> [T]he existence of seven [R]BOCs increases the number of benchmarks that can be used by regulators to detect discriminatory pricing. Indeed, federal and state regulators have in fact used such benchmarks in evaluating compliance with equal access requirements . . . and in comparing installation and maintenance practices for customer premises equipment.[248]

128. In another case, the court relied in part on benchmarking in rejecting a DOJ proposal to restrict RBOC marketing of customer premises equipment (CPE) to residential and single-line business customers. Specifically, the court noted that, "with seven different [RBOCs] involved in installation and maintenance, claims of one Operating Company that it had particular difficulties or problems with the equipment of manufacturers it did not sell could be readily undermined by a comparison with the practices of the other six companies."[249]

129. In addition to recognizing the value of benchmarking, federal courts regularly employed benchmarking by comparing practices among the RBOCs. For example, in ordering Pacific Bell to provide access lines for AT&T's coinless public telephones, the district court twice noted that Pacific Bell appeared to be the only RBOC not providing the required access.[250] Ruling on a separate motion, the court noted that no other RBOC had attempted, as Bell Atlantic had, to sell embedded CPE to the General Services Administration prior to the divestiture-related assignment of CPE accounts, assets and employees to AT&T.[251]

b) The Commission's Use of Comparative Practices Analyses

130. The Commission has long used various forms of comparative practices analyses in carrying out the objectives of the Communications Act. Broadly speaking, comparing the practices of several major incumbent LECs has enabled the Commission to determine whether an individual incumbent's claim concerning technical feasibility is warranted, or to monitor service quality with minimal regulatory intervention. Below are a sample of the examples of the Commission's use of such comparisons to implement the Communications Act and, most notably, the pro-competitive mandates of the 1996 Act.

131. The Commission employed "best-practices" benchmarking in implementing the local competition provisions of the 1996 Act. In interpreting the requirement that incumbent

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248 *United States v. Western Elec. Co.*, 993 F.2d 1572, 1580 (D.C. Cir.), *cert. denied*, 510 U.S. 984 (1993) (citation omitted).

249 *United States v. AT&T*, 1982-2 Trade Cas. (CCH) ¶ 64,980, 1982 WL 1893 at *2 n.8 (D.D.C. Aug. 23, 1982).

250 *United States v. Western Elec. Co.*, 583 F. Supp. 1257, 1258 n.4, 1259 n.11 (D.D.C. 1984), *aff'd* 846 F.2d 1422, *cert. denied*, 488 U.S. 924 (1988).

251 *United States v. Western Elec. Co.*, 578 F. Supp. 680, 684 n.13 (D.D.C. 1983). Specifically, the court queried that "[i]f Bell Atlantic had that right with respect to CPE, why would not every other Operating Company have that same right with respect to all the other assets (*e.g.*, switches, land, buildings, transmission facilities) that under the decree and the plan are to go to AT&T on January 1, 1984?" *Id.*

LECs provide interconnection and access to UNEs at any "technically feasible point,"[252] for example, the Commission concluded that successful interconnection or access to a UNE at a particular point in one incumbent LEC's network is substantial evidence that interconnection or access is technically feasible at that point in other networks employing substantially similar facilities.[253] Similarly, the Commission found that successful interconnection at a particular level of quality in one LEC's network is substantial evidence of the feasibility of interconnection at the same level of quality in another LEC's network.[254]

132. This Commission also adopted a "best-practices" approach in addressing collocation issues in its recent *Advanced Services Further Notice*. Specifically, we concluded that any collocation method used by one incumbent LEC is presumptively technically feasible for all other incumbents.[255] We stated that "[t]he incumbent LEC refusing to provide such a collocation arrangement, or an equally cost-effective arrangement, may only do so if it rebuts the presumption before the state commission that the particular premises in question cannot support the arrangement because of either technical reasons or lack of space."[256] We emphasized that "[w]e believe this 'best practices' approach will promote competition."[257] The Commission therefore considered the use of comparative practices analyses to be an efficient, pro-competitive method of evaluating the parameters of incumbents' interconnection or access arrangements.

133. The *Advanced Services* proceeding also illustrates that an incumbent LEC's unique approach can set the industry standard. In that proceeding, we addressed the issue of how to allocate the "up-front" costs incurred in preparing collocation space. Relying on an approach developed by Bell Atlantic in its New York section 271-pre-filing statement, under which each competitor was responsible only for its pro-rata share of the cost of conditioning the collocation space, we adopted Bell Atlantic's approach as a national standard and required incumbent LECs to allocate space preparation and other collocation charges on a pro-rated basis.[258] The

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252 47 U.S.C. § 251(c)(2), (c)(3).

253 *Local Competition Order*, 11 FCC Rcd. at 15606, para. 204. The Commission stated that the "substantial similarity of networks" may be evidenced by adherence to the same interface or protocol standards.

254 *Id.*

255 *Advanced Services Further Notice*, 14 FCC Rcd at 4786-87, para. 45.

256 *Id.* After noting that U S West already had provided cageless collocation to competitors, the Commission rejected the counter-arguments of Bell Atlantic, SBC and GTE regarding alleged risks to their equipment from such arrangements and required all incumbent LECs to provide a cageless collocation option for competitors. *Id.* at 4784-85, 4786-87, paras. 42, 45.

257 *Id.* at 4786-87, para. 45.

258 *Id.* at 4789-90, paras. 50-51. The Commission's adoption of Bell Atlantic's pro-rata approach for allocating space preparation costs is reminiscent of the Commission's adoption of Northwestern Bell's (NWB) pro-rata allocation plan in the *Default Traffic Plan* proceeding. *See Investigation of Access and Divestiture Related Tariffs*, CC Docket No. 83-1145, Memorandum Opinion and Order, 101 FCC2d 911, 924 (1985), at para. 32 (*Default Traffic Plan Order*). In that proceeding, most of the RBOCs had adopted the plan approved by the MFJ Court for routing of all default inter-exchange traffic to AT&T. NWB's experience with its pro-rata allocation plan led the DOJ and the Commission to reverse their support of the original default plan. DOJ noted, *inter alia*, that "NWB's experience has proved that a viable and reasonable alternative to default exists." *Id.* at 914, para. 8. The Commission, which ultimately adopted a uniform pro-rata allocation plan modeled after NWB's approach, explained that "prior concerns that an allocation plan would cause undue customer burden and confusion have been

Commission's explicit reliance on benchmarking in our recent orders implementing the advanced services provisions of the 1996 Act highlights the continued vitality of benchmarking as a market-opening tool for the future.

134. Just as best-practices benchmarking forms the foundation for the Commission's analysis of technical feasibility and collocation issues, average-practices benchmarking is the Commission's primary tool for monitoring service quality and detecting unreasonable or discriminatory costs or practices. In creating the Automated Reporting Management Information System (ARMIS) to monitor the effect of price cap regulation on large incumbent LECs' service quality and infrastructure development, the Commission directed the Common Carrier Bureau to promote uniformity in reporting factors so that the data collected would "be similar enough to permit ready benchmarking."[259] In response to a request by various incumbent LECs asking the Commission to reverse a Bureau decision to use ARMIS reports as the benchmark for comparing service quality among incumbent LECs, the Commission, affirming the Bureau's decision, stated that uniform ARMIS reporting allows for "useful comparisons on incumbent LEC performance."[260] Reaffirming the importance of benchmarking in identifying instances where an incumbent LEC has allowed its service quality to degrade in order to extract greater profits from its capped rates, the Commission emphasized that "[f]rom the inception of the monitoring program, benchmarking has been a primary goal."[261]

135. As a final example highlighting the Commission's continued use of comparative practices analyses in the post-1996 Act era, the Commission has employed average-practice benchmarking in reviewing the cost support filed by incumbent LECs in connection with new services. For example, in investigating physical collocation tariffs, the Commission, recognizing that most incumbent LECs had little or no relevant operating experience or historical data, concluded that it was reasonable to pool all incumbent LECs' direct cost estimates in order to calculate an industry-wide average.[262] Then, if any individual incumbent LEC's cost estimate

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dispelled by NWB's experience," and "[t]he implementation of the NWB Plan has provided sufficient evidence that a viable alternative to default exists." *Id.* at 918, 920-21, paras. 18, 23.

[259] *Policy and Rules Concerning Rates for Dominant Carriers*, CC Docket No. 87-313, Second Report and Order, 5 FCC Rcd. 6786, 6828, para. 341, n.455 (1990) (*LEC Price Cap Order*).

[260] *See Service Quality Standards Order,* 12 FCC Rcd. at 8140, 8141, paras. 59, 61. *See also Service Quality Modifications Order*, 8 FCC Rcd at 7475-76, at paras. 7-8 ("While we acknowledge that there are differences among the LECs, we also affirm that benchmarking is not only desirable but indispensable. . . . We believe that benchmarking will enable us to evaluate the impact of price cap regulation on the quality of service provided by the LECs and on the rate of development of technological improvements that are reflected in the LEC infrastructure reports.").

[261] *Service Quality Standards Order*, 12 FCC Rcd at 8139-40, para. 57. As Sprint noted, SBC implicitly conceded the importance of this type of service quality monitoring when it submitted a document in this proceeding defending the post-merger performance of Pacific Bell by making comparisons with other incumbents. *See* Sprint Apr. 2 *Ex Parte* Att., John B. Hayes et. al., "Empirical Analysis of the Footprint Effects of Mergers Between Large incumbent LECs," at 9 (*citing Pacific Bell: Post-Merger Performance*, submitted as attachment to Letter from Zeke Robertson, SBC, to Magalie Roman Salas, FCC, CC Docket No. 98-141 (filed Feb. 23, 1999)).

[262] *In the Matter of Local Exchange Carriers' Rates, Terms, and Conditions for Expanded Interconnection Through Physical Collocation for Special Access and Switched Transport,* CC Docket No. 93-162, Second Report and Order, 12 FCC Rcd. 18730, 18793-96 at paras. 142-46 (1997).

substantially deviated from the benchmark average, the Commission could set that LEC's tariff for further investigation into reasonableness. The Commission has used a similar average-practice methodology in other tariff review proceedings, including evaluating non-primary residential line counts for presubscribed interexchange carrier charges[263] and number portability cost components.[264]

c) State Regulators' Use of Comparative Practices Analyses

136. State regulators likewise have relied on various forms of comparative practices analysis in carrying out their roles in monitoring carrier activity in their state and opening local markets to competition.[265] State regulators periodically compare the practices of incumbent LECs operating within their state. For example, an Illinois Commerce Commission (ICC) arbitration decision between AT&T and GTE included numerous examples in which the ICC directed GTE to adopt terms for AT&T that Ameritech had agreed to with other parties.[266] Likewise, when Ameritech recently objected to the Ohio Public Utilities Commission's requirement that it allow customers with past-due toll balances to switch to a new interexchange carrier, the commission observed that "every LEC except Ameritech has implemented our

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263 *See In the Matter of Access Charge Reform*, CC Docket No. 96-262, First Report and Order, 12 FCC Rcd. 15982 (1997) (*Access Charge Reform Order*). When evaluating tariff filings of the price cap LECs implementing the Presubscribed Interexchange Carrier Charge (PICC) required by the Commission's 1997 *Access Reform Order*, the Commission set a benchmark by calculating the percentage of non-primary residential lines to total residential lines reported by price cap LECs and then comparing those percentages to data collected by the Bureau, independent studies, and price cap LECs' public statements. *In the Matter of Tariffs Implementing Access Charge Reform*, CC Docket No. 97-251, Memorandum Opinion and Order, 13 FCC Rcd 14683 (1998), at paras. 29-31 (*Access Charge Reform Tariffs Investigation Order*). Because SNET's penetration ratios were significantly lower than the benchmark, the Bureau ordered SNET to detail the procedures and data used to estimate non-primary residential lines and to present evidence to justify its low penetration ratio. *1998 Annual Access Tariff Filings, SNET Revisions to Tariff FCC No. 731*, CC Docket No. 98-104, Memorandum Opinion and Order, Order Designating Issues for Investigation and Order on Reconsideration, 13 FCC Rcd. 13977, 13983-84 at paras. 15-19 (1998). Thus, as with best-practices benchmarking, the use of average-practice benchmarking may be less intrusive than alternative measures to assess improper or discriminatory behavior, such as initially requiring full detail from every incumbent.

264 In designating for investigation Bell Atlantic's imposition of a "transport component," the Commission noted that "no other carrier includes such a component or establishes different rates for Tandem and End Office queries." *See Number Portability Query Services*, CC Docket No. 98-14, Order Designating Issues for Investigation, 13 FCC Rcd 12063, 12068-69 at para. 9 (1998). The Commission also designated for investigation Pacific Bell's and Southwestern Bell's imposition of "non-recurring" charges that were nevertheless imposed on a monthly basis, noting "that no other carrier has proposed similar charges." *Id.* In that same paragraph, the Commission employed comparative practices analyses in noting "that charges for some query services vary widely among carriers. For example, Ameritech's proposed tandem query charge is 3.6 times that of Southwestern Bell." *Id.*

265 *See* Comments of the Public Service Commission of Wisconsin, CC Docket No. 98-141 (filed July 15, 1999), at 7 ("Benchmarking can be used to evaluate a company's quality of service, cost characteristics, rate levels, innovation efforts, competitive efforts, and technical and economic feasibility issues.").

266 *AT&T Communications of Illinois, Inc. Respondents: GTE North Inc; GTE South Inc,* Illinois Commerce Commission, Arbitration Decision, 96-AB-005 at 2, 4, 11, 17, 28, 30 (ICC Dec. 3, 1996).

existing toll blocking policy," and thus found no basis to exempt Ameritech "from the requirements which every one of the other LECs is following."[267]

137. State regulators at times also compare the practices of the major incumbent LECs operating in other regions to the conduct of incumbents in their state.[268] For example, as AT&T points out, in rejecting the claims of Ameritech that it could not provide competitors using unbundled local switching with the billing information necessary to bill for terminating access or for originating toll free access, the ICC found "it quite instructive that many other RBOCs have voluntarily agreed to or have been ordered by state commissions to provide such information."[269] Likewise, in the New York section 271 collaborative hearings, after Covad indicated that no security problems arose in its cageless collocation arrangements with U S WEST in Washington state, Bell Atlantic retreated from its claims that security concerns and network risks prevented it from providing cageless collocation.[270] Similarly, in reviewing Ameritech Indiana's central office floor space charge, the Indiana Utility Regulatory Commission found "no reason to believe that Ameritech's central offices are constructed at a level of quality different than any other RBOC's central offices."[271]

138. As an example of a state regulators' use of RBOC average-practice benchmarking, the Public Utility Commission of Texas (Texas PUC), in arbitrating Southwestern Bell Telephone Company's interconnection agreements with five competitive LECs, found insufficient record evidence for collocation costs and therefore deemed "it reasonable to base interim rates on the average rates set in collocation agreements entered into by a sample of other RBOCs."[272] Similarly, the Texas PUC adopted an aggregate methodology for assessing avoided cost discounts when it found, *inter alia*, that SWBT's service-specific avoided

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[267] *Amendment of Chapter 4901:1-5 of the Ohio Administrative Code*, PUCO Case No. 96-1175-TP-ORD, Finding and Order at para. 16 (Ohio PUC Apr. 8, 1999), (directing Ameritech to bring itself into full compliance with Ohio PUC's selective toll blocking policy).

[268] *See* SBC/Ameritech Nov. 16 Reply Comments, Schmalansee and Taylor Reply Aff. at 28 (observing that "state regulators frequently compare local interconnection and retail service prices across states as a guide to the reasonableness of the prices proposed in their state.").

[269] *See* AT&T Apr. 7 *Ex Parte* at 14 n. 7 (*citing* Investigation into Forward Looking Cost Studies and Rates of Ameritech Illinois for Interconnection, Network Elements, Transport and Termination of Traffic, *et al.*, Illinois Commerce Commission, Docket Nos. 96-0486/96-0569, Second Interim Order at 115 (ICC Feb. 17, 1998)).

[270] *See* AT&T Apr. 7 *Ex Parte* at 16 n.9 (*citing* Proceeding on Motion of the Commission to Examine Methods by Which Competitive Local Exchange Carriers Can Obtain and Combine Unbundled Network Elements, Docket No. 98-C-0690, Opinion No. 98-18, at 20-23 (N.Y. PSC Nov. 23, 1998)). Bell Atlantic ultimately offered a compromise form of cageless collocation.

[271] *Investigation and Generic Proceeding on Ameritech Indiana's Rates for Interconnection, Service, Unbundled Elements, and Transport and Termination Under the Telecommunications Act of 1996 and Related Indiana Statutes*, Indiana Utility Regulatory Commission, Cause No. 40611 at 40 (Jun 30, 1998), (finding no basis to accept Ameritech's selection of the highest cost percentile in applying the Building Construction Cost Data Guide).

[272] *Petition of AT&T Communications of the Southwest, Inc. for Compulsory Arbitration to Establish an Interconnection Agreement Between AT&T and Southwestern Bell Telephone Company*, Docket No. 16226, Arbitration Award at 43 (Tex PUC Nov. 7, 1996).

cost estimates, "on their face, are so inconsistent with the experiences of the FCC and other states."[273]

139. As a final form of state regulators' use of comparative practices analyses, occasionally states compare divergent approaches among different local operating companies owned by the same holding company. For example, the Michigan PUC's requirement that Ameritech implement number portability in Michigan uses Ameritech's progress in Illinois as a benchmark.[274] Because such comparisons would be impossible if the local operating companies initially were to act in lock-step fashion (*i.e.*, before a best practice is identified), this form of comparison depends upon the local operating companies retaining independence to adopt innovative practices, notwithstanding their common ownership by one regional holding company.[275] As this sample of benchmarking examples illustrates, the ability to make benchmark comparisons, across independent, or at least semi-autonomous, operating companies constitutes an effective, and minimally intrusive, tool for state regulators.

d) Competitors' Use of Comparative Practices Analyses

140. Comparative practices analyses are also crucial for the incumbents' competitors which must rely on incumbent LECs for interconnection, access and unbundled elements. This explicit need to rely on the incumbents' facilities and services distinguishes the section 251 negotiation process from commercial negotiations in other competitive markets.[276] Consistent with the analysis above, competitive LECs commenting in this proceeding assert that in their interconnection negotiations with incumbent LECs, and in various state or federal proceedings implementing the Communications Act, they compare the incumbent LEC's price structure, provisioning, or claims about the feasibility of a particular service against their experiences with other incumbents.[277]

141. Both MCI WorldCom and AT&T, as well as other competitive LECs, provide examples of their use of benchmarking among the major incumbent LECs. When Bell Atlantic faced problems with premature switch translations and re-use of customer facilities, for example, MCI WorldCom urged Bell Atlantic to use BellSouth's process for local number portability cutovers (*i.e.*, deploying a direct interface from the Number Portability Administration Center to

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[273] *Id.* at 18.

[274] *See Ohio, Colorado, Michigan Adopt Local Competition Rules*, State Telephone Regulation Report, Vol. 14, No. 13 (June 27, 1996).

[275] As discussed below, SBC indicates that it intends to apply largely uniform policies for all its operating companies in dealings with competitive LECs following merger with Ameritech. *See infra* at Section V.C.4.b)(Loss of Independence of Operating Companies).

[276] *See Local Competition Order*, 11 FCC Rcd at 15611, para. 216.

[277] MCI WorldCom Oct. 15 Comments, Joint Decl. of Michael A. Beach and Therese K. Fauerbach, at para. 18-19. As discussed above, competitive LECs generally must study and compare the practices employed by various incumbents in order to offset the informational advantage held by the incumbents in interconnection negotiation and arbitration.

its provisioning systems).[278] Similarly, after NYNEX developed a special "VETS" testing vehicle for ensuring that competitors' NXXs are opened and dated correctly, MCI WorldCom suggested to other incumbents, such as Pacific Bell, that they adopt this improved internal NXX activation and testing process.[279] MCI WorldCom also objected to certain proposed collocation requirements of one RBOC (BellSouth) by pointing out that other RBOCs did not require those practices.[280] Finally, in appealing an interconnection agreement, MCI WorldCom argued against Bell Atlantic-Massachusetts's assumption that feeder facilities constructed of fiber-optic cable, rather than copper, were most cost-efficient for all loops, regardless of length, by showing that no other incumbent LEC had cost-justified the use of fiber-optic cable in loops with lengths less than 9,000 feet.[281] As these examples illustrate, MCI WorldCom's ability to compare the practices of a large number of independent major incumbent LECs has enabled it to refer certain incumbent LECs to proven alternate, and more pro-competitive, practices.

142. AT&T also cites several instances in which it used the practice of one RBOC as leverage to defeat claims by another RBOC regarding technical feasibility. AT&T's examples include the following:

- *Selective Routing of Operator and Directory Assistance Services.* When SBC claimed that selective routing of a competitive LEC's operator and directory assistance traffic to the competitive LEC's own operator centers was not technically feasible, AT&T introduced evidence that Bell Atlantic had agreed to perform such selective routing in Pennsylvania. SBC subsequently committed to develop the capability to perform the same function.[282]

- *Mechanized Loop Testing.* AT&T, challenging SBC's contention in state arbitrations that it was technically infeasible to provide mechanized loop testing (MLT) to competitive LECs using unbundled local switching,[283] pointed out that Bell Atlantic and BellSouth, which use

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[278] MCI WorldCom May 13 *Ex Parte* at 2 (citing *Petition of New York Telephone Company for Approval of Its Statement of Generally Available Terms and Conditions Pursuant to Section 252 of The Telecommunications Act of 1996 and Draft Filing of Petition of InterLATA Entry Pursuant to Section 271 of the Telecommunications Act of 1996*, Case 97-C-0271, MCI WorldCom Affidavit at para. 59 (filed Oct. 24, 1998))).

[279] MCI WorldCom May 13 *Ex Parte* at 4.

[280] Specifically, MCI WorldCom's expert testified in a Tennessee proceeding that BellSouth's proposal that competitive LECs use drywall enclosures with a security mesh above the 8'6" level appeared unnecessary, as Bell Atlantic and other incumbent LECs that did not have analogous requirements were operating without any apparent safety or transmission problems. MCI WorldCom May 13 *Ex Parte* at 3-4 (*citing Permanent Cost Proceeding for UNEs in Tennessee*, Tennessee Regulatory Authority, Docket No. 97-01262, Rebuttal Testimony of Gerald B. Crockett on Behalf of MCI Telecommunications Corp and AT&T Communications of the South Central States, Inc. at 6-8 (filed Oct. 17, 1997)).

[281] MCI WorldCom May 13 *Ex Parte* at 2 (*citing MCI Telecommunications Corp., et al. v. New England Telephone & Telegraph Co.*, Civil Action No. 98-CV-12375 (RCL), Opening Brief of MCI, at 17 (filed Apr. 30, 1999), (stating that Southwestern Bell uses copper feeder lengths for loops less than 12,000 feet, as do BellSouth and Ameritech for loops less than 9,000 feet)).

[282] *See* AT&T Apr. 7 *Ex Parte* at 17 (*citing* Petition of AT&T Communications of the Southwest, Inc. for Compulsory Arbitration to Establish an Interconnection Agreement Between AT&T and Southwestern Bell Telephone Company, Docket No. 16226, Arbitration Award at 5, Att. Stipulation at 1 (Tex. PUC Nov. 7, 1996)).

[283] *See* AT&T Apr. 7 *Ex Parte* at 15.

the same switch technology as SBC, were able to provide competitive LECs with such MLT capability. As a result, at least two states, Texas and Missouri, have required SBC to provide MLT.[284]

- *Collocation of Remote Switching Module.* When Bell Atlantic claimed that collocation of remote switching modules (RSMs) was not feasible because it would exhaust central office space and require extensive central office modifications for its unique grounding requirements,[285] AT&T demonstrated that SBC had stipulated in its Texas arbitration that it would allow competitive LECs to collocate RSMs for access to unbundled elements without any restrictions on equipment.[286] Ultimately, AT&T won the right to conduct RSM collocation in every Bell Atlantic state except Virginia.

- *Interim Number Portability.* When Bell Atlantic resisted AT&T's requests that it provide two particular methods of implementing interim number portability, namely Route Indexing-Portability Hub (RIPH) and Directory Number Route Indexing (DNRI), AT&T pointed out that other RBOCs had agreed or been ordered to provide the methods and arranged for a representative from BellSouth to provide Bell Atlantic technical guidance on performing the translations required by RIPH or DNRI. After speaking with the BellSouth representative, Bell Atlantic agreed to provide DNRI, subject to joint technical and operational testing.[287]

- *Advanced Intelligent Network (AIN) Triggers.* In an arbitration with New York Telephone, AT&T responded to New York Telephone's concerns that AT&T's requested AIN access would raise security and network reliability issues by stating that the technology had been satisfactorily tested in a trial conducted by AT&T and BellSouth.[288]

143. The Applicants themselves confirm the existence of this type of benchmarking. For example, John Starkey, Vice President of Sales for SBC, explains that competitive LECs

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[284] *See id.* (*citing* Petition of AT&T Communications of the Southwest, Inc., for Compulsory Arbitration to Establish an Interconnection Agreement Between AT&T and Southwestern Bell Telephone Company, Docket No. 16226, Order at App. B, 10-11 (Tex. PUC Sept. 30, 1997); Order Approving implementation Schedule at Att. A, 13, 15 (Tex. PUC Mar, 17, 1998); AT&T Communications of the Southwest, Inc.'s Petition for Second Compulsory Arbitration Pursuant to section 252(b) of the Telecommunications Act of 1996 to Establish an Interconnection Agreement with Southwestern Bell Telephone Company, Case No. TO-98-115, Report and Order at 21-22 (Mo. PSC Jan. 2, 1998)).

[285] *See* AT&T Apr. 7 *Ex Parte* at 16.

[286] *See* AT&T Apr. 7 *Ex Parte* at 16-17 (*citing Petition of AT&T Communications of the Southwest, Inc. for Compulsory Arbitration to Establish an Interconnection Agreement Between AT&T and Southwestern Bell Telephone Company*, Docket No. 16226, Arbitration Award (Tex. PUC Nov. 7, 1996), at para. 5; Att. Stipulation at 1).

[287] *See* AT&T Apr. 7 *Ex Parte* at 17-18 (*citing* Affidavit of Penn Pfautz on Behalf of AT&T Communications of Maryland, Inc., Maryland 271 Investigation, Case No. 8751 (Maryland PSC, filed Apr. 11, 1997)).

[288] *Petition of AT&T Communications of New York, Inc. for Arbitration of an Interconnection Agreement with New York Telephone Company*, Case Nos. 96-C-0723, 96-C-0724, Opinion and Order Resolving Arbitration Issues (Nov. 29, 1996), at 28 (granting AT&T the ability to interconnect with New York Telephone's AIN system subject to testing and certification).

often bring to SBC's attention the practice of one SBC operating company, or of another RBOC. He further acknowledges that SBC has been compelled to adopt such practices throughout SBC's region to ensure a good flow-through rate.[289] One of Ameritech's affiants, Wharton B. Rivers, also cites an example where AT&T successfully argued for a modification in Ameritech's policy regarding the purchase of high capacity transport (services with DS1 or greater capacity) by comparing the methods used by all the major carriers and requesting that Ameritech implement SBC's procedures.[290] "Because of AT&T's request," Mr. Rivers explains, "many of [SBC's] procedures that were superior to those we were previously using have become standard with [Ameritech]."[291] Thus, the examples provided by competitors of SBC and Ameritech, as well as the Applicants themselves, confirm the importance of benchmarking to competitors seeking to offset incumbent LECs' informational and bargaining advantages.

4. Adverse Effects of SBC/Ameritech Merger

144. We now examine the potential effect of the proposed merger on the effectiveness of comparative practices analyses as a minimally-intrusive market-opening tool. More specifically, we consider in turn the merger's likely impact upon the diversity of approaches among major incumbent LECs to comply with the Communications Act and adopt market-opening measures (a) at the holding company level, (b) at the local operating company level, and (c) at the industry level. We conclude that the merger of SBC and Ameritech would have a significant adverse impact on the ability of regulators and competitors to employ comparative practices analyses, which ultimately would force regulators to substitute more intrusive, more costly, and less effective methods of regulation to the detriment of the public interest.

a) Loss of Ameritech as Independent Holding Company

145. We find that, with only six major incumbent LECs remaining today (the RBOCs and GTE), the elimination of Ameritech as an independent source of observation would seriously impair the ability of regulators and competitors to use comparative practices analyses to facilitate implementation of the Communications Act, particularly sections 251 and 271, the core provisions for promoting and assuring competition in local telephony. Moreover, by reducing the number of major incumbent LECs, the merger makes it less likely that deviations from the average benchmark will be identified confidently as unreasonable and punishable. Finally, if prior experience is any indication, the loss of Ameritech would severely affect the likelihood that a maverick would emerge to present a different approach or, at a minimum, to assist regulators and competitors in evaluating the claims of other incumbents.

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[289] SBC Mar. 29, 1999, *Ex Parte* Meeting. Memo from To-Quyen Truong, Common Carrier Bureau, to File (filed Aug. 18, 1999) (Truong Memo).

[290] SBC/Ameritech July 24 Application, Rivers Aff. at 8-9, para. 21. Mr. Rivers describes himself as a "firm believer in the use of best practices analysis," who regularly measures and compares operating performance "both internally across operation centers and externally with other companies." *Id.* at 7, para. 18.

[291] *Id.*, at 9, para. 21.

146. As with the Bell Atlantic/NYNEX merger, which the Commission concluded would reduce experimentation and diversity of viewpoints in the process of opening markets,[292] the proposed merger removes another independent source of experimentation and diversity. By admitting that each company, pre-merger, has different practices, the Applicants essentially acknowledge that there is diversity in the manner in which these companies market and provision services, deploy new technologies and respond to competitors. As a result of the merger, regulators and competitors will lose the problem-solving opportunities that flow from this diversity of approaches.

147. The record from prior RBOC mergers shows that, after both mergers, the acquiring firm quickly eliminated certain policies of the acquired company that were in conflict with those of the acquiring company.[293] For example, following their respective mergers, NYNEX and PacTel each altered their prior support of a three-category approach for delineating the scope of services for which carriers can use customer proprietary network information to conform with the favored approach of their merger partner.[294] As KMC notes, following its merger with SBC, Pacific Bell rescinded its pre-merger market trial of a "Calling Party Pays" billing and collection arrangement with a cellular provider.[295] Similarly, Sprint points out that Bell Atlantic, following its acquisition of NYNEX, reversed NYNEX's pre-merger practice of allowing assignment of existing customer contracts to resellers without treating the assignments as contract terminations triggering termination penalties.[296]

148. In particular, the proposed merger's elimination of Ameritech as an RBOC benchmark would acutely affect regulators and competitors seeking to ensure compliance with section 271. Retaining a significant number of independent RBOCs is particularly important as regulators consider whether, under section 271, an RBOC has opened its local market

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292 *Bell Atlantic/NYNEX Order*, 12 FCC Rcd at 20060-61, paras. 152-53.

293 *See also* State Attorneys General Apr. 27 *Ex Parte* at 20 ("RBOC mergers tend to facilitate the presentation of a united RBOC front and coherent strategy to the CLECs and regulators that are trying to their markets open.").

294 *See Implementation of the Telecommunications Act of 1996: Telecommunications Carriers' Use of Customer Proprietary Network Information and Other Customer Information*, CC Docket No. 96-115, Second Report and Order and Further Notice of Proposed Rulemaking, 13 FCC Rcd 8061 (1998), at para. 28 n.105 ("We note that NYNEX and PacTel also deemed the three category approach acceptable in their initial pleadings in this docket. . . . Since their respective mergers, which occurred after their comments were received in this proceeding, however, Bell Atlantic/NYNEX and SBC/PacTel now support the 'single category approach.'").

295 KMC Oct. 15 Comments at 18. *See also* Sprint Apr. 1 *Ex Parte* Att. 2 "Post-merger Examples of the Spread of Degraded Practices in the Acquired BOC's Territory and Worsening Conditions in the Acquiring BOC's Territory," at . According to KMC, SBC later told the carrier that it could not use Pacific Bell's tariffed billing and collection services to provide CPP. Sprint notes that the same cellular provider currently has billing and collection agreements with Ameritech that allow for the provision of CPP, which could be placed in jeopardy by SBC's acquisition of Ameritech.

296 Sprint Apr. 1 *Ex Parte* Att. 2, at 2 (citing *Joint Application for Approval of the Reorganization of Illinois Bell Telephone Co. d/b/a Ameritech Illinois, and the Reorganization of Ameritech Illinois Metro, Inc.*, Dkt. 98-0555, Direct Test. Of Charlotte F. Terkeurst on behalf of the Government and Consumer Intervenors, GCI Ex. 2.0 at 50 (ICC Oct. 28, 1998)).

sufficiently to qualify to provide in-region, interLATA services in a given state.[297] Indeed, benchmarking among the RBOCs may become even more important after they have received section 271 authorization, as regulators and competitors seek to prevent possible backsliding by the RBOCs.

149. The loss of Ameritech's independence would be especially severe because Ameritech frequently has taken an approach that differs from the position taken collectively by the other RBOCs. The Commission has emphasized that, by proposing a framework to eliminate legal, economic and technical barriers to local competition, Ameritech's Customers First Plan, announced in 1993, constituted a major advance in telecommunications policy.[298] Ameritech also exhibited a willingness to adopt a flexible approach to competition by entering into a cooperative venture with Northpoint Communications, Inc., a data competitive LEC. This venture led to Ameritech's general support of the Commission's proposal for a separate subsidiary approach to advanced services, in contrast to the strong opposition from the other RBOCs.[299]

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[297] Although DOJ and the Commission evaluate each BOC's section 271 application for each state on an individual basis, reference to the best practices and average practices within the industry, and among BOCs in particular, sheds light on the evaluation of whether the BOC has complied with the 14-point competitive checklist in that state. For instance, the Applicants provide an example of DOJ's comparison of the performance of Ameritech in Michigan with BellSouth in Louisiana in terms of the number of unbundled loops that had been provisioned at the time the BOC filed its section 271 application. *See* SBC/Ameritech May 25 Supplemental Memo at 14, n.49. They also point out DOJ's consideration of the OSS testing methodology for Bell Atlantic in New York as superior to BellSouth's Louisiana consultant's methodology. *Id.* In addition to DOJ, this Commission has found comparisons among BOC practices, as reflected in their section 271 applications, to be useful in determining whether a BOC has met the section 271 statutory requirements. *See also Application of BellSouth Corporation, et al. Pursuant to Section 271 of the Communications Act of 1934, as amended, To Provide In-Region, interLATA Services In South Carolina*, CC Docket No. 97-208, Memorandum Opinion and Order, FCC 97-418, 13 FCC Rcd 539, 599-600 (1997), at para. 108 (stating, in contrast to BellSouth's failure to provide substantiation of its conclusion that the causes of high order errors in its South Carolina section 271 application were due to competing carriers' mistakes, that Ameritech did provide such information in its Michigan application); *id.*, 13 FCC Rcd at 606, para. 121 (doubting that any technical obstacle would prevent BellSouth from providing electronic error notification and noting that "at least one other BOC, Ameritech, does provide electronic notification of error messages through an EDI interface.") (*citing Ameritech Michigan Order*, 12 FCC Rcd at 20642, para. 186)).

[298] *See Application of Ameritech Michigan Pursuant to Section 271 of the Communications Act of 1934, as amended, To Provide In-Region, InterLATA Services in Michigan*, CC Docket No. 97-137, Memorandum Opinion and Order, 12 FCC Rcd 20543 (1997), at para. 2.

[299] *Compare* Deployment of Wireline Services Offering Advanced Telecommunications Capability, Comments of Ameritech (filed Sept. 25, 1998), at 3 ("Ameritech agrees with the Commission's proposal as a component in a framework for interLATA relief."); Reply Comments of Ameritech (filed Oct. 16, 1998), at 1 ("The collaborative effort between Ameritech and Northpoint stands in sharp contrast to the usual adversarial posturing offered by most other commenters."); at 6 ("Beyond some minor modifications . . . no further changes to the separation requirements are warranted.") *with* Comments of SBC Communications Inc. (filed Sept. 25, 1998), at 2 ("Unfortunately, as currently proposed, the '272-like' structure for an advanced services affiliate . . . would appear to have too many inefficiencies, restrictions, and unknowns to provide an expected return commensurate with the risks of deploying the significant investment associated with advanced services."). *See also* Comm. Daily, Vol. 18, Iss. 152, Aug. 7, 1998 (Following Commission's release of *Advanced Services Order and NPRM*, "SBC, U S West and other incumbent phone companies immediately issued statements decrying requirement that they form separate subsidiaries in order to get deregulation."); Communications Today, Dec. 8, 1998, 1998 WL 23367826 (discussing

150. Ameritech also departed from the position taken by the other RBOCs and GTE in the *Number Portability* proceeding where the other major incumbents urged the Commission to allow incumbents to use the Query on Release (QOR) method rather than the Location Routing Number (LRN) method.[300] In concluding, contrary to the other RBOCs' assertions, that QOR offered no long-term cost savings relative to LRN, the Commission specifically noted Ameritech's support of LRN by emphasizing that "at least one incumbent LEC, Ameritech, has already decided that it is beneficial to deploy LRN from the outset."[301] Accordingly, the proposed acquisition of Ameritech by SBC would eliminate an important source of innovation and a major independent voice that has assisted regulators and competitors in implementing the 1996 Act's market-opening provisions.

b) Loss of Independence of Operating Companies

151. We find that, although the actual number of operating companies may not diminish following the merger of SBC and Ameritech, the combined entity will have greater incentive to unify the practices of these companies, resulting in an overall loss of independence at the operating-company level. Although we agree with the Applicants that, by requiring data to be provided on an operating-company or study-area level, this Commission and state authorities could retain the same number of data points and limit the Applicants' abilities to aggregate data following the merger,[302] we find that collection of operating-company specific or study-area specific data would be useless for benchmarking purposes if all the local companies follow a uniform policy set by the holding company. In that case, the result would be a reduction in the number of independent approaches, this time at the operating company level.

152. The operating companies involved in the instant merger are aligned with two distinct holding companies, each having a distinct top-level management philosophy. Each holding company also has adopted, or required of its operating companies, different policies and practices, particularly in negotiating interconnection agreements, which represent a certain level of autonomy.[303] Accordingly, in order to accept the Applicants' argument that the merger would not reduce the number of independent points of observation, we also would have to assume that the merger would have no effect on the likelihood that the local operating companies would

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petition by several incumbent LECs, including SBC, BellSouth, Bell Atlantic, GTE and U S WEST, for Commission to reduce requirements on incumbents' provision of DSL, and commenting that "[n]otable by its absence was Ameritech, which is the only Bell operating company (BOC) that thinks it will be possible to offer DSL service under the conditions currently under consideration by the FCC.").

300 *See Telephone Number Portability*, CC Docket No. 95-116, First Memorandum Opinion and Order on Reconsideration, 12 FCC Rcd 7236 (1997)(*Number Portability Order*).

301 *Id.* at 7257-58, para. 38.

302 SBC/Ameritech Nov. 16 Reply Comments at 56-57 (stating that "[a]fter the merger, each of the nine SBC and Ameritech operating companies will report all the same information to the same regulators as they do now.").

303 For example, we alluded earlier to Ameritech's acceptance of a separate subsidiary proposal for advanced services, which conflicted with the position taken by SBC. *See* Section V.C.4.a) (Loss of Ameritech as Independent Holding Company).

adopt independent approaches that differ from one another. Logic and evidence both point to the contrary. Post-merger, because of its larger size, the merged firm would be affected more than either company standing alone if regulators and/or competitors use best-practices benchmarking to force the firm to adopt throughout its region a market-opening measure adopted independently by one of its operating companies. Accordingly, following its acquisition of Ameritech's five operating companies, SBC will have a greater incentive to ensure that all thirteen of its local operating companies' policies are consistent.

153. The merged firm also will have a greater incentive to coordinate decisions made at the local operating company level in order to affect the outcome of average-practices benchmarking. The merger of SBC and Ameritech would create the largest incumbent LEC controlling approximately one-third of access lines nationwide. Because the merged firm would be disproportionately large compared to other incumbent LECs, the aggregate data reported by it would have a direct impact on the industry's average benchmarks. The merged firm thus would have both the capability and incentive to skew its decisions in order to affect the average benchmark strategically. Moreover, the merged firm's size could cause it to dominate the standards-setting process and establish *de facto* standards that advantage itself and disadvantage potential competitors or consumers. The proposed merger thus seriously would undermine the value of average-practices benchmarking among incumbent LECs.

154. SBC effectively admits that it will impose greater uniformity in policies toward competitive LECs following consummation of its merger with Ameritech. For example, Sandy Kinney, President of SBC's wholesale operations and John Starkey, Vice President of Sales for SBC, stated that SBC's policy is to adopt its "best practices" company-wide.[304] Ms. Kinney and Mr. Starkey also confirmed that, although SBC must file separate interconnection contracts in each state, SBC generally negotiates with competitive LECs on a region-wide basis, unless competitive LECs request state-by-state negotiation, and then modifies the standard agreement for specific states only as necessary to comply with any differing state rules.[305] SBC's representatives also stated that the performance measures that it will adhere to as a result of the section 271 collaborative process in California are a subset of those to which it is bound in the Texas section 271 process.[306] The Applicants' statements that the merger will eliminate overlapping functions and spread the adoption of best practices throughout the holding company, detailed below in our analysis of the merger's claimed public benefits, provide further evidence

[304] Remarks of Sandy Kinney, SBC President of Industry Markets, and John Starkey, SBC Vice-President of Sales, Truong Memo.

[305] *Id.* The SBC employees assigned to deal with the provision of wholesale services to competitive LECs and interexchange carriers are not assigned to state-specific operating companies, but rather to specific SBC regions or SBC headquarters.

[306] *Id.* SBC's representatives explained that, because the same parties generally are involved, there is a high level of cross-referencing between the various state proceedings that results in similar performance measures being adopted in different states within SBC's region, with some variation due to state public utility commissions' preferences.

that the various operating units' policies and operations will become more uniform post-merger.[307]

155. Even if the merged firm were to continue reporting data at the operating company level, therefore, indications from SBC, as well as logic and experience, suggest that a merger of SBC and Ameritech would likely lead to more uniform policies being adopted at the operating company level throughout the combined entity's region, again resulting in fewer independent points of observation for regulators and competitors.

c) Increased Risk of Coordination Among Remaining Major Incumbent LECs

156. The proposed merger, by reducing to five the number of major incumbent LECs, also would increase the incentive and ability of the remaining incumbents to coordinate their behavior, either explicitly or implicitly, to impede benchmarking and resist market-opening measures. As an initial matter, by merging Ameritech into SBC, the merger reduces by one the number of independent holding companies whose behavior must be coordinated, which simplifies the process of coordination. Coordination requires that the incentives of all parties are aligned, and reducing the number of companies reduces the number of incentives that must be aligned.

157. Reducing the number of firms also increases each firm's incentive to coordinate its behavior to undermine regulatory processes. As we have mentioned, SBC will grow larger as a result of the merger, and therefore stands to sustain a larger loss as the result of any comparative practices analysis that constrains its behavior. This gives the merged firm greater incentive to enter into tacit agreement with the remaining firms to convey minimal information to regulators and/or competitors and to eliminate outlying policies and practices that could become industry benchmarks. Moreover, the merger will create a demonstrably large incumbent LEC that can act as an industry leader for collusive purposes.

158. As a result of Ameritech's merger with SBC, the other major incumbent LECs also will have more incentive to cooperate in attempts to impede comparative practices analysis. Cooperative ventures, either explicit or implicit, involve the risk that one or more parties will deviate from the cooperative behavior, thereby spoiling the venture. With the cooperation of fewer firms necessary, the merger reduces the risk that a venture will fail, which translates into a lower risk for each firm from participating in the venture. This reduction in risk increases a firm's incentive to cooperate. By reducing the number of major incumbent LEC benchmark firms to five, with each firm facing more incentive to cooperate and little unilateral incentive to break an agreement to impede benchmarking,[308] the proposed merger will facilitate any attempts,

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[307] *See* Section VI (Analysis of Potential Public Interest Benefits).

[308] *See supra* at Section V.C.2.c)(Effect at Industry Level) (contrasting a firm's unilateral incentive to cheat on a pricing agreement with less incentive for it to break an agreement to conceal information to impede regulators' and competitors' benchmarking efforts).

especially implicit attempts, to coordinate behavior to conceal forms of competitive deterrence from regulators and competitors. The merger of SBC and Ameritech therefore increases the incentive and abilities of the merged firm and other incumbent LECs to cooperate in becoming less effective benchmarks for regulators and competitors seeking to promote competitive entry and rapid deployment of advanced services.

5. Continued Need for Major Incumbent LEC Benchmarks

159. We reject the Applicants' arguments that smaller incumbent LECs and competitive LECs provide adequate benchmark alternatives to the major incumbent LECs,[309] and that parity requirements make the incumbent LEC's dealings with itself the only relevant benchmarks in a post-1996 Act era.[310] As discussed below, we find, to the contrary, that benchmarking among the large incumbent LECs will continue to be a crucial market-opening tool as regulators and competitors carry out the objectives of the 1996 Act.

160. Comparative practices analyses are effective only when the firms under observation are similarly situated, including the size of the firms relative to the size of the market. With comparable firms – *e.g.*, in their customer base, access to capital, network configuration, and the volume and type of demands from competitors – regulators and competitors can establish more effectively that approaches and rates adopted by one incumbent would be equally feasible for other incumbents. Significant variation between the major incumbent LECs and the other carriers cited by the Applicants preclude the use of the latter categories as alternative benchmarks in evaluating the major incumbent's LECs' compliance with their statutory obligations.

161. We agree with the broad principle that the methods of comparison may evolve over the course of the transition to full competition in local markets.[311] For instance, it may turn out, as Applicants assert, that the importance of benchmarking access charge rates will decline as interexchange carriers reach customers through more competitive LECs rather than incumbent LECs.[312] Nonetheless, as explained above, we find an acute present need for benchmarking to, among other tasks, facilitate implementation of the market-opening measures of the 1996 Act and promote the rapid deployment of advanced services. For these types of comparisons, we predict that the high percentage of access lines nationwide controlled by the RBOCs and GTE will keep them at the forefront in establishing benchmark rates, terms and conditions for an extended future period.

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309 *See* SBC/Ameritech Nov. 16 Reply Comments at 53-54, 60. *See also id.*, Schmalansee and Taylor Reply Aff. at 27-29.

310 *See* SBC/Ameritech Nov. 16 Reply Comments at 57, 62. *See also id.*, Schmalansee and Taylor Reply Aff. at 31; SBC/Ameritech Mar. 25 Supplemental Memo at 2.

311 *See* SBC/Ameritech Nov. 16 Reply Comments at 62 (stating that "the vast majority of the benchmarks being developed under section 251 are best practices or parity benchmarks, not industry averages.").

312 *See* SBC/Ameritech Nov. 16 Reply Comments at 62; SBC/Ameritech Mar. 25 Supplemental Memo at 20.

a) Inadequacy of Other Firms As Benchmarks Against Major Incumbent LECs

162. We reject the Applicants' contention that other types of firms serve as adequate benchmarks to the major incumbent LECs.[313] We are not persuaded that the presence of small incumbent LECs and/or competitive LECs eliminate the need for regulators and competitors to make direct comparisons among the RBOCs and GTE.[314] The Applicants' arguments ignore vital differences in the 1996 Act's treatment of large incumbent LECs, the RBOCs in particular, as compared with other incumbents and competitive carriers. Equally important, structural and operational differences between these carriers and the major incumbent LECs also make direct comparisons between them inappropriate.

(1) Differences in Regulatory Treatment

163. We conclude that the distinct obligations imposed on major incumbent LECs, as compared with other LECs, under the 1996 Act undermines the abilities of regulators and competitors to draw useful comparisons between the conduct of the major incumbent LECs and these other carriers. In short, small incumbent LECs and competitive LECs cannot qualify as adequate alternatives to the RBOCs and GTE as benchmarks for implementation of sections 251(c) and 271, the core market-opening provisions of the 1996 Act.

164. The Applicants fail to explain how smaller incumbent LECs or competitive LECs could substitute for other RBOCs in assessing compliance with certain prominent provisions of the 1996 Act that apply solely to the RBOCs. The ability to compare the RBOCs' policies and practices in areas such as OSS performance, unbundling, and interconnection arrangements, for example, is a practical tool for regulators, competitors and DOJ in determining a BOC's compliance with section 271, or in monitoring to prevent potential backsliding.[315] Similarly, analyzing the structure of other LECs not subject to a statutory separate affiliate requirement for manufacturing activities, or for the provision of in-region interLATA telecommunications services and interLATA information services, will not aid regulators or competitors in assessing

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[313] The Applicants repeatedly assert the notion that there is "a growing body of ILEC and CLEC market experience that will be available for FCC reference if necessary." SBC/Ameritech Mar. 25 Supplemental Memo at 18. *See also* SBC/Ameritech Nov. 16 Reply Comments, Schmalansee and Taylor Aff. at 30. Specifically, the Applicants claim that adequate alternative benchmarks can be found in small incumbent LECs (such as Sprint's operating subsidiaries, ALLTEL, Frontier and Cincinnati Bell) and multi-state competitive LECs (such as Focal, Hyperion, ITC, MGC, and RCN). *See* SBC/Ameritech Nov. 16 Reply Comments at 58.

[314] We also are not prepared to take the novel step in this proceeding of treating foreign carriers as adequate benchmarks for the large incumbent LECs operating in the United States. To establish such a showing, we would have to find, at minimum, that a country's regulatory regime is comparable to our system, notably the 1996 Act's unbundling requirements and pro-competitive framework, and that the regime, as well as the relevant LEC's practices and agreements, is sufficiently transparent to yield adequate benchmarking information for use by this Commission, state commissions and competitors in implementing the Communications Act. Any such showing would be undermined if the foreign LEC faced different operational demands and employed different network architectures from the RBOCs and GTE.

[315] *See supra* n. 297.

an RBOC's compliance with section 272. At a minimum, therefore, both regulators and competitors have a strong continuing need for separate comparative practices analyses among several RBOCs in order to ensure compliance with RBOC-specific provisions of the 1996 Act.

165. Equally important, we find a pivotal distinction between the section 251 obligations imposed on the major incumbent LECs versus those of rural incumbents or competitive LECs. In contrast to the major incumbent LECs that are subject to section 251(c)'s market-opening requirements,[316] many of the alternate carriers cited by the Applicants are not subject to full section 251(c) obligations. First, by definition, competitive LECs do not fall within the 1996 Act's definition of an "incumbent local exchange carrier" for the given service area, nor do such carriers own the operative facilities for which interconnection and access is sought.[317] Instead, competitive LECs are subject to the lesser requirements of section 251(b) that are applicable to all LECs.[318]

166. Second, many of the smaller incumbent LECs fall within section 251(f)'s exemption from certain section 251(c) obligations for rural carriers.[319] In the *SBC/SNET Order*, for instance, we concluded that the proposed merger was not likely to affect the public interest adversely in part because SBC and SNET were not comparable in size. The Commission noted that "SNET is substantially smaller than the 'first tier' LECs -- the BOCs and GTE -- and has long been subject to different regulatory treatment."[320] Here, both SBC and Ameritech are among the largest incumbent LECs, and those that formerly comprised the Bell System, and thus are subject to the statutory obligations suitable to those entities. We therefore find that regulators and competitors are restricted largely to the class of large incumbent LECs, principally the RBOCs and GTE, in making benchmark comparisons under section 251(c).[321]

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316 *See* 47 U.S.C. § 251(c) (requiring incumbent LECs to negotiate in good faith and provide, *e.g.*, interconnection, unbundled access to network elements, resale, and collocation).

317 *See* 47 U.S.C. § 251(h).

318 47 U.S.C. § 251(b) (requiring all LECs to allow resale, number portability, dialing parity, access to rights of way, and reciprocal compensation).

319 Under section 251(f), rural incumbent LECs are exempt from the requirements of section 251(c) until (i) it has received a "bona fide request for interconnection, services, or network elements," and (ii) the state commission determines that "such request is not unduly economically burdensome, is technically feasible, and is consistent with section 254" universal service provisions. 47 U.S.C. § 251(f). *See* State Attorney Generals Apr. 27 *Ex Parte*, Rosston and Mercurio Rept. at 26.

320 *SBC/SNET Order*, 13 FCC Rcd at 21302, para. 21 (*citing Policy and Rules Concerning Rates for Dominant Carriers*, CC Docket No. 87-313, Second Report and Order, 5 FCC Rcd 6786, 6818-20 (1990); 47 U.S.C. § 251(f)(2)).

321 Not surprisingly, therefore, certain reporting requirements apply solely to the large incumbent LECs. *See* State Attorney Generals Apr. 27 *Ex Parte*, Rosston and Mercurio Rept. at 26 (noting that ARMIS reporting requirements differentiate between Tier I and Tier II incumbent LECs, and that the X-factor is determined based on large incumbent LECs' data). The current difference in treatment between the large and the small incumbent LECs reflects a policy determination regarding the greater importance of the major incumbent LECs as benchmarks. We believe it inappropriate to impose additional reporting burdens on small incumbents in order to facilitate a large incumbent LEC's consolidation to even greater size.

(2) Differences in Structure and Operation

167. We also find that crucial distinctions in structure and operation undermine the value of using smaller incumbents and competitors as benchmarks for the RBOCs and GTE.

168. *Small Incumbent LECs.* We find that, because their service areas include fewer large metropolitan areas and thus tend to be subject to less competitive entry and less demand for budding advanced services, smaller incumbent LECs are not likely to provide useful benchmarks for measuring the market-opening performance of major incumbent LECs. In contrast to the smaller incumbents, the major incumbents tend to operate in markets characterized by high population density or a large number of business lines, which generally are more attractive to new entrants. The level of competitive activity in a given area can implicate the network architecture or capability required of certain incumbent facilities such as OSS and physical collocation. A small incumbent facing little demand for interconnection, collocation or facilities for advanced services is less likely to have traffic levels or performance measurements that would render meaningful comparisons with a large incumbent who must employ more sophisticated management systems to meet greater demand. Moreover, different market structures may result in different network configurations that limit the usefulness of comparisons. For example, the loop costs of an RBOC may not be comparable to those of a small rural incumbent LEC with longer average loops or less densely concentrated customers.

169. Furthermore, by arguing that large size enables an incumbent LEC to achieve economies of scale, upgrade its network and provide more advanced services than smaller incumbent LECs,[322] the Applicants imply that the less developed networks and higher costs of smaller incumbent LECs would make them inappropriate benchmarks for the large incumbent LECs. As detailed in Section V.D. (Increased Discrimination) below, the large footprints of the major incumbent LECs may offer these carriers greater opportunities to engage in anticompetitive behavior that would be difficult to detect using comparisons to smaller incumbents. Finally, in average-practices benchmarking, no small incumbent LEC could provide an adequate counterpoint to the combined entity's control of one-third of the nation's access lines.

170. *Competitive LECs.* We are not persuaded that competitive LECs presently stand as adequate firms with which to compare the market-opening performance of incumbents. The Applicants' suggestion that competitive LECs, whether or not facilities-based, can be used as suitable benchmarks for the large incumbent LECs[323] defies the logic and structure of the 1996 Act. As discussed above, a primary motivation behind benchmarking is to increase the level of information regarding the incumbents' networks for competitors seeking access to those facilities, as well as for regulators. Moreover, competitive LECs are pursuing numerous

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322 *See* SBC/Ameritech July 24 Application, Description of the Transaction, at 1-2, 4-8, 11-12, 38-46, 52-55; Section VI (Analysis of Potential Public Interest Benefits).

323 *See* SBC/Ameritech Mar. 25 Supplemental Memo at 13.

strategies using a variety of wireline and wireless technologies, and their limited facilities are far from comparable to the millions of local lines controlled by the RBOCs and GTE.[324]

171. Despite arguing that competitive LECs can serve as interconnection benchmarks by providing wholesale service to other competitive LECs,[325] the Applicants provide no evidence demonstrating that competitive LECs actually are serving as wholesale suppliers in such a way as to generate useful comparisons for incumbent performance. Moreover, even if some competitive LECs decide to act as wholesalers, their incentives are likely to differ considerably from those of the incumbents. These new entrants' strategies are directed at expanding their reach and filling their vacant capacity, whereas incumbent LECs are likely to focus first on protecting their customer base from erosion by competitors. Competitive LECs which are voluntarily and eagerly opening their networks to other carriers cannot provide useful benchmarking information for the detection of incumbents' subtle forms of resistance to market-opening measures.

172. We also reject the Applicants' assertion that sections 251 and 252 of the 1996 Act increase the information flow to competitors sufficiently to eliminate the need for comparative practices analyses.[326] By asserting that the publication of interconnection agreements supplants the need for benchmarking,[327] the Applicants brush past the complementary nature of the publication requirement and comparative practices analyses. The publication of interconnection agreements assists competitive LECs in making benchmark comparisons, not only as between what one particular incumbent LEC offers to different competitors but also as among the general practices of several different incumbents. By increasing the flow of information to competitors and regulators, sections 252(h) and 252(i) facilitate the ability of competitors and regulators to engage in active benchmarking among the incumbents. Thus, the entire section 251 process benefits from having more rather than fewer large incumbent LECs to provide a diversity of approaches in negotiating interconnection agreements.

173. All of the foregoing factors suggest that comparisons between a major incumbent LEC and a small incumbent or a competitive LEC are less likely to yield the kind of benefits that would flow from comparisons among the RBOCs and GTE. In this regard, we note that the Applicants fail to provide examples where a regulator or competitor has relied on the

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324 *See* SBC/Ameritech Nov. 16 Reply Comments, Schmalansee and Taylor Reply Aff. at 29 (observing that new entrants in local markets "are frequently very different from ILECs; they use different technologies and different back-office systems, provide different mixes of services, etc.").

325 *See* SBC/Ameritech Nov. 16 Reply Comments at 60.

326 SBC/Ameritech Nov. 16 Reply Comments at 54-55, 58-59. *See also id.*, Schmalensee and Taylor Decl. at 30-32. The Applicants argue that section 252(h)'s requirement that interconnection agreements be signed by state regulators and made available for public inspection adds to the information available to competitive LECs and regulators, and that section 252(i)'s most-favored nation provision assures that competitive LECs can make use of their increased information by requiring incumbent LECs to make "available any interconnection service or network element supplied in any agreement approved under section 252 to any other telecommunications carrier under the same terms and conditions." *See* 47 U.S.C. § 252(h), (i).

327 *See* SBC/Ameritech Nov. 16 Reply Comments at 54-55; SBC/Ameritech Mar. 25 Supplemental Memo at 13, 18-19.

performance of these claimed benchmark alternatives as adequate benchmarks against an RBOC or GTE. We therefore reiterate our conclusion that the large incumbent LECs, because they are of similar size and face relatively similar market conditions, remain the principal sources of benchmarks for their own behavior.

b) Inadequacy of Parity Requirements

174. We are also unpersuaded by the Applicants' argument that maintaining a large number of major incumbent LECs as benchmarks is no longer necessary because, as they assert, rather than comparisons among major incumbent LECs, the relevant benchmarks during the transition to competitive local markets are parity comparisons focusing on how an incumbent LEC treats competitive LECs vis-à-vis itself.[328] According to the Applicants, "performance measures designed to compare the access and interconnection the Bell Operating Companies provide to CLECs on a state-by-state basis with that provided to their own retail operations have become the new 'benchmarks.'"[329]

175. We certainly agree with the notion that an incumbent LEC's treatment of its retail operations or its affiliates as compared with its treatment of competitors can provide useful benchmarks for regulators and competitors. In certain contexts, such as detecting discriminatory behavior in interconnection, provisioning, and maintenance, parity comparisons provide a useful, and minimally-intrusive, way to obtain information regarding an incumbent's performance.[330] As Sprint observes, however, implementation of a parity rule itself may require traditional benchmarking between major incumbent LECs[331] -- *e.g.*, in setting mutually acceptable performance standards to determine if an incumbent LEC has complied sufficiently with the parity requirement.

176. While we agree that parity rules are valuable, we nonetheless find that parity considerations cannot substitute for all forms of benchmarking. Parity rules will not serve the public and protect competition if, for example, an incumbent LEC deems it profitable to provide lackluster service or charge excessive rates to both its own retail affiliates and its competitors. For example, without discriminating, the incumbent LEC may profit from imposing high loop charges, or access charges, on both its affiliates and its competitors, because the charges to its affiliates constitute only an internal transfer. While parity requirements attempt to level the

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328 SBC/Ameritech Mar. 25 Supplemental Memo at 2, 13. *See also* SBC/Ameritech Nov. 16 Reply Comments at 57 (contending that in many instances "the only necessary benchmark is supplied by the incumbent LEC itself: the dispositive regulatory issue is whether an incumbent LEC is treating competitors differently from itself.").

329 SBC/Ameritech Mar. 25 Supplemental Memo at 13.

330 *See, e.g.*, *Local Competition Order*, 11 FCC Rcd at 15614, para. 224 (Section 251(c)(2)(C) requires an incumbent LEC to provide interconnection between its network and that of a requesting carrier at a level of quality that is at least indistinguishable from that which the incumbent provides itself or any other party). *See Performance Measurements and Reporting Requirements for Operations Support Systems, Interconnection, and Operator Services and Directory Assistance*, Notice of Proposed Rulemaking, 13 FCC Rcd. 12817 (1998), at para. 14.

331 Sprint Apr. 12 *Ex Parte*, Farrell and Mitchell, *Response to Some Criticisms of Benchmarking Analysis*, at 3.

playing field, therefore, traditional comparative practices analyses remain necessary to ensure that this level does not sink below an acceptable standard.

177. For innovative entrants, in particular, parity rules will not always suffice. As Sprint notes, if the innovation requires a new form of interconnection or access, "[t]he incumbent can slow-roll the innovator, declining to provide the new kind of input, until the incumbent has a similar or leapfrogging innovation available."[332] As discussed further in Section V.D.2.a) (Advanced Services) below, if a competitive LEC seeks the provision of properly conditioned loops in order to provide xDSL service, an incumbent LEC which is not ready to provide xDSL service itself would have the incentive to deny this competitor the properly conditioned loops. In this circumstance, parity rules would provide no remedy for the competitive LEC, for the incumbent LEC would not be providing to its retail arm anything that it was denying its competitor. Exclusive reliance on parity rules, therefore, could slow the provision of innovative services to the public.

178. For the foregoing reasons, we conclude that parity rules complement, but do not supplant, the use of traditional comparative practices analyses by regulators and competitors. Indeed, if parity alone mattered, as the Applicants' analysis suggests, then all the remaining RBOCs would be permitted to merge into one entity, leaving regulators and competitors unable to compare distinct practices of several independently-owned firms.

c) Sufficiency of Remaining RBOC Benchmarks

179. Finally, we reject the Applicants' argument that because benchmarking requires only one firm to "break ranks" with others, the proposed merger will not impair benchmarking by eliminating the only remaining benchmark.[333] In other words, the Applicants have stated that the "benchmarking issue thus has been narrowed . . . to the question of whether the 'loss' of Ameritech as an independently owned RBOC would so affect the Commissions ability to determine whether a proposed practice is technically feasible as to outweigh the benefits presented by the merger."[334] They go on to argue that there are no examples of this Commission using only a single RBOC-to-RBOC comparison as a benchmark.[335] Thus, according to the Applicants, the loss of one RBOC would not have changed the outcome of any benchmarking analysis because other firms, or the BOCs, could still be used as benchmarks for assessing technical feasibility. We disagree and find, to the contrary, that the merger would result in dangerously few RBOC and major incumbent LEC benchmarks.

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332 *Id.*

333 *See* SBC/Ameritech Mar. 25 Supplemental Memo at 24 (finding no evidence "that preserving the current number of independently owned RBOCs is material to the regulatory process, particularly on issues raised by the transition to competition.").

334 SBC/Ameritech Mar. 25 Supplemental Memo at 4.

335 *Id.* at 9-12, App. 1.

180. The Applicants' assertion that the Commission's analysis has never turned solely on RBOC-to-RBOC comparisons, or on an RBOC outlier, disregards not only the examples of the Commission's use of comparative practices analysis cited above, but also SBC's and Ameritech's prior recognition and support of Commission benchmarking among the RBOCs.[336] More importantly, we reject the Applicants' implied presumption that reducing the number of independently-owned RBOCs could be harmful only if the Commission in its decision relies solely on an RBOC-to-RBOC comparison. Analyzing the practices of the large incumbent LECs, the RBOCs included, may reveal trends within the industry or other qualitative factors that, although not determinative, may heavily influence the Commission's reasoning. The Commission's regulatory processes are cumulative, and rarely rely solely upon any one rationale for action.

181. With technical feasibility concerns, in particular, the loss of one source of observation could in fact eliminate the single observation that would have proven a particular arrangement feasible.[337] This is especially true in making assessments regarding advanced services, where the major incumbent LEC benchmark firms have taken different strategies, or are in different stages, in terms of their own deployment or cooperation with others. Furthermore, as shown above, there are examples in which a single firm used as a benchmark.[338] Thus, reducing the number of potential benchmark firms increases the chance that regulators and competitors will lose the ability to observe the decisive benchmark.

182. More importantly, we disagree with the Applicants' assertion that the issue has been narrowed to the question of whether a proposed practice is technically feasible.[339] As we have stated above, aside from determining the simple feasibility of a proposed activity, benchmarking can be used to help determine the cost of a specific service, estimate the future cost of providing new services, or decide which out of a number of services is the most cost effective. In each of these cases, more independent observations will yield more useful information and improve the decisions of the regulator. To the extent that the mergers reduces the level of observation, this process is impaired. For example, finding that several major incumbent LECs can provide a service at a particular cost and level of quality will be more valuable than finding that only one major incumbent LEC can do so. With new services and

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336 *See supra* at Section V.C.3.a)(Comparative Practices Analysis under the Modified Final Judgement). We note that in 1987, Ameritech submitted to the MFJ Court a compilation of benchmark comparisons containing twelve pages of examples of the "Use of Benchmark Comparisons by the Federal Communications Commission." *See United States v. Western Elec. Co.*, Civil Action No. 82-0192, Ameritech Comments on the Report and Recommendations of the United States Concerning the Line-of-Business Restrictions, Att. A at 16-27 (filed Mar. 13, 1987). To take but one example, Ameritech states that the Commission in its *Third Computer Inquiry* proceeding considered Ameritech's proposal to introduce a new network architecture, Feature Node/Service Interface, "as an indication that an architecture with highly efficient interconnection can be designed." *Id.* (*citing Amendment of Section 64.702 of the Commission's Rules and Regulations*, 104 FCC 2d 958, 1063-64 (1986), at para. 212). It is not clear what action the Commission might have taken, such as requiring more detailed information from incumbents, or when it might have reached a similar conclusion, had it not examined Ameritech's proposal.

337 *See* State Attorneys General Apr. 27 *Ex Parte* Rosston and Mercurio Rept. at 22.

338 *See infra* at Section V.C.3.b) (The Commission's Use of Comparative Practices Analyses).

339 SBC/Ameritech Mar. 25 Supplemental Memo at 4.

technologies, reaching appropriate decisions will likely involve making predictive judgments regarding the costs and future demand for the innovative service or technology. Although it is impossible for regulators to predict the value of these variables with certainty, having more rather than fewer independent estimates of such values will yield more useful information.[340]

183. Although we do not view the instant merger's reduction of the number of major incumbent LECs (the RBOCs and GTE) from six to five to be an automatic trigger of benchmarking harms, we cautioned in the *Bell Atlantic/NYNEX Order* that these harms increase disproportionately with each additional decline in the number of major incumbent LECs.[341] As explained above, along with further restricting diversity, each successive reduction in benchmark firms materially increases the risk that the remaining firms could successfully coordinate behavior, implicitly or explicitly, to reduce the effectiveness of comparative practices analyses. With only five remaining benchmark firms, this risk is far greater than with six.[342]

6. Conclusion

184. We conclude that, by further reducing the number of separately-owned large incumbent LECs, the proposed merger of SBC and Ameritech would significantly harm the ability of regulators and competitors to rely on comparative practices analyses to carry out their obligations under the Communications Act. In particular, the proposed merger of SBC and Ameritech poses a significant potential harm to the public interest by: (1) removing a source of potential diversity from independent major incumbent LECs during the transition to competition; (2) creating an incentive for the combined firm to coordinate behavior at the operating company level, thereby reducing other potential sources of innovation; and (3) increasing the incentive and opportunity for collusion and concealment of information among the few remaining major incumbent LECs. All of these occurrences lead to an overall reduction in diverse policies, practices and approaches that otherwise could have been used to implement the Communications Act most effectively, particularly in overseeing the transition to competitive local markets. As a result, the Commission would have to substitute more intrusive regulation to enforce the Communications Act, representing a less effective and more costly solution for both the regulated firms and the public. Only firms comfortable with a monopolistic environment would welcome such results.

185. As noted above, in allowing the Bell Atlantic/NYNEX merger, we expressly cautioned that further consolidation among the RBOCs or comparable incumbent LECs would present serious public interest concerns.[343] Because the harm to regulators' and competitors' ability to use benchmarking to implement and enforce the Communications Act is greater as the

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340 For example, in choosing whether to require LRN or allow the interim use of QOR, the Commission estimated the speed at which numbers would be ported and the relative costs of rolling out the two different technologies, along with estimates of the benefit and technical shortcomings of each. *Number Portability Order*, 12 FCC Rcd at 7257-58, para. 38.

341 *Bell Atlantic/NYNEX Order*, 12 FCC Rcd at 20062-63, para. 156.

342 *See infra* at n. 240.

343 *Bell Atlantic/NYNEX Order*, 12 FCC Rcd at 20062-63, para. 156.

number of independent large incumbent LECs decreases, the Applicants must prove countervailing public interest benefits of this merger significantly exceeding those from previous incumbent LEC mergers in order to demonstrate that this merger, on balance, serves the public interest. Alternatively, we need to fashion very substantial market-opening, benchmarking conditions to alleviate the grave harms this merger poses to the regulatory processes and the operation of the 1996 Act's interconnection requirements.

D. Increased Discrimination

1. Overview

186. In the preceding section, we explained why this merger, as initially proposed, would seriously weaken oversight of the Applicants' behavior toward competitors. In this section, we explain why we also believe that this merger will increase predation while weakening our ability to combat it. We conclude that incumbent LECs, such as SBC and Ameritech, have the incentive and ability to discriminate against competitors in the provision of advanced services,[344] interexchange services, and circuit-switched local exchange services,[345] and that such incentive and ability will increase as a result of the merger. This increased incentive to discriminate will result in a public interest harm, because it will adversely affect national competitors' provision of services in the new, combined region, and, as a further result, will harm consumers who ultimately will be forced to pay more for retail services, with reduced quality and choice.

187. We believe the merger is likely to have particularly harmful, discriminatory effects on competition in the provision of new types of advanced services. Telecommunications markets today exhibit a continuing shift from a circuit-switched to a packet-switched environment capable of allowing the provision of a variety of new, advanced services.[346] Any discrimination against non-incumbent competitors who use these advanced packet-switched

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[344] For purposes of this order, we define the term "advanced services" as we did in the *Advanced Services Further Notice*, to mean "high speed, switched, broadband, wireline telecommunications capability that enables users to originate and receive high-quality voice, data, graphics or video telecommunications using any technology." *Advanced Services Further Notice*, 14 FCC Rcd at 4762, n.2. The Commission there stated: "[t]he term 'broadband' is generally used to convey sufficient capacity -- or 'bandwidth' -- to transport large amounts of information. As technology evolves, the concept of 'broadband' will evolve with it: we may consider today's 'broadband' services to be 'narrowband' services when tomorrow's technologies appear." *Id.* For a further description of xDSL technology, *see id.* at paras. 9-12.

[345] Throughout this section, "local exchange service," refers to circuit-switched local exchange service, otherwise known as Plain Old Telephone Service (POTS), rather than services, such as advanced services, based on digital subscriber line technology or packet-switched technology that may have a local component.

[346] A packet-switched network is one that transmits information by breaking it into small packets that are independently routed through the network from source to destination according to a destination address that is included in each packet. Packet switching differs from the circuit switching used in Plain Old Telephone Service (POTS): in a circuit-switched network, a dedicated circuit between the parties is established and reserved for the exclusive use of those parties. *See* Harry Newton, *Newton's Telecom Dictionary* (Flatiron Publishing, 14th ed. 1998) at 527.