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mpower Communications

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Magalie R. Salas
Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554

Re: *Ex Parte*
CC Docket No. 01-112

Dear Ms. Salas:

The attached "Supplemental Comments" of Mpower Communications Corp. dated September 5, 2001 contain the attachments referred to in the comments. These attachments were inadvertantly omitted from these "Supplemental Comments" when initially filed on that date.

Sincerely,

Francis D. R. Coleman
Vice President, Regulatory Affairs

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List ABCDE

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of:	)	
	)	
	)	
Petition of Mpower Communications Corp. for	)	
Establishment of New Flexible Contract	)	CC Docket No. 01-117
Mechanism Not Subject to "Pick and Choose"	)	

SUPPLEMENTAL COMMENTS

MPOWER COMMUNICATIONS CORP.

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September 5, 2001

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ORIGINAL

A. Introduction

As local competition continues to develop, the incumbent local exchange carriers' ("ILECs'") wholesale activities are experiencing growth rates faster than the ILECs' retail activities. This growth in the ILECs' wholesale activities appears to be altering the relationship between ILECs and competitive local exchange carriers ("CLECs") that are resellers and/or unbundled network element ("UNE") based. Specifically, Mpower will show that increasingly the relationship between ILECs, resellers and UNE-based[1] CLECs is being recognized as a symbiotic wholesaler-retailer relationship rather than as a "zero-sum" competitor-to-competitor relationship. In view of this, Mpower urges the FCC to grant Mpower's petition including initiation of a rulemaking proceeding to establish a mechanism, referred to by Mpower as FLEX contracts, that allows ILECs and CLECs to negotiate mutually beneficial terms and conditions for interconnection. While under Mpower's proposal ILECs and CLECs will be able to negotiate contracts free from the strictures of the current "pick-and-choose" regime,[2] it is important to note that Mpower's proposal is not an effort to replace the current regime of mandatory unbundling of the ILECs' network at TELRIC-based prices. To the contrary, the continued availability of TELRIC based UNEs remains an absolutely essential safety net for CLECs. Mpower's proposed FLEX contracts should be viewed, therefore, not as substitutive of, but as ancillary to, the current regime.

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[1] In these comments, the term "UNE-based CLECs" refers, except when noted to the contrary, to CLECs that use the ILECs network to provide services.

[2] The "pick and choose" requirement should not apply to voluntary FLEX contracts because it would inhibit mutually beneficial FLEX contract relationships between CLECs and ILECs by requiring ILECs to negotiate on the basis of making a concession to all CLECs rather than to the individual CLEC participating in the voluntary FLEX contract negotiation in question. In this connection, it is noteworthy that the resale interexchange market grew dramatically after the Commission permitted AT&T some flexibility to establish individual customer arrangements in AT&T's Tariff 12 offerings. FLEX contracts not subject to "pick and choose" could encourage similar results for wholesale arrangements between ILECs and CLECs.

B. THE TELECOMMUNICATIONS ACT OF 1996 PROMOTES COMPETITION BY MEANS OF WHOLESALE RELATIONSHIPS BETWEEN THE ILEC AND ITS WOULD-BE COMPETITORS

In its *Local Competition Order*,[3] the FCC notes that the Telecommunications Act of 1996 (the "1996 Act") envisions that carriers will enter local markets with diverse strategies. Some carriers will build their own facilities, other carriers will lease facilities from the incumbents, and yet others will pursue a hybrid strategy that involves the construction of new facilities and leased facilities. As the FCC states:

> The Act contemplates three paths of entry into the local market -- the construction of new networks, the use of unbundled elements of the incumbent's network, and resale. The 1996 Act requires us to implement rules that eliminate statutory and regulatory barriers and remove economic impediments to each.[4] (Emphasis added.)

As a result of the pro-competitive provisions of the 1996 Act and the efforts of federal and state regulators, the telecommunications industry has gone through a dramatic transformation and, to a growing degree, local entry is occurring in the various forms anticipated by the framers of the 1996 Act. In New York State, for example, one can find CLECs that provide service mostly over their own facilities, CLECs that are resellers or UNE-based providers, and CLECs that provide service over a combination of their own facilities and the ILECs' facilities.

Mpower would like to focus here on the wholesale relationship between the ILEC and CLECs that use the incumbent's facilities to offer services. In its *Local Competition Order* and a large number of subsequent orders, the FCC has spent an enormous amount of time and energy on constructing a functioning regulatory framework to govern this wholesale relationship between the ILEC and CLECs. As the FCC recognizes in various orders, because the ILECs have traditionally viewed the CLECs as both customers and competitors, this wholesale relationship is often strained by the ILEC's countervailing incentives: while the ILEC may be inclined to promote its wholesale business -- and it

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3 *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-98, First Report and Order, 11 FCC Rcd 15499, 15509, (1996) *("Local Competition First Report and Order"*)

4 *Id.*, paragraph 12.

does -- it also has had an incentive to handicap its would-be competitors in order to protect its own retail business.

There are growing indications that with the further development of local competition, ILECs will increasingly view resellers and UNE-based CLECs as customers and not just as competitors. As discussed in more detail below, the ILECs' annual and quarterly financial reports show that their wholesale business is growing faster than their retail business. Further, various ILECs have publicly recognized that UNE-based CLECs can be valuable allies in ensuring that end users do not migrate to the competing networks of, say, cable companies. These developments are encouraging, since they are signs that local exchange markets are slowly beginning to behave consistent with competitive market principles.

At this juncture, therefore, it is important to introduce a mechanism that will allow ILECs and CLECs to become wholesale *partners*. To this purpose, Mpower has filed its petition requesting initiation of a rulemaking to establish "FLEX contracts." As discussed in more detail in the Mpower petition, FLEX contracts are flexible arrangements, free from the strictures of "pick-and-choose" so that ILECs and CLECs could develop terms and conditions for interconnection based on their mutual interests in the wholesale partnership.[5] FLEX contracts could be a "win-win-win" solution because they would be good for ILECs, good for CLECs and good for their customers.

C. AS COMPETITION DEVELOPS, ILECS, RESELLERS AND UNE-BASED CLECS SHOULD DEVELOP A MORE SYMBIOTIC WHOLESALER-RETAILER RELATIONSHIP

As local competition continues to develop, ILECs are increasingly being confronted with a spectrum of competitors, ranging from competitors that use the ILECs' network facilities, such as resellers and UNE-based CLECs, to competitors that almost exclusively offer service over their own facilities, such as cable companies.

In considering the ILECs' potential responses to competitive entry, it is important to recognize that each form of competition impacts the ILECs' revenues and profits differently. In the case of competitors that offer service entirely over their own

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5 *See* n. 2, *supra*.

networks, the *ILECs stand to lose literally all of the revenues and profits associated with the end user*. By contrast, when competitors use in whole or in significant part the ILECs' facilities, the ILECs' loss of an end-user customer results only in a partial loss of revenues and profits. Thus, in determining their posture towards resellers and UNE-based CLECs, the ILECs must consider the choice between wholesaling or losing all sales altogether. As competing networks continue to develop, the choice for the ILECs is increasingly "wholesale or no sale."

The spectrum of competition and the implications for the ILECs' revenues and profits may be illustrated as below.

Again, the important distinction here is between competitors that use the ILEC's facilities, such as UNE-based CLECs and resellers, and those that operate or use competing networks. As long as the ILEC wholesales its facilities to a competitor, *it will retain part of the revenues and profits associated with the end user*. Specifically, the ILEC will retain the wholesale-related revenues and profits.

D. ILECs Benefit In Various Ways From A Wholesale Alliance With Resellers and UNE-Based CLECs

In addition to retaining the wholesale-related revenues and profits, ILECs will experience additional benefits from their wholesale relationship with resellers and UNE-based CLECs. The ILECs' full benefits of wholesaling are twofold:

- ILECs will continue to earn revenues and profits from wholesaling their network even where the growth of certain segments of their retail customer base may be stagnating. Wholesaling to CLECs also ensures continued utilization of the ILECs' networks and avoids their having to incur costs for maintaining facilities that are unutilized. This is a significant benefit given the predominantly *fixed-cost* nature of telecommunications facilities. In most other industries, a lost customer typically means a corresponding reduction in costs. Not so in the telecommunications industry. Once the network is built, the majority of a carrier's network costs are fixed and will be incurred whether or not there is a customer. The loss of a customer, therefore, does not result in a zero profit, but rather in a negative profit. It is for this reason, among others, that wholesale should be an attractive alternative to losing an end user altogether.

- In establishing a close relationship with resellers and UNE-based CLECs, the ILEC strengthens its competitive position vis-à-vis competitors that use or operate competing networks. Most importantly, by nurturing its wholesale relationship with resellers and UNE-based CLECs, the ILEC benefits from the resellers' and

CLECs' retailing activities. That is, the retailing, marketing and advertising activities of competitors that use or operate competing networks now need to match the combined level of activity of the ILEC, resellers and UNE-based CLECs. In short, a close and healthy wholesale relationship between ILECs, resellers and UNE-based CLECs could greatly enhance the ILEC's overall competitive position in the market place.

One should note that each of these effects is amplified in importance as facilities-based local competition grows in importance.

E. Indications Are that ILECs Are Increasingly Valuing Their Wholesale Customers

Undeniably, ILECs will continue to prefer, as they have in the past, to retail directly to end users -- the revenues and profits associated with retailing vertical features and certain business services remain high. This explains, in part, why most ILECs have some form of win-back programs in place by which they seek to bring lost customers back onto their networks.

Nevertheless, as the industry evolves and becomes more competitive, one would expect that the ILECs become naturally more interested in nurturing relationships with entities that are able to efficiently retail their network services to end users. In this sense, the vertically integrated ILECs may gravitate toward the model followed in other capital intensive industries, such as the automobile industry, where GM, Ford and other manufacturers have close and well developed relationships with independent dealers that perform many of the retail functions necessary to sell cars to end-user customers. In fact, we may already be witnessing a change in this direction.

For example, at least two of the four RBOCs, BellSouth and Qwest, appear to have programs in place under which *they pay commissions to their sales representatives for sales of TELRIC-based UNEs to CLECs*. This is most interesting because it may signal that the ILECs are starting to recognize that the wholesale business: (a) is profitable (why else promote it through sales commissions), and (b) that they have an interest in keeping customers on their networks, either as their own end users or as end users served by resellers or UNE-based CLECs.

The same change in attitude can be gleaned from statements made by ILEC representatives in legal pleadings, speeches, etc. The following statement taken from

Qwest's comments before the FCC is illustrative of how ILECs may be viewing the changing role of wholesale:

> ... ILECs and CLECs alike have an economic incentive to work together to maximize the competitiveness of DSL offerings. Qwest is trying to engage in such joint efforts at this time. If an ILEC, in a competitive broadband market place, were to try to behave in a manner which discouraged other providers of DSL services from optimizing their own services over the ILEC's loops, customers could simply purchase broadband services from cable providers. [6]

Qwest then goes on to note

> [I]t is also important to keep in mind that CLECs still need access to ILEC loops in order to provide DSL services. It would be a serious mistake, in today's marketplace, to allow a situation to develop whereby CLECs were unable to make efficient use of ILEC loops. Such a situation would harm both CLECs and ILECs alike.[7]

Another illustrative statement is the one made by a Verizon officer in a recent speech before the *Progress and Freedom Foundation*:

> Now, unlike some other network providers, Verizon is willing to make our network available to other players, even competitors; in fact, we see the wholesaling of our network as a legitimate business opportunity as long as we're permitted to operate this business on rational economic and technical grounds.[8]

These statements made by Verizon and Qwest articulate the changing role of wholesale in the competitive market place. As discussed in more detail in Mpower's petition requesting a rulemaking to establish FLEX contracts, the current UNE regime that rules interconnection agreements between ILECs and CLECs – although essential for UNE-based CLEC survival -- is too restrictive and does not allow parties sufficient flexibility to nurture closer and voluntary wholesale relationships.

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6 Comments of Qwest Communications International Inc. On Further Notice of Proposed Rulemaking, CC Dockets Nos. 98 – 147, 96 – 98. Page 3.

7 *Id,* Page 3.

8 Tom Tauke, Senior Vice President Public Policy and External Affairs Verizon Communications, "Delaying the Last Mile," Speech delivered before the *Progress and Freedom Foundation*, Aspen, August 21, 2001.

F. ILECS ARE ENGAGED IN SIGNIFICANT WHOLESALE ACTIVITIES WARRANTING A ROLE SUPPORTIVE OF RESELLERS AND UNE-BASED CLECs

Attached to this paper are some select RBOC data on local exchange carrier revenues and wholesale and retail access line counts. These data show that RBOCs are experiencing significant growth in their wholesale activities. As the FCC is well aware, however, detailed data on competitive entry is often highly proprietary and therefore extremely hard to obtain. The data presented here are gathered from public sources and are not intended to be a comprehensive review of the state of competition. Rather, they are presented to show instances in which ILECs are experiencing increased wholesale activities and therefore should have an incentive to nurture closer wholesale relationships with resellers and UNE-based CLECs, as discussed above.

Undoubtedly, the development of local competition is still heavily influenced by regulatory policies. Given that state commissions are independent and do not move in tandem, a review of the status of competition across the country shows a fairly uneven development. Nevertheless, data show significant wholesale activity in various markets.

At this point it appears that the New York market is perhaps the most competitive one. According to recent testimony filed by Verizon, there is significant competitive entry in the New York market:

> Verizon estimates that well over *3 million access lines* in its operating area in New York are served by competitive local exchange providers[9]... Facilities-based competitors currently provide about *1.15 million business and 121,000 residence lines* and are present in wire centers that serve over 90% of Verizon's business lines and 64% of its residence lines, respectively. Competitors are growing rapidly and growth has accelerated since Verizon NY's entrance into the interLATA market became imminent.[10] (Emphasis added.)

Verizon then goes on to discuss that a significant portion of this competition consists of competitors that use or operate competing networks. While these data have not been subjected to cross-examination, they indicate that: Verizon in New York is

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[9] NYPSC Case 00 – C – 1945, Verizon Panel testimony, May 15, 2001. Page 10.

[10] *Id.*, page 73.

experiencing significant wholesale activity where there are competing networks. The New York market, therefore, is perhaps the best illustration of a situation in which the incumbent, Verizon, is faced with what Mpower calls the "retail, wholesale, or no-sale" proposition. The same observation can be made for BellSouth, which claims to have lost 1.8 million lines serving area-wide to competitors that use or operate competing networks.[11] As discussed, the worst scenario for the ILECs in this spectrum of competitive possibilities is the "no-sale" outcome: a "no-sale" outcome leaves the ILEC without any revenues to cover the ongoing fixed costs of its network and operations.

While the competitive situation appears most intense in New York State, the same pattern of the wholesale business developing into an increasingly important segment of the ILECs operations is found across the country. For SBC, BellSouth and Verizon, the relative recent growth in their retail and wholesale operations has been as follows:

Table 1:
Growth in Local Service Revenues (For the Six Months Ended June 30, 2001 Versus June 30, 2000), and Change in Retail and Wholesale Access Lines As of June 30, 2001 Versus June 30, 2000[12]

	SBC % CHANGE	BELLSOUTH % CHANGE	QWEST % CHANGE	VERIZON % CHANGE
LOCAL SERVICE REVENUE				
TOTAL	8.4%	2.7%	NA	1.8%
ACCESS LINES SERVED				
RETAIL	15.1%	24.9%	N/A	20.7%
WHOLESALE	55.6%	42.7%	N/A	31.0%
TOTAL	15.9%	25.2%	29.9%	21.0%

These numbers reflect some important developments. As indicated, for SBC there was a 55.6 percent year-over-year increase in wholesale lines as of June 30, 2001. Through the 2nd Quarter ending June 30, 2001, *growth in wholesale activities accounted for no less than 20 percent of the overall growth in SBC's local service revenues*

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11 BellSouth, Communications Group, 2nd Quarter, 2001 10Q.

12 10Qs, 10Ks, Annual Reports and Investor Briefings. More detailed data are found in the attachment.

compared to the same six-month period in 2001.[13] This number is even more startling if one realizes that wholesale growth is typically more concentrated in select geographic areas than retail growth. This means that in certain areas, growth in SBC's wholesale revenues may have possibly exceeded growth in SBC's retail revenues. This is an important development, underscoring the increasingly important role of the ILEC/CLEC wholesale relationship.

SBC's situation is not unique. For Qwest, wholesale drove *25 percent* of the year-over-year growth in revenues for the company, as of the 2nd Quarter, 2001.[14] In general, as the table above indicates, for SBC, BellSouth, and Verizon, growth rates for the wholesale business significantly outpaced those for the retail business.

To put the percentage growth rates in perspective, however, the table below shows the relative number of retail and wholesale access lines served by those companies as of the end of last year. Also shown are the total local service revenues for these companies:

Table 2:
Local Retail Revenues, Retail Access Lines and Wholesale Access Lines
(as of 12/31/2000)[15]

	SBC	BELLSOUTH	QWEST	VERIZON
LOCAL SERVICE REVENUE				
TOTAL	**$22.1 B.**	**$12.6 B.**	**N/A**	**$21.4 B.**
ACCESS LINES SERVED				
RETAIL	**103,456,000**	**54,229,000**	**N/A**	**108,833,000**
WHOLESALE	**1,633,000**	**1,308,000**	**N/A**	**3,543,000**
TOTAL	**105,089,000**	**55,537,000**	**41,861,000**	**112,376,000**

The above tables show that while wholesale is still small relative to the ILECs' total retail activities, it is among the fastest growing segments of the ILECs' operations.

13 SBC, 2nd Quarter, 2001 10Q.

14 Morgan Stanley Dean Witter, "Qwest: 2Q01 Largely In Line, but Surprises Below the Line," *Telecom – Wireline* – August 21, 2001.

15 10Ks, Annual Reports and Investor Briefings. More detailed data are found in the attachment.

As noted, attached to this document are more detailed data that break down wholesale activities for SBC, BellSouth and Verizon. The important observation, however, is that the fast growing wholesale business allows the ILECs to retain end users on their networks rather than to lose them to competitors that use or operate competing networks. As this trend continues, we should expect the ILECs to become increasingly interested in developing closer ties with their resellers and UNE-based CLECs.

G. Conclusion

While ILECs are experiencing significant growth in their wholesale business, there is continued growth in competing networks. In view of this, ILECs will increasingly be interested in developing close relationships with resellers and UNE-based CLECs. To accommodate the need of ILECs and CLECs to engage in mutually agreeable terms and conditions for interconnection, the FCC should promptly grant Mpower's petition including initiation of a rulemaking proceeding to establish a mechanism, referred to by Mpower as FLEX contracts. Again, while under Mpower's proposal, ILECs and CLECs will be able to negotiate contracts free from the strictures of the current "pick-and-choose" regime, Mpower's proposed FLEX contracts should be viewed as ancillary to, and not as substitutive of, the current regime. As such, the FLEX contracts proposed by Mpower would be a "win-win-win" solution that is good for ILECs, good for CLECs and good for their customers.

Respectfully submitted,

Francis D R Coleman

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September 5, 2001

CERTIFICATE OF SERVICE

I hereby certify that the foregoing Supplemental Comments have been served by hand delivery to the persons listed below on this 5th day of September, 2001.

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ANALYSIS OF RBOC RETAIL AND WHOLESALE LOCALS SERVICE ACTIVITY

(AMOUNTS IN THOUSANDS)
(sources include 10Q, 10K, Annual Reports and Investor Briefings)

	6/30/01	% OF TOTAL	6/30/00	% OF TOTAL	INCREASE (DECREASE)	% CHANGE
LOCAL SERVICE [illegible]						
RETAIL		*0.0%*		*0.0%*		0.0%
WHOLESALE		*0.0%*		*0.0%*		0.0%
TOTAL		0.0%		0.0%	$ -	0.0%
[illegible]						
RETAIL - EQUIVALENT LINES						
RESIDENTIAL	12,786	24.6%	12,424	31.0%	362	2.9%
BUSINESS	39,261	75.4%	27,648	69.0%	11,613	42.0%
TOTAL RETAIL	52,047	100.0%	40,072	100.0%	11,975	29.9%
WHOLESALE		0.0%		0.0%	-	0.0%
TOTAL	52,047	100.0%	40,072	100.0%	11,975	29.9%
[illegible] PER MONTH						
RETAIL	N/A		N/A		N/A	
WHOLESALE	N/A		N/A		N/A	
COMBINED	N/A		N/A		N/A	

	6/30/01	% OF TOTAL	6/30/00	% OF TOTAL	INCREASE (DECREASE)	% CHANGE
LOCAL SERVICE [illegible]						
RETAIL		*0.0%*		*0.0%*		0.0%
WHOLESALE		*0.0%*		*0.0%*		0.0%
TOTAL		0.0%		0.0%	$ -	0.0%
[illegible]						
RETAIL - EQUIVALENT LINES						
RESIDENTIAL	12,786	24.6%	12,424	31.0%	362	2.9%
BUSINESS	39,261	75.4%	27,648	69.0%	11,613	42.0%
TOTAL RETAIL	52,047	100.0%	40,072	100.0%	11,975	29.9%
WHOLESALE		0.0%		0.0%	-	0.0%
TOTAL	52,047	100.0%	40,072	100.0%	11,975	29.9%
[illegible] PER MONTH						
RETAIL	N/A		N/A		N/A	
WHOLESALE	N/A		N/A		N/A	
COMBINED	N/A		N/A		N/A	

	12/31/00	% OF TOTAL	12/31/99	% OF TOTAL	INCREASE (DECREASE)	% CHANGE
LOCAL SERVICE [illegible]						
RETAIL		*0.0%*		*0.0%*		0.0%
WHOLESALE		*0.0%*		*0.0%*		0.0%
TOTAL		0.0%		0.0%	$ -	0.0%
[illegible]						
RETAIL - EQUIVALENT LINES						
RESIDENTIAL	12,678	30.3%	12,259	35.4%	419	3.4%
BUSINESS	29,183	69.7%	22,369	64.6%	6,814	30.5%
TOTAL RETAIL	41,861	100.0%	34,628	100.0%	7,233	20.9%
WHOLESALE		0.0%		0.0%	-	0.0%
TOTAL	41,861	100.0%	34,628	100.0%	7,233	20.9%
[illegible] PER MONTH						
RETAIL	N/A		N/A		N/A	
WHOLESALE	N/A		N/A		N/A	
COMBINED	N/A		N/A		N/A	

EXCERPTS FROM 2nd Quarter 10Q (amounts in millions)

Commercial wholesale revenues were sparked by strong demand for Internet and optical network capacity worldwide. Contributing to this demand was a "flight to safety" spurred by reported and perceived difficulties of many new carriers. Wholesale revenue from Qwest's 14-state local service territory benefited from strong demand for private line and access services stimulated in part by local competition.

EXCERPT FROM 2000 10K (amounts in millions)

Qwest operates in four segments: retail services, wholesale services, network services and directory services. The retail services segment provides local telephone services, long-distance services, wireless services and data services. The wholesale services segment provides (i) exchange access services that connect customers to the facilities of IXCs and (ii) interconnection to the Qwest telecommunications network to CLECs. For the year 2000, TOTAL revenue was comprised of retail (70%), wholesale services (19%), network services (2%), and directory services (11%). Local voice revenues grew despite the fact that access line growth slowed to approximately 2 percent year-over-year. Total access lines increased by 341,000 with business lines comprising the majority of the change. The decline in access line growth was partially attributable to businesses converting single access lines to a lower number of high-speed, high-capacity lines allowing for transport of data at higher rates of speed. On a voice-grade equivalent basis, the Company's business access lines grew by 30.5 percent as compared to 1999.

At December 31, 1999, the Company had added 408,000 residential and business access lines, an increase of 2.5 percent over the end of 1998. Of this increase, residential second line installations accounted for 187,000 lines, an increase of 11.8 percent as compared with 1998. Second line additions by residential and small business customers increased primarily as a result of the growing demand for Internet access and data transport capabilities. Although Qwest's revenues continued to grow in 1999, some areas of service experienced a decline in growth rates from 1998, particularly retail and wholesale basic monthly services and calling services. The drop in the growth rate was primarily attributable to increased competition as well as the Company's customer retention strategy of offering bundles of services to customers at lower prices in return for entering into longer-term contracts.

Qwest signed ground-breaking wholesale agreements with McLeodUSA and Eschelon Telecom for voice and data services totaling nearly $750 million, significantly expanding competition within the 14-states where Qwest provides local service. In addition, Cable & Wireless signed a multi-year agreement valued at more than $100 million for high-speed network capacity.

ANALYSIS OF RBOC RETAIL AND WHOLESALE LOCALS SERVICE ACTIVITY

(AMOUNTS IN THOUSANDS)
(sources include 10Q, 10K, Annual Reports and Investor Briefings)

	6/30/01	% OF TOTAL	6/30/00	% OF TOTAL	INCREASE (DECREASE)	% CHANGE
LOCAL SERVICE REVENUES						
RETAIL		*0.0%*		*0.0%*		0.0%
WHOLESALE		*0.0%*		*0.0%*		0.0%
TOTAL	$5,545,000	0.0%	$5,537,000	0.0%	$ 8,000	0.1%
[illegible]						
RETAIL						
RESIDENTIAL	39,841	30.9%	40,034	37.6%	(193)	-0.5%
BUSINESS	21,989	17.1%	22,007	20.6%	(18)	-0.1%
DSO EQUIVALENTS	62,729	48.7%	41,010	38.5%	21,719	53.0%
PUBLIC	635	0.5%	680	0.6%	(45)	-6.6%
TOTAL RETAIL	125,194	97.1%	103,731	97.3%	21,463	20.7%
WHOLESALE	3,726	2.9%	2,844	2.7%	882	31.0%
TOTAL	128,920	100.0%	106,575	100.0%	22,345	21.0%
[illegible]						
RETAIL	N/A		N/A		N/A	
WHOLESALE	N/A		N/A		N/A	
COMBINED	$ 14		$ 17		$ (3)	

	6/30/01	% OF TOTAL	6/30/00	% OF TOTAL	INCREASE (DECREASE)	% CHANGE
LOCAL SERVICE REVENUES						
RETAIL		*0.0%*		*0.0%*		0.0%
WHOLESALE		*0.0%*		*0.0%*		0.0%
TOTAL	$11,165,000	0.0%	$10,967,000	0.0%	$ 198,000	1.8%
[illegible]						
RETAIL						
RESIDENTIAL	39,841	30.9%	40,034	37.6%	(193)	-0.5%
BUSINESS	21,989	17.1%	22,007	20.6%	(18)	-0.1%
DSO EQUIVALENTS	62,729	48.7%	41,010	38.5%	21,719	53.0%
PUBLIC	635	0.5%	680	0.6%	(45)	-6.6%
TOTAL RETAIL	125,194	97.1%	103,731	97.3%	21,463	20.7%
WHOLESALE	3,726	2.9%	2,844	2.7%	882	31.0%
TOTAL	128,920	100.0%	106,575	100.0%	22,345	21.0%
[illegible]						
RETAIL	N/A		N/A		N/A	
WHOLESALE	N/A		N/A		N/A	
COMBINED	$ 14		$ 17		$ (3)	

	12/31/00	% OF TOTAL	12/31/99	% OF TOTAL	INCREASE (DECREASE)	% CHANGE
LOCAL SERVICE REVENUES						
RETAIL		*0.0%*		*0.0%*		0.0%
WHOLESALE		*0.0%*		*0.0%*		0.0%
TOTAL	$21,368,000	0.0%	$20,600,000	0.0%	$ 768,000	3.7%
[illegible]						
RETAIL						
RESIDENTIAL	39,999	35.6%	39,606	42.8%	393	1.0%
BUSINESS	22,242	19.8%	21,701	23.5%	541	2.5%
DSO EQUIVALENTS	45,931	40.9%	28,712	31.0%	17,219	60.0%
PUBLIC	661	0.6%	697	0.8%	(36)	-5.2%
TOTAL RETAIL	108,833	96.8%	90,716	98.1%	18,117	20.0%
WHOLESALE	3,543	3.2%	1,772	1.9%	1,771	99.9%
TOTAL	112,376	100.0%	92,488	100.0%	19,888	21.5%
[illegible]						
RETAIL	N/A		N/A		N/A	
WHOLESALE	N/A		N/A		N/A	
COMBINED	$ 16		$ 19		$ (3)	

EXCERPTS FROM 2ND QTR. 2001 10Q, PAGES 8 & 20 (amounts in millions)

Local service revenues are earned by our telephone operations from the provision of local exchange, local private line, wire maintenance, voice messaging and value-added services. Value-added services are a family of services that expand the utilization of the network, including products such as Caller ID, Call Waiting and Return Call. **The provision of local exchange services not only includes retail revenue but also includes local wholesale revenues from unbundled network elements (UNEs), interconnection revenues from competitive local exchange carriers, certain data transport revenues, and wireless interconnection revenues. Growth in local service revenues of $8 million, or 0.1%, and $198 million, or 1.8%, in the second quarter and first six months of 2001, respectively, reflect higher payments received from competitive local exchange carriers for interconnection of their networks with our network and solid demand for our value-added services as a result of new packaging of services.** These factors were substantially offset by the effects of lower demand and usage of our basic local wireline services and mandated intrastate price reductions. Our switched access lines in service declined 0.4% from June 30, 2000, primarily reflecting the impact of an economic slowdown. In addition, technology substitution is increasing, as more customers are choosing wireless and Internet services over certain basic wireline services.

During June 2000, we sold approximately 471,000 access lines located in Iowa, Nebraska and Oklahoma for combined cash proceeds of $1,433 million and $125 million in convertible preferred stock.

EXCERPT FROM 2000 10K, PAGES F-9 AND F-10 (amounts in millions)

Local service revenues are earned by our operating telephone subsidiaries from the provision of local exchange, local private line, wire maintenance, voice messaging and value-added services. Value-added services are a family of services that expand the utilization of the network, including products such as Caller ID, Call Waiting and Return Call. **Local services also include wholesale revenues from unbundled network element (UNE) platforms, certain data transport revenues, and wireless interconnection revenues. Local service revenue growth was partially offset in both years by the effect of resold and UNE platforms, as well as the effect of net regulatory price reductions and customer rebates.**

During 2000, we sold non-strategic access lines of former GTE properties listed above, except for those located in Arizona and California, for combined cash proceeds of approximately $4,903 million and $125 million in convertible preferred stock.

For comparability purposes, the adjusted results of operations shown above exclude the operating revenues and expenses contributed by the properties that have been sold or will be sold in early 2001. These operating revenues were approximately $766 million and $1,151 million for the years 2000 and 1999.

ANALYSIS OF RBOC RETAIL AND WHOLESALE LOCALS SERVICE ACTIVITY

(AMOUNTS IN THOUSANDS)
(sources include 10Q, 10K, Annual Reports and Investor Briefings)

	6/30/01	% OF TOTAL	6/30/00	% OF TOTAL	INCREASE (DECREASE)	% CHANGE
[illegible]						
RETAIL		0.0%		0.0%	$ -	0.0%
WHOLESALE / OTHER WIRELINE		0.0%		0.0%	$ -	0.0%
TOTAL RETAIL & OTHER WIRELINE	$2,964,000	0.0%	$2,891,000	0.0%	$ 73,000	2.5%
[illegible]						
RETAIL						
RESIDENTIAL	17,011	27.9%	17,203	35.3%	(192)	-1.1%
BUSINESS	8,426	13.8%	8,401	17.2%	25	0.3%
ACCESS LINE EQUIVALENTS (data circuits)	33,877	55.5%	21,821	44.8%	12,056	55.2%
OTHER	229	0.4%	260	0.5%	(31)	-11.9%
TOTAL RETAIL	59,543	97.6%	47,685	97.9%	11,858	24.9%
WHOLESALE						
UNE	739	50.0%	259	25.0%	480	185.3%
RESALE	739	50.0%	777	75.0%	(38)	-4.9%
TOTAL WHOLESALE	1,478	2.4%	1,036	2.1%	442	42.7%
TOTAL	61,021	100.0%	48,721	100.0%	12,300	25.2%
AVERAGE REVENUE PER LINE PER MONTH						
RETAIL	N/A		N/A		N/A	
WHOLESALE	N/A		N/A		N/A	
COMBINED	$ 16		$ 20		$ (4)	

	6/30/01	% OF TOTAL	6/30/00	% OF TOTAL	INCREASE (DECREASE)	% CHANGE
[illegible]						
RETAIL		0.0%		0.0%	$ -	0.0%
WHOLESALE / OTHER WIRELINE		0.0%		0.0%	$ -	0.0%
TOTAL RETAIL & OTHER WIRELINE	$5,874,000	0.0%	$5,719,000	0.0%	$ 155,000	2.7%
[illegible]						
RETAIL						
RESIDENTIAL	17,011	27.9%	17,203	35.3%	(192)	-1.1%
BUSINESS	8,426	13.8%	8,401	17.2%	25	0.3%
ACCESS LINE EQUIVALENTS (data circuits)	33,877	55.5%	21,821	44.8%	12,056	55.2%
OTHER	229	0.4%	260	0.5%	(31)	-11.9%
TOTAL RETAIL	59,543	97.6%	47,685	97.9%	11,858	24.9%
WHOLESALE						
UNE	739	50.0%	259	25.0%	480	185.3%
RESALE	739	50.0%	777	75.0%	(38)	-4.9%
TOTAL WHOLESALE	1,478	2.4%	1,036	2.1%	442	42.7%
TOTAL	61,021	100.0%	48,721	100.0%	12,300	25.2%
AVERAGE REVENUE PER LINE PER MONTH						
RETAIL	N/A		N/A		N/A	
WHOLESALE	N/A		N/A		N/A	
COMBINED	$ 16		$ 20		$ (4)	

	12/31/00	% OF TOTAL	12/31/99	% OF TOTAL	INCREASE (DECREASE)	% CHANGE
[illegible]						
RETAIL		0.0%		0.0%	$ -	0.0%
WHOLESALE / OTHER WIRELINE		0.0%		0.0%	$ -	0.0%
TOTAL RETAIL & OTHER WIRELINE	$12,655,000	0.0%	$11,903,000	0.0%	$ 752,000	6.3%
[illegible]						
RETAIL						
RESIDENTIAL	17,135	30.9%	17,002	38.6%	133	0.8%
BUSINESS	8,525	15.4%	8,232	18.7%	293	3.6%
ACCESS LINE EQUIVALENTS (data circuits)	28,321	51.0%	17,770	40.3%	10,551	59.4%
OTHER	248	0.4%	265	0.6%	(17)	-6.4%
TOTAL RETAIL	54,229	97.6%	43,269	98.1%	10,960	25.3%
WHOLESALE						
UNE	N/A	N/A	N/A	N/A	N/A	N/A
RESALE	N/A	N/A	N/A	N/A	N/A	N/A
TOTAL WHOLESALE	1,308	2.4%	816	1.9%	492	60.3%
TOTAL	55,537	2.4%	44,085	1.9%	11,452	26.0%
AVERAGE REVENUE PER LINE PER MONTH						
RETAIL	N/A		N/A		N/A	
WHOLESALE	N/A		N/A		N/A	
COMBINED	$ 19		$ 23		$ (4)	

EXCERPT FROM [illegible] COMMUNICATIONS GROUP (amounts in millions)

The increase in local service revenues of $73 in the second quarter and $155 for the year-to-date period is attributable to strong growth in digital and data revenues, wholesale revenues, and by our marketing of calling features. Those increases were offset by a decrease in basic service revenues reflecting competition, rate reductions and a slowing economy as well as reduced payphone related revenues at our telephone operations. Since second quarter 2000, residential access lines declined 1.1% to 17,011, while business access lines increased 0.3% to 8,426. The core business was affected by a slowing economy, as well as competitive and technological changes. The technological changes are manifested in the shifting of customers from wireline to wireless and second line customers to high-speed access service. **At June 30, 2001, we provided 1.5 million wholesale lines to competitors, on both a resale and unbundled network elements (UNE) basis. At June 30, 2000, UNEs accounted for approximately 25% of our wholesale lines and at June 30, 2001 they represented 50%. Because of the larger discounts, this shift to UNEs is negatively impacting our revenue growth. We also estimate that we have lost an additional 1.8 million lines to facilities-based competitors.** Due to expanding demand for our digital and data services, we ended the second quarter with over 59 million total equivalent access lines, an increase of 24.9% since June 30, 2000.

EXCERPT FROM 2000 10K, PAGE [illegible] (amounts in millions)

Local service
Local service revenues increased $857 during 1999 and $522 during 2000, attributable to strong demand for calling features and digital and data services. Total equivalent access lines increased 16.3% during 1999 and 25.3% during 2000. Residential access lines rose 3.1% during 1999 and 0.8% during 2000. **The growth in residential lines has slowed substantially as a result of increasing competition and slowing of economic growth in our wireline service area. Business access lines, including both switched access lines and data circuits, grew 27.1% during 1999 and 41.7% during 2000, propelled by expanding demand for our digital and data services, and offset by the effects of increasing competition.**

Other wireline and intersegment revenues
Other wireline and intersegment revenues increased 22.5%, from $1,209 in 1998 to $1,481 in 1999, and increased 13.5% to $1,681 in 2000. **Higher revenues of $177 in 1999 and $293 in 2000 resulted primarily from sales of unbundled network elements, collocation of competing carriers' equipment in our facilities, interconnection charges to wireless carriers, demand for our Internet access offering and proceeds from universal service funds.**

ANALYSIS OF RBOC RETAIL AND WHOLESALE LOCALS SERVICE ACTIVITY

(AMOUNTS IN THOUSANDS)
(sources include 10Q, 10K, Annual Reports and Investor Briefings)

	6/30/01	% OF TOTAL	6/30/00	% OF TOTAL	INCREASE (DECREASE)	% CHANGE
LOCAL SERVICE REVENUE						
RETAIL		0.0%		0.0%	$ 363,000	
WHOLESALE		0.0%		0.0%	$ 93,000	
TOTAL	$ 5,923,000	0.0%	$ 5,467,000	0.0%	$ 456,000	8.3%
ACC[illegible]						
RETAIL - EQUIVALENT ACCESS LINES					-	
RESIDENTIAL	42,123	37.3%	39,683	40.8%	2,440	6.1%
BUSINESS	66,916	59.3%	54,900	56.4%	12,016	21.9%
OTHER	590	0.5%	703	0.7%	(113)	-16.1%
TOTAL RETAIL	109,629	97.2%	95,286	97.9%	14,343	15.1%
WHOLESALE	3,200	2.8%	2,056	2.1%	1,144	55.6%
TOTAL	112,829	100.0%	97,342	100.0%	15,487	15.9%
AV[illegible] MONTH						
RETAIL	N/A		N/A		N/A	
WHOLESALE	N/A		N/A		N/A	
COMBINED	$ 17		$ 19		$ (2)	

	6/30/01	% OF TOTAL	6/30/00	% OF TOTAL	INCREASE (DECREASE)	% CHANGE
LOCAL SERVICE REVENUE						
RETAIL		0.0%		0.0%	$ 700,000	
WHOLESALE		0.0%		0.0%	$ 192,000	
TOTAL	$11,487,000	0.0%	$10,595,000	0.0%	$ 892,000	8.4%
ACC[illegible]						
RETAIL - EQUIVALENT ACCESS LINES					-	
RESIDENTIAL	42,123	37.3%	39,683	40.8%	2,440	6.1%
BUSINESS	66,916	59.3%	54,900	56.4%	12,016	21.9%
OTHER	590	0.5%	703	0.7%	(113)	-16.1%
TOTAL RETAIL	109,629	97.2%	95,286	97.9%	14,343	15.1%
WHOLESALE	3,200	2.8%	2,056	2.1%	1,144	55.6%
TOTAL	112,829	100.0%	97,342	100.0%	15,487	15.9%
AV[illegible] MONTH						
RETAIL	N/A		N/A		N/A	
WHOLESALE	N/A		N/A		N/A	
COMBINED	$ 17		$ 18		$ (1)	

	12/31/00	% OF TOTAL	12/31/99	% OF TOTAL	INCREASE (DECREASE)	% CHANGE
LOCAL SERVICE REVENUE						
RETAIL		0.0%		0.0%	$ 2,193,000	
WHOLESALE		0.0%		0.0%	$ 389,000	
TOTAL	$22,126,000	0.0%	$19,544,000	0.0%	$ 2,582,000	13.2%
ACC[illegible]						
RETAIL - EQUIVALENT ACCESS LINES						
RESIDENTIAL	41,385	39.4%	37,919	42.2%	3,466	9.1%
BUSINESS	61,419	58.4%	49,720	55.3%	11,699	23.5%
OTHER	652	0.6%	752	0.8%	(100)	-13.3%
TOTAL RETAIL	103,456	98.4%	88,391	98.3%	15,065	17.0%
WHOLESALE	1,633	1.6%	1,496	1.7%	137	9.2%
TOTAL	105,089	100.0%	89,887	100.0%	15,202	16.9%
AV[illegible] MONTH						
RETAIL	N/A		N/A		N/A	
WHOLESALE	N/A		N/A		N/A	
COMBINED	$ 18		$ 18		$ -	

EXCERPT FROM 2ND QTR., 2001 10Q, WIRELINE NORMALIZED RESULTS (amounts in millions)

Local service revenues increased $456, or 8.3%, in the second quarter and $892, or 8.4%, for the first six months of 2001. Approximately $145 of the increase in the second quarter and $337 for the first six months was attributable to continued demand from business customers for network integration services. **Increases in wholesale revenues, which include unbundled network elements and resale services, accounted for approximately $93 of the second-quarter increase and $192 for the first six months.**

EXCERPT FROM 2000 ANNUAL REPORT, PAGES 7 & 18 (amounts in millions)

Local service revenues increased $2,582, or 13.2%, in 2000 and $1,998, or 11.4%, in 1999. Excluding the operations of Sterling, acquired in March 2000, the increase was approximately 10.9% in 2000. Approximately $619 of the increase in 2000 was attributable to increased demand from business customers for network integration and Internet services. ..... **Increased demand for wholesale services, including the resale and sale of unbundled network elements, accounted for approximately $389 of the increase in 2000 and $193 in 1999.** ..... Total access lines in service at the end of 2000 increased by approximately 1%, while access lines in service at the end of 1999 increased more than 3%. **The lower growth rate in access lines is due largely to competitive losses, as discussed in the "Competition" section of "Operating Environment and Trends of the Business"**, as well as DSL penetration, particularly in California, which has reduced demand for additional lines.

We have reached over 1,400 wireline interconnection agreements with competitive local service providers, and most have been approved by the relevant state commission. In addition, AT&T, MCI and other competitors are reselling our local exchange services, and **as of December 31, 2000, we had approximately 1.6 million access lines (approximately 2.7% of our total access lines supporting services of resale competitors throughout our 13-state area**, primarily in Texas, California and Illinois. **We expect resale access lines to increase, both absolutely and as a percentage of our total access lines, in 2001.** Many competitors have placed facilities in service and have begun advertising campaigns and offering services.