Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
GENERAL COMMUNICATION, INC.,	)	
Complainant,	)	
	)	
v.	)	EB-00-MD-016
	)	
ALASKA COMMUNICATIONS SYSTEMS	)	
HOLDINGS, INC. and ALASKA	)	
COMMUNICATIONS SYSTEMS, INC.	)	
d/b/a ATU TELECOMMUNICATIONS d/b/a	)	
ANCHORAGE TELEPHONE UTILITY,	)	
Defendants.	)	

MEMORANDUM OPINION AND ORDER

Adopted: January 23, 2001 **Released:** January 24, 2001

By the Commission:

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I. INTRODUCTION

1. In this Order, we grant in part and deny in part a complaint filed on August 24, 2000 by GCI Communication, Inc. ("GCI") against Alaska Communications Systems, Inc. d/b/a ATU Telecommunications d/b/a Anchorage Telephone Utility (collectively "ATU") and Alaska Communications Systems Holdings, Inc. ("ACS Holdings") pursuant to section 208 of the Communications Act of 1934, as amended ("Act").[1] We find that ATU unlawfully earned more than its allowable rate of return for the period from January 1, 1997 through December 31, 1998 ("1997-1998 Monitoring Period") by 1) improperly assigning to the interstate jurisdiction for separations purposes the traffic-sensitive costs of carrying Internet Service Provider ("ISP") traffic, and 2) improperly calculating dial equipment minutes ("DEMs") for intraoffice calls. ATU's violation of its prescribed rate of return constitutes a violation of section 201(b) of the Act.[2] Accordingly, we grant Counts 1 through 3 of GCI's complaint. Given our ruling on Counts 1 through 3, we dismiss the remaining Counts of GCI's complaint (Counts 4 through 6) as moot, because, although they allege different legal violations, they seek the same relief for the same

[1] 47 U.S.C. § 208.

[2] 47 U.S.C. § 201(b).

ATU conduct specified in Counts 1 though 3.

2. In conjunction with our ruling in GCI's favor on Counts 1 through 3 of its complaint, we award damages, with prejudgment interest, to GCI for ATU's overearnings. Further, we direct ATU to: 1) revise its 1997-1998 Monitoring Report in accordance with this Order; 2) allocate to the intrastate jurisdiction for separations purposes the traffic-sensitive costs of carrying ISP traffic from January 1, 1999 forward, until otherwise ordered by the Commission; and 3) count each minute of intraoffice calls as two DEMs from January 1, 1999 forward, until otherwise ordered by the Commission.

3. Finally, we dismiss all of GCI's claims against defendant ACS Holdings. GCI has not alleged that ACS Holdings overcharged it for any services or overearned in violation of the Act or any Commission order or rule.

II. BACKGROUND

4. ATU is the incumbent local exchange carrier ("LEC") in Anchorage, Alaska.[3] ATU is wholly owned and controlled by ACS Holdings.[4] GCI provides facilities-based interstate and intrastate interexchange services in the state of Alaska, and competitive local exchange services in Anchorage, Alaska.[5] GCI purchased interstate access services from ATU throughout the 1997-1998 Monitoring Period for the origination and termination of GCI's interstate interexchange traffic from and to customers located in Anchorage.[6] GCI continues to purchase interstate interexchange services from ATU.

5. ATU is a "rate-of-return" carrier. Rate-of-return carriers are permitted to earn no more than a Commission-prescribed return on the investments they make in providing exchange access services.[7] To comply with this prescription, rate-of-return carriers estimate their costs of providing exchange access services and project their demand for such services for a two-year period in the future (*i.e.*, the monitoring or enforcement period).[8] They then file tariffs containing rates for their access services that they believe, given their estimate of costs and demand, will

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[3] Joint Statement of General Communication, Inc. and Alaska Communications Systems Holdings, Inc. and Alaska Communications Systems, Inc., File No. EB-00-MD-016 (September 29, 2000) ("Joint Statement"), at ¶ 3.

[4] *Id.* at ¶ 4.

[5] *Id.* at ¶ 1.

[6] *Id.* at ¶ 5.

[7] *See generally Represcribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers,* Order, 5 FCC Rcd 7507, 7532 at ¶¶ 1, 216 (1990) ("*Rate-of-Return Prescription Order*"); 47 C.F.R. § 65.700.

[8] *See* 47 C.F.R. §§ 65.700-702; *see also MCI Telecom. Corp. v. FCC*, 59 F.3d 1407, 1415 (D.C. Cir. 1995) (discussing the general process carriers follow in setting rates to comply with the rate-of-return prescription).

result in earnings within the prescribed rate of return at the end of the two-year forecast period. During the course of the two-year monitoring period, rate-of-return carriers must review how their actual costs and demand calculations compare to their earlier projections, and make rate adjustments, if necessary, to ensure that they do not exceed their prescribed rate of return.[9] If a rate-of-return carrier ultimately exceeds its rate of return at the end of the two-year monitoring period, the Commission may then require refunds of any such overearnings to affected customers.[10]

6. In estimating their access services costs to prepare their tariffs in a manner that will allow them to earn no more than their prescribed rate of return, rate-of-return carriers must apply, *inter alia*, the Commission's jurisdictional separations rules and Commission orders implementing and interpreting those rules.[11] Jurisdictional separations, generally speaking, is the process by which carriers apportion the costs of providing telecommunications services to either the intrastate or interstate jurisdiction, depending on the use of their equipment and other resources in providing those services.[12]

7. Pursuant to the foregoing regulatory regime, on April 2, 1996, ATU filed an annual access tariff setting forth its rates for interstate access service, effective from July 1, 1996 through June 30, 1998 ("1997 Tariff").[13] ATU's 1997 Tariff contained no statement indicating how ATU would allocate ISP traffic costs[14] for separations purposes or how it would count DEMs for intraoffice calls.[15]

8. On December 17, 1997, ATU filed an access tariff containing revised rates for interstate access service for the period from January 1, 1998 through June 30, 1998 ("January 1998 Tariff").[16] This tariff was filed on 15-days' notice, purportedly pursuant to the

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[9] *MCI*, 59 F.3d at 1415; *see In the Matter of Amendment of Part 65, Interstate Rate of Return Prescription: Procedures and Methodologies to Establish Reporting Requirements*, Report and Order, 1 FCC Rcd 952, 954 at ¶ 10 (1986).

[10] *MCI*, 59 F.3d at 1414.

[11] *See* 47 C.F.R. Part 36.

[12] *See generally* 47 C.F.R. §§ 36.1 and 36.2.

[13] Formal Complaint of General Communication, Inc., File No. EB-00-MD-016 (August 24, 2000) ("Complaint"), at Exhibit 1.

[14] ISP traffic consists of communications traffic from end users dialing up connections to ISPs. Our references herein to "ISP traffic costs" refer only to the traffic-sensitive costs of ISP traffic, unless otherwise indicated.

[15] *Id*. Intraoffice calls are calls that originate and terminate in the same central office. DEMs are defined as the minutes of holding time of the originating and terminating local switching equipment, where holding time is defined generally as the time the equipment is in use. 47 C.F.R. § 36.125(a)(3).

[16] Complaint at Exhibit 3.

"streamlining" provisions of section 204(a)(3) of the Act.[17] Like its 1997 Tariff, ATU's January 1998 Tariff did not indicate how ATU intended to assign ISP traffic costs for separations purposes or how it would count DEMs for intraoffice calls.[18] During the course of the instant proceeding, ATU has stated that it treated ISP traffic costs as *intrastate* and counted each minute of intraoffice calls as *two DEMs* in preparing its January 1998 Tariff.[19]

9. On March 31, 1998, ATU submitted a preliminary monitoring report for the period January 1, 1997 to December 31, 1997.[20] ATU noted on the back of the report that "THESE RESULTS REFLECT THE FOLLOWING: 1. RECORDING OF INTRAOFFICE CALLS AS ONE DEM[;] 2. INTERNET SERVICE PROVIDER TRAFFIC HAS BEEN CATEGORIZED AS INTERSTATE."[21]

10. On June 24, 1998, ATU filed an annual access tariff setting forth its rates for interstate access service for the period from July 1, 1998 through June 30, 2000 ("July 1998 Tariff").[22] ATU filed this tariff on seven-days' notice, also purportedly pursuant to the streamlining provisions of section 204(a)(3). The "Description and Justification" section of ATU's July 1998 Tariff indicated that "[t]his filing reflects the recording of intraoffice traffic as one (1) dial equipment minutes (DEM) and the treatment of all identifiable Internet Service Provider (ISP) traffic as interstate."[23] This was the first time that ATU had indicated, in a tariff

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[17] 47 U.S.C. § 204(a)(3) (providing that a local exchange carrier may file a new or revised charge, classification, regulation, or practice on a streamlined basis, and that such charge, classification, regulation or practice shall be deemed lawful and effective either 7 days or 15 days after the date on which it is filed (depending on the contents of the filing), unless the Commission takes action to suspend and investigate the filing).

[18] ATU has stipulated that its January 1998 Tariff did not provide notice that ATU would assign to the *interstate* jurisdiction for separations purposes the costs of ISP traffic or would count each minute of intraoffice calls as *one DEM*. *See* Letter from Christopher N. Olsen, Attorney, Market Disputes Resolution Division, Enforcement Bureau, to Joe D. Edge, et al., Drinker Biddle & Reath LLP, and Karen Brinkmann, et al., Latham & Watkins, File No. EB-00-MD-016 (October 6, 2000), at 1-2; Stipulation of Defendants Alaska Communications Systems Holdings, Inc. and ACS of Anchorage, Inc., File No. EB-00-MD-016 (October 20, 2000), at 1.

[19] Reply Brief of Defendants Alaska Communications Systems Holdings, Inc. and ACS of Anchorage, Inc., File No. EB-00-MD-016 (November 3, 2000) ("ATU Reply Br.") at 12, n.11 ("the 1997 and January 1998 Tariffs treated ISP traffic as intrastate and counted intraoffice calls as two DEMs. . .").

[20] Answer of Defendants Alaska Communications Systems Holdings, Inc. and ACS of Anchorage, Inc., File No. EB-00-MD-016 (September 13, 2000) ("Answer"), at Exhibit 2. ATU, like other rate-of-return carriers, is required to file a preliminary monitoring report each year of the two-year monitoring period. *See* 47 C.F.R. §§ 65.600, 65.701. The final monitoring report, which includes any required adjustments to the preliminary reports, must be filed by September 30 of the year following the conclusion of the monitoring period. 46 C.F.R. § 65.600.

[21] Answer at Exhibit 2.

[22] Complaint at Exhibit 4.

[23] *Id.* at Description and Justification, Section 4 at 14.

filing, how it intended to allocate ISP traffic costs and count DEMs for intraoffice calls. Moreover, these statements differed from the way that ATU had allocated ISP traffic costs and counted DEMs for intraoffice calls in preparing its January 1998 Tariff.[24]

11. On September 30, 1999, ATU filed its 1997-1998 Monitoring Report.[25] The reported cumulative rate of return for the Switched Traffic Sensitive Category was 7.86 percent.[26] On the back of the 1997-1998 Monitoring Report, ATU stated: "THESE RESULTS REFLECT THE FOLLOWING: 1. INTRAOFFICE CALLS HAVE BEEN COUNTED AS ONE DEM[;] 2. INTERNET SERVICE PROVIDER TRAFFIC HAS BEEN CATEGORIZED AS INTERSTATE."[27]

12. The parties agree that if, for the 1997-1998 Monitoring Period, ATU had assigned the costs for ISP traffic to the intrastate jurisdiction and counted two DEMs for each minute of intraoffice calls, then ATU's rate of return for the interstate switched traffic sensitive category would have been 32.12 %, far in excess of the maximum allowable rate of return of 11.65%.[28]

13. GCI filed this Complaint on August 24, 2000. GCI alleges that ATU's conduct during the 1997-1998 Monitoring Period violated the Act in several ways. In Count 1, GCI alleges that ATU violated Commission orders requiring ISP traffic costs to be assigned to the intrastate jurisdiction for jurisdictional separations purposes.[29] In Count 2, GCI alleges that ATU violated section 36.125(a)(3) of the Commission's rules by counting only one DEM for each minute of an intraoffice call.[30] In Count 3, GCI alleges that ATU unlawfully exceeded its prescribed rate of return, in violation of 201(b) of the Act, by improperly assigning ISP traffic

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24 *See* ATU Reply Br. at 12, n.11 ("the 1997 and January 1998 Tariffs treated ISP traffic as intrastate and counted intraoffice calls as two DEMs and the July 1998 Tariff treated ISP traffic as interstate and counted intraoffice calls as one DEM").

25 Complaint at Exhibit 5.

26 Rate-of-return carriers must compute their returns for several access service categories. 47 C.F.R. § 65.702(a). The switched traffic sensitive category, which includes services provided by local exchange carriers to their access customers, such as line termination and local switching, is the category affected by ATU's allocation of ISP traffic costs and counting of DEMs for intraoffice calls.

27 Complaint at Exhibit 5.

28 Joint Statement at ¶ 14. *See Rate-of-Return Prescription Order*, 5 FCC Rcd at 7532, ¶ 216 (prescribing maximum rate of return of 11.25%); 47 C.F.R. § 65.700(a) (providing that the maximum allowable rate of return is determined by adding four tenths of one percent to the maximum prescribed rate of return). The total amount in dispute for the 1997-1998 Monitoring Period is $2,765,371, excluding interest. Joint Statement at ¶ 15. This amount represents the difference between the amount GCI paid to ATU for interstate access services and the amount GCI would have paid to ATU if ATU had not assigned ISP traffic costs to the interstate jurisdiction or counted DEMs improperly and had not thereby exceeded its prescribed rate of return.

29 Complaint at ¶¶ 25-31.

30 47 C.F.R. § 36.125(a)(3); Complaint at ¶¶ 32-35. ATU has agreed, at the Commission's request, to count each minute of intraoffice calls as two DEMs on a going-forward basis. Complaint at Exhibit 10.

costs for separations purposes and improperly counting DEMs for intraoffice calls.[31] In Count 4, GCI alleges that ATU's tariffs are unjust and unreasonable in violation of section 201(b) of the Act, because they permitted ATU to exceed its prescribed rate of return.[32] In Counts 5 and 6, respectively, GCI alleges that ATU's assignment to the interstate jurisdiction of ISP traffic costs unjustly and unreasonably imposed charges on GCI for a service to which it did not subscribe, and violated the Commission's "ESP exemption."[33]

III. DISCUSSION

14. Counts 1 through 3 of GCI's Complaint collectively allege that ATU unlawfully exceeded its prescribed rate of return, in violation of section 201(b) of the Act, by improperly 1) assigning to the interstate jurisdiction for separations purposes the costs of ISP traffic, and 2) counting each minute of intraoffice calls as one DEM, rather than two. For the following reasons, we agree with GCI.

A. ATU Exceeded its Prescribed Rate of Return for the 1997-1998 Monitoring Period, in Violation of Section 201(b) of the Act.

15. For the reasons described below, we conclude that, by allocating ISP traffic costs to the interstate jurisdiction for separations purposes, and by counting one DEM rather than two DEMs for each minute of intraoffice calls, ATU erroneously inflated its interstate cost base. This enabled ATU to charge its interstate access service customers, like GCI, more than it would have been able to charge if it had properly allocated ISP traffic costs and counted DEMs for intraoffice calls. These two practices collectively resulted in ATU's unlawfully earning more than its allowable rate of return during the 1997-1998 Monitoring Period.

1. ATU's Allocation of ISP Traffic Costs to the Interstate Jurisdiction for Separations Purposes Was Unlawful.

a. ATU's Allocation of ISP Traffic Costs to the Interstate Jurisdiction Violated Commission Orders.

16. GCI argues that the Commission requires carriers to assign ISP traffic costs to the intrastate jurisdiction for separations purposes.[34] In response, ATU asserts that the Commission has never issued such a *requirement*, but has only expressed a *preference* for such treatment of ISP traffic costs.[35] We agree with GCI that the assignment of ISP traffic costs to the intrastate

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[31] Complaint at ¶¶ 36-41.

[32] *Id.* at ¶¶ 42-44.

[33] *Id.* at ¶¶ 45-52. *See* Part III(A)(1)(a), *infra*.

[34] Complaint at ¶¶ 27-30; Brief of General Communication, Inc., File No. EB-00-MD-016 (October 27, 2000) ("GCI Br.") at 3-6.

[35] Answer at ¶ 76; ATU Reply Br. at 9-11.

jurisdiction is a legal requirement, rather than merely a suggestion.

17. Our requirement that ISP traffic costs be assigned to the intrastate jurisdiction derives from our decision to exempt enhanced service providers ("ESPs"), including ISPs, from purchasing interstate access services from interstate access tariffs. The Commission determined long ago that ESPs should obtain interstate access services by paying the local business exchange service rates contained in intrastate tariffs, rather than the access rates contained in interstate tariffs. The Commission made this determination to avoid severe rate impacts that would affect the continuing viability of the ESP industry.[36] The Commission recently retained that policy for the present, largely because it would have been illogical to apply the existing, inefficient interstate access charge rate structure to ISP traffic for the first time, just as the Commission is modifying that structure to eliminate implicit universal service subsidies from access charges and to move such charges toward competitive levels.[37]

18. In conjunction with affirming the ESP exemption, the Commission has explained how the ESP exemption affects carriers' assignment of costs for separations purposes. For example, in the *ONA NPRM*, in a section entitled "Analysis of the Existing Exemption," the Commission stated:

> ESP traffic over local business lines is classified as local traffic for separations purposes, with the result that TS [traffic sensitive] costs associated with ESP traffic are apportioned to the intrastate jurisdiction, and are recovered through intrastate charges paid by ESPs and other purchasers of intrastate services.[38]

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[36] *MTS and WATS Market Structure,* Memorandum Opinion and Order, 97 FCC 2d 682, 715 at ¶ 83 (1983), *aff'd, NARUC v. FCC*, 737 F.2d 1095, 1137 (D.C. Cir. 1984). The Commission has affirmed this "ESP exemption" several times. *See, e.g., Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Inter-Carrier Compensation for ISP-Bound Traffic,* Declaratory Ruling and Notice of Proposed Rulemaking, 14 FCC Rcd 3689, 3702 at ¶ 20 (1999) ("*Reciprocal Compensation Order*"); *In the Matter of Access Charge Reform*, First Report and Order, 12 FCC Rcd 15982, 16133 at ¶ 344 (1997) ("*First Access Charge Reform Order*"); *Amendments of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Subelements for Open Network Architecture,* Report and Order and Order on Further Reconsideration and Supplemental Notice of Proposed Rulemaking, 6 FCC Rcd 4524, 4535 at ¶ 60 (1991) ("*ONA Order*"); *Amendments of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Subelements for Open Network Architecture*, Notice of Proposed Rulemaking, 4 FCC Rcd 3983, 3987 at ¶¶ 33-34 (1989) ("*ONA NPRM*"); *In the Matter of Filing and Review of Open Network Architecture Plans*, Memorandum Opinion and Order, 4 FCC Rcd 1, 167-68 at ¶¶ 318-20 (1988); *Amendments of Part 69 of the Commission's Rules Relating to Enhanced Service Providers,* Order, 3 FCC Rcd 2631, 2635, nn. 8, 53 (1988).

[37] *See First Access Charge Reform Order*, 12 FCC Rcd at 16133, ¶¶ 343-45; *Southwestern Bell Tel. Co. v. FCC,* 153 F.3d 523, 541-42 (8th Cir. 1998) ("*SBC*"), *petition for rehearing denied,* 2000 U.S. App. LEXIS 16086 (June 7, 2000).

[38] *ONA NPRM*, 4 FCC Rcd at 3987-88, ¶ 34. The Commission cited section 36.125 of the separations rules as support for this separations treatment. *Id.* at 3987, n.82 (citing 47 C.F.R. § 36.125). Section 36.125 governs the separations treatment of local switching equipment.

This statement stemmed from the Commission's examination and tentative rejection of two alternatives to the ESP exemption. Significantly, both alternatives that the Commission considered encompassed the same separations treatment of ISP traffic costs that ATU adopted in this case – assignment of ISP traffic costs to the interstate jurisdiction rather than the intrastate jurisdiction for separations purposes. The Commission tentatively rejected these alternatives, noting that this "reclassification of ESP traffic that has been deemed to be intrastate for separations purposes would increase TS [traffic sensitive] costs apportioned to the interstate jurisdiction," and would "tend to increase the TS rates that other interstate access customers would bear, at a pace proportionate to the increase in ESP interstate traffic."[39] That is precisely what ATU tried to accomplish here. ATU reclassified ISP traffic costs from the intrastate to the interstate jurisdiction for separations purposes, which increased the traffic sensitive costs apportioned to the interstate jurisdiction. This, in turn, increased the interstate access rates that GCI had to bear as ISP traffic increased.

19. The Commission acted on the *ONA NPRM* and issued an order "conclud[ing] that the best approach is the adoption of the tentative conclusion of the Notice: retention of the current form of the [ESP] exemption," which "maintain[ed] the status quo."[40] The Commission rejected the two alternatives described in the *ONA NPRM* that would have allowed for the separations treatment of ISP traffic costs implemented by ATU here.[41] Although the Commission did not expressly discuss the separations treatment encompassed in the tentative conclusion of the *ONA NPRM*, the Commission implicitly adopted the separations treatment set forth therein by adopting the tentative conclusion of the *ONA NPRM*.

20. Moreover, in the *First Access Charge Reform Order*, the Commission concluded that "the *existing pricing structure* for ISPs should remain in place. . . ."[42] The Commission did not explicitly reference the separations treatment of ISP traffic costs set forth in the *ONA NPRM* and subsequently adopted in the *ONA Order*. However, the "existing pricing structure" maintained by the *First Access Charge Reform Order* necessarily encompassed that separations treatment. Most recently, in the *Reciprocal Compensation Order*, the Commission recognized this history of the ESP exemption and did not disturb the attendant "long-standing determination" by the Commission that, for jurisdictional separations purposes, both the revenues and traffic-sensitive costs of ISP traffic "will continue to be accounted for as intrastate."[43]

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[39] *Id.* at 3988, ¶¶ 35-37.

[40] *ONA Order,* 6 FCC Rcd at 4535, ¶ 60.

[41] *Id.*

[42] *First Access Charge Reform Order*, 12 FCC Rcd at 16133, ¶ 344 (emphasis added).

[43] *Reciprocal Compensation Order,* 14 FCC Rcd at 3710, ¶ 36. We acknowledge that the D.C. Circuit Court of Appeals subsequently vacated and remanded the *Reciprocal Compensation Order*. *Bell Atlantic Tel. Cos. v. FCC*, 206 F.3d 1 (D.C. Cir. 2000). However, as both parties agree, the vacatur did not affect the ESP exemption or the corresponding separations treatment of ISP traffic costs addressed in the *Reciprocal Compensation Order*. GCI Br. at 9-10; Brief of Defendants Alaska Communications Systems Holdings, Inc. and ACS of Anchorage, Inc., File No. EB-00-MD-016 (October 27, 2000) ("ATU Br.") at 3, 7-9.

21. On two recent occasions, the Commission's Common Carrier Bureau has implemented the Commission's rulings regarding the ESP exemption and concomitant separations requirements. In particular, two local exchange carriers tried to do exactly what ATU has done here – assign ISP traffic costs to the interstate jurisdiction for separations purposes. In both situations, the Common Carrier Bureau ordered the carriers to change their conduct and assign ISP traffic costs to the intrastate jurisdiction for separations purposes.[44] The Bureau further ordered the carriers to revise reports that they had previously filed containing the incorrect assignment of ISP traffic costs.[45]

22. In our view, the foregoing refutes ATU's assertion that the Commission has only expressed a preference, rather than a requirement, concerning how ISP traffic costs should be allocated for separations purposes.[46] The Commission has made clear that local exchange carriers *must* assign ISP traffic costs to the intrastate jurisdiction for separations purposes.[47] Accordingly, we find that ATU's allocation of ISP traffic costs to the interstate jurisdiction for separations purposes during the 1997-1998 Monitoring Period violated Commission orders.[48]

b. The Commission Has Jurisdiction to Require Carriers to Assign ISP Traffic Costs to the Intrastate Jurisdiction for Separations Purposes.

23. ATU next asserts that, even if the Commission has purported to require that ISP

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[44] *Common Carrier Bureau Issues Letter to SBC Regarding its Jurisdictional Separations Treatment of Internet Traffic,* Public Notice, 14 FCC Rcd 8178 (Com. Car. Bur. 1999) ("*SBC Letter*"), *application for review pending*; *Common Carrier Bureau Issues Letter to Bell Atlantic Regarding Jurisdictional Separations Treatment of Reciprocal Compensation for Internet Traffic,* Public Notice, 14 FCC Rcd 13148 (Com. Car. Bur. 1999) ("*Bell Atlantic Letter*").

[45] *SBC Letter*, 14 FCC Rcd at 8180-81; *Bell Atlantic Letter*, 14 FCC Rcd at 13149-150.

[46] *See generally In the Matter of Jurisdictional Separations Reform and Referral to the Federal-State Joint Board*, Recommended Decision, CC Docket No. 80-286, FCC 00J-2 (July 21, 2000) ("*Recommended Decision on Separations*") at n.66 (pointing out that the *Reciprocal Compensation Order* acknowledged a Commission *requirement* that carriers assign the traffic-sensitive costs of ISP traffic to the intrastate jurisdiction for separations purposes).

[47] We note that the Commission is currently considering a recommendation from the Federal-State Joint Board on Jurisdictional Separations that may address how ISP traffic costs should be allocated for separations in the future. *See In the Matter of Jurisdictional Separations Reform and Referral to the Federal-State Joint Board*, Recommended Decision, CC Docket No. 80-286, FCC 00J-2 (July 21, 2000). However, this does not affect our enforcement of the existing separations rules.

[48] ATU does not argue that it was unaware of the Commission and Common Carrier Bureau pronouncements concerning how to treat ISP traffic costs for separations purposes. Further, ATU acknowledges that it complied with the Commission's requirements at least until the time it filed its July 1998 Tariff. ATU Reply Br. at 12, n.11. These facts strongly suggest that ATU understood the Commission's requirements for the treatment of ISP traffic costs for separations purposes. Nevertheless, ATU now contends that the numerous Commission pronouncements discussed herein have no merit or binding effect. Answer at ¶ 76; ATU Reply Br. at 9-11.

traffic costs be assigned to the intrastate jurisdiction, the Commission was (and is) without jurisdiction to impose such a requirement. ATU relies on section 2 of the Act, which restricts federal regulation to "interstate" communication and reserves to the states authority to regulate "intrastate" communication.[49] According to ATU, because ISP traffic is largely interstate, forcing ATU to characterize such traffic as intrastate for separations purposes runs afoul of the section 2 jurisdictional boundaries, because it permits states to regulate or set rates for interstate communications.[50] We disagree, for the following reasons.

24. It is well-settled that when communications, such as ISP traffic, are jurisdictionally mixed, containing both interstate and intrastate components, the Commission has authority to regulate such communications.[51] This exercise of federal regulation over jurisdictionally mixed traffic necessarily encompasses the regulation and treatment of such traffic within the ambit of the Commission's separations rules.[52] Although the Commission's exercise of its discretion in treating jurisdictionally mixed communications in a particular manner under its separations rules may be subject to challenge as arbitrary and capricious, the Commission's *authority* to regulate such traffic in the first instance cannot seriously be challenged.

25. The United States Court of Appeals for the Eighth Circuit recently rejected essentially the same jurisdictional challenge ATU presents here. In *Southwestern Bell Tel. Co. v. FCC* ("*SBC*"), local exchange carriers appealed the Commission's decision to retain the ESP exemption and argued, just as ATU does here, that the ESP exemption unlawfully "forces state regulators to set rates for the recovery of interstate costs," because ISP traffic costs are "undeniably interstate costs."[53] The carriers argued that the ESP exemption, and the concomitant recovery by carriers of the costs of carrying ISP traffic only from local business tariffs, "amount[ed] to a dereliction of the Commission's obligation to retain exclusive jurisdiction over interstate communications and forces state regulatory commissions to overstep their authority by recovering interstate costs."[54]

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[49] Answer at ¶¶ 78-80 (citing 47 U.S.C. §§ 152(a), (b)); ATU Reply Br. at 7-9.

[50] Answer at ¶¶ 78-80; ATU Reply Br. at 7-9.

[51] *See, e.g., Louisiana Pub. Serv. Comm'n. v. FCC,* 476 U.S. 355, 376 n.4 (1986) (stating that federal regulation of traffic is appropriate where it is not possible to separate the interstate and intrastate components of the asserted regulation); *SBC,* 153 F.3d at 541-42 (holding that federal regulation of "jurisdictionally mixed" traffic is appropriate).

[52] *See, e.g.,* 47 U.S.C. § 221(c) (allowing the Commission to classify the property used by wireline communications providers for interstate communications services). The Commission's separations rules were adopted pursuant to and in accordance with section 221(c). *See Crockett Tel Co. v. FCC*, 963 F.2d 1564, 1566-67 (D.C. Cir. 1992) (describing that the Part 36 separations rules were adopted pursuant to section 221(c) and pointing out that the separations rules necessarily have some affect on state ratemaking authority to the extent that they apply to companies operating within state jurisdictions).

[53] 153 F.3d at 541-42.

[54] *Id*. at 542.

26. The Eighth Circuit rejected these jurisdictional contentions. The court noted that ISP traffic is jurisdictionally mixed and includes both interstate and intrastate components.[55] Because of the jurisdictionally mixed nature of this traffic, and because the Commission had valid policy reasons for creating the ESP exemption in the first place (*i.e.*, preserving the competitiveness and vitality of the emerging ESP industry), the court concluded that the Commission had "appropriately exercised its discretion to require an ISP to pay intrastate charges for its line . . . but not to pay the per-minute interstate access charge."[56] The court noted that the Commission's action left states free "to assess intrastate tariffs as they see fit."[57] Thus, the court concluded that the Commission had neither "shirked its responsibility to regulate interstate telecommunications nor . . . directed States to inflate intrastate tariffs to cover otherwise unrecoverable interstate costs, thereby exceeding its statutory authority [under section 2 of the Act]."[58]

27. Our well-established authority over jurisdictionally mixed traffic requires rejection of ATU's jurisdictional argument here. As in *SBC*, our requirement that ISP traffic costs be assigned to the intrastate jurisdiction for separations purposes does not result in an impermissible delegation of regulation of interstate communications to the states. In particular, our action does not impose any intrastate rates and states remain free to assess intrastate tariffs as they see fit. Thus, our action does not cross the jurisdictional line drawn by section 2 of the Act.[59]

28. At bottom, ATU's disagreement with the Commission's treatment of ISP traffic costs for separations purposes is not so much a challenge to the Commission's ultimate "jurisdiction" or authority over such traffic under section 2 of the Act as it is a challenge to the *manner* in which the Commission exercised its jurisdiction over such traffic in the circumstances presented. We address this challenge in the next section.

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[55] *Id.* at 543.

[56] *Id.* at 543-44.

[57] *Id.* at 543.

[58] *Id. See also Reciprocal Compensation Order*, 14 FCC Rcd at 3700-01, ¶ 16 (citing with approval the jurisdictional analysis employed in *SBC* and stating, "[w]e emphasize that the Commission's decision to treat ISPs as end users for access charge purposes and, hence, to treat ISP-bound traffic as local, does not affect the Commission's ability to exercise jurisdiction over such traffic.").

[59] *Louisiana Pub. Serv. Comm'n*, relied upon by ATU (ATU Reply Br. at 7-8), does not dictate a contrary result. *Louisiana Pub. Serv. Comm'n* held that the Commission could not pre-empt state regulation concerning depreciation of dual-jurisdiction property for rate-making purposes. No such pre-emption is occurring here, because the Commission is not directing states to set rates to recover for interstate costs. As in *SBC*, "states are free to assess intrastate tariffs as they see fit." *SBC*, 153 F.3d at 543. ATU's other cited authority on the jurisdiction issue is equally unavailing, as it merely supports the uncontroverted proposition that the federal government regulates interstate communications, while state governments regulate intrastate communications. *See, e.g., Crockett*, 963 F.2d at 1569 ("[A]ny attempt to impose intrastate rates is beyond federal authority; conversely, states may not trench upon interstate matters."); *Competitive Telecommunications Ass'n v. FCC,* 117 F.3d 1068, 1075, n.5 (8th Cir. 1997) (same).

c. Assigning ISP Traffic Costs to the Intrastate Jurisdiction Is Consistent With Separations Rules.

29. ATU asserts that the Commission abused its discretion by requiring carriers to allocate ISP traffic costs to the intrastate jurisdiction for separations purposes.[60] In ATU's view, the Commission's decision to define ISP traffic as intrastate for separations purposes, even while acknowledging that such traffic is "largely interstate," is arbitrary and improperly ignores the actual usage of the local equipment that processes ISP traffic.[61] Because ISP traffic is largely interstate, according to ATU, the costs of such traffic must be assigned to the interstate jurisdiction, in accordance with the holding of *Smith v. Illinois Bell,* the seminal case concerning jurisdictional separations.[62] ATU argues that the principles espoused in *Smith* are contravened if ATU is required, merely as a matter of convenience, to allocate entirely to one jurisdiction its costs of providing ISP services, and this allocation bears no relationship to the actual usage of its equipment used in providing such services.[63]

30. ATU's argument reflects an overexpansive reading of *Smith*. *Smith* concerned a situation in which a state commission failed to require a carrier to make *any* separations at all of equipment costs between interstate and intrastate uses. The Supreme Court stated that the state commission's failure to require any allocation at all violated the statutory predecessor to section 2 of the Act.[64] Here, the Commission has not failed to require ATU to allocate the costs of its local switching equipment between jurisdictions. Moreover, ATU does not contend that it has made no allocation of the costs of its local switching equipment between the interstate and intrastate jurisdictions. Instead, ATU's concern is that the Commission has allegedly required ATU to assign too much of certain traffic passing through its equipment to the intrastate jurisdiction for separations purposes. Thus, *Smith* does not help ATU.

31. In fact, *Smith* supports our conclusion here, because *Smith* recognizes that it is inherently difficult, if not impossible, to apportion with mathematical precision the uses of exchange plant equipment. The Court stated that, in ascertaining the proper apportionment of costs, "extreme nicety is not required, only reasonable measures being essential."[65] Further, as the

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[60] Answer at ¶¶ 77, 83-84; ATU Br. at 3-8; ATU Reply Br. at 9-11.

[61] Answer at ¶¶ 77, 83-84; ATU Br. at 7-9; ATU Reply Br. at 9-11.

[62] Answer at ¶ 78; ATU Reply Br. at 9-11 (citing *Smith v. Illinois Bell*, 282 U.S. 133 (1930)).

[63] *Id.*

[64] *Smith,* 282 U.S. at 149-50.

[65] *Id. See also Recommended Decision on Separations* at ¶ 12 ("*Smith v. Illinois Bell* does not require absolute precision for cost allocation between the federal and state jurisdictions"); *In the Matter of Applications for Review of the Common Carrier Bureau's Letter of Interpretation Regarding the Clarification of the Role of Direct Assignment in the Jurisdictional Separations Process,* Memorandum Opinion and Order, 8 FCC Rcd 1558, 1560-61 at ¶ 10 (1993) ("*Direct Assignment Order*") (concluding that *Smith* does not require an exact apportionment of interstate and intrastate usages of property, but only a reasonable apportionment; further, (continued….)

D.C. Circuit has recognized, "[c]ost allocation is not purely an economic issue – it necessarily involves policy choices that are not constitutionally prescribed."[66]

32. Assigning ISP traffic costs to the intrastate jurisdiction is a "reasonable measure" based on sound "policy choices." First, as explained above, the Commission was justified in treating ISP traffic-sensitive costs as intrastate for separations purposes, in conjunction with the ESP exemption, to preserve the viability of the still-growing ISP industry. More recently, the Commission retained this policy because it would have been illogical to apply the admittedly inefficient access charge rate structure to ISP traffic for the first time, when the Commission is in the process of modifying that structure.[67] The Commission's decision to retain the ESP exemption has been affirmed as a lawful exercise of the Commission's discretion.[68] The assignment of the traffic-sensitive costs of ISP traffic to the intrastate jurisdiction that follows from the ESP exemption is also lawful, because it derives from the application of our general separations principles to ISP traffic in implementing the ESP exemption. As explained below, the treatment of ISP traffic costs as intrastate for separations purposes prevents a cost-revenue mismatch that the separations rules are designed to avoid.

33. Under Commission rules, separations is "[t]he process by which telecommunications property costs, revenues, expenses, taxes and reserves are apportioned among the [carrier's] *operations*."[69] Further, "[t]he fundamental basis on which separations are made is the use of the telecommunications plant in each of the [carrier's] *operations*."[70] Finally, "operations" is defined as "the general classifications of services rendered to the public for which separate *tariffs* are filed, namely exchange, state toll and interstate toll."[71] Thus, our rules generally link the apportionment of "operations" and the filing of tariffs. The "operation" at issue here is local exchange service, of which ISP services are a part pursuant to the ESP exemption. Local exchange service is provided under intrastate tariffs. Thus, as the "operation" at issue is tariffed at the intrastate level, the carrier should also allocate the costs associated with that operation to the intrastate jurisdiction.[72] To do otherwise would result in the carrier incurring

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separations procedures "provide a balance between the need to reasonably reflect cost causation principles and the goal of simplification").

66 *MCI Telecom. Corp. v. FCC*, 750 F.2d 135, 141 (D.C. Cir. 1984). The Commission's separations rules repeatedly reflect such policy considerations. *See, e.g.,* 47 C.F.R. § 36.125(f) (DEM weighting for small carriers); 47 C.F.R. § 36.154(a) (the ten percent "contamination" rule); 47 C.F.R. § 36.154(c) (allocating 25 percent of local loop costs to interstate jurisdiction).

67 *First Access Charge Reform Order*, 12 FCC Rcd at 16133, ¶¶ 344-45.

68 *SBC*, 153 F.3d at 543-44.

69 47 C.F.R. Part 36, Glossary (emphasis added).

70 *Id.*

71 47 C.F.R. § 36.1(c); 47 C.F.R. Part 36, Glossary (emphasis added).

costs for a service in one jurisdiction, while charging rates to recover those costs in the other jurisdiction, thereby creating a mismatch that the foregoing rules were designed, in part, to prevent.[73]

34. The Commission has previously considered the advisability of permitting such a jurisdictional mismatch between the costs and revenues associated with ISP traffic, and has expressly rejected it. In the *ONA NPRM*, several parties supported allowing ISP traffic costs and revenues to be apportioned to different jurisdictions as an alternative to the ESP exemption.[74] The Commission tentatively rejected this proposal, noting that it would lead to a cost-revenue mismatch between the jurisdictions.[75] Because the Commission had, for valid policy reasons, already required that carriers earn revenues for ISP traffic from the intrastate jurisdiction, the Commission continued to require that costs for such traffic be allocated to the intrastate jurisdiction.[76] Subsequently, in the *ONA Order*, the Commission formally rejected the cost-revenue mismatch proposal.[77]

35. Similarly, in the *Reciprocal Compensation Order*, the Commission acknowledged that one objective of assigning ISP traffic costs to the intrastate jurisdiction for separations purposes is *to avoid* a cost-revenue mismatch associated with such traffic. Significantly, the Commission did not alter this separations treatment even though it acknowledged that ISP traffic is "largely interstate."[78] Indeed, the Commission saw no reason to depart from the "long-standing determination" that, for purposes of jurisdictional separations, "both the costs and the revenues

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[72] Matching the costs with the revenues is not a perfect process, and the separations rules do not require it to be. As explained, *supra,* at n. 76, there may be a small amount of costs, non-traffic-sensitive costs, associated with ISP traffic that are assigned to the interstate jurisdiction pursuant to the flat rate allocator rule embodied in rule 36.154(c) of our rules.

[73] Further, if costs are assigned to a particular jurisdiction, but revenues cannot be recovered in that jurisdiction to recover those costs, then a carrier may rely on that cost-revenue mismatch to assert a "takings" claim (*i.e.*, a claim that the Commission has, by regulation, prevented a carrier from recovering the costs of providing its services).

[74] *ONA NPRM,* 4 FCC Rcd at 3989, ¶ 44.

[75] *Id.*

[76] *ONA NPRM*, 4 FCC Rcd at 3987-88, ¶ 34. We note that this separations treatment of ISP traffic costs applies to traffic-sensitive costs of ISP traffic, which represent the bulk of costs that local exchange carriers incur to process ISP traffic. Any non-traffic-sensitive costs associated with ISP service, such as local loop costs, are subject to a flat rate allocation of 75% to the intrastate jurisdiction and 25% to the interstate jurisdiction. 47 C.F.R. § 36.154(c). However, ATU's assignment of non-traffic-sensitive costs is not at issue in this case. Moreover, the Commission's separations treatment of ISP costs, and the desire to avoid a cost-revenue mismatch, focuses on the traffic-sensitive costs of ISP traffic, not the application of the flat rate allocator to non-traffic-sensitive costs. *ONA NPRM*, 4 FCC Rcd at 3987-88, ¶ 34.

[77] *ONA Order*, 6 FCC Rcd at 4535, ¶ 65.

[78] *Reciprocal Compensation Order*, 14 FCC Rcd at 3702, ¶¶ 18-20.

associated with such [ISP traffic] will continue to be accounted for as intrastate."[79] The Commission was mindful of concerns that a different separations treatment of ISP traffic "may result in allocation to different jurisdictions of the costs and revenues associated with ISP-bound traffic," and the Commission emphasized the undesirability of permitting such a "mismatch" to occur.[80]

36. ATU does not dispute that its conduct caused a cost-revenue mismatch, but argues that the proper remedy is elimination of the ESP exemption, not allocation of ISP traffic costs to the intrastate jurisdiction.[81] ATU's contention ignores the many policy reasons supporting the ESP exemption, which we need not repeat here. Moreover, elimination of the ESP exemption could have prospective effect only, and thus would have no bearing on GCI's damages claims.[82] Thus, we decline ATU's invitation to alter the existing rule in the context of this adjudication.

37. ATU also argues that the Commission's requirement that ISP traffic costs be assigned to the intrastate jurisdiction for separations purposes contravenes section 36.125(b) of the Commission's rules, which generally requires that traffic sensitive costs be separated based on the relative number of interstate and intrastate minutes that pass through the carrier's local switching equipment.[83] However, because the Commission has determined previously that end user access charge rules apply to ISP-bound traffic,[84] and that ISPs must, therefore, purchase their access services pursuant to *intrastate* tariffs,[85] ISP traffic cannot be considered *interstate* for purposes of section 36.125.

38. Finally, ATU argues that, if it must assign ISP traffic costs to the intrastate jurisdiction, then it will not recover revenues adequate to compensate it for the costs of carrying ISP traffic.[86] The Commission addressed this same contention in the *First Access Charge Reform*

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[79] *Id.* at 3710, ¶ 36.

[80] *Id.*

[81] ATU Br. at 9-10. Of course, in so arguing, ATU essentially concedes, as it must, that the Commission has jurisdiction to regulate ISP traffic, contrary to its assertions addressed above based on section 2(b) of the Act.

[82] *See, e.g., Motion Picture Assn. of America, Inc. v. Oman*, 969 F.2d 1154, 1156 (D.C. Cir. 1992) (holding that agencies are not permitted to engage in retroactive rulemaking unless expressly authorized by Congress); *McElroy Electronics Corporation For Authorization to Service Unserved Areas in Metropolitan Statistical Area Market No. 2B*, Memorandum Opinion and Order, 10 FCC Rcd 6762, 6768 (1995) ("the Supreme Court made clear . . . retroactive rulemaking is unlawful unless permitted by statute").

[83] Answer at ¶ 77 (citing 47 C.F.R. § 36.125(b)); ATU Br. at 8-9; ATU Reply Br. at 3-4.

[84] *See, e.g., ONA NPRM*, 4 FCC Rcd at 3988, ¶ 39.

[85] *Id.* at 3988, n. 71.

[86] Answer at ¶¶ 81-82; ATU Reply Br. at 7-8. ATU initially appeared to argue that not allowing it to recover costs for ISP traffic in the interstate jurisdiction would constitute confiscatory rate-making. *Id.* Subsequently, ATU clarified that it was not making such a "takings" claim here. ATU Reply Br. at 8, n.7.

Order, and rejected it as a basis for eliminating the ESP exemption. There, the Commission considered whether continuing to preclude local exchange carriers from assessing access charges on ESPs imposed uncompensated costs on local exchange carriers. The Commission observed that, in addition to the business line rates and subscriber line charges that local exchange carriers receive from ISP customers, local carriers earn additional revenue from ISP usage "through higher demand for second lines by consumers, usage of dedicated data lines by ISPs, and subscription to incumbent LEC Internet usage services."[87] Although the Commission acknowledged that intrastate rates might insufficiently compensate local exchange carriers, like ATU, for the costs of carrying ISP traffic, the Commission expressly noted that carriers could address their concerns in this regard to state regulators.[88] The Eighth Circuit affirmed this analysis in *SBC*.[89] ATU has apparently chosen not to seek such relief from the state regulatory authority for any revenue shortfall it may be experiencing.[90]

39. In sum, we conclude that ATU's assignment of traffic-sensitive ISP traffic costs to the interstate jurisdiction for separations purposes during the 1997-1998 Monitoring Period violated valid Commission orders that the Commission had jurisdiction to issue and that are consistent with separations principles and rules. This improper assignment permitted ATU erroneously to increase its interstate costs for the 1997-1998 Monitoring Period and thereby unlawfully to earn more than its prescribed rate of return.[91]

2. ATU Improperly Counted Only One, Rather Than Two, DEMs for Each Minute of Intraoffice Calls.

40. DEMs are one of the factors that a local exchange carrier must consider in determining how to allocate for separations purposes the costs of local switching equipment. Section 36.125(a)(3) of our rules defines DEM as follows:

> Dial equipment minutes of use (DEM) is defined as the minutes of holding time of the originating and terminating local switching equipment.[92]

The Glossary for Part 36 defines "Holding Time" as:

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[87] 12 FCC Rcd at 16133-34, ¶ 346. ATU has not suggested that it fails to earn such ancillary revenues from ISP traffic.

[88] *Id*. at 16133, ¶ 345.

[89] 153 F.3d at 542.

[90] ATU has not cited any evidence of such a request for relief from state regulatory authorities. Similarly, ATU has not cited any evidence that it has requested a waiver from the Commission for the separations treatment of ISP traffic costs at issue here or for a declaratory ruling that its proposed separations treatment is permissible.

[91] The parties do not dispute that, if ATU had assigned ISP traffic costs to the intrastate jurisdiction for the 1997-1998 Monitoring Period, ATU would have exceeded its prescribed rate of return. Joint Statement at ¶ 14.

[92] 47 C.F.R. § 36.125(a)(3).

> The time in which an item of telephone plant is in actual use either by a customer or an operator. For example, holding time includes conversation time as well as other time in use. . . .[93]

41. As part of the separations process, a local exchange carrier must determine how many DEMs it incurred to carry interstate traffic and how many DEMs it incurred to carry intrastate traffic. For rate-of-return carriers, such as ATU, the greater the proportion of interstate DEMs to the total DEMs, the greater the revenues that the local exchange carrier can obtain from its interstate access customers, such as GCI.

42. The parties disagree concerning how section 36.125(a)(3) of the separations rules should be interpreted and applied to intraoffice calls. Intraoffice calls are intrastate calls that originate and terminate in the same central office. ATU argues that the proper application of section 36.125(a)(3) differs depending on whether the central office at issue employs a digital or an analog switch.[94] According to ATU, when a call originates and terminates at the same central office served by an analog switch, two separate pieces of equipment are actually used (a piece for originating traffic and a piece for terminating traffic), and section 36.125(a)(3) requires that a one-minute call be counted as two DEMs; however "when a call originates and terminates at the same central office served by a digital switch, the relevant 'item of telephone plant' that is 'in actual use' is the single digital switch. . . . Because that single digital switch is the 'originating and terminating' equipment for intraoffice calls, the plain text of Section 36.125 requires that one minute of holding time on that switch be counted as one DEM."[95] ATU asserts, therefore, that because its central offices use digital switches, it properly counted each minute of intraoffice calls as one DEM.

43. We disagree with ATU's approach. The text of section 36.125(a)(3) makes no distinction between digital and analog switches, and it requires carriers to count each minute of intraoffice calls as two DEMs in all circumstances. In particular, the rule requires carriers to count the holding time for both the originating *and* the terminating equipment. Thus, for an intraoffice call lasting one minute, the holding time of the originating local switching equipment is one DEM, and the holding time for the terminating local switching equipment is one DEM, regardless of whether or not the originating and terminating equipment is the same physical device. Accordingly, under section 36.125(a)(3), a one-minute intraoffice call generates two DEMs, not one.

44. Indeed, in 1987, the Federal State Joint Board on Separations ("Joint Board")[96]

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[93] 47 C.F.R. § 36 at Appendix-Glossary.

[94] Answer at ¶ 92; ATU Br. at 10-11.

[95] ATU Br. at 10-11.

[96] The Joint Board was convened in 1980, pursuant to section 410(c) of the Act, to consider various separations procedures and issues and to make recommendations concerning the same to the Commission. 47 U.S.C. § 410(c). It is comprised of three members of the Commission and four state commissioners.

interpreted DEM and its application to intraoffice calls in precisely the manner described above:

> DEM is a measurement of local dial central office switching equipment for jurisdictional separations purposes, where one minute of use is recorded per minute of an originating interoffice or intraoffice call and one minute of use is recorded per minute of a terminating interoffice or intraoffice call.[97]

The Joint Board recognized that this definition meant that each minute of use would be counted as two DEMs for intraoffice calls.[98]

45. Moreover, the Joint Board considered the same argument that ATU asserts here – that it is inappropriate to count two DEMs for each minute of intraoffice calls where a single digital switch, rather than two analog switches, is employed to originate and terminate intraoffice calls.[99] However, instead of accepting that argument and recommending to the Commission that DEM be defined or construed differently to accommodate the digital/analog distinction, the Joint Board sought comment on whether a different cost allocator – Switched Minute of Use (SMOU) – should be adopted for digital central office equipment.[100] The effect of using SMOU as a cost allocator would have been exactly that advocated by ATU here – one minute of use would be counted for each minute of an intraoffice call.[101] As even ATU acknowledges, the Commission

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[97] *In the Matter of Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board*, Order Inviting Comments, 2 FCC Rcd 3787, 3800, n.17 (1987) ("*Order Inviting Comments*"). The *Order Inviting Comments* cited to former section 67.138(c) of our rules for the definition of DEM. 47 C.F.R. § 67.138(c) (1987). Section 67.138 was later replaced by section 36.125, with no substantive change to the definition of DEM.

[98] *Id*. at 3788, ¶ 7.

[99] *Id.*

[100] *Id*. at 3788, ¶¶ 6-12. SMOU was defined as follows: "SMOU is defined as a measurement of local dial central office switching equipment for jurisdictional separations purposes where one minute of use is recorded per minute of an originating interoffice call, one minute of use recorded per minute of a terminating interoffice call, and one minute of use is recorded per minute of an originating intraoffice call." *Id*. at 3800, n.20. *See also, In the Matter of Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board*, Recommended Decision and Order, 2 FCC Rcd 2551, 2560 at ¶¶ 53-54 (1987) (recognizing that various parties were arguing that SMOU, rather than DEM, should be utilized as the allocation factor for central offices employing digital switches).

[101] *Id.* The *Order Inviting Comments* reveals that the application of DEM to intraoffice calls over digital switches that we affirm here was clear not only to the Joint Board, but to those who disagreed with that application, as well. Had DEM been interpreted as ATU suggests now (*i.e*., that intraoffice calls using a digital switch would generate only a single DEM for each minute of use), then it would have been unnecessary for parties to argue that SMOU should be used instead of DEM as the allocation factor for digital switches. The DEM factor, had it been defined as ATU proposes, would have already provided for the result the parties hoped to attain by employing SMOU as the allocation factor. Thus, the fact that parties urged the adoption of SMOU as an allocation factor for intraoffice calls using digital switches, rather than relying on an expansive construction of DEM, supports our conclusion that DEM has never been defined or applied, and should not be defined or applied, as ATU suggests it should be here.

subsequently declined to take any action to adopt the SMOU cost allocation factor. Thus, DEM has remained the applicable factor for all kinds of local switching equipment since 1987.[102]

46. Finally, ATU challenges the consistent, thirteen-year history of DEM allocation and treatment under section 36.125(a)(3) by arguing that requiring DEM to be counted twice for intraoffice calls using a single digital switch would somehow contravene the general principle that rates be cost-based.[103] ATU essentially contends that requiring carriers to count as two DEMs each minute of intraoffice calls switched through digital equipment conflicts with general separations principles, which provide that "the fundamental basis on which separations are made is the use of the telecommunications plant in each of the operations."[104] According to ATU, if the costs are not properly allocated in the separations process, then the rates set as a result of that process will not be cost-based.

47. As we have previously held, however, the specific separations rules govern the general principles: "These general rules [those contained in sections 36.1 and 36.2], are not intended . . . to have primacy over the specific rules."[105] The general separations principle of tying costs to actual usage for rate-making purposes "is intended to supplement, not override, the more detailed procedures prescribed for apportioning specific costs."[106] Thus, even assuming, *arguendo*, that some degree of tension exists between sections 36.1(c) and 36.125(a)(3), section 36.125(a)(3) still governs.

48. In sum, we conclude that ATU's counting of one DEM, rather than two DEMs, for each minute of intraoffice calls violated section 36.125(a)(3) of our rules. This improper counting of DEMs raised the proportion of interstate DEMs to the total DEMs, which permitted ATU erroneously to increase its interstate costs for the 1997-1998 Monitoring Period. This, in turn, enabled ATU unlawfully to earn more than its prescribed rate of return.

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[102] ATU Br. at 11. ATU cites no rule, regulation, or order suggesting that the interpretation of DEM discussed by the Commission in 1987 has been altered or amended. Further, ATU apparently understood, at least until recently, that section 36.125(a)(3) requires it to count each minute of intraoffice calls as two DEMs. ATU concedes that even as late as its January 1998 Tariff filing, it counted intraoffice calls as two DEMs. Responses of Alaska Communications Systems Holdings, Inc. and ACS of Anchorage, Inc. to Interrogatories, File No. EB-00-MD-16 (filed October 20, 2000), at Response to Interrogatory No. 6. If ATU now believes that 36.125(a)(3) should be interpreted differently than it has been in the past, ATU should seek such relief through appropriate means, such as a petition for declaratory ruling, rather than unilaterally adopting a new interpretation of the rule.

[103] Answer at ¶ 90; ATU Reply Br. at 11-12.

[104] 47 C.F.R. § 36.1(c). *See* 47 C.F.R. § 36.2(a).

[105] *Direct Assignment Order*, 8 FCC Rcd at 1560, ¶ 8.

[106] *Id*. at 1559, ¶ 4.

3. ATU's Improper Allocation of ISP Traffic Costs and Counting of DEMs for Intraoffice Calls Result in a Violation of the Rate-of-Return Prescription for the 1997-1998 Monitoring Period.

49. It is well established that the Commission's rate-of-return prescription has the force of a statute, so exceeding that prescription subjects a carrier to liability:

> We have repeatedly held that a rate-of-return prescription has the force of law and that the Commission may therefore treat a violation of the prescription as a per se violation of the requirement of the Communications Act that a common carrier maintain "just and reasonable" rates. . . .[107]

If a carrier exceeds its prescribed rate of return, the Commission can order refunds and award damages to aggrieved customers.[108] Damages may be based on the difference between the amount the customer paid to the carrier and the amount the customer would have paid to the carrier if the carrier had charged and applied its rates in a manner that produced earnings within the prescribed rate-of-return ceiling.[109]

50. The parties agree that, if ATU had assigned ISP traffic costs to the intrastate jurisdiction and counted each minute of intraoffice calls as two DEMs during the 1997-1998 Monitoring Period, then ATU's rate of return would have been approximately 32%, well above its allowable rate of return of 11.65%.[110] Thus, absent some means of "immunity," ATU owes GCI for the difference between the amount of access charges GCI paid to ATU during the 1997-1998 Monitoring period and the amount of access charges that GCI would have paid to ATU during the 1997-1998 Monitoring Period if ATU had achieved earnings within the 11.65% ceiling.

4. Section 204(a)(3) of the Act Does Not Preclude the Commission From Awarding Damages to GCI Based On ATU's Violation of the Rate-of-Return Prescription.

51. ATU argues that the Commission cannot award damages to GCI for ATU's rate-

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[107] *MCI*, 59 F.3d at 1414 (citing and quoting 47 U.S.C. § 201(b)). *See American Tel. & Tel. Co. v. FCC,* 836 F.2d 1386, 1392 (D.C. Cir. 1988); *New England Tel. & Tel. Co. v. FCC*, 826 F.2d 1101, 1106-07 (D.C. Cir. 1987); *Nader v. FCC*, 520 F.2d 182 (D.C. Cir. 1975).

[108] *See New England Tel.*, 826 F.2d at 1107-08 (stating that section 4(i) of the Act provides the Commission with the authority to enforce the rate-of-return prescription by ordering refunds); *see also In the Matter of Amendment of Parts 65 and 69 of the Commission's Rules to Reform the Interstate Rate of Return Represcription and Enforcement Processes*, Report and Order, 10 FCC Rcd 6788, 6848-49 at ¶ 137 (1995) (noting that the complaint process embodied in section 208 of the Act provides a useful tool in enforcing the rate-of-return prescription, and that the Commission is authorized to award damages for violations of the rate-of-return prescription).

[109] *MCI*, 59 F.3d at 1415.

[110] Joint Statement at ¶ 14. *See Rate-of-Return Prescription Order*, 5 FCC Rcd at 7532, ¶ 216; 47 C.F.R. § 65.700(a).

of-return violation in connection with its January 1998 and July 1998 Tariffs, because ATU filed those tariffs under section 204(a)(3) of the Act.[111] According to ATU, section 204(a)(3) and Commission precedent construing that provision immunize ATU from any liability for damages for exceeding its prescribed rate of return for the period covered by the January 1998 and July 1998 Tariffs.[112] For the following reasons, we disagree with ATU.

52. Section 402(b)(1)(A)(iii) of the Telecommunications Act of 1996 added a new section 204(a)(3) to the Communications Act.[113] Section 204(a)(3) provides:

> A local exchange carrier may file with the Commission a new or revised charge, classification, regulation, or practice on a streamlined basis. Any such charge, classification, regulation, or practice shall be *deemed lawful* and shall be effective 7 days (in the case of a reduction in rates) or 15 days (in the case of an increase in rates) after the date on which it is filed with the Commission unless the Commission takes action under paragraph [204 (a)(1)] before the end of that 7-day or 15-day period, as is appropriate.[114]

53. In 1997, the Commission addressed the meaning of the phrase "deemed lawful," as used in section 204(a)(3) of the Act.[115] The Commission concluded that this language provides certain new protections to local exchange carriers who elect to file tariffs on a streamlined basis pursuant to section 204(a)(3). In particular, section 204(a)(3) "immuniz[es] from challenge those rates that are not suspended or investigated before a finding of unlawfulness."[116] The Commission further concluded that, although section 204(a)(3) does not preclude the Commission from requiring a carrier, on a prospective basis, to change a rate or practice that the Commission finds unlawful, section 204(a)(3) does preclude the Commission from subjecting a carrier to liability for damages in a section 208 complaint proceeding for charging such a rate or engaging in such a practice during the period that the streamlined tariff was in effect and prior to the determination of unlawfulness.[117] This conclusion stemmed, in part, from judicial

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111 Answer at ¶¶ 94-96; ATU Br. at 11-20; ATU Reply Br. at 14-18.

112 ATU Br. at 11-20; ATU Reply Br. at 14-18. ATU concedes that its arguments based on section 204(a)(3) afford no protection against calendar year 1997 damages, because ATU filed its 1997 Tariff prior to the effective date of section 204(a)(3). Answer at ¶ 96. The parties agree that the damages amount for 1997, excluding interest, is $1,329,442. Joint Statement at ¶ 15.

113 Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56, § 402(b)(1)(A)(iii); 47 U.S.C. § 204(a)(3).

114 *Id.* (emphasis added).

115 *In the Matter of Implementation of Section 402(b)(1)(A) of the Telecommunications Act of 1996*, Report and Order, 12 FCC Rcd 2170 (1997) ("*Streamlined Tariff Order*").

116 *Id.* at 2183, ¶ 21.

117 *Id.* at 2182-83, ¶¶ 20-21.

interpretations of the same "deemed lawful" language in other statutes.[118] However, it also stemmed, in part, from the fact that section 204(a)(3)'s notice periods provide the Commission and the public with a meaningful, albeit stringent, opportunity to contest filed rates and practices before they become effective.[119]

54. We conclude that section 204(a)(3) affords ATU no relief from GCI's rate-of-return claim in connection with either of ATU's two 1998 tariffs. Regarding the January 1998 Tariff, section 204(a)(3) does not protect ATU, because ATU's violation of the rate-of-return prescription was not ascertainable from the information contained in that Tariff. Regarding the July 1998 Tariff, section 204(a)(3) does not protect ATU, because that Tariff failed to comply with the notice requirements of section 204(a)(3).

55. The text of section 204(a)(3) provides that a LEC "may *file* with the Commission a new or revised charge, classification, regulation, or practice on a streamlined basis," and that any such "charge, classification, regulation, or practice shall be deemed lawful" within a specified time "after the date on which it is *filed*. . . ."[120] Therefore, under the plain language of section 204(a)(3), a practice can be "deemed lawful" only if it is "filed" in a tariff pursuant to the requirements of that section.

56. GCI's rate-of-return claim is predicated on two unlawful practices (*i.e.*, assigning ISP traffic costs to the interstate jurisdiction and counting only one DEM for each minute of intraoffice calls), and neither of these practices appeared in any way in ATU's January 1998 Tariff.[121] Thus, ATU's practices of assigning ISP traffic costs to the interstate jurisdiction for separations purposes and counting only one DEM for each minute of intraoffice calls were not "filed" within the meaning of section 204(a)(3). As a result, these practices cannot be "deemed lawful" under section 204(a)(3). Accordingly, GCI's rate-of-return claim supports an award of damages, because it is based on "practices" that were not "filed" in ATU's January 1998 Tariff in accordance with section 204(a)(3).

57. Our conclusion is supported by the Commission's and courts' prior acknowledgments of the basic differences between a challenge to the lawfulness of a carrier's tariffed rate and a challenge to the lawfulness of a carrier's rate of return. A challenge to the lawfulness of a rate focuses on the reasonableness of the rate in question. A rate-of-return

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[118] *Id.* at 2182, ¶ 19.

[119] *Id.* at 2183, ¶ 24.

[120] 47 U.S.C. § 204(a)(3) (emphases added).

[121] ATU acknowledges that its January 1998 Tariff did not contain information that provided notice that it would assign to the interstate jurisdiction for separations purposes the costs of ISP traffic or would count each minute of intraoffice calls as one DEM. *See,* Letter from Christopher N. Olsen, Attorney, Market Disputes Resolution Division, Enforcement Bureau, to Joe D. Edge, et al., Drinker Biddle & Reath LLP and Karen Brinkmann, et al., Latham & Watkins, File No. EB-00-MD-016 (October 6, 2000), at 1-2; Stipulation of Defendants Alaska Communications Systems Holdings, Inc. and ACS of Anchorage, Inc., File No. EB-00-MD-016 (October 20, 2000), at 1.

challenge, on the other hand, focuses not on the reasonableness of an individual rate in a tariff, but on the cumulative effect of the tariffed rates on the carrier's earnings at the end of a monitoring period, well after the tariff in question was filed.[122] Thus, as the D.C. Circuit has pointed out, a carrier's tariff typically will not provide notice of a future rate-of-return violation, because it is usually difficult, if not impossible, to determine, at the time a tariff is filed, whether the rates set forth in the tariff will produce earnings within the prescribed rate of return at some defined point in the future.[123] This is particularly true here, because ATU failed to include in its January 1998 Tariff any information concerning the two practices that enabled it subsequently to exceed its rate of return. Accordingly, the requirement in section 204(a)(3) that only practices that are "filed" in a tariff warrant "deemed lawful" protection avoids the anomalous result of immunizing from a damage award a violation that was not apparent from the tariff filing involved.

58. ATU argues that the information it includes or fails to include in its tariff is irrelevant for purposes of determining whether section 204(a)(3) applies. In ATU's view, unless a customer or the Commission acts to challenge a carrier's tariff within the seven or fifteen-day period provided for pre-effective tariff reviews in section 204(a)(3), then the carrier is immunized from liability for any subsequent rate-of-return violation covering a period in which the subject tariff was in effect.[124] However, neither the Commission nor the carrier's customers would have any reason or basis to challenge a carrier's tariff filing unless the tariff provides advance notice of a prospective rate-of-return violation.[125] Indeed, ATU's contention that section 204(a)(3) protects it from a rate-of-return violation, regardless of whether it identified certain practices in its tariff is belied by the Commission's emphasis on pre-effective tariff reviews in the *Streamlined Tariff Order*. As the Commission explained, the pre-effective review of tariff filings protects against the imposition of unjust and unreasonable practices and rates. Although the Commission noted that customers and the Commission must conduct swift pre-effective reviews of tariffs filed on a streamlined basis under 204(a)(3), the Commission nevertheless concluded that such reviews

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[122] *See, e.g., MCI*, 59 F.3d at 1415; *AT&T Corp. v. Telephone Util. Exch. Carrier Assoc.,* Memorandum Opinion and Order, 10 FCC Rcd 8405, 8409, n.20 (1995) (stating that an overearnings complaint does not allege that any individual rates are unlawful, but rather alleges that the cumulative application of those rates produced an excessive rate of return). *See also New England Tel.*, 826 F.2d at 1107 (explaining the difference between an order prescribing a maximum rate of return and an order requiring a carrier to set individual rates at specific levels).

[123] *MCI,* 59 F.3d at 1415 ("[A]ny calculation of the rate that will produce a targeted rate of return, whether it is done by the Commission, [a customer], or for that matter a LEC, is necessarily but an estimate. It is not possible to know precisely the effect that any given rate, or change from a prevailing rate, will have upon revenues (and therefore upon the LEC's rate of return); that depends upon the elasticity of the demand for the service, which cannot be known for certain. . .").

[124] ATU Br. at 12-13; ATU Reply Br. at 15-17.

[125] The D.C. Circuit has pointed out the difficulties inherent in predicting rate-of-return violations from information typically contained in tariffs: "If the LEC, with its superior information, could not (or did not) accurately establish such a rate [that would lead to a lawful rate of return], then it seems obvious that the [customer] could not (or should not be expected to) establish such a rate from the outside looking in." *MCI*, 59 F.3d at 1415.

are available and meaningful.[126] If a carrier does not "file" in its tariff the practices that will cause an excessive rate-of-return, then the pre-effective tariff review process is rendered futile for purposes of identifying potential rate-of-return violations, rather than merely difficult.[127]

59. Our rejection of ATU's position finds additional support in the fact that neither the text nor the legislative history of section 204(a)(3) even references, much less vitiates, the Commission's long-standing rules concerning liability for rate-of-return violations.[128] Similarly, the *Streamlined Tariff Order* does not address the impact of its interpretation of the phrase "deemed lawful" on the rate-of-return prescription. The absence of any discussion by Congress or the Commission of the potential impact of section 204(a)(3) on the rate-of-return prescription strongly suggests that neither Congress nor the Commission intended the drastic change to rate-of-return regulation that ATU argues for here.

60. Finally, our conclusion with respect to ATU's section 204(a)(3) argument is not undermined by the fact that, in its July 1998 Tariff, ATU *did* state how it would allocate the costs of ISP traffic and count DEMs for intraoffice calls. This is because, as explained below, the July 1998 Tariff did not satisfy the filing requirements of section 204(a)(3).

61. Under the *Streamlined Tariff Order*, tariffs "that change terms and conditions or apply to new services even where there is no rate increase or decrease" must be filed on 15-days' notice.[129] In fact, "*all* LEC tariff transmittals, other than those that *solely* reduce rates, shall be filed on 15-day's notice."[130]

62. ATU's July 1998 Tariff filing indicated, for the first time, that ATU would engage in "the recording of intraoffice calls as one (1) dial equipment minutes (DEM) and the treatment of all identifiable Internet Service Provider (ISP) traffic as interstate."[131] ATU concedes that those practices differed from those that ATU used in preparing its 1997 and January 1998 Tariffs: "the 1997 and January 1998 Tariffs treated ISP traffic as intrastate and counted intraoffice calls

126 12 FCC Rcd at 2184, ¶ 24.

127 GCI asserts that the "deemed lawful" language of section 204(a)(3) has no application at all to a rate-of-return violation, even where the tariff at issue describes the practices that cause the violation. GCI Br. at 22-25; Reply of General Communication, Inc., File No. EB-00-MD-016 (September 18, 2000) ("GCI Reply") at 5-10. We need not and do not reach this issue here. We conclude only that where, as here, the tariff at issue failed to specify the practices that caused the rate-of-return violation, the carrier who exceeded its prescribed rate of return is not immunized by section 204(a)(3) from a damages award in a complaint proceeding under section 208.

128 Joint Statement of Managers, S. Conf. Rep. No. 104-230, 104th Cong., 2d Sess. at Section 402 (1996); 141 Cong. Rec. S7881-7902 at 7898 (1995); 141 Cong. Rec. S7926-27 (1995). ATU does not dispute that, prior to the 1996 Act, the Commission had long required a carrier who exceeds its allowable rate of return to refund the excess to the affected customers.

129 12 FCC Rcd at 2202-03, ¶¶ 67-68.

130 *Id.* at 2203, ¶ 68 (emphasis added).

131 Complaint, Ex. 4 at 14.

as two DEMs and the July 1998 Tariff treated ISP traffic as interstate and counted intraoffice calls as one DEM."[132] Thus, ATU's treatment of ISP traffic costs and counting of DEMs for intraoffice calls were "change[d] terms and conditions" under the *Streamlined Tariff Order*, and ATU was obligated to file the July 1998 Tariff on 15-days' notice. ATU, however, filed its July 1998 Tariff on only 7-days' notice.[133]

63. It is clear, and the parties do not dispute, that failure to comply with governing notice requirements renders a tariff ineligible for "deemed lawful" treatment under section 204(a)(3).[134] Because ATU failed to comply with the notice requirements applicable to the July 1998 Tariff by filing the tariff on only seven, rather than 15-days' notice, the July 1998 Tariff is not "deemed lawful" under section 204(a)(3).[135]

64. In sum, we conclude that section 204(a)(3) of the Act does not immunize ATU from a damages award for exceeding its prescribed rate of return during the 1997-1998 Monitoring Period. We so conclude because (1) the rate-of-return violation was not ascertainable from the information contained in the January 1998 Tariff, and (2) the July 1998 Tariff did not satisfy the notice requirements of section 204(a)(3).

[132] ATU Reply Br. at 12, n.11. ATU's discovery responses state that, for the January 1998 Tariff, ATU "did not include ISP traffic in its demand projections or the projected traffic sensitive costs associated with such traffic in its revenue requirement." ATU Response to Interrogatory No. 5. It is not clear whether these two assertions by ATU are consistent (*i.e.*, whether ATU treated ISP traffic as intrastate for purposes of its January 1998 Tariff, or whether it simply failed to account for ISP traffic at all in its January 1998 Tariff). Under either scenario, however, ATU's treatment of ISP traffic as interstate in its July 1998 Tariff represents a new or revised treatment of such traffic by ATU, as compared to the January 1998 Tariff.

[133] We need not determine whether the language ATU included in the "Description and Justification" section of its July 1998 Tariff filing concerning ISP traffic and DEM counting for intraoffice calls necessarily constitutes a "charge, classification, regulation, or practice" within the meaning of section 204(a)(3). We need only conclude that, if ATU's statement *is* considered to be a "charge, classification, regulation, or practice" within the meaning of section 204(a)(3), then ATU failed to comply with applicable notice requirements and cannot, therefore, benefit from section 204(a)(3). Alternatively, if ATU's statement as to ISP traffic costs and DEM counting for intraoffice calls is *not* considered to be a "charge, classification, regulation, or practice" within the meaning of section 204(a)(3), then section 204(a)(3) simply does not apply at all.

[134] *See 1997 Annual Access Tariff Filings*, Memorandum Opinion and Order, 13 FCC Rcd 5677, 5705-06 at ¶¶ 78-79 (Com. Car. Bur. 1997) (concluding that tariffs filed on eight and sixteen day's notice not "deemed lawful" under section 204(a)(3)); *Streamlined Tariff Order,* 12 FCC Rcd at 2181-84, 2189 at ¶¶ 25-34 and 62-71.

[135] GCI also contends that the July 1998 Tariff is not deemed lawful, because it allegedly reflected an increase in one of the rates from that set forth in the January 1998 Tariff, and ATU failed to file it on 15-days' notice, as is required for rate increases. GCI Reply at ¶ 11; GCI Reply Br. at 14-16. ATU disputes whether the July 1998 Tariff reflects a rate increase. ATU Br. at 19-20. However, we need not and do not resolve this dispute, because we have concluded that the July 1998 Tariff is not "deemed lawful" for a separate reason.

5. The Statute of Limitations Does Not Bar GCI's Recovery for ATU's Overearnings in 1997.

65. Section 415(c) of the Act provides that complaints against carriers for recovery of damages based on overcharges shall be filed within two years from the time the cause of action accrues.[136] ATU argues that GCI's cause of action accrued in March 1998, when GCI allegedly knew or should have known of the conduct at issue here; ATU further argues, therefore, that the two-year statute of limitations bars GCI's claims for damages for any overcharges in calendar year 1997, because GCI failed to take action as required until more than two years later.[137]

66. ATU's statute of limitations argument is premised on its submission of a preliminary rate-of-return report, dated March 31, 1998, which covered the period January 1, 1997 to December 31, 1997 (Preliminary Monitoring Report).[138] The Preliminary Monitoring Report stated that ATU's preliminary earnings reflected that each minute of intraoffice calls was recorded as one DEM and ISP traffic costs were categorized as interstate.[139] ATU asserts that, because it put GCI on notice on March 31, 1998, as to how it was counting intraoffice calls and treating ISP traffic for calendar year 1997, then GCI was obligated to serve its complaint letter, under section 415(c), or file suit to recover for any damages or overcharges relating to 1997, no later than March 31, 2000.[140] Because GCI did not serve ATU with its complaint letter until April 4, 2000, GCI's claims relating to 1997 are barred, according to ATU.[141]

67. In *MCI v. FCC*, the D.C. Circuit considered when a cause of action accrues for violation of a rate-of-return carrier's prescribed rate of return.[142] The defendant carriers made the same argument that ATU makes here – that submission of a preliminary monitoring report triggered the running of the statute of limitations. The court squarely rejected this argument. The court noted that, until the final monitoring report is submitted, the carrier has the right and opportunity to adjust information contained in preliminary reports.[143] The court explained that "it would be passing strange to require [a complainant] to assume that the preliminary report is a reliable indicator of whether the [carrier] has earned more than allowed."[144] Thus, the court

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136 47 U.S.C. § 415(c).

137 ATU Br. at 20-21. Although ATU failed to allege the statute of limitations as an affirmative defense in its Answer and may, therefore, have waived it, we address the argument, in any event, because the statute of limitations might have affected our jurisdiction to decide GCI's claims for 1997 damages.

138 Answer at Exhibit 2.

139 *Id.*

140 ATU Br. at 20-21.

141 *Id.*

142 59 F.3d at 1416-17.

143 *Id.*

144 *Id.*

"agree[d] with the Commission that a cause of action for damages [. . .] does not accrue until after [the carrier] files its *final* monitoring report."[145]

68. *MCI v. FCC* provides ample support for our conclusion that the statute of limitations did not begin to run until ATU submitted its final monitoring report in September 1999.[146] ATU had the ability to adjust its practices at any time between the time it filed its preliminary report in March 1998 and the time it filed its final report in September 1999.[147] Accordingly, it would be inappropriate to bind GCI to the representations contained in ATU's preliminary report, and we conclude that the statute of limitations does not bar any portion of GCI's claims for damages here.[148]

B. GCI's Remaining Claims Are Dismissed As Moot.

69. In addition to the section 201(b) violation that GCI alleges for ATU's violation of its prescribed rate of return, GCI also alleges that: 1) ATU's tariffs are unjust and unreasonable in violation of section 201(b) of the Act (Count 4); 2) ATU's assignment of ISP traffic costs unjustly and unreasonably imposed charges on GCI for services to which it did not subscribe (Count 5); and 3) ATU's assignment of ISP traffic costs violated the Commission's ESP exemption (Count 6). As explained, *supra*, these counts are based on the same facts and seek the same relief as Counts 1 through 3, which we grant herein. Because we find in favor of GCI and against ATU on Counts 1 through 3 and award the relief GCI seeks in all its counts against

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[145] *Id*. (emphasis added).

[146] *See also AT&T v. TUECA*, 10 FCC Rcd at 8415 ("[T]he date of the filing of the final monitoring report is dispositive with regard to the date a complainant discovers the right or wrong or the facts on which such knowledge is chargeable as a matter of law"); *Allnet Communications Serv., Inc. v. US West, Inc.,* Memorandum Opinion and Order, 8 FCC Rcd 3017, 3019 at ¶ 13 (1993); *US Sprint Communications Ltd. Partnership v. Pacific Northwest Bell Tel. Co*., Memorandum Opinion and Order, 8 FCC Rcd 1288, 1291-92 at ¶ 16 (1993). The D.C. Circuit has also previously rejected the notion that a rate-of-return violation claim can be analyzed for a period less than the full monitoring period. *Virgin Islands Tel. Corp. v. FCC*, 989 F.2d 1231, 1238-39 (D.C. Cir. 1993) ("the target 'authorized return' is a number that has meaning only in relation to the full two-year monitoring period. Thus, it makes no sense to speak of the 'authorized return' for [a six month period]. . . . In order to assess the reasonableness of [the carrier's] earnings as against the authorized rate of return, the Commission was required to consider earnings for the entire period during which the authorized rate was in effect.")

[147] *See* 47 C.F.R. § 65.600(b) (allowing final adjustments to be made to the enforcement period monitoring report until September 30 of the year following the monitoring period in question).

[148] ATU makes a half-hearted attempt to distinguish *MCI v. FCC,* but ultimately ATU "generally agrees that a cause of action in an overearnings case accrues on the date the final monitoring report was filed." ATU Reply Br. at 18. ATU argues that the statute of limitations may bar GCI's claims that do not constitute a claim for overearnings. *Id.* Because we dismiss these other claims (*i.e.*, Counts 4-6 of the Complaint) as moot, *see* Part III(B), *infra*, we need not decide whether the statute of limitations defense would have barred any portion of damages to which GCI would otherwise have been entitled for such claims.

ATU,[149] Counts 4 through 6 of GCI's Complaint are rendered moot and are dismissed.

C. ACS Holdings Is Dismissed From the Case.

70. GCI named the parent company of ATU, ACS Holdings, as a party defendant. GCI claims that ACS Holdings "acted in concert" with ATU in preparing the 1997-1998 Monitoring Report that provided notice of ATU's overearnings.[150] GCI claims that this participation by ACS Holdings makes ACS Holdings a proper party under section 411(a) of the Act, despite the fact that ACS Holdings is not a carrier.[151]

71. GCI's allegation that employees of ACS Holdings assisted ATU in the preparation and filing of the 1997-1998 Monitoring Report that is the subject of the Complaint is insufficient to state a claim against ACS Holdings. GCI does not allege that ACS Holdings itself charged GCI for any services, that ACS Holdings is subject to a rate-of-return prescription, or that ACS Holdings unlawfully exceeded any applicable rate of return. Although the preparation of the 1997-1998 Monitoring Report is relevant to GCI's claims, it is not conduct that, by itself, injured GCI. Because GCI has not alleged that ACS Holdings is responsible for any overcharges to GCI or overearnings by ATU that damaged GCI, we dismiss ACS Holdings from the case.

D. We Calculate the Amount of Prejudgment Interest Due On GCI's Damages Award Based on the I.R.S. Interest Rate for Tax Overpayments.

72. The parties agree that an award of prejudgment interest is appropriate should GCI prevail on its overcharge claim, and that such interest begins to accrue on the date the Monitoring Period ended.[152] The parties disagree, however, concerning which of the following three I.R.S. interest rates should apply to GCI's damages claim (listed here in ascending order of magnitude): 1) the rate for tax underpayments; 2) the rate for tax overpayments; or 3) the rate for large corporate tax overpayments exceeding $10,000.[153] GCI asserts that the first and largest rate is most appropriate here, given that ATU engaged in "willful misconduct."[154] ATU counters that

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149 We do not find in GCI's favor, however, on its claims against ACS Holdings, and we dismiss ACS Holdings from the case. *See* Part III(C), *infra*.

150 Complaint at ¶ 4; GCI Br. at 29; GCI Reply at 11.

151 47 U.S.C. § 411(a) (providing that it is lawful to include in any proceeding to enforce the provisions of the Act, "all persons interested in or affected by the charge, regulation, or practice under consideration, and inquiries, investigations, orders, and decrees may be with reference to and against such additional parties in the same manner, to the same extent, and subject to the same provisions as are or shall be authorized by law with respect to carriers"). The parties apparently agree that ACS Holdings is not itself a carrier within the meaning of the Act.

152 Complaint at ¶ 61; Answer at ¶¶ 97-98. *See, e.g., MCI Telecom. Corp. v. Pacific Northwest Tel. Co.,* Memorandum Opinion and Order, 8 FCC Rcd 1517, 1529-30 at ¶¶ 46-48 (1993).

153 *See* 2000-25 I.R.B. 1262 (GCI Reply at Exhibit 21).

154 GCI Reply Br. at 17-18.

the Commission has never applied the I.R.S. rate for tax underpayments in a case such as this one, and there is no justification to do so here.[155] Further, since the "overpayment" here exceeds $10,000, ATU asserts that the I.R.S. rate for large corporate overpayments should be applied.[156]

73. The award of interest in complaint proceedings under section 208 is a matter left to our sound discretion.[157] In awarding interest, we are guided by considerations of fairness. As part of this analysis, we consider the defendant's conduct in determining which interest rate to apply.[158]

74. We conclude that the I.R.S. rate for tax overpayments, but not large corporate overpayments, is the most appropriate rate to be applied in this case.[159] First, this is the overpayment rate that the Commission has most recently applied, despite the apparent availability of the rate for large corporate overpayments.[160] Further, although we do not necessarily agree with GCI that ATU engaged in "willful misconduct," which might merit awarding the highest interest rate as a penalty, we do note that ATU had at least constructive knowledge, before it prepared its final Monitoring Report, that the Commission had rejected other carriers' attempts to assign ISP traffic to the interstate jurisdiction, and would similarly reject ATU's attempt.[161] Despite this knowledge, ATU improperly assigned its ISP traffic costs to the interstate jurisdiction for separations purposes, which enabled it to reflect an apparently lawful rate of return on its 1997-1998 Monitoring Report. Because ATU acted in a manner that it at least should have known the Commission had already rejected as unlawful, it is proper to award interest at the higher of the two rates for corporate overpayments. Although we might appropriately apply the

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[155] ATU Br. at 22-23.

[156] *Id.*

[157] *MCI,* 8 FCC Rcd at 1529, ¶ 46.

[158] *See, Mile Hi Cable Partners, L.P. v. Public Serv. Co. of Colorado*, Order, 15 FCC Rcd 11450, 11458 at ¶ 14 (Cab. Serv. Bur. 2000); *Long Term Telephone Number Portability Tariff Filings*, 14 FCC Rcd at 17341, n.15 (suggesting that there may be instances where the IRS tax underpayment rate is appropriately applied as a penalty).

[159] *See* 2000-25 I.R.B. 1262 (GCI Reply at Exhibit 21).

[160] *See Long Term Telephone Number Portability Tariff Filings of Ameritech Operating Cos., Pacific Bell, Southwestern Bell Tel. Co. and U.S. West Comm., Inc.*, Memorandum Opinion and Order, 14 FCC Rcd 17339, 17341 at ¶ 5 (1999); *Time Warner Entertainment/Advance-Newhouse Partnership v. Florida Power & Light Co.,* Order, 14 FCC Rcd 9149, 9154, n.36 (1999); *In the Matter of Section 208 Complaint Alleging Violations of the Commission's Rate of Return Prescription,* Memorandum Opinion and Order, 12 FCC Rcd 4007, Attachment A (1997). ATU concedes that it is not aware of any situation in which the Commission has awarded interest at the rate for large corporate overpayments (those exceeding $10,000) and suggests that this dearth of precedent exists because the large corporate overpayment rate was not established until 1995. ATU Br. at 23-24. However, the decisions cited herein were rendered after the adoption of the large corporate overpayment rate in 1995, and we assume that the amount involved in the orders described herein, given the significant rate actions described, exceeded $10,000.

[161] *See supra* at ¶ 21.

rate for large corporate overpayments exceeding $10,000 when a defendant has simply miscalculated revenue or demand and accidently exceeded its rate of return, such is not the case here.

IV. CONCLUSION

75. As explained herein, we conclude that ATU violated Commission orders and rules by assigning to the interstate jurisdiction for separations purposes the costs of carrying ISP traffic, and improperly counted each minute of intraoffice calls as one DEM. These improper practices allowed ATU unlawfully to exceed its prescribed rate of return for the 1997-1998 Monitoring Period, in violation of section 201(b) of the Act. We award damages to GCI for this violation and order additional relief as set forth below.

V. ORDERING CLAUSES

76. Accordingly, IT IS ORDERED, pursuant to sections 4(i), 4(j), 201(b), 206, 207, 208, and 209 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 154(j), 201(b), 206, 207, 208, and 209, that Counts 1, 2, and 3 of the Complaint of GCI ARE GRANTED as against defendant ATU.

77. IT IS FURTHER ORDERED, pursuant to sections 4(i), 4(j), 201(b), 206, 207, 208, and 209 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 154(j), 201(b), 206, 207, 208, and 209, that ATU shall pay GCI damages in the amount of $2,765,371,[162] plus prejudgment interest computed from January 1, 1999 to the date of release of this Order at the I.R.S. rate for corporate overpayments (but not large corporate overpayments exceeding $10,000). ATU shall pay this amount to GCI within 90 days of the date of release of this Order.

78. IT IS FURTHER ORDERED, pursuant to sections 4(i), 4(j), 201(b), and 208 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 154(j), 201(b), and 208, that ATU shall revise its 1997-1998 Monitoring Report in accordance with this Order, and submit the revised report within 90 days of the date of release of this Order.

79. IT IS FURTHER ORDERED, pursuant to sections 4(i), 4(j), 201(b), and 208 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 154(j), 201(b), and 208, that, until further ordered otherwise by the Commission, ATU shall (i) assign to the intrastate jurisdiction for separations purposes the traffic-sensitive costs of carrying ISP traffic, and (ii) count DEMs for intraoffice calls in the manner specified herein.[163]

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[162] The parties agree on the amount of damages at issue here, excluding interest. The parties concluded that ATU's assignment of ISP traffic costs to the interstate jurisdiction and calculation of one DEM for each minute of interoffice calls resulted in disputed charges of $2,765,371 to GCI for the 1997-1998 Monitoring Period. Joint Statement at ¶ 15.

[163] ATU initially challenged the Commission's authority to order any relief other than damages in this case. Answer at ¶ 102. ATU subsequently retreated from that position and agreed to comply with any Commission order requiring it to submit a revised monitoring report and to treat ISP traffic costs and count intraoffice calls as dictated by the Commission. ATU Br. at 24-25. In any event, we note that we do have broad authority, under (continued….)

80. IT IS FURTHER ORDERED, pursuant to sections 4(i), 4(j), 201(b), and 208 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 154(j), 201(b), and 208, that Counts 4, 5, and 6 of the Complaint of GCI ARE DISMISSED as moot.

81. IT IS FURTHER ORDERED, pursuant to sections 4(i), 4(j), 201(b), and 208 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 154(j), 201(b), and 208, that defendant Alaska Communications Systems Holdings, Inc. IS DISMISSED as a defendant in each and every count of the Complaint.

FEDERAL COMMUNICATIONS COMMISSION

Magalie Roman Salas
Secretary

(Continued from previous page)
section 4(i) of the Act, to order relief other than damages. *See, e.g., Amendment of Rules Governing Procedures to be Followed When Formal Complaints Are Filed Against Common* Carriers, Report and Order, 12 FCC Rcd 22497, 22566 at ¶ 159 and n. 464 (stating that the Commission has authority under section 4(i) of the Act to award injunctive relief); *Streamlined Tariff Order*, 12 FCC Rcd at 2182-83 (recognizing the Commission's ability to direct that a carrier cease charging a particular rate for future periods); *Ashtabula Cable TV, Inc. v. Ashtabula Tel. Co.,* Decision, 17 FCC 2d 113, 119 at ¶ 16, *recon. denied*, 18 FCC 2d 193, Memorandum Opinion and Order, (1969) (section 4(i) permits the Commission to tailor remedies to "best meet the particular factual situation before [it]").