

FCC Clarifies “Carrier” Definition in Prepaid Calling Card Appeal

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On October 19, 2010, the FCC adopted an *Order* that clarifies which entity is subject to universal service fund (USF) contribution obligations in the prepaid calling card context. The *Order*: (1) clarifies that a "platform provider" does not provide prepaid card service based solely on the provision of platform services; and (2) reaffirms stringent due diligence requirements on service providers to document reseller revenues. In its *Order*, the FCC granted in part, and remanded in part, a request for review of a decision of the Universal Service Administrative Company (USAC) filed by Enhanced Network Telecom, LLP ("NetworkIP"). A 2008 USAC audit concluded that NetworkIP's services constituted prepaid calling card services, subject to USF contributions, and that a significant percentage of NetworkIP's customers were wholesale carriers subject to USF contribution assessments. On June 29, 2009, NetworkIP filed a Petition for Review with the FCC, challenging USAC's audit findings.

FCC Finds NetworkIP's Service Not Prepaid Calling Card Service

In the *Order*, the FCC analyzed NetworkIP's services and found that it was not structured as a prepaid calling card service provider under the FCC's rules. NetworkIP provides web-based computer software that enables switching and processing for long distance wholesale capability for prepaid calling card provider customers. The FCC held that NetworkIP's calling card platform service is not a prepaid calling card service, contrary to USAC's finding. The FCC reasoned that NetworkIP's software platform lacked characteristics of prepaid calling card service - NetworkIP does not create or sell calling cards to end-users, retailers, or its carrier customers, rather it sells minute-based access to its software enabling its customers to create and sell prepaid calling card services to end-users. Instead, it is NetworkIP's customers who perform the activities that constitute the provision of prepaid card service - principally, establishing PINs and setting the price of cards, the number of minutes available, and the rate at which value is decremented from the card.

This finding is significant for universal service contribution purposes. The FCC bases Universal Service contributions on end-user revenues. Prepaid calling card revenues are classified as end-user revenues and therefore are subject to universal service contribution assessments. The FCC's *Order* affirms that the identification of which entity is operating as a "carrier," and therefore, which entity is subject to USF contribution obligations, depends upon the factual circumstances in each case. Entities involved in the provision of prepaid card services should be careful to determine which entity is providing card service to end-users, and which are merely providing inputs to that service.

FCC Remands Case to Determine Whether Revenue Misclassified as Reseller Revenue

In addition to its platform service, NetworkIP provides "ordinary long distance transport" for at least some of its customers. This unquestionably is telecommunications service, and the FCC remanded the case back to USAC to address the issue of whether the NetworkIP improperly classified some of these revenues as "carrier's carrier revenue." During the 2008 audit, USAC directed NetworkIP to reclassify some of its revenue as end-user revenue because NetworkIP failed to document and maintain: (1) reseller certifications from some of its customers; (2) up-to-date reseller certifications from some of its customers (some were more than a year old); and (3) Form 499-A filer identification number (which demonstrates USF contribution) for certain customers and/or verify the USF contributions. NetworkIP challenged these assertions.

Although the FCC remanded the case to determine whether revenue's were misclassified, the FCC reaffirmed the need for service providers to properly document their reseller revenues - or face reclassification. The distinction between end-user and reseller revenue is significant. Whereas revenues from end-users are subject to USF assessments, revenues from resellers are not. The key distinction between resellers and end-users is that resellers are reasonably expected to contribute to the USF based on revenues from their offerings to end-users. The FCC places the burden on the wholesale carriers to demonstrate that revenues are from resellers reasonably expected to contribute to USF. The FCC requires at a minimum for service providers to have "documentation procedures" in place to verify reseller revenues and maintain reseller legal name, address, and name and phone number of a contact person. The FCC Form 499-A instructions provide additional guidelines for carriers to document reseller revenues such as maintaining: (1) a reseller's Form 499-A identification number; (2) a link to current USF contributors; and (3) a signed certification from the reseller certifying USF contributions.

Due Diligence Necessary to Verify Reseller Status

In the *Order*, the FCC emphasized that wholesale carriers must exercise due diligence to verify the reseller status of its customers. The FCC affirmed USAC's position in two key respects. First, it held that to the extent that NetworkIP failed to maintain filer ID numbers for its customers, USAC properly reclassified NetworkIP's revenues as end-user revenues. In so doing, the FCC reaffirmed due diligence requirements on wholesale carriers to verify the reseller status of their customers to satisfy the Reasonable Expectation Standard. Second, the FCC held that a reseller certificate, by itself, is not sufficient to certify reseller revenues. Carriers must exercise due diligence in addition to obtaining the certificate, such as verifying the reseller status of their customers by checking the USF filer database, maintaining filer ID numbers, or other independent evidence. Not properly documenting customer revenues can lead to reclassification subject to USF contributions during a USAC audit.

For further information on this *Order* and the implications for carriers, please contact the [Communications Practice Group](#) at Kelley Drye & Warren LLP.