STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

In the matter of XO Illinois, Inc.	)	
Petition for Arbitration pursuant to	)	
Section 252 (b) of the Telecommunications	)	Docket No. 01- 0466
Act of 1996 to establish an Interconnection	)	
Agreement with Illinois Bell Telephone	)	
Company d/b/a Ameritech Illinois	)	
	)	

AMERITECH ILLINOIS=
INITIAL POST-HEARING BRIEF

Dennis G. Friedman
Mayer, Brown & Platt
190 S. LaSalle Street
Chicago, Illinois 60603
(312) 701-7319

Nancy J. Hertel
Ameritech Illinois
225 W. Randolph St.
Chicago, Illinois 60606
(312) 727-4517

TABLE OF CONTENTS

Page

Illinois Bell Telephone Company ("Ameritech Illinois") respectfully submits its initial post-hearing brief in this matter.

INTRODUCTION

The principal issue in this arbitration is whether the Commission should adopt the bifurcated reciprocal compensation rates that Ameritech Illinois proposes for the interconnection agreement between XO Illinois, Inc. ("XO") and Ameritech Illinois. As we demonstrate in Section I below, the Commission should adopt those rates. It is uncontested that bifurcated reciprocal compensation rates – *i.e.*, rates that accurately reflect call duration – are more faithful to the cost-based pricing requirement of the Telecommunications Act of 1996 ("1996 Act" or "Act") than are Ameritech Illinois' current reciprocal compensation rates. Staff, while not disputing that proposition, speculates that bifurcation may not be appropriate in this particular instance because Ameritech Illinois' cost studies, notwithstanding that they were approved by this Commission, *may* have misidentified setup costs as duration costs, or vice versa. There is no evidence that Staff's speculation is correct, however. Quite the contrary, the weight of the evidence indicates it is not. Staff also raises the possibility that even if bifurcation would yield more truly cost-based rates, the cost of implementing bifurcation might outweigh the benefit that bifurcation would yield. Again, the record shows that is not the case.

The Commission should therefore accept Ameritech Illinois' proposed bifurcated rates as they appear in the Appendix Reciprocal Compensation that Ameritech Illinois is proposing for the parties' interconnection agreement. The remainder of the Appendix Reciprocal Compensation should be included in the parties' agreement as well. There is solid support for it, and neither XO nor Staff has offered any cogent objection to any of its provisions.

XO contends that the Commission cannot consider Ameritech Illinois' Appendix Reciprocal Compensation in this proceeding, because XO claims it is entitled to adopt the intercarrier compensation provisions in the Focal/Ameritech Illinois interconnection agreement ("Focal Agreement") – except, XO concedes, those provisions that govern intercarrier compensation on ISP-bound traffic. As we demonstrate in Section II, XO is mistaken. Section 252(b) of the 1996 Act gives Ameritech Illinois the right to have its proposals considered in this arbitration. Furthermore, what XO is proposing would leave the parties with an interconnection agreement that does not address in any way intercarrier compensation on ISP-bound traffic. As recent experience has taught, the Commission should take pains to ensure that its arbitration decision explicitly tells the parties exactly what their interconnection agreement must say; otherwise, the parties and the Commission are apt to find themselves embroiled in lengthy disputes about how to implement the arbitration decision. Given the record in this proceeding, the only way the Commission can be certain the parties will come out of the arbitration with a complete interconnection agreement is by directing the parties to include Ameritech Illinois' Appendix Reciprocal Compensation in their interconnection agreement.

In Section III below, we demonstrate that the Commission should reject Staff's proposal to require Ameritech Illinois to declare immediately whether it wishes to avail itself of the rates the FCC made available for ISP-bound traffic in its *ISP Compensation Remand Order*.[1] Staff's proposal is inconsistent with the *ISP Compensation Remand Order* itself and, in any event, cannot properly be entertained in this proceeding.

Finally, Ameritech Illinois responds in the attached Appendix to the questions posed by the Administrative Law Judge at hearing.

[1] *Order on Remand and Report and Order (FCC 01-131), In the Matter of the Local Competition Provisions in the Telecommunications Act of 1996; Intercarrier Compensation for ISP-bound Traffic,* CC Dockets No. 96-98 and 99-68 (rel. April 27, 2001).

ARGUMENT

I. THE COMMISSION SHOULD ADOPT AMERITECH ILLINOIS' PROPOSED BIFURCATED RATES.

The following propositions are undisputed and indisputable:

- The 1996 Act requires that reciprocal compensation rates be cost-based.
- The more precisely reciprocal compensation rates reflect costs, the better – so long as the costs of achieving the greater precision do not outweigh the benefits.
- Ameritech Illinois' proposed bifurcated rates reflect costs more precisely than the reciprocal compensation rates that are currently in place, at least in theory.

We say "at least in theory" because Staff, while acknowledging that bifurcation would yield more precisely cost-based rates if the cost inputs are accurate, suggests that the cost inputs for Ameritech Illinois' current reciprocal compensation rates (and consequently for the proposed bifurcated rates) MAY be inaccurate in such a way as to yield a different conclusion. As we show below, however, there is no credible evidence that that is the case. In addition, as we also show, there is no credible evidence that the costs of implementing bifurcated rates would outweigh the benefits. Accordingly, the Commission should adopt Ameritech Illinois' proposal.

A. Reciprocal Compensation Rates Must Be Cost-Based.

Section 252(d)(2)(A) of the 1996 Act provides in pertinent part (with emphasis added):

> [A] State commission shall not consider the terms and conditions for reciprocal compensation to be just and reasonable unless—
>
> (i) 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; and
>
> (ii) such terms and conditions determine such costs on the basis of a reasonable approximation of *the additional costs of terminating such calls.*

The FCC's implementing Rule, 47 C.F.R. § 709(a), confirms that reciprocal compensation rates are to be structured consistently with the manner in which costs are incurred:

> In state proceedings, a state commission shall establish rates for the transport and termination of telecommunications traffic that that are structured consistently with the manner that carriers incur those costs, and consistently with the principles in §§ 51.507 and 51.509 of this part.

That rule is grounded in a sound policy analysis by the FCC, which recognized that reciprocal compensation rates that depart from cost causation principles would create incentives for narrow and economically inefficient competitive entry, rather than the broad-based, economically efficient competitive environment envisioned by the 1996 Act. That is exactly what has happened under the current non-cost-based rate structure – competitive local service providers have focused almost exclusively on the few niche customer groups and services that provide them with the opportunity to receive excessive compensation through arbitrage of an uneconomic rate structure. (*See* Ameritech Ex. 1 (Panfil Direct) at 10-11.)

Indeed, it is fundamental that the reciprocal compensation rates that a carrier charges should accurately reflect the costs that carrier incurs in providing the transport and termination for which it is being compensated. Thus, Staff witness Zolnierek agreed at hearing that "having rates that are more reflective of costs is a good thing and should be done to the extent that the costs of implementing such a change don't outweigh the benefit." (Tr. 181.) The inquiry thus becomes whether Ameritech Illinois' proposed bifurcated rates are more reflective of costs than its current reciprocal compensation rates, and, since the answer to that question is "yes," whether the benefit of implementing bifurcated rates would outweigh the cost.

B. Ameritech Illinois' Proposed Bifurcated Rates More Accurately Reflect Costs Than Do Ameritech Illinois' Current Reciprocal Compensation Rates.

Ameritech Illinois' reciprocal compensation rates have four components: end office switching; tandem switching; tandem transport termination; and tandem transport facility.[2] The

[2] When a CLEC delivers traffic directly to Ameritech Illinois' end office for termination to the Ameritech Illinois customer, the reciprocal compensation that Ameritech Illinois charges includes only the charge for end

bifurcated rate proposal affects the first two of these components – end office switching and tandem switching. (*See* section 5.7 in Appendix Reciprocal Compensation in the interconnection agreement submitted with Ameritech Illinois' response to XO's arbitration petition; *see also* Ameritech Ex. 1 at 14.)

Schedule 1 to the Direct Testimony of Eric Panfil (Ameritech Ex. 1) shows Ameritech Illinois' current, Commission-approved end office switching and tandem switching rates ($.003746 per minute and $.001072 per minute, respectively), and also shows the calculation by which those rates were derived from the inputs set forth on the Schedule. Schedule 1 also shows Ameritech Illinois' proposed bifurcated rates for end office switching ($.009512 for setup, plus $.000967 per minute) and tandem switching ($.000496 for setup, plus $.000927 per minute), *based on the same inputs*.

There is no question that the bifurcated rates more accurately reflect costs than the current rates, *assuming the inputs are not so inaccurate as to compel a different conclusion*. Indeed, Dr. Zolnierek acknowledges that fact. (Tr. 183-184.) Although the point appears to be undisputed, we go on in this subsection to explain why it is so.

Ameritech Illinois' current per-minute reciprocal compensation rate elements are a composite of two separate cost streams: setup costs and duration costs. (Ameritech Ex. 1 at 8.) It is universally understood and accepted in the telecommunications industry that the cost of switching and transporting a call includes both costs that are incurred only once per call (setup costs) and costs that continue to accrue for the duration of the call (duration costs). (*Id.*) In the design of Ameritech Illinois' current reciprocal compensation rates, those two types of costs

office switching. When the CLEC delivers traffic to Ameritech Illinois at the Ameritech Illinois tandem switch, the reciprocal compensation rate comprises all four components.

were melded into a single per-minute cost, because it was assumed that hold times were relatively stable, and would not vary significantly from carrier to carrier. (*Id.*)[3]

However, developments over the last few years have rendered that assumption obsolete. Hold times for calls subject to reciprocal compensation are not stable at all now, and average overall hold times now vary greatly from provider to provider. (*Id.* at 9.) The nature of the traffic on the networks of local service providers has changed dramatically, driven primarily by the explosion in Internet access traffic. (*Id.*) Internet access calls originating on Ameritech Illinois' network have an average duration of about 26 minutes per call, and the average duration of such calls has been increasing over time. (*Id.*) Applying the current per-minute rate to a 26-minute call results in recovery of the proper amount of duration cost, but recovers over six times the setup cost. (*Id.*) And while the explosion in Internet access traffic has been the primary driver of the wide disparity in average hold times from one provider to another, other sorts of traffic contribute to the disparity as well. (*Id.* at 9-10.)

Thus, with all or virtually all service providers in Illinois charging reciprocal compensation rates that mirror Ameritech Illinois' rates[4], the current rate structure causes many service providers to be systematically over-compensated, and others to be under-compensated,[5] for the transport and termination of telecommunications traffic on their networks. (*Id.* at 7.)

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3 For example, when Ameritech Illinois' cost studies for reciprocal compensation end office switching rates were originally developed in 1996, the setup and duration costs were melded based on an assumed duration of about 3.5 minutes per call. (Ameritech Ex. 1 at 8.) The result (using the slightly revised "compliance" version of those costs filed in April 1998) was a switching rate of $.003746, which included the setup cost ($.009512 per message) spread over each of the 3.5 minutes (as an addition to a duration cost of $.000967 per minute). (*Id*.) The tandem switching rate element also has components that are setup-related and others that are duration-related. (*Id*.)

4 Under 51 C.F.R. § 51.711, a competing LEC may charge either the incumbent LEC's reciprocal compensation rates ("symmetrical" or "mirrored" rates) or such higher rates as the competing LEC may prove it is entitled to charge by means of a forward-looking cost study. In practice, all or virtually all competing LECs in Illinois charge the mirrored rates.

5 The current rate structure under-compensates carriers that terminate calls that are, on average, shorter than the historical average, such as CMRS providers.

Even as applied to Ameritech Illinois itself, rates that result from the averaging of setup and duration cost components based on an assumed duration per call cannot reasonably be judged to be consistent with FCC Rule 709(a). (*Id.* at 12.)

The solution to this problem is to apply a two-part (bifurcated) rate structure consisting of separate per-call and per-minute rates. This bifurcated structure would be implemented for each rate element for which separate setup and duration costs were identified in the cost studies underlying Ameritech Illinois' current reciprocal compensation rates, namely, the end office switching element and the tandem switching element. (*Id.*)

The process of separating costs into setup and duration components is straightforward. (*Id.* at 14.) It simply requires "un-doing" the averaging step that was performed at the end of the TELRIC analysis. (*Id.*) The original cost studies clearly identify which costs are setup (per-call) costs and which costs are duration (per-minute) costs. (*Id.*) As a final "averaging" step in those studies, the setup costs were divided by the assumed average hold time per call (slightly under 3.5 minutes in the case of the cost studies at issue here) and were added to the true duration costs in order to produce a per-minute cost/rate that would recover both setup and duration costs, provided that the assumption regarding the average hold time per call turned out to be accurate. (*Id.*) In order to create bifurcated rates, one simply uses the setup and duration cost components identified in the original study, without melding them. (*Id.*)

The sources and origins of Ameritech Illinois' current reciprocal compensation rates are described in Ameritech Ex. 1 at 12-13. Those rates, developed based on an "average per-minute" rate structure, are (*id.* at 13):

End Office Switching	$0.003746 per MOU
Tandem Switching	$0.001072 per MOU
Tandem Transport Termination	$0.000201 per MOU
Tandem Transport Facility Mileage	$0.000013 per MOU per Mile

Those rates reflect the melding of separate setup and duration components for two elements: end office switching and tandem switching. (*Id.*) Based on the same inputs, the bifurcated rate structure proposed by Ameritech Illinois would result in the following rates (*id.* at 13-14):

	Rate per Call	Rate per MOU
End Office Switching	$0.009512	$0.000967
Tandem Switching	$0.000496	$0.000927
Tandem Transport Termination	(none)	$0.000201
Tandem Transport Facility Mileage	(none)	$0.000013 per Mile

The Commission should require the parties to pay each other reciprocal compensation at those bifurcated rates, as provided in Ameritech Illinois' Appendix Reciprocal Compensation. Such a requirement would be an important and beneficial step in the direction of truly cost-based rates.

C. Last Year, Staff Agreed With Ameritech Illinois' Analysis.

As noted above, Staff and XO do not contest the proposition that the bifurcated rates Ameritech Illinois is proposing would more accurately reflect costs than do current reciprocal compensation rates, so long as the inputs are not so inaccurate as to compel a different conclusion. Just last year, Staff went a significant step further. In Docket No. 00-0027, Staff testified:

> Although the reciprocal compensation rate . . . is a per minute charge, it is actually comprised of a set-up cost and a duration cost. The set-up costs are those costs that are incurred on a per call basis and are not sensitive to minutes of use. Duration costs, on the other hand, are those costs that depend on the length of the call. Since the set-up costs are one-time costs and are generally greater than the duration costs, Ameritech has melded the set-up costs into a per-minute rate based on the average duration of a local call (3.3 minutes) and

> combined that cost with the duration costs to arrive at a composite per-minute reciprocal compensation rate. Therefore, *when Ameritech pays reciprocal compensation rates on ISP traffic, which have an average duration of 26 minutes, it is paying the set-up cost more than seven times over*. Thus, Ameritech is overcompensating . . . for the cost of an ISP call when using the currently structured reciprocal compensation rate.

(Verified Statement of Patrick L. Phipps (Staff Ex. 2.0) (Feb. 28, 2000) Docket No. 00-0027, at 15-16) (emphasis added).

In its post-hearing brief in that docket, Staff sought "the implementation of all of [Mr. Phipps'] recommendations," including "his recommendation that Focal receive a reciprocal compensation rate that has been adjusted to reflect [] longer holding times" (Initial Brief of the Staff of the Illinois Commerce Commission (March 27, 2000) Docket No. 00-0027, at 5-6) – exactly what Ameritech Illinois is proposing here. In doing so, Staff relied on Mr. Phipps' testimony concerning call duration. (*Id.* at 12).[6]

The italicized language in the Staff testimony quoted above shows that Staff accepted the accuracy of Ameritech Illinois' cost inputs; that is the only way Staff could have come to the conclusion that payment of reciprocal compensation on a 26-minute call includes "the set-up cost more than seven times over." In its response to XO's arbitration petition in this docket, Ameritech Illinois pointed out that Staff had unreservedly endorsed in 00-0027 the analysis on which Ameritech relies here. Staff countered that it had not really changed its position, but stated, in an attempt to explain what certainly appeared to be a change in position: "Ameritech cites evidence of a solution, endorsed by Staff, to address issues associated with reciprocal compensation rates for ISP-bound traffic. As I have repeatedly emphasized, the FCC's Order

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[6] In its final order in 00-0027, the Commission agreed that the evidence suggested "dramatic shifts in the utilization of the local exchange network, associated with the explosion of Internet traffic, and the resultant effects these changes are having upon the issue of reciprocal compensation. Due to these changes, the issue of reciprocal compensation demands further scrutiny by this Commission in order to ensure that just and reasonable rates are in place in Illinois." Arbitration Decision, Docket No. 00-0027 (May 8, 2000), at 12.

preempts the Commission's authority to address these issues." (Staff Ex. 1.0 at 25.) That simply will not do. Bifurcating Ameritech Illinois current reciprocal compensation rates is either a good idea or a bad idea, and in Docket 00-0027, Staff thought it was a good idea. Staff may believe the Commission no longer has authority to implement the good idea (as we show below, Staff is mistaken about that), but that belief cannot make a good idea in 2000 a bad idea in 2001.

D. There Has Been No Showing That Ameritech Illinois' Cost Inputs Are Inaccurate.

Staff acknowledges that if the inputs for Ameritech Illinois' reciprocal compensation rates are sufficiently accurate, bifurcation is a step in the right direction – *i.e.*, in the direction of more precisely cost-based rates. (*See* Tr. 183-84.) Staff suggests, however, that the inputs may be inaccurate to the point that bifurcation would not result in more precisely cost-based rates. Note again that these doubts cannot be squared with Staff's endorsement of bifurcated rates in Docket 00-0027. In 00-0027, Staff stated, "when Ameritech pays reciprocal compensation rates on ISP traffic, which have an average duration of 26 minutes, it is paying the set-up cost more than seven times over." That statement necessarily accepts the accuracy of the inputs.

We demonstrate why Staff's criticisms of the inputs are ill-founded. First, however, we emphasize that Staff does not contend that the inputs are in fact inaccurate to the point that bifurcation would not result in more precisely cost-based rates – only that they might be. As Dr. Zolnierek testified at hearing, "[W]hile I'm not ruling out that they could be the correct numbers that you're proposing, I've also said that . . . there is reason to believe that they're not appropriate." (Tr. 186.)

Dr. Zolnierek's uncertainty about the appropriateness of Ameritech Illinois' numbers is entirely speculative and, as the testimony of Ameritech Illinois witness Panfil showed, rests on a very shaky footing. Dr. Zolnierek suggests that when Ameritech Illinois' current reciprocal compensation rates were developed, the concern was the total bottom-line per-minute-of-use costs, not the separation of those costs into setup costs vs. duration costs, and thus that little scrutiny may have been given to that separation. (Staff Ex. 1.0 at 31.) The implication is that the allocation of costs as between setup and duration may have been inaccurate, so that a calculation that relies on that allocation (*i.e.*, the proposed bifurcation) may be inaccurate.

This suggestion is fundamentally flawed, because it rests on the mistaken assumption that in performing (or challenging) a cost study, one looks at costs in a vacuum, without regard to what the costs are for. The point is perhaps best made by means of an example: As Panfil Schedule 1 shows, one component of Ameritech Illinois' end office switching rate is what the underlying cost study identified as a setup cost of $0.006617 per message. That $.006617 is itself comprised of several elements, including, for example, $0.000075 for "Measurement (Recording)." Dr. Zolnierek's theory is that that $.000075 may have legitimately been included in the end office switching cost, but perhaps was misidentified as a setup cost, when in fact it should have been identified as a duration cost. His thought, again, is that that could have happened because those with an interest in challenging Ameritech Illinois' cost study would have been indifferent as to whether the $.000075 was identified as a setup cost or a duration cost.

As Ameritech Illinois witness Panfil testified (Tr. 144-149), it is unlikely that such a thing happened in the real world. In order to understand (and potentially challenge the accuracy of) that cost, one must look to the details of how that cost was developed and the functions that are included in that cost. So, for example, one cannot assess the appropriateness of measurement costs without understanding that if it is a function that is invoked only at the beginning and the end of a call, if would not vary based on the duration of the call but would be identical for each call regardless of duration. It is the functionality provided that drives the cost, and one cannot understand the functionality without also understanding the manner in which the costs relate to the parameters of demand, such as frequency (*i.e.* number of calls), duration, and distance. The establishment of reciprocal compensation rates was not, therefore, a zero sum game in which Ameritech Illinois could have arbitrarily (or intentionally) put a lump of cost in the setup pile when it belonged in the duration pile with no one noticing.

There is no evidence that Dr. Zolnierek, has any experience with cost studies. (*See* Staff Ex. 1.0 at 1-2.) Clearly, his views concerning what may have happened in the investigation of Ameritech Illinois' current reciprocal compensation costs are not based on any first-hand knowledge. Mr. Panfil, in contrast, has extensive experience with Ameritech Illinois' cost studies. He has "been responsible on a number of occasions for the assembly of [cost] components, if you will, the understanding of the components and the assembly of those into full service cost studies." (Tr. 97-98.) When Mr. Panfil, a conspicuously credible witness, testifies it is highly unlikely that components of Ameritech Illinois' reciprocal compensation costs were misallocated as between setup costs and duration costs, the Commission should give that testimony great weight – certainly enough weight to overcome Dr. Zolnierek's speculation that such a thing *might* have happened.

In an attempt to corroborate his speculation, Dr. Zolnierek compared Ameritech Illinois' most recent but not yet approved cost study with Ameritech Illinois' most recent approved cost study, and noted that end office setup costs had significantly decreased while end office duration costs had increased. (Staff Ex. 1.0 at 31-32.) The implication is that this is suggestive of a misallocation as between setup costs and duration costs. But it is not at all suggestive of such a thing. The two cost studies Dr. Zolnierek looked at were performed approximately four years apart, which is ample time for some of the costs, particularly those that are specific to Ameritech

Illinois' rapidly evolving wholesale operations, to have changed. Also, the methodology for performing the cost studies for the switching and transport cost elements was entirely changed between the two studies, and one of the main factors driving the changes was criticism leveled against the previous cost studies by Staff and the Commission in earlier proceedings. (Ameritech Illinois Ex. 3 (Panfil Additional Testimony) at 4.)

Dr. Zolnierek also notes that the bifurcated rates approved in Michigan and Texas do not jibe with the bifurcated rates Ameritech Illinois is proposing here. (Staff Ex. 1.0 at 33-34.) The differences that Dr. Zolnierek observes, however, do not support the hypothesis that Ameritech Illinois' cost studies misidentified setup costs or duration costs. The Michigan rates were not even based on Ameritech Michigan's cost studies, but instead were based on competing studies submitted by another party. And the Texas rates were based on relatively old cost studies that used cost methods entirely different from those employed either now or in the past by Ameritech, and were reflective of an entirely different structure of traffic measurement and billing (*i.e.* originating carrier measurement). Thus, neither the Michigan rates nor the Texas rates are an appropriate benchmark for assessing the Ameritech Illinois cost studies. (Ameritech Ex. 3 at 4-5.)

In sum: All agree that the adoption of Ameritech Illinois' proposed bifurcated rates is a step in the direction of more precisely cost-based rates, so long as the cost inputs are not so inaccurate as to compel a different conclusion. And to compel a different conclusion, the cost inputs would have to be inaccurate in a very specific way: setup costs would have had to be misidentified as duration costs or vice versa. Staff – departing from the view it espoused last year in Docket 00-0027 – speculates that that could have happened, but offers no sound reason for the Commission to conclude that it in fact did happen. Ameritech Illinois, speaking through the testimony of the only witness in this case who is knowledgeable about how cost studies are put together and tested in this Commission, showed that it is highly unlikely that it happened. On this record, the Commission should conclude that Ameritech Illinois' bifurcated rate proposal is sound.

E. The Cost Of Implementing Bifurcated Rates Would Not Outweigh The Benefit.

As Dr. Zolnierek testified, "Staff fully acknowledges that moving to the properly set bifurcated rates would yield societal benefits." (Staff Ex. 1.0 at 26.) Dr. Zolnierek suggests, however, that the move to bifurcated rates would entail costs that might outweigh the benefits. (*Id.* at 11, 26.) Dr. Zolnierek is not specific about what those costs would be (the closest he comes is a reference to "changes to the compensation terms and physical interconnection arrangements between carriers' networks" (*id.* at 11)), and implies it is Ameritech Illinois' burden to show that those costs are relatively small (*id.* at 26).

Ameritech Illinois does not agree that it is Ameritech Illinois' burden to show that the costs of implementing bifurcated rates would be small. Rather, Ameritech Illinois must show that the bifurcated rates it is proposing are more in line with the cost-based requirements of the 1996 Act and the FCC's implementing Rule than are its current reciprocal compensation rates. Ameritech Illinois having made that showing, it is XO's or Staff's burden to show that the costs of implementing bifurcation exceed the societal benefits.

In any event, however, Ameritech Illinois has shown that the costs of implementing bifurcation would be *de minimis*. There would be no significant cost to Ameritech Illinois in implementing bifurcated rates; nor would other carriers be significantly impacted. (Ameritech Ex. 3 at 2.) The message recordings that are currently used to bill per-minute rates already contain all the information necessary for the billing of bifurcated rates, so no changes to the network or the message recording equipment are needed. (*Id.*) Ameritech Illinois' billing systems are already being updated to handle bifurcated rates that are now in effect in Michigan and that will also be in place later this year in Wisconsin. (*Id.*) In any case, those billing system changes are simple and straightforward. (*Id.*) Most other carriers will also be updating their billing systems to accommodate bifurcated rates regardless whether such rates are adopted in Illinois (for example, XO also operates in Michigan), and in any case the necessary changes are not at all difficult to implement. (*Id.*)

There has been some suggestion that under Ameritech Illinois' proposal, physical interconnection between networks might need to be altered. That, however, is not the case. There is nothing in Ameritech Illinois' proposal that is intended to require or that would require the alteration of physical interconnection or trunking arrangements. (*Id.* at 9.)

F. Ameritech Illinois' Bifurcated Rate Proposal Is Not Foreclosed By The FCC's *ISP Compensation Remand Order*

Staff has suggested that Ameritech Illinois' proposal is "an attempt to circumvent the FCC's decision." (Staff Ex. 1.0 at 20.) By this Staff means that the FCC, in its *ISP Compensation Remand Order* made clear that state commissions do not have jurisdiction to regulate ISP-bound traffic, and that Ameritech Illinois' proposal is an improper attempt to induce the Commission to adjust intercarrier compensation rates on ISP-bound traffic. *Id.* at 19-20. This is not a valid reason for rejecting Ameritech Illinois' sound proposal.

The fact of the matter is that this Commission retains jurisdiction to set reciprocal compensation rates for section 251(b)(5) traffic. Staff recognizes that. (*E.g.*, Staff Ex. 1.0 at 20, lines 402-407.) As it happens, the state of the law is such that whatever rates the Commission establishes for 251(b)(5) calls will also apply to ISP-bound calls.[7] But that is because the FCC has so ruled, not because of any decision that this Commission will be making about ISP-bound calls.

This Commission should rationalize reciprocal compensation in Illinois – as the State commissions in Michigan, Wisconsin, California and Texas have done (*see* Ameritech Ex. 1 at 18) – by requiring the termination rates paid on each call to be based on the duration of that call. To be sure, intercarrier compensation rates for ISP-bound traffic may be rationalized along with reciprocal compensation rates for 251(b)(5) calls – in a manner that precisely accords with Staff's recommendation to the Commission in Docket 00-0027 – but that by-product will be by operation of the FCC's *ISP Compensation Remand Order*, not by any improper exercise of jurisdiction over ISP-bound traffic by this Commission.

In a word, the Commission is free to decide on the merits – and should decide on the merits – whether or not to adopt Ameritech Illinois' proposed bifurcated rates. To be sure, the Commission can, in making that decision, appropriately take into account the fact that adoption of the bifurcated rates for 251(b)(5) traffic would (until such time, if any, as Ameritech Illinois opts for the FCC caps) yield application of those bifurcated rates to ISP-bound traffic. But the Commission need not, and should not, concern itself with the notion that the proposal somehow contravenes the *ISP Compensation Remand Order*. It simply does not.

Looked at another way, Staff's contention may be that by making available capped rates for ISP-bound traffic, the FCC in effect mooted Ameritech Illinois' bifurcated rate proposal. Any such contention would be mistaken, for two reasons.

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[7] There is an exception to this general statement: If Ameritech Illinois chooses at some point to avail itself of the FCC rate caps on ISP-bound traffic, it would have to make an offer to all carriers in the State to exchange section 251(b)(5) traffic at those rates. If XO were to decline that offer, then XO and Ameritech Illinois would be exchanging ISP-bound traffic at the FCC rates and 251(b)(5) traffic at the rates established by this Commission.

First, bifurcated rates are desirable separate and apart from their application to ISP-bound traffic. While it is difficult to determine the extent to which other types of traffic are also driving differences in average hold times among carriers' networks, the differences in effective prices for traffic with different hold-time characteristics, and the potential for regulatory arbitrage offered by simple per-minute rates (particularly in conjunction with legislative mandates for residential flat-rate "local" calling), make it imperative to move to a rate structure that more accurately reflects the nature of cost causation for transport and termination of traffic. (Ameritech Ex. 3 at 1-2.) Ameritech Illinois is therefore committed to the goal of adopting a bifurcated rate structure regardless of its ultimate decision regarding the implementation of the FCC rate caps for ISP-bound traffic. (*Id.* at 2.)

Second, the FCC's rate cap plan, while in many respects reasonable, in effect requires Ameritech Illinois, as a pre-condition to availing itself of the FCC rates for ISP-bound traffic, to offer all local carriers in Illinois the opportunity to engage in arbitrage. (Ameritech Ex. 1 at 16-17.) The arbitrage opportunity lies in each carrier's choice to exchange 251(b)(5) traffic at either higher or lower rates, depending on the characteristics of the traffic that carrier exchanges, and, for that matter, to target particular classes of customers or particular classes of traffic in order to maximize the benefit of exchanging such traffic at the higher or lower rates it has chosen. (*Id.*) This arrangement is economically inefficient, because it encourages carriers to base their business plans not on their ability to provide services economically, but on their ability to take advantage of an anomaly in the inter-carrier compensation rate structure. (*Id.* at 17.) Also, of course, the arrangement is a losing proposition for Ameritech Illinois, which would wind up exchanging 251(b)(5) traffic at higher rates with "heavy terminating" carriers and at lower rates with "heavy originating" carriers. (*Id.*)[8]

II. THE COMMISSION SHOULD USE THIS DOCKET TO CONSIDER AND ADOPT AMERITECH ILLINOIS' PROPOSED BIFURCATED RATES.

Staff, while advocating against Ameritech Illinois' bifurcated rate proposal, recognizes that the Commission does have jurisdiction to consider the proposal. (Staff Ex. 1.0 at 20, lines 402-407; Tr. 172, line 22 – 173, line 11.) The Commission should not decline to exercise that jurisdiction.

A. XO's Request That The Commission Determine Its Rights Under Section 252(i) Of The 1996 Act Does Not Preclude The Commission From Considering Ameritech Illinois' Proposal.

XO contends it is entitled to take the reciprocal compensation provisions in the Focal Agreement – except to the extent they pertain to ISP-bound traffic – and that the Commission therefore cannot entertain Ameritech Illinois' bifurcated rate proposal. XO is mistaken.

XO initiated this proceeding as an arbitration under section 252(b) of the 1996 Act. It labeled its pleading a "Petition for Arbitration" and styled the case, "In the matter of XO Illinois, Inc. Petition for Arbitration pursuant to Section 252(b) of the Telecommunications Act of 1996 to establish an Interconnection Agreement with Illinois Bell Telephone Company d/b/a Ameritech Illinois."

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[8] XO and Staff have suggested that if Ameritech Illinois were to make the offer that it must make in order to qualify to exchange ISP-bound traffic at the FCC's capped rates, CLECs could not decline that offer. Ameritech Illinois wishes XO and Staff were correct, but believes they are not. The *ISP Compensation Remand Order* repeatedly speaks (at ¶¶ 8 and 89, for example) in terms of the incumbent LEC "offering" to exchange all section 251(b)(5) traffic at the same capped rates. The making of an "offer" implies the possibility of a rejection, and there is nothing in the *ISP Compensation Remand Order* that suggests that this offer is any different. As an alternative formulation of the view that individual CLECs may have to accept the offer, Staff has suggested that the Commission could adopt the FCC caps as the going reciprocal compensation rate for 251(b)(5) traffic. Ameritech Illinois agrees with Staff that the Commission has authority to do that, but cannot base its business plans, or its position in this proceeding, on the hope that the Commission might.

Having initiated the proceeding as an arbitration under section 252(b), XO has to live with the rules Congress established for such a proceeding. That includes section 252(b)(3) and 252(b)(4)(A), which entitled Ameritech Illinois to file a response that set forth issues in addition to those set forth in the petition.[9] And, more important, it includes section 252(b)(4)(C), which provides, in pertinent part:

> The State commission ***shall*** resolve each issue set forth in the petition *and the response* . . . . (emphasis added).

In its response to XO's petition for arbitration (at 17-18), Ameritech Illinois set forth as issues for arbitration the question whether Ameritech Illinois' proposed Appendix Reciprocal Compensation should be included in the parties' agreement and, to be extra cautious, whether each individual section of the Appendix Reciprocal Compensation should be included in the parties' agreement. This includes section 5.0, in which the proposed bifurcated rates appear. The 1996 Act now requires the Commission to decide those issues.

If XO wanted a proceeding limited to the question of what XO's rights are under section 252(i) of the 1996 Act, XO should not have filed a petition for arbitration under section 252(b). In fact, XO's section 252(i) rights cannot properly be determined in a section 252(b) arbitration at all. In a section 252(b) arbitration, the Commission has jurisdiction only to resolve disagreements about the incumbent carrier's duties *under section 251 of the Act*. This is because the subject matter of the arbitration is "open issues" (*see* section 252(b)(1)) arising out of the parties' negotiations under section 252(a), and the subject matter of those negotiations, in turn, is "the particular terms and conditions of agreements to fulfill the duties described in" section 251. (*See* section 251(c)(1).) The incumbent's duties under section 251

[9] Section 252(b)(3) authorizes the filing of the response, and section 252(b)(4)(A) makes clear that the response may set forth issues for arbitration in addition to those set forth in the Petition.

are many, and the scope of arbitrable issues is therefore extensive. But the incumbent's obligations under section 252(i) are separate from and in addition to its duties under section 251, and the interpretation of the 252(i) obligations is not within the scope of the arbitrator's jurisdiction under section 252(b). This is not to say that the Commission does not have authority to interpret and enforce section 252(i). It does. But not in an arbitration under section 252(b).[10]

Thus, the Commission, as arbitrator in this proceeding under section 252(b) of the Act, is bound to consider Ameritech Illinois' proposals.

B. Ameritech Illinois' Appendix Reciprocal Compensation Is The Only Available Vehicle For Arriving At A Complete Interconnection Agreement.

Recent experience teaches that if there is anything the Commission should avoid when it arbitrates an interconnection agreement, it is an arbitration decision that does not make absolutely clear exactly what the parties' agreement is supposed to say.[11] Here, that consideration weighs heavily in favor of considering, and adopting, Ameritech Illinois' proposed Appendix Reciprocal Compensation, because the interconnection agreement XO is proposing is woefully inadequate, and no tenable approach to fixing it is on the table.

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10 In his initial Verified Statement, XO witness Kinkoph testified (XO Ex. 1 at 5), "XO has proposed language that would remain in effect until such time as Ameritech has notified XO of its intent to implement the 'mirroring rule' set forth in paragraph 89 of the FCC Order. That language is similar to the language in the Focal agreement. A copy of XO's proposed language was attached to XO's petition as Appendix E." Based in part on that testimony, Ameritech Illinois demonstrated in its response to XO's petition for arbitration (at 1-3) that by proposing extensive language for section 4.7 of the agreement, XO opened the door to the counter-proposal that appears in Ameritech Illinois' proposed Appendix Reciprocal Compensation. XO thereafter indicated that it was not actually proposing the language that was attached to its petition as Exhibit E, but rather that it was seeking to opt into that language as it appears in the Focal Agreement. Ameritech Illinois' argument that section 252(b)(4)(C) requires the Commission to assess the Appendix Reciprocal Compensation on its merits is not, of course, dependent on the premise that XO opened the door by "proposing" section 4.7.

11 Ameritech Illinois refers to its arbitration with Verizon Wireless, Docket No. 01-0007. There, the Commission issued its arbitration decision on May 1, 2001, but the parties were thereafter unable to agree on language for their conforming interconnection agreement. The dispute about conforming language carried on for nearly four months, until the Commission resolved it in its August 23, 2001 Interim Order in Docket No. 01-0521. Even that order is currently being challenged by Verizon Wireless, and it remains uncertain when the parties will have an approved interconnection agreement in place.

In the context of this proceeding, the most important single thing for the XO/Ameritech Illinois interconnection agreement to address is ISP-bound traffic. If nothing else, the agreement must clearly say whether the parties are going to compensate each other for the transport and termination of such traffic and, if they are, at what rates. The agreement XO is proposing does not even touch on the subject. One can study XO's proposed section 4.7 and its subsections (Ex. E to XO's petition for arbitration) backwards and forwards and find no mention of ISP-bound traffic, and certainly no clue how it is to be treated for purposes of intercarrier compensation. This became painfully clear at hearing, when XO witness Kinkoph was unable to answer what should be a very simple question: If XO's proposed agreement were approved, and the parties later fell into disagreement over the payment of intercarrier compensation on ISP-bound traffic, where in the agreement could they find the answer to their disagreement? (Tr. 43-48.)

Mr. Kinkoph seemed to think it is somehow understood that the reciprocal compensation provisions in XO's proposed section 4.7 would apply to ISP-bound traffic. (*Id.*) Since Mr. Kinkoph is not an attorney, that is perhaps an understandable mistake. But it is still a mistake. The parties' agreement must explicitly address compensation for ISP-bound traffic, and XO's proposed agreement does not.

It was mentioned at hearing that this defect might be cured by adding to the language that XO is proposing the following sentence, which appears in section 4.7 of the Focal Agreement[12]:

> Pursuant to the arbitration decision of the Commission with respect to this Agreement in Docket No. 00-0027 ("Arbitration Decision"), the Reciprocal Compensation arrangements are applicable to Internet Service Provider ("ISP") bound traffic.

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[12] XO initially did not include the sentence in the language it is proposing because XO recognizes that the FCC's *ISP Compensation Remand Order* prohibits it from adopting the sentence under section 252(i) of the 1996 Act. As we show in the text, however, the problem with the sentence runs far deeper than that.

But that sentence cannot lawfully be included in the XO/Ameritech Illinois agreement, because the reciprocal compensation provisions of the XO/Ameritech Illinois agreement cannot apply to ISP-bound traffic under the rationale of the Arbitration Decision in Docket 00-0027. In that proceeding, the Commission determined that ISP-bound traffic is local and therefore subject to reciprocal compensation under section 251(b)(5) of the 1996 Act. In the *ISP Compensation Remand Order*, however, the FCC ruled that ISP-bound traffic is interstate, rather than local; that ISP-bound traffic is not subject to reciprocal compensation under section 251(b)(5); and, for that matter, that the determination whether traffic is subject to reciprocal compensation under section 251(b)(5) does not even depend on the old local vs. non-local dichotomy. Thus, the Commission cannot properly deal with the question of intercarrier compensation on ISP-bound traffic in this docket by importing the obsolete sentence from the Focal Agreement.

XO's proposed contract language not only fails to address intercarrier compensation on ISP-bound traffic under the circumstances as they now exist – *i.e.*, with Ameritech Illinois not having elected to avail itself of the FCC rate caps – but also fails to make any provision for the possibility that Ameritech Illinois might elect to take those caps in the future. *Cf*. Ameritech Illinois' proposed Appendix Reciprocal Compensation section 12.1. Mr. Kinkoph acknowledged that he could "see a need for," or that XO "would not oppose" language making provision for such an election. (Tr. 81.) No such provision is included in the language XO is proposing, however.

It is understandable that XO devotes more energy to trying to convince the Commission not to entertain Ameritech Illinois' bifurcated rate proposal than it does to challenging the proposal on its merits, because the proposal is clearly sound. The Commission should not be distracted by XO's arguments that the Commission cannot consider Ameritech Illinois' proposal.

The Commission not only can consider the proposal, but must consider it if the parties are to emerge from this proceeding with a workable interconnection agreement.

III. THE COMMISSION SHOULD NOT REQUIRE AMERITECH ILLINOIS IMMEDIATELY TO DECLARE WHETHER IT WISHES TO ADOPT THE FCC'S RECIPROCAL COMPENSATION RATE CAPS.

Staff proposes that the Commission "require Ameritech to immediately determine whether it wishes to adopt the reciprocal compensation rate caps established by the Federal Communications Commission (FCC") in" the *ISP Compensation Remand Order.* (Staff Ex. 1.0 at 2.) This proposal invites the Commission to exceed its authority and to make a decision that is at odds both with the *ISP Compensation Remand Order* and the schedule for this proceeding. The Commission should decline to consider Staff's proposal, and if the Commission does consider it, should reject it.

A. The Commission Cannot Properly Consider Staff's Proposal, Because It Goes Beyond The Issues Set Forth For Arbitration.

In this proceeding, the Commission is acting as arbitrator under section 252(b) of the 1996 Act. Accordingly, the permissible range of Commission action is confined to the boundaries Congress established in the 1996 Act. There are many decisions that the Commission has jurisdiction to make under some other source of authority (*e.g.*, Illinois statute) that the Commission does not have jurisdiction to make under section 252(b). In particular, section 252(b)(4)(A) of the 1996 Act provides:

> The state commission shall limit its consideration of any [arbitration] petition . . . (and any response thereto) to the issues set forth in the petition and in the response, if any . . . .

Neither XO's arbitration petition nor Ameritech Illinois' response to XO's petition presents the question whether Ameritech Illinois should be required to declare whether it wishes to adopt the FCC's rate caps. Indeed, the petition does not contain even a glimmer of a complaint about the fact that Ameritech Illinois has not declared itself. To be sure, the petition does mention that fact (at ¶ 19), but there is no suggestion that Ameritech Illinois has any duty to declare itself at any particular time, much less that the Commission should require Ameritech Illinois to do so.

Thus, Staff is asking the Commission to decide an issue that was set forth neither in the petition nor in the response. Section 252(b)(4)(A) forbids this.

Nor do the issues that the parties have set forth for arbitration implicate the question whether Ameritech Illinois has a duty to declare itself. Sometimes, no doubt, an arbitration issue requires the determination of some sub-question or related question that the party raising the issue did not recognize and thus did not set forth. In such a case, the State commission would have no alternative but to address the sub-question or related question in order to reach the arbitration issue. This, however, is not such a case. The Commission can readily decide all the issues that XO and Ameritech Illinois have set forth for arbitration without delving into the question raised by Staff.

B. Staff's Proposal Could Not Be Considered In A Section 252(b) Arbitration Even If It Were Set Forth As An Issue In The Petition Or Response.

Assume that XO had set forth as an arbitration issue the question whether Ameritech Illinois should be required to declare whether it wishes to avail itself of the FCC's rate caps. That would eliminate the section 252(b)(4)(A) prohibition just discussed. But the issue still would not be arbitrable, because it is not within the scope of that which is eligible for arbitration under section 252(b).

A disagreement is not subject to arbitration under section 252(b) merely because it is set forth as an issue in the petition or the response. If XO offered to buy some Ameritech Illinois office furniture, for example, and the parties were not able to agree on terms, the disagreement could not be arbitrated in a section 252(b) proceeding. Congress drew a line between that which is arbitrable and that which is not, and the line appears on the face of the 1996 Act.

A section 252(b) arbitration arises when negotiations under section 252(a) fail to yield an agreement. The matters that are subject to negotiation under section 252(a), in turn, are identified in section 251(c)(1) of the Act. Those matters are "the particular terms and conditions of agreements to fulfill the duties described in paragraphs (1) through (5) of subsection [251](b) and this subsection [251(c)]." It is these matters, and only these matters, that produce the "open issues" that are eligible for arbitration. (*See* section 252(b)(1).) Thus, the statutory explanation for the self-evident fact that the Commission cannot resolve in a section 252(b) arbitration the terms and conditions of a purchase and sale of office furniture is that such terms and conditions are not "the particular terms and conditions of agreements to fulfill the duties described in" paragraphs (1) through (5) of subsection 251(b) of the Act or in subsection 251(c) of the Act.

The question whether Ameritech Illinois should be required to declare itself with respect to the FCC rate caps is no more a question about rights or duties under subsection 251(b) or 251(c) than is a question about the purchase and sale of office furniture. There is an easy way to corroborate that this is correct: If the Commission were to entertain Staff's proposal, it would not assess the proposal by looking to anything in section 251(b) or section 251(c), or to any FCC rule or regulation implementing subsection 251(b) or 251(c). Indeed, *the rate caps themselves are not even a creature of section 251*. Rather, the FCC promulgated them pursuant to its authority under section 201 of the Communications Act of 1934. *See, e.g., ISP Compensation Remand Order* at ¶¶ 1, 4, 52, 66.

C. As A Practical Matter, Staff's Proposal Is An Impossibility.

Law aside, it would be impossible for the Commission to adopt Staff's proposal in this arbitration in a way that could have any effect on the content of the parties' interconnection agreement while at the same time keeping the proceedings on schedule.

Staff has never made clear how it sees events playing out if the Commission were to adopt Staff's proposal. Presumably, the requirement that Staff is proposing would be included in the arbitration award. Immediately, that would create an enormous problem. The arbitration award is supposed to resolve all the open issues between the parties, so that the parties can prepare an interconnection agreement that conforms with the award and submit the award for Commission approval. Typically, in fact, the Commission's arbitration award allows the parties only two weeks or so to prepare and submit the conforming award. Here, though, the parties would not proceed from the arbitration award to an agreement, but instead would proceed from the arbitration award to a series of follow-up steps (declaration by Ameritech Illinois; response by XO in light of declaration; etc.) that could delay the completion of an agreement for a considerable time.

It became apparent at hearing just how unworkable Staff's proposal is in the context of this arbitration. Dr. Zolnierek suggested that the Commission can order XO – if Ameritech Illinois offers to exchange all 251(b)(5) traffic and ISP-bound traffic at the FCC's caps – to accept Ameritech Illinois' offer. If, then, the Commission were to order Ameritech Illinois to declare itself, one possible scenario would be as follows:

1. The Commission adopts Staff's proposal and, and its arbitration award, orders Ameritech Illinois to declare itself within, say, one week.

2. Ameritech Illinois declares that it wishes to opt into the FCC rate caps, and accordingly makes an offer to all carriers in Illinois to exchange all 251(b)(5) traffic and all ISP-

bound traffic at the FCC caps;

3. Some indeterminate period of time later, XO rejects Ameritech Illinois' offer to exchange 251(b)(5) traffic at the FCC caps;[13]

4. Ameritech Illinois brings XO's rejection to the Commission's attention, and the Commission – still within this proceeding, Dr. Zolnierek recommended (Tr. 170, lines 16-21) – orders XO to accept Ameritech Illinois' offer.[14]

Plainly, there is not time for all of that to happen in this proceeding. And even if there were enough time, that wouldn't be the end of it; somehow, and presumably still within the confines of this proceeding, the parties would have to arrive at, or the Commission would have to order, contract language to address the parties' inter-carrier compensation arrangements in light of the foregoing developments. It simply cannot be done.

D. Staff's Proposal Is Inconsistent With the *ISP Compensation Remand Order*.

Nothing in the *ISP Compensation Remand Order* remotely suggests that incumbent LECs have a duty to declare at any particular time whether they wish to avail themselves of the rate cap plan set forth in the order. Quite the contrary, the FCC deliberately and explicitly left the decision as to when (or whether) to declare its intention to implement the rate caps up to each ILEC on a state-by-state basis. In structuring its order, the FCC understood that situations varied among states and carriers as to factors such as the remaining life of preexisting agreements and the existence of varying types of "change of law" provisions (including some that specifically reference the FCC docket which resulted in the *ISP Compensation Remand Order*). Under the circumstances, the FCC chose to structure its compensation plan in a manner that provides a

[13] XO witness Kinkoph testified that XO does not know how it would respond to such an offer from Ameritech Illinois, so a refusal is certainly a possibility. (Tr. 68-69.)

[14] Ameritech Illinois does not believe the Commission can order XO to accept Ameritech Illinois' offer, but is accepting Dr. Zolnierek's view to the contrary for the sake of illustration.

great deal of flexibility, but also uncertainty, for all of the carriers (including Ameritech Illinois) to which it applies. It creates a complex range of possibilities, in which each carrier must make its business decisions based on the full range of options available to it. The ability of ILECs such an Ameritech Illinois to choose whether and when to invoke the rate caps for ISP-bound traffic is certainly one source of uncertainty, but it is far from the only one. Even if Ameritech Illinois were to choose to invoke the rate caps, there would be uncertainty as to which existing agreements will be subject to change at which points in time, based on their varying "change of law" provisions; uncertainty as to the effective date of the capped rates in each such agreement; and uncertainty as to whether the FCC's default proxy for identification of ISP-bound traffic would be determined to be adequate by both parties to each agreement. Certainly, there are other sources of uncertainty also, such as the efforts by CLECs to have the FCC's *ISP Compensation Remand Order* overturned in the courts. That is apparently an uncertainty that the CLEC industry believes it can live with, though it plainly raises the level of uncertainty for ILECs as well as CLECs in planning for the future.[15]

[15] There was some suggestion at hearing that Ameritech Illinois might intend to repeatedly opt into and out of the FCC rate caps as the balance of incoming and outgoing traffic changed from time to time. There is no reason to believe Ameritech Illinois has any such intention, and the Commission plainly need not concern itself with such a scenario in this proceeding. The Commission would have occasion to do so when and if Ameritech Illinois were to engage in the hypothesized gymnastics.

CONCLUSION

For the reasons set forth above, the Commission should reject XO's proposed section 4.7 for the parties' interconnection agreement and instead require the parties to include Ameritech Illinois' Appendix Reciprocal Compensation.[16]

Dated: September 4, 2001

Respectfully submitted,

AMERITECH ILLINOIS

By: ______________________________

Nancy J. Hertel
Ameritech Illinois
225 W. Randolph St.
Chicago, Illinois 60606
(312) 727-4517

Dennis G. Friedman
Mayer, Brown & Platt
190 S. LaSalle Street
Chicago, Illinois 60603
(312) 701-7319

[16] Setting aside XO's position that the Commission should not entertain Ameritech Illinois' proposed Appendix Reciprocal Compensation, XO does not appear to find the individual provisions in the appendix objectionable. Ameritech Illinois' testimony explained and supported a number of those provisions, and invited questions and criticisms of the appendix as a whole. (Ameritech Ex. 1 at 19-23.) XO offered no criticisms, and XO witness Kinkoph testified that XO has no problem with the key provisions in the appendix that were discussed at hearing (*see* Tr. 58-61). To the extent that XO may raise objections in its initial post-hearing brief, Ameritech Illinois will address them on reply.

RESPONSES TO QUESTIONS POSED BY ADMINISTRATIVE LAW JUDGE

Question 1: The penultimate sentence in paragraph 89 of the FCC's *ISP Compensation Remand Order* states, "For those incumbent LECs that choose not to offer to exchange section 251(b)(5) traffic subject to the same rate caps we adopt for ISP-bound traffic, we order them to exchange ISP-bound traffic at the **state-approved or state-arbitrated reciprocal compensation rates reflected in their contracts**." (Emphasis added.) To which reciprocal compensation rates was the FCC referring in the boldface language? If the incumbent LEC's contracts have varying reciprocal compensation rates, is the boldface language ambiguous? Do "state-approved or state-arbitrated rates" include tariffed rates?

<u>Ameritech Illinois' Response to Question 1</u>:

Ameritech Illinois believes that all the FCC meant by the language in question is that the incumbent LEC would exchange ISP-bound traffic with each individual competing LEC at whatever rate(s) apply to 251(b)(5) traffic exchanged by the incumbent LEC and that competing LEC. Differently stated, Ameritech Illinois does not believe the FCC intended to establish any general rule (or even to express any preference) concerning *which* of several possible 251(b)(5) rates would apply to ISP-bound traffic in the event that the incumbent does not offer to exchange all traffic at the FCC caps. To illustrate the point, assume that an incumbent LEC announces on September 15, 2001, that it is choosing not to exchange all 251(b)(5) traffic and ISP-bound traffic at the FCC's capped rates.[17] Assume also that as of September 15, 2001, the incumbent LEC is positioned as follows with respect to certain competing LECs ("CLECs"):

1. It has an interconnection agreement with CLEC X that provides that the parties will exchange 251(b)(5) traffic at rate X. The interconnection agreement has a year left on its term, and the parties are not yet negotiating a successor agreement. Rate X was negotiated by the parties, and thereafter approved by the Commission.

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[17] Ameritech Illinois does not believe that any such announcement is required, and that an incumbent LEC can instead manifest its election not to avail itself of the FCC caps by inaction alone. We posit an announcement just for ease of discussion.

2. It has an interconnection agreement with CLEC Y that provides that the parties will exchange 251(b)(5) traffic at rate Y. The interconnection agreement has fifteen months left on its term, and the parties are not yet negotiating a successor agreement. Rate Y was arbitrated by the parties, and thereafter approved by the Commission.

3. It has an interconnection agreement with CLEC Z that provides that the parties will exchange 251(b)(5) traffic at Ameritech Illinois' tariffed reciprocal compensation rates. The interconnection agreement has ten months left on its term, and the parties are not yet negotiating a successor agreement. The tariffed rate was either affirmatively approved or allowed to go into effect by the state commission.

4. It has an interconnection agreement with CLEC R that provides that the parties will exchange 251(b)(5) traffic at rate R, which was a negotiated rate. The interconnection agreement expires in four months, and the parties are arbitrating a successor agreement.

Under the *ISP Compensation Remand Order*, including the portion of paragraph 82 that prompted the ALJ's question, Ameritech Illinois will, effective as of September 15, 2001, exchange ISP-bound traffic with CLEC X at rate X; with CLEC Y at rate Y; and with CLEC Z at the tariffed rate (which may or may not be the same as rate X or rate Y). Again, the FCC was not pointing to any particular 251(b)(5) rate as "THE" state-arbitrated or state-approved rate that would apply to ISP-bound traffic if the incumbent did not opt for the FCC caps; the FCC was merely saying that whatever 251(b)(5) rate applied as between the incumbent and any particular CLEC would likewise apply to ISP-bound traffic exchanged by the incumbent and that CLEC.

Of the four scenarios described above, the one that is closest to the one presented here is scenario 4. In that scenario, the incumbent LEC will, effective as of September 15, 2001, and for the duration of the current agreement, exchange ISP-bound traffic with CLEC R at rate R – the rate that applies to 251(b)(5) traffic under the current agreement. Under the parties' new agreement – the one being arbitrated – the parties will compensate each other for ISP-bound traffic at the rate that applies to 251(b)(5) traffic under their new agreement – *whatever that rate may turn out to be*. If the parties have agreed on a reciprocal compensation rate for 251(b)(5) traffic (whether that rate be rate R, or the incumbent's tariffed rate, or some other rate), then that will be the rate at which they will exchange ISP-bound traffic as well. If, on the other hand, the parties are arbitrating the rate at which they will exchange 251(b)(5) traffic, as in this proceeding, then the rate that emerges from the arbitration will apply to ISP-bound traffic as well as to 251(b)(5) traffic.

Question 2: Section 252(d) of the 1996 Act requires that reciprocal compensation rates be "just" and "reasonable," provide for the "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"; and be based on "a reasonable approximation of the additional costs of terminating such calls." Section 252(i) of the 1996 Act (the ALJ's question assumes) permits a requesting carrier to adopt the reciprocal compensation provisions, including the rates, that appear in the incumbent's state-approved interconnection agreement with any other carrier. If CLEC Q wants to adopt under section 252(i) the reciprocal compensation provisions, including the rates, of CLEC T, but the adoption would result in rates that are not cost-based for CLEC Q (*i.e.,* that do not meet the standards of section 252(d)), then how does one resolve the tension between the command of section 252(d) and the rights conferred by section 252(i)?

<u>Ameritech Illinois' Response to Question 2</u>:

The question assumes that reciprocal compensation rates are subject to section 252(i), that is, that CLEC Q can, in general, adopt the reciprocal compensation rates that appear in an interconnection agreement between CLEC T and the incumbent LEC. Although Ameritech Illinois has not taken the position in this proceeding that reciprocal compensation rates are generally not subject to section 252(i), there is a strong argument, set forth below, that they are not.

Even if reciprocal compensation rates are generally subject to section 252(i), there are circumstances where they would not be. One is where CLEC T is charging reciprocal compensation rates that do not mirror the incumbent's rates, but that instead are based on CLEC T's own proven costs. In that event, CLEC Q would not be permitted to adopt CLEC T's reciprocal compensation rates as its own. Framed in the terms of the ALJ's question, the tension between section 252(d) and section 252(i) would be resolved in this instance by ruling that section 252(d) in effect trumps section 252(i). Ameritech Illinois is not aware of any law on this point, however. For other circumstances where reciprocal compensation rates would not be subject to adoption under section 252(i) even in the face of a general rule to the contrary, *see* 47 C.F.R. § 809 (limiting availability of provisions under section 252(i) in certain circumstances).

There is a strong argument that a requesting carrier does not have the right under section 252(i) to adopt the reciprocal compensation rates in another interconnection agreement. By its terms, section 252(i) applies only to an "interconnection, service, or network element" provided by the incumbent LEC. Transport and termination of traffic is not interconnection; it is not a service as that term is used in section 252(i)[18]; and it is not a network element. Therefore, section 252(i), by its terms, does not entitle one carrier to opt into the reciprocal compensation provisions of another carrier's interconnection agreement.

Nor is reciprocal compensation a term or condition of interconnection. The 1996 Act makes clear that transport and termination (for which reciprocal compensation is paid) is distinct from interconnection. Interconnection is the physical linking of two networks; transport and termination of telecommunications is what happens afterwards.

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18 The "services" referred to in section 252(i) are the telecommunications services that the incumbent sells at retail and must provide at wholesale to requesting carriers under section 251(c)(4).

That much is clear from both the structure of the 1996 Act and the FCC's *Local Competition Order*.[19] The duty of a LEC to establish reciprocal compensation arrangements for the transport and termination of telecommunications is set forth in section 251(b)(5) of the Act. Section 251(c), which follows, begins by stating: *"In addition to the duties contained in subsection (b), . . .* " and then sets forth the additional obligations of incumbent LECs. These additional obligations include the duty to provide interconnection on "rates, terms, and conditions that are just, reasonable, and nondiscriminatory." (Section 251(c)(2)(D).) The fact that Section 251(c)(2) makes absolutely no reference to reciprocal compensation, which is addressed in an entirely different subsection, sustains the conclusion that reciprocal compensation is not a term or condition of interconnection.

The *Local Competition Order* also recognizes the distinction between interconnection, on the one hand, and reciprocal compensation, on the other. Indeed, the FCC specifically discussed the relationship between interconnection under section 251(c)(2) and reciprocal compensation under section 251(b)(5). The discussion makes eminently clear that "interconnection" under section 251(c)(2) refers only to the physical linking of the two networks and does not include the transport and termination of traffic within the meaning of section 251(b)(5). Noting that interconnection and reciprocal compensation are subject to separate pricing standards under the Act, the FCC stated (*Local Competition Order* ¶ 176):

> We conclude that the term "interconnection" under section 251(c)(2) refers only to the physical linking of two networks for the mutual exchange of traffic . . . and not the transport and termination of traffic . . . .

Congress's exclusion of reciprocal compensation from section 252(i) was not a fluke. On the contrary, it makes perfect sense that a requesting carrier is not allowed to adopt the reciprocal

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[19] First Report and Order (FCC 96-325), *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98 (rel. Aug. 8, 1996).

compensation provisions of another carrier's agreement, because the Act requires each carrier's reciprocal compensation rates to be based on its *own* costs. Specifically, the Act requires that reciprocal compensation rates must "provide for the mutual and reciprocal recovery by *each* carrier of costs associated with the transport and termination of *each* carrier's network facilities of calls that originate on the network facilities of the other carrier." (Section 251(d)(2).) Because reciprocal compensation payments must reflect the costs of the carrier receiving those payments, reciprocal compensation arrangements were not included in section 252(i).[20]

Nor would it make economic sense to hold otherwise. If a particular requesting carrier has higher costs than the rest of the industry and is thus entitled to higher reciprocal compensation payments, it would defy sound economics to allow every other carrier to opt into that same rate. Indeed, to adopt such an absurd rule would turn the Act's forward-looking cost methodology on its head. Under that methodology, costs are assumed to be the costs of the most efficient provider. Applying section 252(i) to reciprocal compensation would allow each competitive LEC to assume the cost structure (for reciprocal compensation purposes) of the least efficient competitor.

[20] This conclusion about Congress' intent is unaffected by the FCC's Rule that allows CLECs to mirror the incumbent carrier's rates, and thus to charge identical reciprocal compensation rates even when their costs are not identical. That FCC Rule was adopted after Congress passed the Act, and was not anticipated by anything in the Act.

CERTIFICATE OF SERVICE

I, Dennis G. Friedman, an attorney, hereby certify that I caused a copy of the foregoing **AMERITECH ILLINOIS' INITIAL POST-HEARING BRIEF** to be delivered to each person listed below via e-mail and overnight delivery on this 4th day of September, 2001.

Ross A. Buntrock
Kelley, Drye & Warren
1200 19th Street, N.W. - 4th Floor
Washington, DC 20036

Carol Pomponio
Manager, Regulatory Affairs
XO Illinois, Inc.
303 East Wacker Drive
Concourse Level
Chicago, IL 60601

David Gilbert
Administrative Law Judge
Illinois Commerce Commission
160 North LaSalle Street
Suite C-800
Chicago, IL 60601

David L. Nixon
Office of General Counsel
Illinois Commerce Commission
160 North LaSalle Street
Suite C-800
Chicago, IL 60601

Stephen J. Moore
Thomas H. Rowland
Rowland & Moore
77 West Wacker Drive
Suite 4600
Chicago, IL 60601

Jim Zolnierek
Illinois Commerce Commission
527 East Capital Avenue
P.O. Box 19280
Springfield, IL 62701

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Dennis G. Friedman