

**IV. THE TRANSACTION DOES NOT RAISE ANY SIGNIFICANT ISSUES UNDER SECTION 271.**

The new NorthPoint will comply fully with the requirements of section 271. This commitment is straightforward, since most of NorthPoint's current arrangements for providing DSL service already satisfy these requirements.

Prior to the closing of this transaction, NorthPoint will ensure that all of the services that it provides — and that the new NorthPoint will provide — comply with the interLATA restrictions that apply to Verizon.<sup>47</sup> In most cases, there will be no need to take action because most segments of NorthPoint's network do not cross LATA boundaries. In most segments of NorthPoint's network, the end user, central office, node, and ISP are all located within the same LATA. *See* Hagmueller Decl. ¶ 2. There are, however, limited segments of NorthPoint's network where this is not the case, and which therefore — in their current form — may raise issues under section 271. Where necessary, NorthPoint will modify its network to ensure that, when the new NorthPoint begins operations, it complies fully with section 271.

There are a few instances where NorthPoint operates transport facilities that carry traffic from one LATA to an immediately adjacent LATA. In one kind of arrangement, NorthPoint carries traffic between a NorthPoint collocation arrangement in a central office and a NorthPoint node in an immediately adjacent LATA. *See id.* ¶ 4. In a second kind of arrangement, NorthPoint carries traffic between a NorthPoint node and an ISP's point of presence in an immediately adjacent LATA. *See id.* ¶ 5. Prior to closing, NorthPoint will reconfigure its network to eliminate both of these arrangements in any states in which Verizon is not authorized

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<sup>47</sup>*See* 47 U.S.C. § 271(b)(1); *Application by Bell Atlantic New York for Authorization under Section 271 of the Communications Act To Provide In-Region, InterLATA Service in the State of New York*, Memorandum Opinion and Order, 15 FCC Rcd 3953 (1999).

to provide originating long distance services. *See id.* ¶¶ 4, 6. Within these states, NorthPoint will make all of the connections between central offices, nodes, and ISPs on an intraLATA basis. *See id.*

In a third arrangement, NorthPoint sells a private-line service to ISPs, transporting traffic from an ISP's end-user customers in one LATA to the ISP's point of presence in another LATA. *See id.* ¶ 7. This arrangement — which NorthPoint offers as “Regional Connect” service — enables ISPs to serve end users in LATAs in which they do not have a point of presence. *See id.* This arrangement therefore provides ISPs — particularly smaller ISPs that do not have widespread facilities — with a very efficient means to reach a large number of customers. *See id.* NorthPoint introduced its Regional Connect service to permit ISPs to enter new markets quickly and with a minimal investment in facilities. *See id.* This arrangement also benefits end-user consumers as it provides them with a wider choice of ISPs providing broadband access than they would otherwise have.

With respect to section 271, NorthPoint's Regional Connect service presents two issues. *First*, in some instances NorthPoint provides its Regional Connect service to ISPs that interconnect with NorthPoint in a state in which Verizon is authorized to provide originating interLATA services (*e.g.*, New York). *See id.* ¶ 8. The end-user customer of the ISPs, however, may be located in an in-region state for which Verizon has not received interLATA authority (*e.g.*, Pennsylvania). Under this scenario, NorthPoint carries traffic from the ISP's end-user customer in Pennsylvania to the ISP's point of presence in New York over a private line. From there, the traffic continues on to the Internet over facilities that the ISP provides itself or that it obtains from other providers; the private line provided by NorthPoint terminates at the ISP's point of presence. This arrangement does not need to be modified, however, because section

271(j) provides that this service is treated as “originating” in New York for purposes of applying section 271’s long distance restrictions.

Section 271(j) is a definitional provision; it defines the circumstances under which certain services are “considered an in-region service subject to the [advance approval] requirements of subsection (b)(1).” 47 U.S.C. § 271(j). Specifically, section 271(j) provides that “800” and “private line services” are treated as services that “originate” in an in-region state where, and only where, they both “(1) terminate in an in-region State of the Bell operating company, and (2) allow the called party to determine the interLATA carrier.” In other words, for certain types of services, section 271(j) provides a unique definition that reverses the usual presumption of where interLATA traffic originates. For the limited set of services where the party selecting the carrier is located in a state other than the state in which the traffic physically originates, what would normally be thought of as the terminating end of the service is treated as the “originating” end for purposes of determining whether it is an in-region service subject to section 271(b)(1). The logic behind section 271(j) is plain: with 800 and private-line services, the real customer (*e.g.*, a business with an 800 number) is located at the opposite end from where that customer’s traffic originates (*e.g.*, end users that call the 800 number). Section 271(j), therefore, prevents a Bell company from providing 800 or private-line services to customers that are located within an in-region state until it obtains authority to provide long distance services that originate in that state. Conversely, where a Bell company has authority to provide originating long distance services in a given state, it may terminate 800 or private-line services to customers that are located in that state.

In the Regional Connect example discussed above, NorthPoint’s customer is the ISP in New York, and not that ISP’s end-user customer located in Pennsylvania. The ISP is the

customer that purchases Regional Connect, which is a private-line service, and that therefore selects the interLATA carrier. As a result, the private-line traffic terminating at that ISP's point of presence in New York is treated under section 271(j) as originating at the ISP's point of presence in New York. NorthPoint accordingly does not need to make any modifications to its network to provide this service.

*Second*, there are some instances where NorthPoint provides its Regional Connect service to ISPs that interconnect with NorthPoint in a state in which Verizon is *not* authorized to provide originating interLATA services. *See id.* ¶ 9. In these cases, section 271 prohibits a Verizon affiliate from providing Regional Connect service even if the ISP's end user is located in a state where Verizon may originate interLATA traffic. NorthPoint will modify these arrangements to comply with section 271.

In particular, NorthPoint will modify its Regional Connect service in these instances so that an interLATA provider – not NorthPoint – provides the interLATA transport from the ISP's interconnection point to NorthPoint nodes in other LATAs. *See id.* ¶ 11.<sup>48</sup> Under this approach, NorthPoint would aggregate an ISP's traffic at a single node in each LATA in which such traffic originates. The ISP would then contract with an interLATA provider to carry the traffic between the various NorthPoint nodes at which that ISP's traffic has been aggregated and the NorthPoint node at which the ISP has located its point of presence. NorthPoint would then provide the

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<sup>48</sup>The interLATA provider in this case performs a function similar to that provided by a Global Service Provider (GSP) in that the ISP (rather than the end user) contracts with a service provider for interLATA transport. As defined in previous Commission orders, a GSP provides end users with connectivity to the Internet via arrangements with other backbone providers. *See, e.g., Qwest Communications International Inc. and US West, Inc., Applications for Transfer of Control of Domestic and International Sections 214 and 310 Authorizations and Application to Transfer Control of a Submarine Cable Landing License, Memorandum Opinion and Order* ¶¶ 37-38, CC Docket No. 99-272 (rel. Jun. 26, 2000).

intraLATA transport between its node and the ISP's point of presence in the same LATA. The ISP then would route the traffic to the Internet. Under this arrangement, any interLATA services would be provided by an interLATA provider, rather than NorthPoint, in conformance with the requirements of section 271.<sup>49</sup>

## V. CONCLUSION.

For the reasons set forth above, the Commission should expeditiously grant NorthPoint's and Verizon's request for authority under section 214 of the Communications Act to transfer control of NorthPoint's blanket section 214 authorization to provide domestic interstate telecommunications services as a non-dominant carrier.

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<sup>49</sup>ISPs would have three additional options: (1) moving the location of the interconnection with NorthPoint to a state where Verizon is permitted to provide originating interLATA services; (2) collocating within the LATA where the ISP's end user customer is located; or (3) selecting an interLATA provider to carry the traffic from NorthPoint's node to another LATA where the ISP has a presence. *See* Hagmueller Decl. ¶¶ 10, 12.



**Before the  
Federal Communications Commission  
Washington, D.C. 20554**

In the Matter of

Joint Application of NorthPoint  
Communications, Inc. and Verizon  
Communications for Authority Pursuant to  
Section 214 of the Communications Act of  
1934, as Amended, To Transfer Control of  
Blanket Authorization To Provide Domestic  
Interstate Telecommunications Services as a  
Non-Dominant Carrier

CC Docket No. \_\_\_\_\_

**DECLARATION OF THOMAS W. HAZLETT, PH.D.**

1. My name is Thomas W. Hazlett. I am a Resident Scholar at the American Enterprise Institute for Public Policy Research in Washington, D.C., and a former Chief Economist of the Federal Communications Commission. Attachment 1 is a short biography.

**INTRODUCTION**

2. The proposed merger of NorthPoint Communications Group, Inc. (NorthPoint) with the wholesale DSL assets of Verizon Communications (Verizon) offers obvious and substantial social benefits. The merger promotes efficiency in creating a more competitive DSL provider. This new competitor will be better able to challenge cable's overwhelming dominance in broadband access and will provide Internet Service Providers (ISPs) with an alternative nationwide distribution system to closed cable systems.

3. The proposed combination also promotes competition in video subscription service. The alliance creates a firm with the technology, national scope, facilities infrastructure, and potential audience size to surmount many of the hurdles facing entrants into the video delivery business. It therefore offers an effective challenge to cable TV's dominance in video subscription service.

4. The proposed combination poses no realistic threat of lessening competition. The alliance joins highly complementary assets. Verizon has focused on residential, asymmetric DSL (ADSL), while NorthPoint has focused on the small-to-medium business enterprise segment as a supplier of symmetric DSL (SDSL).<sup>1</sup> NorthPoint and Verizon are only two of many new entrants in the broadband access business. In fact, 97 percent of the central offices where both NorthPoint and Verizon provide service already contain two or more additional facilities-based competitors (without counting cable modem providers, traditional CLECs that offer broadband services, fixed wireless broadband, or satellite access suppliers). See Attachment 2. There are numerous rivals, and low entry barriers, eliminating the incentive or ability of the merging parties to engage in output restriction. Moreover, safeguards are in place to remove any possible anti-competitive result, including the New NorthPoint's independent corporate status, and the legally guaranteed open access environment in local telecommunications markets.

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<sup>1</sup> SDSL operates at the same speed upstream and downstream, whereas ADSL economizes on bandwidth by offering slower upstream service (returning from the end user to the Internet). ADSL is used primarily by residential consumers for standard web surfing, while SDSL is the overwhelming choice for business applications (where web hosting, video conferencing, and large file transfers are common). SDSL is typically three or four times more expensive than ADSL on a monthly basis because SDSL is engineered to provide a minimum committed amount of bandwidth. (See discussion below.)

## THE MERGER ACCELERATES DSL DEPLOYMENT

5. As the FCC has found, the race to provide broadband “last mile” access features at least four major technologies – cable modem service, digital subscriber line (DSL), fixed wireless, and satellite.<sup>2</sup> Broadband service is being adopted very rapidly; annual growth rates range from 150% to over 350%.<sup>3</sup> Still, only a modest fraction of U.S. homes and businesses currently access the Internet with two-way high-speed service (200 kbps or higher).<sup>4</sup> At the end of the second quarter of 2000, there were just over 3 million residential broadband subscribers, about three percent of the 103.9 million U.S. households.<sup>5</sup> See Attachment 3. Very large social gains will likely be realized as penetration increases, building much larger user groups for broadband distribution networks. This will stimulate new online services, driving further demand for broadband access. Ultimately, communications will be transformed in fundamental ways, and important efficiencies achieved. Hence, speeding advanced telecommunications service towards mass market coverage tends to be relatively more important here, in a nascent industry segment, than were such services provided in a more mature, less dynamic, sector.

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<sup>2</sup> D. Lathen, Bureau Chief, Cable Services Bureau, *Broadband Today, A Staff Report to William E. Kennard, Chairman Federal Communications Commission on Industry Monitoring Sessions Convened by Cable Services Bureau*, at 27 (Oct. 1999) [“*Broadband Today*”].

<sup>3</sup> Federal Communications Commission, *FCC Issues Report on the Availability of High-Speed and Advanced Telecommunications Services* (Aug. 3, 2000).

<sup>4</sup> This was the threshold established for broadband service by the Federal Communications Commission. See FCC, *In the Matter of Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996*, CC Docket No. 98-146 [“*FCC Advanced Services Report*”] (Feb. 2, 1999), par. 20. The Commission calls two-way high-speed access “Advanced Telecommunications Services.”

6. The merger will provide national scale for New NorthPoint to market its DSL product, allowing it to quickly assemble superior solutions for nationwide ISPs and business customers with dispersed branch offices. The alliance will also have immediate entrée into scores of telephone markets out of Verizon's local exchange region, igniting head-to-head rivalry with SBC, Qwest, BellSouth and other ILECs, CLECs (including IXCs), and a multitude of network service providers. Finally, the New NorthPoint will have the opportunity, through such enhancements in the scale and scope of DSL offerings, to develop new applications and content for broadband competitors such that it (and other DSL providers) might successfully challenge cable television's continuing dominance in subscription video service.

7. Cable easily leads the race for broadband access, supplying approximately three-quarters of residential broadband access subscribers. The two leading cable modem ISPs, Excite@Home (majority owned by the largest U.S. cable operator, AT&T) and Road Runner (majority owned by the second largest U.S. cable operator, Time Warner), serve approximately one million subscribers each. No DSL service provider approaches even half that scale. See Attachment 3. Moreover, this cable advantage is unlikely to be eliminated in the near future given that cable broadband providers have such easy access to additional residential customers. For example, Excite@Home and Road Runner have exclusive contracts to pass approximately 57 million and more than 30 million households, respectively.<sup>6</sup>

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<sup>5</sup> *Broadband!* McKinsey & Co., Sanford C. Bernstein & Co. (Jan. 2000), at 24, Exhibit 21.

<sup>6</sup> Excite@Home, *Excite@Home Reports Second Quarter 2000 Results* (July 19, 2000); Excite@Home, *Second Quarter 2000 Key Financial and Operating Metrics* (July 19, 2000); Time Warner Press Release, *Time Warner Businesses Report Record 1999 and*

8. Of the 2.27 million cable broadband access subscribers, over 2 million, or about 89%, are served by Excite@Home and Road Runner. This concentrated cable gateway to the emerging mass market in broadband offers program distributors certain transacting advantages, and evolving products and standards may be crafted around them. To compete, DSL suppliers must promote the creation of content increasing the value of DSL access to customers. Efficiently aggregating services is part of this effort. At this formative stage in the development of rival networks, constraints on scale economies can seriously undermine competitive forces. The emerging network – DSL – needs to promote applications and functionality to attract users.

9. Looked at from the reverse angle, content creators should welcome the New NorthPoint as a major step towards increasing competition in program distribution. Not only is creation of an alternative channel for broadband programming a positive development for broadband content creators in a general sense, the specific advantages of a non-cable broadband distributor are apparent: DSL suppliers do not have split loyalties in promoting Internet access to video. Already a controversy has erupted regarding rules imposed on subscribers by the two largest cable ISPs, Excite@Home and Road Runner, limiting video streaming to just ten or fifteen (continuous) minutes.<sup>7</sup> The restrictions have been condemned by critics as anti-competitive actions to protect against

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*Fourth-Quarter Results* (Feb. 2, 2000); MediaOne Press Release, *MediaOne Group Inc. 1999 Fourth Quarter Earnings* (Feb. 28, 2000); *Road Runner Launches on Fanch CABLECOMM Systems in Pennsylvania*, Business Wire (Jan. 27, 1999); *Top 50 MSOs' Geiger Counter Shows Shifts*, Television Digest (June 14, 1999) (citing Warren Publishing March 1999 data); Charter Press Release, *Charter Communications' Acquisition of Fanch Cable Systems Final* (Nov. 15, 1999).

<sup>7</sup> F. Dawson, *RealNetworks, @Home Team Up on Streaming*, Multichannel News, (Jan. 18, 1999), at 2; *Do They Have Anything in Common?* The Economist (Feb. 13, 1999), at 61; Gary Arlen, *Stream-Rolling Into Video Reality*, Multichannel News (July 19, 1999).

cannibalization of cable subscription fees. Cable TV companies defend their policies as necessary to maintain broadband access over shared bandwidth. Either way, it is clear that cable modem service providers actively seek to limit Internet distribution of video programming. The emerging DSL platform, conversely, faces no conflict in aggressively pursuing competitive options for video. Moreover, the DSL conduit is open to a competitive mix of ISPs, promoting opportunities for program distribution not available in the exclusive ISP system adopted by cable modem service providers.

10. It is critical that the emerging DSL providers be permitted to achieve economies of scale and scope to construct an effective competitive platform to cable broadband. Lacking this, DSL may lag in the “content war,” become relatively unattractive to subscribers, and then lose further ground in content due to small audience size.<sup>8</sup> The over-arching competitive struggle in broadband access revolves around the functionality of rival networks.

#### THE MERGER PROMOTES AN OPEN DSL PLATFORM TO COMPETE FOR VIDEO SERVICES

11. The merger will help accelerate the deployment of DSL to the mass consumer market. By doing so, it will help establish an open platform to challenge the cable incumbents that dominate the residential broadband access business.

The merger will also provide added scale needed to compete with the cable operators in the video subscription business they dominate.

12. While the market power of cable television companies is well established, and closed cable Internet access service potentially threatens consumer choice, the

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<sup>8</sup> Brian Ploskina, *DSL Providers Gird for Content War*, Inter@ctive Week (July 24, 2000).

Commission has declined to impose open access rules on cable operators. This stems from the finding that “regulation.... ultimately slows deployment of broadband,” and a belief that, “[m]arket forces will compel cable companies to negotiate access agreements with unaffiliated ISPs.”<sup>9</sup> The Commission has pointedly noted that should “market forces fail and cable becomes the dominant means of Internet access, regulation might then be necessary....”<sup>10</sup>

13. Competition from DSL, an open platform inviting competitive ISPs to utilize shared infrastructure, is currently the key marketplace alternative to closed cable modem broadband access. Many ISPs, denied cable access, are depending on DSL network development in the broadband race.

14. Some of the most substantial benefits of the proposed merger lie in the potential to create an additional national distribution channel for video services. This is facilitated by the likelihood that New NorthPoint will better utilize NorthPoint’s virtual-video-on-demand technology, Blast!<sup>11</sup> This network system transmits full motion video, in real time, to customers with DSL connections. History indicates that entry is not easy in subscription video markets.<sup>12</sup> Blast! offers the possibility of a “killer app” that will drive customers to embrace DSL, thereby driving content developers to further support applications for DSL.

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<sup>9</sup> Federal Communications Commission Press Release, *FCC Chairman Kennard Releases Cable Staff Report on the State of the Broadband Industry, Provides Evidence of Emerging Competition and the Importance of National Policy*, Press Release (Oct. 13, 1999), at 2.

<sup>10</sup> *Id.*

<sup>11</sup> “NorthPoint Communications is ironing out its Blast service, which uses an architecture similar to Qwest’s to put the content as close as possible to where the customer is.” Brian Ploskina, *DSL Providers Gird for Content War*, INTER@CTIVE WEEK (July 24, 2000), <http://www.zdnet.com/intweek/stories/news/0,4164,2606329,00.html>.

15. In addition, the FCC has determined, in annual reports since 1994, that monopoly cable television operators possess substantial market power and charge prices significantly above competitive levels.<sup>13</sup> Head-to-head cable competitors (overbuilders) and direct broadcast satellite service providers have begun to make inroads. Yet the Commission finds cable systems, averaging over 80% market share, maintain substantial market power.<sup>14</sup> And capital markets suggest that cable TV systems – in offering bundled video and Internet access – now enjoy *enhanced* ability to extract supra-competitive returns. (See discussion below.) This implies that potential competitors to cable TV operators continue to face significant entry barriers.

16. The merger attempts to create scale economies whereby infrastructure and technology can be more effectively utilized. This investment, if successful, will relieve the current bottleneck in video program distribution presented by the dominance of cable television systems. The programming industry will benefit from this competition, creating more efficient ways to reach customers. Importantly, this monopoly bypass will only offer an effective alternative platform to the extent that it allows programmers efficient scale in quickly accessing large audiences.

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<sup>12</sup> Hazlett, *Predation in Local Cable Television*, Antitrust Bulletin (Fall 1995).

<sup>13</sup> See FCC, *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming* [“*First Annual FCC Cable Report*”], CS Docket No. 94-48 (Sept. 28, 1994), pars. 13, 213; FCC, *In the Matter of Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming* [“*Sixth Annual FCC Cable Report*”], CS Docket No. 99-230 (Jan. 14, 2000), pars. 5, 9.

<sup>14</sup> “The market for the delivery of video programming to households continues to be highly concentrated and characterized by substantial barriers to entry.” *Sixth Annual FCC Cable Report*, at par. 140.

17. In content creation, scale economies are crucial to product development. The FCC has specifically noted the importance of minimum efficient scale for creating new programming networks aimed at significant national audiences.

Because programmers have an incentive to minimize transactions costs of securing access to the 15-20 million subscribers needed for viability, large MSOs have some bargaining power, especially vis-à-vis start-up programming networks.<sup>15</sup>

This particular level of minimum scale is not a standard for the creation of all innovative programming; basic cable networks and Internet video programs have distinct business models making direct financial comparisons difficult. But the essential economics are similar in both cable networks and Internet video: content is produced under conditions of high fixed costs and low marginal costs. Once a given program is created, reproduction or rebroadcast costs are essentially zero. Moreover, the investments made to create any one successful product can typically be amortized across some number of “spin-off” creations.

18. The argument for permitting a large-scale non-cable supplier to establish sufficient scale in order to challenge cable’s video dominance is clear and persuasive. If DSL providers, or ISPs using DSL, are able to efficiently attract new program services, it may compete robustly with cable for high-speed last-mile connectivity. If, however, DSL providers are prohibited from achieving the scale economies long enjoyed by their cable rivals, the lack of content will itself form a substantial barrier to entry, potentially locking in another generation of monopoly rents in cable television.

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<sup>15</sup> FCC, *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, [“Fifth Annual FCC Cable Report”] CS Docket No. 98-102 (Dec. 23, 1998), at par. 157.

19. Investors may already, however, be anticipating continued cable dominance in the broadband world. Cable television system values more than doubled from 1997-2000, on a per subscriber basis. See Attachment 4. Comparing market prices paid for cable systems to the replacement cost of tangible capital yields a measure of the rents (above-competitive returns) available to cable TV system owners, which is also called a “*q* ratio” analysis.<sup>16</sup> That cost can be approximately determined up through 1997 by the FCC’s 1994 estimate: \$538 per sub. For 1998-2000, I use the 1999 estimate provided by the Federal Communications Commission for an upgraded cable system capable of delivering high-speed two-way (cable modem) service: \$800 -\$1000 per subscriber.<sup>17</sup> The margin between the market value and the capital cost constitutes economic rent.

20. Attachment 5 shows these rents (differences from Attachment 4). With recent market sales exceeding \$5,000 per subscriber, the implied *q* ratio falls in the range of 5 to 7, *larger* than those identified by the FCC as evidence of monopoly power in the early to mid 1990s.<sup>18</sup> This indicates that investors forecast large profits flowing from advanced services.

#### THE PROPOSED MERGER DOES NOT POSE RISK OF ANTI-COMPETITIVE CONDUCT

21. The merging parties possess highly complementary assets, offering services that are largely distinct. Historically, Verizon has focused on residential, ADSL subscribers while NorthPoint has focused on business, SDSL customers. Due to their technical

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<sup>16</sup> In such an analysis,  $q = (\text{market value of assets})/(\text{replacement cost of tangible assets})$ . In a highly competitive industry, *q* is likely to be approximately one.

<sup>17</sup> *FCC Advanced Services Report* at Chart 2.

<sup>18</sup> In September 1994, the FCC found cable industry *q* ratios of between 3.95 and 5.23. The Commission concluded that, “the current *q* ratios suggest that, overall, cable

differences, ADSL is the service of choice for households (where email and web surfing are the primary demand drivers, and slower return access is not a large inconvenience), while SDSL is the service of choice for businesses (where large file transfer, web hosting, and database access typically demand two-way high-speed service).

22. Although the FCC has not formally defined separate residential and business broadband markets, it has looked separately at competition for these two customer segments.<sup>19</sup> Similarly, without formally defining relevant antitrust markets, I examine competition for residential and business customers.

23. In residential broadband, cable is the clear leader, with approximately three-quarters of the cable/DSL subscriber total. See Attachment 3. As noted above, the two leading cable ISPs, Excite@Home and Road Runner, serve approximately one million subscribers each, having (individually) more residential customers than all DSL providers combined. Moreover, cable operators are further along than DSL suppliers in the deployment of the networks. The nation's two largest cable operators, Time Warner and AT&T, already have upgraded 90 and 51 percent of their networks, respectively.<sup>20</sup> The FCC has projected that by year-end 2000 the five largest cable companies "will have upgraded systems that cover at least 61 million" homes passed, or 80% of their service

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television operators possess substantial market power." *First Annual FCC Cable Report* par. 211, Table 5.2

<sup>19</sup> *Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations from MediaOne Group, Inc., to AT&T Corp.*, Memorandum Opinion and Order pars. 106 - 109, CS Docket No. 99-251 (rel. June 6, 2000); *Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996*, Report, 14 FCC Rcd 2398, pars. 27-33 (1999).

<sup>20</sup> Bear Stearns, *Cable TV & Broadband*, (Apr. 2000), at 57, Exhibit 15.

areas.<sup>21</sup> As the Commission has noted, “[c]able modem deployment is expected to dramatically increase in the coming years,” as “[c]able operators have adopted an aggressive schedule to upgrade their networks to provide broadband services.”<sup>22</sup> The Commission does not anticipate that DSL will catch up in subscribership until 2007.<sup>23</sup>

24. Head-to-head rivalry between cable modems and DSL service is an important constraint on DSL, as was clearly anticipated when the Commission wrote the following:

[W]e are already seeing DSL services priced to be directly competitive with cable modems... ADSL and ADSL-lite, while offering lower data speeds [than cable modems] likely will see price declines over the next 12-18 months to levels more in line with cable modem pricing...<sup>24</sup>

The FCC Report lists DSL rates as then (Jan. 1999) being in the \$50-60 per month range. Since, they have generally declined to the \$39.95 price point under pressure from cable modem service.

25. For business users, DSL competition is intense. Many new firms are entering into DSL service provision, taking advantage of the open markets now prevailing in local telecommunications. Within the Verizon service territory, at least 27 competitors have already collocated DSLAMs in Verizon’s central offices (COs), an investment that directly facilitates competitive provision of DSL service over local loops to end users rented from the incumbent local exchange carrier (ILEC). The list of collocated DSL providers in Verizon’s territory includes Broadslate, Covad/BlueStar, Digital Broadband, DSLnet, Florida Digital Network, HarvardNet, Interpath, Jato Communications, LogOn America, Maxcess, Network Access Solutions, Net2000, New Edge Networks,

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<sup>21</sup> *Broadband Today* at 26.

<sup>22</sup> *Id.*

<sup>23</sup> *Id.* at 27.

<sup>24</sup> *FCC Advanced Services Report*, at App. A pars. 16, 19.

NewSouth Communications, PATHNET, Prism, PROSPEED.NET, Rhythms, and Votts.<sup>25</sup>

26. Head-to-head rivalry between these firms can be charted through examination of DSLAM collocations.<sup>26</sup> Throughout Verizon's service territory, there are approximately 6,300 COs, of which approximately 2,000 are equipped for DSL service provision. Of these, 667 contain both Verizon and NorthPoint facilities. In 662 of the 667 overlapping COs, or 99%, there is at least one additional DSL CLEC already present. Post-merger, 648 of the overlapping COs (97%) would feature 2 or more CLEC DSL collocations, and 602 (90%) three or more. See Attachment 2.

27. These numbers do not include additional broadband competitors such as cable operators, traditional CLECs, fixed wireless, or satellite. Cable operators have already deployed cable modem service on systems that overlap with 291 (44%) of the COs in which Verizon and NorthPoint both provide DSL service,<sup>27</sup> and the FCC expects that 80 percent of all cable systems will be upgraded to provide cable modem service by the end of this year.<sup>28</sup> With cable added to the mix, the CO-by-CO analysis reflects still greater post-merger rivalry, with 92% of COs having 3 or more competitors in place. See Attachment 2.

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<sup>25</sup> Within Verizon's local exchange region, there are 27 data CLECs accounting for 5604 CO collocations. Mean collocations = 296, median = 58, and the range is 1 (3 different CLECs) to 845 .

<sup>26</sup> The number of collocation arrangements a DSL competitor has can be a more useful measure of their competitive presence than line counts given the rapid development of this sector.

<sup>27</sup> Cable Datacom News, *Commercial Cable Modem Launches in North America* (updated July 27, 2000), <http://www.cabledatacomnews.com/cm/cmic7.html>.

<sup>28</sup> *Broadband Today* at 27.

28. A wide range of CLECs already have extensive collocation arrangements throughout Verizon's region, making it easy and inexpensive for these firms to deploy a DSLAM or other technology to provide advanced services. As a leading sector analyst has noted, "Established CLECs such as Allegiance and Mpower are deploying their own DSLAMs and reinventing themselves as DSL providers. Intermedia, the oldest and largest independent CLEC, is embracing DSL to solve last mile connectivity issues. Additionally, NEXTLINK and PaeTec, two companies that originally had no intention of providing data services.... have announced DSL strategies."<sup>29</sup> McLeodUSA<sup>30</sup> and KMC Telecom<sup>31</sup> are other CLECs that operate in Verizon's region and have begun providing facilities-based DSL services.

29. Each of the big three long distance carriers has announced plans to begin competing extensively in the provision of DSL services. AT&T recently announced that it "has accelerated the market roll-out of its Digital Subscriber Line (DSL) Internet service," in order to "reinforce[] its position as the premiere provider for businesses seeking a nationwide, single-vendor broadband solution."<sup>32</sup> AT&T claims that its "[b]usiness DSL Internet service is available today in nearly 100 markets throughout the

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<sup>29</sup> New Paradigm Resources Group, *CLEC Report 2000, 12<sup>th</sup> ed.*, Ch.1 at 3.

<sup>30</sup> McLeod recently reported that in the second quarter of 2000 "it increased its collocations by nearly 25 percent to 230 and installed DSLAM equipment in 110 of those collocations. McLeodUSA expects to exceed 400 collocations by year end with more than 50 percent equipped for DSL service." McLeodUSA Press Release, *McLeodUSA Reports Solid Results for Second Quarter 2000* (July 26, 2000).

<sup>31</sup> Part of KMC's strategy is "to be a premier provider of DSL service." KMC's number of collocations increased to 81 as of year-end 1999, and of these, 35 were DSL-ready, with the others underway for DSL-rollout during the remainder of 2000. KMC Telecom Press Release, *KMC Telecom Reports Fourth Quarter and Full Year 1999 Financial Results* (Mar. 31, 2000).

<sup>32</sup> AT&T Press Release, *AT&T Accelerates Deployment of Broadband Business Services* (July 26, 2000).

United States,” and that it has “expanded our DSL service roughly twice as fast as originally planned.”<sup>33</sup> Sprint plans to deliver its Integrated On-Demand Network (ION) service by building local broadband facilities in cities across the country, using a mix of DSL and fixed wireless technologies.<sup>34</sup> It claims that, “DSL is one of the cornerstone technologies for enabling Sprint ION nationwide.”<sup>35</sup> Sprint states that its “introduction of Sprint High Speed DSL and [its] associated partnerships with leading broadband multimedia content providers truly set [it] apart from other companies vying to become players in the fast connection marketplace.”<sup>36</sup> A year ago, WorldCom announced that its DSL deployment had reached more than 1,000 Points of Presence (POPs), covering 850 cities in 22 metropolitan areas across the U.S. WorldCom noted that, “This announcement demonstrates MCI WorldCom’s leadership-role in providing nationwide DSL access.”<sup>37</sup>

30. Two of the largest incumbent local exchange carriers — SBC and Qwest — have plans to provide DSL services for business and residential customers outside of their region, including those within Verizon’s territory. SBC plans to begin competing in 11 major markets in Verizon’s region,<sup>38</sup> beginning with Boston, in the fall of 2000, followed by New York City, Washington, D.C., Baltimore, and Philadelphia by the end of the

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<sup>33</sup> *Id.*

<sup>34</sup> *Sprint to Offer Nation’s First Integrated Communications Services for the Home*, PR Newswire (June 21, 1999).

<sup>35</sup> *Sprint EarthLink DSL Delivers Broadband Solutions for Charlottesville Businesses and Consumers*, PR Newswire (Aug. 31, 1999).

<sup>36</sup> *Sprint Advances Broadband Content Strategy with Florida Launch, Addition of Two New Providers*, PR Newswire (Oct. 19, 1999).

<sup>37</sup> *MCI WorldCom DSL Deployment Reaches Milestone Mark of 1,000 Points of Presence*, M2 Presswire (July 14, 1999).

<sup>38</sup> SBC Telecom, *Service Territories*, <http://www.sbctelecom.com/Territory/1,1503,,00.html>.

year.<sup>39</sup> SBC Telecom intends to provide DSL service, which it will initially obtain from Concentric Networks.<sup>40</sup> Qwest has announced plans to provide DSL services to small- and medium-sized business customers in 25 markets outside of the U S WEST region,<sup>41</sup> and has already made DSL service available in five major markets in Verizon's territory: Boston, New York, Philadelphia, Baltimore, and Washington, D.C.<sup>42</sup> Although Qwest began providing out-of-region services as a reseller, it recently began deploying its own out-of-region DSL facilities, and has claimed that "[w]e are going to build out of region."<sup>43</sup>

31. As the Commission explains, LMDS operators also "offer a variety of broadband services to small and medium-sized businesses in several metropolitan markets."<sup>44</sup> LMDS operators such as Teligent, Winstar, NEXTLINK, and Advanced Radio Telecom already provide service within Verizon's region. For example, WinStar provides service in 38 of Verizon's 50 largest markets,<sup>45</sup> and Teligent provides service in 40 of Verizon's 50 largest markets.<sup>46</sup> Advanced Radio Telecom has launched LMDS service in Washington, DC, and plans to serve many additional markets in Verizon's territory.<sup>47</sup>

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<sup>39</sup> SBC Telecom, *About SBC Telecom*, <http://www.sbctelecom.com/About/>.

<sup>40</sup> New Paradigm Resources Group, *CLEC Report 2000*, 12th ed., Ch. 9 - SBC at 4.

<sup>41</sup> *Qwest and U S WEST Announce First National Market to Receive Integrated High-Speed Internet, Data and Voice Services*, PR Newswire (Nov. 2, 1999).

<sup>42</sup> Qwest, *DSL Services*, [http://cnms.qwest.net/dsl/qwdsi\\_avail.html](http://cnms.qwest.net/dsl/qwdsi_avail.html).

<sup>43</sup> A. Backover, *U S West Boldly Enters 'Foreign' Realm Smallest Baby Bell to Battle Industry Giant SBC on its Turf in Four California Markets*, *The Denver Post* at C-01 (May 11, 2000).

<sup>44</sup> *Broadband Today* at 29.

<sup>45</sup> New Paradigm Resources Group, Inc., *CLEC Report 2000*, 12th ed. Ch. 9 - WinStar Communications at 15-22.

<sup>46</sup> *Id.* Ch. 9 - Teligent, Inc. at 10-13.

<sup>47</sup> Advanced Radio Telecom Press Release, *Advanced Radio Telecom Launches Wireless IP Networks in Phoenix* (June 30, 2000).

32. DBS is rapidly improving its broadband capabilities. Hughes has announced that, in the fourth quarter of 2000, it will begin providing two-way broadband capabilities for its high-speed satellite Internet service, DirecPC, which will have upstream speeds of between 128Kbps and 256Kbps, and downstream speeds of over 40Mbps.<sup>48</sup> Hughes already has agreements with AOL and Juno to support these companies' broadband platforms, AOL Plus and Juno Express.<sup>49</sup>

33. Sprint and WorldCom have made significant investments to provide broadband wireless access.<sup>50</sup> WorldCom is testing its MMDS offerings in five markets;<sup>51</sup> its service, Warp 310, offers Internet access at 310kbps upstream and downstream for \$39.95 a month.<sup>52</sup> WorldCom recently announced that it was filing "its first round of applications for licensing authority to offer broadband fixed wireless services in more than 60 markets

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<sup>48</sup> Hughes Network Systems Press Release, *Hughes Network Systems Announces Upcoming Two-Way DirecPC Satellite Internet Service* (Apr. 27, 2000).

<sup>49</sup> *Id.*; Hughes Network Systems Press Release, *Juno and Hughes Network Systems Form High-Speed Satellite Access Relationship* (July 10, 2000).

<sup>50</sup> In March 1999, MCI WorldCom invested \$200 million in four MMDS providers – CAI, CS Wireless, Wireless One, and People's Choice. *MCI WorldCom's Wireless Cable Plans Seen Widening Broadband Options*, Communications Daily (Mar. 31, 1999). See *MMDS Provider People's Choice TV Merging Into Sprint*, Telecommunications Report Daily (Apr. 12, 1999). In April 1999, Sprint announced an agreement to merge with People's Choice TV, and said it would use PCTV's MDS licenses to provide wireless broadband services as a part of its Sprint ION offering. Sprint stated that: "Along with recently announced plans to build asymmetrical digital subscriber lines (ADSL) in 35 major markets by the end of the year, the purchase offers Sprint another way to deliver Sprint ION broadband services to business and residential customers." *Id.*

<sup>51</sup> Jackson, Miss., Baton Rouge, La., Memphis, Tenn., Boston, Mass., and Ft. Worth/Dallas, Texas. MCI Worldcom Press Release, *MCI Worldcom Adds Dallas to 'Fixed Wireless' Service Trials* (Apr. 5, 2000).

<sup>52</sup> MCI WorldCom Press Release, *MCI Worldcom Announces 'Fixed Wireless' Service Trials* (Mar. 7, 2000).

nationwide,” including many major markets within Verizon’s region.<sup>53</sup> Sprint has launched commercial MMDS service in Phoenix and Tucson;<sup>54</sup> its service, “Sprint Broadband Direct,” provides upstream speeds of 1-2 Mbps and downstream speeds of up to 5Mbps for \$39.95 per month.<sup>55</sup> Nucentrix has also begun offering high-speed Internet access via MMDS licenses.<sup>56</sup> AT&T recently launched its broadband wireless access with “Project Angel” in Fort Worth, Texas.<sup>57</sup> It has quickly attracted two thousand subscribers.<sup>58</sup> AT&T plans an aggressive build-out, expecting to make the service available to some 15 million homes in 40 markets by the end of 2002. “About half of the U.S. is covered with cable,” said Michael Keith, chief executive of AT&T’s fixed wireless division. “We’re going after the other half.”<sup>59</sup>

## SUMMARY

34. Although broadband access service is in its infancy, it promises to have far-reaching consequences in improving communications, increasing business efficiency, empowering consumers, and bringing the benefits of the Information Age to every segment of our population. Rapid development of this new infrastructure technology is

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<sup>53</sup> WorldCom Press Release, *WorldCom Seeks Broadband Fixed Wireless Authority* (Aug. 14, 2000) (the cities within Verizon’s region that WorldCom will enter include Boston, Providence, Pittsburgh, Buffalo, and Norfolk, VA).

<sup>54</sup> Sprint Press Release, *Sprint Launches First Broadband Wireless Market in Phoenix* (May 8, 2000).

<sup>55</sup> *Id.*

<sup>56</sup> The company’s two-way wireless Internet access service offers businesses speeds of up to 768Kbps upstream and 1.5 Mbps downstream. Nucentrix, *Products and Services – Wireless Internet Access*, <http://www.nucentrix.com/site/internet/products/wireless.html>.

<sup>57</sup> AT&T Corp., *Technology: Angel Takes Flight* (May 18, 2000) at <http://www.att.com/technology/features/0005fixedwireless.html>.

<sup>58</sup> AT&T Press Release, *AT&T Wireless To Offer Residential Broadband Service in Four New Cities* (July 19, 2000).

<sup>59</sup> John Borland, *AT&T’s “Project Angel” Spreads Its Wings*, CNET News (Mar. 22, 2000), <http://news.cnet.com/news/0-1004-200-1581606.html>.

likely to deliver very high social returns. “Our challenge today is to make broadband happen and make it happen fast.”<sup>60</sup> This is the appropriate focus across a range of public policy issues in broadband, including the extant matter.

35. The proposed merger creating New NorthPoint is likely to:

- a) substantially accelerate broadband deployment to U.S. homes and businesses;
- b) improve DSL service by integrating two highly complementary firms;
- c) provide infrastructure and momentum for an open network to rival the closed network of cable modem broadband access;
- d) facilitate development of broadband content, stimulating demand for DSL;
- e) help to create an alternative subscription video delivery platform to cable TV.

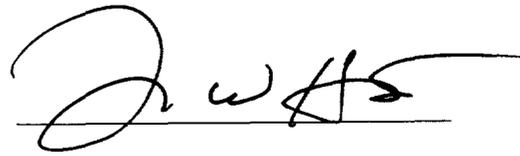
36. The New NorthPoint venture produces social benefits in multiple dimensions while risking anti-competitive consequence in none. The merger will bring valuable synergies, intensifying rivalry between DSL providers in a nation-wide competition with a very large number of DLECs, CLECs, ILECs, and IXCs. Perhaps more important is the enhanced rivalry the merger is likely to spark between DSL and cable modem service, the dominant broadband access medium. DSL’s open system can and should challenge the closed cable modem model. The competitive attack on cable broadband is not limited to data, however, as the new firm would have the ability and incentive to aggressively promote a new platform for video content via the Internet. This would spur competition both in the upstream market for content distribution and in the downstream market for customers. These sizeable social benefits will be augmented, and policed, by other players in the broadband access space, including cable, fixed wireless providers and

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<sup>60</sup> Remarks of Deborah A. Lathen, Chief, Cable Services Bureau, Federal

satellite access systems. Finally, the pro-competitive terms of this combination are ensured by the separate and independent nature of New NorthPoint, as well as the regulatory structure mandating open access to ILEC facilities for firms wishing to enter local telecommunications markets to provide voice or data.

I declare, under penalty of perjury, that the foregoing is true and correct.

A handwritten signature in black ink, appearing to read 'T. W. Hazlett', written over a horizontal line.

Thomas W. Hazlett

Executed on: August 15, 2000

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Communications Commission, *The Mind's Eye* (Nov. 9, 1999), at 7.

## Attachment 1

### **Thomas W. Hazlett: Short Biography (August 2000)**

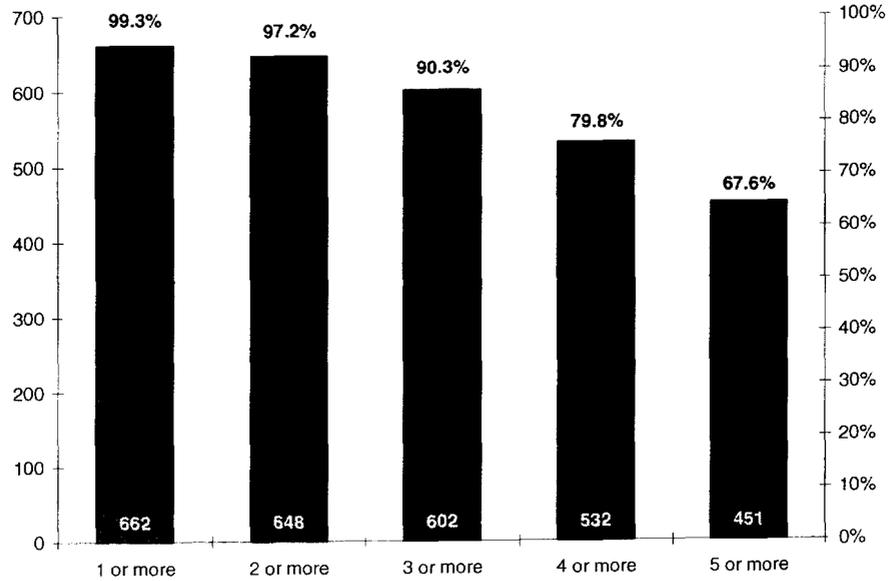
Thomas W. Hazlett is a Resident Scholar at the American Enterprise Institute for Public Policy Research in Washington, D.C. From 1984 through June 2000 he taught economics and finance at the University of California, Davis, where he last served as Professor of Agricultural & Resource Economics and Director of the Program on Telecommunications Policy. In 1990-91 he was a Visiting Scholar at the Columbia University Graduate School of Business, and in 1991-92 he served as Chief Economist of the Federal Communications Commission in Washington, D.C. He currently serves as Senior Adviser to Arthur Andersen, the international accounting and financial services firm, and is a columnist for *Forbes ASAP*.

Dr. Hazlett has written for such general interest periodicals as the *Wall Street Journal*, *New York Times*, *Newsday*, *Los Angeles Times*, *Chicago Tribune*, *Sacramento Bee*, *San Francisco Chronicle*, *The Economist*, *Reason*, *Reader's Digest*, *Barron's*, *Across the Board*, *Chief Executive*, *The American Enterprise*, *The Weekly Standard*, *Forbes*, the *National Post* (Toronto) and *The New Republic*. He wrote the "Selected Skirmishes" column in *Reason Magazine*, 1989-2000, and previously served as a contributing editor to *Harper's*. His academic research has been published in scholarly journals and law reviews, including the *Journal of Law & Economics*, *Journal of Financial Economics*, *Economic Inquiry*, *Southern Economic Journal*, *Review of Industrial Organization*, *Journal of Legal Studies*, *Columbia Law Review*, *Journal of Regulatory Economics*, *Supreme Court Economic Review*, *Business & Politics*, *Hastings Law Journal*, *The Public Interest*, *International Journal of the Economics of Business*, *Public Choice*, *Regulation*, *Managerial & Decision Economics*, *Yale Journal on Regulation*, *Telecommunications Policy*, *Journal of Broadcasting & Electronic Media*, *Harvard Journal on Law & Public Policy*, *Connecticut Law Review*, *Michigan Telecommunications and Technology Law Review*, *Federal Communications Law Journal*, *Cornell Journal of Law & Public Policy*, and the *University of Pennsylvania Law Review*. He has provided expert testimony in federal and state courts, before the Department of Commerce, General Accounting Office, and the Federal Communications Commission, and before committees of Congress. In addition, he has served as a consultant to numerous private firms, the State of California, Congressional Budget Office, federal agencies, municipal governments and foreign governments.

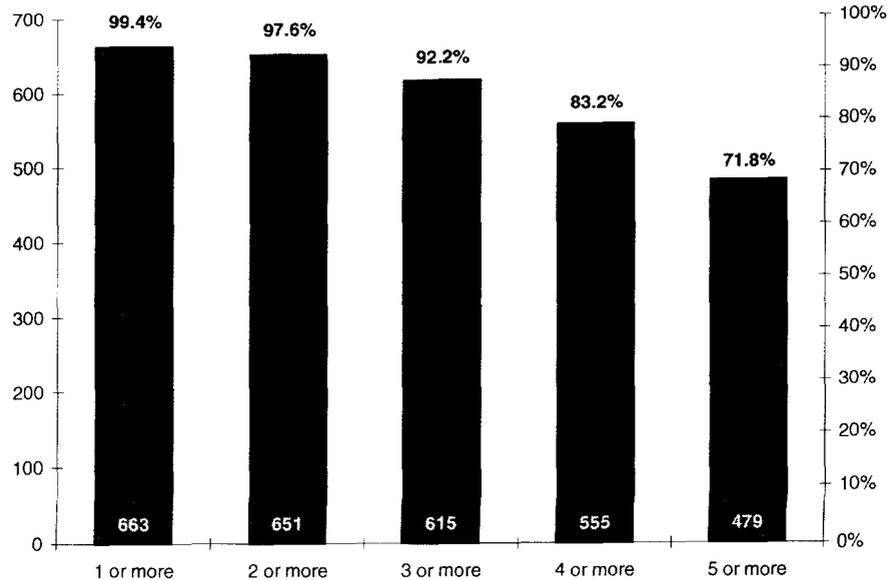
Professor Hazlett is an internationally recognized expert on government regulation of business, specializing in the area of telecommunications policy. He received his doctorate in economics from UCLA in 1984, and is a member of the Mont Pelerin Society, a Senior Research Associate of the Columbia Institute for Tele-information, and a Senior Fellow of the Liberal Institute in Prague, Czech Republic. In 1990-91 he was awarded the Wriston Citicorp Fellowship, a prize awarded annually by the Manhattan Institute to a young scholar working in an important area of public policy. His book (with Matthew L. Spitzer), *Public Policy Toward Cable Television*, was published by the MIT Press in November 1997.

Attachment 2

**Number of Facilities-Based Data CLECs in 667 Verizon/NorthPoint  
Overlap Central Offices (Not Including Cable)**



**Number of Facilities-Based Data Competitors in 667 Verizon/NorthPoint  
Overlap Central Offices (Including Cable)**

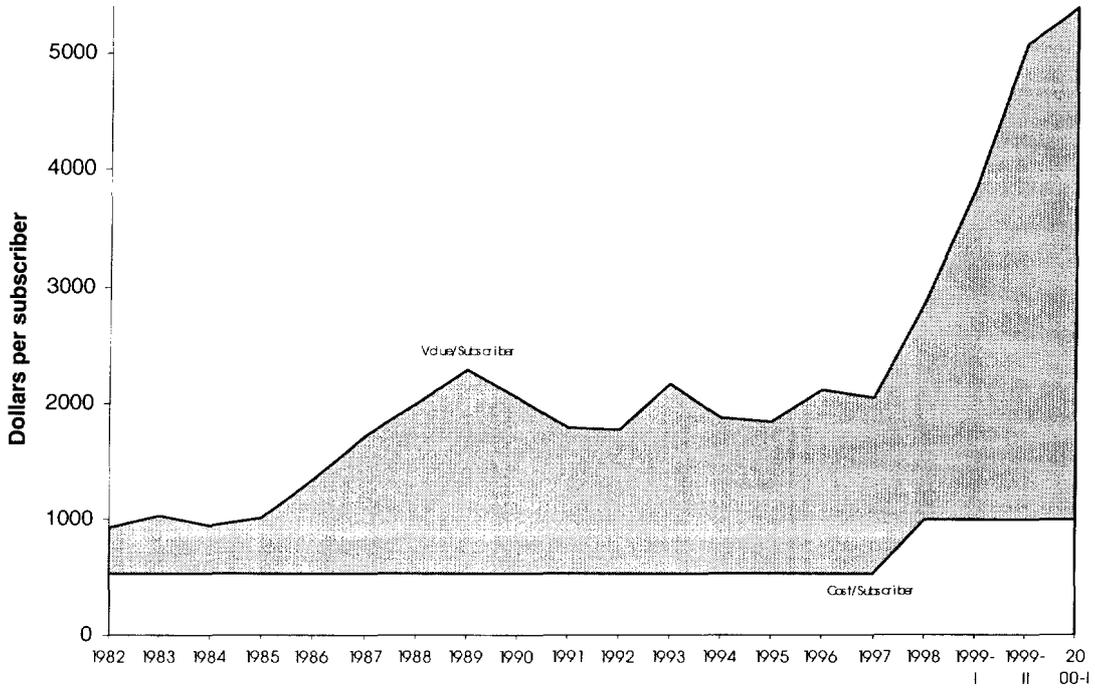


Attachment 3

<b>Estimated Residential DSL and Cable Modem Subscribers, 2Q00</b>	
<i>Cable Modem</i>	<i>Subscribers</i>
Excite@Home	1,100,000
Road Runner	912,000
Other	258,000
<b>Cable Modem Total</b>	<b>2,270,000</b>
<i>DSL</i>	
Verizon	176,000
BellSouth	59,200
Qwest	140,000
SBC	319,200
Rhythms	8,990
Covad	40,020
NorthPoint	17,980
Other	15,559
<b>DSL Total</b>	<b>776,949</b>
<b>Total Residential Broadband</b> (excludes satellite, fixed wireless)	<b>3,046,949</b>
Cable	75%
DSL	25%
Sources: TR Daily, <i>NCTA Reports Fast Growth in Cable Modem, Telephony Rollouts</i> (July 26, 2000); XDSL.com, <i>TeleChoice DSL Deployment Summary</i> (Aug. 9, 2000) at <a href="http://www.xdsl.com/content/resources/deployment_info.asp">http://www.xdsl.com/content/resources/deployment_info.asp</a> ; Qwest Press Release, <i>Qwest Communications Reports Strong Revenue and EBITDA for Second Quarter 2000</i> (July 19, 2000); Verizon Press Release, <i>Verizon Communications Announces Second Quarter Results</i> (August 8, 2000); BellSouth Press Release, <i>BellSouth Second Quarter EPS Increases 9.8%</i> (July 20, 2000). SBC Communications, <i>Investor Briefing</i> (July 20, 2000) at <a href="http://www.sbc.com/Investor/Financial/Earning_Info/docs/2QIB.pdf">http://www.sbc.com/Investor/Financial/Earning_Info/docs/2QIB.pdf</a> .; Rhythms Press Release, <i>Rhythms Netconnections Announces Second Quarter Results</i> (July 25, 2000); Covad Press Release, <i>Covad Communications Announces Record Second Quarter Results</i> (July 26, 2000); NorthPoint Press Release, <i>NorthPoint Reports Second-Quarter Results</i> (August 8, 2000). NOTE: Residential DSL numbers have been calculated by multiplying TeleChoice's second quarter 2000 percentages of residential lines for ILECs and CLECs/IXCs by second quarter 2000 DSL deployment figures for individual entities.	

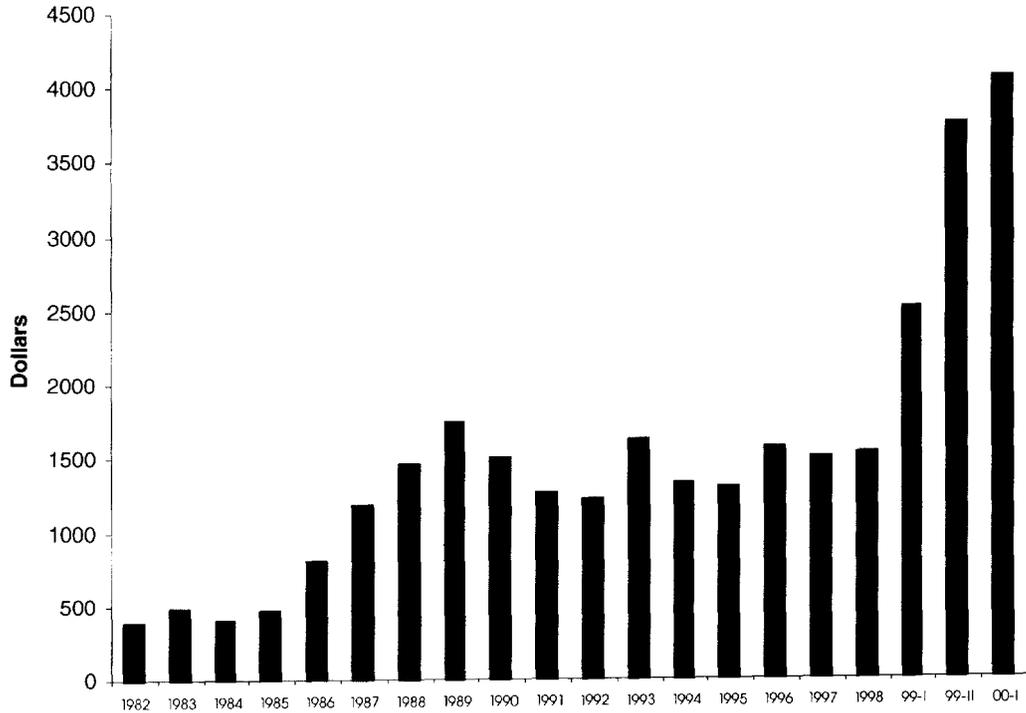
Attachment 4

**Cable TV System Values & Capital Costs**



Attachment 5

**Economic Rent per Cable Subscriber  
(Value/Sub - CapEx/Sub)**



\* 99-I is first half of 1999.  
99-II is second half of 1999.  
00-1 is first half of 2000.