FEDERAL RESPONDENTS' UNCITED RESPONSE TO THE JOINT INTERCARRIER COMPENSATION PRINCIPAL BRIEF OF PETITIONERS

IN THE UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

NO. 11-9900

IN RE: FCC 11-161

ON PETITIONS FOR REVIEW OF AN ORDER OF THE
FEDERAL COMMUNICATIONS COMMISSION

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

STATUTES

REGULATIONS

ADMINISTRATIVE DECISIONS

OTHER AUTHORITIES

GLOSSARY

1996 Act	Telecommunications Act of 1996
ACA	Affordable Care Act
Act	Communications Act of 1934
APA	Administrative Procedure Act
ARC	Access Recovery Charge
Br.	Petitioners' Brief
CAF	Connect America Fund
CLEC	Competitive Local Exchange Carrier
FCC	Federal Communications Commission
ICC	Intercarrier Compensation
ILEC	Incumbent Local Exchange Carrier
IP	Internet Protocol
IXC	Interexchange Carrier
JA	Joint Appendix
LEC	Local Exchange Carrier
LSS	Local Switching Support
VoIP	Voice over Internet Protocol

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ISSUE PRESENTED

Whether the FCC lawfully reformed its intercarrier compensation rules to implement – following a gradual transition that minimizes disruption to consumers and service providers – a bill-and-keep regulatory framework for all telecommunications traffic exchanged with local telephone companies.

INTRODUCTION AND SUMMARY OF ARGUMENT

In the *Order* on review,[1] the FCC comprehensively reformed an antiquated intercarrier compensation ("ICC") regime. That regime had developed at a time when local phone companies – also known as incumbent local exchange carriers ("incumbent LECs" or "ILECs") – were regulated monopolies and the cost of providing local phone service was effectively

[1] *Connect America Fund*, 26 FCC Rcd 17663 (2011) ("*Order*") (JA__).

subsidized by "access charges" paid to LECs by long-distance carriers (known as "interexchange carriers" or "IXCs"). While technology and market changes developed at a rapid pace, until the FCC adopted its *Order*, the ICC framework largely had remained frozen in time. This resulted in regulatory distortions, extensive arbitrage, and waste – with IXCs paying LECs rates well above the incremental cost of initiating ("originating") or delivering ("terminating") telephone calls. As described in greater detail in the FCC Preliminary Brief (at 1-5, 13-20), this archaic regime was an obstacle to the deployment of more advanced and efficient Internet Protocol ("IP") networks and gave traditional phone companies an economically unsound regulatory advantage over their wireless and Voice-over-IP ("VoIP") competitors. The regime also had become increasingly unstable, as ICC revenues were eroding at an uncertain pace, making it difficult for companies to plan and make investment decisions. *See Order* ¶9 (JA ___) (summarizing shortcomings of the existing ICC systems).

To modernize ICC – and in lieu of a patchwork of 50 different state regimes that had produced intrastate access charge rates as high as 13 cents a minute, even though the incremental cost of call termination was close to zero[2] – the FCC adopted a ratemaking methodology known as bill-and-keep. Under the bill-and-keep framework, carriers recover their costs from their own customers (supplemented by explicit universal service subsidies, when necessary), rather than from their competitors.

In essence, the FCC adopted for local telephone companies the same model that was already in place and continues to work well for the wireless industry. The FCC concluded that a "uniform national bill-and-keep framework" for "all telecommunications traffic exchanged with a LEC" would best serve the goals of the Communications Act of 1934 ("the Communications Act" or "the Act") while also preserving the state-federal partnership that Congress envisioned in the Telecommunications Act of 1996 ("the 1996 Act"). *Order* ¶¶34, 776 (JA__, __).

The FCC explained that, in addition to its other benefits, a bill-and-keep approach would more accurately reflect "cost causation" principles (the economic theory that costs should be borne by those who cause them) than the existing intercarrier compensation systems. *Order* ¶744 (JA__). Those existing systems relied on a "calling-party-network-pays" approach predicated on "the assumption that the calling party [is] the sole beneficiary

[2] *Order* ¶753 (JA__); *Connect America Fund*, 26 FCC Rcd 4554 ¶54 (2011) ("*2011 NPRM*") (JA__).

and sole cost causer of a call." *Id.* For example, under that approach, when someone in Dallas makes a conventional long-distance call to someone in Denver, the access charges that both the Dallas and Denver LECs impose on the caller's IXC ultimately are paid – through elevated long-distance charges – by the caller in Dallas. Similarly, when someone makes a local call, any charges that the originating LEC pays the terminating LEC for delivering the call are ultimately paid by the originating LEC's end users.

The FCC, however, credited "recent analyses" recognizing that "*both* parties generally benefit from participating in a call, and therefore, that both parties should split the cost of the call." *Order* ¶744 & n.1304 (JA__) (emphasis added) (cataloguing economic analyses). Bill-and-keep reflects that shared benefit and thus better adheres to cost causation principles. Regardless of the direction of the call, both the calling and called parties pay their own providers for the costs those providers incur in carrying the call on their respective networks.

To the extent carriers in costly-to-serve areas are unable to recover their costs through affordable charges to their end users, they may do so through universal service support. Thus, where necessary, affordable service will be ensured by *explicit* subsidies, not implicit subsidies contained in inefficiently high ICC rates. That result follows directly from "the direction from Congress in the 1996 Act" that subsidies should be "explicit rather than implicit." *Id.* ¶747 (JA__); *see* 47 U.S.C. §254(e); *Rural Cellular Ass'n v. FCC*, 685 F.3d 1083, 1085 (D.C. Cir. 2012) ("[Congress] directed the Commission to replace the system of implicit subsidies with explicit ones.").

The FCC also determined that a bill-and-keep regime, when compared with existing ICC-based systems, would improve consumers' ability to choose lower-cost, more efficient carriers. *Order* ¶745 (JA__). Because each carrier could recover its costs only from its own subscribers (and could not shift costs to users of other networks through intercarrier charges), bill-and-keep "helps reveal the true cost of the network to potential subscribers." *Id.* That transparency, in turn, provides appropriate incentives to efficient carriers that offer the best mixes of service in terms of features, quality, and price. *Id.* n.1307 (JA__).

The FCC concluded that, because of these varied benefits, bill-and-keep is an essential component of the comprehensive universal service and ICC reforms adopted in the *Order* – reforms that would provide consumer benefits "outweigh[ing] any costs by at least 3 to 1." *Order* ¶14 (JA__); *see generally id.* ¶¶6, 9, 736-54 (JA__, __, __-__).

In their brief, petitioners do not challenge the need for ICC reform or dispute the benefits of adopting bill-and-keep. Instead, they argue that the

Order is *ultra vires* and conflicts with the Administrative Procedure Act ("the APA") and the Constitution. Those claims lack merit.

I.A. Section 251(b)(5) of the Act, 47 U.S.C. §251(b)(5), imposes upon LECs the "duty to establish reciprocal compensation arrangements for the transport and termination of *telecommunications*" (emphasis added), without regard to historical distinctions based on the interstate or intrastate nature of the traffic. Moreover, 47 U.S.C. §201(b) authorizes the FCC to "prescribe such rules … as may be necessary in the public interest to carry out the provisions of this [Act]," including section 251(b)(5). *See AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 378 & n.6, 381 n.7 (1999) ("*AT&T*"). The FCC reasonably determined that, together, these provisions authorize it to regulate the default compensation arrangements applicable to all telecommunications traffic exchanged with a LEC. *Order* ¶¶760, 770 (JA__, __).

With respect to traffic exchanged with wireless carriers and interstate traffic, other statutory sections provide additional, independent authority for the FCC to adopt its reforms. *See Order* ¶¶771, 779 (JA__, __) (citing 47 U.S.C. §§201(b), 332(c)(1)(B)).

As to all these points, the FCC's statutory interpretations are uniformly reasonable and should be affirmed under *Chevron USA, Inc. v. Natural Res.*

Def. Council, 467 U.S. 837, 842-43 (1984). *See Sorenson Commc'ns, Inc. v. FCC*, 659 F.3d 1035, 1042 (10th Cir. 2011).

B. The FCC reasonably concluded that the Act authorizes the bill-and-keep ratemaking methodology adopted in the *Order*. *Order* ¶¶771-776 (JA__-__).

Section 252(d)(2) expressly authorizes "arrangements that waive mutual recovery (*such as bill-and-keep arrangements*)." 47 U.S.C. §252(d)(2)(B)(i) (emphasis added). End-user charges under bill-and-keep also comply with the first sentence of section 201(b), which requires carrier rates to be "just and reasonable." *Id*. §201(b).

In the face of that language, petitioners nevertheless argue that they have a statutory right to be compensated *through charges to other carriers*. In fact, however, nothing in the statute compels the FCC to permit recovery of the costs of telecommunications traffic from other carriers, as opposed to end users or direct universal service subsidies. In the absence of such a clear statutory command, the FCC's reasonable result must be upheld.

II. The FCC was fully justified in adopting a recovery mechanism designed to enable ILECs to recover some – but not all – of the ICC revenues that are reduced under the new rules. *Order* ¶¶847-853 (JA__-__). Historical trends – which the FCC reasonably predicted were likely to continue in the absence of reform – showed that rate-of-return LECs were already losing access revenues at an annual rate of approximately 7 percent. *Order* ¶894 (JA__). The record also suggested that existing access charge levels – which, for rate-of-return carriers, reflected a 20-year-old 11.25 percent rate-of-return prescription – were overly generous. *Id.* ¶¶638, 892, 894 (JA__, __, __). In these circumstances, the FCC reasonably determined that limiting revenue reductions under ICC reform to 5 percent per year – less than had been occurring before the *Order* – would be "more than sufficient to provide carriers reasonable recovery for regulated services." *Id.* ¶924 (JA__). Contrary to petitioners' argument (Br. 49-50), there was no need formally to separate interstate and intrastate costs associated with the recovery mechanism, because all of the traffic at issue is subject to FCC jurisdiction.

III. The Act permits small LECs to petition state commissions to suspend or modify section 251(b) obligations upon demonstrating, among other things, that such relief would serve the "public interest." 47 U.S.C. §251(f)(2). Petitioners challenge the FCC's prediction (*Order* ¶824 (JA__)) that any future state commission decision to suspend or delay the bill-and-keep methodology would be "highly unlikely" to satisfy section 251(f)(2)'s "public interest" component. Br. 45-49. That claim is unripe because the agency's prediction is not final agency action. *See United States Telecom*

Ass'n v. FCC, 359 F.3d 554, 594 (D.C. Cir. 2004) ("*USTA*"). In any event, the FCC's explanation of the need to replace the ICC system fully justified its predictive statements regarding section 251(f)(2). *See Order* ¶¶741-759, 788-797, 824 (JA__-__, __-__, __).

IV.A. Petitioners provide no support for their contention (Br. 58) that the FCC violated the APA and principles of due process by relying on filings that lawfully were placed in the record. The FCC's permit-but-disclose filing rules are designed to enable the agency and the public to evaluate the record before the agency acts. The FCC followed those rules and gave all parties the "opportunity to participate" that the APA requires. 5 U.S.C. §553(c). Indeed, petitioners actively employed the agency's procedures to make numerous filings, including filings late in the proceeding.

B. The FCC has well-established authority to place conditions on the receipt of universal service subsidies. *TOPUC v. FCC*, 183 F.3d 393, 444 (5th Cir. 1999). Petitioners present no support for their contention (Br. 62-63) that certain universal service conditions and other requirements adopted in the *Order* unconstitutionally burden state sovereignty.

ARGUMENT

I. THE FCC REASONABLY DETERMINED THAT MULTIPLE PROVISIONS OF THE COMMUNICATIONS ACT AUTHORIZE THE ADOPTION OF A BILL-AND-KEEP RATEMAKING METHODOLOGY FOR THE EXCHANGE OF TELECOMMUNICATIONS WITH LECS.

Having detailed why bill-and-keep promotes the goals of the Communications Act, *see Order* ¶¶736-759 (JA__-__), the FCC also explained its legal authority to adopt it, *see id.* ¶¶760-781 (JA__-__). This legal analysis addresses two questions: (1) whether particular sources of regulatory authority reach the traffic at issue, and (2) whether those provisions permit bill-and-keep as a default methodology for that traffic. As to both questions, petitioners assert (Br. 3) that the FCC's statutory analysis fails under *Chevron* "step one." To succeed on such a challenge, petitioners must demonstrate that the statute "unambiguously forecloses the Commission's interpretation." *Nat'l Cable & Telecomms. Ass'n v. FCC*, 567 F.3d 659, 664 (D.C. Cir. 2009). Petitioners cannot show that the FCC breached any such unambiguous requirement. The agency's reasonable interpretation of the law, which comports with Congress's explicit policy goals, should be affirmed.

A. The FCC Reasonably Found That It Has Regulatory Authority To Establish The Applicable Ratemaking Regime For Telecommunications Exchanged With A LEC.

The FCC determined in the *Order* that it had rulemaking authority to establish a regulatory structure for "telecommunications" that a LEC delivers to or receives from another telecommunications provider in the course of originating or completing a call. The FCC further explained that its authority to establish rules as to that traffic flows directly from the last sentence of section 201(b), which grants the agency broad power to "prescribe such rules and regulations as may be necessary in the public interest to carry out the provisions of this Act." *Order* ¶760 (JA__) (quoting section 201(b)); *see AT&T*, 525 U.S. at 378 ("[T]he grant in §201(b) means what it says: The FCC has rulemaking authority to carry out the 'provisions of this Act,' which include §§251 and 252.").

As we demonstrate below, in adopting the *Order*'s ICC reforms, the FCC reasonably employed this broad grant of rulemaking power to implement three of the Act's substantive provisions: (1) section 251(b)(5), which imposes on LECs a "duty to establish reciprocal compensation arrangements for the transport and termination of telecommunications," *Order* ¶760 (JA__) (quoting section 251(b)(5)); (2) section 201(b), the first sentence of which requires that *interstate* communications traffic be provided on "just and reasonable" rates and terms, *id.* ¶771 (JA__) (quoting section 201(b)); and (3) section 332(c)(1)(B), which obligates LECs to interconnect with wireless carriers "pursuant to the provisions of section 201," *id.* ¶779 (JA__) (quoting section 332(c)(1)(B)).

1. Section 251(b)(5) Authorizes The FCC's Intercarrier Compensation Reforms.

The FCC lawfully concluded that its authority to adopt rules implementing section 251(b)(5) empowered it to establish a regulatory structure to govern how LECs are compensated when they exchange *any* telecommunications traffic that originates or terminates on their networks. Specifically, the FCC reasonably interpreted that provision to reach not just local traffic (*i.e.*, traffic exchanged between carriers operating within the same service area), but also to cover the exchange of access traffic involving the use of LEC facilities to originate or terminate long-distance calls (also known as interexchange or "IXC" traffic). *See Order* ¶¶761-762 (JA__-__). Petitioners' challenges (Br. 7-26) to the FCC's interpretation lack merit.

First, and most importantly, reading section 251(b)(5) to apply to interstate and intrastate traffic comports with the statutory text. Section 251(b)(5) provides, by its terms, that the traffic to which the reciprocal compensation regulatory structure applies is "the transport and termination of *telecommunications*." *Order* ¶761 (JA__) (emphasis added) (quoting section

251(b)(5)). "[T]elecommunications," in turn, is in no way limited to local traffic. It "means the 'transmission, between or among points specified by the user, of information of the user's choosing, without change in the form or content of the information as sent and received' *and thus encompasses communications traffic of any geographic scope (e.g., 'local,' 'intrastate,' or 'interstate') or regulatory classification (e.g., 'telephone exchange service,' 'telephone toll service,' or 'exchange access')*." *Id.* (emphasis added) (quoting 47 U.S.C. §153(43), (47), (48), (16)).

Moreover, when Congress wants to refer to narrower subsets of "telecommunications," it does so clearly. *See*, *e.g.*, 47 U.S.C. §254(d) (requiring carriers "that provide[] *interstate* telecommunications services" to contribute to the federal universal service fund (emphasis added)); *id.* §271(c)(2)(B)(iv) – (vi) (referencing "*local* loops," "*local* transport," and "*local* switching" (emphasis added)). The fact that Congress did not do so in section 251(b)(5) strongly supports the FCC's reading that that provision applies to all telecommunications exchanged with a LEC. *See United States v. Manatau*, 647 F.3d 1048, 1052 (10th Cir. 2011) ("Where Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion." (citation omitted)).

Petitioners' arguments are thus all contrary to the defined meaning of the specific term that Congress used – "telecommunications" – to establish the set of traffic subject to section 251(b)(5). Petitioners nevertheless claim (Br. 7-9) that section 251(b)(5)'s reference to "reciprocal compensation" indicates that that provision applies only to local (that is, non-access) traffic. The term "reciprocal compensation," however, does not establish the scope of section 251(b)(5) – that is what the broad, statutorily defined term "telecommunications" does. Rather, it refers to a *method* of compensation, specifically including the "bill-and-keep" methodology the FCC adopted here. *See* 47 U.S.C. §252(d)(2)(B)(i).

Nor can petitioners establish a clear statutory limitation on the traffic covered by section 251(b)(5) by suggesting that, historically, all access charge payments ran in one direction – from the IXC to the LEC, and never the other way around. Such payments, they assert, are not "reciprocal" in the sense of being made "by 'each to the other.'" Br. 10 (quoting dictionary definition). But the historical direction of access charge payments is merely a relic of the existing calling-party-network-pays ICC system that the *Order* replaces. There is no logical reason that compensation for this traffic must flow in only one direction, and Congress did not dictate any such result. Thus, even from its earliest orders construing the 1996 Act, the FCC has rejected the view that traffic direction controls the scope of section 251(b)(5). *See Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, 11 FCC Rcd 15499, 15517 ¶34, 15997 ¶1008 (1996) ("*Local Competition Order*") (ruling that the exchange of telecommunications between LECs and paging carriers is subject to section 251(b)(5), even though the flow of and compensation for that traffic ran in only one direction); *see also Pacific Bell v. Cook Telecom, Inc.*, 197 F.3d 1236, 1242-45 (9th Cir. 1999) (affirming as lawful the application of section 251(b)(5) to one-way traffic from a LEC to a paging carrier).

Petitioners also indirectly cite general trade press accounts (Br. 8 n.4) to suggest that the term "reciprocal compensation arrangement[]" in section 251(b)(5) was clearly understood in 1996 to extend only to local traffic and not to long-distance traffic. Br. 7-9. Those accounts, however, simply list early (pre-1996 Act) state commission efforts to accommodate the advent of competition in the local telephone markets within their jurisdictions by adopting "reciprocal compensation" regulatory structures, including "bill-and-keep." Those accounts of the existing regime in no way undermine the fact that section 251(b)(5) applies to all "telecommunications" or indicate that any regulatory structure under that provision *must* be confined to the exchange of local traffic.[3]

Petitioners similarly cite (Br. 9 n.5) a two-and-a-half-year-old "Issues of Interest" informational page on the FCC's public website, which describes how "reciprocal compensation" previously operated under FCC rules that *pre-dated* the *Order*. There is no dispute here that FCC rules under section 251(b)(5) previously applied more narrowly. That does not mean, however, that the statute plainly precludes the creation of a broader regime, as petitioners must establish to prevail on their *Chevron* Step I claim. As noted above, in fact, the statutory text strongly supports the FCC's authority to adopt a broader regime under section 251(b)(5). *See Order* ¶¶763-764 (JA__-__). Nothing petitioners have cited indicates that the statute must be read in a way that contradicts that text; accordingly, the FCC's reasonable interpretation must be upheld.

Nor is there merit to petitioners' contention (Br. 13) that the FCC's reading of section 251(b)(5) to reach beyond local telecommunications is an "unexplained departure from prior interpretations." The agency

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[3] *Cf. Jama v. Immigration & Customs Enforcement*, 543 U.S. 335, 349 (2005) (courts do not presume that Congress intended to incorporate prior judicial constructions unless "the supposed judicial consensus [is] so broad and unquestioned that [the Court] must presume Congress knew of and endorsed it").

acknowledged and explained its change of views. The FCC stated that it once had construed section 251(b)(5) "to 'apply only to traffic that originates and terminates within a local area.'" *Order* ¶761 (JA__) (quoting *Local Competition Order*, 11 FCC Rcd at 16013 ¶1034). But it changed its reading of the statute – and fully explained that change – more than a decade ago "[i]n the 2001 *ISP Remand Order*."[4] It "reiterated" that view in 2008 in the *Second ISP Remand Order*,[5] and "proposed [it again] in the [*2011 NPRM*]."[6] Finally, as discussed above (at 12-16), the FCC fully explained its current position in the *Order* on review. *See Order* ¶¶761-765 (JA__,__). *Chevron* requires no more. *See Rivera-Barrientos v. Holder*, 666 F.3d 641, 645 (10th Cir. 2012) (so long as an agency acknowledges its prior interpretation, review under *Chevron* is "no[] more searching where the agency's decision is a change from prior policy").

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[4] *Order* ¶761 (JA__) (citing *Intercarrier Compensation for ISP-Bound Traffic*, 16 FCC Rcd 9151, 9165-67 ¶¶31-34 (2001) ("*ISP Remand Order*")). The FCC explained in the *ISP Remand Order* that, but for the temporary preservation of access charge regulation in section 251(g), "section 251(b)(5) would require reciprocal compensation for transport and termination of *all* telecommunications traffic" exchanged with a LEC. 16 FCC Rcd at 9166 ¶32.

[5] *Order* ¶761 (JA__) (citing *Developing a Unified Intercarrier Compensation Regime*, 24 FCC Rcd 6475, 6479 ¶¶7-8 (2008) ("*Second ISP Remand Order*"), *aff'd*, *Core Commc'ns Inc. v. FCC*, 592 F.3d 139 (D.C. Cir. 2010).

[6] *Order* ¶761 (JA__) (citing *2011 NPRM* ¶514 (JA__-__)).

Although the broad scope of section 251(b)(5) itself is adequate to support the FCC's conclusion that it reaches exchange access traffic, that result is buttressed by the text of section 251(g). *Order* ¶¶763, 766 (JA__, __). Section 251(g) requires LECs to continue to "provide exchange access … to interexchange carriers … in accordance with the same equal access and nondiscriminatory interconnection restrictions and obligations (including receipt of compensation)" that were applicable prior to the 1996 Act "until such restrictions and obligations are explicitly superseded by regulations prescribed by the Commission." 47 U.S.C. §251(g). If section 251(b)(5), by its terms, did not otherwise reach exchange access traffic, there would have been no reason for Congress to enact section 251(g) to preserve the pre-existing access charge regime "until" the FCC affirmatively takes action to "supersede[]" that regime. *2011 NPRM* ¶514 (JA__). The very existence of section 251(g) thus suggests that Congress envisioned the kind of comprehensive reform the FCC adopted in the *Order*. Petitioners' narrow reading of section 251(b)(5), by contrast, would render section 251(g) essentially a nullity, contrary to established canons of statutory construction. *In re Dawes*, 652 F.3d 1236, 1242 (10th Cir. 2011) (statutes should be construed so that no part will be superfluous).

Petitioners nevertheless suggest that preservation of access charges for a time pursuant to section 251(g) somehow permanently limited the scope of section 251(b)(5). The FCC, however, reasonably concluded, in accord with its text, that section 251(g) "preserves access charge rules only during a *transitional* period, which ends when we adopt superseding regulations." *Order* ¶766 (JA__) (emphasis added); *see WorldCom, Inc. v. FCC*, 288 F.3d 429, 430 (D.C. Cir. 2002) (section 251(g) "is worded simply as a transitional device, preserving various LEC duties that antedated the 1996 Act until such time as the Commission should adopt new rules pursuant to the Act").

Nor does the fact that section 251(g) expressly preserves, among other things, interstate access charge regulations "of the [Federal Communications] Commission" for a transitional period, without mentioning state commission (that is, intrastate) access charge regulations, mandate that the FCC preserve the latter indefinitely. *See* Br. 23-25. To the contrary, if the absence of an express reference to intrastate access in section 251(g) were read to imply anything, it would be that Congress intended the broad language of section 251(b)(5) to displace the intrastate access regime immediately – without a transitional period. Such a reading would have limited practical effect today, however, given that "all traffic" exchanged with a LEC "will, going forward, be governed by section 251(b)(5) regardless of whether section 251(g) previously covered the state intrastate access regime." *Order* n.1374 (JA__).

In any event, the FCC explained that, although section 251(g) does not refer to intrastate access charge mechanisms by name, "it would be incongruous to conclude that Congress was concerned about the effects of the potential disruption to the interstate access charge system, but had no such concerns about the effects on analogous intrastate mechanisms." *Order* n.1374 (JA__) (quoting *Local Competition Order*, 11 FCC Rcd at 15869 ¶732). The FCC found support for this view in the fact that (1) section 251(g) expressly *does* preserve access charge mechanisms created by any "court order [or] consent decree," and (2) the court order accompanying the consent decree that broke up the Bell System "made clear that the decree required access charges to be used in both the interstate and intrastate jurisdictions." *Order* n.1374 (JA__) (citing *United States v. AT&T*, 552 F. Supp. 131, 169 n.161 (D.D.C. 1982)). "Because both the interstate and intrastate access charge systems were created by the same consent decree," the FCC explained, it is "reasonable to conclude that both systems were preserved by section 251(g)" until they are superseded by FCC regulations. *Order* n.1374 (JA__).

Finally, even if petitioners' section 251(g) arguments created an ambiguity as to the proper interpretation of the scope of section 251(b)(5), they again do not establish that the FCC violated a clear statutory command, and thus the agency's reasonable understanding of the relevant statutory provision should be affirmed under *Chevron.*

Petitioners are no more successful in arguing that section 251(b)(5) does not apply to *originating* access traffic. They claim that, because section 251(b)(5) addresses reciprocal compensation arrangements for "the transport and *termination* of telecommunications," not for the *origination* of telecommunications, Congress intended to exempt that traffic from the section 251(b)(5) regime. Br. 26. As the FCC has long determined, however, the absence of any reference to originating traffic means that – apart from access charge rules temporarily preserved by section 251(g) – the originating carrier is *barred* from charging another carrier for delivery of traffic that falls within the scope of section 251(b)(5). *See Local Competition Order*, 11 FCC Rcd at 16016 ¶1042 (finding that because section 251(b)(5) does not specify "charges payable to a carrier that originates traffic," it is best read to "prohibit[]" a LEC from "charg[ing] a [wireless] provider or other carrier for terminating LEC-originated traffic"); *Order* ¶817 (JA__) (reaffirming that view of section 251(b)(5) in the context of a bill-and-keep regime).

Relatedly, petitioners appear to argue (Br. 12-13, 26-27) that, because the FCC's initial discussion of section 251(b)(5) in the 1996 *Local Competition Order* separately defined "transport" and "termination" with reference only to "terminating traffic," the current *Order*'s conclusion that section 251(b)(5) reaches originating access is an unlawful *sub silentio* repeal of the agency's earlier definitions. Not so. The purpose of those definitions was not to narrow the scope of section 251(b)(5) traffic, but to establish that "transport and termination should be treated as two distinct functions," because each has "its own cost." *Local Competition Order*, 11 FCC Rcd at 16015-16 ¶¶1039-1040. Neither in form nor substance does the *Order* repeal those definitions.

2. Sections 201(b) And 332 Provide The FCC Independent Substantive Authority To Establish The *Order*'s Regulatory Framework.

For the reasons discussed above, petitioners' arguments that section 251(b)(5) does not reach some or all access traffic do not meet *Chevron* standards for overturning an agency decision. Even if their section 251(b)(5) argument were accepted, however, that would not prevent the FCC from establishing a regulatory framework for *interstate* access or for the exchange of *any* traffic, access or otherwise, between LECs and wireless providers.

a. Section 201(b) Provides The FCC Authority Over Interstate Traffic Exchanged With A LEC.

With respect to interstate traffic generally, the first sentence of section 201(b) of the Act empowers – indeed *requires* – the FCC to ensure that a carrier's rates and terms of service are "just and reasonable." 47 U.S.C. §201(b) (cited in *Order* ¶771 (JA__)). Section 201(b) thus supplies a separate and independent statutory basis to reach interstate traffic exchanged by a LEC.

Petitioners allege that section 201(b) is only a general provision that is trumped by the "specific instructions with respect to pricing" in sections 251(b)(5) and 252(d)(2). Br. 38. However, the D.C. Circuit rejected that same argument in upholding the FCC's prior reliance on section 201(b) as an independent basis for regulating traffic that also fell within the scope of section 251(b)(5). *Core*, 592 F.3d at 143-46. The court determined that "it is inaccurate to characterize §201 as a general grant of authority and §§251-252 as a specific one." *Id.* at 143. Rather:

> "When . . . two statutes apply to intersecting sets . . . , neither is more specific." *Hemenway v. Peabody Coal Co.*, 159 F.3d 255, 264 (7th Cir. 1998). That is the case here. Not all inter-LEC connections are used to deliver interstate communications, just as not all interstate communications involve an inter-LEC connection.

Core, 592 F.3d at 143-44. The court found added support for this reading in 47 U.S.C. §251(i), which provides that "[n]othing in this section shall be construed to limit or otherwise affect the [FCC's] authority under section 201." 592 F.3d at 143 (quoting section 251(i)). "Given th[e] overlap" between section 201(b) and 251(b)(5) traffic, the court determined that "§251(i)'s specific saving[s]" clause protects the FCC's authority under section 201(b) from "any negative implications from §251." *Id.* at 144; *accord Order* ¶¶770-771 (JA__-__) (citing *Core* and section 251(i)). Contrary to petitioners' assertion (Br. 40), nothing in the court's analysis is logically limited to the specific traffic at issue in that case (Internet Service Provider-bound traffic), which was just one subset of the overlapping "inter-LEC connection[s]" described in its analysis.

b. Section 332 Provides The FCC With Authority Over All Wireless Traffic Exchanged With A LEC.

The Eighth and D.C. Circuits have confirmed that 47 U.S.C. §332 provides the FCC with independent authority to establish reciprocal compensation terms with respect to wireless traffic exchanged with a LEC. *See Iowa Utils. Bd. v. FCC*, 120 F.3d 753, 800 n.21 (8th Cir. 1997), *vacated and remanded in part on other grounds*, *AT&T*, 525 U.S. 366; *MetroPCS California, LLC v. FCC*, 644 F.3d 410, 414 (D.C. Cir. 2011) (recognizing that the FCC "*can* issue [rate] guidance" under section 332 in connection with the exchange of intrastate traffic between LECs and wireless carriers, although it need not do so).

These holdings follow from the fact that section 332 "obligates LECs to interconnect with wireless providers 'pursuant to the provisions of section 201,'"[7] and preempts states from "regulating the entry of or the rates charged by [wireless] providers."[8] They also follow from the language in section 2(b) of the Act that "[e]xcept[s]" section 332 from any limitation on the FCC's jurisdiction over intrastate wireless communications that otherwise might apply.[9] Petitioners' brief nowhere challenges this basis for ICC reform.

3. The FCC's Statutory Authority Provides Ample Basis For The *Order*'s Narrow And Tailored Preemption Of State Regulation.

Relying on the proposition that preemption of state law is "not lightly to be presumed,"[10] as well as on two statutory provisions that assertedly limit the FCC's power to override pre-existing state regulations,[11] petitioners

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[7] *Order* ¶779 (JA__) (quoting 47 U.S.C. §332(c)(1)(B)).

[8] *Id.* (quoting 47 U.S.C. §332(c)(3)(A)).

[9] *Id.* (quoting 47 U.S.C. §152(b)).

[10] Br. 14 & nn.13-14.

[11] Br. 15-16 (citing the 1996 Act, §601(c)(1), and 47 U.S.C. §251(d)(3)).

contend that the FCC lacks the power to preempt state regulatory authority over intrastate access.

These claims are foreclosed by controlling Supreme Court precedent. The Court has squarely held that section 251 applies to both interstate and intrastate traffic, and section 251(b)(5), as discussed, applies broadly to all "telecommunications" traffic exchanged by LECs within both those categories. In *AT&T*, which involved (among other things) the claim that the FCC lacked authority to adopt regulations applying section 251(b)(5) to intrastate traffic, the Supreme Court acknowledged the existence of a "presumption against the pre-emption of state police power regulations" that would ordinarily require a "clear and manifest showing of congressional intent to supplant." 525 U.S. at 378 n.6. But the Court emphasized that section 251(b)(5) – among other provisions added by the 1996 Act – "unquestionably" has "taken the regulation of local telecommunications competition away from the States." *Id.* Moreover, Congress has "explicitly … given rulemaking authority" with respect to that provision to the FCC. *Id.* at 381 n.7; *see also id.* at 378 n.6, 381 n.8 (holding that the 1996 Act established a "new federal regime [that] is to be guided by federal-agency regulations" and "removed a significant area from States' exclusive control").[12]

In this regard, petitioners notably do not dispute that the reference to "telecommunications" in section 251(b)(5) displaces state regulation of local (non-access) intrastate traffic exchanged by LECs; in fact, they (wrongly) contend (Br. 10) that it applies only to that form of intrastate traffic. Nothing in the text of that provision suggests that Congress intended to include one species of intrastate traffic but exclude another within the scope of federal regulation (more specifically, to cover intrastate *local* traffic while leaving out intrastate *access* traffic). Petitioners' argument thus relies on a distinction between types of intrastate traffic that has no basis in the statutory text.

Petitioners also contend that section 601(c)(1) of the 1996 Act – which provides that "[t]his [1996] Act and the amendments made by this Act shall not be construed to modify, impair, or supersede Federal, State, or local law unless expressly so provided in such Act or amendments" – prevents the FCC

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[12] The Supreme Court in *AT&T* also rejected the argument, which petitioners make only in passing here (Br. 14, 19), that section 2(b) of the Act and *Louisiana PSC v. FCC*, 476 U.S. 355 (1986), deny the FCC authority to implement section 251(b)(5) with respect to intrastate matters. *See AT&T*, 525 U.S. at 378-81; *Order* ¶760 (JA__). Although *AT&T* did not specifically address intrastate *access* service, its analysis applies with equal force here: as explained above, such service falls comfortably within the term "telecommunications" in section 251(b)(5).

from applying section 251(b)(5) to preempt state regulation of intrastate access charges. Br. 15. No party raised the section 601(c)(1) issue before the FCC. Judicial review of that question thus is barred by 47 U.S.C. §405(a), which prevents review of "questions of fact or law upon which the Commission ... has been afforded no opportunity to pass." *E.g.*, *Sorenson*, 659 F.3d at 1044 (quoting section 405(a)).

The claim is baseless in any event. Courts have properly read section 601(c)(1) narrowly, because "it is a general rule in preemption analysis that a savings provision does not 'bar the ordinary working of conflict preemption principles' ... lest [it] 'permit[a] law to defeat its own objectives, or potentially ... to destroy itself.'" *Farina v. Nokia Inc.*, 625 F.3d 97, 131 (3d Cir. 2010) (quoting *Geier v. Am. Honda Motor Co.*, 529 U.S. 861, 869, 872 (2000)); *accord Qwest Corp. v. Minn. Pub. Utils. Comm'n*, 684 F.3d 721, 731 (8th Cir. 2012). Section 251(b)(5), by its terms, applies to all "telecommunications" traffic exchanged by a LEC, and the access traffic that LECs exchange with other providers indisputably is "telecommunications," as that term is defined in the Communications Act. Moreover, section 251(g) expressly contemplates that the FCC will adopt new regulations "supersed[ing]" existing exchange access rules, including those governing "receipt of compensation." 47 U.S.C. §251(g). Accordingly, ordinary conflict preemption principles displace intrastate access charge regulation here, and section 601(c)(1) does not apply.

Petitioners also incorrectly assert (Br. 16-19) that section 251(d)(3) of the Communications Act bars preemption of state access charge regulation. That section preserves any regulation, order, or policy of a state commission that:

> (A) establishes access and interconnection obligations of local exchange carriers; (B) is consistent with the requirements of this section [251]; and (C) does not substantially prevent implementation of the requirements of this section and the purposes of this part [sections 251 through 261 of the Communications Act].

47 U.S.C. §251(d)(3).

Section 251(d)(3), as a threshold matter, is inapplicable here because it "addresses state authority to prescribe regulations relating to [network element] unbundling" by incumbent LECs for the benefit of new "competitive" LECs ("CLECs"), as provided in the 1996 Act.[13] *See* 47 U.S.C. §251(c)(3) & (d)(2) (providing for network element unbundling); *see also id.* §153(35) (defining "network element"). The "access" at issue under section 251(d)(3) is thus "access" to "network elements," which are piece-parts of ILEC telephone networks that Congress authorized CLECs to lease to

[13] *BellSouth Telecommunications, Inc. Request for Declaratory Ruling*, 20 FCC Rcd 6830, 6841 ¶23 (2005).

provide competing services. The provision is not relevant to the wholly distinct issue of access charges for delivering interexchange traffic.

The text and structure of section 251(d) support this understanding. Section 251(d)(2), the immediately preceding subsection, is titled "Access standards" and requires the FCC to consider whether "access" to ILEC *network elements* should be required. *See* 47 U.S.C. §251(d)(2). Thus, when section 251(d)(3) refers to "access … obligations of local exchange carriers," it is referring back to access to network elements, not to the distinct issue of access charges for interexchange service.

Even if that were incorrect, however, there is no merit to petitioners' assertion (Br. 16) that the FCC "conduct[ed] no analysis of §251(d)(3) and fail[ed] to articulate any criterion that allows the agency to override this express reservation of State authority." To the contrary, the agency explained that "section 251(d)(3) does not speak to the preemptive effect of the statute" itself. *Order* n.1374 (JA__); *see id.* ¶¶767-768 (JA__-__). Because intrastate access involves "telecommunications" exchanged with a LEC within the meaning of section 251(b)(5), the statute itself preempts states' intrastate access charge regimes, except as temporarily preserved by section 251(g). *See Order* ¶¶761-762 (JA__-__).

Finally, section 251(d)(3) cannot bar the preemptive force of the FCC's ICC reforms because that provision does not preserve state regulations that "substantially prevent *implementation* of the requirements of this section and the purposes of [sections 251 through 261]," 47 U.S.C. §251(d)(3)(C) (emphasis added).[14] As discussed above (at 1-5), the FCC determined in the *Order* that a uniform national approach that brings all telecommunications traffic exchanged by LECs within the section 251(b)(5) framework would best implement "the objectives of section 251(b)(5) and other provisions of the Act." *Order* ¶767 (JA__). State-by-state departures from that approach would "substantially prevent implementation" of a national framework. *Id.* ¶¶767, 793-794, 824 (JA__, __-__, __); *cf. Verizon New England, Inc. v. Me. Pub. Utils. Comm'n*, 509 F.3d 1, 5, 12 (1st Cir. 2007) (holding that "state agency may [not] require [ILECs to offer certain unbundled network] elements that the FCC has delisted" as a matter of national policy).

Citing Pennsylvania's regime of access charge regulation and the state's broadband deployment efforts by way of general example, petitioners contend that there was "[n]o record evidence" that state regulation would interfere with federal intercarrier compensation reforms. Br. 21-23.

[14] *Order* ¶767 (JA__) (citing, *e.g.*, *Local Competition Order*, 11 FCC Rcd at 15550 ¶103).

Regardless of the activities of any one state, there was substantial record evidence supporting the FCC's conclusion that "a uniform national framework for the transition of intercarrier compensation to bill-and-keep" was warranted to advance the legitimate goals of "accelerating the migration to all-IP networks, facilitating IP-to-IP interconnection, and promoting deployment of new broadband networks by providing certainty and predictability to carriers and investors." *Order* ¶790 (JA__).

In particular, the record established that intrastate access rates "vary widely" – creating "incentives for arbitrage and pervasive competitive distortions within the industry." *Order* ¶791 & nn.1467-68 (JA__). Moreover, the states that have initiated intrastate access reforms "have taken a variety of approaches," *id.* ¶794 & nn.1473-76 (JA__), while some state commissions "lack authority to address intrastate access reform" at all, *id.* ¶794 & n.1478 (JA__). As a consequence, the FCC determined (with some state support in the record) that "a state-by-state process would likely result in significant variability and unpredictability of outcomes," *id.* ¶794 & n.1479 (JA__), while a uniform nationwide approach would "ensure that the intercarrier compensation modernization effort will continue apace without unnecessary delays needed to harmonize disparate state actions," *id.* ¶793 (JA__).

B. The FCC Reasonably Concluded That It Has Regulatory Authority To Adopt Bill-And-Keep As The Default For Telecommunications Exchanged With A LEC.

1. The Bill-And-Keep Methodology Is Consistent With Section 252(d)(2) Ratemaking Standards.

The Communications Act itself identifies bill-and-keep as a permissible ratemaking methodology. Specifically, section 252(d)(2)(A) states that a "just and reasonable" recovery under that section must include "mutual and reciprocal recovery by each carrier of costs associated with … transport and termination." 47 U.S.C. §252(d)(2)(A). Crucially, section 252(d)(2)(B) then states that section 252(d)(2) "shall not be construed" to "preclude" "arrangements … that waive mutual recovery (such as bill-and-keep arrangements)." 47 U.S.C. §252(d)(2)(B). That should be the end of the matter. Congress explicitly contemplated that the specific methodology of bill-and-keep would be permissible, *i.e.*, would not be precluded.

Moreover, beyond its reliance on that explicit statutory authorization of bill-and-keep, the FCC reasonably concluded that such a methodology ensures "just and reasonable" compensation and "mutual and reciprocal recovery by each carrier of costs" associated with transport and termination, as contemplated by section 252(d)(2)(A)(i). The FCC explained that the statute "does not specify from whom each carrier may (or must) recover those costs." *Order* ¶775 (JA__). The FCC thus found that the statute permits it to establish a regime in which "each carrier will 'recover' its costs from its own end users or from explicit support mechanisms such as the federal universal service fund." *Id.* Such recovery would be "reciprocal" within the meaning of section 252(d)(2) because "a bill-and-keep framework" entitles carriers exchanging traffic "to recover their costs through the same mechanism, *i.e.*, through the rates they charge their own customers." *Id.* n.1408 (JA__).

This reading of "reciprocal" also comports with standard dictionary definitions. *See* Webster's Third New Int'l Dictionary 1895 (2002) (defining "reciprocal" to mean "corresponding to each other: being equivalent or complementary"). Bill-and-keep meets this definition because, under such arrangements, both carriers recover their costs from "equivalent" sources – their own customers.

Petitioners nevertheless contend (Br. 36-37) that adopting bill-and-keep as the default for all telecommunications exchanged with a LEC departs without explanation from the FCC's 1996 view that, in general, bill-and-keep would be consistent with section 252(d)(2) only when rates are symmetrical and the traffic in each direction is roughly in balance. *See Local Competition Order*, 11 FCC Rcd at 16055 ¶1112. Although the FCC did depart from that position in the *Order*, it acknowledged and fully explained the departure. *Order* ¶¶756, 774 n.1405 (JA__, __).

The prior position was predicated on the view, rejected in the *Order*, "that the calling party's network should bear all the costs of a call." *Order* ¶756 (JA__). Given the FCC's finding "that both the calling and called party benefit from a call, the 'direction' of the traffic" – and thus its relative balance – "is no longer relevant." *Id.* "Additionally," the FCC explained, "bill-and-keep is most consistent with the models used for wireless and IP networks … that have flourished and promoted innovation and investment without any symmetry or balanced traffic." *Id.*

Further supporting its rejection of a traffic symmetry requirement, the FCC found that new technology makes the incremental cost of call termination "very near $0." *Order* ¶¶746 & n.1309, 752-753 (JA__, __-__). Even in its earlier analysis of the issue, the FCC had recognized that slight differences in traffic balance or relative costs could be outweighed by the "administrative burdens and transaction costs" associated with calculating ICC payments. *Local Competition Order*, 11 FCC Rcd at 16055 ¶1112. Reprising that earlier theme, the FCC explained that "[e]xact identification of efficient termination charges would be extremely complex," and the "costs of metering, billing, and contract enforcement that come with a non-zero termination charge" would be significant. *Order* ¶753 (JA__). Given these difficulties and the fact that the cost of termination was likely "very nearly zero," the FCC determined that any "benefits obtained from imposing even a very careful estimate of the efficient interconnection charge would be more than offset by the considerable costs of doing so." *Id.* In short, the FCC acknowledged and fully justified its changed position on the application of bill-and-keep. That is all the APA requires. *See Qwest Corp. v. FCC*, 689 F.3d 1214, 1224 (10th Cir. 2012).

Petitioners further assert (Br. 36) that, for traffic subject to section 252(d)(2), the statutory reference to "waive[r]" of mutual recovery means that bill-and-keep may only be voluntarily adopted, and may not be imposed by regulation. But the FCC reasonably determined that such a construction would render Congress's express endorsement of the bill-and-keep ratemaking methodology "superfluous" because, under the statute, the section 252(d)(2) pricing standards apply *only* to terms imposed by arbitration, and not to "voluntarily-negotiated agreements." *Order* n.1407 (JA__).

In particular, section 252(c) provides that "[i]n resolving *by arbitration* under subsection (b) of this section any open issues …, a State commission shall – … (2) establish any rates … *according to subsection (d)*." 47 U.S.C. §252(c) (emphasis added). By contrast, section 252(a)(1) provides that "an incumbent local exchange carrier may *negotiate* and enter into a binding agreement with the requesting telecommunications carrier or carriers *without* *regard* to the standards set forth in subsections (b) and (c) of section 251 [which include reciprocal compensation]." *Id.* §252(a)(1) (emphasis added); *see Qwest Corp. v. Pub. Utils. Comm'n of Colorado*, 479 F.3d 1184, 1188 (10th Cir. 2007) (voluntary agreements may "contradict the specific statutory requirements that an incumbent must follow").

Accordingly, petitioners' argument that the statutory reference to bill-and-keep applies only to voluntary agreements has it exactly backwards. *See MCI Telecomms. Corp. v. U.S. West Commc'ns*, 204 F.3d 1262, 1270-71 (9th Cir. 2000) (upholding state arbitrator's imposition of bill-and-keep under section 252(d)(2)). At the very least, their argument does not show that the FCC's contrary understanding conflicts with the plain meaning of the statute or is so unsupported as to be unreasonable, as would be necessary to prevail under *Chevron*.

2. Section 201(b) Independently Authorizes Bill-And-Keep As A Ratemaking Methodology For Interstate Traffic.

Section 201(b) provides, with respect to communications common carriers engaged in interstate or foreign communications by wire or radio, that "[a]ll charges, practices, classifications, and regulations for and in connection with such communication service, shall be just and reasonable." 47 U.S.C. §201(b). The "generality" of the terms "just and reasonable" "opens a rather large area for the free play of agency discretion." *Bell Atl. Tel. Cos. v. FCC*, 79 F.3d 1195, 1202 (D.C. Cir. 1996). That discretion is cabined only by the requirement that the FCC engage in reasoned decisionmaking and that it produce a constitutional "end result." *Id.* (citing *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944)).

In the *Order*, the FCC determined that the adoption of bill-and-keep for interstate traffic exchanged with a LEC was fully consistent with this flexible ratemaking standard. *Order* ¶771 (JA__). In particular, because bill-and-keep allows carriers to charge their own end users "just and reasonable" rates for the transport and termination of interstate traffic, section 201(b) authorized that ratemaking method. *Id.*

Petitioners contend (Br. 41) that, by phasing out ICC payments from the originating carrier to the terminating carrier, bill-and-keep fails section 201(b)'s "just and reasonable" rate standard. This argument wrongly assumes, however, that the only relevant source of compensation for purposes of section 201(b) is the carrier with which the LEC exchanges traffic. Nothing in section 201(b) compels that result – which is a relic of the calling-party-network-pays regime that the FCC's new bill-and-keep framework replaces for local and access traffic. *See Order* ¶¶771, 775 n.1409 (JA__, __). Under the new regime, carriers are free to recover their costs with just and reasonable charges to their end users. The FCC's conclusion that bill-and-keep comports with section 201(b) is reasonable and entitled to *Chevron* deference. *Rivera-Barrientos*, 666 F.3d at 645.[15]

Finally, this Court should reject petitioners' contention (Br. 43-44) that the FCC may not, under section 201(b), prescribe "just and reasonable" rates for the exchange of interstate traffic without first conducting a rate prescription proceeding under 47 U.S.C. §205. Section 205 provides remedies that may be available when the FCC investigates the lawfulness of an individual carrier's rates, such as those filed under tariff pursuant to section 203 of the Act. *See* 47 U.S.C. §§203, 205. Section 205 does not limit the FCC's authority to adopt general pricing methodologies using its section 201 ratemaking and rulemaking authority. *See Global Crossing Telecomms., Inc. v. Metrophones Telecomms., Inc.*, 550 U.S. 45, 53 (2007) (providing that FCC can implement section 201(b) either through section 205 rate prescription or through general "rules that … insist upon certain carrier practices"). Indeed, as noted in the *Order* (¶641 (JA__)), the agency previously has capped rate levels through general notice-and-comment

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[15] Petitioners contend that, because section 332 incorporates the standards of section 201, section 332 provides no authority to adopt bill-and-keep with respect to wireless traffic. Br. 44. This contention fails for the same reasons as petitioners' section 201(b) argument.

rulemaking proceedings, rather than through hearings on particular tariff filings.[16]

AT&T Co. v. FCC, 487 F.2d 865 (2d Cir. 1973), is not to the contrary. *See* Br. 44. That case simply "held that the Commission may not require a carrier to seek permission to file a tariff effecting a rate increase, but instead must process such a tariff in accordance with the procedures set forth in sections 203 to 205 of the Act." *Order* n.1390 (JA__). "Nothing in that decision calls into question" the FCC's "authority to adopt rules to define what constitutes a just and reasonable rate for purposes of section 201." *Id.* In any event, even if section 205 were applicable to the ratemaking rules adopted in the *Order*, the notice-and-comment procedures the FCC employed here fully satisfied the hearing requirements of that provision. *See AT&T v. FCC*, 572 F.2d 17, 22 (2d Cir. 1978) (holding that notice-and-comment provides a "full opportunity to be heard" sufficient under section 205); *Order*

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[16] *See, e.g.*, *Access Charge Reform*, 12 FCC Rcd 15982, 16012-18 ¶¶75-87 (1997) (prescribing new limits on subscriber line charges through general rulemaking procedures), *aff'd*, *Sw. Bell Tel. Co. v. FCC*, 153 F.3d 523 (8th Cir. 1998); *Access Charge Reform*, 15 FCC Rcd 12962, 12984 ¶58, 12988-991 ¶¶70-75 (2000) (prescribing revised rate ceilings through general rulemaking procedures), *aff'd in pertinent part*, *TOPUC v. FCC*, 265 F.3d 313 (5th Cir. 2001).

¶641 (JA__) ("[A] formal evidentiary hearing is not required under section 205.").[17]

3. The FCC's Bill-And-Keep Framework Does Not Impermissibly Intrude On State Authority To Establish Actual Rates.

Petitioners argue that bill-and-keep is a rate (as opposed to a methodology), and that sections 252(c)(2) and 252(d)(2) permit only a state entity, not the FCC, to impose such a rate. In this regard, petitioners analogize bill-and-keep to the default proxies that the FCC established in 1996 and that the Eighth Circuit struck down in *Iowa Utils. Bd. v. FCC*, 219 F.3d 744, 757 (8th Cir. 2000).

That analogy does not withstand scrutiny. The FCC considered the Eight Circuit precedent but reasonably determined that, unlike the default proxies – which established the full and specific amount of compensation that carriers could receive – its bill-and-keep framework does not impermissibly "intrude[] on the states' right to set the actual rates pursuant to §252(c)(2)." *Order* ¶773 (JA__) (quoting *Iowa Utils. Bd.*, 219 F.3d at 757). In this regard,

[17] Petitioners' undeveloped two-sentence claim (Br. 45) that the FCC unlawfully amended its Part 36 rules without a Joint Board referral overlaps claims presented at greater length in the petitioners' Additional Universal Service Fund Issues Brief. It is addressed in our response to that brief. *See* FCC Additional USF Issues Brief, Argument II.

the FCC's action was lawful both as to the interim transitional rate caps set by the *Order* and as to the ultimate bill-and-keep framework.

Although the FCC's interim regime caps some of the rates states may establish for *intercarrier* compensation, that is so only because the agency sensibly decided to transition to bill-and-keep gradually, rather than adopting a "flash cut" that could "entail significant market disruption." *Order* ¶¶809-810 (JA__-__). The FCC has well-established discretion to exercise statutory powers flexibly when moving from one regulatory regime to another. *See NARUC v. FCC*, 737 F.2d 1095, 1135-36 (D.C. Cir. 1984). Thus, although the FCC could, under the statute, have "mov[ed] to bill-and-keep immediately," *Order* ¶809 (JA__), its decision to move gradually was reasonable and is entitled to "substantial deference," *id.* (quoting *Rural Cellular Ass'n v. FCC*, 588 F.3d 1095, 1106 (D.C. Cir. 2009)).

Moreover, the effect of the intercarrier rate caps the FCC imposed is not to prescribe the precise *amount* carriers may charge for section 251(b)(5) traffic, but to control the *source* of a carrier's section 251(b)(5) revenues – a quintessential methodological issue. Specifically, the caps do not determine how much carriers may collect for transporting and terminating traffic; they simply require that any further recovery come from end users, not other carriers. Significantly, with respect to intrastate traffic, states retain authority "to regulate the rates that the carriers will charge *their end users* to recover the costs of transport and termination." *Order* ¶776 (JA__). Accordingly, state commissions ultimately have discretion and responsibility (subject to federal standards) in determining the aggregate amount carriers may recover for section 251(b)(5) traffic.

Furthermore, state commissions retain additional "important responsibilities in the implementation of a bill-and-keep framework," such as determining the point on the terminating carrier's network – known as the "edge" – to which a carrier must deliver traffic "to avail itself of bill-and-keep." *Order* ¶776 (JA__). This determination has significant implications for intercarrier compensation. The FCC explained that, "[d]epending upon how the 'edge' is defined … [intercarrier] payments still could change hands." *Id.* Because states will make that determination in arbitration proceedings, the FCC's conclusion is consistent with the Supreme Court's statement that the states "determin[e] the concrete result in particular circumstances." *Id.* (quoting *AT&T*, 525 U.S. at 384).

In any event, the FCC also concluded that the rate-versus-methodology limitation of sections 252(c) and (d) does not control the agency's authority with respect to "most of the traffic that is the focus of this *Order*." *Order* ¶774 (JA__). First, the distinction between rate and methodology has no bearing on the interstate and wireless traffic for which the FCC has independent regulatory authority under sections 201(b) and 332. *See id.* ¶¶771, 779 (JA__, __) (recognizing independent authority under those sections).

Moreover, even where section 251(b)(5) provides the FCC's sole source of authority, the distinction has limited significance. Section 252 applies only to arbitration proceedings involving "traffic exchanged with an *ILEC*," the former monopoly provider in each local area. *Id.* ¶774 (JA__) (emphasis added); *see* 47 U.S.C. §252(b)(1) (providing that an *ILEC*'s receipt of "a request for negotiation" triggers application of section 252 procedures); *id.* §252(c)(2) (providing that in resolving arbitrations "*under subsection (b)*," state commissions shall "establish" rates "according to subsection (d)" (emphasis added)); *id.* §252(d)(2) (establishing ratemaking standard "[f]or the purposes of compliance *by an incumbent local exchange carrier* with section 251(b)(5)" (emphasis added)). Thus, traffic exchanged between CLECs and IXCs, between two CLECs, and between CLECs and wireless providers are all "categorically beyond [the] scope" of the pricing provisions of section 252(c) and (d). *See Order* ¶774 (JA__).

Finally, the *Order* explains that even some ILEC traffic – specifically, that exchanged between ILECs and IXCs – is excluded from the rate-versus-methodology limitation. The section 252(d) pricing standard applies, by its terms, only where the traffic "originate[s] on the network facilities of the other carrier." 47 U.S.C. §252(d)(2)(A)(i). IXCs, however, "typically do not originate (or terminate) calls on their own network facilities but instead transmit calls that originate and terminate on distant LECs." *Order* ¶774 (JA__). Accordingly, the bill-and-keep framework the FCC adopted does "not implicate any question of the states' authority under section 252(c) or (d) or the Eighth Circuit's interpretation of those provisions," even as to most traffic exchanged between ILECs and IXCs. *Id.*

II. THE RECOVERY MECHANISM ADOPTED IN THE *ORDER* IS A REASONABLE INTERIM MEASURE TO OFFSET REDUCED INTERCARRIER COMPENSATION REVENUES DURING THE TRANSITION TO BILL-AND-KEEP.

The *Order* establishes a multi-year transition to bill-and-keep that initially caps existing intercarrier rates for terminating access and local traffic at existing levels, and then gradually reduces those rates each year until they reach bill-and-keep (in six years for price cap carriers, and nine years for rate-of-return carriers). *See Order* ¶801 & Figure 9 (JA__, __). The FCC sought further comment on how to transition to bill-and-keep for originating access and other rate elements not specifically affected by the *Order*. *Id.* ¶¶1297-1305 (JA__-__). In the meantime, the *Order* caps all originating access charges for price cap carriers and interstate originating switched access charges for rate-of-return carriers. *Id.* ¶¶739, 800-801 & Figure 9 (JA__, __-__).

To mitigate the effect of its reforms on incumbent LECs' revenues, the FCC created a "recovery mechanism" designed to enable those LECs to recover some of the ICC revenues that are reduced during the transition to bill-and-keep. *Order* ¶¶847-853 (JA__-__). For rate-of-return LECs,[18] the *Order* establishes a formula that determines eligible revenues on the basis of an initial baseline, consisting of (a) the carrier's 2011 revenue requirement for the interstate access elements subject to reform, (b) the carrier's Fiscal Year 2011 revenues from the intrastate access elements subject to reform, plus (c) the carrier's net reciprocal compensation revenues for Fiscal Year 2011 (generated under the FCC's prior reciprocal compensation rules governing local traffic). *See id.* ¶¶851, 892, 899 (JA__, __, __). Each rate-of-return ILEC is entitled to recover that amount – which is reduced by 5 percent each year. *See id.* ¶¶851, 899 (JA__, __).

This revenue recovery comes from three sources. First, carriers receive revenues from their remaining ICC charges, some of which are not currently

[18] Petitioners, which (on this issue) consist mainly of rural rate-of-return carriers, do not challenge the recovery mechanism as it applies to price cap carriers. *See* Br. 52-57.

being transitioned to bill-and-keep. *Order* ¶896 (JA__).[19] Second, carriers may recover revenues by assessing a new, federally tariffed Access Recovery Charge ("ARC") on their end users (subject to certain limitations). *See id.* ¶¶896, 906-916 (JA__, __-__). Finally, if the remaining ICC charges and the ARC do not produce all of the revenues eligible for recovery, carriers may recover the remainder through direct subsidies from the Connect America Fund ("CAF"), which was created as part of the *Order*'s universal service reforms. *See id.* ¶¶896, 917-919 (JA__, __-__).

The FCC predicted that this recovery mechanism "will be more than sufficient to provide carriers reasonable recovery for regulated services." *Order* ¶924 (JA__). Nevertheless, as an added measure of protection, the FCC provided for a "Total Cost and Earnings Review" process "to allow individual carriers to demonstrate that ... additional recovery is needed to prevent a taking." *Id.*

Petitioners challenge the bill-and-keep transition and the recovery mechanism as arbitrary and capricious on several grounds. First, citing *Smith v. Illinois Bell Tel. Co.*, 282 U.S. 133 (1930), petitioners contend that the FCC arbitrarily failed to apportion the costs of the services subject to reform between the state and federal jurisdictions. Br. 49-50. In *Smith*, the Illinois

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[19] *See Order* ¶801 (JA__) (outlining transition schedule).

regulatory agency had set Chicago telephone rates based on the total cost of the telephone company's property in the city, even though that property was used to provide not just intrastate service, but also interstate service. *See* 282 U.S. at 146-47. The statutory scheme for telephone regulation then in place, however, granted the federal Interstate Commerce Commission *exclusive* jurisdiction over interstate communications and the various state commissions jurisdiction only over intrastate communications. *See id.* at 148-49. The Court ruled that, although "extreme nicety is not required" in separating regulated costs between jurisdictions, the Illinois agency's decision to set local rates on the basis of the *total* (interstate and intrastate) cost of the carrier's property improperly "ignore[d] *altogether* the actual uses to which property is put." *Id.* at 150 (emphasis added). The Court thus set aside the rate order, finding, on those facts, that "separation of the intrastate and interstate property, revenues and expenses of the company" was "essential to the appropriate recognition of the competent governmental authority in each field of regulation." *Id.* at 148.

Smith is inapplicable here. First, while the statutory scheme in that case gave the Interstate Commerce Commission exclusive jurisdiction over interstate communications, sections 251(b)(5) and 201(b) give the FCC jurisdiction over *all* of the traffic subject to reform – both interstate and intrastate. *See AT&T*, 525 U.S. at 381 n.7; *see also* Argument I.A., above. Moreover, although the *Order* asserts jurisdiction over some intrastate access traffic that previously was regulated by the states, states are *not* left with responsibility for recovering intrastate access revenues that are reduced by ICC reform. *Order* ¶795 (JA__). Rather, the *Order*'s federal recovery mechanism "provide[s] carriers with recovery for reductions to eligible interstate *and* intrastate revenue." *Id.*; *see id*. ¶¶847-920 (JA__-__). Thus, far from "ignor[ing] altogether," *Smith*, 282 U.S. at 150, the use to which carrier property is put, that mechanism takes into account the previously separated costs of section 251(b)(5) traffic by starting the transition to bill-and-keep with existing interstate and intrastate rates and determining eligible revenue recovery on the basis of a formula that is tied initially to existing interstate and intrastate revenues, *see Order* ¶892 (JA__). And the additional safeguard of the Total Cost and Earnings Review process – which includes a separations study requirement – permits carriers to make a comprehensive cost showing *to the FCC* that additional recovery is needed. *See id.* ¶¶924, 932 (JA__, __). Accordingly, no formal reapportionment was necessary, at this time, to ensure that only "the competent governmental authority" exercises jurisdiction. *Smith*, 282 U.S. at 148.

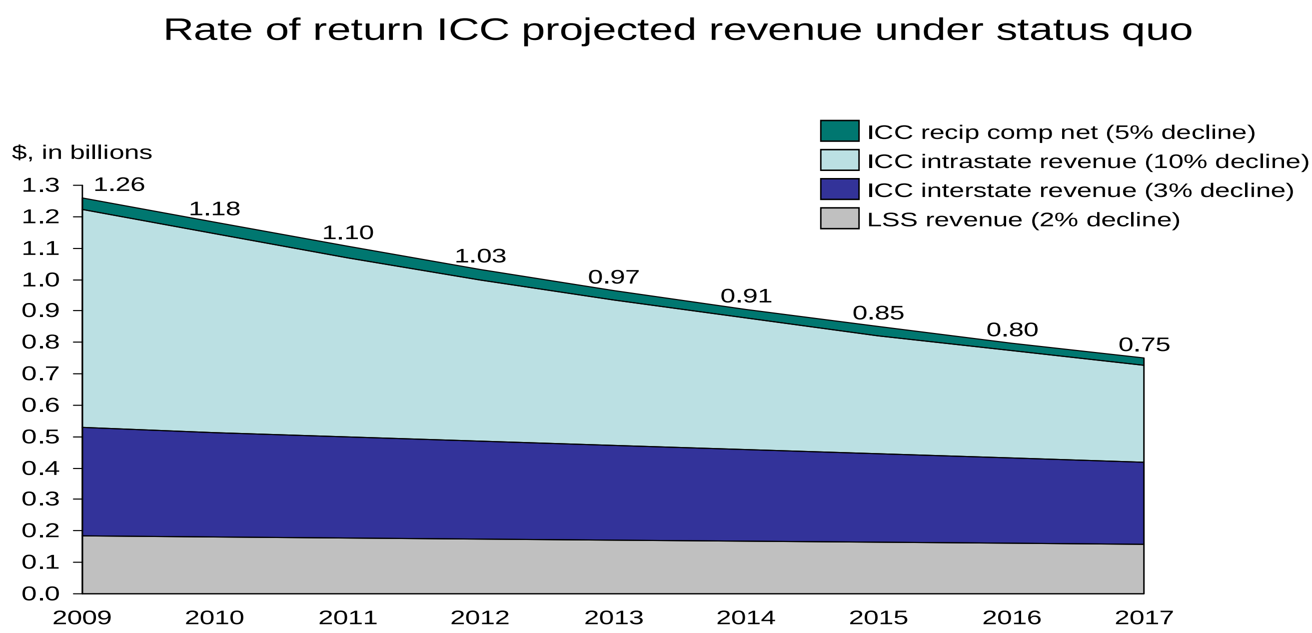
Petitioners' remaining arbitrary-and-capricious claims – apparently intended to show that the recovery mechanism denies carriers an opportunity to recover their costs – consist largely of undeveloped references to decades-old FCC decisions addressing past regulatory policies. *See generally* Br. 51-56 (citing various FCC access charge orders from 1986, 1990, 1998, 2000, and 2001). Nothing in the cited references suggests that the fully articulated reforms adopted in the *Order* are unreasonable, especially in light of intervening statutory and technological changes, and the deference due to transitional mechanisms.

In this regard, the FCC's recovery mechanism, by design, does not "provide 100 percent revenue neutrality relative to today's revenues." *Order* ¶881 (JA__). The agency nevertheless reasonably predicted that it would be "more than sufficient to provide carriers reasonable recovery for regulated services." *Id.* ¶924 (JA___).

Numerous factors supported that conclusion. First, an annual 5 percent decline in revenues was likely an *improvement* over recent trends. The FCC observed that interstate access revenue requirements for rate-of-return carriers recently had declined on average by 3 percent per year, and projections in the record suggested that that trend would continue for the next five years. *Order* ¶892 (JA__). At the same time, intrastate access revenues for rate-of-return carriers had been declining by about 10 percent per year. *Id.* ¶893 (JA__).[20] The FCC determined that a weighted average of these interstate and intrastate revenue declines "could justify a possible Baseline reduction of approximately seven percent annually." *Id.* ¶894 (JA__). The selection of a 5 percent annual reduction for the recovery mechanism was thus "a conservative approach." *Id.* ¶¶894, 900-901 (JA__, __-__). The chart below illustrates rate-of-return LECs' projected revenue losses under the status quo.

[20] The downward trends in interstate and intrastate access revenues had resulted largely from the combined effects of lost lines and minutes of use to competitors (*e.g.*, wireless and VoIP providers) and decreasing switching costs. *See Order* ¶¶885-886, 892-894 (JA__-__, __-__).

Id. ¶893, Figure 11 (JA__).[21]



In addition, the FCC had sound reasons to believe that existing access charge rates were above levels required for efficient operation. Because the existing regime permitted rate-of-return ILECs to increase their rates to offset declining minutes of use, such carriers "had insufficient incentive to reduce costs." *Order* ¶892 (JA__). Those incentives are reversed under the new recovery mechanism, because "carriers that realize … efficiencies will not experience a resulting reduction in support" (beyond the 5 percent annual

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[21] "LSS" in the chart refers to Local Switching Support explicit subsidies. *See Order* ¶892 (JA__).

reduction to the recovery baseline), but rather can increase their profits. *Id.* ¶902 (JA__).[22]

Additionally, although the *Order* expressly "takes interstate rate-of-return carriers off of rate-of-return based recovery … for interstate switched access" rate elements subject to reform, *Order* ¶900 (JA__), the FCC was well aware that the existing interstate switched access revenue requirement included a potentially excessive authorized rate of return of 11.25 percent. *See Order* n.1736 (JA__). The FCC tentatively found that "the current rate of return of 11.25 percent is no longer consistent with the Act and today's financial conditions." *Id.* ¶638 (JA__). The existing rate-of-return prescription (set in 1990) was more than two decades old, and "fundamental changes in the cost of debt and equity" had occurred in the intervening years. *See id.* ¶1046 (JA__). Accordingly, even rate-of-return carrier associations had, as part of a broader proposal, suggested a reduction in the prescribed rate

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[22] Petitioners contend that the FCC's concern with improving rate-of-return ILECs' cost-cutting incentives conflicts with its decision in 1990 to make the incentive-based price cap regime optional for smaller LECs. Br. 54 (citing *Policy and Rules Concerning Rates for Dominant Carriers*, 5 FCC Rcd 6786, 6799 (1990)). That claim is misdirected. The FCC simply decided there that *the record* failed to establish that small carriers could afford to reduce their rates as rapidly as the price cap formula required large carriers to do. 5 FCC Rcd at 6799 ¶¶103-104. Here, the FCC has separately analyzed the circumstances of price cap and rate-of-return carriers and adopted a less demanding schedule of revenue reductions for rate-of-return carriers. *See Order* ¶¶851, 867-904 (JA__, __-__).

of return from 11.25 percent to 10 percent, and the state members of the Federal-State Joint Board had proposed a greater reduction to 8.5 percent. *See* i*d.* The FCC's record-based concern that the existing rate-of-return prescription was too high supports its predictive judgment that the transitional recovery mechanism would give carriers a reasonable opportunity to recover their costs. *See id.* ¶¶924, 1046 (JA__, __); *see also Franklin Sav. Ass'n v. Dir., Office of Thrift Supervision*, 934 F.2d 1137, 1146 (10th Cir. 1991) ("[R]eviewing courts should be particularly deferential when they are reviewing an agency's predictive judgments, especially those within the agency's field of discretion and expertise.").

Finally, the Total Cost and Earnings Review process the FCC established, which "allow[s] individual carriers to demonstrate that … additional recovery is needed to prevent a taking," eliminates any remaining risk that the recovery mechanism arbitrarily denies carriers an opportunity to recover their costs. *Order* ¶924 (JA__); *see Time Warner Entm't Co. v. FCC*, 56 F.3d 151, 169 (D.C. Cir. 1995) (upholding as reasonable FCC rules that required across-the-board 17 percent cable rate reductions, but provided a cost-of-service "safety valve" for cable systems for which the "reduction would result in unreasonably low rates").

III. PETITIONERS' CHALLENGE TO THE FCC'S TENTATIVE PREDICTION THAT STATES LIKELY COULD NOT SUSPEND OR MODIFY THE *ORDER*'S BILL-AND-KEEP FRAMEWORK IS UNRIPE AND, IN ANY EVENT, UNSOUND.

Section 251(f)(2) provides that certain small LECs "may petition a State commission for a suspension or modification" of the requirements of section 251(b) or (c), and that the "State commission shall grant such petition" if it determines that such suspension or modification

> (A) is necessary – (i) to avoid a significant adverse economic impact on users of telecommunications services generally; (ii) to avoid imposing a requirement that is unduly economically burdensome; or (iii) to avoid imposing a requirement that is technically infeasible; and (B) is consistent with the public interest, convenience, and necessity.

47 U.S.C. §251(f)(2). Although this provision "entrusts state commissions with the job" of acting on section 251(f)(2) petitions, the FCC is authorized to issue "rules to guide the state commission judgments" on such matters. *AT&T*, 525 U.S. at 385.

The FCC nevertheless declined "at this time" to adopt "specific rules regarding section 251(f)(2)." *Order* ¶824 (JA__). The agency observed, though, that "suspensions or modifications of the bill-and-keep methodology [adopted in the *Order*] would, among other things, re-introduce regulatory uncertainty, shift the costs of providing service to a LEC's competitors and the competitor's customers, increase transaction costs for terminating calls, and undermine the efficiencies gained from adopting a uniform national framework." *Id.* Accordingly, although the FCC did not preempt states, it suggested that it was "highly unlikely that any attempt by a state" to grant a suspension or modification petition "would be 'consistent with the public interest, convenience and necessity' as required by section 251(f)(2)(B)." *Id.*

Petitioners contend that the FCC's discussion of section 251(f)(2)(B) "unlawfully circumscribes" carrier rights under that provision and "infringes on State jurisdiction to address lawful suspension and modification requests." Br. 45. This claim is unripe and, in any event, lacks merit.

In *USTA*, 359 F.3d 554, the D.C. Circuit held unripe a closely analogous claim. The case arose out of a rulemaking in which the FCC had determined that incumbent LECs need not unbundle certain network elements for requesting carriers pursuant to section 251(c)(3) and (d)(2). The FCC had also "predict[ed] that *state* unbundling requirements for elements that the FCC has determined need not be unbundled under §251(d)(2) are 'unlikely' to be found consistent with the Act." *USTA*, 359 F.3d at 594 (emphasis added) (quoting *Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, 18 FCC Rcd 16978, 17101 ¶195 (2003)). On judicial review, the petitioners claimed that the FCC had unlawfully preempted state unbundling authority with respect to the network elements at issue. The court of appeals, however, dismissed the claim because "[t]he general prediction voiced in [the order] [did] not constitute final agency action, as the Commission ha[d] not taken any view on any attempted state unbundling order." *Id.* "Besides," the court explained, "the state petitioners ha[d] not – and probably could not [have] – identif[ied] any substantial hardship that they would suffer by deferring judicial review of the preemption issues until the FCC actually issue[d] a ruling that a specific state unbundling requirement [was] preempted." *Id.*

The same result should obtain here. As in *USTA*, the FCC has not taken final action. Rather, the FCC has merely made "predictions" about whether state modification grants would be consistent with the statute. Also as in *USTA*, petitioners here do not identify any substantial hardship they might suffer by deferring judicial review unless and until the FCC actually rules with respect to a state's action under section 251(f)(2). *See Friends of Marolt Park v. U.S. Dep't of Transp.*, 382 F.3d 1088, 1093-94 (10th Cir. 2004) (ordinarily, the ripeness of an agency order "depends on whether the plaintiffs challenge a final agency action," but "[e]ven where an agency action is considered final, … a claim may not be ripe if there is no direct, immediate effect on plaintiffs").

Petitioners' challenge to the merits of the FCC's section 251(f)(2)(B) discussion is mistaken, in any event. First, contrary to petitioners' claim (Br. 48), the FCC's section 251(f)(2) discussion is wholly unlike the rule that the Eighth Circuit set aside in *Iowa Utils. Bd. v. FCC*, 219 F.3d 744. The Eighth Circuit interpreted that rule to *remove* two of three statutory prerequisites for terminating a rural ILEC's exemption (under 47 U.S.C. §251(f)(1)) from section 251(c) obligations. *Id.* at 760. The section 251(f)(2)(B) discussion at issue here does not remove any statutory suspension or modification criteria.

Moreover, the FCC's public interest discussion was reasonable. The FCC provided a detailed explanation of the need to replace the broken legacy system of intercarrier compensation with a bill-and-keep framework. *See generally Order* ¶¶741-759, 788-797, 824 (JA__-__, __-__, __). The FCC's findings justified its prediction that the grant of a section 251(f)(2) petition would likely fail the "public interest, convenience and necessity" prong of section 251(f)(2)(B).

IV. PETITIONERS' ADMINISTRATIVE PROCESS AND CONSTITUTIONAL CLAIMS FAIL.

A. The Administrative Record Was Developed Consistent With The APA, The FCC's *Ex Parte* Rules, And Notions Of Fundamental Fairness.

In the administrative proceedings culminating in the *Order*, the FCC sought comment on the "subjects and issues involved" in the rulemaking, 5

U.S.C. §553(b)(3), through the issuance of four formal notices.[23] Those notices generated more than 650 formal comments and reply comments from approximately 300 parties, including petitioners, and thousands more informal comments.[24] In addition, the FCC held "over 400 meetings with a broad cross-section of industry and consumer advocates," held "three open, public workshops, and engaged with other federal, state, Tribal, and local officials throughout the process." *Order* ¶12 (JA__). As permitted by its *ex parte* rules,[25] the FCC also received numerous lawful presentations from

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[23] *2011 NPRM*, 26 FCC Rcd 4554 (JA__); *Mobility Fund NPRM*, 25 FCC Rcd 14716 (2010) (JA__); *Mobility Fund Tribal Public Notice*, 26 FCC Rcd 5997 (WTB 2011) (JA__); *August 3, 2011, Public Notice*, 26 FCC Rcd 11112 (WCB 2011) (JA__).

[24] *See Order* Apps. J, K, L, M (JA__-__).

[25] *See EchoStar Satellite LLC v. FCC*, 457 F.3d 31, 39 (D.C. Cir. 2006).

stakeholders, including petitioners.[26] *See Order* ¶12 (JA__) (describing the "enormous interest in and public participation in" the reform process).

Petitioners nevertheless claim that the FCC violated the rulemaking provisions of the APA and their due process rights "by relying in part on unchallenged *ex parte* filings submitted so late in the decision-making process" that petitioners allegedly were denied "a meaningful opportunity to be heard." Br. 58. This claim is without merit.

The APA requires, in informal notice-and-comment rulemaking proceedings, that the agency "give interested persons an opportunity to participate … through submission of written data, views, or arguments with or without opportunity for oral presentation." *Phillips Petroleum Co. v. EPA*,

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[26] *See* 47 C.F.R. §1.1206 (providing permit-but-disclose standards for informal rulemaking proceedings). Under these *ex parte* rules, parties must place copies of all written *ex parte* presentations in the record, and must expeditiously follow up oral presentations with written summaries of "all data presented and arguments made" during the presentations. *Id.* §1.1206(b)(1) & (b)(2)(iii). *Ex parte* filings, including written summaries of oral presentations, must be submitted to the FCC Secretary and are included in the administrative record for public inspection. *See id.* §1.1206(b)(2)(i); *see also id.* §1.1206(b)(2)(ii) (establishing special procedures for submissions containing confidential information). The rules also establish a period of repose (referred to as the "sunshine period"), which runs from about a week before the public meeting at which the FCC votes on the rulemaking order until the text of the order is released. *See id.* §1.1203(b). During that period, *ex parte* presentations are generally prohibited, *see id.* §1.1203(a), although the rules permit expeditious written replies during the sunshine period to filings made on the eve of the period of repose, *see id.* §1.1206(b)(2)(iv).

803 F.2d 545, 559 (10th Cir. 1986) (quoting 5 U.S.C. §553(c)). That "opportunity to participate is all that the APA requires." *Id.*

Due process likewise "generally requires a 'meaningful opportunity' to be heard" before an agency takes action that may adversely affect a party's property interests. *Blumenthal v. FERC*, 613 F.3d 1142, 1145 (D.C. Cir. 2010) (citation omitted). Nevertheless, "informal contacts between agencies and the public are the 'bread and butter' of the process of administration and are completely appropriate so long as they do not frustrate judicial review or raise serious questions of fairness." *EchoStar*, 457 F.3d at 39 (quoting *Home Box Office, Inc. v. FCC*, 567 F.2d 9, 57 (D.C. Cir. 1977)).

Petitioners have not come close to establishing that the FCC breached these standards. Although they complain of various filings pursuant to the FCC's *ex parte* rules in the days and weeks prior to the *Order*'s adoption, they identify only one – a two-page filing by Verizon that urged the FCC to allow the ARC to be recovered "at the holding company level." Br. 59 (citing Letter from Chris Miller, Verizon, to FCC Secretary, at 1 (Oct. 20, 2011) (JA__)). That letter, however, merely elaborated briefly on aspects of the ARC that had already been discussed in the "ABC Plan" submitted by a group of price cap LECs. *See Order* ¶910 & n.1791 (JA__). That Plan had been a prominent part of the record for over two-and-a-half months at the time of Verizon's filing and was the subject of a separate request for public comment by the agency.[27] Petitioners were not denied a reasonable opportunity to participate or even to address the specific plan they identify.

Petitioners also complain generally about unidentified *ex parte* presentations submitted by AT&T and Verizon in the days immediately before the "sunshine period" (*see* n.26, above) commenced on October 21, 2011. Br. 60. But every administrative process must have an end point, and the FCC's rules – including both the sunshine period deadline and the opportunity provided for expeditious response to filings made on the eve of that deadline (*see* 47 C.F.R. §§1.1203(b) & 1.1206(b)(2)(iv)) – are designed to enable both the FCC and the public to evaluate filings before the agency acts. Indeed, petitioners actively employed those rules to exercise the "opportunity to participate" that the APA requires. *Phillips Petroleum*, 803 F.2d at 559.[28]

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[27] Letter from Robert W. Quinn, *et al.*, to FCC Secretary (July 29, 2011) (JA__) (presenting ABC Plan); *August 3, 2011*, *Public Notice*, 26 FCC Rcd 11112 (WCB 2011) (JA__) (soliciting public comment on the ABC Plan).

[28] Notably, the *Order* addresses October 2011 *ex parte* letters submitted by the petitioners, as well as Verizon and AT&T submissions. *See, e.g.*, *Order* n.2224 (JA__) (citing petitioner NASUCA October 2011 *ex parte*), *id.* n.1506 (JA__) (citing petitioner Gila River Telecommunications Inc. October 2011 *ex parte*).

In any event, petitioners' APA and due process claims fail under the "rule of prejudicial error." 5 U.S.C. §706(2)(F). Even where a procedural error exists (and there was no such error here), a mistake by the agency "does not require reversal unless a [petitioner] demonstrates prejudice resulting from the error." *Hillsdale Envt'l Loss Prevention, Inc. v. U.S. Army Corps of Eng'rs*, 702 F.3d 1156, 1165 (10th Cir. 2012). Specifically, it is "incumbent upon a petitioner objecting to an agency's late submission of documents to indicate with 'reasonable specificity' what portions of the documents it objects to and how it might have responded if given the opportunity." *Air Transport Ass'n v. CAB*, 732 F.2d 219, 224 n.11 (D.C. Cir. 1984) (citation omitted). The petitioner must also demonstrate that the agency actually relied upon the late-filed documents and that they were "critical to the formulation of the rule." *American Mining Congress v. Marshall*, 671 F.2d 1251, 1261 (10th Cir. 1982); *accord New Mexico v. EPA*, 114 F.3d 290, 295 (D.C. Cir. 1997) (explaining that late-filed comments are not problematic if the agency "can justify its rules entirely by reference to" timely filed documents in the record (citation omitted)).[29]

[29] If, as here, the agency's procedures permit aggrieved parties to contest late-filed pleadings through petitions for administrative reconsideration, the availability of such a process also may render harmless any procedural

Petitioners make no effort to satisfy any of these requirements. They offer no explanation (and cannot properly provide one only on reply) of how the cited Verizon letter – or any of the other, wholly unidentified filings to which they object – harmed them.

B. The *Order* Poses No Unconstitutional Burden On State Sovereignty.

Petitioners claim that the *Order* unconstitutionally undermines state sovereignty by imposing on states a "regulatory 'gun to the head.'" Br. 62-63 (quoting *Nat'l Federation of Ind. Businesses v. Sebelius*, 132 S. Ct. 2566, 2604 (2012)). Although their brief cites no specific section of the *Order*, petitioners presumably intend to challenge the FCC's decision to limit federal high-cost universal service support to carriers where end-user rates "do not meet a specified local rate floor," *see Order* ¶¶235, 237 (JA__, __), and the agency's decision to "permit carriers to determine at the holding company level how Eligible Recovery will be allocated among their incumbent LECs' ARCs," *id.* ¶910 (JA__). The FCC adopted the "rate floor" rule to ensure that the universal service fund did not "subsidize[] artificially low local rates in rural areas." *Id.* ¶235 (JA__). The FCC adopted the "holding company" rule, among other things, to enable carriers to "spread [eligible recovery through

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irregularity that allegedly exists. *See Blumenthal*, 613 F.3d at 1146; *NARUC*, 737 F.2d at 1121.

the ARC] among a broader set of customers, minimizing the increase experienced by any one customer." *Id.* ¶910 (JA__).[30]

Petitioners' *Sebelius* arguments are unsound. *Sebelius* dealt with the *state*-operated and partially *state*-funded Medicaid program. It did not, as do the challenged portions of the *Order*, deal with subsidies to and regulation of *private parties*. Thus, in setting aside a provision of the Affordable Care Act ("ACA") that withdrew all federal Medicaid funding to states if they declined to participate in the statute's Medicaid expansion, the Court relied heavily on precedent that "the Framers explicitly chose a Constitution that confers upon Congress the power to regulate individuals, not States." *Printz v. United States*, 521 U.S. 898, 920 (1997) (quoting *New York v. United States*, 505 U.S. 144, 166 (1992)); *see Sebelius*, 132 S. Ct. at 2601-02 (citing *Printz* and

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[30] Separate challenges to the FCC's statutory (as opposed to constitutional) authority to adopt both rules are presented in other petitioners' briefs. As demonstrated in our separate briefs in response to those filings, those challenges are unavailing. *See* FCC Principal USF Brief, Argument V.A. (addressing the rate floor condition on federal universal service support); FCC Response to NASUCA Brief, Argument III (addressing a challenge to the ARC holding company allocation).

New York). Petitioners point to nothing in the *Order* that violates that principle.[31]

CONCLUSION

For the foregoing reasons, the petitions for review should be dismissed in part and otherwise denied.

[31] Even if *Sebelius* somehow applied to the challenged reforms, petitioners make no showing of coercion remotely like that imposed on states by the ACA. *Cf.* 132 S. Ct. at 2604-05 (because "Medicaid spending accounts for over *20 percent* of the average State's total budget, with federal funds covering *50 to 83 percent* of those costs," the ACA's threatened withdrawal of all federal Medicaid funding constituted "economic dragooning that leaves the States with no real option but to acquiesce") (emphasis added).

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

Certificate of Compliance With Type-Volume Limitations, Typeface Requirements, Type Style Requirements, Privacy Redaction Requirements, and Virus Scan

1. This brief complies with the type-volume limitation of the Second Briefing Order. It does not exceed 15% of the size of the brief to which it is responding. The Joint Intercarrier Compensation Principal Brief of Petitioners was certified to be 11,805 words in length. Therefore, the FCC may file a response brief up to 13,575 words in length. This brief contains 13,507 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii). If the words in the chart on p.52 were included, the total would be 13,571 words.

2. This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and 10th Cir. R. 32(a) and the type style requirements of Fed. R. App. P. 32(a)(6) because this filing has been prepared in a proportionally spaced typeface using Microsoft Word 2010 in 14-point Times New Roman font.

3. All required privacy redactions have been made.

4. This brief was scanned for viruses with Symantec Endpoint Protection, version 11.0.7200.1147, updated on March 6, 2013, and according to the program is free of viruses.

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March 6, 2013

CERTIFICATE OF SERVICE

I hereby certify that on March 6, 2013, I caused the foregoing Federal Respondents' Uncited Response to the Joint Intercarrier Compensation Principal Brief to be filed by delivering a copy to the Court via e-mail at FCC_briefs_only@ca10.uscourts.gov. I further certify that the foregoing document will be furnished by the Court through (ECF) electronic service to all parties in this case through a registered CM/ECF user. This document will be available for viewing and downloading on the CM/ECF system.

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