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FEDERAL COMMUNICATIONS COMMISSION
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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of the Local Competition Provisions of the Telecommunications Act of 1996	)))	CC Docket 96-98

AT&T CORP. REPLY

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Summary

The Commission may not accede to the incumbent LECs' baseless requests for use restrictions on unbundled network elements. As before, the incumbents' legal arguments fail to support their claim that the Commission has the authority to impose such restrictions. Indeed, doing so would run directly counter to the clear text of the 1996 Act and the Commission's own decisions implementing the Act. The Commission has already concluded that Section 251(c)(3)'s prohibition of use restrictions is "not ambiguous," and that "there is no statutory basis" on which a different conclusion could defended. Thus, all of the incumbent LECs' arguments to the contrary are clearly wrong. (*See* Part I below)

Nor may the Commission take the incumbents' suggestion to apply a "service specific" impairment test under Section 251(d)(2). As shown in Part II, this is merely an attempt at an end-run around the clear mandates of Section 251(c)(3) and is forbidden under the Act, because Section 251(d)(2) cannot be construed to authorize what Section 251(c)(3) plainly prohibits. Moreover, despite the incumbent LECs' assertions, the Commission has *never* applied Section 251(d)(2) in a service specific manner.

There is also no basis for the incumbent LECs' "policy" arguments. As shown in Part III.A, even if the Commission had the authority to impose use restrictions on loop and transport elements that are used to provide special access services (which it does not), the Commission's findings in the *Remand Order* bar such a result here. The Commission made detailed findings in the *Remand Order* that CLECs' ability to compete would be impaired if they do not have the ability to access the loop and transport elements at cost-based rates. None of the facts the incumbents submit here changes any

of the essential facts underlying those decisions. Indeed, the incumbents add no significant new data regarding the availability of competitive loop or transport facilities, or the CLECs' costs and practical and operational difficulties in obtaining alternatives to such facilities. Rather, the incumbents proffer an unreliable market share analysis for special access services and make unsupported claims regarding the alleged revenue effects that would result if CLECs were permitted to use UNEs to replace current special access services. Thus, the incumbent LECs have failed to provide any data upon which the Commission could rationally change its decisions in the *Remand Order* that CLECs would be impaired in the absence of access to loops and transport at TELRIC rates. Thus, there is no basis on which the Commission may, as a matter of policy, carve out unique use or availability restrictions relating to special access services. Indeed, to do so would directly violate the basic policy considerations underlying the 1996 Act, especially since the incumbents admit (as they must) that there are no universal service subsidies in special access rates.

Part III.B demonstrates that the incumbent LECs' "sky is falling" view of their economic situation is both unsubstantiated and overblown. First, it is indisputable that incumbent LECs wield enormous market power over special access services and their access rates are significantly above cost. Moreover, the incumbents' claims of anticipated "loss" are mere assertions that are not supported with facts that can be reviewed by the Commission or other interested parties. Critically, in discussing the economic consequences of allowing CLECs to purchase unbundled network elements to provide special access, the incumbents simply ignore the fact that they have been the beneficiaries of huge windfalls that have resulted from the explosive growth in such services since the Act was passed. Thus, their claims of a perpetual entitlement to such windfalls ring hollow.

Finally, Part IV identifies a host of anticompetitive practices that AT&T has experienced in its efforts to convert special access facilities to unbundled network elements, even in cases where the Commission has already determined that CLECs are entitled to do so. This consistent pattern of obstruction requires a strong response from the Commission, in order that the Act may be full implemented as Congress intended.

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AT&T CORP. REPLY ON THE FOURTH FURTHER NOTICE OF PROPOSED RULEMAKING

Pursuant to the Commission's November 5, 1999 *Third Report and Order and Fourth Further Notice of Proposed Rulemaking* ("*Remand Order*"), FCC 99-238, and its November 24, 1999 *Supplemental Order*, FCC 99-370, AT&T Corp. ("AT&T") respectfully submits the following reply to the comments on the Fourth Further Notice of Proposed Rulemaking.

I. THE ACT PROHIBITS USE RESTRICTIONS ON NETWORK ELEMENTS

All of the incumbent LECs' attempts to develop a legal justification for use restrictions on unbundled network elements are flawed for one simple reason: the Commission has already concluded that (1) Section 251(c)(3) is "not ambiguous" in prohibiting use restrictions, and (2) "there is no statutory basis" on which a different conclusion could be reached or defended.[1] Thus, each of the incumbent LECs' arguments is easily refuted.

First, two incumbent LECs claim that the Commission may limit the particular services for which CLECs may use network elements because the first sentence of

[1] *See First Report and Order*, ¶¶ 356, 359; *see also* AT&T, pp. 3-6; Cable & Wireless, p. 3; CompTel, p. 8; MCI, pp. 3, 6; TRA, pp. 3-6.

Section 251(c)(3) refers to "a" telecommunications service rather than "any" telecommunications service.[2] But these LECs misread Section 251(c)(3). That section imposes on incumbent LECs "[t]he *duty* to provide, to any requesting telecommunications carrier for the provision of a telecommunications service, nondiscriminatory access to network elements on an unbundled basis. . . ." 47 U.S.C. § 251(c)(3) (emphasis added). Thus, incumbent LECs have a "duty" to provide access – and cannot lawfully withhold it - whenever a requesting carrier seeks access to a network element in order to provide "a telecommunications service." Because exchange access is clearly a "telecommunications service," *see First Report and Order*, ¶ 356 - a fact the incumbents do not dispute - the statutory duty applies whenever a CLEC requests access to network elements for the purpose of providing exchange access service.

Indeed, the incumbent LECs previously made – and the Commission properly rejected – the same argument about the second sentence of Section 251(c)(3). That sentence provides that "[a]n incumbent LEC shall provide such network elements in *a* manner that allows requesting carriers to combine such elements in order to provide such telecommunications service." 47 U.S.C. § 251(c)(3) (emphasis added). Some BOCs maintained that they could "limit a competitive carrier's choice to collocation as the only method for gaining access to and recombining network elements," claiming that collocation is "a" method for combining network elements.[3] The Commission, however,

[2] *See* Bell Atlantic, p. 17; SBC, p. 20.

[3] *See* Memorandum Opinion and Order, *Application of BellSouth Corporation, BellSouth Telecommunications, Inc., and BellSouth Long Distance, Inc., for Provision of In-Region, InterLATA Services in Louisiana*, CC Docket No. 98-121 (Oct. 13, 1998), ¶164 (emphasis added).

saw through this obvious distortion of the statutory language and held that this position was "inconsistent with section 251(c)(3)," under which "[c]ompetitive carriers are entitled to request *any other* 'technically feasible' methods of gaining access to and combining unbundled network elements . . . ."[4]

Second, the incumbent LECs argue that the Commission may place use restrictions on unbundled network elements because the language in Section 251(c)(3) states that access to network elements may be subject to "rates, terms, and conditions that are just, reasonable and nondiscriminatory."[5] But these arguments fail as well, because the incumbents uniformly *omit* the remainder of the statutory provision. The full text of that portion of Section 251(c)(3) only authorizes "rates, terms, and conditions that are just, reasonable and nondiscriminatory *in accordance with* the terms and conditions of the agreement and *the requirements of this section* and Section 252." 47 U.S.C. § 251(c)(3) (emphasis added). The Commission has held that one of "the requirements of this section" - that incumbent LECs provide access to network elements to any carrier that seeks to use them to provide a "telecommunications service" - necessarily and unambiguously prohibits use restrictions. Use restrictions, therefore, cannot be permissible "terms and conditions" under Section 251(c)(3).[6] Indeed, the entire notion of use restrictions is completely at odds with the nondiscrimination principles of Section

[4] *See id.* (emphasis added).

[5] *See* Bell Atlantic, pp. 3, 18; BellSouth, p. 14; GTE, p. 5; SBC, pp. 19, 21.

[6] SBC's claim that Section 4(i) of the Act supplies the missing authority for use restrictions fails for the same reason. Section 4(i) only authorizes the Commission to adopt rules "not inconsistent with the Act." 47 U.S.C. § 154(i). Because Section 251(c)(3) prohibits use restrictions, Section 4(i) cannot authorize them.

251(c)(3). Incumbents are permitted to use any element in their networks to provide any service they choose, maximizing their economies of scale and scope, as well as their practical flexibility. Denying competitors access to the same economies and practical flexibility would be inherently discriminatory and create a major barrier to competition.

Third, SBC contends (p. 27) that the Commission's analysis of this issue in the *First Report and Order* somehow rested on an aspect of its interpretation of Section 251(c)(3) that was disapproved by the Supreme Court – specifically, the Commission's prior understanding that Section 251(c)(3)'s reference to "technical feasibility" related to when, not where, access must be provided. This contention is baffling. Nothing in the *First Report and Order* drew any linkage between these two, separate interpretive issues. The Commission's determination that the Act prohibits use restrictions was based on the language relating to "telecommunications service," not "technical feasibility." *See First Report and Order*, ¶¶ 356, 359.

Fourth, BellSouth asserts that, because the Commission need not have permitted CLECs to obtain network element combinations in the first place, it may attach any conditions it deems appropriate to the leasing of network element combinations.[7] This premise is absurd. The availability of network element combinations is a matter of *statutory command*, not regulatory grace. Section 251(c)(3) specifically requires incumbent LECs to make network elements available in a way that permits them to be combined to provide telecommunications services. As the Commission has explained in discussing the incumbent LECs' earlier efforts to distort the statute's requirements by

[7] *See* BellSouth, pp. 19-20.

separating network elements that were combined before providing them to CLECs, "[t]hat anticompetitive exercise in economic waste is so plainly discriminatory that, even in the absence of a Commission rule, it would violate an incumbent's statutory obligation to provide '*nondiscriminatory* access to network elements . . . .'"[8]

Fifth, the incumbent LECs claim that the Commission's interpretations of other provisions of the Act support their position here, but in each case the Act's specific language makes clear that those other provisions must be construed differently from Section 251(c)(3). For example, Bell Atlantic contends that use restrictions on network elements are analogous to "'restrictions prohibiting . . . cross class reselling of residential services,'" which the Commission "upheld." *See* Bell Atlantic, p 18 (quoting *First Report and Order*, ¶ 962). Bell Atlantic neglects to note, however, that the Commission "upheld" such restrictions because Section 251(c)(4), which governs resale, provides that "a State commission may, consistent with regulations prescribed by the Commission under this section, prohibit a reseller that obtains at wholesale rates a telecommunications service that is available at retail only to a category of subscribers from offering such service to a different category of subscribers." *See First Report and Order*, ¶ 958 (quoting 47 U.S.C. § 251(c)(4)(B)). Section 251(c)(3), by contrast, contains no language permitting use restrictions; rather, it specifically forbids them.

Similarly, SBC (pp. 20-21) argues that the Commission may treat access services differently from other telecommunications services because it held that Section 251(b)(5), which establishes requirements relating to "reciprocal compensation" – *i.e.*,

[8] *See* Reply Brief for the Federal Petitioners, *FCC* v. *Iowa Utils. Bd.*, p. 23 (filed June,17, 1998) (emphasis added by Commission).

"the transport and termination of telecommunications" – relates only to local calls and not toll calls. *See SBC*, pp. 20-21 (citing *First Report and Order*, ¶ 1034). But the Commission did so because *another* provision of the Act – Section 251(d)(2)(A)(i) – made clear that Section 251(b)(5) was limited to "a situation in which two carriers collaborate to complete a local call." *First Report and Order*, ¶ 1034. By contrast, all parties here agree that Section 251(c)(3) is *not* limited to local calls, for even the incumbent LECs concede that CLECs may use network elements for exchange access where they also use those elements for local service.

Sixth, the incumbent LECs continue to claim that Section 251(g) "preserved incumbent local exchange carriers' existing rights . . . to collect access charges from interexchange carriers,"[9] even when they purchase network elements. This claim is obviously wrong. Indeed, if the incumbents' claim were true, CLECs would not be able to use network elements for exchange access even when the CLECs were using them to provide local service. The Commission has held, however, that Section 251(g) "does not apply to the exchange access 'service' requesting carriers may provide themselves or others when purchasing unbundled elements." *First Report and Order*, ¶ 362. Instead, "the primary purpose of section 251(g) is to preserve the right of interexchange carriers to order and receive exchange access services if such carriers elect not to obtain exchange access through their own facilities or by means of unbundled elements purchased from an incumbent." *Id.*[10]

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[9] *See* Bell Atlantic, p. 15; *see also* BellSouth, p. 15; GTE, p. 17; SBC, p. 22.

[10] The incumbents' argument is also inconsistent with the pricing principles underlying the Act. When CLECs purchase network elements, they pay the incumbent for the entire

(footnote continued on next page)

Finally, the incumbent LECs argue that the Eighth Circuit's decision in *Competitive Telecommunications Association* v. *FCC*, 117 F.3d 1068 (8th Cir. 1997) (*CompTel*)[11] supports their position on use restrictions. That reliance is badly misplaced.

In *CompTel*, the Eighth Circuit upheld the Commission's decision in the *First Report and Order* to allow incumbent LECs to impose certain access charges on users of unbundled switching, *but only until June 30, 1997*, and *solely* because of the fact that the Commission, at that time, was faced with a multitude of tasks under the Act. Indeed, the Commission recognized in the *First Report and Order* that the Act *required* it to move "access charges to more cost-based and economically efficient levels." However, at the time the Commission issued the *First Report and Order*, it perceived a conflict arising out of the disparate statutory deadlines for establishing local competition and universal service rules. Notably, the Commission was required to adopt its local competition rules by August 1996, before it had even begun to consider universal service issues, and the Commission did not believe that it would be able to adopt any of the universal service regulations required by Section 254 of the Act, 47 U.S.C. § 254, until May 1997.[12] Accordingly, the Commission "adopt[ed] *a narrowly-focused 10-month transition rule* that permitted the imposition of certain interstate access charges on the sale of [network elements] in order to sustain, *during a period of uncertainty accompanying the initial*

(footnote continued from previous page)

economic cost of those elements. Allowing incumbents to collect non-cost-based access charges on top of TELRIC rates would result in a multiple recovery for those elements and an enormous windfall for the incumbents.

[11] *See* BellSouth, pp. 15-17; GTE, p. 16; SBC, p. 24; USTA, pp. 16-23.

[12] *See First Report and Order*, ¶ 716.

implementation of the 1996 Act, the contributions that access charges traditionally have made to universal service subsidies."[13] The Court in *CompTel* found it "significant to our review for unlawfulness that the CCLC and TIC being assessed may be collected no later than June 30, 1997," and it upheld the Commission's transitional relief *only* because of its "brief life."[14]

Both the Commission (in its defense of the transitional rule) and the Court (in upholding that rule) emphasized that this was a highly limited exception to otherwise applicable statutory requirements. Both agreed that the exception was permissible only because of its fixed and short duration and the specific exigency to which it responded during the initial implementation of the Act. In sharp contrast, the incumbent LECs here seek a far more extensive limitation in order to address a situation that does not remotely present the concerns that gave rise to the transitional rule adopted in 1996. First, the incumbent LECs' proposed use restrictions would not have a "brief life" but a long and indefinite one – based on precisely the rationale that the Commission rejected in adopting the transitional rule that was upheld in *CompTel*. Indeed, the *Local Competition Order rejected* incumbent LECs' requests for "interim" relief that would last until the Commission had completed both its access and universal service reform proceedings:

> We can conceive of no circumstances under which the requirement that certain entrants pay [access charges] on calls carried over unbundled network elements would be extended further. The fact that access or universal service

[13] *See* Brief for Respondents Federal Communications Commission and United States of America, *Iowa Utils. Bd.* v. *FCC*, No. 96-3321, p. 50 (8th Cir. Sept. 17, 1999) (emphasis added).

[14] *See CompTel*, 117 F.3d at 1073-75.

> reform have not been completed by that date would not be a sufficient justification, nor would any actual or asserted harm to the financial status of the incumbent LECs. By June 30, 1997, the industry will have sufficient time to plan for and adjust to potential revenue shifts that may result from competitive entry.[15]

Accordingly, even though the Commission had not completed its universal service and access charge reform by June 30, 1997, it nonetheless terminated the transitional access charge mechanism. Moreover, the Eighth Circuit subsequently rejected the claims advanced by several incumbent LECs that they should be permitted to continue to recover access charges and purported universal service subsidies in connection with the sale of network elements until a new, explicit universal service system is fully operational.[16]

Today, in February 2000, we are no longer at the initial stages of implementation of the 1996 Act, and, as explained below, there is no conceivable basis for believing that universal service would be threatened without the proposed restriction.[17] *CompTel* therefore provides no support for the radical rule the incumbent LECs seek here.

II. THE ACT DOES NOT PERMIT OR REQUIRE THE COMMISSION TO APPLY A "NECESSARY AND IMPAIR" ANALYSIS TO SPECIFIC SERVICES

Several incumbent LECs advocate an end-run around the Commission's prior holding that Section 251(c)(3) plainly and unambiguously prohibits use restrictions, asserting that use restrictions nonetheless can be imposed through Section 251(d)(2).

[15] *See First Report and Order*, ¶ 725.

[16] *See Southwestern Bell Tel. Co.* v. *FCC*, 153 F.3d 523, 540-541 (8th Cir. 1998).

[17] *See also* AT&T, pp. 12-13.

They maintain that Section 251(d)(2) requires the Commission to conduct a "service-specific unbundling test" for combinations of network elements (and individual network elements).[18] This is nonsense.

Under the incumbents' approach, the Commission would impose use restrictions on network elements whenever it determines that requesting carriers would not be impaired in their ability to provide particular services if they were restricted from using the network elements they lease to provide those services. Here, the incumbent LECs maintain that special access is provided in a competitive market; that other carriers therefore would not be impaired if network element combinations could not be used for special access services; and consequently that the Commission can and should impose such a use restriction pursuant to Section 251(d)(2).

As shown in Part III.A. below, even if the Act permitted such an approach, the incumbent LECs have not made the necessary competitive showing. More fundamentally, however, the Act does not permit the "service-specific unbundling test" the incumbents propose. Section 251(d)(2) cannot be construed to authorize what Section 251(c)(3) plainly prohibits. The incumbents can argue otherwise only by patently misreading the law.

Section 251(d)(2) requires the Commission to "determin[e] *what network elements* should be made available." 47 U.S.C. § 251(d)(2) (emphasis added); *see also AT&T Corp.* v. *Iowa Utils. Bd.*, 119 S. Ct. 721, 736 (1999) (Section 251(d)(2) requires the Commission to decide *which network elements* must be made available") (emphasis

[18] *See* Bell Atlantic, pp. 17-18; *see also* BellSouth, pp. 12, 22; GTE, pp. 4, 9; SBC, p. 8.

partially in original and partially supplied). In making that decision, the Commission must consider whether access "to such network elements" as are proprietary is "necessary," and, for non-proprietary elements, whether the failure to provide access "to such network elements" would "impair" the requesting carrier's ability to provide the services it seeks to offer. *See* 47 U.S.C. § 251(d)(2)(A, B). The Section 251(d)(2) determination must therefore be made on a *network element-by-network element* basis. Indeed, that is just the analysis the Commission used in assessing network elements in the *Remand Order*.

That point is dispositive. The Act is clear that network elements are types of facilities or functionalities, not services. Indeed, as the Commission has consistently held, "network elements are *defined* by facilities or their functionalities or capabilities, and thus *cannot* be defined as specific services." *First Report and Order*, ¶ 264 (emphasis added); *see also* 47 U.S.C. §153(29) (defining "network element" as "a facility or equipment used in the provision of a telecommunications service"). Once the determination is made that a network element must be "made available for purposes of subsection [251]c(3)" (*see* 47 U.S.C. § 251(d)(2)), Section 251(c)(3) imposes a "duty" on incumbent LECs to make it available, free of use restrictions, to enable CLECs to provide any telecommunications service.

Section 251(d)(2)(B) directs the Commission to consider whether a competitive carrier will be impaired in its ability "to provide the services that it seeks to offer." Contrary to the incumbent LECs' claims (Bell Atlantic, p. 13; SBC, p. 8), that language does not remotely support their argument for service-specific unbundling. The Commission considers that factor in determining "what network elements" (47 U.S.C.

§ 251(d)(2)), *not* "what services," the incumbents must make available. Thus, subject to other considerations (*see Remand Order*, ¶¶ 26-28), if the Commission determines that requesting carriers will be impaired in offering the services they want to offer without access to a particular element, *the element* must be made available under Section 251(c)(3).[19]

Thus, contrary to Bell Atlantic's claim (p. 14), the Commission has never before conducted a "service-by-service unbundling analysis." Indeed, in both the *First Report and Order* and the *Remand Order*, the Commission conducted, as the Act requires, an element-by-element unbundling analysis, determining "which network elements" must be placed on the "national list" and made available.[20] The Commission has never separately analyzed each and every *service* that could be supported by each element, much less by each possible network element combination.

III. THERE IS NO POLICY BASIS UPON WHICH TO OVERRIDE THE ACT'S CLEAR LEGAL REQUIREMENTS

As shown above, the commands of the Act are clear and straightforward, and they do not afford the Commission any discretion to override them on "policy" grounds.

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[19] Indeed, the incumbent LECs' argument on this point highlights another respect in which their approach is not contemplated by the statutory scheme: Section 251(d)(2)(A), which contains the "necessary" standard, contains no such language regarding the "services that [the CLEC] seeks to offer." The incumbent LECs never offer any reason why Congress would direct a service-specific approach for services provided through non-proprietary elements but not for services provided through proprietary elements.

[20] *See, e.g., Remand Order*, ¶¶ 4, 16, 148. SBC is simply wrong in suggesting (pp. 8-9) that the exception the Commission made in the *Remand Order* to the availability of the switching element in certain circumstances is analogous. Under the terms of the *Remand Order*, switching is either available for all services (where the exception does not apply) or for no services (where the exception does apply). No "service-by-service" analysis was conducted, and no use restriction was imposed.

Thus, the Commission may not prohibit CLECs from using the loop and transport UNEs (and associated network equipment) to provide service that competes with the ILECs' special access services. And, contrary to the incumbent LECs claims', there is also no legitimate policy basis to impose the restrictions the incumbents seek on special access. Indeed, as described in detail below, the procompetitive policies underlying the Act all strongly support the CLECs' right to obtain loops and transport at their economic cost.

The Commission has already made detailed findings that CLECs' ability to compete would be impaired if they do not have the ability to access the loop and transport elements at cost-based rates. Moreover, it is clear that incumbents continue to exercise market power over both the loop and transport UNEs. Strikingly, however, the incumbents' comments read as though they had never reviewed the *Remand Order*. Rather, they rehash old arguments the Commission has already rejected and ignore key facts regarding the incumbent LECs' huge and continuing market power.

Further, the incumbents' "sky is falling" predictions of financial disaster are unsubstantiated and overblown. In particular, the incumbent LECs fail to acknowledge that they have been the beneficiaries of large – and unintentional - windfalls in recent years because of the huge growth in special access revenues. Accordingly, the incumbents' claim that they should be entitled to retain this windfall in perpetuity rings hollow.

A. The Incumbent LECs' Comments Ignore The *Remand Order's* Findings And The Fact That They Continue To Exercise Market Power Over Loops And Transport

1. The *Remand Order*'s Findings Bar the Incumbents' Claims

The incumbent LECs' comments add no significant data regarding the availability of competitive loop or transport facilities, or the CLECs' costs and practical and operational difficulties in obtaining alternatives to such facilities. Rather, the incumbents rely on an unreliable market share analysis for special access services[21] and the alleged

[21] The data relied upon in the RBOC/GTE "Special Access Fact Report" (p. 6) to develop the incumbent LECs' market share estimates are highly questionable at best. The report asserts that non-ILEC special access revenues amounted to $5.7B for 1999. This number, in turn, is based on a report by New Paradigm Resources Group (NPRG). Examination of the latter report reveals that the bulk (80%) of the special access revenues are attributed to MCI and AT&T which, according to NPRG, each had 25% of their local revenues derived from special access sources. According to NPRG, AT&T and MCI had $10.5B and $7.7B in local revenues, respectively in 1999. Neither the local revenues nor the percentage of those revenues attributable to special access/transport service are reported publicly by AT&T, however. Indeed, the NPRG report provides no information whatsoever as to how it arrived at these figures and NPRG merely states that these numbers were "NPRG Estimates." In sharp contrast, other industry analysts have offered much more conservative estimates of non-ILEC local revenues. Atlantic ACM estimated 1998 local revenues of $0.926B and $1.193B for AT&T and MCI, respectively. (Atlantic ACM, *U.S. CLEC Market Analysis : Company Profiles, Sizing & Share 1999-2003;* August, 1999) International Data Corporation (IDC) estimated AT&T and MCI 1998 local revenues of $0.974B and $1.205B, respectively, which are very consistent with Atlantic ACM's estimate. (International Data Corporation, *CLEC Mid-Year 1999 Review;* December, 1999). Similarly, IDC (*id.*) estimated first half 1999 revenues for AT&T and MCI of $0.718B and $0.704B, respectively, a far cry from the NPRG 1999 estimates. Furthermore, NPRG's CLEC 1999 report (which is also cited in the RBOC/GTE "Fact Report") states that AT&T's local revenues for 1998 were roughly .900B (directly in line with Atlantic ACM and IDC), and that AT&T's special access/transport accounted for 15% of those revenues. Therefore, if NPRG's 1999 analysis is to be believed, AT&T's local revenues would have grown over $9.5B from 1998 to 1999 and its special access/transport revenue would have grown nearly *twenty* times -- from $135M to $2.625B -- in a single year. Taken in context, according to NPRG, the entire CLEC industry's special access revenue grew from 2.5B to 5.7B during that same period, and almost all of that growth (and almost half of the overall CLEC revenue) is attributable to the fantastical and unexplained leap attributed to AT&T.

revenue effects that would result if CLECs were permitted to use UNEs to replace current incumbent LEC special access services. As a result, the Commission's analysis here regarding CLECs' need to access unbundled loops and transport as UNEs must rest on the same facts that were the foundation for the *Remand Order* itself. Because the incumbent LECs have failed to provide any data upon which the Commission could rationally reach a different conclusion, the *Remand Order* bars their assertions that the Commission should, as a matter of policy, carve out unique use or availability restrictions relating to special access services.[22]

The *Remand Order* correctly held that incumbent LECs must provide CLECs access to both loops and transport at cost-based (TELRIC) rates, because failure to do so would impair their ability to compete on a national basis. Specifically, the Commission found that the record evidence revealed few alternatives for these functionalities, and that the direct and indirect costs and practical difficulties (including the need to obtain access to rights of way[23]) CLECs must incur to obtain access to alternative facilities are competitively significant. The facilities that CLECs use to provide special access services are no different from the facilities they use to provide other services, and the incumbent LECs do not pretend otherwise. Thus, there is no basis to treat CLECs' use of

[22] *See, e.g.*, SBC, pp. ii-iv.

[23] *Remand Order* ¶¶ 186, 364 (recognizing the delays inherent in requiring CLECs to obtain rights-of-way and construct new loop or transport facilities).

these UNEs to provide special access services differently from the use of the same facilities to provide other telecommunications services.[24]

With respect to loops, the Commission (¶ 182) found that "[s]elf-provisioning is not a viable alternative to the incumbent's unbundled loops, because replicating an incumbent's vast and ubiquitous network would be prohibitively expensive and delay competitive entry."[25] The Commission (¶ 321) made an identical finding with respect to interoffice transport, stating that "self-provisioning ubiquitous interoffice transmission facilities, or acquiring these facilities from non-incumbent LEC sources, materially increases a requesting carrier's costs . . . delays broad-based entry, and materially limits the scope and quality of a requesting carrier's service offerings."[26]

Moreover, despite the fact that some carriers "have deployed transport facilities along certain point-to-point routes," the Commission found (*id.*) that the record did not support the incumbent LECs' contention that transport "is sufficiently available as a practical, economic and operational matter to warrant exclusion of interoffice transport from an incumbent LEC's unbundling obligations at this time." Rather, it found (¶ 341) that "only at a granular, wire center-by-wire center level does the record show the presence of competitive alternatives to the incumbents' interoffice transport, *albeit on a*

[24] The ILECs do not – and cannot – contend that access services are not telecommunications services. *See* AT&T, pp. 4-5.

[25] *See also id.* ¶ 183 ("as a practical matter, building loop plant continues to be, in most cases, prohibitively expensive and time-consuming").

[26] *See also id.* ¶ 332 ("[n]either self-provisioning interoffice transport facilities nor obtaining these facilities from third-party sources is an adequate alternative to the ubiquitous transmission facilities that a competitor can obtain from the incumbent LEC").

non-ubiquitous basis."[27] The Commission (¶ 184) reached an identical conclusion with respect to loops, finding that the fact that "some competitive LECs, in certain circumstances, have found it economical to serve certain customers using their own loops suggests to us only that carriers are unimpaired in their ability to serve those particular customers."

In addition, the Commission squarely held that CLECs are entitled to loops and transport facilities of all different sizes and types, including high-capacity lines,[28] which they need to provide all types of services to end users.[29]

Critically, the Commission (¶ 345) specifically rejected incumbent LEC arguments that dedicated transport should be excluded from their unbundling obligations "in any area where at least one requesting carrier has deployed transport facilities and has collocated its own transmission equipment in an incumbent LEC's central office." In doing so, the Commission found (*id.*) that even in areas where there are alternatives to the incumbent's facilities, "the alternatives generally do not travel the same routes as the incumbent's facilities . . . [so that] competitors more than likely have to route their traffic along indirect, inefficient routing patterns, thereby increasing their costs of transport."

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[27] Emphasis added. *See also id.* ¶ 333 ("the competitive transport facilities that currently exist do not interconnect all of an incumbent LEC's central offices and all interexchange carriers' points of presence within an MSA, or a substantial portion thereof").

[28] *Id.* ¶ 185 (rejecting incumbent LEC proposals to exclude "larger business loops in Special Access Pricing zones 1 and 2"); ¶¶ 176, 187 (requiring access to high capacity loops); ¶ 323 ("dedicated transport . . . includes all technically feasible capacity-related services such as DS-1, DS-3 and OC-3-96 dedicated transport services . . . and such higher capacities as become available over time").

[29] *Id.* ¶ 177 (finding no basis for placing a restriction on what services a carrier may offer using the loop network element).

This finding is indisputably correct. The mere fact that a single potential competitor may have enough aggregated traffic to permit it to arrange for alternative facilities between two specific points does not support a conclusion that alternatives exist for other competitors, even if additional capacity is available at an incumbent's office.[30]

Thus, the Commission (¶ 344) properly rejected "any bright-line test that triggers elimination of an incumbent LEC's [transport] unbundling obligation based on the presence of a single competitor that has self-provisioned transport in a particular market." Its rationale for doing so was also clearly correct: the Commission (¶ 345) refused to allow the degree, pace and scope of competition in an area to be dictated by the actions of a single non-incumbent LEC competitor, which "would potentially result in the presence of . . . a duopoly."

Finally, even though the Commission (¶ 346) recognized that competition for "entrance facilities" (i.e., the transport link between and IXC's point of presence and an incumbent LEC's serving wire center) is more mature than for other types of transport, it found that the record simply did not support a finding that competitive alternatives were

[30] Therefore, the incumbent LECs' reliance on data regarding the amount of fiber being installed by competitors is misplaced. Given the high cost and difficulties encountered with rights of way, CLECs will sensibly install fiber facilities containing as much fiber capacity as can reasonably be afforded given their available capital. With installation costs of up to $100,000 per mile and the incremental cost of additional fiber strands approximating only $158 per mile, installation of additional capacity is a prudent decision, even if there is little prospect for its immediate future use. Thus, contrary to the impression the ILECs have attempted to create, the current pace of fiber deployment does not demonstrate that alternative transport or loop facilities are widely available or that local markets (or even access services) are significantly competitive.

available "for all, or substantially all of the routes requesting carriers would need in order to provide the services they seek to offer."[31]

None of the incumbent LECs' facts or arguments here change any of the Commission's recent findings, nor do they refute the fact that the incumbents have substantial market power in the provision of special access services. Accordingly, there is no basis to modify the *Remand Order*'s conclusions to deal solely with special access service.[32]

As in their comments on the *Remand Order*, the incumbent LECs' comments here offer data on the collocation facilities CLECs have constructed.[33] Then, alluding to the

[31] The *Remand Order* (¶ 354) also rejects – again – the tired incumbent LEC argument that special access services are a substitute for unbundled transport.

[32] Although the Commission (¶ 177) did not decide how its analysis applied to the enhanced extended link ("EEL"), which is a combination of the loop and transport UNEs, the answer cannot be different if the facts show, as they do here, that both the loop and transport elements pass the "impairment" test.

[33] "Special Access Fact Report" prepared for Bell Atlantic, BellSouth, GTE, SBC and U S WEST ("RBOC/GTE 'Fact Report'"), pp. 8-10. In fact, it is misleading to focus upon collocation in these circumstances. A CLEC's main purpose in building a collocation facility is to obtain a means to access customers who are served by the office in which it is collocated (i.e., to develop a means to have access to customers' loops). Given the high fixed costs and large economies of scale involved in building transport facilities (especially optical facilities that can be expanded simply by replacing electronics at the end of the fiber), a collocator's interest in constructing alternative transport facilities is always secondary. A collocator will generally consider directing its scarce capital to build transport facilities only after it has (1) made sufficient switch-related investments necessary to provide its own differentiated service, (2) deployed sufficient assets to become a viable competitor for emerging services, such as advanced services, (3) deployed assets to reduce the reliance on competitors for direct access to high value customers, and (4) developed a sufficient understanding of its traffic patterns and volumes to warrant the high fixed costs of a very high-capacity link between its collocation and its other facilities. Indeed, because transport facilities generally do not enable a competitor to provide a differentiated service and ILECs already have large transport networks in place (which are often optical and expandable through the use of

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Price Cap Flexibility Order,[34] the incumbent LECs make claims regarding the proportion of offices with collocation in which at least one collocator has obtained transport from a source other than the incumbent LEC itself. But as shown above, the Commission flatly rejected that mode of analysis, noting that such arguments

- at best lead to a "patchwork of alternative facilities" or a requirement that CLECs must construct their own facilities, whether or not it is economic to do so,[35] and
- do not promote full-fledged competition because they leave CLECs at the mercy of a duopoly.[36]

At most, the incumbent LECs' data merely point to a conclusion the Commission already reached, *i.e.*, that competition for entrance facilities is "more mature" than competition for other types of transport facilities.[37] However, the Commission found

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electronics rather than new construction), the building of alternative transport is typically one of the CLEC's lowest priorities. Nevertheless, the incumbent LECs ask the Commission to reverse and reprioritize these logical investment incentives through pervasive regulatory intervention which, in the final analysis, will only sap the capital available to CLECs and unfairly advantage the ILECs themselves.

[34] Fifth Report and Order and Further Notice of Proposed Rulemaking, *Access Charge Reform: Price Cap Performance review for Local Exchange Carriers*, CC Docket No. 96-262 (released August 27, 1999) ("*Price Cap Flexibility Order*").

[35] *Remand Order* ¶ 341.

[36] *Id.* ¶ 345.

[37] There should be little surprise that the entrance facilities of a CLEC will be the first ones that are replaced by self-provided facilities. The entrance facility is the "pipe" through which all its customers' services flow between the incumbent LEC and CLEC networks. Thus, the entrance facility is the point of maximum traffic aggregation for the CLEC. But the mere fact that a *portion* of a service from a customer's premises to a

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that, even in this limited context, the record did not demonstrate there was competition *"for all, or substantially all of the routes that requesting carriers . . . need"* to provide the telecommunications services they wish to offer.[38] Given the fact that special access is a point-to-point service, even the exaggerated market share numbers cited by the incumbents bear out the Commission's conclusion -- and in all events the incumbents fail to show that alternative transport facilities are ubiquitously available both to and from the specific points where CLECs need them.[39]

Moreover, the incumbent LECs' analysis seeks to prove too much. In order to provide a competitive special access service, a CLEC typically needs to obtain both a channel termination (typically a DS-1 facility) and a transport link (typically a DS-3 or larger facility), together with associated multiplexing from the incumbent LEC. At best, the incumbent LECs' analysis shows the existence of some modest - albeit insufficient – alternatives to optical level (or possibly DS-3 level) facilities. Critically, however, it ignores the complete dearth of alternatives at and below the DS-1 level.[40] Indeed, the

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CLEC network routes through a single high-capacity facility for a small part of the journey should not and must not lead to the erroneous conclusion that all CLEC services carried within that facility are competitive, or that all parts of any specific service have alternatives for supply. *See* n.41 below.

[38] *Id.* ¶ 346 (emphasis added).

[39] It is for exactly this reason that any reference to the comparative market shares in special access and long distance is at best misleading. *See* RBOC/GTE "Fact Report", p.6. The incumbents ignore the fact that, unlike switched long distance services, special access services are provided over point-to-point facilities.

[40] It also ignores the fact that incumbent LECs have attempted to forestall CLECs' ability to convert existing access services to network elements by claiming that traffic on

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incumbents provide no data at all to support a finding that there is competition for DS-1 channel terminations in particular or for loops in general. Thus, this portion of the incumbent LECs' argument is naked bootstrapping.[41]

Furthermore, the mere fact that there is limited competition for the highest capacity transport facilities in some places creates a misleading impression as to the availability of alternative transport. In fact, DS-3 circuits are not generally constructed individually; rather, they are derived from the capacity in much larger (and more economically efficient) facilities, typically at optical levels. Thus, to the extent there is any competition for "DS-3s" it is usually a result of the fact that there is a very large amount of aggregated demand between two specific points that would support the construction of a much larger facility. This means that alternative facilities are available

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multiplexers must be *either* local *or* access traffic, but not both. There is no technical or policy justification for such an anticompetitive position.

[41] *See* Declaration of Janusz Ordover and Robert Willig, CC Docket No. 99-65 ¶¶ 15-17, filed March 31, 1999. ("Economic theory and experience both teach that a supplier of a service will have the ability to exercise market power with respect to that service if the supplier maintains market power over a single critical input to providing the service-even if the provision of all other components of the service is fully competitive. So long as the incumbent retains monopoly power over any such bottleneck input to special access services, for example, it can extract monopoly rents from special access customers (or from resellers who must buy the bottleneck inputs from the incumbent. . . . [I]t is important to recognize that special access services comprise at least two distinct components: local distribution channels ("LDCs") and dedicated transport. . . . If competing special access suppliers are to constrain the retail price of special access services to competitive market levels, there must be a competitive supply of both inputs. For that reason, retail market share figures are meaningless in this context. An unregulated incumbent with zero percent of the retail special access services market could nonetheless earn monopoly rents-and ensure that retail special access service prices remain well above competitive market levels-through its control of one or more of the inputs to those services").

only in the very limited circumstances that warrant such an investment, typically a few locations in the highest density areas.[42] Thus, the figures the incumbent LECs cite overstate the availability of transport alternatives as required by the *Remand Order*, *i.e.*, *at the specific points where CLECs need them*, and market competitiveness cannot be correlated with the mere pace at which alternative transport capacity has been installed.

2. The Incumbent LECs' Comments Also Ignore Their Market Power over Special Access Service

Just as important, the incumbent LECs' comments ignore that they wield a huge amount of market power in the special access services market. This can be directly deduced from four simple facts:

1. The Commission's recent decision denying incumbent LEC requests for forbearance with respect to special access services specifically refused to find the incumbents lacked such power;[43]

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[42] In order to achieve the greatest efficiency for such facilities (when they are available), it is critical that CLECs are able to route all of their traffic, regardless of service, over the same facilities. If CLECs were not permitted to do so, they would be required to use separate facilities for different types of traffic, which would condemn them permanently to a discriminatory and less efficient cost structure than the incumbent LECs, who can route all types of traffic over the same facilities without restriction. Thus, imposing use restrictions that allow aggregation of only *specific* services within *specific* facilities will not increase incentives for CLEC investment but rather will reduce CLEC transport efficiencies. Indeed, imposing use restrictions would force CLECs into a Hobson's choice of using inefficient, smaller and duplicative incumbent LEC services that are priced at supracompetitive rates or building their own facilities. In such circumstances, CLECs will often choose the former alternative due to the practical constraints caused by rights-of-way problems, construction lags and limited availability of capital. Thus , the use restrictions that the incumbent LECs seek here would increase regulation, reduce incentives for *efficient* investment and increase the unit costs for CLECs – all to the incumbent LECs' competitive advantage.

[43] Memorandum Opinion and Order, *Petition of U S West Communications, Inc. For Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA*, CC

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2. Incumbent LECs' special access rates are at or near the price caps for such services;[44]

3. Even after the Commission granted incumbent LECs additional flexibility to lower their special access rates in the *Price Cap Flexibility Order*[45] they have chosen not to do so. Indeed, their comments acknowledge this fact;[46] and

4. Since the passage of the Act, RBOC and GTE special access revenues and installed lines have grown at more than a 24% compounded annual growth rate.[47]

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Docket No. 98-157, et al., released November 22, 1999 ("*Forbearance Order*"), ¶¶ 10, 25-29, 33 (RBOCs failed to make "a *prima facie* showing of competition"), 34 ("[a]bsent a sufficient showing of competition, it is clear that regulation of the BOC petitioners' special access and high capacity dedicated transport services is necessary to protect consumers").

44 *See* Attachment 1, showing that the largest incumbent LECs' price cap indices are in no instance less than 6% below the caps.

45 AT&T has appealed that portion of the Commission's order because, in addition to giving unprecedented flexibility for "new" services without any competitive showing and greater deaveraging unrelated to the costs characteristics of the service, the tests the Commission adopted for Phase I and Phase II pricing flexibility are inadequate to determine the presence of actual competition. The "triggers" for such phased relief are predicated on the incumbent LEC showing that competitors have operational collocations in a given percentage of wire centers (or wire centers accounting for a percentage of the LEC's revenues in an MSA) and that in each wire center at least one competitor is using non-LEC-provided transport. This test does *not* account for the fact that the collocated competitor(s) may have no customers or only a negligible amount of customers.

46 *E.g.*, Bell Atlantic, Declaration of Robert W. Crandall ("Crandall Declaration"), n.15.

47 As reflected in their annual ARMIS reports, the special access revenues and lines for these companies grew at rates of 24.9% and 29% per year, respectively, from 1995 to 1998, the last year for which data are currently available.

The implications of these facts are also clear. Despite the presence of limited competition in a handful of specific locations, incumbent LECs have such a significant hold on the rest of the market that it more advantageous for them to keep their rates at the price caps throughout their territories than to lower their rates to meet niche competition.[48] Moreover, as noted above, incumbent LECs have been the beneficiaries of the enormous growth in data services, and the growth in special access revenues have enabled them to reap huge profits, which are maintained if they do not lower their access rates.

There is also no basis for the incumbent LECs' claim that above-cost special access rates are needed to support the growth of a competitive market.[49] As a threshold matter, the Commission has effectively rejected the contention that competitors need a "price umbrella" in order to enter the market, agreeing with the CLECs that they have

[48] *See also* Crandall Declaration, n.15 (Incumbent LECs have not asked for such relief because it would require them to give up the right to a "lower formula adjustment" to price cap regulation in the future, *i.e.*, the ability to keep special access rates higher in the future).

[49] E.g., Bell Atlantic, p. 10; SBC, pp. 13-14. The incumbent LECs' claim (SBC, pp. 13-14) that special access services ought to be treated similarly to xDSL service also misses the mark by a wide margin. First, the Commission did not apply any use restrictions in connection with xDSL service. Second, the Commission's decision was intended to spur competition in a new area – data services – rather than in a traditional area such as access. Third, the Commission's decision (wrongly in AT&T's view) concluded that all carriers had a comparable ability to obtain and implement packet switching. *See Remand Order*, ¶ 307. In sharp contrast, if the Commission's assumptions regarding data services applied equally to access services, the decade-long experience with competitive access providers should have produced a marketplace in which access services are much more competitive than they are today. In fact, whatever the merits of the Commission's decision on packet switching, the current paucity of access competition reveals that incumbent LECs still retain enormous market power as a result of the tremendous size, scale and scope of their voice networks, which have been publicly supported works in progress for decades.

many incentives to construct their own facilities, including the ability to control their own fate in the market and not be dependent upon their principal competitor.[50] The incumbent LECs' comments do not – and cannot – refute the common sense of this conclusion. Indeed, there is no reason to believe that competitors will cease their efforts to invest in and enter the marketplace as long as telecommunications is viewed as a growth industry.[51] More importantly, even if establishing a cost-based rate for special access diverted *economically rational* capital away from building transport facilities, that would benefit consumers and competition generally. Contrary to the incumbents' claims, such capital would not disappear; rather, it would be used in areas that enhance competition, including additional collocation and switching facilities and deployment of advanced services for less densely populated areas.

AT&T's experience in the limited circumstances where it has access to alternative suppliers also refutes the notion that CLECs cannot compete in a market with cost-based pricing for transport services. As noted in AT&T's Comments (pp. 10-12), rational CLECs cannot invest in facilities on the assumption that they can maintain above-cost rates. Rather, they must assume that competition will drive their prices to cost. And AT&T's experience demonstrates that competition can in fact lead to lower transport rates. AT&T has been able to purchase dedicated transport from CLECs at significant discounts from the prices charged by the incumbent LEC, often without the term or

[50] *Remand Order* ¶¶ 110-113.

[51] In fact, if telecommunications were not a growth market, no public purpose would be served by encouraging investment that is merely duplicative; indeed, that would merely be a waste of resources.

volume commitments that the incumbents require. A common CLEC practice is to set the base price for its services based on the lowest (or close to the lowest) unit cost that is available from an incumbent LEC.[52] Using that as the base price, the CLEC then includes a discount that may range into double-digits. CLECs may also offer additional discounts if AT&T is willing to make term commitment or volume commitments. Thus, the CLEC price may be 30 percent or more lower than a comparable ILEC month-to-month DS-1 rate, prices that likely approach the incumbent LEC's TELRIC.

Overall, this demonstrates in microcosm the path envisioned by the Act in general. TELRIC-based UNE rates are necessary to open the market, because they operate as a surrogate for competitive market conditions and provide the certainty that competitors and capital markets need to develop economically rational investment plans. In cases where competition actually takes root, CLECs generally will be able to obtain comparable functionalities in the market (either through self-provisioning or purchase from third parties) at prices which are at or below TELRIC levels and in timeframes and at quality levels comparable to UNEs. When that happens, market forces will drive the incumbent LECs to sell their UNEs – voluntarily – at a "market" price that approximates TELRIC. At that time, of course, the whole notion of UNEs will become irrelevant, not because of regulatory action but because real market activity has mooted any need for it. Until then, however, the incumbent LECs' inherent advantages of size, scale and scope (as well as the practical advantage of having in-place facilities that do not need to be

[52] For example, in pricing a month-to-month DS-1 service, the CLEC may start with the incumbent LEC's price for a 24-Pack, seven-year term service, divide that price by 24 DS-3s per 24-Pack, divide it again by 26 (assuming a fill factor of 26 out of 28 DS-1s on a DS-3), and then add 1/28th the price of a DS-1/3 multiplexer.

constructed, that can often be expanded without additional construction, and for which the incumbent already has the rights-of-way), require that CLECs be able to obtain loops and transport at TELRIC rates.

In fact, this is the policy the Act demands, because it is the only economic model that will support truly competitive markets over the long term. Only this model places all competitors, including the incumbents, on an equal economic footing and does not require new entrants to build unnecessary facilities, pay discriminatory and uneconomic prices for existing facilities, or waste capital on one type of facilities that could more productively be spent on other network elements. This is particularly true for loops and transport facilities, because these "dumb pipes" are only used to move traffic and cannot be used to offer consumers new or differentiated services; rather, they only offer CLECs an opportunity to emulate the incumbents' economies of scale and to direct scarce capital where it can produce the best economic advantage. In contrast, the policies urged by the incumbent LECs would force CLECs to make uneconomic investments, reduce their ability to offer differentiated services, stunt advanced services deployment, and generate huge unearned profits for the ILECs that they can use to extend their market power in local and access services into adjacent markets, while assuring that only incumbent LECs have the flexibility to make unconstrained investment decisions.

B. Incumbent LECs' Claims Regarding the Financial Impacts Of Following The Act's Requirements Are Unsubstantiated And Overblown

The incumbent LECs assert that they will suffer dire financial consequences if the Commission follows the Act's requirements and refuses to adopt use restrictions to protect their admittedly above-cost special access revenues. On their face, however, the incumbents' supporting data are nothing more than across-the-board assertions about the claimed impact on their special access revenues if the Commission does not come to their aid. The RBOCs and GTE provide no detailed analysis comparing current special access rates to current UNE rates. Rather, they simply assert (*e.g.* SBC, p. 14) that incumbents will, on average, suffer a 50% reduction in their special access revenues if CLECs are able to purchase such facilities at UNE prices (as the Act requires) and produce a series of conclusory numbers that have no supporting facts.[53] Indeed, the sketchiness of the data provided here matches the incumbents' unconvincing showing in support of their forbearance petitions - which covered only the largest cities in their territories. As in those cases, the data here compel the same findings that the Commission made in its *Forbearance Order* less than three months ago: the incumbents have simply failed to show that the special access market is competitive.

As a threshold matter, it is impossible to credit *both* the incumbents' claim of a 50% differential between access and UNE rates *and* their assertion that the market for special access services is competitive. In fact, in the real world, these facts are mutually exclusive, because *no* competitive market could sustain such a differential. Thus, either one side or the other of the incumbents' house of cards is doomed to collapse under even cursory analysis.

[53] Such an across-the-board assertion is particularly curious for certain RBOCs. U S WEST, for example, does not even have UNE DS-1 rates in 13 of its 14 states. Thus, no actual comparison is even possible.

Moreover, the incumbent LECs have been forced to admit that their significantly above-cost special access rates do not contain any universal service subsidies.[54] Indeed, SBC (pp. ii, 15) attempts to divert attention from this fact by weakly claiming that its huge special access profits are used to support its "general overhead," and it suggests that the Commission should take this into account to support the imposition of otherwise forbidden use restrictions on CLECs.[55] This claim is incredible. Notwithstanding SBC's claims of poverty (and public service) here, it has recently managed to *acquire control of two other RBOCs and SNET* and become one of the largest telecommunications companies in the world. Thus, there is little doubt that continuing the flow of excessive and above-cost special access revenues will enable incumbent LECs to increase their own market position and financial strength - and will not generate increased competition or improved consumer welfare.

In all events, even if the incumbent LECs' calculations are correct, they do not tell the whole story. As noted above, the incumbents have been the beneficiaries of recent and explosive growth in special access revenues, most of which occurred after the Act was passed. This, in turn, is associated with the extraordinary growth in the use of data services by large business customers, most of which has occurred since 1996.[56]

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[54] *See Remand Order*, n.994; AT&T, pp. 12-13.

[55] This claim is also a thinly disguised – and impermissible – attack on the Commission's TELRIC pricing principles

[56] SBC's argument (p. 4) that only CLECs and large business customers will benefit from the ability to transition from high-priced special access services to UNEs is thus a red herring. (*See also* Crandall Declaration, p. 14 (claiming that IXCs will receive a windfall in the absence of use restrictions)). First, the reality is that competitive markets force prices to cost. Therefore, CLECs will not be able to retain these cost reductions,

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Predictably, although the incumbent LECs' comments dwell on CLEC growth in this time period, they virtually ignore the extent to which their own revenues have increased.

ARMIS data for the RBOCs and GTE show that they have experienced phenomenal growth in this area since 1995. As noted above, their data show their special access revenues grew at a compounded rate of 24.9% from 1995 to 1998, the last date for which such data are available.[57] Moreover, special access lines for these companies grew at a rate of over 29% per year over the same period, with digital lines growing at over 32%. Based on these growth rates, in the unlikely event that incumbent LECs actually experienced a 50% reduction in special access rates resulting from the CLECs' exercise of their statutory right to transition to UNEs, they would replenish their "lost" revenues in about three years, even without taking account of demand stimulation.

Moreover, a very simple financial analysis shows that currently projected RBOC and GTE earnings per share growth would offset the impact of even a 50% reduction in special access revenues *in less than a year*. A 50% effective price reduction applied to a base of \$6.0B results in a \$3.0B gross revenue reduction. Net income, in turn, would be

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especially since special access services are purchased by the customer set that wields the greatest bargaining power. Second, large business customers have been forced to bear the burden of incumbent LECs' inflated special access rates for years. It is both fair and economically rational to permit them to benefit from reductions in special access costs. Moreover, since special access rates contain no universal service subsidies, there is also no policy reason why reductions in the underlying costs of those services should not benefit the users of those services. Indeed, the notion that *anyone* would receive a "windfall" if the incumbent LECs' rates were reduced to competitive cost-based charges is absurd.

[57] *See also* RBOC/GTE "Fact Report", n.34 (stating in a footnote that the incumbent LECs' growth rate for the previous year was 25.8%).

reduced by about $1.8B, assuming a 40% composite state, federal and local income tax rate. These companies have an aggregate of 8,454M outstanding shares,[58] so that earnings per share are reduced by about $0.21 per share ($1.8B reduced net income/8,454M outstanding shares). However, the projected GAAP EPS growth (weighted for outstanding shares) from 2000 to 2001 is, on average, $0.33 per share.[59] Thus, these companies' projected earnings growth for calendar year 2000 would, on average, offset the impact of the worst case scenario of the special access price reduction within about 8 months ([$0.21/$0.33]*12).[60]

Thus, a reduction the incumbent LECs' special access profits would not affect their ability to do business, including their obligation to meet universal service requirements. Rather, it would at most return them to the state they were in prior to the time the Act was passed.

In light of these facts, the incumbent LECs' claims that Congress did not intend the Act to increase competition for access services (*see* SBC, n.31) ring especially hollow.[61] Indeed, when the Act was passed in very early 1996, Congress could not have

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[58] *See* U. S. Telecom Services Wireline, Credit Suisse First Boston Corporation, January 6, 2000, Table 2.

[59] *Id.* This figure is obtained by (1) multiplying the outstanding shares for each company times the projected EPS growth for that company, (2) accumulating the result across all of the companies and (3) dividing by the total outstanding shares.

[60] Even on an individual company basis the longest recovery period is 12 months. *See* Attachment 2.

[61] Incumbent LECs' assertion that unbundling was not intended to promote access competition (*e.g.*, SBC, n.31) is absurd. Monopolies over exchange access services are just as harmful to consumers as monopolies over local service. Therefore, as the Commission has already held, "Congress intended the 1996 Act to promote competition

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known that the market for special access services would explode. Nor could it have foreseen the impact that a four year deferral of its unbundling rules would have on the development of competition in the telecommunications industry.

In sum, there is there no evidence that Congress intended that incumbents should be allowed to reap in perpetuity the windfalls they have already received as a result of their ability to maintain above-cost special access rates for over four years. In fact, the central purpose of the Act was to develop and foster competition in *all* telecommunications markets and to break up, rather than perpetuate, the incumbents' monopolies. Most ironically, the Act's chief vehicle to establish the economic foundation necessary for a fully competitive marketplace is the very unbundling requirement that the incumbent LECs seek here to avoid. The Commission should thus reject the incumbent LECs' claims that public policy considerations support the imposition of use restrictions on special access services.[62]

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for . . . exchange access services" too. *First Report and Order*, ¶ 361. Indeed, the text of Section 251(c)(2)(A) makes this point unmistakably clear. Section 251 requires incumbent LECs to permit interconnection "for the transmission and routing of telephone exchange service *and exchange access*" (emphasis added), and, as already noted, Section 251(c)(3) permits the use of unbundled network elements to provide any "*telecommunications service*," not just local exchange service.

[62] Similarly, there is no reason to reach a different conclusion regarding switched access services, especially if the Commission promptly adopts the CALLS proposal. *See* AT&T, pp. 15-17.