
- Encourages uneconomic preferences for ALECs to serve ISPs due to the fact that ALECs can choose the customers they want to serve and ALECs could offer lower prices to ISPs without reducing the ALEC's net margin;
- Increases burden on end user customers;
- Establishes unreasonable discrimination among providers (IXCs versus ISPs);
- ILEC is not compensated for any costs incurred in transporting ISP-bound traffic; and
- Creates incentives to arbitrage the system, such as schemes designed solely to generate reciprocal compensation.

Q. AT PAGE 13, MR. STARKEY ATTEMPTS TO BUILD A CASE FOR WHY ISP PROVIDERS SEEK OUT ALECS. PLEASE COMMENT.

A. In attempting to show why ISPs seek out ALECs to provide their access service versus ILECs such as BellSouth, Mr. Starkey merely succeeds in demonstrating why ALECs should not be subsidized by the ILEC through reciprocal compensation. Mr. Starkey says that ALECs attract ISPs' business because ALECs provide the service, products, technology, capacity, flexibility and low prices that ISPs desire. If, in fact, all of this is true, ICG should be able to attract ISP business even more easily than they attract other business customers. Why then is it necessary for ICG to receive a subsidy from BellSouth when it can so easily attract ISPs due to ICG's inherent advantages? In fact, if these advantages are so significant, ICG should be able to charge a higher price than BellSouth charges and still win the ISPs' business.

Q. FURTHER, ON PAGE 22, MR. STARKEY STATES, "HOWEVER, IN THE CASE OF RECIPROCAL COMPENSATION, IT HAS COME TO BST'S ATTENTION THAT IT HAS BECOME, IN MANY CASES, A NET PAYOR OF TERMINATION CHARGES BECAUSE ALECS HAVE BEEN SUCCESSFUL IN ATTRACTING ISP PROVIDERS AND OTHER TECHNOLOGICALLY DEMANDING CUSTOMERS. HENCE, IF INDEED ITS RATES FOR TRAFFIC TRANSPORT AND TERMINATION ARE OVERSTATED, IT BECOMES THE PARTY MOST LIKELY TO BE HARMED." WHAT IS YOUR RESPONSE?

A. The above statement is wrong. Reciprocal compensation does not apply to access traffic. BellSouth is not arguing for a lower reciprocal compensation rate for this traffic. BellSouth is not objecting to paying reciprocal compensation simply because ISPs have a high volume of incoming traffic. BellSouth has not objected to paying reciprocal compensation for end users with these characteristics (e.g., pizza delivery service, etc.). BellSouth, however, is objecting to paying reciprocal compensation on access traffic because it is not applicable and is not in the public interest.

Q. MR. STARKEY CONTINUES ON PAGE 25 BY STATING, "THE APPROPRIATE WAY FOR BST TO MITIGATE ITS 'NET PAYOR' STATUS FOR RECIPROCAL COMPENSATION IS NOT TO SIMPLY REFUSE TO PAY FOR ITS CUSTOMERS' USE OF THE ICG NETWORK,

BUT INSTEAD TO FOLLOW THE DEMANDS OF THE COMPETITIVE MARKETPLACE JUST AS ICG AND THE LONG DISTANCE COMPANIES HAVE." WHAT IS YOUR RESPONSE?

A. ICG proposes to distort the marketplace by requiring reciprocal compensation where it is inappropriate. Instead of removing distortion, their proposal creates distortion in the form of subsidies to ISPs.

Q. WHAT IS YOUR RESPONSE TO MR. STARKEY'S ARGUMENT ON PAGES 26-27 THAT, BECAUSE OF BELLSOUTH'S SUCCESS IN ADDING SECOND LINES, BELLSOUTH SHOULD PAY RECIPROCAL COMPENSATION FOR ISP-BOUND TRAFFIC?

A. None of this discussion is relevant to the issue at hand. These second lines are no different from first lines when it comes to the question of who should pay for access traffic. This entire discussion is irrelevant to the issue of reciprocal compensation.

Q. HOW DO YOU RESPOND TO MR. STARKEY'S CONTENTION THAT BELLSOUTH.NET'S "UNLIMITED USAGE" RATES ARE FAR BELOW OTHER COMPETITIORS?

A. Mr. Starkey is clearly misinformed. It is obvious by the newspaper advertisements contained in Exhibit AJV-1 attached to this testimony, that BellSouth.net's rates are not out of line with other ISPs.

Q. REFERING TO DIAGRAM 3 IN HIS TESTIMONY, MR. STARKEY CONTENDS ICG PERFORMS TRANSPORT FUNCTIONS IN ADDITION TO SWITCHING FUNCTIONS. PLEASE RESPOND.

A. Diagram 3 clearly reflects that ICG's Lucent 5ESS switch is functioning only as an end office switch. Without specific information from ICG to the contrary, the "piece of equipment" in ICG's collocation cage appears to be nothing more than a Subscriber Loop Carrier which is part of loop technology and provides no "switching" functionality. 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. This is the same conclusion the Commission determined in its Metropolitan Fiber Systems of Florida, Inc. ("MFS") and Sprint arbitration order. The Commission determined that "MFS should not charge Sprint for transport because MFS does not actually perform this function." (Order No. PSC-96-1532-FOF-TP, issued December 16, 1996) The circumstances in the MFS/Sprint arbitration case can be logically extended to the issue raised by ICG in this arbitration proceeding. In fact, the Commission reaffirmed this conclusion when it issued its Order in the MCI/Sprint arbitration case in Docket No. 961230-TP (Order No. PSC-97-0294-FOF-TP, issued April 14, 1997) The evidence in the record does not support ICG's position that its switch provides the transport or tandem switching elements; and the Act does not contemplate that the compensation for transporting and terminating local traffic should be symmetrical when one party does not actually use the network facility for which it seeks compensation. Any decision by this Commission should be consistent with its previous rulings.

Q. AT PAGE 32, MR. STARKEY STATES THAT ICG SHOULD BE PAID THE SAME TANDEM TERMINATION RATE AS PAID TO BELLSOUTH EVEN THOUGH ICG ONLY USES ONE SWITCH. PLEASE COMMENT.

A. In the MFS/Sprint order referenced above, the Commission found, "[s]ince MFS has only one switch, there technically can be no transport." ICG only has one switch. As was the case with MFS, technically there can be no transport since ICG has only one switch and, therefore, ICG is not entitled to compensation for transport and tandem switching unless it actually performs each function.

Q. PLEASE RESPOND TO MR. STARKEY'S CONTENTION THAT VOLUME AND TERM COMMITMENTS BY ICG WOULD REDUCE THE TELRIC PRICES.

A. There is no rational basis for ICG's position. The basic flaw in Mr. Starkey's analysis is that he assumes that TELRIC prices were based on network costs as they <u>are</u> instead of what they are <u>projected to be.</u> For example, Mr. Starkey's claim that a volume commitment by ICG would increase the utilization of plant ignores the way the costs were developed. Plant utilization in the study represents this Commission's view of plant utilization in the future. Any impact of volume requested by ICG is already included in this utilization percentage.

Q. PLEASE RESPOND TO MR. STARKEY'S CONTENTION THAT LONG-TERM COMMITMENTS BY ICG WOULD MINIMIZE BELLSOUTH'S RISK OF STRANDED INVESTMENT.

A. Mr. Starkey is basing his conclusion on an incorrect understanding of the cost studies. He is correct that in the retail world the risk of stranded plant costs would be reduced by a term commitment. However, none of the costs that a term commitment would reduce are included in TELRIC. Therefore, the impact of any reduction, even if it exists, is irrelevant with respect to UNE prices. The other major point that Mr. Starkey misses is that retail prices typically exceed costs. Consequently, discounts due to term commitments simply reduce the level of contribution, not the level of costs. UNE prices do not include any contribution. And since there are no savings of TELRIC costs, there is no basis for offering term discounts.

Q. MR. HOLDRIDGE CONTENDS THAT BELLSOUTH SHOULD BE HELD TO ALL INTERVALS, RESPONSIBILITIES AND LEVELS OF SERVICE TO WHICH BELLSOUTH COMMITS IN THE AGREEMENT, INCLUDING ANY STANDARDS IT COMMITS TO THAT EXCEED ITS COMMITMENTS TO ITS OWN CUSTOMERS. PLEASE RESPOND.

A. The Telecommunications Act of 1996 ("the Act") cites three standards by which ILECs are to be held accountable. The first is that ILECs will provide access to services in "substantially the same time and manner" ALECs), that it provides to the ILEC's own retail customer, FCC 96-325, First Report and Order, Adopted August 1, 1996, § V.5, ¶ 518. The second standard requires that an ILEC will "provide an efficient competitor a meaningful opportunity to compete", FCC 96-325, Second Order for Reconsideration, Adopted December 13, 1996, § I., ¶ 9. Finally, ILECs are to provide interconnection services that are "equal in quality" to that which ILECs provide themselves, FCC 96-325, First Report and Order, Adopted August 1, 1996, § IV.H, ¶ 224. No where does the Act suggest, as Mr. Holdridge contends, that an ILEC should commit to any standards that exceed its commitments to its own customers.

Q. WHAT IS BELLSOUTH'S POSITION REGARDING ICG'S PROPOSED STANDARDS ATTACHED TO MR. HOLDRIDGE'S TESTIMONY AS EXHIBIT I?

A. BellSouth believes that the standards proposal submitted by ICG is both overly burdensome and complicated and that the escalating scale of enforcement penalties is excessive. The purpose of penalties, if agreed to by any ILEC, is to reimburse the ALEC for discriminatory treatment, not to create a financial windfall for the ALEC.

Q. ON PAGE 7, MS. NOTSUND REQUESTS THAT THIS COMMISSION NOT ARBITRATE THIS ISSUE BUT RATHER INITIATE A GENERIC

PROCEEDING TO CONSIDER APPROPRIATE PERFORMANCE MEASUREMENTS AND ENFORCEMENT MECHANISMS. PLEASE RESPOND.

A. BellSouth agrees with ICG that this issue should not be arbitrated. As this Commission recently concluded in the MediaOne/BellSouth Arbitration proceeding (Docket No. 990149-TP), it lacks the authority under state law to impose liquidated damages provisions in arbitrated agreements.

Regarding Ms. Notsund's request for the initiation of a generic proceeding to address this issue, the Commission's Order in Docket No. 960786-TL dated August 9, 1999, adopted the Commission Staff's Proposal for Independent Third Party Testing of BellSouth's Operations Support Systems. This Order concluded that the testing plan would be used to determine whether BellSouth had established adequate performance measures. Even though the Commission may choose to address performance measurements in a generic proceeding, the fact remains that this Commission lacks the statutory authority to impose liquidated damages or penalty requirements regardless of whether the issue is addressed in a generic proceeding or an arbitration proceeding.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

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BellSouth Telecommunications, Inc.
FPSC Docket No. 990691-TP
September 7, 1999
Exhibit AJV-1

The Atlanta Journal-Constitution
Wednesday, Sept. 1, 1999

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