BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In the Matter of:	)	
	)	
Petition by ICG TELECOM GROUP, INC. for Arbitration of an Interconnection Agreement with BELLSOUTH TELECOMMUNICATIONS, INC. Pursuant to Section 252(b) of the Telecommunications Act of 1996.	)	**Docket No. 990691-TP** **Filed: September 7, 1999**

REBUTTAL TESTIMONY

OF

MICHAEL STARKEY

ON BEHALF OF

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Q. PLEASE STATE YOUR NAME.

A. My name is Michael Starkey.

Q. ARE YOU THE SAME MICHAEL STARKEY WHO PREVIOUSLY FILED DIRECT TESTIMONY IN THIS PROCEEDING?

A. Yes, I am.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. My rebuttal testimony will respond to a number of issues raised by BellSouth Telecommunications, Inc. ("BellSouth") in its direct testimony. Specifically, I will address the following issues:

I. I will respond to arguments raised by Alphonso J. Varner describing BellSouth's duty to compensate ICG for ISP-bound traffic. Specifically, I will dispel BellSouth's argument that the Commission should simply not address this extremely important issue within the context of this arbitration. (Varner direct, 15).

II. I address Mr. Varner's arguments that ICG should, instead of receiving reciprocal compensation payments for carrying BellSouth's traffic, pay

BellSouth for carrying that traffic, though it is my understanding that this testimony is subject to a Motion to Strike. I conclude that Mr. Varner has so twisted the FCC's decisions and the rubric of common sense that this proposal can't be taken seriously.

III. I show that Mr. Varner is mistaken in his contention that ICG is not entitled to be compensated at the tandem interconnection rate.

Q. BEFORE YOU EXPLAIN YOUR POSITION ON EACH OF THE ISSUES ABOVE, CAN YOU FIRST SUMMARIZE YOUR RESPONSE TO BELLSOUTH'S POSITION THAT ICG SHOULD PAY BELLSOUTH FOR CARRYING BELLSOUTH'S CUSTOMERS' ISP-BOUND TRAFFIC?

A. As a preliminary matter, I note that concurrently with the filing of its rebuttal testimony, ICG Telecom, Inc. (ICG) has filed a Motion to Strike the portion of Mr. Varner's testimony addressing this argument as outside the scope of the issues to be arbitrated. My discussion of this matter is subject to the ruling on that motion.

BellSouth's proposition is outlandish. BellSouth's argument is an obvious attempt to shift the Commission's attention away from the proper cost recovery mechanisms required to ensure that carriers like ICG are compensated for carrying traffic generated by BellSouth's end users. At its heart, BellSouth's position makes obvious the fact that while it continues to sell enormous amounts of second access lines and generally does everything it can to reap windfall profits from its customers' internet usage, it is unwilling to pay the carriers that end up carrying the brunt of its end users' traffic - the ICGs of the marketplace (i.e. ALECs). Boiled down, BellSouth asks this Commission to believe that carriers like ICG should pay BellSouth for the privilege of carrying the traffic of BellSouth's customers! When the Commission applies sound economics, good public policy, and common sense to the subject of reciprocal compensation, it will reject the argument out of hand. Later in my testimony, I discuss at greater length why on every front BellSouth's argument in support of its "switched access sharing" proposal is grossly flawed and inappropriate.

Q. CAN YOU REITERATE ICG'S POSITION REGARDING THE ISSUE OF PROPER PAYMENT FOR TRAFFIC ORIGINATED ON THE NETWORK OF ONE INTERCONNECTING LEC AND PASSED TO AN ISP SERVED BY THE OTHER INTERCONNECTING LEC?

A. It is ICG's position that sound economic and public policy rationales require that another carrier be compensated for costs incurred when a first carrier uses the other carrier's network for purposes of completing the originating traffic of a customer of that first carrier. BellSouth's customers use ICG's network whenever they dial an ICG customer, regardless of whether ICG's customer is a residential customer or an ISP. BellSouth's use of ICG's network generates costs that ICG must recover, just as ICG's use of the BellSouth network generates costs for which ICG is willing to compensate BellSouth. As I fully explained in my direct testimony, the costs generated by a call bound for an ISP customer do not differ from those generated by calls bound for other types of ICG customers. Hence, BellSouth should be required to compensate ICG for its use of ICG's network regardless of whether the call is bound for an ISP or any other type of local customer. Because calls to an ISP are identical to other local calls, the reciprocal compensation rate applicable to local traffic is the best cost-based rate available for purposes of establishing reasonable compensation for ISP-bound traffic.

Q. CAN YOU BRIEFLY DESCRIBE BELLSOUTH'S POSITION ON THIS MATTER AS YOU UNDERSTAND IT?

A. I will attempt to, though BellSouth's position appears to be multi-layered. The following citations from the testimony of Mr. Varner give us some insight:

1. Mr. Varner says reciprocal compensation is not applicable to ISP-bound traffic. (Varner direct at 4).
2. BellSouth recommends this Commission not address this issue because it asserts compensation for ISP bound traffic is not subject to a §252 arbitration. (Varner direct at 15).
3. Mr. Varner argues that payment of reciprocal compensation for ISP-bound traffic is inconsistent with sound public policy and economic principles of cost causation.
4. According to Mr. Varner, ICG should compensate BellSouth for the use of ICG facilities by a BellSouth customer to place a call to an ICG served ISP. (Exhibit No. AJV-6).

Q. PLEASE RESPOND TO BELLSOUTH'S CONTENTION THAT RECIPROCAL

COMPENSATION RATES ARE NOT APPLICABLE TO ISP BOUND TRAFFIC.

A. Mr. Varner's statements fly in the face of pertinent FCC rulings. It is clear from reading the FCC's *Declaratory Ruling in C.C. Docket No. 96-98 and Notice of Proposed Rulemaking in CC Docket No. 96-98* (hereafter *Declaratory Ruling*), that while the FCC made a number of critical decisions impacting compensation for ISP bound traffic, the FCC left to the states an enormous responsibility to determine the proper compensation that carriers should receive for this traffic until a national rule is established. The following excerpt from paragraph 26 of the FCC's *Declaratory Ruling* best frames a state commission's responsibility in this regard:

> Although reciprocal compensation is mandated under Section 251(b)(5) only for the transport and termination of local traffic, <u>neither the statute</u> <u>nor our rules prohibit a state commission from concluding in an arbitration</u> that reciprocal compensation is appropriate in certain instances not addressed by section 251(b)(5), so long as there is no conflict with governing federal law. A state commission's decision to impose reciprocal compensation obligations in an arbitration proceeding - or a subsequent state commission decision that those obligations encompass ISP-bound traffic - does not conflict with any Commission rule regarding ISP-bound traffic. *By the same token, in the absence of governing federal law, state commissions also are*

> *free not to require the payment of reciprocal compensation for this traffic and to adopt another compensation mechanism*.

(Footnotes omitted, emphasis added).

Q. WHY DID YOU HIGHLIGHT THE LAST SENTENCE OF THE ABOVE QUOTATION?

A. I think there is an important point the FCC is making in the last sentence that it reiterates more directly in paragraph 29:

> We acknowledge that, no matter what the payment arrangement, LECs incur a cost when delivering traffic to an ISP that originates on another LEC's network.

It seems clear from these two paragraphs that while a state Commission is "...free not to require the payment of reciprocal compensation for this traffic...", if it chooses this path it must "adopt another compensation mechanism." It is clear that the FCC's pronouncements leave no room for BellSouth's position that the Commission should ignore the issue.

The FCC has obviously left the state commissions to determine an appropriate rate of compensation one LEC should pay another for ISP-bound traffic. It appears that it has given the state commissions an option to either adopt the reciprocal compensation rates that they have adopted as reasonable payment for all other types of local traffic, or, to construct another means of compensation specific to ISP-bound traffic. While ISP-bound traffic may no longer meet the legal definition of local traffic that the FCC has found appropriate for compensation under §251(b)(5) of the Act, the FCC has given a strong indication that such reciprocal compensation rates are a good place to start when determining reasonable rates for ISP-bound traffic.

Q. HAVE OTHER STATE COMMISSIONS MADE DECISIONS IN THIS RESPECT SINCE THE FCC ISSUED ITS DECLARATORY RULING?

A. Yes, as many as 16 states have issued decisions since the FCC's issuance of its *Declaratory Ruling* and have found that payments for ISP-bound traffic are appropriate. Among those that have interpreted the FCC's *Declaratory Ruling* for purposes of governing interconnection agreements within their intra-state jurisdictions is the Maryland Public Service Commission. In my opinion, the Maryland Commission provides the most reasoned reading to date of the FCC's intentions. In Order No. 75280 at pages 16 and 17, the Maryland Commission finds as follows:

> Thus, under the FCC's *ISP Order*, it is incumbent upon this Commission to determine an interim cost recovery methodology which may be used until the FCC completes its rulemaking on this issue and adopts a federal rule governing inter-carrier compensation arrangements.
>
> In fact, according to the FCC, "State commissions are free to require reciprocal compensation for ISP-bound calls, or not require reciprocal compensation and **adopt another compensation mechanism**, bearing in mind that ISP/ESPs are exempt from paying

access charges." This directive does not leave us the option of providing for no compensation for ISP-bound calls. State commissions must either require reciprocal compensation or develop another compensation mechanism. To fail to provide for any compensation would violate the 1996 Act, which states:

> A State commission shall not consider the terms and conditions for reciprocal compensation to be just and reasonable unless such terms and conditions provide for the mutual and reciprocal recovery by each carrier of costs associated with the transport and termination on each carrier's network facilities of calls that originate on the network facilities of the other carrier. (47 USC §252(d)(2)(A)).

We are very concerned that the adoption of BA-MD'S position will result in ALECs receiving no compensation for terminating ISP-bound traffic. Such an effect will be detrimental to our efforts to encourage competition in Maryland. No one disputes that local exchange carriers incur costs to terminate the traffic of other carriers over their network. In the absence of finding that reciprocal compensation applies, a class of calls (ISP traffic) will exist for which there is no compensation. The reciprocal compensation rates established by our arbitration order and

> contained in the approved Statement of Generally Available Terms ("SGAT") reflect the costs of this termination. Until the FCC establishes an appropriate inter-carrier compensation mechanism for ISP-bound traffic, we find that it is in the public interest to require BA-MD to pay our arbitrated reciprocal compensation rates contained in the SGAT as an **interim** compensation mechanism.

(Footnotes omitted; emphasis in original).

Q. MR. VARNER SUGGESTS IN HIS TESTIMONY THAT "COMPENSATION FOR ISP BOUND TRAFFIC IS NOT SUBJECT TO A SECTION 252 ARBITRATION." HOW DO YOU RESPOND?

A. One needs only to place Mr. Varner's testimony beside the FCC's pronouncement to see that he is wrong. In footnote 87, found in paragraph 26 of the FCC's *Declaratory Ruling*, the FCC states:

> As discussed, *supra*, in the absence of a federal rule, state commissions have the authority under section 252 of the Act to determine inter-carrier compensation for ISP-bound traffic.

Moreover, in its *Notice of Proposed Rulemaking* included as a portion of its *Declaratory Ruling*, the FCC tentatively concludes that even as a result of the federal policy it ultimately adopts in a federal rule, states should still play the role of setting inter-carrier compensation rates for ISP-bound traffic:

> 30. We tentatively conclude that, as a matter of federal policy, the inter-carrier compensation for this interstate

telecommunications traffic [ISP-bound traffic] should be governed prospectively by interconnection agreements negotiated and arbitrated under sections 251 and 252 of the Act. Resolution of failures to reach agreement on inter-carrier compensation for interstate ISP-bound traffic then would occur through arbitrations conducted by state commissions, which are appealable to federal district courts.

Q. PLEASE RESPOND TO BELLSOUTH'S ASSERTION THAT ICG SHOULD PAY BELLSOUTH FOR ORIGINATING THE CALL WHEN A CALL IS ULTIMATELY PASSED TO AN ISP?

A. BellSouth's claim is the absurd result of its erroneous argument that switched access charges should apply to traffic passed to ISP customers and that the switched access charge regime is the proper framework within which to view ISP traffic and its proper compensation.

Q. PLEASE EXPLAIN.

A. BellSouth's mistaken premise is that ISPs actually purchase switched access services from ILECs and ALECs when gaining access to the public switched network and that ISPs are thereby "carriers" that should be required to bear the burden of all costs generated from their customers (i.e. BellSouth and ICG customers) that subscribe to internet services. From this notion, BellSouth derives the argument that it should be compensated, by ICG, for originating those switched access calls, i.e., ICG should pay BellSouth when a

Bellsouth end user calls an ISP served by ICG.

Q. PLEASE DESCRIBE THE DIFFERENCES BETWEEN THE SWITCHED ACCESS AND RECIPROCAL COMPENSATION FRAMEWORKS.

A. The differences are major. Within the switched access charge regime, long distance carriers of toll traffic compensate local exchange carriers both to originate and terminate calls placed over their networks. On the other hand, reciprocal compensation obligates the local exchange carrier originating a local call to compensate the carrier to which the call is sent for delivery to the called number. The switched access framework is not the appropriate framework within which to view ISP-bound traffic.

Q. WHY NOT?

A. Very simply, because the switched access framework is intended for long-distance carriers and toll traffic, neither of which is present when ICG completes a call from a BellSouth customer to its ISP. The FCC has already found that switched access charges do not apply to such traffic. Hence, it is important that even if this Commission decides that the reciprocal compensation rate paid for all other local traffic is not applicable to ISP-bound traffic and that some other rate should apply, it must find that the reciprocal compensation *framework* (i.e., the originating carrier is responsible for costs associated with carrying the call) is the proper framework within which to establish reasonable rates for ISP-bound traffic. If any semblance of economic cost causality is to remain in the local exchange marketplace, BellSouth's proposal to charge ALECs for carrying

BellSouth's traffic must be rejected.

Q. BELLSOUTH CONTENDS THAT THE FCC HAS REGULATED DATA CARRIERS AS INTERSTATE CARRIERS FOR OVER 30 YEARS AND HAS HELD THAT WHILE THESE CARRIERS ARE BEING PROVIDED ACCESS SERVICES, THEY ARE ALLOWED TO COLLECT TRAFFIC AT THE PRICES FOR BUSINESS SERVICES. CAN YOU COMMENT?

A. ISP's are not "carriers" based on the FCC rules. In the FCC's *Computer II Inquiry* (77 FCC 2d 384, 387, May 2, 1980), the FCC found that ESPs (of which ISPs are a subset) are not common carriers within the meaning of Title II of the Communications Act (Title II includes all requirements associated with common carriage). This FCC decision was codified in FCC rule 64.702. Section 64.702 of the FCC rules provides:

> [T]he term enhanced service shall refer to services offered over common carrier transmission facilities used in interstate communications which employ computer processing applications that act on the format, content, code, protocol or similar aspects of the subscriber's transmitted information; provide the subscriber additional, different or restructured information, or involve subscriber interaction with stored information. <u>Enhanced services are not regulated under Title II of the Act</u>.

(Emphasis added). In addition, more recent FCC regulations clearly specify that ISPs are to be treated as end users, not as carriers. The FCC's *Declaratory*

Ruling from earlier this year at paragraph 15 specifically comments on the status of ISPs:

> The Commission's treatment of ESP [enhanced service providers, of which ISPs are a subset] traffic dates from 1983 when the Commission first adopted a different access regime for ESPs. <u>Since then, the Commission has maintained the ESP exemption, pursuant to which it treats ESPs as end users under the access charge regime and permits them to purchase their links to the PSTN through intrastate local business tariffs rather than through interstate access tariffs</u>. As such, the Commission discharged its interstate regulatory obligations through the applications of local business tariffs. Thus, although recognizing that it was interstate access, the Commission has treated ISP-bound traffic as though it were local.

(Emphasis added). This plain language clearly discredits the testimony of Mr. Varner with respect to his characterization of ISPs as carriers rather than end users. Indeed, Mr. Varner fails to include a single reference in his testimony supporting why he believes the FCC or any other authority has ever considered ISPs to be "carriers."

Q. IS THERE ADDITIONAL INFORMATION WHICH REFUTES MR. VARNER'S CONTENTION THAT ISPS ARE CARRIERS WHO PURCHASE SWITCHED ACCESS SERVICES FOR PURPOSES OF PROVIDING INTERSTATE TOLL SERVICES TO

THEIR CUSTOMERS?

A. Yes, there is. Regardless of how the FCC has regulated "data carriers," as Mr. Varner has used that term, ISPs, to the extent they compare to the "data carriers" to which Mr. Varner refers, are not purchasing or being provided interstate access services when they purchase connection to the public switched network.

The FCC has provided an exemption such that ISPs are not purchasing access and do not pay access charges. BellSouth concludes from this information that ISP-bound traffic is subject to the switched access regime, and the FCC has simply suspended the requirement that ISPs pay these charges. Indeed, BellSouth goes so far as to suggest that the rates ISPs pay local carriers like ICG are actually access charges assessed on a per month, instead of a per minute basis. As such, goes the argument, local carriers like ICG should be responsible for sharing those monthly access charges with BellSouth in compliance with industry standard access sharing arrangements. (Carriers often share switched and special access revenues through "meet point billing" arrangements, wherein the percentage ownership of facilities required to provision the service is determined and the access charge revenues are divided among the carriers based on this percentage. But, in meet point billing, the carrier receiving jointly provided service from the provider carrier <u>is</u> purchasing access.) This analysis is tortured and self-serving.

Q. PLEASE ELABORATE.

A. First, the revenue ICG, or any other local exchange carrier, receives from an ISP is not switched or special access revenue charged on a monthly, instead of on a per minute of use basis. The FCC has stated on numerous occasions that ISPs are to connect to the public switched network using intrastate, local business access line tariffs. That is what they pay, and that is what they <u>purchase</u>. (*Declaratory Ruling,* ¶20).

Second, the FCC in its *Declaratory Ruling* makes clear that the proper framework within which to view compensation for ISP-bound traffic is the reciprocal compensation framework wherein the carrier originating a call is responsible for the costs of carrying the call. Therefore, it seems clear from the FCC rulings that compensation for ISP-bound traffic is not subject to the switched access framework. (*Declaratory Ruling*, ¶30. The FCC states, "...We tentatively conclude that, as a matter of federal policy, the inter-carrier compensation for this interstate telecommunications traffic should be governed prospectively by interconnection agreements negotiated and arbitrated under Sections 251 and 252 of the Act." Switched access services are not part and parcel of sections 251 and 252, as held by the FCC in its *First Report and Order* in C.C. Docket No. 96-98 (paragraph 478), hence, it is clear that the FCC considers reciprocal compensation requirements, as exclusively included in sections 251 and 252 of the Act, as the model by which "this (i.e. ISP-bound traffic) interstate telecommunications traffic should be governed....").

Third, switched access charges are assessed on toll traffic generated by a local exchange carrier's customer and passed to an interexchange carrier. Fundamentally, the traffic at issue here, traffic to an ISP, is not toll traffic. The end user customer dialing the call is not assessed toll charges, the ISP to which the traffic is ultimately passed is not purchasing switched access service, and perhaps most importantly, none of the revenues generated by either the ILEC or the ALEC can be considered toll or access revenue. Hence, despite BellSouth's arguments, there is little if any relationship between traffic bound for an ISP customer and traffic bound for an IXC. All technical, economic and regulatory comparisons between local traffic, ISP traffic and long distance/access traffic indicate that local traffic and ISP traffic share far more similarities than do ISP traffic and toll/access traffic.

Q. CAN YOU EXPLAIN IN GREATER DETAIL WHY NONE OF THE REVENUES GENERATED BY EITHER THE ILEC OR THE ALEC IN A CALL TO AN ISP CAN BE CONSIDERED TOLL OR ACCESS REVENUE?

A. The FCC has specifically held that revenues and costs generated by traffic to an ISP must be considered to be intrastate, not interstate, traffic. In fact, both SBC and Bell Atlantic have attempted to reclassify costs and revenues from traffic to an ISP provider as interstate access traffic. The FCC rejected both filings. In the most recent attempt made by Bell Atlantic in this regard the FCC's Common Carrier Bureau had the following to say:

> As I recently explained to SBC Communications, the Commission requires carriers to classify the costs and revenues associated with

ISP-bound traffic as intrastate for jurisdictional separations and reporting purposes.

(July 29, 1999 letter from Lawrence E. Strickling, Chief, Common Carrier Bureau, to Don Evans, Vice President, Regulatory Affairs, Bell Atlantic). It is interesting to note that Mr. Strickling, the Chief of the FCC's Common Carrier Bureau and the author of the Commission's letter to Bell Atlantic, cited the FCC's *Declaratory Ruling* as the authority for requiring Bell Atlantic to classify its ISP-bound traffic as intrastate, not interstate, traffic.

Q. IF ALL TECHNICAL, ECONOMIC, AND REGULATORY COMPARISONS INDICATE THAT TRAFFIC BOUND FOR ISP PROVIDERS MORE CLOSELY RESEMBLES LOCAL TRAFFIC AS OPPOSED TO SWITCHED ACCESS TRAFFIC, ON WHAT BASIS DOES BELLSOUTH CONTEND THAT THIS TRAFFIC IS SWITCHED ACCESS TRAFFIC FOR WHICH RECIPROCAL COMPENSATION IS NOT REQUIRED?

A. BellSouth's entire rationale for refusing to pay reciprocal compensation for ISP-bound traffic is based upon the argument that ISP-bound traffic is interstate, not local, traffic.

Q. WHAT ECONOMIC CONDITIONS BEAR ON BELLSOUTH'S PREMISE?

A. Certainly, sound economic and public policies must recognize that when a carrier uses another carrier's network and costs result, the carrier upon whose network the call originates (the true cost causer) must be responsible for compensating the other carrier for the costs it incurs. Even BellSouth acknowledges this point. At page 47 of his testimony, Mr. Varner has no problem understanding why compensation must be paid whenever a local call originates on the BellSouth network and is directed to the ICG network. Only when the exact same local call is passed by a competitive local provider to an ISP end user does Mr. Varner begin to reassess the economic and public policy ramifications of such compensation. However, neither the economic nor technical characteristics of the call have changed. The only change that BellSouth can even argue is one of the regulatory definition of the traffic. Regardless, Mr. Varner and BellSouth assert that this change requires a substantial shift in the way in which costs for this traffic must be recovered. Now, instead of BellSouth paying ICG to carry this traffic originated by its local exchange customers, BellSouth says ICG should compensate BellSouth for carrying the exact same traffic. All of this results not from a change in calling patterns, a change in the equipment required to carry the traffic, or really, any physical or economic change at all. It results simply from the fact that Mr. Varner and BellSouth assert a regulatory paradigm shift has occurred. That is, the end user receiving the call (i.e., the ISP) should now be considered a "carrier" who is purchasing switched access services to provide an interstate toll service. Mr. Varner's testimony in this respect specifically highlights the fact that BellSouth's position has no basis in sound economic or public policy rationale and that BellSouth's position is nothing more than a contrived strawman.

Q. EVEN IF IT WERE APPROPRIATE TO DISCARD SOUND ECONOMIC AND PUBLIC POLICY RATIONALE, DO YOU AGREE WITH BELLSOUTH'S ARGUMENT?

A. No, I do not. Neither does BellSouth's affiliate.

Q. PLEASE EXPLAIN.

A. In a press release dated March 12, 1997, hailing a strategic agreement between BellSouth (via BellSouth.net) and IBM that would provide a comprehensive set of internet/intranet services to customers in the Southeast, John Robinson, president of BellSouth.net, Inc. said,

> By connecting to the Internet through the IBM Global Network, BellSouth customers will get an important benefit - the ability to access the Internet from more than 830 locations in 49 counties <u>with just a local call</u>.

(From the BellSouth Website. *Emphasis added*).

When marketing the internet to its own customers BellSouth makes every effort to make accessing the internet as easy and economical as possible for its own ISP customers. Indeed, in the excerpt above, BellSouth is not only admitting that a call made to its wholly owned ISP (Bellsouth.net) is a local call, it is marketing this fact as a major advantage of using BellSouth.net.

Q. MR. VARNER INCLUDES A NUMBER OF DIAGRAMS WITH HIS TESTIMONY DEPICTING A NUMBER OF CALL SCENARIOS. CAN YOU DESCRIBE THE POINT MR. VARNER IS ATTEMPTING TO MAKE AND PROVIDE

YOUR ANALYSIS OF HIS TESTIMONY?

A. Mr. Varner includes the following diagrams in his testimony: AJV-1, AJV-2, AJV-4, and AJV-5. If I understand Mr. Varner's point correctly, he is, through these diagrams, attempting to show the differences between calls made to an end user customer and calls made to what he refers to as an ISP/IXC. AJV-1 provides two diagrams (A&B) depicting the difference between a local call carried solely by BellSouth (Diagram A) and then a call carried by both BellSouth and an ALEC such as ICG (Diagram B).

Mr. Varner at pages 19-20 of his testimony describes Diagram A as follows:

> In this scenario, the ILEC receives a monthly fee from its end user to apply towards the cost of that local call. For that payment the ILEC provides the end user with transport and termination of local calls throughout the local calling area. End users typically do not pay for calls terminated to them. Importantly, in this case, the end user is the ILEC's customer, which means that the end user pays the ILEC revenue for the service.

Similarly, at page 20 Mr. Varner describes Diagram B as follows:

> By comparison, Diagram B illustrates a typical local call that is handled by two carriers – one end of the call is handled by an ILEC, and an ALEC handles the other end of the call. In this scenario, when the ILEC's end user makes a local call to the ALEC's end

> user, the ILEC's end user is paying the ILEC the same price for local exchange services as in Diagram A.... As previously noted, end users do not pay for local calls terminated to them, so the ALEC cannot be expected to charge its end user. While the ILEC is receiving the same revenues as shown in Diagram A, its costs are lower. Consequently, reciprocal compensation would be paid by the ILEC to compensate the ALEC for terminating that local call over its network. If the reciprocal compensation rate equals the ILEC's cost, the ILEC is indifferent to whether the ILEC or the ALEC completes the call.

Now, importantly, Mr. Varner attaches Exhibit AJV-5 that includes Diagram G. Diagram G is Mr. Varner's depiction of a call originated on the BellSouth network, transported to an ALEC for transfer to the ALEC's ISP customer. It is *important to note that Diagram G is in every way exactly the same as Diagrams* A and B, except that Mr. Varner has changed the name (and shape) of the end user receiving the call from an "end user" (the *shape of a telephone) to an* "ISP" (the shape of a STOP sign). Diagrams A, B and G use exactly the same network schematic. They incorporate all of the same facilities and functionality, indicating that the route of the call and all other handling characteristics are exactly the same regardless of whether the call is completed to a residential, business or ISP customer. Indeed, if you were to remove the verbiage from Mr. Varner's diagrams I think you would find that they are all derived from exactly the same underlying picture.

Q. WHY IS THIS IMPORTANT?

A. These diagrams directly contradict Mr. Varner. Mr. Varner attempted to demonstrate that there are major differences between calls made to ALEC business and residential end users (calls subject to reciprocal compensation) and calls made to ISPs (calls not subject to reciprocal compensation according to Mr. Varner). However, the fact that Mr. Varner is required to use exactly the same network diagram, incorporating exactly the same facilities and functions for purposes of depicting both types of calls, shows that there is no difference from a technical or economic perspective between these calls. The only difference that is apparent is made in Mr. Varner's verbiage wherein <u>he likens the ISP to an IXC</u> and therefore decides that calls to ISPs are, or should be, regulated differently.

Q. PLEASE CONTINUE.

A. Mr. Varner's diagrams actually make my point that BellSouth should be economically indifferent as to whether it pays reciprocal compensation for calls bound for an ISP or whether it completes those calls itself. With respect to Diagram B and its depiction of a local call terminated by ICG on BellSouth's behalf, Mr. Varner suggested the following:

> As previously noted, end users do not pay for local calls terminated to them, so the ALEC cannot be expected to charge its end user. While the ILEC is receiving the same revenues as shown in Diagram

> A, its costs are lower. Consequently, reciprocal compensation would be paid by the ILEC to compensate the ALEC for terminating that local call over its network. If the reciprocal compensation rate equals the ILEC's cost, the ILEC is indifferent to whether the ILEC or the ALEC completes the call.

(Varner direct at 20.) Even though there is no difference between a call depicted in Diagram B (about which Mr. Varner is speaking here) and Diagram G (a call to an ISP served by ICG), Mr. Varner's characterization as to the way that such calls should be treated in terms of reciprocal compensation differs by 180 degrees. Indeed, Mr. Varner argues that calls depicted by Diagram G are so different, that BellSouth should pay ICG for carrying the call in one scenario, but BellSouth should receive revenue from ICG in another. I emphasize that nothing in the network, the routing of the call, or the economics of the call (i.e. cost causation) actually changed between Diagram B (local calls for which BellSouth says reciprocal compensation is appropriate) and Diagram G (calls to ALEC ISPs for which BellSouth says it must receive payment for originating). At best, a purported regulatory distinction (i.e. the claim that the ISP is an IXC and not an end user – a distinction that I have refuted above) has been made between the two call types. Regardless, this regulatory distinction does not change the fundamental technical, economic, or public policy nature of the call and the manner by which costs should be recovered. In short, Mr. Varner's diagrams prove that there is no difference between calls made to an ICG residential or business customers and an ICG ISP. Likewise, the costs ICG incurs in carrying this traffic when generated by BellSouth local exchange customers do not differ and hence, the rates assessed by ICG on BellSouth for purposes of recovering the costs of this traffic should not differ.

Q. MR. VARNER AT PAGE 38 OF HIS TESTIMONY INCLUDES A TABLE INTENDED TO SHOW THAT THE LACK OF RECIPROCAL COMPENSATION FOR ISP BOUND TRAFFIC WOULD NOT DISTORT THE MARKETPLACE MAKING ISP CUSTOMERS LESS ATTRACTIVE THAN OTHER TYPES OF CUSTOMERS. DO YOU HAVE ANY COMMENTS REGARDING MR. VARNER'S TABLE?

A. Yes, I do. Mr. Varner at page 38 of his testimony includes the following chart:

	SERVING AN ISP AND RECEIVING RECIPROCAL COMPENSATION	***SERVING AN ISP WITHOUT RECEIVING RECIPROCAL COMPENSATION***
REVENUE FROM ISP FOR SERVICE	$600	$900
RECIPROCAL COMPENSATION REVENUE PAID	$300	$0
COST OF PROVIDING SERVICE TO ISP	($600)	($600)
NET MARGIN	$300	$300

In my direct testimony I argued that the absence of reciprocal compensation payments would distort the marketplace. Mr. Varner attempts to use the table above to show that reciprocal compensation paid for ISP bound traffic is the culprit responsible for distorting the competitive marketplace. However, properly viewed, Mr. Varner's table actually undermines his point and supports mine.

Q. WHY DO YOU BELIEVE THE ABOVE TABLE SHOWS THAT THE ABSENCE OF RECIPROCAL COMPENSATION PAYMENTS FOR ISP BOUND TRAFFIC WOULD DISTORT THE MARKETPLACE?

A. The table above makes a number of assumptions: (1) that it costs an ALEC $300 to carry traffic originated on the ILECs network to the ISP, (2) that it costs an ALEC $300 to provide an access line to an ISP, and (3) that the ALEC receives a $300 margin. Using these assumptions lets review two scenarios: (1) the Commission requires BellSouth to compensate ICG for carrying BellSouth's customers' traffic to ICG ISPs, and (2) the Commission decides to not require reciprocal compensation for such ISP bound traffic.

Under scenario (1), ICG would receive $600 from its ISP customer for an access line allowing the ISP to connect to the network. Likewise, it would receive $300 from BellSouth for carrying traffic originated from BellSouth customers to the ISP (a total of $900 in revenue). All told, the ALEC would incur $600 in costs ($300 for provisioning the access line and $300 for carrying BellSouth's traffic) and receive $900 in revenue while charging its ISP customer $600.

If the Commission were to decide not to require BellSouth to pay for ICG's carriage of its traffic, scenario number (2) would look much different.

Under scenario number 2, ICG would receive $0 from BellSouth for carrying its traffic. Regardless, it would still incur both its own $300 in cost for providing an access line to the ISP and it would continue to incur $300 in costs associated with carrying BellSouth's traffic. Hence, in order to maintain its $300 net margin, ICG would be required to charge $900 to its ISP instead of the $600 it charged earlier.

You need only compare scenario 2 above with a scenario wherein the ICG customer in question is a large business user instead of an ISP to appreciate the market distortion. The following table compares a scenario very much like Mr. Varner's, except that it compares a business customer and an ISP customer served by ICG and assumes reciprocal compensation payments for ISP bound traffic are not required:

	SERVING A BUSINESS CUSTOMER WITH LARGE INBOUND CALLING PATTERNS	***SERVING AN ISP***
REVENUE FROM ACCESS LINE SERVICE	$600	$900
RECIPROCAL COMPENSATION REVENUE PAID	$300	$0
COST OF PROVIDING SERVICE	($600)	($600)
NET MARGIN	$300	$300

Because BellSouth agrees that calls to ICG business users are subject to reciprocal compensation, it would reimburse ICG for the $300 in costs associated with carrying its traffic. Hence, serving a large business user would look very much like scenario number 1 above, in which ICG was required to charge only $600 for a network access line to serve the customer. In the marketplace under scenario 2, however, assuming the Commission allowed BellSouth to avoid reimbursing ICG for carrying its traffic, ICG could offer the exact same business line to a business customer at $600 that it must offer to an ISP at $900 to receive the same net margin. Or, looking at it another way, ICG could charge $600 to a business customer for an access line and receive $300 in net margin while offering the same access line to an ISP for $600 and receiving $0 in net margin. It is easy to see that under such a scenario, ISPs would become less attractive than any customer for which reciprocal compensation would be paid. Further, it is likely rates to ISPs would go up or carriers serving large numbers of ISPs would find themselves with a large population of unprofitable customers.

Q. HOW WOULD THIS SITUATION BE AFFECTED BY BELLSOUTH'S PROPOSAL THAT ICG PAY BELLSOUTH FOR ORIGINATING CALLS TO ITS ISP CUSTOMERS?

A. This aspect reveals the ludicrous nature of BellSouth's proposition. If ICG were required to pay BellSouth for carrying large amounts of BellSouth's traffic to its ISP customers, ISPs would not be merely unprofitable (i.e. generating $0 in net margin); they would be a financial burden. Under such a circumstance, ICG would be providing a great service to BellSouth's customers (i.e. carrying traffic bound for the internet) and incurring substantial costs to do so, while at the same time being required to pay BellSouth for the"opportunity." It simply doesn't make any sense.

Q. WOULD SUCH A SITUATION BENEFIT BELLSOUTH?

A. Undoubtedly. Such a circumstance would greatly benefit BellSouth at the expense of the ALECs and the marketplace. This is exactly the point I made in my direct testimony. When the Commission attempts to understand BellSouth's underlying rationale for its somewhat bizarre recommendation regarding reciprocal compensation, it should keep in mind the likely results of adopting such a recommendation. In a world where ALECs are required to pay BellSouth for carrying its customers' internet traffic, ISPs will undoubtedly pay higher rates for the same services offered to other businesses and they are likely to simply become far less attractive. As a result, fewer and fewer carriers would attempt to serve them. In general, life becomes hard as an ISP.

However, there is a class of ISPs in the market that would be somewhat insulated from this effect. Any ISP that had an affiliation with a local exchange carrier <u>and provided services primarily to customers served by the local exchange carrier</u>, would create a situation wherein the LEC rarely, if ever, was required "share" ISP revenues with another LEC. This lack of sharing would lower the costs of providing services to the ISP and would increase the profitability not only of the LEC serving the ISP, but also of the ISP itself. This type of ISP would be a powerful competitor against ISPs without such an "on-net" customer base. It could charge prices significantly below ISP competitors who were paying higher rates to ALECs while maintaining profitability. To illustrate, BellSouth.net would be such a competitor. Because BellSouth still maintains a near monopoly market position in the provision of services to residential and small business customers (the primary customer base responsible for dial-up internet access), BellSouth would, under BellSouth's compensation proposal, rarely if ever need to share ISP revenues with other local carriers. Rarely would an ALEC customer dial into BellSouth.net (at least compared to the number of BellSouth customers calling non-BellSouth ISPs) such that BellSouth would be required to share revenues with the local exchange carrier. In the vast majority of circumstances, BellSouth.net would serve BellSouth's local exchange customers so that BellSouth would receive all revenues.

Q. IS THERE ANY REQUIREMENT THAT BELLSOUTH.NET SERVE ALL CUSTOMERS THAT REQUEST ITS SERVICE?

A. I am not aware of any such requirement. However, it is not likely that BellSouth.net would turn customers away simply because they happen to obtain local service from another carrier. What is more likely, is that BellSouth would attempt to provide better ISP prices and services to its own local exchange customers as opposed to local exchange customers of other carriers. In that way, BellSouth.net would be an attractive alternative only to BellSouth local customers and customers of other local carriers would be unlikely to subscribe to BellSouth.net. Not only is this likely, it happens today. BellSouth currently offers promotions that tie its local exchange services and its internet services together at discounted rates. Indeed, it is my understanding that e.spire and the Competitive Telecommunications Association (Comptel) have recently filed a complaint with this Commission highlighting BellSouth's marketing efforts in this regard.

Q. IF BELLSOUTH OFFERED SERVICES TO ISPS OTHER THAN BELLSOUTH.NET, WOULDN'T THIS FORCE BELLSOUTH TO SHARE REVENUES WITH ALECS WHOSE CUSTOMERS DIALED THOSE NON-BELLSOUTH AFFILIATED ISPS?

A. Yes, if BellSouth were to serve a non-BellSouth affiliated ISP that had no incentive to serve primarily BellSouth customers, it is likely BellSouth, under its own proposal, would be required to share the revenues associated with serving the ISP with other ALECs. However, I already highlighted in my direct testimony the fact that BellSouth has lost an enormous number of ISP providers (or new providers have chosen never to obtain service from BellSouth). This results from the fact that ALECs provide those ISPs with more flexible service offerings and work directly with the ISPs to enhance their business. BellSouth, because of BellSouth.net, has no incentive to assist the ISPs in their business. Likewise, it has no incentive (indeed it has a disincentive) to provide those ISPs with quality services at reasonable rates. A primary example of BellSouth's unwillingness to accommodate the unique needs of ISPs is BellSouth's unwillingness to allow ISPs to collocate in its central offices. ISPs prefer to share the environmentally controlled offices used by local exchange carriers to aggregate traffic. These offices provide efficient means by which to connect to the public switched network. Many ALECs allow the ISPs, just like they allow other large users, to use their central office space to house equipment. To this point, however, BellSouth has refused to allow similar access to its central offices. In this way, and simply by not meeting the needs of ISPs, BellSouth could, and would have an incentive to, dissuade non-BellSouth affiliated ISPs from using its services and thereby requiring that BellSouth share revenues with other ALECs.

Q. CAN YOU SUMMARIZE BELLSOUTH'S POSITION AS TO WHETHER ICG SHOULD BE ALLOWED TO CHARGE BELLSOUTH A RECIPROCAL COMPENSATION RATE EQUAL TO THAT WHICH BELLSOUTH CHARGES, INCLUDING TANDEM SWITCHING AND TRANSPORT COSTS?

A. BellSouth believes that while it should be allowed to charge ICG a "reciprocal" compensation rate including the recovery of end office, tandem and transport costs, ICG should be allowed to charge BellSouth a rate only recovering end office costs. At page 45 of his testimony Mr. Varner states as follows:

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. BellSouth will pay the tandem interconnection rate only if ICG's switch is identified in the local exchange routing guide ("LERG") as a tandem..

Likewise, at page 44 of his testimony Mr. Varner states:

> ICG is seeking to be compensated for the cost of equipment it does not own and for functionality it does not provide.

Q. CAN YOU REITERATE ICG'S POSITION ON THIS ISSUE?

A. BellSouth should pay ICG a reciprocal compensation rate based upon the recovery of tandem, transport and end office switching costs. The FCC at paragraph 1090 of its *First Report and Order in C.C. Docket No. 96-98* (hereafter referred to as the FCC's Local Competition Order) provides the following guidance with respect to the appropriate rate of reciprocal compensation ICG should receive from BellSouth:

> 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. <u>*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*</u> 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*.

(Emphasis added).

The actual FCC rule that discusses this issue is even more direct:

> **51.711 Symmetrical reciprocal compensation**
>
> (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. (Rule 41.711 also includes subparts (a)(1) and (a)(2) that have been excluded from the above excerpt.)

Accordingly, 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. 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 <u>and</u> provides comparable functionality. That is to say, ICG's switching platform transfers traffic among discrete network nodes that exist in the ICG network for purposes of servicing groups of its customers in exactly the same fashion that BellSouth's tandem switch distributes traffic - a similarity that the FCC does not require to justify the application of the tandem rate. In 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.

Q. WOULD THERE BE A SEPARATE BASIS FOR APPLYING THE TANDEM RATE?

A. Yes. As ICG deploys its network in Florida, when it provides comparable functionality, that will provide a separate, independent basis for the tandem rate.

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the ICG Telecom Group, Inc.'s Rebuttal Testimony of Michael Starkey have been furnished by (*)hand-delivery and by U.S. mail this 7th day of September, 1999 to:

* Lee Fordham
Florida Public Service Commission
Division of Legal Services
2540 Shumard Oak Boulevard
Gunter Building, Room 370
Tallahassee, FL 32399

Nancy B. White
Michael P. Goggin
c/o Nancy Sims
BellSouth Telecommunications, Inc.
150 South Monroe Street, Suite 400
Tallahassee, FL 32301

Joseph A. McGlothlin

Joseph A. McGlothlin
Vicki Gordon Kaufman
McWhirter, Reeves, McGlothlin,
Davidson, Decker, Kaufman,
Arnold & Steen, P.A.
117 South Gadsden Street
Tallahassee, Florida 32301
Telephone: (850) 222-2525
Telecopy: (850) 222-5606

Attorneys for ICG Telecom Group, Inc.