Intercarrier Compensation: Nuts and Bolts

by Donna T. Urban and John B. Messenger

To the typical user, telecommunications is a technological black box. You key in a phone number, the call goes through, and you're connected. Unless something goes wrong, you don't know or care how your call is set up and routed, and you'd probably be amazed at how many different telecom providers had a hand in completing it.

You might also be amazed at the complexity and contention involved in determining how much these multiple telecom providers pay each other for their respective roles in completing your calls. This area, known as intercarrier compensation, has consumed an inordinate amount of time and attention on the part of policymakers, regulators, litigators, and the courts over the past decade or two. Although largely invisible to the calling public, intercarrier compensation has a major impact on a telecom carrier's ability to offer service at an attractive price, and to stay in business if it does so. It is, therefore, of tremendous importance to the carriers' investors, employees, suppliers, and customers, in New Jersey and elsewhere.

You might assume that since telecommunications has featured multiple providers for years, the major problems of intercarrier compensation would have been worked out long ago. You might also assume that, as the per-minute price of voice calling has plummeted from over 20 cents to near zero, the importance of intercarrier compensation would have correspondingly diminished.

You would, in fact, be wrong on both counts. Intense financial and market pressures, coupled with the inability of rate levels and regulatory rulings to keep up with industry changes, have resulted in a situation where carriers, like starving hyenas, fight ever more fiercely over ever-diminishing fees. And, of course, the explosion in calling volumes means that disputes over tenths of a cent per minute can still add up to millions of dollars.

This article will provide a brief overview of the issues and tactics involved in intercarrier compensation disputes.

A Complicated Hodgepodge

The law currently governing intercarrier compensation includes jargon, doctrines and rulings from various historical policies dating back to the 1880s. As a result, the 'rules' that determine how much carriers can charge for performing functions are complex, and can be difficult to apply and enforce. This gives rise to widespread confusion and disputes, creating financial uncertainty for telecom carriers.

Local carriers pay for access to each other's networks to deliver calls from their own customers to called parties who are customers of the other local carrier. Long-distance carriers (IXCs) pay for access to both the network of the local carrier serving the calling party and the network of the local carrier serving the called party.

The charges for terminating a call (*i.e.*, for delivering an incoming call to a local carrier's end user customer) depend in part on where the call originated. For terminating a long-distance call that originated in another state, a landline local exchange carrier (LEC) can assess access charges under its interstate access tariff filed with the Federal Communications Commission (FCC). An intrastate long-distance call is subject to access charges regulated by the state public utility commission. And for terminating a local call, the LEC assesses reciprocal compensation charges set forth in an interconnection agreement negotiated with the LEC that originated the call and arbitrated, if necessary, before the state commission based on pricing standards set by the FCC. Because they are set by different jurisdictions using different methodologies, the charges for terminating a call can vary significantly.

The amount that a landline LEC can charge may also depend on what type of technology was used to originate the call. Different charging rules may apply if the call originated on a wireless network or with a voice over Internet protocol (VoIP) provider, even though the LEC on the terminating end uses the same wireline network to complete the call.

Finally, different charging methods may apply if the carrier terminating the call is itself a wireless or VoIP provider, or even based on whether a landline carrier is an incumbent LEC (ILEC) or competitive LEC (CLEC). ILECs are the original former monopoly carriers that existed prior to 1996, while CLECs are those formed after the Telecommunications Act of 1996 permitted local competition. The result of all this is the application of very different rates for performing the same or similar functions.

These rate differences appear to make little sense. The cost to the LEC of terminating a call does not vary depending on where the call came from or what technology it originated in, even though the rate the LEC can charge for it (or whether it can charge at all) varies considerably. And the rate an IXC collects from its customer for a long-distance call does not vary depending on whether the call is terminated to an ILEC, a CLEC, or a wireless carrier, even though the amount the IXC pays to terminate the call (or whether it pays anything at all) does. The result is a series of arbitrary burdens or windfalls.

For certain scenarios it is not always obvious or generally acknowledged what the intercarrier compensation should be. One example of this is the issue of whether tariffed access charges should apply at the terminating end to a call that was originated in VoIP format. Enhanced/information services are exempt from common carrier regulation. The FCC has also permitted providers of these services to connect to the public switched telephone network (PSTN) without paying access charges under the enhanced service provider (ESP) exemption. This depends principally on whether VoIP providers may rely on the ESP exemption created by the FCC in the 1980s for enhanced service providers like pre-Internet computer bulletin boards.

Over the past decade this issue remained unresolved by the FCC, despite numerous requests by multiple parties using a variety of procedural devices. And, although the FCC finally ruled on this issue late last year (see the section on intercarrier compensation reform below), it did so prospectively only, leaving the state of prior law still in doubt. As a result, the void has been filled by inconsistent decisions by state commissions, bankruptcy judges, and federal district courts.

Intercarrier compensation rules can be inherently difficult to apply or enforce. Although the amount to be charged for a call depends in part on where the call originated, the terminating carrier may not always be able to determine this. The telephone number of the calling party is not always transmitted, and even when it is, it is not always a valid indicator of where the call originated. Cellular roaming, nomadic VoIP, and the growing use of virtual telephone numbers and spoofing (*i.e.*, the insertion of a different telephone number for marketing, cosmetic, or other reasons) all result in situations where a call that appears to be interstate may actually be intrastate, or a call that appears to be local may actually be long-distance.

Similar difficulties attend the question of whether a given call originated in VoIP or wireless format, or on a landline. There is typically no information transmitted with the call detail by which the terminating LEC can tell in what type of technology the call originated.

Further compounding the complexity is the issue of which carrier to charge. Calls are often routed to the terminating LEC's network through a tandem switch belonging to another provider, typically a larger LEC. The carrier that owes the compensation (which is usually not the tandem provider) may have no direct network connection or contractual relationship with the terminating LEC that seeks to impose the charges. And it may not always be evident who that carrier is. For various motives (including a desire to avoid a compensation dispute with the terminating LEC), carriers often hand off traffic to least cost routers or other carriers for completion, resulting in a daisy chain through which the call passes on the way to its destination.

At the originating end there is the additional problem of which direction the intercarrier compensation should flow. A LEC that originates a long-distance call typically collects originating access charges from the IXC that provides the long-distance service. If the call is local, the originating LEC does not collect access charges, but instead pays the relevant reciprocal compensation to the terminating LEC. A misclassification can result in a carrier collecting when it should be paying, or vice versa.

Intercarrier Compensation Reform

Help is on the way. After a decade of unsuccessful attempts to improve the intercarrier compensation process, the FCC last year took major strides to resolve the issues outlined above, culminating in a report and order and further notice of proposed rulemaking released Nov. 18, 2011, and effective Dec. 29, 2011.[1]

It is beyond the scope of this article to provide a detailed analysis of the FCC's order, which amounts to 751 pages, including appendices and separate statements by the commissioners. In brief, the FCC laid out a plan that will, over a multi-year transition period, eliminate the rate differences between interstate access, intrastate access, and local reciprocal compensation. It will also eliminate the distinction, for intercarrier compensation purposes, between VoIP-originated calls and calls originated in wireless or traditional circuit-switched technology. And ultimately it will move to a default bill and keep system, in which each carrier collects the revenues it needs to originate or terminate calls from its own end user customers and not from other carriers—much as wireless companies do today.

In the near term, however, the intercarrier compensation reform order will not eliminate intercarrier compensation issues or the need to resolve them. During the multi-year transition period many of the same complexities and difficulties will continue to exist, at least to some extent. Moreover, the order is mostly prospective in effect, meaning it does not address the intercarrier compensation disputes (often amounting to millions of dollars) that were pending or accrued before the end of 2011. For these past-period cases, for example, the order explicitly left undecided whether access charges apply to VoIP-originated calls.

Despite the FCC's commendable efforts this time to promptly address and resolve requests to clarify or reconsider portions of the intercarrier compensation reform order, it is likely that given the magnitude and complexity of the order, differences of opinion will arise regarding how to interpret certain portions of it, and that these differences will lead to disputes that require resolution through litigation or otherwise. And finally, the intercarrier compensation reform order itself is under review in 30 consolidated cases currently pending at the U.S. Court of Appeals for the Tenth Circuit.[2]

Intercarrier Compensation Disputes Nuts and Bolts

Given the level of complexity involved with intercarrier compensation, carriers are disputing increasing amounts of charges, and often refusing to pay altogether. This raises numerous practical and tactical issues for a carrier and its litigation counsel.

Billing

Intercarrier compensation is typically billed in arrears: The bill is not issued until at least a month or two after the traffic is terminated (and the service rendered). In order to issue an accurate bill for the traffic it has already terminated, a LEC must know both whom to bill and how much. If the carrier that owes the compensation is directly (*i.e.*, physically) connected to the billing LEC's network, the LEC can usually determine the details from information recorded by its own switch. But for CLECs and small ILECs, the carrier to be billed is often connected only indirectly, through the tandem switch of a large ILEC or independent tandem provider. In that case the data necessary for billing is recorded by the tandem provider and delivered to the terminating LEC in a computerized format. Either way, the billing LEC must analyze the data and determine the proper carrier to bill (the whom) for each call. The LEC must also be able to jurisdictionalize each call (*i.e.*, determine whether the call was interstate or intrastate, local or long-distance), in order to properly rate it (the how much).

Notice of Dispute

Tariffs and interconnection agreements generally contain provisions requiring the billed party to formally dispute any charges with which it disagrees, and spelling out how and when that must be done. This generally means communicating with the billing carrier to identify the charges being disputed and to provide some notice of the basis of the dispute. Failure to timely and properly dispute the challenged charges can place the billed party at a disadvantage, including perhaps waiver of any claim.

Payment

Classic filed rate doctrine law requires a billed party to pay first, then dispute any challenged charges, and a refusal to comply is sometimes derisively referred to as 'self-help.' However, possession being nine-tenths of the law, this maxim is seldom observed in practice. Typically, disputed charges are only paid if the billed party believes it necessary in order to avoid service-disrupting action by the billing LEC, or if the decision to dispute was not made until after the charges had been paid. Otherwise the billed party is likely to withhold payment of the disputed charges, leaving the billing party with the dilemma of how to collect.

Physical Remedies

Where the billed carrier is directly interconnected to the LEC's network and the governing tariff or interconnection agreement provides for it, the billing LEC may be able to suspend or disconnect service for nonpayment of the disputed charges. Even a credible threat to do this can be a much more effective means of compelling payment than litigation. The disputing carrier may try to seek an injunction to prevent disruptive action, but agencies and courts have generally held that the billed party's ability to pay first negates the necessary irreparable harm showing and precludes injunctive relief.

Where the network connection is only indirect, the terminating LEC is generally unable to refuse to provide service, since the offending carrier's traffic is intermingled with those of other (presumably paying) carrier-customers.

In the reverse situation, a carrier may attempt to block traffic or degrade service on calls bound for a particular LEC as a means of avoiding the LEC's charges for termination. This form of self-help has been held to violate the Communications Act.[3]

Clawbacks and Setoffs

Where the billed carrier has already paid the disputed charges, it may seek to regain the possession advantage by clawing back (*i.e.*, by withholding payment of current (undisputed) charges in an equal amount). Alternatively, a LEC seeking to collect unpaid charges may attempt to 'pay' itself by withholding other, unrelated amounts it owes to the billed carrier, thereby working a unilateral setoff. There may be legal and practical problems with these tactics, but a party's desire to be the one holding the disputed funds can be a powerful motivator.

Forum Selection

When all else fails, the billing carrier may have to resort to litigation in order to collect its charges. But where should intercarrier compensation disputes be litigated (*e.g.*, federal court, the FCC, state public utility commissions)?[4] Under the Communications Act choice of forum provision, Section 207, a carrier may file a complaint with the FCC, or may file suit in federal court, but cannot do both.[5] Federal court is often an attractive alternative to agency proceedings because the court process typically is quicker, and intercarrier compensation disputes often involve interpretation of contract-type tariff language, which is well within the court's competence. Indeed, the FCC has made clear that it is not a collection agency and, therefore, likely will not even accept straightforward intercarrier collection disputes.[6]

A carrier's selection of forum, however, may not always be determinative. Disputes that raise or appear to involve unresolved policy and reasonableness issues, and/or require technical agency expertise, may be more appropriate for agency determination. Although the court generally has jurisdiction over these disputes, courts may elect to invoke the primary jurisdiction doctrine, and thus seek to refer the matter, or particular issues, to the agency (the FCC) for determination (requiring the parties to initiate an administrative proceeding before the FCC and resulting in a stay of the federal court proceeding). Referral is not usually favorable to the litigants, however, because it can result in years of delay and added expense.

FCC Amicus *Briefs*

A growing trend, and an alternative to primary jurisdiction referral, has been for courts to seek guidance from the FCC by inviting the filing of *amicus* briefs by the FCC. This option is becoming more and more prevalent as courts are faced with disputes among carriers that involve contested interpretation of seemingly unclear or ambiguous agency regulations and orders.

Recently, the Supreme Court, in *Talk America, Inc. v. Michigan Bell Telephone Co.*,[7] reinforced the concept that courts owe substantial deference to an agency's interpretation of its own regulations; however, deference to the agency's view does not mean abdication. An agency's interpretation of its own regulations is not entitled to deference if the interpretation is "plainly erroneous or inconsistent with the regulation[s]," or there is any other "reason to suspect that the interpretation does not reflect the agency's fair and considered judgment on the matter in question."[8] Indeed, if an agency's opinions always controlled, then agency action could never be challenged.

Deemed Lawfulness

Another concept to be aware of when intercarrier compensation disputes arise is 'deemed lawfulness.' Deemed lawfulness is a fundamental and statutorily required federal telecommunications concept that bars retrospective relief. Under Section 204(a)(3) of the Communications Act, LECs can seek deemed lawful protection for their tariffs by filing access tariffs on a streamlined basis, and those tariffs are deemed lawful unless they are suspended by the commission before taking effect.

> 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….47 U.S.C. 204(a)(3). Deemed lawfulness results in a conclusive presumption that the LEC's tariff is reasonable and lawful during the time period the tariff is in effect—"a streamlined tariff that takes effect without prior suspension or investigation is conclusively presumed to be reasonable and, thus, a lawful tariff during the period that the tariff remains in effect."[9]

The key effect of this principle is that 'deemed lawful' tariffs must be enforced and cannot be modified retroactively—the tariff must be enforced until the date, if any, that a decision is rendered holding it to be unlawful. Therefore, retrospective relief cannot be awarded on a lawful tariff even if that tariff is later invalidated or declared unlawful in a legal proceeding.[10]

Conclusion

As reform unfolds, it is still important for carriers and their counsel to be conversant with the issues and tactics involved in intercarrier compensation disputes, even as they keep up with new regulatory decisions, rules and court rulings. ⚖

Endnotes

1. *See In the Matter of Connect America Fund, A National Broadband Plan for Our Future, Establishing Just and Reasonable Rates for Local Exchange Carriers, High-Cost Universal Service Support, Developing an Unified Intercarrier Compensation Regime, Federal-State Joint Board on Universal Service, Lifeline and Link-Up, Universal Service Reform—Mobility Fund*, WC Docket No. 10-90, GN Docket No. 09-51, WC Docket No. 07-135, WC Docket No. 05-337, CC Docket No. 01-92, CC Docket No. 96-45, WC Docket No. 03-109, WT Docket No. 10-208, Report and Order and Further Notice of Proposed Rulemaking, FCC 11-161, 26 FCC Rcd 17663 (2011)(Intercarrier Compensation Reform Order). Petitions for review and notices of appeal pending *sub nom. In re: FCC 11-161,* No. 11-9900 (10th Cir. filed Dec. 8, 2011).
2. *In re: FCC 11-161*, No. 11-9900 (10th Cir. filed Dec. 8, 2011).
3. *Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, *Establishing Just and Reasonable Rates for Local Exchange Carriers*, WC Docket No. 07-135, Declaratory Ruling DA 12-154, 27 FCC Rcd 1351 (WCB 2012).
4. State public utility commissions (PUCs) handle disputes involving intrastate charges and therefore have certain limitations. If the charges in dispute span multiple states, the carrier electing the state PUC route will be required to file multiple separate

state proceedings. This could be very costly and could lead to sporadic and perhaps inconsistent rulings.

5. "Any person claiming to be damaged by any common carrier subject to the provisions of this chapter may either make complaint to the Commission…or may bring suit for the recovery of the damages for which such common carrier may be liable under the provisions of this chapter, in any district court of the United States of competent jurisdiction; but such person shall not have the right to pursue both such remedies." 47 U.S.C. § 207.
6. *U.S. Telepacific Corp. v. Tel-America of Salt Lake City, Inc.*, 19 FCC Rcd. 24552, 2004 WL 2889847 (2004) (proper forum for "action for recovery of unpaid access charges that are allegedly due under the terms of a federal tariff" is federal district court).
7. *Talk America, Inc. v. Michigan Bell Telephone Co.*, 131 S. Ct. 2254, 2261 (2011).
8. *Talk America*, 131 S. Ct. at 2261 (*quoting Auer v. Robbins*, 519 U.S. 452, 461-62 (1997)).
9. Report and Order, *In re Implementation of Section 402(b)(1)(A) of the Telecommunications Act of 1996*, 12 FCC Rcd. 2170, 1997 WL 37342, ¶ 19 (1997), *reconsideration denied*, 17 FCC Rcd. 17040, 2002 WL 31039872 (2002) (Streamlined Tariff Order); *see also, e.g., ACS of Anchorage, Inc. v. FCC*, 290 F.3d 403 (D.C. Cir. 2002); *Virgin Islands Tel. Corp. v. FCC*, 444 F.3d 666, 669 (D.C. Cir. 2006).
10. *See ACS of Anchorage*, 290 F.3d at 411 (Even if such a tariff is later determined to be unlawful, "the Commission's available remedies will be prospective only."); *Virgin Islands Tel. Corp.*, 444 F.3d at 669 ("[r]emedies against carriers charging lawful rates later found unreasonable must be prospective only.") (emphasis added); *Qwest Communications Corp. v. Farmers and Merchants Mutual Telephone Co.*, 22 FCC Rcd. 17973, 2007 WL 2872754, n. 52 ("Since the passage of section 204(a)(3) of the Act, the Commission cannot award refunds in connection with tariffs that are deemed lawful."); Streamlined Tariff Order, 1997 WL 37342, ¶¶ 8, 18 (interpreting "deemed lawful" to mean that the FCC "could not award refunds or damages for the time that the rate was in effect but could only order tariff revisions or award damages on a prospective basis.")

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