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December 6, 2010

EX PARTE

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554

RE: <u>Establishing Just and Reasonable Rates for Local Exchange Carriers, WC Docket No. 07-135</u>

Dear Ms. Dortch:

Empowered by years of Commission inaction to stop traffic pumping, North County Communications Corporation ("NCC"), a longtime traffic pumper, is now attempting to legitimize these harmful scams through a contrived attack on Verizon. NCC's latest filings follow from traffic pumping litigation with Verizon in California.[1] The allegations in NCC's diatribe are frivolous and wrong and have been recycled by traffic pumpers many times. There is nothing redeeming about illegal traffic pumping scams. The Commission must step up and put a stop to traffic pumping—immediately.

Traffic pumping is a growing problem that has cost consumers and the industry approximately $2.3 billion over the last five years and approximately $400 million per year.[2]

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1 Letter from Joseph G. Dicks, Counsel to NCC, to Marlene H. Dortch, FCC, *Developing a Unified Intercarrier Compensation Regime*; *Establishing Just and Reasonable Rates for Local Exchange Carriers*, CC Docket No. 01- 92, WC Docket No. 07-135 (Nov. 12, 2010) ("NCC Letter"); *see also* Letter from Jonathan E. Canis, Arent Fox (counsel to NCC), to Marlene H. Dortch, FCC, WC Docket No. 07-135 (Nov. 18, 2010) ("NCC Follow-Up Letter") (repeating allegations in the NCC Letter).

2 *See* TEOCO Corp., "Traffic Pumping Bleeds CSPs of Billions," http://www.teoco.com/local/upload/fckjail//homenews/file/access-stimulation-responsible-for-2-3-billlion-in-cost.pdf (2010); *see also* Ex Parte Letter from Donna Epps, Verizon, to Marlene H. Dortch, FCC, *Developing a Unified Intercarrier Compensation Regime*; *Establishing Just and Reasonable Rates for Local Exchange Carriers*, CC Docket No. 01- 92, WC Docket No. 07-135 (Nov. 12, 2010).

These schemes cost the domestic wireless industry alone more than $190 million annually[3] and now have the potential to explode in the wake of the Commission's decision in *North County Communications Corp. v. FCC*, Order on Review, 24 FCC Rcd 14036 (2009) ("*North County Order*"), declining to enforce Commission rules or to provide any guidance as to the proper rate for intraMTA CMRS traffic terminated by CLECs. In fact, wireless companies are now engaged in more than 60 traffic pumping disputes nationwide—despite NCC's claim that there is no problem.[4] Equally bizarre, NCC now suggests that because the Commission thus far has not adopted a long-term solution to traffic pumping, IXCs and wireless carriers should instead raise their prices to cover the cost of these scams and dump huge windfalls on perpetrators such as NCC. NCC Letter at 2, 7. Attractive as that might be to the traffic pumpers, this is hardly a consumer-first response.

Try as NCC does to distinguish the situation, the present traffic pumping scams are but the latest iterations of arbitrage following the dial-up ISP schemes that resulted in the Commission's ISP rate regime. *Id*. These schemes also siphoned billions of dollars out of the intercarrier compensation system and did not stop until the Commission took decisive action. In fact, the ISP scams festered for more than a decade and were not killed for good until just a few weeks ago when the Supreme Court denied *certiorari*, refusing to hear a further appeal on the Commission's authority to put a stop to this harmful arbitrage.[5] Traffic pumping must, likewise, be stopped. These schemes are ultimately no good for anyone except those like NCC seeking to get rich on the backs of consumers.

NCC is a bad actor and Verizon is not "harassing" anyone. NCC opens its letter with a plea that action by the Commission to stamp out traffic pumping abuses will harm non-profit organizations, such as an AIDS information hotline. NCC Letter at 1-2. The business conducted by NCC, however, is nothing of the sort and serves no public interest purpose. From what Verizon can determine, NCC is a CLEC whose business consists of serving sex chat lines (NCC's "customers") that are accessed by making a regular telephone call.[6] NCC's "customer"

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[3] *See* Connectiv Solutions, *Understanding Traffic Pumping, Industry Study*, http://www.connectiv-solutions.com/traffic-pumping.html (2010).

[4] *See* Ex Parte Letter from Scott K. Bergmann, CTIA– The Wireless Association, to Marlene H. Dortch, FCC, *Developing a Unified Intercarrier Compensation Regime*; *Establishing Just and Reasonable Rates for Local Exchange Carriers*, CC Docket No. 01- 92, WC Docket No. 07-135 (Nov. 24, 2010) ("CTIA Traffic-Pumping Letter").

[5] Petition for a Writ of Certioriari, *Pennsylvania Public Utility Commission v. Federal Communications Commission*, No. 10-189 (Aug. 6, 2010); *cert. denied* (Nov. 15, 2010).

[6] *North County Communications. Corp. v. Allegiance Telecom Int'l, Inc.*, 2010 U.S. Dist. LEXIS 117187 (D. Or. Oct. 4, 2010), n.2.; *see also* Petition for a Writ of Certioriari, *North*

is in fact the chat-line company that is also owned by NCC's president, Todd Lesser. That company, HFT, Inc., is served by NCC and provides free pornographic chat services, as well as pay-per-call 900 services. Mr. Lesser also is the president of Jartel, Inc., another chat-line company.

Customers of Verizon and other carriers make calls to these supposed "free" chat lines served by NCC. NCC uses different techniques to ensure that Verizon's end-users make long-distance, rather than local calls, to reach these chat-lines. For example, the prerecorded information on the call often directs callers to make calls to other telephone numbers with "non-local" NPA-NXX codes for other services—or for "better action." It also appears as though HFT encourages Verizon customers and other consumers to make long-distance calls by promoting service with a San Diego area code in Phoenix, and calls with a Phoenix area code in Illinois, even though NCC has local numbers in all these areas. HFT appears to be encouraging long-distance calling because NCC and HFT would prefer to collect access charges rather than reciprocal compensation. NCC's bills for reciprocal compensation to Verizon's ILEC in California are de minimis despite overlapping territories.

As Verizon has previously explained, co-ownership of a LEC and a customer jointly providing high-volume calling services constitutes an illegal kickback even if there is no explicit contract governing the arrangement. If the customer operates at a loss such that it would not be independently viable standing alone but exists solely to generate intercarrier compensation revenue for its affiliate, that is as much a kickback as if the LEC were paying the customer a portion of the intercarrier compensation revenue directly.

Verizon is engaged in litigation with NCC in California, including a discovery dispute. That dispute is currently pending before a federal magistrate, and there is no need for the Commission to concern itself with these issues. In any event, NCC's allegations in its letter related to its litigation with Verizon are completely baseless. Verizon is seeking the evidence the court will need to decide whether NCC's conduct constitutes an illegal kickback scheme. The court has already indicated that much or all of the requested discovery is appropriate and necessary, despite NCC's representations in its letter.[7] Indeed, among multiple affirmative misstatements and mischaracterizations in the NCC Letter, NCC attacks Verizon for "harassing

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County Communications Corp. v. Cellco Partnership, No. 10-257 (Aug. 20, 2010); *cert. denied* (Nov. 29, 2010).

[7] Relying on the Commission's Second Order on Reconsideration in the *Farmers* proceeding, the district judge ruled that Verizon is entitled to develop "additional facts . . . to determine the relationship, if any, between [NCC] and [its] alleged chat-line providers." *North County Communications Corp. v. Verizon Global Networks, Inc.* 685 F.Supp.2d 1112, 1121 (S.D.Cal. 2010); *see also id.* ("[I]t is clear from the [*Second Farmers Reconsideration Order*] that the determination of whether chat-line providers are end-users is fact-driven."); and *Qwest Communications Corp. v. Farmers and Merchants Mut. Tel. Co.,* Second Order on Reconsideration, 24 FCC Rcd 14801 (2009) ("*Second Farmers Reconsideration Order*").

depositions of NCC's customer." NCC Letter at 9. NCC fails to mention that NCC's "customer" is in fact the chat-line company that is also owned by NCC's president, Mr. Lesser.

Legitimate telecommunications ventures are not analogous to traffic pumping. NCC suggests that traffic pumping is no different from "customers calling their friends" or the typical "business teleconferencing service" and other legitimate telecommunications activities of Verizon and other carriers. NCC Letter at 3, 5-7. This is false and intentionally misleading. Traffic pumping is a discrete practice that involves very different activities and raises very different concerns from any lawful telecommunications service.

Traffic pumping involves a direct or indirect arrangement between the LEC and a traffic pumping partner such as a conference calling, international calling, chat line (sometimes pornographic), or other company. In most cases the company provides a service which generates only in-bound traffic. By generating these large relative traffic imbalances between in-bound and out-bound calling services, traffic pumpers seek to maximize their collection of intercarrier compensation. While there are legitimate consumers of predominantly in-bound telecommunications services—e.g., call center or non-800 customer service numbers—these customers do not advertise "free services" that are really funded by regulatory arbitrage.

In a typical traffic pumping scam, a conference calling or chat-line company will locate bridging equipment in a LEC facility, or in another location within a state where the call termination rate is high, and then gin up traffic to its bridge reached through local phone numbers provided by the LEC by marketing its services as "free" or below cost. The prospect of a "free" service often generates a very large volume of traffic and corresponding intercarrier compensation payments from IXCs and interconnected wireless carriers based on the LEC's tariffs. Once paid, the traffic pumping LEC then typically gives its pumping partner a kickback of some portion of the LEC's regulated intercarrier compensation revenues. The scam is an attempt to hold IXCs and interconnected wireless carriers hostage under the intercarrier compensation system—forced to complete calls from their customers to the LEC that would not have been made but for the scheme to spike traffic, and then forced (if the traffic pumper's tariff actually applies to its purported services) to pay the resulting charges.

None of the examples of legitimate telecommunications services cited by NCC exhibit the same relative traffic imbalances coupled with marketing efforts designed to increase the intercarrier compensation revenues for call termination sought by the terminating LEC. For example, traffic pumping is obviously different from encouraging Internet users to click on "social networking" sites, such as Facebook, MySpace and the like. NCC Letter at 3. The social networking companies do not charge Internet service providers, and Internet service providers are not obligated by intercarrier compensation regulations to pay a fee each time their customers click on one of those sites the same way that NCC seeks intercarrier compensation payments from IXCs and wireless carriers such as Verizon on pumped traffic. NCC also incorrectly suggests that Verizon and other ILECs have engaged in the very same kind of traffic pumping by running "their own chatlines in the past and continu[ing] to sell services to chat line providers" today. *Id*. at 5. In support of this contention, NCC cites to advertisements for two "chat-lines on Verizon's network." *Id*. at 5 n.8 (referring to Ex. 4). Those advertisements, however, are from 1987 and 1991, and have nothing whatsoever to do with Verizon other than what is apparently a

standard business-line service arrangement with a Verizon predecessor company. The advertisements themselves even make clear, in print, that "New York Tel. is not in any way involved with this service." NCC Letter at Ex. 4. NCC also cites to a 1985 chat line purportedly run by the predecessor to Qwest and an undated "Talkline" offered by AT&T's predecessor (PacBell). *Id.* at 5. Likewise, these advertisements make clear that—unlike the "free" services associated with traffic pumping—the caller was required to pay a fee for the services he or she used.

The same thing distinguishes NCC's claims that, by "sell[ing] chat-line provider services using regular ten digit telephone lines, 900 numbers, 976 numbers and even special overseas numbers," Verizon and other carriers are engaged in traffic pumping. NCC Letter at 6. With 900-number and similar services, the callers who use the services pay for them. These arrangements do not involve any regulatory arbitrage or forced subsidies because the end users who initiate the calls pay for both the cost of the call and the cost of the services they access.

NCC also compares various unrelated forms of "revenue sharing" to traffic pumping, claiming that because "[m]ost ILECs have revenue sharing agreements with prisons, hotels, large businesses, universities, airports and even pay phone providers" that sell their services, traffic pumping revenue sharing arrangements "should be of no concern to the FCC." *Id*. This is another apples-to-oranges comparison. Verizon and other carriers do have legitimate commission arrangements with hotels and other entities. In those arrangements, the carriers are compensating a third party that plays a role similar to that of a sales agent—for instance, a hotel that offers long-distance services to its patrons. The carrier does not pay the hotel to be its customer, and the patrons pay for the services they use.

The solution to traffic pumping is for NCC and others to stop pumping, not for Verizon to charge its customers more. NCC contends that the root of the traffic pumping problem is inexpensive, in some cases unlimited, long-distance wireline and wireless calling plans—and that the solution to traffic pumping is for IXCs and wireless carriers to charge more for their services in order to cover the costs of these schemes. NCC Letter at 2, 7. In support of this bizarre theory, NCC recycles a "fact report" from earlier this year suggesting that IXCs actually benefit from traffic pumping and, therefore, Verizon's true motive in this proceeding must be to gain market share by taking over the "free" conferencing space.[8] Verizon and others have responded to this argument many times. The suggestion that traffic pumping actually benefits IXCs is belied by the fact that the long-distance market has nearly evaporated as consumers increasingly purchase converged, any-distance (and often wireless) services. In addition, if Verizon and other legitimate providers were really motivated to take over the "free" conferencing space, then it stands to reason that they would actually enter this supposed market.

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[8] *See* Letter from Alan Pearce, Information Age Economics, Inc., to Marlene H. Dortch, FCC, *Developing a Unified Intercarrier Compensation Regime*; *Establishing Just and Reasonable Rates for Local Exchange Carriers*, CC Docket No. 01- 92, WC Docket No. 07-135 (March 1, 2010), attaching *Fact Report: The Economic Impact of Free Conference Calling Services*.

They have not done so because these traffic pumping scams are nothing more than illegal arbitrage.

In support of its confusing allegations of anti-competitive practices, NCC also cites to two state interconnection proceedings, in West Virginia and Illinois, claiming that Verizon sought to keep NCC out of the markets by refusing to transport NCC's 500-number traffic and to interconnect at desired locations. NCC Letter at 8. These disputes arose because NCC initially failed to provide Verizon with sufficient information to determine what services NCC would be providing in these states, forcing Verizon to question whether interconnection was appropriate. It is difficult to understand why NCC believes these cases are relevant to this proceeding. They are standard interconnection disputes that were handled pursuant to the states' authority under the 1996 Act. Confusion aside, NCC's insinuation that in the West Virginia proceeding the Public Service Commission staff somehow blessed traffic pumping as a "perfectly legal" practice is false. *Id*. There is no discussion in the West Virginia transcript pages NCC provided about traffic pumping. *Id.* at Ex. 13.

NCC's baseless allegations of anticompetitive motives are an attempt to distract from the issues actually at stake in this proceeding. The issue for the Commission to resolve is whether it is just and reasonable under Section 201(b) for a LEC to partner with a conferencing or other service provider and share the windfall profits that result when the provider offers a "free" service for the sole purpose of stimulating a huge increase in traffic. As the Commission has preliminarily (and correctly) concluded, if a LEC enjoys enough of an intercarrier compensation windfall that it can share those regulated revenues with a conferencing or other business partner in order to spike traffic, then the LEC's rates are by definition excessive.[9]

IntraMTA wireless traffic pumping is real and will only get worse. Responding to concerns from all corners of the industry about the Commission's *North County Order* ushering in a new traffic pumping frontier, NCC suggests that the absence of Commission guidance on the terminating rate for intraMTA CMRS-CLEC traffic is not a problem. NCC Letter at 2. This is not only self-motivated fiction, but it also appears to be an apparent change of heart for NCC. After the Enforcement Bureau issued its order in April 2009 in the *NCC v. MetroPCS* dispute, NCC appealed to the full Commission, predicting (correctly) that the decision would result in a flood of new litigation and disputes in multiple forums. *See North County Communications v. MetroPCS,* Application for Review, EB-06-MD-007, at 6 (April. 29, 2009) ("The Commission should reject the Bureau's approach, which if left to stand, would require piecemeal litigation in at least two forums- the state commission and this Commission- to establish an interconnection agreement that provides for compensation as required under section 20.11 of the Commission's rules.").

The flood of "piecemeal litigation" that NCC predicted is now here—and getting worse every day. Prior to the *North County Order*, Verizon Wireless had relative success negotiating

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[9] *Establishing Just and Reasonable Rates for Local Exchange Carriers*, Notice of Proposed Rulemaking, 22 FCC Rcd 17989 (2007).

and entering into commercial interconnection agreements with many CLECs. However, after the full Commission order upholding the bureau order was issued in November 2009, Verizon Wireless has experienced a marked decrease in the number of commercial agreements being reached with CLECs[10]—leading to protracted litigation and administrative disputes, and encouraging many CLECs to start pumping intraMTA wireless traffic through the same familiar traffic pumping scams. Overall, the wireless industry is now mired in more than 60 disputes nationwide involving traffic pumping activities, a growing number of which involve intraMTA traffic.[11] Specific to this traffic, Verizon Wireless and other CMRS providers have active intercarrier compensation disputes with CLECs before state commissions in California, New York, Pennsylvania, and in multiple state and federal courts.

NCC also attacks Verizon's argument that the traffic patterns CMRS providers are observing between traffic pumping CLECs and CMRS providers are reminiscent of the dial-up ISP traffic arbitrage schemes that plagued the industry until recently. *Id.* In reality, the similarity between these schemes is stark: The hallmark of the ISP cases was significant traffic imbalances in favor of the terminating CLECs (i.e., greater than a 3:1 ratio). Verizon Wireless is now in fact observing the same extreme one-way traffic imbalances (95 to 99 percent in some cases) with CMRS-originated intraMTA traffic. Unless the Commission gets out in front of this new problem, intraMTA traffic pumping will surely explode just as the dial-up ISP arbitrage schemes did. In that situation, the Commission's failure to act quickly resulted in disputes over billions of dollars, which were not finally resolved for more than 10 years when the Supreme Court declined to hear a further appeal on the matter just a few weeks ago.[12]

NCC's legal arguments are nonsense. The NCC Letter concludes with two highly strained legal arguments in support of NCC's suggestion that the Commission should leave undisturbed (or even affirmatively protect) unlawful traffic pumping activities. Both of those arguments should be rejected.[13]

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[10] Verizon Wireless experienced a 60 percent decrease in the number of negotiated agreements reached with CLECs for intraMTA traffic from December 2009 to November 2010.

[11] CTIA Traffic-Pumping Letter at 1.

[12] Petition for a Writ of Certioriari, *Pennsylvania Public Utility Commission v. Federal Communications Commission*, No. 10-189 (Aug. 6, 2010); *cert. denied* (Nov. 15, 2010).

[13] NCC also argues that the Commission must satisfy the requirements of 15 U.S.C. §§ 45 and 57a in order to stop traffic pumping. NCC Letter at 10. Those sections restrict the powers of the Federal *Trade* Commission. This proceeding is before the Federal *Communications* Commission. *See* 47 U.S.C. § 151. We trust no further response is needed.

First, NCC urges the Commission to "clarify" its *Second* and *Third*[14] *Reconsideration Orders* in the *Farmers* complaint proceeding. NCC Letter at 8-10. The relief that NCC seeks is not entirely clear but appears to involve limiting those orders to apply only to rate-of-return ILECs because Farmers (the traffic-pumping rural ILEC in that case) was involved in, as NCC puts it, "rate-of-return fraud." *Id*. at 9. The Commission has already made clear however, that Farmers had violated Section 201(b) for two "independent, alternative" reasons.[15] One reason was indeed the fact that Farmers' traffic-pumping scheme had caused it to exceed its authorized rate of return.[16] But the other reason was that Farmers had engaged in the unjust and unreasonable practice of charging tariffed switched access rates for purported service that its switched access tariffs did not cover, because the conference-calling companies who were participants in the scheme were not "end users" within the meaning of Farmers' tariffs.[17] Nothing in the Commission's finding that Farmers had charged for a service that was outside the terms of its tariffs depended on Farmers' status as a rural ILEC or its rates for those services. NCC thus mischaracterizes the Commission's previous orders in an attempt to argue for a major substantive change in them. That change would be, moreover, wholly unjustified. Regardless of the rates it charges, no carrier should be able to impose tariffed rates as charges for services to which its tariff simply "does not apply."[18]

Second, NCC claims that a ruling by this Commission that would "[t]reat[] chat lines as a separate category" of telecommunications or would "regulat[e] the payment of commissions" to chat-line providers would be an "improper[]" attempt to "regulate [the] content" of speech. NCC Letter at 10-14. This is frivolous. Nothing about any of the proposed solutions to traffic pumping raises the possibility of a restriction on speech. The issues before the Commission in this proceeding center on economic arrangements and policy questions over who should pay for services—nothing more.

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[14] *Qwest Communications Corp. v. Farmers and Merchants Mut. Tel. Co.,* Third Order on Reconsideration, 25 FCC Rcd 3422 (2010) ("*Third Farmers Reconsideration Order*").

[15] *Third Farmers Reconconsideration Order* ¶ 14 ("We clarify that the Commission could have relied solely on its ruling on [Qwest's rate-of-return claim] as an independent, alternative basis for finding that Farmers violated section 201(b) of the Act.").

[16] *See Qwest Communications Corp. v. Farmers and Merchants Mut. Tel. Co.,* Memorandum Opinion and Order, 22 FCC Rcd 17973 ¶¶ 21-25 (2007).

[17] *Second Farmers Reconsideration Order* ¶ 26 (finding that "Farmers' transport of traffic to [certain conference-calling companies] (?) did not constitute 'switched access' under [its] tariff" and that its "practice of charging Qwest tariffed switched access rates for its termination of traffic from the conference calling companies is unjust and unreasonable in violation of section 201(b)").

[18] *Second Farmers Reconsideration Order* n. 98 (emphasis omitted).

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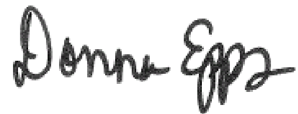
The NCC Letter and the NCC Follow-Up Letter are merely the latest smokescreens thrown up by traffic pumpers who should have been put out of business long ago. Ironically, Verizon and NCC *agree* on one fundamental point: The "FCC Must Stop Running From This Issue" and actually make "decisions to resolve these disputes." NCC Follow-Up Letter, Attachment at 8. The Commission's decisions, however, must put an end to traffic pumping once and for all—not legitimize these get-rich-quick schemes.

Sincerely,



cc: Zachary Katz
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