ALTS

ASSOCIATION FOR LOCAL TELECOMMUNICATIONS SERVICES

An ALTS Analysis:

Local Competition Policy & The New Economy

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Introduction

Nearly five years ago, Congress passed the Telecommunications Act of 1996 (The Act). This groundbreaking law ended the 100+ year local telecommunications monopoly held by the Regional Bell Operating Companies (RBOCs) or Baby Bells. The immediate result of The Act was the creation of a new breed of company called competitive local exchange carriers (CLECs). The nascent CLEC industry competes with the Baby Bells in the $100+ billion local telecommunications market, providing voice and data services to business and residential consumers alike. Five years after the passage of The Act, CLECs have competed vigorously with the RBOCs and now claim 6% to 8% of the local telecommunications market.[1] These emerging competitors have ignited the explosive growth of the Internet, promoted the deployment of high-speed broadband services, and contributed to the nation's longest economic expansion in history.

However, bringing true competition to the marketplace has been an uphill battle. For over two years, the RBOCs sued to block implementation of The Act. Furthermore, CLECs continue to face anti-competitive barriers that have significantly delayed CLECs' efforts to bring competition to local markets. The three greatest barriers that stymie full, effective competition are: (1) the failure of the incumbent local exchange carriers (ILECs)[2] to open their networks to competition, (2) the failure of building owners to open their buildings to competitors, and (3) the failure of municipalities to approve entry quickly and on a competitively-neutral basis. In addition, restricted capital markets in the last year have forced many CLECs to scale back their expansion plans.

The purpose of this paper is to document the link between local competition policy and the explosion of the Internet and the nation's economic growth. The paper will also explore the barriers that continue to impede competition, especially for residential consumers. Finally, this paper will suggest proposals that Congress and policymakers across the country should consider to further promote competition.

The Act, the Internet & Economic Growth

In passing The Act, Congress intended that the United States would lead the world in Internet accessibility and placed a priority on the deployment of advanced telecommunications services (broadband) as a means to economic growth. Congress chose to promote competition for local

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[1] Federal Communications Commission (FCC), *FCC Releases Data on Local Telephone Competition*, 4 December 2000, http://www.fcc.gov/Bureaus/Common_Carrier/Reports/FCC-State_Link/IAD/lcom1200.pdf & New Paradigm Resources Group (NPRG), *CLEC Report 2001 (13th edition),* December 2000.

[2] The ILECs are the incumbent carrier in a particular service region (e.g., Verizon, BellSouth, etc.).

telecommunications services as the best engine for deployment of these advanced technologies. Indeed, the House Report from 1995 notes that the impending law would "promote competition and reduce regulation in order to secure lower prices and higher quality services for… consumers and **encourage the rapid deployment of new communications technologies**."[3] Further, realizing the importance of the Internet, Congress instructed the FCC and state regulatory bodies to "encourage the deployment on a reasonable and timely basis of advanced telecommunications capability to all Americans"[4]. Congress also focused especially on the deployment of advanced services in rural and high-costs areas. Section 254 of The Act specifies that "consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications..."[5]

The Internet

The Act has been quite successful in promoting the deployment of advanced technologies and the expansion of the Internet. When The Act was passed, most Internet users were large institutions (e.g., universities, libraries, etc.). However, The Act dramatically altered the Internet landscape. CLECs set out to serve an untapped and underserved market among Internet Service Providers (ISPs) and small and medium-sized businesses. These two customer groups required new technologies that could be customized and rapidly deployed. Because the ILECs were unwilling or unable to cater to the needs of ISPs and small business, CLECs found a market niche in which their superior technology, enhanced time-to-market and customized products were enthusiastically embraced.

CLECs also provide higher quality service to ISPs. Rural Northern California is a case in point. Peter Engdahl, President of SnowCrest, an ISP in northern California notes that his ILEC was "unwilling to add more services in cities into which [SnowCrest] needed to expand… [t]he presence of CLECs has brought about large increases in competition in California which gives consumers greater choice, lower prices and faster access to new technologies." Engdahl goes on to note that in his hometown, Mt. Shasta, SnowCrest and the RBOC were the only ISP available until a CLEC entered the market allowing non-local ISPs to establish service. Today, Mt. Shasta has as many as 20 ISPs from which residents and businesses may obtain service.[6]

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[3] U.S. House of Representatives, *Report together with Additional & Dissenting Views [to accompany HR.1555]*, 24 July 1995, p. 47.

[4] The principal section of The Act concerning advanced telecommunications services is Section 706, Pub.L. 104-104, Title VII § 706, Feb. 8, 1996, 110 Stat. 153, reproduced in the notes under 47 U.S.C. § 157.

[5] 47 U.S.C. §254(b)(3).

[6] Testimony of Robert Taylor, President & CEO, Focal Communications before the House Subcommittee on Telecommunications Trade & Consumer Protection, 22 June 2000. (Appendix C: Remarks of Peter Engdahl, President, SnowCrest), http://www.alts.org/Filings/062200BobTaylorTestimony.pdf

Additionally, Brad Jenkins, President of JPS.net, the largest ISP in Northern California outside San Francisco notes that his ISP uses CLEC "networks to reach a lot of rural communities" and that without such new networks, "rural communities like… Laytonville, Mojave, and Yosemite would pay per-minute charges to reach the nearest larger city."[7]

The United States Internet Service Providers Association (USISPA)[8] further describes the dilemma many ISPs have faced when attempting to secure the proper facilities to expand and grow their businesses. The Association notes that ISPs have been poorly served by the ILECs and that "only the CLECs have shown any interest in serving ISPs. Moreover… CLECs' services and network facilities are far superior to comparable ILEC services and facilities prior to the enactment of the 1996 Telecommunications Act."[9]

A survey by the New Networks Institute (NNI) also points to the value to the Internet added by competitors. In it's *Summary Report of the ISP Survey*, NNI notes that "only 8% of ISPs… gave the Bell an overall passing grade (above 6.5 out of a possible 10)… on a scale of one to ten, the survey respondents gave the Bells an overall average of just 3.7, a seriously failing grade."[10] Prior to the enactment of The Act, the ISP industry struggled to grow under the weight of inadequate facilities and services. NNI goes on to note that those [ISPs] who use a CLEC gave the companies almost **double** the rating of their LEC counterparts."[11]

The investment house Credit Suisse First Boston (CSFB) also notes the importance of CLECs to the Internet. CSFBs equity research on telecom services notes, "CLECs should be viewed as Internet 'enablers' because they supply last-mile broadband data connectivity and host various data services. For many business customers, these services were unknown or unavailable prior to the advent of the CLEC sector."[12]

Both the ISP and CLEC industries are characterized by forward-looking start-ups and both industries rely on the others' end users and communications networks for a major portion of their operations. **Today, CLECs carry approximately 60% of local dial-up ISP traffic[13].** It is a symbiotic relationship that has led to increased competition in the two industries and has greatly impacted the virtual explosion of the Internet in the United States.

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[7] Xpress Press, *Proposed CPUC Decision Puts ISPs and Internet Customers at Risk* (13 November 2000), http://www.pacwest.com/company/newstand/newstories/prcpuc.cfm

[8] USISPA is a coalition of independent Internet Service Providers (ISPs), ISP trade associations and competitive suppliers. http://www.usispa.org/

[9] USISPA Press Release, *USISPA Says Focus of Reciprocal Compensation Debate Should Be on Internet & Consumers*, 19 September 2000, http://www.usispa.org/media/article7.html

[10] New Networks Institute (NII), *Summary Report of the ISP Survey*, 4 April 2000, p. 3, http://newnetworks.com/ispresults.pdf

[11] Ibid, p. 4.

[12] Credit Suisse First Boston (CSFB), *Telecom Services – CLECs*, 5 January 2000, p.8.

[13] NPRG.

Broadband Deployment

For many small businesses that wanted to obtain high-speed Internet services, a T-1[14] from the local RBOC was often the only available option. However, the cost of a T-1 can exceed $1,000 per month. Additionally, many businesses have no need for such a large and costly connection. With the introduction of digital subscriber line (DSL) by many CLECs, small businesses and consumers may now obtain high-speed Internet access via DSL for as little as $29.95 per month (residential) to a few hundred dollars per month (business).

CLECs have led the way in deploying high-speed services. CLECs like Covad, NorthPoint Communications, Rhythms and New Edge Networks, are among the competitive carriers bringing DSL to businesses and consumers and now claim 23% of the DSL market.[15] These companies specialize in deploying equipment in ILEC central offices (COs) that channel enormous amounts of data over the telephone companies' copper wires. As of 3Q00, CLECs had 8,200 DSL-equipped COs while the ILECs had 4,979 and the long-distance carriers (IXCs) had 2,050.[16] **As a result of such an aggressive rollout of facilities, advanced, high-speed broadband services are now available to over 50% of American households**. Additionally, analysts predict over 17 million customers will subscribe to DSL by year-end 2004.[17]

Without the advent of the CLEC sector, it is likely that many of the technologies fueling Internet growth may have been indefinitely delayed. Fearing they would cannibalize their existing T-1 revenue stream, the RBOCs delayed introduction of cheaper DSL technology. The Council of Economic Advisors (CEA) noted in the 1999 *Economic Report of the President* that:

> Although DSL technology has been available since the 1980s, only recently did local telephone companies begin to offer DSL service to businesses and consumers seeking low-cost options for high-speed telecommunications. The incumbents' decision finally to offer DSL service followed closely the emergence of competitive pressure from… the entry of new direct competitors attempting to use the local-

[14] A T-1 line provides connectivity of up to 1.5 mbps.
[15] TeleChoice, *TeleChoice DSL Deployment Summary*, (13 November 2000), http://www.xdsl.com/content/resources/deployment_info.asp
[16] Ibid.
[17] TeleChoice, *TeleChoice Expects U.S. DSL Market to Reach 17.4 Million by End of 2004*, (24 January 2001), http://www.xdsl.com/content/tcarticles/wp012401.asp

competition provisions of the Telecommunications Act of 1996 to provide DSL over the incumbents' facilities.[18]

The competition in broadband markets is intensifying each month. The DSL Forum estimates there are 2.5 million subscribers to DSL in the United States. SBC is installing 3,000 to 4,000 lines per day. America On-Line (AOL) is receiving more than 5,000 DSL orders per week through marketing agreements with Verizon and SBC.[19] Both CLECs and the Bell Companies are working overtime to meet the enormous demand for broadband services.

Economic Growth

Technologies such as broadband are examples of the drivers that have fueled the explosive economic growth of the last decade. Federal Reserve Chairman Alan Greenspan, while not singling out The Act or any other legislative initiative, has attributed much of the recent productivity growth and deepening of capital markets to the communications and information technology (IT) industries. He notes that "it is the growing use of information technology throughout the economy that makes the current period unique… the full value [of which]… could be realized only after ways had been devised to link computers into large-scale networks."[20]

Aside from contributing to the economic growth associated with the rise of the Internet, CLECs have also contributed to the economic expansion through their capital investment in infrastructure and equipment and their demand for skilled labor. Between 1997 and 2000, CLECs spent in excess of $55 billion on capital investments[21] – infrastructure that will serve the booming demand for voice and data telecommunications services. And, as of 2000, CLECs employed 94,000 workers.[22] Most notable is that these jobs are higher paying and require greater education and skill-levels than the traditional workforce.

With carriers across the board rushing to deploy the full array of broadband services, Governors across the country have been actively promoting the goal of broadband deployment as a means to advancing the economic welfare of their respective States. In his 2001 Inaugural Address, North Dakota Governor John Hoeven noted that the State "will provide high-speed Internet access capabilities to 194 communities… For business and education, this is the infrastructure upon which our next level of economic

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[18] Council of Economic Advisers, *Economic Report of the President*, February 1999, pp. 187-188, http://w3.access.gpo.gov/usbudget/fy2000/pdf/erp.pdf

[19] Jade Boyd, 'Business Could See DSL Rise in 2001,' *InternetWeek*, 8 January 2000, p. 11.

[20] Remarks by Chairman Alan Greenspan, *Technology Innovation and its Economic Impact,* before the National Technology Forum, St. Louis, Missouri (via videoconference), 7 April 2000.

[21] NPRG, C*LEC Report(s) 1997, 1998, 1999, 2000 & 2001.*

[22] NPRG, *CLEC Report 2001 (13th Edition).*

growth will come."[23] In the Arkansas 2001 State of the State address, Governor Mike Huckabee committed to devoting the resources that will "build a strong technology infrastructure so high-speed connectivity is accessible to every Arkansan, providing the backbone for recruiting high-tech businesses" to the State.[24] And in his annual State of the State address, Wyoming Governor Jim Geringer cited broadband connectivity as a way to "help increase the quantity of jobs and the quality of income" and as a means to "foster and sustain growth throughout Wyoming."[25]

CLECs have focused on bringing DSL, fixed wireless, and fiber technologies to the market. The new telecom networks built by the CLECs have fueled the explosive increase in Internet connectivity and economic growth. As Texas Public Utility Commissioner Brett Perlman noted, "providing high quality telecommunications infrastructure will be the key to Texas' economic growth in the 21st century. In particular, broadband deployment will become a primary driver of economic development in the Texas economy."[26] What is true for Texas is equally true for the nation as a whole.

Impediments to Fulfilling the Promise of The Act

Despite the progress made by CLECs, a number of impediments still frustrate the emergence of full and effective competition. These impediments to The Act limit the expansion of the Internet and the deployment of broadband technologies. The Federal Reserve Bank of Dallas notes "by some projections broadband will only [be subscribed to by] 15 percent of households by 2002. Although fast by historical standards, this pace limits the Internet's economic potential."[27] CLECs are deploying broadband infrastructure as rapidly as possible, and, as noted, broadband services are now available to over 50% of the nation's population. However, to fully achieve the gains associated with continued broadband deployment, the following remaining impediments must be overcome.

- ILECs have been unable or unwilling to open their markets to competition (despite their legal obligation to do so). **According to the FCC, after almost five years, the ILECs have opened their networks to competitors in only four[28] states.** CLECs have great

[23] Governor John Hoeven, '2001 Inaugural Address,' Bismarck, North Dakota, 9 January 2001. http://www.governor.state.nd.us/speeches/sos2001/InauguralAddress.htm
[24] Governor Mike Huckabee,'2001 State of the State Address,' Little Rock, Arkansas, 9 January 2001. http://www.state.ar.us/governor/state_of_state_2001/state_of_state_2001_text.html
[25] Governor Jim Geringer, '2001 State of the State Address,' Cheyenne, Wyoming, 10 January 2001. http://www.state.wy.us/governor/press_releases/2001/january_2001/sos2001.html
[26] 'PUCs Perlman Sees Broadband As Crucial to Development of Texas Economy', *Texas CLEC Bulletin*, Volume 2, Issue 11 (November 1999), http://www.puc.state.tx.us/about/perlmaninterview.cfm
[27] Meredith Walker, 'Speeding Up the Broadband Wagon,' *Southwest Economy,* Federal Reserve Bank of Dallas, Issue 6 (November/December 1999), http://www.dallasfed.org/htm/pubs/swe/11_12_99.html#Anchor-Speedin-16827
[28] New York, Texas, Kansas & Oklahoma.

difficulty obtaining the essential unbundled network elements (UNEs) that The Act requires the RBOCs to provide. As a result, competition has not developed as quickly as many had hoped.

- Building owners refuse to give tenants access to high-quality, affordable telecommunications services provided by competitors. Many building owners give exclusive access to telecom companies they own, and bar entry by unaffiliated competitors.

- Municipalities overregulate competitors and charge CLECs excessive fees. Whether unintentional or not, the cities' actions contribute to perpetuating the ILEC monopoly.

Incumbent Local Exchange Carriers (ILECs)

Handed the advantage of starting with 100% market share, the ILECs have implemented a three-part strategy to thwart competition. First, they used the courts to stay enforcement of The Act. This initial strategy succeeded in creating tremendous uncertainty in the marketplace concerning such important matters as pricing, unbundling and collocation requirements.

Second, they have delayed opening their networks to competitors. They have been extremely slow to provision loops, and they have often created significant obstacles to allowing competitors to collocate equipment in the central office. The most common description of the behavior of the incumbents is that they engage in "strategic incompetence." They simply refuse to devote the resources necessary to solve the basic provisioning problems that stall competitors. Another CLEC executive put it differently: he says, "the RBOCs treat competitors the same way that they treat their customers – badly."

Third, the incumbents are reengineering the network to make it technically impossible for competitors to collocate their equipment. They design their networks to work around the pro-competitive measures of The Act, blocking CLEC access to consumers.

The following anecdotes represent only a handful of the anti-competitive practices CLECs face when interacting with the ILECs[29]:

- Delay tactics on the part of the ILECs when CLECs attempt to collocate equipment and/or obtain loops to provision service.

[29] For extended examples, see Appendix A (Barriers to Competition: ILECs).

- Non-cost based and disparate pricing on unbundled network elements (UNEs).

- Inaccurate or incomplete information regarding available facilities or loop qualification.

- Discriminatory treatment of CLECs *vis a vis* affiliated ILEC data subsidiaries (e.g., preferential pricing, etc.)

To place the ILECs in compliance with the letter and spirit of The Act and to promote the competition intended by The Act, Congress should consider the following proposals:

- Impose greater enforcement penalties on the ILECs for failure to open their networks to competitors.

- Separate the ILECs into wholesale and retail units as under Senator Hollings' bill in the 106th Congress (S.1312), *The Telecommunications Competition Enforcement Act of 1999.*

- Require that all combinations of network elements and full functionality of the loop be provided to competitors (line sharing & line splitting).

- Extend collocation requirements to include multifunctional equipment, equipment used to provide advanced services and at remote terminals.

- Affirm the FCCs UNE forward-looking pricing methodology.

- Permit interconnection among RBOC-collocated competitive carriers.

Regulators, the Courts and Congress must begin advocating stronger enforcement penalties for non-performance and non-compliance with The Act. The Act was, in part, based upon the theory that the carrot of long distance entry would be sufficient incentive to convince the RBOCs to open their local markets. After five years, regulators must consider that the lure of the carrot may not be enough and begin considering stronger sticks.

Building Owners

For the millions of Americans who live and work in multi-tenant environments (MTE), securing access to choice in local telephone and Internet service has been a great disappointment. According to the Smart Buildings Policy

Project (SBPP)[30], less than 5% of commercial tenants, and less than 1% of residential tenants have access to competitive high-speed telecommunications services.[31] These tenants live and work in the 20 million apartments, 3.5 million hotels and 750 million commercial buildings across the United States.[32]

The following anecdotes represent only a few among thousands of challenges faced by CLECs in attempting to bring competitive choice to consumers in MTEs[33]:

- Outright refusal of access to a building by the landlord despite a tenant's request for service.
- Auctioning of building access rights to the highest bidder, generally leading to the deep pockets of the incumbent outbidding all others.
- Denial of access even after a CLEC has installed equipment and initiated service, resulting in stranded capital assets.
- Requiring tenants to use an exclusive provider chosen by the landlord in which the landlord often has a vested financial interest.

Non-discriminatory access to MTEs does have precedent in American public policy. In October 1998, in response to what the United States Government viewed as anti-competitive trade practices by Japan, the U.S. encouraged the Government of Japan (GOJ) to:

> Establish rules that facilitate access to privately owned buildings, particularly multi-dwelling units, to ensure that cable TV and new telecommunications competitors can reach the same customers as the incumbent carrier. For example, the GOJ should consider setting rules on demarcation points for telecommunications carriers to access buildings and prohibiting owners of multi-dwelling units from denying a tenant access to any telecommunications or cable TV service.[34]

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[30] The SBPP is a growing coalition of telecommunications carriers, equipment manufacturers, and organizations that support nondiscriminatory telecommunications carrier access to tenants in multi-tenant environments. http://www.buildingconnections.org/

[31] *SBPP,* http://www.buildingconnections.org/pages/get_the_facts.html

[32] NPRG, *BLEC Report 2000 (1st Edition),* p. 1.

[33] For extended examples, see Appendix B (Barriers to Competition: Building Owners).

[34] Office of the United States Trade Representative (USTR), *Submission by the Government of the United States to the Government of Japan Regarding Deregulation, Competition Policy, and Transparency and Other Government Practices in Japan,* 7 October 1998, p. 10.

In October 2000, the Federal Communications Commission (FCC) adopted an Order[35] in the Competitive Networks proceeding that (1) prohibits exclusive contracts between competitive carriers and commercial building owners, (2) extends outward the point of demarcation between the ILEC and the building owners, (3) requires local utilities to provide non-discriminatory access to building conduits and rights-of-way (ROW), and (4) prohibits restrictions that impair use and/or maintenance of external antennas on property.

This FCC Order sends an extremely significant message to building owners that exclusive contracts between building owners and telecom providers will not be tolerated. The FCCs Order, however, falls short on two fronts. First, it does not cover residential apartment buildings; the Order only bans exclusive contracts for commercial tenants. Second, the FCC refused to take the next step of imposing penalties on building owners that deny access to CLECs. Once again, the FCC has announced an affirmatively pro-competitive policy but has left the enforcement of that policy uncertain. ALTS is currently monitoring the impact of the FCCs decision on building owners to determine whether further action, either by the FCC or by Congress, will be necessary to ensure that **all** tenants can benefit from The Act.

Additionally, in late 2000, the United States Congress passed report language that promotes non-discriminatory access for competitive carriers to rooftops of buildings owned or used by the Federal Government. ALTS expects that the Federal Government will comply with this directive from Congress and will serve as the model for the private sector by opening its doors to all competitors.

If building owners continue to bar tenants their right to choose, then Congress should once and for all, guarantee non-discriminatory access to the broad range of MTEs by competitive carriers. To remove the bottleneck in MTEs, which is preventing full and fair competition, Congress should consider the following proposal:

- Require building owners to provide non-discriminatory access to their buildings to all local competitors while at the same time protecting the security of the building and ensuring that competitors pay for the costs of installing equipment.

Without such action, the millions of businesses and consumers that live and work in commercial office buildings and residential apartment buildings will remain unable to choose their local telephone and Internet service providers. To realize the full potential of The Act, Congress must insure non-

[35] FCC, First Report and Order & Further NPRM, *In the Matter of Promotion of Competitive Networks in Local Telecommunications Markets*, WT Docket 99-217, FCC 00-366 (25 October 2000), http://www.fcc.gov/Bureaus/Wireless/Orders/2000/fcc00366.pdf

discriminatory access to MTEs so that all Americans may benefit from the fruits of competition.

Municipalities

To provide telecommunications services, CLECs require nondiscriminatory access to public rights-of-way. While CLECs must request such access, the incumbent often has such access already through its historic monopoly of the telephone network. CLECs must comply with the thousands of different regulatory regimes that exist at the local level all across the country even though many such regimes impose regulations on CLECs that are not imposed on the incumbent. As the Technology Alliance[36] notes, "Unfortunately, some public entities have begun to see their authority over the public rights-of-way not as something which can be fairly and equitably applied to encourage investment in their communities, but rather as a revenue source which can be auctioned off to the highest bidders."[37]

In addition, CLECs face excessive delay in having applications for access to rights-of-way approved. Such extensive approval intervals delay the deployment of equipment and facilities, introduces uncertainty into company business plans and investor confidence and acts as an overall barrier to competition.

Rights-of-way abuses also pose serious danger to the development of e-commerce and the Internet. Rights-of-way fees can often run up to 10% of carriers' revenues. The e-Freedom Coalition[38] notes that fees imposed by municipalities "drive up costs for consumers."[39] Additionally, the National Governors' Association (NGA) notes that "municipalities have moved away from cost-based fees; many of today's rights-of-way and franchise fees are indistinguishable from taxes."[40] Indeed, the Municipal Telecommunications Strategies Program (MTSP)[41] notes that rights-of way management could be an economic windfall, the MTSP notes that the "expansion [of telecommunications construction]... represents a potential source of new

[36] The Technology Alliance, based in Washington State, was founded in 1996 as a statewide consortium of technology-based businesses, Washington's leading research institutions, and high tech trade associations. http://www.technology-alliance.com/

[37] Technology Alliance, *Policy Initiatives to Increase the Availability of Advanced Telecommunications Services Throughout Washington State,* (January 1999), http://www.technology-alliance.com/publications/telecom99fullreport.htm

[38] The e-Freedom Coalition is an association of taxpayer groups, think tanks, and other organizations whose aim is to promote the growth and accessibility of the Internet. http://www.e-freedom.org/

[39] The e-Freedom Coalition, *The e-Freedom Coalition's Proposal to the Advisory Commission on Electronic Commerce*, (10 November 1999), http://www.ecommercecommission.org/document/138e-FreedomProposal.doc

[40] National Governors Association (New Economy Taskforce), *Telecommunications Tax Policies: Implications For The Digital Age*, (2 February 2000), http://old.nga.org/Pubs/IssueBriefs/2000/000202TeleCom.asp

[41] MTSP is a project of the Center for Civic Networking focusing on telecommunications issues involving local government. http://www.munitelecom.org/

revenue"[42]. With thousands of municipalities looking to profit from CLECs, the financial prospects are bleak.

The Technology Alliance notes that in California, Colorado and Hawaii, state regulators have the authority to preempt rights-of-way in local jurisdictions. Realizing the inherent benefits of state oversight of rights-of-way, in November 2000, the National Association of Regulatory Utility Commissioners (NARUC)[43] noted that it "supports and recommends State Commissions consider asserting jurisdiction over the rates, terms and conditions governing access to poles, ducts, conduits, and rights-of-way"[44]. In states where regulators lack appropriate oversight of rights-of-way, competition is beholden to local regulations which often violate The Act. Regulators at the State level must assert a greater role in rights-of-way management in order to ensure full competition develops.

The following anecdotes represent only a handful of the challenges CLECs face in attempting to access public rights-of-way[45]:

- Preferential treatment in the form of preferred access to rights-of-way for city affiliated carriers.
- Imposition of fees that in some instances run in the thousands of dollars per mile.
- Delays in approving applications for franchises or access to rights-of-way, extending to multiple years in some instances.
- Discriminatory treatment of CLECs *vis a vis* ILECs (preferential access, etc.).

To ensure that competitors are able to gain access to the necessary rights-of-way to provision service, Congress should consider amending §253 of The Act. This would allow the FCC to ensure fair and consistent public policy by:

- Ensuring expeditious intervals for approval of applications for access to rights-of-way.

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[42] Miles Fidelman, 'Is There Cash in Your Conduit?,' *Municipal Telecommunications Strategies Program* (July 1998), http://208.201.97.6/pubs/1998/july/civ-firstper-7-13-1998.html

[43] NARUC represents the governmental agencies that are engaged in the regulation of utilities and carriers in the fifty States and before the three branches of the Federal government and independent Federal agencies. http://www.naruc.org/

[44] NARUC, *Resolution Regarding Access to Poles, Ducts, Conduits, and Rights-of-Way*, (15 November 2000), http://www.naruc.org/Resolutions/2000_conv/tel_access_to_poles.htm

[45] For extended examples, see Appendix C (Barriers to Competition: Municipalities).

- Requiring franchise fees to be based on the actual costs of managing the rights-of-way, not on a percentage of carriers' revenues.

- Establishing non-discriminatory access on a competitively neutral basis (e.g., CLECs vs. ILECs).

- Barring cities from imposing unreasonable telecom and universal service requirements on telecom carriers.

- Ensuring that carriers have a private right of action in the courts to enforce §253.

- Establishing a process for obtaining rights of way across areas under federal jurisdiction (including marine areas) at cost based rates, without unnecessary restrictions.

Financial Constraints

There are financial impediments to fulfilling The Act as well. CLECs have been especially hard hit in the recent downturn in the equity markets. The *Bear Stearns CLEC Index* shows that as of December 22, 2000, the stock prices of public CLECs are **down 73.1% since the start of 2000**.[46] In the meantime, the Baby Bell Companies have grown even stronger by merging instead of competing with each other outside their home regions.

Due to the recent slowing trend in the economy, the capital markets have been virtually shut down to the CLEC sector and telecommunications as a whole. As seen in the precipitous drop in the Bear Stearns index, public and private market valuations have dropped to all time lows. Bear Stearns notes that "interest rate hikes built a 'Wall of Worry' and the high-yield markets deteriorated."[47] Severing access to capital in a market such as local telecommunications is a significant event given that, as Bear Stearns reiterates, "local network assets are the most time-consuming and costly to deploy".[48]

The current year will undoubtedly be a critical time for CLECs and the future of The Act. With some analysts predicting that half of CLECs will file for bankruptcy or face consolidation, Bear Stearns cautions investors to "watch bankruptcies, reciprocal compensation, access rate reform, M&A activity... building access... 4Q00 reporting and Fed interest rate cuts."[49] Congress

[46] James H. Henry, *2001 CLEC Investment Outlook,* Bear Stearns, December 2000, p. 3.
[47] Ibid, p. 6.
[48] Ibid, p. 7.
[49] Ibid, p. 23.

must carefully evaluate the potential effect of anti-competitive legislation (reciprocal compensation, interLATA data relief) which threatens an already fragile market. In addition, to further bolster investor confidence, Congress must act to correct the market place failures that are standing in the way of full, effective competition and preventing the full intent of The Act from being realized.

To overcome the enormous financial constraints, competitors face in building new networks, Congress should consider the following proposals:

- Establish programs to extend credit to eligible telecommunications carriers to finance the deployment of broadband services to eligible rural areas, such as HR.267 (*The Broadband Internet Access Act of 2001*) introduced by Representative Phillip English and S.88 (*The Broadband Internet Access Act of 2001*)[50] introduced by Senator John D. Rockefeller, IV.

- Establish programs authorizing the use of financial incentives for the deployment of broadband services to targeted rural and urban communities.

Pro-Competitive Measures

To further strengthen the mandate and force of The Act, there are additional pro-competitive measures that Congress may take:

- Provide competitors with an expedited, private dispute resolution process.

- Establish a post-271 enforcement and monitoring process.

- Require an annual Department of Justice (DOJ) report on telecommunications enforcement efforts.

- Establish a uniform operation support systems (OSS) measurement.

- Enact consumer service quality standards.

- Provide for a telecommunications wholesaler 'Lemon Law'.

While The Act has sown the seeds of competition, Congress must now fine-tune the progress of the last five years so that all Americans may benefit from the vision of The Act and its authors.

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[50] Office of Senator Jay Rockefeller, *Rockefeller Introduces Legislation to Encourage 'High Speed' Internet Access in Rural Communities,* (23 January 2001), http://www.senate.gov/~rockefeller/2001/pr012301.html

Conclusion

One of the most significant results of the passage of The Act has been its contribution to the explosive growth of the Internet and the resulting economic expansion in the United States within the last five years. Federal Reserve Vice Chairman Roger Ferguson, Jr. notes that the investments made by the communications industry along with broad deregulatory initiatives (such as the 1996 Act) are the two leading contributors to sustained domestic economic growth.[51]

However, the nation's telecom competition policy, and our nation's economic growth, are in great peril. The competitive community is in an extremely fragile state. Of the over 300 CLECs that began providing service since 1996, less than ten publicly traded CLECs are cash-flow positive today. Several CLECs have declared bankruptcy and several others are on the verge of failing. Not surprisingly, the nation's economy is slowing as well. Barron's notes that "the elephant in the room that now threatens to bring down the economy is the telecommunications industry".[52]

Our competition policy is at a critical juncture. The Act launched a new industry, but its long-term success depends upon whether or not the remaining barriers to competition are removed. The ILECs, building owners and municipalities all continue to present challenges to carriers attempting to enter the local market. Now is the time for policymakers to take additional steps to promote competition. Only then will investors have the confidence to contribute capital to the CLECs that are building our nation's digital future and spanning the "Digital Divide."

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[51] Remarks by Vice Chairman Roger W. Ferguson, Jr. Widener University, Chester, Pennsylvania, (6 April 2000), http://www.federalreserve.gov/BOARDDOCS/SPEECHES/2000/20000406.htm

[52] Jacqueline Doherty, 'Telecom Tightrope: Like Real Estate a Decade Ago, Telecom Threatens to Topple the Economy,' *Barron's Online, 8* January 2001.

Appendix A

Barriers to Competition: ILECs

1. In February 2000, the FCC launched an investigation into Bell Atlantic's (now Verizon) compliance with sections 251 and 271 of The Act. In March 2000, the FCC found that Bell Atlantic had used delay tactics in New York, where the FCC recently approved Bell Atlantic's application to provide long distance service. The FCC reports that, during January and February 2000, Bell Atlantic failed to process orders from local competitors in a proper manner. The company lost or mishandled electronically submitted orders which caused delay in or outright lack of order fulfillment. This in turn resulted in service delays to CLEC customers. In a settlement agreement with the FCC, Bell Atlantic paid $3 million to the U.S. Treasury because of its poor performance, with additional liability of up to $24 million.[53]

2. One of the most severe obstacles to CLECs provisioning service in a timely manner is the ILEC ordering process. "ILEC ordering literature, often called a 'CLEC Handbook,' indicates that the guideline for provisioning DS-1 loops[54] [to CLECs] is 45 days. Under present processes, however, CLECs cannot order any loops until completion and turnover of collocation facilities. Thus, the operative interval for receiving a DS-1 loop in the CLECs crucial initial phase of deployment becomes, at a minimum, 165 days. It is unlikely that an ILEC waits more than five months to install a DS-1 for its own services."[55] In addition, KPMG, an independent auditor, found that "information and procedures that have been stated in the CLEC handbook are inconsistent with actual practice and can mislead a CLEC or delay a CLECs ability to conduct business".[56]

3. The Bells have also used a variety of pricing maneuvers to thwart competition. For example, a typical loop charge to remove equipment from a line is under $200. By comparison, Bell Atlantic recently filed a tariff in New York, which included a charge of up to $750 per loop for removal of loop devices. SBC and BellSouth charge up to $2000 per loop for the same service. No competitor

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[53] FCC, *FCC Ensures Bell Atlantic Compliance with Terms of Long Distance Approval; Bell Atlantic Agrees to Pay Up to $27 Million*, 9 March 2000, http://www.fcc.gov/Bureaus/Enforcement/News_Releases/2000/nren0004.html

[54] A DS-1 loop is a broadband connection providing 1.544 mbps of connectivity.

[55] ALTS Petition for Declaratory Ruling: Broadband Loop Provisioning, *In the Matter of Deployment of Wireline Services Offering Advanced Telecommunications Capability*, CC Docket 98-147 (17 May 2000), p. 9, http://www.alts.org/Filings/051700LoopProvisioning.pdf

[56] ALTS Comments, *In the Matter of Application of Verizon for Authorization to Provide In-Region, InterLATA Services in Massachusetts*, CC Docket 00-176 (16 October 2000), p. 23, http://www.alts.org/Filings/101600VerizonMA271.pdf

could possibly pay these exorbitant charges and recover them from end-user rates.[57]

4. Many CLECs, such as IP Communications, have found that they are unable to receive accurate information from ILEC databases. For example, when a residential or business user requests DSL from a CLEC, the CLEC must inquire with the ILEC as to whether the customers telephone line qualifies for DSL. In Kansas and Oklahoma, contrary to its legal obligations, the ILEC often 'filters' the information resulting in the CLEC being unable to accurately surmise if the customer is eligible for DSL.[58] The Department of Justice (DOJ) notes that there are only 556 CLEC DSL lines in Kansas and 548 CLEC DSL lines in Oklahoma.[59] With such anti-competitive practices by the ILEC, the ability of CLECs to gain a foothold in the market is virtually impossible.

5. "In a decision that it calls 'critically important to Kentucky's economic future,' the Public Service Commission... ordered BellSouth to stop 'unreasonable, discriminatory and destructive' practices that... thwarted competition in high-speed Internet access. The ruling was a... victory for Louisville's IgLou Internet Services, which filed a complaint about a year ago accusing the telephone company of using discriminatory pricing and other illegal tactics to maintain a stranglehold on DSL (digital subscriber line) service... IgLou alleged in its complaint that BellSouth had structured its wholesale fees for DSL lines so that only the largest Internet service providers, which [include] its own BellSouth.net, could receive the best discount. Jonathon Amlung, IgLou's attorney, said that IgLou was charged $49.95 per month for each DSL line, while BellSouth.net paid $29.95 a month. The effect was to stifle DSL competition, he said." [60]

6. The California Internet Service Providers Association (CISPA) notes that Pacific Bell and ASI [an affiliated ISP] "engaged in a long-standing pattern of discrimination against ISPs unaffiliated with SBC Communications [parent of Pacific Bell]. In particular, Pacific Bell and ASI... implemented ordering, provisioning, service and billing practices that disadvantage ISPs unaffiliated with SBC, thereby harming hundreds of thousands of actual and potential California

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[57] ALTS Members.

[58] IP Communications Comments, *In the Matter of Application of Southwestern Bell Telephone Company for Authorization to Provide In-Region, InterLATA Services in Kansas & Oklahoma*, CC Docket 00-217 (15 November 2000), p. 13.

[59] Department of Justice Evaluation, *In the Matter of Application of Southwestern Bell Telephone Company for Authorization to Provide In-Region, InterLATA Services in Kansas & Oklahoma*, CC Docket 00-217 (4 December 2000), pp. 7 & 10. http://www.usdoj.gov/atr/public/comments/sec271/sbc/7095.pdf

[60] Richard des Ruisseaux, 'BellSouth Told to Fix DSL Fees,' The Courier-Journal, 6 December 2000, http://www.courier-journal.com/business/news/001206bell.html

Internet subscribers. Further, Pacific Bell/ASI's conduct - possibly by design - threatens the continued existence of a marketplace with multiple diverse ISPs."[61]

[61] CISPA Prehearing Conference Statement, *In the Matter of the Application of Pacific Bell Telephone Company for Authority Pursuant to Public Utilities Code Section 851 to Lease Space in Administrative Buildings and Central Offices and to Transfer Assets to SBC Advanced Solutions, Inc.*, California PUC Application 00-01-023 (29 August 2000), http://www.cispa.org/fl006.html

Appendix B

Barriers to Competition: Building Owners

1. In New York City, the property manager of an MTE has refused even to meet with a CLEC to discuss access despite a tenant's request for service from the CLEC. The property manager indicated that the CLEC simply will not be allowed in the building at all. The customer has told the CLEC that it is afraid the property manager will make life difficult for the customer if the CLEC aggressively pursues access. The property manager has given the names of other vendors in the building to the tenant, and told the customer to use one of them instead of the telecommunications carrier the customer had chosen. The tenant has written to the property manager to explain why it cannot use the existing vendors and that it wants service from the originally requested CLEC. The CLEC still has no access, and cannot take further action with the property manager because of the customer's fear of property manager reprisals.[62]

2. In Washington State, the owner of a new building put the provision of telecommunications services to the tenants out to bid. The winning bidder would gain exclusive access to provide telecommunications services to the tenants in the building. The incumbent provider was able to outbid all other providers, offering to pay $10,000 every year to the building owner. The incumbent was thereby able to shut its competitors out of the building entirely.[63]

3. In one Arizona building, a CLEC had pulled its fiber cable into the building, had access to the telephone closet and building risers, and had begun providing service to customers in the building with the landlord's permission. However, one of the CLECs customers in that building recently requested expanded service from the CLEC, requiring an expansion of facilities. The building owner informed the CLEC that it could no longer have access to the telephone closet -- that it was the property of the incumbent LEC. Moreover, the building owner informed the CLEC that the building was now under *exclusive contract to* another carrier and that the CLEC would have to obtain permission from that carrier to service the equipment that the CLEC had already installed in the building. As a result, the customer in the building is experiencing delays in receiving expanded service while the CLEC negotiates with the building owner and the "exclusive" telecommunications carrier for access. Moreover, the CLECs relationship with the customer is at risk and the CLECs facilities that

[62] *SBPP*, http://www.buildingconnections.org/pages/the_problems/anecdotes.html

[63] Testimony of John D. Windhausen, Jr., President, Association for Local Telecommunications Services (ALTS) before the House Subcommittee on Telecommunications Trade & Consumer Protection, 13 May 1999.

were installed in the building several years ago are in jeopardy of becoming stranded assets.[64]

4. In Pennsylvania, the landlord informed the tenants of one building that they must switch their local telephone company to a company selected by the landlord. Tenants were required to "satisfy their dial-tone, long distance and broadband service needs by contracting with" the carrier of the building owners choice. Many tenants did not want to switch and upon delaying the transition, were informed by the landlord that "failure to comply would constitute a breach of [the] Lease Agreement."[65] The tenant is being forced to switch carriers effectively denying any semblance of choice.

5. One ALTS member cites a litany of barriers in accessing MTEs. The CLEC notes that building owners have: (1) prevented a tenant who occupies several floors in an office building to get service, until the CLEC signs a contract for that entire building and the building owner's other properties, as well, (2) demanded substantial equity in the form of "penny" warrants, (3) required CLEC lease payments be based on total space in the building as opposed to the space occupied, (4) required lease payments based on all the buildings owned, even when the CLEC is not interested in other buildings, (5) required very large one-time, up-front payments, based on floor space of all the buildings in addition to lease payments and a percentage of revenue.

6. Several building owners with a financial interest in a particular service provider informed Edge Connections that they could not grant Edge access to their buildings due to a year-long blackout period imposed by their agreement with the existing carrier. These agreements guarantee preferential treatment to the existing carrier while keeping facilities-based competitors out of the building, and eliminating consumer choice for up to one year.[66]

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[64] *SBPP.* http://www.buildingconnections.org/pages/the_problems/anecdotes.html

[65] SBPP Letter to FCC Chairman & Commissioners, *In the Matter of Promotion of Competitive Networks in Local Telecommunications Markets*, WT Docket 99-217 (5 September 2000), http://www.buildingconnections.org/pages/pdf_files/FCC_let9_5_00.pdf

[66] Ibid.

Appendix C

Barriers to Competition: Municipalities

1. The city of Chicago plans to "give its proposed "CivicNet" telecommunications company substantial advantages that would not be available to other, privately-owned companies, including… access to city owned fiber and exclusive or preferred access to city rights of way and the rights of way of private companies required by contracts with the city to provide such access to the city." [67]

2. "In a new take on Internet taxation, Utah and other states plan to charge access fees to companies laying cable for Internet and other telecommunications services along interstate highways. Utah's Rights of Way Task Force earlier this year recommended a one-time $500-per-mile charge for telecom firms installing cable along right-of-way strips bordering interstates. But Utah governor Michael Leavitt has rejected the recommendation and has publicly suggested an annual fee of $1,000 per mile. Still, some observers in Utah say fees under consideration run as high as $250,000 per mile." [68]

3. One ALTS member began negotiations for a municipal franchise in 1995. The city in question demanded free fiber and a higher franchise than that of the ILEC. Additionally, the city wanted the CLEC to construct a free city network which did not coincide with the CLECs business or network plan. Negotiations lasted two years and the CLEC was forced to abandon the market in 1997. Negotiations covered thirty meetings which eventually included the CLECs President and outside counsel. Legal costs for the two years exceeded $100,000. The CLEC went onto deploy service in two other cities in the State and seven additional cities throughout the country during the timeframe in question. In early 2000, the State government asked the CLEC why two cities in the State were built-out while the other was not. After listening to the situation, the State convinced the CLEC to return to the negotiating table in the middle of 2000. However, the situation had not changed and the city continued to demand concessions not required of the ILEC. The CLEC in question, should it receive non-discriminatory approval from the city, intends to deploy an advanced fiber-optic network.

4. In 1999, the FCC struck down a Minnesota agreement which gave exclusive access to the developer of the interstate highway rights-of-

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[67] Jeffrey A. Eisenach, Ph.D., 'Does Government Belong In the Telecom Business?,' *The Progress & Freedom Foundation*, (January 2001), http://www.pff.org/POP%208.1%20GovtTelecom010400.pdf

[68] John Moore, 'Will You Pay Internet Tolls?,' *ZDNet*, (September 27 1999), http://www.zdnet.com/sp/stories/news/0,4538,2341710,00.html

way for 10 years. In return, the developer would have constructed 1,900 miles of fiber-optic cabling throughout the State and provided the State with a portion of the capacity. The FCC noted that the State's action, effectively granting an exclusive license to the Developer, appear[ed] fundamentally inconsistent with the primary goal of [The Act], to replace exclusivity with competition." Such an agreement would have essentially barred access to highway rights-of-way by competitive carriers for a decade. CLECs would have been beholden to a carrier with monopoly control over State rights-of-way.[69]

5. In Tennessee, TCG, MCI and BellSouth complained that the franchise fees and compensation required of carriers violated The Act. The federal district court issued a decision, in which it held that the City of Chattanooga had no authority under state law to impose franchise fees, because such imposition was either a prohibited form of taxation or an unlawful rent not supported by the police power. [70]

6. In Michigan, TCG alleged that the City of Detroit had violated §253, among other ways, by failing to impose on Ameritech the same ordinance and franchise obligations that the City sought to impose on TCG. The court first, while rejecting the argument that exact parity was required in the terms of the franchises imposed on the ILEC and CLEC, held that §253 obligated the City to impose "comparable" franchise obligations on TCG and Ameritech.[71]

[69] FCC, Memorandum Opinion & Order, *In the Matter of The Petition of the State of Minnesota for a Declaratory Ruling Regarding the Effect of §253 on an Agreement to Install Fiber Optic Wholesale Transport Capacity in State Freeway Rights-of-Way,* CC Docket 98-1, FCC 99-402, (20 December 1999), http://www.fcc.gov/Bureaus/Common_Carrier/Orders/1999/fcc99402.txt

[70] Paul Glist, Wesley R. Heppler & T. Scott Thompson, *Telecommunications Franchising*, (January 2001), Cole, Raywid & Braverman, LLP, p. 20.

[71] Ibid, p. 21.

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Association for Local Telecommunications Services (ALTS)

ALTS is the leading national industry association whose mission is to promote facilities-based local telecommunications competition. Created in 1987, ALTS is headquartered in Washington, DC and now represents more than 200 companies that build, own, and operate competitive networks – CLECs that are *facilities-based*. ALTS was founded to harness the shared energy and vitality of the new local competitors and to help ensure that the 1996 Telecom Act is fully implemented and enforced.

[72] http://www.wto.org/
[73] http://www.itu.org/
[74] http://www.citel.oas.org/