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Big phone companies try to end rural windfall

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South Dakota moved closer this week to becoming the first state to prohibit a controversial issue facing the telecommunications industry.

In question is a practice known as access stimulation, often referred to as "traffic pumping." While the debate is conducted in the technical language of telecommunications law, at stake is millions of dollars made by a few rural phone companies working with out-of-state firms to offer free conference calls and pornographic chats.

The kicker is that telecommunications giants - such as Qwest, Verizon and AT&T - are forced to pick up the bill.

Following spirited testimony Wednesday before the State Affairs committee, the panel voted to recommend legislation favoring the national companies.

"This is a complicated issue," said Dusty Johnson, commissioner of the South Dakota Public Utilities Commission, who did not take a position on the legislation, said in an interview.

"The whole notion of access charges is very foreign to people," he said. "Consumers don't pay access charges - it is what one telephone company charges another telephone company to use its network. It is behind the scenes for a lot of consumers."

Regulatory cases, eight lawsuits

Access stimulation is neither new nor exclusive to South Dakota. But here, where the great expanses of the state are fertile territory for abuse of rural telecommunications subsidies and an entrepreneurial spirit is championed, the issue has grown to a dull roar not heard anywhere else.

It has attracted the attention of some of the state's largest employers, its highest governmental bodies and, arguably, its most powerful political players.

The practice is at the center of eight lawsuits in the federal court system, several cases before regulatory boards and now legislation moving to the House floor.

And you still don't know what it is.

Why would you?

The effects of access stimulation don't show up on your telephone bill, and it doesn't affect your service - at least not yet.

Proposal would end sharing of fees

The practice involves some local telephone companies in rural areas of the United States driving up the volume of incoming calls to their networks by working with high-traffic services - often Web sites - that offer conference calling, pornographic chat or international calling. The calls are routed through a local phone number.

They make money because rural carriers can charge access fees to the national companies for incoming calls, even though firms such as AT&T can't control the flow of those calls. Then the small rural carrier splits the money with the calling service.

The legislation before the House would prevent revenue sharing between telephone companies and nontelephone companies, something lawyers, physicians and accountants are familiar with, said Rep. Deb Peters, R-Hartford, who drafted the legislation.

The practice undermines a compensation system that is supposed to support rural telecommunications and creates a bad image for the state, she said.

"Carriers engaged in such arrangements hurt all customers in South Dakota," Peters said.

Here's an example of how access stimulation works.

A person in New York City picks up their Verizon landline to call Aunt Rosie in rural Redfield. Since Verizon doesn't have a telephone line directly to Rosie's house, it has to work with someone who does, her local exchange carrier. To complete the call - which Verizon is required by law to do - it must pay to use the lines to Aunt Rosie's house.

Rosie's rural local company gets to charge a higher amount per minute on the call than a call from New York to Sioux Falls, say, because it is more expensive to connect Aunt Rosie's farm to the network. The reasons are fixed infrastructure costs and low-call volume in her area.

A typical connection fee to a nonrural area is a half a cent a minute. Calls to parts of South Dakota are relatively expensive - 8 or 12 or 18 cents a minute.

Phone giants decry practice of pumping

These calls - if multiplied by hundreds of callers joining a conference call or sex chat service - can mean revenue for a single rural company of millions of dollars a month. The share for carriers such as Verizon and AT&T can get to hundreds of thousands of dollars a month."

They don't like it one bit.

"This pattern of behavior was designed for one express purpose: to abuse the state's subsidy system, which supports phone service in rural areas, by siphoning off huge profits for private gain," said Beth Canuteson of AT&T.

She said AT&T applauds the legislation put forth that will, "rid South Dakota of fraudulent traffic pumping schemes designed to artificially inflate access revenues at the expense of consumers and long distance companies."

Not all local exchange carriers participate in access stimulation - in fact, a small minority increasingly is expensive to the long distance carriers.

Of the 700 rural carriers that AT&T works with all across the country, only 12 have been identified as "traffic pumpers." Those made up 40 percent of the company's expenses in September. That was up from February of last year when those 12 companies made up 33 percent of its expenses.

In South Dakota, calls for conferencing, pornographic chat and international calling services are five times all the terminated traffic that Qwest does in the entire state, according to testimony Wednesday.

Long-distance carriers, diligently checking their own phone bills, notice these sudden spikes in call volume.

"You might have had 2,000 minutes of access (per month) for a company and the next month just jumps to 2 million," said Max Phillips, state president of Qwest in South Dakota and Iowa. "You can see that these historical relationships are blown out of the water when they are engaging in this."

Phillips said he could not think of one good reason why anyone would vote against this legislation.

"It gives South Dakota an opportunity to set the landscape going forward and say we're going to stop this deceptive practice and level the playing field."

'No such thing as traffic pumping'

One of the companies in South Dakota the national long distance corporations want to get on level ground with is Northern Valley Communications in Aberdeen, a firm with 55 employees.

In opposition to the bill, Northern Valley's CEO, James Groft, said his company is involved in conference calling but, "it is not porn, it is not sex, it is not traffic pumping."

"There is no such thing as traffic pumping," he said. "It was created by large out-of-state ... carriers to put down a legitimate business practice."

Groft graduated from high school in Mellette and attended the University of South Dakota before heading to Aberdeen to start his business and raise his four children with his wife on a family farm. He said he is living the "typical South Dakota life."

Except that he has some uncollected payments due him.

Northern Valley, one of three companies in the state engaging in access stimulation, began participating in high-volume conferencing in 2005. Until 2007, all the national companies tasked with delivering calls to 605 numbers were paying their bills.

But beginning in 2007 some began to stop paying, including Sprint, which Groft said owes Northern Valley \$15 million, and AT&T, which he said owes \$20 million.

"That might be a drop in the bucket to them," Groft said. "It is not to us. It is a lot of money that could go to support South Dakota jobs and South Dakota investment."

He said that without the conference calling business these companies would owe Northern Valley about \$1 million over this period. Fees for that have not been received either.

To fight the legislation his company has hired some of the most prominent lobbyists in the state, including Jeremiah Murphy, a partner at Murphy, Goldammer & Pendergast in Sioux Falls; Harry Christianson, former counsel to Gov. Bill Janklow and former secretary for the state's Department of Commerce and Regulation; and Roger Tellinghuisen, former state attorney general.

"I don't know why that it is improper for any a business to grow their revenue, especially a South Dakota business," Groft said.

Lawmaker says S.D. part of 'bad five'

In 1996, when telecommunications were deregulated, the monopoly functions of the large corporations were broken down and the market set the price for phone service. That is why consumers now have flat-rate long distance plans.

One exception is rural areas.

A monopoly function remains for the business-to-business transaction of what a company such as Qwest pays rural carriers.

"South Dakota does have high access rates because we are a rural state and it is expensive to deliver calls," said Johnson of the Public Utilities Commission.

But Johnson points out "the fact that we have high access rates is not a sign of anything that is inappropriate."

Still, access stimulation happens only in states that have these high-access charges.

"We are one of the bad five," Peters said.

She lumps South Dakota with Iowa, Minnesota, North Dakota and Missouri, which also have local telecommunication companies taking part in this practice.

Concerns about paying for sex chats

Online, companies offering "totally free" conference calling, "free calls to China" and, most controversially, "hot live sex chat," provide people services for only the cost of a call to a the 712 area code in western Iowa, the 507 area code in southern Minnesota, or the 605 area code in South Dakota.

Many of these services are located in places such as California, Florida or Nevada, far from the termination of their phone calls and millions of people removed from the benefit of the rural subsidy.

One Houston-based company that terminates at a 605 area code offers an opportunity to help connect American men with Latina women by, "personally introducing you to some of the most beautiful and sincere ladies in the world and achieve your dreams too."

In addition to the revenue sharing concern, lawmakers are concerned some of the pornographic services are operating outside of the 1-900 designation that phone customers can block. Not only can children easily access it, they argue, it looks to a parent or any concerned person like a regular long distance call on a bill.

When asked by lawmakers whether he was aware how much of his conference call business is sexual, Groft said it is against the law for him to tap lines to find out.

"Anything we know about the type of calls is what we hear from other people," Groft said. "I don't think much, if any, of the traffic in our case is pornographic or sexual in nature."

Groft and his advocates said they feel very strongly that is a matter to be addressed by pending litigation and regulators, not the Legislature.

For others at the committee meeting Wednesday the vote, although 7-6, was a sign that legislators understand that pending litigation and other issues before regulators address disputes in the past and that this bill looks forward to address the practice in the future.

"The legislation does not outlaw conference calling, it just prohibits fee splitting between phone companies and nonphone companies," said Dan Nelson, director of Governmental Affairs at Midcontinent and a backer of the legislation.

"Those issues aren't before the courts right now. Yes there are lawsuits out there, but we're asking the policy making body of this government to take action and say we're uncomfortable with this going forward."

From here, the bill is scheduled to go before the full House on Tuesday.

"The debate will feature some of the same participants, making the same points, with a larger audience," Nelson said.

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