

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

Pac-West Telecomm, Inc.,

Complainant,

vs.

AT&T Communications of California, Inc.,  
Teleport Communications Group of San  
Francisco, Teleport Communications Group of  
Los Angeles, Teleport Communications Group of  
San Diego,

Defendants.

Case 04-10-024  
(Filed October 20, 2004)

**JOINT ASSIGNED COMMISSIONER AND  
ADMINISTRATIVE LAW JUDGE'S RULING AND SCOPING MEMO**

**A. Summary**

Pursuant to Rules 6(b)(3) and 6.3 of the Commission's Rules of Practice and Procedure, this ruling sets forth the procedural schedule, assigns a presiding officer, and addresses the scope of the proceeding following a prehearing conference (PHC) held on January 7, 2005.

**B. Background**

The complaint in this case alleges that defendant AT&T Communications of California, Inc. and three of its subsidiaries (collectively, AT&T) have refused to pay the complainant, Pac-West Telecomm, Inc. (Pac-West), the charges lawfully due for calls that AT&T originates for its local exchange customers and

routes to Pac-West through the tandem switches of incumbent local exchange carriers (ILECs).

The complaint notes that while Pac-West and AT&T each have interconnection agreements with California's two principal ILECs, Pacific Bell Telephone Company<sup>1</sup> and Verizon California, they do not have an interconnection agreement with each other. In the absence of such an agreement, Pac-West contends, it is entitled to the termination charges set forth in its intrastate tariffs for traffic that originates with AT&T customers and is transmitted to Pac-West by the ILECs. Pac-West alleges that AT&T has refused to pay any of the statements it has rendered for these charges, which now total about \$6 million.<sup>2</sup> As relief, Pac-West asks not only that AT&T be ordered to pay all the charges for which it has been invoiced, but also to pay all future charges based on Pac-West's intrastate tariffs "unless and until the AT&T Companies enter into a direct interconnection agreement with Pac-West."

In its answer, AT&T contends that no charges are due. Since the overwhelming majority of the traffic that ILECs transmit to Pac-West for AT&T is bound for Internet service providers (ISPs), AT&T argues, this case is governed by the so-called "ISP Remand Order" issued by the Federal Communications

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<sup>1</sup> Pacific Bell Telephone Company now does business as SBC California, the name by which it is referred to in the complaint.

<sup>2</sup> Paragraph 5 of the complaint alleged that "the AT&T Companies have refused to pay over \$3.5 million of applicable tariffed Pac-West charges that they have incurred." In an e-mail message sent to the Administrative Law Judge on December 21, 2004, Pac-West's counsel stated that she had discovered this amount was incorrect, that errors had been made by the billing company used by Pac-West to prepare the bills submitted to AT&T, and that the amount that should have been billed to AT&T under Pac-West's theory of the case was closer to \$6 million. As explained in the text, Pac-West has been instructed to set forth in its testimony on relief the amount it contends is actually due from AT&T.

Commission (FCC) in April 2001.<sup>3</sup> In the ISP Remand Order, the FCC concluded that because of the regulatory arbitrage that had arisen as a result of certain competitive local exchange carriers (CLECs) targeting ISPs as their customers (thus entitling these CLECs to substantial amounts of reciprocal compensation),<sup>4</sup>

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<sup>3</sup> *Order on Remand and Report and Order*, CC Docket Nos. 96-98 and 99-68 (FCC 01-131), released April 27, 2001, 16 FCC Rcd 9151. AT&T acknowledges that the United States Court of Appeals for the District of Columbia Circuit subsequently found that the statutory provisions relied on by the FCC did not support the ISP Remand Order, but points out that the D.C. Circuit remanded the order to the FCC for further consideration without vacating it. *Worldcom, Inc. v. FCC*, 288 F.3d 429, 434 (D.C. Cir 2002), *cert. denied sub nom. Core Communications, Inc. v. FCC*, 538 U.S. 1012 (2003). As a result of this unusual procedural posture, other courts (including the Ninth Circuit) have noted that the provisions of the ISP Remand Order remain in effect despite the D.C. Circuit's conclusions about the deficiencies in its statutory analysis. *See, e.g., Pacific Bell v. Pac-West Telecomm, Inc.*, 325 F.3d 1114, 1122-23 (9<sup>th</sup> Cir. 2003).

<sup>4</sup> In the ISP Remand Order, after noting (in ¶ 20) that reciprocal compensation had grown up because of the assumption that “traffic back and forth on . . . interconnected networks would be relatively balanced,” the FCC described the problem of regulatory arbitrage connected with ISPs as follows:

“Internet usage has distorted the traditional assumptions because traffic to an ISP flows exclusively in one direction, creating an opportunity for regulatory arbitrage and leading to uneconomical results. Because traffic to ISPs flows one way, so does money in a reciprocal compensation regime. It was not long before some LECs saw the opportunity to sign up ISPs as customers and collect, rather than pay, compensation because ISP modems do not generally call anyone in the exchange. In some instances, this led to classic regulatory arbitrage that had two troubling effects: (1) it created incentives for inefficient entry of LECs intent on serving ISPs exclusively and not offering viable local telephone competition, as Congress had intended to facilitate with the 1996 Act; (2) the large one-way flows of cash made it possible for LECs serving ISPs to afford to pay their own customers to use their services, potentially driving ISP rates to consumers to uneconomical levels. These effects prompted the Commission to consider the nature of ISP-bound traffic and to examine whether whether there was any flexibility under the statute to modify and address the pricing mechanisms for this traffic . . .” (ISP Remand Order ¶ 21; 16 FCC Rcd at 9162.)

the FCC should use its authority to preempt this area and require the affected carriers to make a three-year transition to the “bill and keep” compensation system.<sup>5</sup>

AT&T especially relies on ¶ 81 of the ISP Remand Order, which states that for carriers not having an interconnection agreement in effect on the issuance date of the ISP Remand Order (as AT&T and Pac-West did not), ISP-bound traffic must be exchanged on a bill-and-keep basis.<sup>6</sup> AT&T concludes that since the ISP

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<sup>5</sup> Footnote 6 of the ISP Remand Order defines “bill and keep” as follows:

“‘Bill and keep’ refers to an arrangement in which neither of two interconnecting networks charges the other for terminating traffic that originates on the other network. Instead, each network recovers from its own end-users the cost of both originating traffic that it delivers to the other network and terminating traffic that it receives from the other network . . . Bill and keep does not, however, preclude intercarrier charges for transport of traffic between carriers’ networks.” (16 FCC Rcd at 9153; citations omitted.)

<sup>6</sup> ¶81 of the ISP Remand Order states in pertinent part:

“[A] different rule applies in the case where carriers are not exchanging traffic pursuant to interconnection agreements prior to adoption of this Order . . . In such a case, as of the effective date of this Order, carriers shall exchange ISP-bound traffic on a bill-and-keep basis during this interim period. We adopt this rule for several reasons. First, our goal here is to address and curtail a pressing problem that has created opportunities for regulatory arbitrage and distorted the operation of competitive markets. In so doing, we seek to confine these market problems to the maximum extent while seeking an appropriate long-term resolution in the proceeding initiated by the companion [notice of proposed rulemaking]. Allowing carriers in the interim to expand into new markets using the very intercarrier compensation mechanisms that have led to the existing problems would exacerbate the market problems we seek to ameliorate. For this reason, we believe that a standstill on any expansion of the old compensation regime into new markets is the more appropriate interim answer. Second, unlike most carriers that are presently serving ISP customers under existing interconnection agreements, carriers entering new markets to serve ISPs have not acted in reliance on reciprocal compensation revenues and thus have no need of a transition

*Footnote continued on next page*

Remand Order preempts state law in this area (including any charges in intrastate tariffs), and since AT&T has met its obligation to exchange traffic on a bill-and-keep basis, it owes Pac-West nothing. AT&T also contends that as a CLEC rather than an ILEC, it has no obligation under the Telecommunications Act of 1996 to enter into an interconnection agreement with Pac-West. Thus, AT&T contends, the complaint herein should be dismissed.

### **C. The Discussion at the PHC**

Shortly before January 7, both parties submitted statements on the issues to be addressed at the PHC. In its statement, after summarizing the pleadings, Pac-West stated that the parties “do not fundamentally disagree over the legal issues that give rise to the dispute,” and proposed that the Commission should have a two-phase proceeding, with the first phase devoted to the question “whether the law requires AT&T to compensate Pac-West and the structure of that compensation mechanism,” before investigating in the second phase “the facts underlying the amounts allegedly due.” In keeping with this suggestion for phasing, Pac-West proposed that the first-phase briefs should be deal with the following issues:

“1. To what extent has the FCC, in its *ISP Remand Order* and subsequent decisions, preempted state jurisdiction over compensation for ISP-traffic exchanged between competitive local exchange carriers?

2. Under what circumstances does the *ISP Remand Order* mandate a bill-and-keep compensation mechanism in situations where two competitive carriers indirectly exchange traffic

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during which to make adjustments in their business plans.” (16 FCC Rcd at 9188-89; footnote omitted.)

pursuant to the terms and conditions regarding transit traffic set forth in the interconnection agreements each competitive carrier has with incumbent carriers?

3. When a bill-and-keep compensation mechanism is not required, as a legal matter, then what compensation mechanism should apply to the traffic that is the subject matter of this Complaint?” (Pac-West PHC Statement, p. 3; footnote omitted.)

Pac-West proposed that the parties exchange opening briefs on February 18 and reply briefs on March 11, 2005. This schedule, Pac-West asserted, would “allow[] the Commission ample time to issue a decision and conduct any subsequent proceedings, should they be necessary, within the [one-year] time period required by Cal. Pub. Util. Code Section 1701.2(d).” (*Id.* at

4.) Pac-West also stated that for purposes of briefing in the first phase, it would stipulate to the following facts:

- “1. AT&T is not required by 47 U.S.C. § 252 to enter into interconnection agreements with other competitive local exchange carriers;
2. AT&T and Pac-West have not entered into an interconnection agreement;
3. AT&T and Pac-West were exchanging traffic on the date of the FCC’s ISP Remand Order; and
4. All of the traffic that is the subject of this dispute is ISP-bound.” (*Id.* at 4.)

In its PHC statement, AT&T agreed that the case presented threshold legal issues as to the scope and effect of the ISP Remand Order, and asserted that the parties’ contentions could be set forth in “briefs that can be characterized as briefs on cross-motions for summary judgment.” (AT&T PHC Statement, p. 2.)

Although differing somewhat in its formulation of the issues to be briefed,<sup>7</sup> AT&T also endorsed the February 18 and March 11 briefing dates proposed by Pac-West. AT&T also agreed that if a decision in Pac-West's favor was issued on the threshold legal questions, then a second phase of the proceeding -- with adequate time for discovery -- should be held to determine the amount of compensation due to Pac-West.

At the PHC, the ALJ agreed that the parties' proposal for briefs on the threshold legal issues was a good one, although he thought the due dates should be shortened somewhat. He also asked Pac-West's counsel to state her position on whether ¶ 81 of the ISP Remand Order was dispositive here, since there seemed to be no dispute that the order has continued in effect despite the D.C. Circuit's decision in *Worldcom, Inc. v. FCC*. In response to the ALJ's question, Pac-West's counsel stated:

“[W]hen you read [¶ 81] in the context of both the rather lengthy section of the ISP Remand Order discussing the whole . . . issue, and when you read it in the context of the subsequent FCC decisions, in particular the Core Communications order that was released back in October . . . that further interpreted it, our theory is that the language in paragraph 81 which AT&T has taken out of context only applies to CLEC-ILEC traffic exchanges; that it

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<sup>7</sup> In its PHC Statement, AT&T framed the legal issues as follows:

“Has the FCC mandated that the exchange of ISP-bound traffic between carriers that have not entered into an interconnection agreement be exchanged on a bill-and-keep reciprocal compensation basis?

Does the Telecommunications Act of 1996 and industry practice support the exchange of terminating local traffic on a bill-and-keep basis between CLECs that have not entered into an interconnection agreement?

Have AT&T and Pac-West been exchanging terminating traffic on a bill-and-keep basis?” (AT&T PHC Statement, p. 3.)

does not apply to CLEC to CLEC traffic exchanges [such as those between Pac-West and AT&T].” (PHC Transcript, p. 11.)

The ALJ noted that because of the one-year deadline in Pub. Util. Code § 1701.2(d), it would not be feasible to have a two-phase proceeding, as both Pac-West and AT&T had suggested. Instead, the ALJ stated, at the same time the parties were writing their briefs on the legal issues raised by the ISP Remand Order, “you want to be putting effort in on seeing if you can reach agreement on the number of minutes that are in dispute and what . . . possible amounts due by AT&T to Pac-West would flow from that in the event Pac-West were to prevail on . . . its [liability] theory.” (Tr. at 16.) Thus, the ALJ stated, the parties would be required to submit testimony on the amount of compensation that should be paid to Pac-West (in the event it prevailed on liability) at the same time that reply briefs on the liability issues were being drafted.

Pac-West and AT&T both replied that although they still preferred phasing, it would be feasible to submit testimony on compensation issues at the same time the legal issues were being briefed. However, they pointed out that even if they could agree on the number of minutes for which compensation would be due under Pac-West’s liability theory, they were likely to submit a menu of possible compensation awards, since there were significant disputes between them as to which rates should apply, as well as the time period for which Pac-West could recover compensation under its liability theory.<sup>8</sup>

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<sup>8</sup> For example, AT&T’s counsel stated:

“I want to make sure that you understand this, that it wouldn’t be just one number. That based on the possibilities of how the legal arguments go, there could be different numbers presented to you for you to decide . . .

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*Footnote continued on next page*

#### D. Scope of the Proceeding

Pursuant to the discussion at the PHC, the issues to be decided in this proceeding are as follows:

1. Does ¶ 81 of the ISP Remand Order control here, so that AT&T is not obliged to compensate Pac-West for ISP-bound traffic originating with AT&T local exchange customers and terminated by Pac-West, but rather is required only to exchange such traffic with Pac-West on a bill-and-keep basis?
2. Under federal law, does ¶ 81 of the ISP Remand Order not apply to the situation here, in which two CLECs that indirectly exchange ISP-bound traffic have not entered into an interconnection agreement, but rather exchange the traffic pursuant to transit arrangements with an ILEC that has entered into separate interconnection agreements with each of them?
3. In the event the answer to Question 2 is that ¶ 81 of the ISP Remand Order does not control here, does the ISP Remand Order nonetheless preempt state regulation of the kind of traffic exchanges described in Question 2? If so, what compensation, if any, is required to be paid to the CLEC that

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For example – I don't know this yet because we haven't seen [support for Pac-West's] change from 3-1/2 to 6 million, but we might want to argue that some of that is barred by estoppel or statute of limitations or whatever . . .” (PHC Transcript, pp. 12-13.)

At another point, AT&T's counsel noted that as a result of Commission decisions, special rules apply as to how long one can back-bill for various types of telecommunications charges; *e.g.*, 90 days for residential customers and 18 months for access charges. (*Id.* at 14.)

Pac-West's counsel noted that if the Commission rules it is due any compensation, Pac-West might want to argue that not all of the terminating traffic for which it is seeking compensation is ISP-bound. Thus, counsel agreed, the fourth stipulation set forth in the text would not apply to any testimony or briefing on compensation issues. (*Id.* at 20.)

terminates the ISP-bound traffic?

4. If the ISP Remand Order does not preempt state regulation of the situation described in Question 2, what compensation, if any, does Commission precedent require to be paid to the CLEC that terminates the ISP-bound traffic?

#### **E. Schedule for the Proceeding**

Pursuant to the discussion at the PHC, the schedule for this proceeding will be as follows:

Opening briefs filed on legal issues	February 11, 2005
Testimony served on what compensation, if any, is due from AT&T to Pac-West	February 25, 2005
Reply briefs filed on legal issues	March 11, 2005
Hearings held on what compensation, if any, is due from AT&T to Pac-West	April 12-15, 2005

At the conclusion of the hearings, the assigned Administrative Law Judge (ALJ) will set due dates for briefs on the compensation issues. At the present time, we do not foresee any circumstances that would preclude the Commission from resolving this case within the 12-month period for adjudicatory proceedings set forth in Pub. Util. Code § 1701.2(d).

#### **F. Categorization and Need for Hearing**

This ruling confirms that this is an adjudication proceeding and that a hearing will be required unless the matter is otherwise disposed of, as set forth in the Instructions to Answer the complaint mailed on October 28, 2004.

#### **G. Assignment of Presiding Officer**

ALJ A. Kirk McKenzie is hereby designated as the presiding officer pursuant to Rule 6.3 of the Commission's Rules of Practice and Procedure.

**H. *Ex Parte* Rules**

*Ex parte* communications as to the issues within the scope of this proceeding are prohibited under Pub. Util. Code § 1701.2(b) and Rule 7(b).

In accordance with the foregoing discussion, **IT IS RULED** that:

1. The scope of this proceeding shall be as set forth in Section D above.
2. The schedule for this proceeding shall be as set forth in Section E above.
3. The presiding officer will be Administrative Law Judge McKenzie.
4. This proceeding is an adjudication scheduled for hearing.
5. *Ex parte* communications are prohibited under Pub. Util. Code § 1701.2(b) and Rule 7(b).

Dated February 14, 2005, at San Francisco, California.

/s/ SUSAN P. KENNEDY  
Susan P. Kennedy  
Assigned Commissioner

/s/ A. KIRK MCKENZIE  
A. Kirk McKenzie  
Administrative Law Judge

**CERTIFICATE OF SERVICE**

I certify that I have by mail, and by electronic mail, to the parties to which an electronic mail address has been provided, this day served a true copy of the original attached Joint Assigned Commissioner and Administrative Law Judge's Ruling and Scoping Memo on all parties of record in this proceeding or their attorneys of record.

Dated February 14, 2005, at San Francisco, California.

/s/ TERESITA C. GALLARDO  
Teresita C. Gallardo

**N O T I C E**

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