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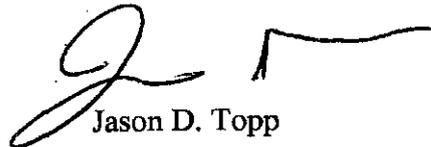
Patricia Van Gerpen, Executive Director
South Dakota Public Utilities Commission
500 East Capitol Avenue
Pierre, SD 57501

Re: In the Matter of the Application of Native American Telecom, LLC for a
Certificate of Authority to Provide Local Exchange Service within the Study
Area of Midstate Communications, Inc.
Docket No. TC11-087

Dear Ms. Van Gerpen:

Enclosed for filing is the Direct Testimony of William R. Easton on behalf of Qwest
Communications Company, LLC regarding the above-referenced matter.

Very truly yours,



Jason D. Topp

JDT/bardm

Enclosures

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CERTIFICATE OF SERVICE

I hereby certify that on this 26th day of March, 2012, the foregoing Direct Testimony of William R. Easton was E-Filed upon the following party:

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Dianne Barthel

**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF SOUTH DAKOTA**

**IN THE MATTER OF THE APPLICATION OF)
NATIVE AMERICAN TELECOM, LLC FOR A)
CERTIFICATE OF AUTHORITY TO PROVIDE)
LOCAL EXCHANGE SERVICE WITHIN THE)
AREA OF MIDSTATE COMMUNICATIONS, INC.)**

DOCKET NO. TC11-087

DIRECT TESTIMONY OF

WILLIAM R. EASTON

ON BEHALF OF

QWEST COMMUNICATIONS COMPANY, LLC

MARCH 26, 2012

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1 **I. IDENTIFICATION OF WITNESS**

2 **Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND POSITION WITH**
3 **QWEST.**

4 **A.** My name is William R. Easton. My business address is 1600 7th Avenue, Seattle
5 Washington. I am employed as Wholesale Staff Director. I am testifying on behalf of
6 Qwest Communications Company, LLC ("Qwest"), doing business as CenturyLink.

7
8 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND**
9 **PROFESSIONAL EXPERIENCE.**

10 **A.** I graduated from Stanford University in 1975, earning a Bachelor of Arts degree. In
11 1980 I received a Masters of Business Administration from the University of
12 Washington. In addition, I am a Certified Management Accountant.

13
14 I began working for Pacific Northwest Bell in 1980, and have held a series of jobs in
15 financial management with U S WEST, Qwest and now CenturyLink, including staff
16 positions in the Treasury and Network organizations. From 1996 through 1998, I was
17 Director – Capital Recovery. In this role I negotiated depreciation rates with the FCC
18 and state commission staffs and testified in various regulatory proceedings. From 1998
19 until 2001 I was a Director of Wholesale Finance, responsible for the management of
20 Wholesale revenue streams from a financial perspective. In this capacity I worked
21 closely with the Product Management organization on their product offerings and
22 projections of revenue. In October of 2001 I moved from Wholesale Finance to the

1 Wholesale Advocacy group, where I am currently responsible for advocacy related to
2 Wholesale products and services.
3

4 **Q. HAVE YOU PREVIOUSLY SUBMITTED TESTIMONY BEFORE THIS**
5 **COMMISSION?**

6 A. Yes. I previously testified in docket numbers TC96-184, TC01-098 and TC10-014.
7

8 **II. INTRODUCTION AND PURPOSE OF DIRECT TESTIMONY**
9

10 **Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?**

11 A. The Commission has a seminal case of great importance before it, because Native
12 American Telecom ("NAT") has admitted that its certification will be utilized to engage in
13 a practice known as "traffic pumping" or "access stimulation." Decisions issued by the
14 Iowa Utilities Board and the Federal Communications Commission ("FCC") have
15 criticized the practice as an "abuse" and as "arbitrage." The FCC's recent Connect
16 America order intended to remove the economic and financial incentives that encouraged
17 some carriers to engage in access stimulation and the FCC also cautioned against other
18 schemes that may constitute an abuse of the current regulatory scheme. Thus, the South
19 Dakota Commission has before it in this docket the threshold and vital issue of whether this
20 state should authorize the practice of access stimulation through the issuance of a
21 certificate to an applicant who has admitted that the certificate will be used in such a
22 manner. Further, to the extent that a certificate is granted for a carrier to engage in access
23 stimulation, the Commission should consider the extent to which conditions are necessary

1 to eliminate or at least limit potential abuses that could result from a carrier continuing to
2 engage in access stimulation after the issuance of the Connect America order.

3
4 The purpose of my testimony is to express Qwest's opposition to NAT's request for a
5 certificate of authority to provide local exchange service in the area of Midstate
6 Communications. NAT's ongoing participation in a scheme to stimulate access billing to
7 interexchange carriers ("IXC") such as Qwest is not consistent with the public interest, a
8 necessary condition to the granting of a certificate. My testimony will first provide some
9 contextual background on access stimulation and review some of the regulatory rulings and
10 interpretations of this practice, including the reasons that access stimulation is an abuse of
11 the regulatory switched access structure. I will then discuss the FCC's recent Connect
12 America order and the guidance it provides on access stimulation schemes. Next I will
13 discuss NAT's past involvement in access stimulation and the reasons that access
14 stimulation is not in the public interest. For these reasons, Qwest proposes that the
15 Commission not grant NAT's request for certification. However, if the Commission is
16 inclined to grant a certificate to NAT, then Qwest requests that it be subject to certain
17 conditions to limit or prevent future arbitrage abuses in South Dakota. Thus, I will also
18 address the concerns, as expressed by the FCC, over forms of abuse in which LECs may
19 engage known as "mileage pumping." In short, mileage pumping is designation by the
20 LEC of distant points of interconnection with interexchange carrier and then the charging
21 of transport on an expensive per minute or per mile basis. Qwest believes that mileage
22 pumping abuses will be exacerbated if the LEC is engaging in traffic pumping at high
23 volumes and applying distant points of interconnection. Based upon these concerns, Qwest

1 proposes conditions to help prevent mileage pumping abuses specifically that Qwest and
2 any other requesting interexchange carrier have the ability to connect directly to NAT's
3 end office where the free service calling companies have placed their equipment through
4 Direct End Office Transport, or sometimes know as Direct Trunked Transport, at just and
5 reasonable rates.

6
7 **III. ACCESS STIMULATION BACKGROUND**

8
9 **Q. WHAT IS ACCESS STIMULATION?**

10 A. Access stimulation, or traffic pumping, is the term used to describe situations where rural
11 local exchange carriers enter into an arrangement with high call volume operations such as
12 free conference calling, chat lines, adult entertainment calls and other "free" calls with the
13 ultimate objective of deriving revenues solely from interexchange carriers. The conference
14 call or chat line operators, also known as free calling companies, place their equipment in
15 the central office of the local exchange carrier, and the local exchange carrier assigns local
16 numbers to the free service calling companies. Because the free service calling companies
17 offer their conference or chat services to customers across the nation for free, this
18 arrangement greatly stimulates the amount of traffic to the equipment of the free service
19 calling companies, and thus inflates the access minutes terminating to the local exchange
20 carrier. The local exchange carrier bills switched access to the interexchange carrier of the
21 person who places the call to the free service calling company at its tariffed rate, which in
22 rural areas in some states is often several times higher than in non-rural areas and

1 exchanges.¹ The local exchange carrier then provides a kickback to the free service calling
2 company, typically about half, of the access revenues that the local exchange carrier
3 collects from the interexchange carriers. The local exchange carrier and the free calling
4 companies more than covers their costs and profits from the shared revenues. The end
5 result is that the IXCs pay higher access charges that provide enormous profits to the free
6 service calling companies and the traffic pumping LECs.

7
8 **Q. WHAT ARE THE REASONS THAT ACCESS STIMULATION CONSTITUTES**
9 **ARBITRAGE AND IS CONTRARY TO PUBLIC POLICY?**

10 A. There are many. First, there is the threshold principle that IXCs must deliver traffic to the
11 numbers and exchanges called by their end user customers. The FCC has directed
12 interexchange carriers to deliver all such traffic in order to promote and safeguard the
13 ability of callers to reach their intended destinations. Qwest and other interexchange
14 carriers are not permitted to block calls destined to traffic pumping LECs, and Qwest never
15 has. Thus, Qwest and other IXCs are forced to deliver the traffic to the traffic pumping
16 LEC exchanges, and traffic pumping LECs manipulate this forced arrangement to attempt
17 to impose inflated switched access charges upon the IXCs.

18
19 Second, traffic pumping LECs abuse the regulatory structure underlying switched access
20 rates in rural exchanges. Historically, switched access rates in rural areas have been set at
21 rates significantly higher than in non-rural areas in order to provide support to a rural

¹ In South Dakota, per RM-05-002 CLECs are not permitted to charge higher switched access rates than the RBOC in the state.

1 carrier providing essential, basic services in high cost areas. That is, the rates are higher to
2 subsidize the high cost of providing basic services to rural residents and businesses. And,
3 IXC's have been generally amenable to paying the higher rates in consideration of these
4 policies and because traffic volumes to rural areas are relatively low. The traffic pumping
5 LECs abuse this laudable structure by placing the conference calling equipment in rural
6 exchanges, generating exponentially higher traffic volumes to the exchange, which
7 combined with their high rural switched access rates lead to increasingly large invoices to
8 IXC's. For example, in rural exchanges where Qwest typically would receive invoices of
9 about a thousand dollars per month before traffic pumping, after certain LECs commenced
10 traffic pumping schemes, Qwest would receive invoices for several hundred thousands of
11 dollars, for just one month. When one multiplies the months by the number of LECs
12 engaging in traffic pumping, the result is tens and hundreds of millions of dollars in
13 increased access charges as a result of this scheme. Thus, the public interest component of
14 higher switched access rates in rural areas – to support basic services to rural residences
15 and businesses – is abused by traffic pumping LECs that bilk millions of dollars out of
16 IXC's for their own profit and that of their free service calling company partners.

17
18 As I discuss below, the FCC has attempted to remove the incentive of high terminating
19 switched access rates for LECs engaging in access stimulation in the Connect America
20 order; however, as I also address below, it appears that traffic pumping LECs such as NAT
21 intend to continue this practice, likely supporting their schemes through high transport rates
22 in the place of terminating switched access rates.

1 Next, it is against public policy that entities that do not use or subscribe to a service be
2 forced to support the costs and enormous profits of the providers of the service. That is,
3 IXC's do not use the services provided by the free service calling companies, such as
4 conference calling or chat line services; rather, it is the end user callers that consume those
5 services. But, the IXC's are forced to deliver and thus incur the switched access charges
6 that are shared with the free service calling companies, and thus the IXC's support the costs
7 and bestow huge profits upon the free service calling companies.

8
9 Finally, IXC's are not permitted to pass on the specific costs of traffic pumping to the
10 individual end user customers that are placing calls to the free service calling companies.²
11 IXC's current charges to their end user customers are not calculated based on traffic
12 pumping traffic patterns, although, as IXC's incur the enormous cost of traffic pumping
13 LEC's switched access bills, all their customers ultimately must absorb these costs through
14 higher rates. Thus, despite the marketing of the underlying calling services as "free," there
15 is little that is free about them. In sum, the Commission and IXC's should be wary of any
16 scheme in which a rural LEC is attempting to generate large volumes of minutes for calls to
17 free service calling companies and in which the LEC intends to invoice IXC's on a usage or
18 per minute basis.

19
20 **Q. WHAT IS THE POLICY SIGNIFICANCE OF AN AGREEMENT TO SHARE**
21 **REVENUES BETWEEN THE LEC AND THE FREE SERVICE CALLING**
22 **COMPANIES?**

² See 47 U.S.C § 254 (g).

1 A. The sharing of access revenues between the LEC and the free service calling companies
2 means that such revenues are being used for more than simply covering the costs of the
3 LEC to provide service. And, such revenues are not being used to support basic services to
4 legitimate residential and business customers in rural areas. When access revenues are
5 shared to support and provide large profits to free service calling companies, the LEC is
6 charging in excess of the rates appropriate to further valid public interests and is misusing
7 the regulatory system that tightly controls access rates.

8
9 **Q. HAS THE FCC ISSUED RULINGS ANALYZING THE POLICY HARMS THAT**
10 **RESULT FROM ACCESS STIMULATION?**

11 A. Yes. In its February 8, 2011, Connect America Fund Notice of Proposed Rule Making and
12 Further Notice of Proposed Rulemaking, the FCC described such traffic pumping
13 arrangements as an "arbitrage scheme" (par. 636) and found that:

14 "Access stimulation imposes undue costs on consumers, inefficiently
15 diverting the flow of capital away from more productive uses such as
16 broadband deployment; and harms competition. Although long distance
17 carriers are billed for and pay for minutes associated with access
18 stimulation schemes, all customers of these long distance providers bear
19 these costs and, in essence, ultimately support businesses designed to take
20 advantage of today's above-cost intercarrier compensation system.
21 Projections indicate that the annual impact to the industry from access
22 stimulators is significant." (par. 637); and

23
24 "Moreover, access stimulation harms competition by giving companies
25 that offer a "free" service a competitive advantage over companies that
26 charge their customers for the service. As a result, "free" conferencing
27 providers that leverage arbitrage opportunities can put other companies
28 that charge consumers for services at a distinct competitive disadvantage."
29 (par. 638).

1 **Q. HAVE STATE REGULATORS INVESTIGATED ACCESS STIMULATION AND**
2 **TAKEN STEPS TO CURB THIS PRACTICE?**

3 A. Yes. In Iowa, Qwest filed a complaint against eight local exchange carriers engaging in
4 traffic pumping. The primary issue before the Iowa Board was, in short, whether the traffic
5 pumping LECs were allowed to charge under their switched access tariffs for calls
6 delivered to free service calling companies. Following extensive discovery and hearings,
7 the Board found in Qwest's favor and stated:

8 Based on the record in these proceedings, the Board finds that the intrastate
9 interexchange calls to the conference calling companies were not subject to access
10 charges. Refunds and credits to the IXC's are ordered. The Board also announces
11 that it is initiating a proceeding to consider proposed rules intended to prevent this
12 abuse in the future.³

13 The Iowa Board also initiated show cause hearings to determine if two of the Iowa local
14 exchange carriers should have their certificates revoked, in part because they had few, if
15 any, traditional local exchange customers.⁴

16 As this Commission is also aware, there is currently a complaint, brought by Sprint against
17 NAT, pending before the Commission regarding access stimulation traffic (TC10-026).

18
19 **Q. HOW DOES THE CONNECT AMERICA ORDER ADDRESS ACCESS**
20 **STIMULATION?**

21
³ Docket FCU-07-2 Final Order Summary, September 21, 2009.

⁴ In Re: Great Lakes Communications Corp., SPU 2011-0004 (TCU-05-6); In Re: Aventure Communication Technology, L.L.C., Docket No. FCU-2011-0002. In the docket involving the traffic pumping LEC known as "Great Lakes", a carrier that engaged in only traffic pumping, the Board indicated during its oral deliberations that continued validity of Great Lakes's certificate would be predicated upon the offering of services to legitimate end user customers. The Board has not issued a final written order.

1 A. The FCC's recent Connect America order was intended to rid the industry of access
2 stimulation by removing the financial incentives for engaging in this form of arbitrage.⁵
3 The order addressed traffic pumpers' exploitation of the switched access rate structure by
4 requiring the filing of new, revised tariffs with a new rate if a LEC satisfies two criteria of
5 "access stimulation." The two criteria are: 1) the existence of a revenue sharing
6 arrangement between the LEC and a calling company; and 2) a volume component, met if
7 the LEC (a) has a three-to-one ratio of terminating-to-originating traffic in any month or (b)
8 experiences more than a 100 percent increase in traffic volume in any month measured
9 against the same month during the previous year.⁶ If a CLEC meets these criteria, then it
10 must file a revised tariff with the FCC setting all of its switched access rates to the rates of
11 the price cap LEC with the lowest interstate switched access rates in the state.

12
13 The overriding intent of the FCC is to reduce traffic pumping by the elimination of traffic
14 pumping and arbitrage incentives. The Order's opening section is entitled "Rules to
15 Reduce Access Stimulation."⁷ The FCC consistently recognizes that access stimulation
16 results in unjust and unreasonable rates to IXCs and presents several other policies
17 supporting the issuance of access stimulation rules -- (one reason for the need to overhaul
18 the entire intercarrier compensation regime is the wasteful and costly arbitrage schemes
19 that have proliferated);⁸ ("curtail wasteful arbitrage practices," including access

⁵ In the Matter of Connect America Fund, "Report and Order and Further Notice of Proposed Rulemaking," FCC 11-161 (released November 18, 2011), at ¶¶ 656-701.

⁶ Connect America, at ¶¶ 33, 667.

⁷ Connect America at ¶ 656.

⁸ Id., at ¶ 9.

1 stimulation),⁹ (“inflated profits that almost uniformly make the LEC's interstate switched
2 access rates unjust and unreasonable”);¹⁰ (“The record confirms the need for prompt
3 Commission action to address the adverse effects of access stimulation”);¹¹ (“Access
4 stimulation imposes undue costs on consumers”);¹² (“Access stimulation also harms
5 competition”);¹³ (“excess revenues that are shared in access stimulation schemes provide
6 additional proof that the LEC's rates are above cost”);¹⁴ (FCC refers to these rule changes
7 as a “prohibition on access stimulation.”);¹⁵ (“similar arbitrage scheme”).¹⁶

8
9 In other parts of the access stimulation section, the FCC expressed the intention of
10 monitoring future access stimulation activities --

11 should the traffic volumes of a competitive LEC that meets the access
12 stimulation definition substantially exceed the traffic volumes of the price
13 cap LEC to which it benchmarks, we may reevaluate the appropriateness
14 of the competitive LEC's rates and may evaluate whether any further
15 reductions in rates is warranted. In addition, we believe the reforms we
16 adopt elsewhere in this Order will, over time, further reduce intercarrier
17 payments and the incentives for this type of arbitrage.¹⁷

18
19 And, the concluding paragraphs of the access stimulation section outline the intended result
20 of the FCC's new rules and required rates:

21 Taking this basic step will immediately reduce some of the inefficient
22 incentives enabled by the current intercarrier compensation system, and
23 permit the industry to devote resources to innovation and investment
24 rather than access stimulation and disputes. We have balanced the need

⁹ *Id.*, at ¶ 33.
¹⁰ *Id.*, at ¶¶ 657, 662.
¹¹ *Id.*, at ¶ 662.
¹² *Id.*, at ¶ 663.
¹³ *Id.*, at ¶ 665.
¹⁴ *Id.*, at ¶ 666.
¹⁵ *Id.*, at ¶ 674.
¹⁶ *Id.*, at ¶ 676.
¹⁷ *Id.*, at ¶ 690.

1 for our new rules to address traffic stimulation with the costs that may be
2 imposed on LECs and have concluded that the benefits justify any
3 burdens. Our new rules will work in tandem with the comprehensive
4 intercarrier compensation reforms we adopt below, which will, when fully
5 implemented, eliminate the incentives in the present system that give rise
6 to access stimulation.¹⁸
7

8 **Q. HAS THE FCC ISSUED FURTHER CLARIFICATION SINCE THE CONNECT**
9 **AMERICA ORDER WAS ISSUED?**

10 A. Yes. One issue arising out of the Connect America order was whether previous FCC
11 precedent adjudicating access stimulation and traffic pumping issues carry over after the
12 effective date of the FCC's new rules. Those FCC cases, in particular the cases known as
13 Farmers & Merchants and Northern Valley, reiterated existing federal law that a LEC's
14 switched access tariffs must include an end user component in which that customer is
15 receiving telecommunications services purchased from the LEC for a fee.¹⁹ Despite this
16 clear precedent, the traffic pumping industry has contended that mere compliance with the
17 FCC's new tariff rules from the Connect America order exonerates them from complying
18 with the rulings from the Farmers and Northern Valley cases. Thus, Sprint filed a petition
19 for clarification in the Connect America docket requesting clarification that:

- 20 ▪ The [Connect America] Order does not overturn previous Commission
21 rulings or standards for determining whether a LEC's free service provider
22 partner is a legitimate end user/customer under its access tariff; and,
23
24 ▪ The Order does not overturn the statutory requirement that
25 telecommunications services be offered "for a fee."²⁰
26

¹⁸ Id., at ¶ 701.

¹⁹ Qwest Comm'ns Corp. v. Farmers & Merchants Mutual Tel. Co. ("Farmers II"), 24 FCC Rcd. 14801 (2009), 2009 WL 4073944 (F.C.C.); In the Matter of Qwest Communications Company, LLC, v. Northern Valley Communications, LLC; File No. EB-11-MD-001; Memorandum Opinion and Order; Released June 7, 2011.

²⁰ Petition for Reconsideration and Clarification of Sprint Nextel Corporation, WC Dkt. 10-90, filed December 29, 2011, at 2.

1 On February 3, 2012, the Wireline Competition Bureau and the Wireless
2 Telecommunications Bureau issued a clarifying order²¹ affirming the points presented by
3 Sprint's petition. The Bureaus' Order says:

4 *25. Access Stimulation and Previous Rulings on End Users.* In the
5 *USF/ICC Transformation Order*, the Commission adopted revisions to its
6 interstate switched access charge rules to address access stimulation. Prior
7 to the *USF/ICC Transformation Order*, the Commission adopted several
8 orders resolving complaints concerning access stimulation under
9 preexisting rules and compliance with the Communications Act. We
10 clarify that the *USF/ICC Transformation Order* complements these
11 previous decisions, and nothing in the *USF/ICC Transformation Order*
12 should be construed as overturning or superseding these previous
13 Commission decisions.²²
14

15 **Q. HAS THE CONNECT AMERICA ORDER ELIMINATED CONCERNS ABOUT**
16 **ACCESS STIMULATION?**

17 A. No. In fact, the Connect America order acknowledged evidence in its record of another
18 form of arbitrage – “mileage pumping,” in which “service providers designate distant
19 points of interconnection to inflate the mileage used to compute the transport charges.”²³
20 The FCC sought comment in its Further Notice of Proposed Rulemaking to investigate this
21 form of arbitrage.²⁴ And, despite the FCC's admonitions against traffic pumping practices,
22 it has come to the attention of Qwest that certain traffic pumping LECs are indeed planning
23 on charging access rates with high transport rates. Thus, abuse of terminating access rates
24 may be replaced by new schemes in which high transport rates are charged for calls
25 delivered to free service calling companies.
26

²¹ In the Matter of Connect America Fund, WC Dkt. No. 10-90, et. al., DA 12-147, released February 3, 2012.

²² Id., at ¶ 25.

²³ Connect America, at ¶ 820.

²⁴ Id.

1 **Q. ARE THERE ALSO PENDING COURT CASES CONCERNING ACCESS**
2 **STIMULATION?**

3 A. Yes. There are a number of pending court cases, including a suit brought by Sprint against
4 NAT which is before the United States District Court for the District of South Dakota (CIV
5 10-4110).

6

7 **IV. NATIVE AMERICAN TELECOM AND ACCESS STIMULATION**

8

9 **Q. WHAT IS THE BASIS FOR YOUR UNDERSTANDING THAT NAT IS**
10 **INVOLVED IN ACCESS STIMULATION?**

11 A. My understanding is based on several pieces of information, including statements made by
12 NAT and individuals directly associated with NAT. As was discussed previously, there are
13 ongoing complaints against NAT, both here before this Commission and before the United
14 States District Court in South Dakota. This ongoing litigation has yielded information that
15 confirms not only that NAT is engaged in access stimulation, but also hat it represents the
16 vast majority of its business. Indeed, without its access stimulation scheme, NAT would
17 likely not exist.

18

19 **Q. HOW SIGNIFICANT A PORTION OF NAT'S BUSINESS IS FREE CONFERENCE**
20 **CALLING SERVICES?**

21 A. It appears to be nearly the entirety of NAT's business. In the Sprint complaint docket
22 which is before this Commission, (TC10-26), a Sprint Access Verification Analyst filed an
23 affidavit on September 27, 2010 stating that study data for July 2010 "indicates that

1 99.98% of the traffic NAT wants to be paid for terminating actually goes to conference
2 bridge equipment and not to an end user on the Reservation.”²⁵ In addition, the Treasurer
3 of Crow Creek Sioux tribe acknowledged the significance of free conference calling
4 services to the NAT business model stating, “Well, if it wasn’t for FreeConferenceCall,
5 there really wouldn’t be a NAT.”²⁶ Attached as Exhibit WRE-1 is the relevant excerpt
6 from the District Court transcript.

7
8 **Q. ARE THERE CLOSE LINKS BETWEEN NAT AND THE FREE CONFERENCE**
9 **CALLING SERVICES?**

10 A. Yes. Testimony in the Sprint complaint case before the United States District Court of
11 South Dakota demonstrates that the entities that manage both NAT and Free Conferencing
12 Corporation are one and the same. The controller for Free Conferencing Corporation of
13 Long Beach, California, whose flagship product is FreeConferenceCall.com, is also the
14 controller for NAT.²⁷ Attached as Exhibit WRE-2 is the relevant excerpt from the District
15 Court transcript. In addition, the acting president of NAT, Jeff Holoubek, is the Director of
16 Legal and Finance at Free Conferencing Corporation.²⁸ Attached as Exhibit WRE-3 is the
17 relevant excerpt from the District Court transcript.

18
19

²⁵ Docket No. TC10-026 - Affidavit of Amy S. Clouser, September 27, 2010, pp. 6-7.

²⁶ Civ 10-4110, United States District Court, District of South Dakota, Southern Division, Sprint Communications Company, L.P., Plaintiff, vs. Native American Telecom, LLC; B.J. Jones, in his official capacity as Special Judge of Tribal Court; and Crow Creek Sioux Tribal Court, Defendants. Transcript of Motion Hearing, March 3, 2011, p. 147.

²⁷ Id., p. 14.

²⁸ Id., p. 68.

1 **Q. WHAT IS THE FINANCIAL LINKAGE BETWEEN THE TWO COMPANIES?**

2 A. The controller for both NAT and Free Conferencing Corporation testified in the same
3 hearing that there is a marketing fee agreement between the two parties whereby Free
4 Conferencing Corporation gets 75% of the access revenues generated and NAT retains the
5 remaining 25%.²⁹ Attached as Exhibit WRE-4 is the relevant excerpt from the District
6 Court transcript. This percentage split, which grants a higher percentage to the free service
7 calling company than I have seen in other cases, demonstrates that a significant portion of
8 access revenues will be directed toward an entity that is not providing the access service
9 itself, and thus suggests that the rates charged by NAT for either termination or transport of
10 calls to its free service calling companies is unjust, unreasonable, and constitutes an
11 arbitrage scheme, for the reasons I state above.

12
13 **Q. HAS NAT ACKNOWLEDGED THAT IT PLANS TO ENGAGE IN ACCESS**
14 **STIMULATION IN THE AREA THAT IS THE SUBJECT OF ITS APPLICATION**
15 **FOR CERTIFICATE OF AUTHORITY?**

16 A. Yes. Attached as Exhibit WRE-5 is a copy of NAT's response to CenturyLink's discovery
17 request 1.8. In its response, NAT states that it will be engaging in access stimulation in the
18 area for which is requesting certification.

19
20 **Q. WILL NAT CONTINUE TO HAVE REVENUE SHARING AGREEMENTS WITH**
21 **FREE SERVICE CALLING COMPANIES?**

²⁹ Id., p. 52.

1 A. Yes. As I discuss above, the Connect America order has a two part test for whether a LEC
2 is engaging in access stimulation. One of the criteria is that the LEC has a revenue sharing
3 agreement with a free service calling company. Thus, by NAT's admission that it will be
4 engaging in access stimulation as defined in the Connect America order there is ample
5 evidence that NAT will continue to split its access revenues with companies such as Free
6 Conferencing at a percentage that siphons 75% of access revenues from IXCs to an entity
7 that is not providing any access services at all.

8
9 **Q. DOES NAT'S BUSINESS MODEL HAVE IMPLICATIONS ON ITS REQUEST**
10 **FOR CERTIFICATION?**

11 A. Absolutely. There are at least two concerns for this Commission to consider related to
12 NAT's reliance on access stimulation. The first concern goes directly to the requirements
13 in the South Dakota statutes and administrative rules that the company requesting
14 certification demonstrate that it has sufficient technical, financial, and managerial
15 capabilities to provide the local exchange services applied for.³⁰ A second concern has to
16 do with deciding whether the public interest is served by certifying a carrier whose true
17 focus is serving only free conference calling services rather than providing traditional local
18 exchange service.

19
20 **Q. PLEASE DESCRIBE THE CONCERNS RELATED TO NAT DEMONSTRATING**
21 **IT POSSESSES SUFFICIENT TECHNICAL, FINANCIAL AND MANAGERIAL**
22 **CAPABILITIES.**

³⁰ SDCL 49-31-37 and ARSD 20:10:32:05.

1 A. NAT's near total reliance on access stimulation revenues raises serious questions about its
2 financial viability. During the United States District Court hearing referenced above, it
3 was revealed that NAT's finances are in a rather precarious state due to Sprint withholding
4 payment. In fact, NAT's counsel stated at the hearing that if Sprint does not pay NAT, it is
5 likely to either file bankruptcy or go out of business.³¹ Attached as Exhibit WRE-6 is the
6 relevant excerpt from the District Court transcript. The future appears even less promising
7 as NAT's access stimulation scheme becomes increasingly unviable as IXC's insist that
8 access stimulators comply with the terms and conditions in their tariffs and as the FCC's
9 intercarrier compensation rates transition to a bill and keep basis. In light of these
10 developments, it is not at all clear that NAT possesses the financial capability necessary for
11 approval of its certification request.

12
13 **Q. ARE THERE ANY OTHER INDICATIONS THAT LECS INVOLVED IN ACCESS**
14 **STIMULATION SCHEMES DO NOT HAVE THE FINANCIAL CAPABILITY TO**
15 **PROVIDE TELECOMMUNICATIONS SERVICES?**

16 A. Yes. Traffic pumping schemes have resulted in claims brought by IXCs, including Qwest,
17 requesting a return of monies illegally obtained by the LEC. But, Qwest's experience has
18 shown that traffic pumping LECs fail to take fiscally responsible steps to cover their
19 potential liabilities. The very nature of their arrangements with free service calling
20 companies indicates that a traffic pumping LEC may not be able to cover its potential
21 liabilities. Under their contracts with free service calling companies, when a traffic

³¹ Civ 10-4110, United States District Court, District of South Dakota, Southern Division, Sprint Communications Company, L.P., Plaintiff vs. Native American Telecom, LLC; B.J. Jones, in his official capacity as Special Judge of Tribal Court; and Crow Creek Sioux Tribal Court, Defendants. Transcript of Motion Hearing, March 3, 2011, pp. 206, 208.

1 pumping LEC receives monies from an IXC, it immediately tenders usually half, and in the
2 case of NAT, 75%, of the money to its free service calling company partners. Thus, the
3 traffic pumping LEC fails to retain the monies that are in dispute and potentially subject to
4 refund. Or, the traffic pumping LEC may attempt to move the monies out of reach of the
5 IXCs, by distributions to its owners, some of whom include family trusts, or by converting
6 the funds into illiquid facilities and plant. Under these circumstances, the traffic pumping
7 LEC fails in its duties of operating and managing itself in a financially responsible manner
8 that reserves funds for its contingent liabilities.

9
10 **Q. PLEASE DISCUSS THE PUBLIC POLICY CONSIDERATIONS OF THE NAT**
11 **APPLICATION.**

12 A. As I stated above, there are real concerns related to whether approving NAT's certification
13 request is in the public interest. Given NAT's past practices and its admission that it will
14 be engaging in access stimulation in the area where it is requesting certification, the
15 Commission must question whether providing service to free conference calling services,
16 as opposed to providing traditional local exchange service, is truly in the public interest. It
17 is telling that the testimony filed by NAT in this case fails to address, or even mention,
18 access stimulation as a service it will be providing, despite the fact that it currently
19 constitutes nearly the entirety of its business.

20
21 NAT touts the economic social and educational impacts of its business on the Crow Creek
22 Reservation, but the FCC rejected this very argument as a justification for access
23 stimulation in its Connect America order, stating:

1 Several parties claim that access stimulation offers economic development
2 benefits, including the expansion of broadband services to rural communities and
3 tribal lands. Although expanding broadband services in rural and Tribal lands is
4 important, we agree with other commenters that how access revenues are used is
5 not relevant in determining whether switched access rates are just and reasonable
6 in accordance with section 201(b). In addition, excess revenues that are shared in
7 access stimulation schemes provide additional proof that the LEC's rates are
8 above cost. Moreover, Congress created an explicit universal service fund to spur
9 investment and deployment in rural, high cost, and insular areas, and the
10 Commission is taking action here and in other proceedings to facilitate such
11 deployment.³² (Footnotes omitted).

12
13 Taking the economic social and educational impacts on the Crow Creek Reservation out of
14 the equation, it is not clear that NAT's providing service to free conference calling services
15 does anything to serve the public interest.

16
17 **V. MILEAGE PUMPING**

18
19 **Q. ARE YOU CONCERNED ABOUT THE PROSPECT THAT TRAFFIC PUMPING**
20 **LECS WILL ENGAGE IN A FORM OF MILEAGE PUMPING?**

21 A. Yes. As I noted earlier, it has come to Qwest's attention that some traffic pumping LECs'
22 intend to designate distant points of interconnection between the LEC and IXCs, and then
23 charge a usage based, per minute transport rate, and a transport rate premised upon
24 mileage. Charging inflated transport charges, even though the LEC is charging the
25 termination rates prescribed by the FCC in the Connect America order, could result in a
26 financially viable traffic pumping scheme for the LEC. In short, a mileage pumping
27 scheme has similar components to the traffic pumping schemes of the recent past – high

³² In the Matter of Connect America Fund, "Report and Order and Further Notice of Proposed Rulemaking," FCC 11-161 (released November 18, 2011), at ¶ 666.

1 traffic volumes, per minute charges, and sharing of revenues with an entity that did not
2 provide any of the access services.

3
4 **Q. DOES QWEST HAVE A RECOMMENDATION TO HELP LIMIT MILEAGE**
5 **PUMPING?**

6 A. Yes. It is a common industry practice for LECs to allow IXCs to directly connect to the
7 end office of the LEC in order to allow the IXC to save on common transport and tandem
8 switching charges. This type of dedicated connection is known as "Direct End Office
9 Transport (DEOT)" or "Direct Trunked Transport (DTT)." Typically, the LEC offers DTT
10 to an IXC by leasing a facility connected between the IXCs Point of Presence (POP) and
11 the LEC's end office. The LEC's charges typically include a non-recurring connection
12 charge, a fixed monthly charge, and a variable charge based upon the distance between the
13 IXC's POP and the LEC's end office. DTT service thus allows an IXC that delivers
14 relatively high volumes of traffic to the LEC's exchange to save from paying per minute
15 tandem switching and transport charges. Qwest Corporation, as a local exchange carrier,
16 offers DTT throughout its incumbent region, including in South Dakota, to any requesting
17 IXC.

18
19 *Qwest recommends that this Commission, if it should grant NAT's certificate, condition its*
20 *certificate upon the requirement that NAT provide DTT to any requesting IXC at*
21 *reasonable rates, terms and conditions.*
22

1 **Q. HAS THE FCC RULED THAT CLECS ARE OBLIGATED TO OFFER DTT TO**
2 **IXCS THAT WANT TO DELIVER TRAFFIC DIRECTLY?**

3 A. Yes, in the PrairieWave case, after stating that CLECs have the ability to charge for tandem
4 switching under certain circumstances, the FCC stated that this ability is premised upon
5 allowing IXCs to interconnect through DTT. The FCC stated as follows:

6 Our decision here is premised on the assumption that a competitive LEC
7 will permit an IXC to install direct trunking from the IXC's point of
8 presence to the competitive LEC's end office, thereby bypassing any
9 tandem function. So long as an IXC may elect to direct trunk to the
10 competitive LEC end offices, and thereby avoid the tandem switching
11 function and associated charges, there should be limited incentive for
12 competitive LECs to route calls unnecessarily through multiple switches,
13 as suggested by AT&T.³³
14

15 **Q. DOES NAT CURRENTLY OFFER DTT THROUGH ITS SOUTH DAKOTA**
16 **INTRASTATE ACCESS TARIFF?**

17 A. Yes. However, the tariff does not provide a rate for DTT. Section 3.8.1 B.1 states that
18 "All elements of Direct-Trunked Transport are priced on an Individual Case Basis (ICB)."
19 Thus Qwest cannot determine whether the DTT rate is reasonable or not.
20

21 **Q. DOES QWEST HAVE A PROPOSAL FOR WHAT WOULD BE A REASONABLE**
22 **RATE FOR DTT?**

23 A. Yes. As discussed above, the FCC in the Connect America order required LECs engaging
24 in access stimulation to apply the access rates of the price cap carrier, which in South
25 Dakota is Qwest Corporation. Qwest's proposes that its DTT rates should apply to any

³³ In the Matter of Access Charge Reform: PrairieWave Telecommunications, Inc. Petition for Waiver of Sections 61.26(b) and (c) or in the Alternative Section 61.26(a)(6) of the Commission's Rules, CC Docket No. 96-262, Released February 14, 2008, at ¶ 27.

1 office to any requesting IXC at the same rates, terms and conditions that Qwest
2 Corporation offers in South Dakota in order to prevent NAT from engaging in any form of
3 mileage pumping scheme.

4

5 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

6 A. Yes it does. Thank you.

Exhibit WRE-1

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UNITED STATES DISTRICT COURT

DISTRICT OF SOUTH DAKOTA

SOUTHERN DIVISION

* * * * *

Case Civ. 10-4110

SPRINT COMMUNICATIONS COMPANY, L.P.,

Plaintiff,

-vs-

NATIVE AMERICAN TELECOM, LLC;
B.J. JONES, in his official capacity
as Special Judge of Tribal Court; and
CROW CREEK SIOUX TRIBAL COURT,

Defendants.

U.S. District Courthouse
Sioux Falls, SD
March 3, 2011, 9:00 a.m.

* * * * *

MOTION HEARING

* * * * *

BEFORE: The Honorable Karen E. Schreier
U.S. District Court Judge

APPEARANCES:

Mr. Scott G. Knudson
Briggs & Morgan
2200 IDS Center
80 S. Eighth St.
Minneapolis, MN 55402-2157

-and-

Mr. Tommy Drake Tobin
Attorney at Law
PO Box 730
Winner, SD 57580

for the Plaintiff

1 A. Yes.

2 Q. Do you want to keep your relationship that you have --
3 do you want to keep NAT's relationship with
4 FreeConferenceCall?

5 A. Yes.

6 Q. Why?

7 A. Well, if it wasn't for FreeConferenceCall, there
8 really wouldn't be a NAT.

9 Q. Because --

10 A. Because of the world marketing they do, and they do
11 all the work.

12 Q. So without FCC, zero percent of zero would be zero.
13 Is that right?

14 A. Exactly.

15 Q. Peter, you touched on this previously back in October,
16 but I want to have you update the Court on NAT's efforts on
17 the Reservation.

18 A. Okay.

19 Q. Share with the Court the benefits that NAT provides to
20 your Tribal members.

21 A. There's a number of different benefits. Because of
22 the poverty there and the close to 90 percent unemployment,
23 a lot of our people cannot provide a phone or pay for a
24 phone. Because of NAT, you know, them services are
25 available, also with the Internet.

Exhibit WRE-2

1 A. So to speak, yes.

2 Q. Carlos, who do you get paid by each month?

3 A. Free Conferencing Corporation.

4 Q. So Free Conferencing Corporation is the entity that
5 actually pays your salary?

6 A. That's correct.

7 Q. In addition to your duties with FreeConferenceCall, do
8 you also serve as the controller for any other entities?

9 A. I do.

10 Q. We're going to go through those in a second. Are you
11 paid any type of money to do the work for those entities?

12 A. No, I'm not.

13 Q. Let's talk about those other entities you serve in
14 this role. What would be the first one?

15 A. Free Conferencing Corporation.

16 Q. You told us what you do for that.

17 A. Yes.

18 Q. What other entities do you serve as the controller or
19 the bookkeeper?

20 A. Native American Telecom.

21 Q. Native American Telecom, LLC, the party that's a
22 Defendant in this case?

23 A. Yes.

24 Q. Carlos, just for sake of shortening things up, if I
25 refer to Native American Telecom, LLC, as NAT, is that

Exhibit WRE-2

Exhibit WRE-3

1 A. I'm not employed by anybody, other than Free
2 Conferencing Corporation as the controller.

3 Q. So you're the controller of Free Conferencing
4 Corporation then?

5 A. Yes.

6 Q. Now, who do you report to at Free Conferencing
7 Corporation?

8 A. Jeff Holoubek.

9 Q. What is Jeff Holoubek's title at Free Conferencing
10 Corporation?

11 A. He's the Director of Legal and Finance.

12 Q. Mr. Holoubek reports to David Erickson?

13 A. I don't know.

14 Q. But David Erickson is the President and CEO of
15 Free Conferencing Corporation. Is that true?

16 A. Yes, it is.

17 Q. Your understanding is Jeff Holoubek is now the
18 President of Native American Telecom?

19 A. He is.

20 Q. Do you know when that took place?

21 A. I don't know the exact date. No.

22 Q. Was it in 2010?

23 A. I believe so.

24 Q. Would it have taken place when you assumed the duties
25 of controller for NAT?

Exhibit WRE-3

Exhibit WRE-4

1 \$6,000?

2 A. Because it still hasn't received any payments, and
3 it's had certain expenses that it's paid.

4 MR. SWIER: Your Honor, if I have not done so, I
5 would move Exhibit 28 into evidence.

6 THE COURT: Any objection?

7 MR. KNUDSON: No objection, Your Honor.

8 THE COURT: 28 is received.

9 BY MR. SWIER:

10 Q. Carlos, as the controller of NAT, are you aware of a
11 Marketing Fee Agreement that Native American Telecom has
12 with FreeConferenceCall?

13 A. Yes, I am.

14 Q. Based only on your knowledge, but what do you
15 understand that agreement between NAT and
16 FreeConferenceCall to be?

17 A. My understanding is that Native American Telecom gets
18 to keep 25 percent of the access charges received.

19 Q. Native American Telecom gets to keep 25 percent of the
20 gross or the net access fees?

21 A. The gross.

22 Q. In your role as a controller for these companies, and
23 based on the knowledge and experience you've gained, have
24 you had an opportunity to review multiple marketing
25 agreements between FreeConferenceCall and other companies

Exhibit WRE-4

0713

Exhibit WRE-5

0714

- 1.8 Will NAT be engaging in access stimulation as defined by the FCC in the Connect America order in the area that is the subject of its Application for Certificate of Authority?

RESPONSE/OBJECTIONS: *Subject to and notwithstanding the aforementioned general objections, such information is neither relevant nor reasonably calculated to lead to the discovery of admissible evidence in this Certificate for Authority matter. Without waiving said objections, yes.*

Exhibit WRE-6

1 the issue was the status quo, and in this case the status
2 quo cannot be maintained without payment being made to NAT.
3 Because if payment is not made to NAT, then NAT, as the
4 testimony indicated, is likely to either file bankruptcy or
5 likely to go out of business.

6 THE COURT: But in Grupo, the issue of whether
7 the money was owed or not was not even really contested,
8 unlike here there is a question that Sprint has raised as
9 to whether they even owe the money. They're not admitting
10 they owe the money. In Grupo that wasn't even a question.
11 The Supreme Court found that entering a preliminary
12 injunction was beyond the Court's power.

13 MR. SWIER: Your Honor, of course we have cited,
14 in our favor, the NewLife vs. Express Scripts case. That's
15 a 2007 --

16 THE COURT: From a District Court.

17 MR. SWIER: -- from a District Court in
18 Pennsylvania.

19 THE COURT: That's not binding on this Court.

20 MR. SWIER: Correct. It's simply used as a
21 factually analogous case. In the NewLife case --

22 THE COURT: They didn't even discuss Grupo.

23 MR. SWIER: They didn't discuss Grupo. That
24 wasn't brought up. But the fact is that Grupo --

25 THE COURT: So you think that's binding on me

Exhibit WRE-6

0717

1 going to read Grupo in that way, that any company can
2 simply cut off the oxygen of any other company, and that's
3 entirely permissible. I don't think Grupo is intended to
4 be read that broadly. I think it was very fact specific.

5 So I think with the claims that are brought, when you
6 look at maintaining the status quo, the only way we can
7 maintain the status quo here is for NAT to receive payment.
8 There's no other way.

9 As the other cases have indicated, if we receive
10 payment four, five, six months down the line, that doesn't
11 do NAT any good. They are either going to close their
12 doors, or they're going to file bankruptcy. We have
13 provided the concrete evidence for the Court to make that
14 determination. So I think that --

15 THE COURT: How is the remedy you are seeking
16 anything different than like prejudgment attachment?

17 MR. SWIER: Your Honor, in most circumstances, of
18 course, prejudgment attachment is not proper. But, again,
19 when you look at the facts here, equity is intended to not
20 let this type of thing happen. It's within the Court's
21 discretion, I believe, even with Grupo, because I think
22 that's a limited decision. I think even with Grupo, this
23 Court still has the ability under the affirmative defenses
24 and under the damages claim to maintain the status quo.

25 If these payments are not made for one or two or three