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March 1, 2002

VIA COURIER

RECEIVED

William Caton, Acting Secretary
Office of the Secretary
Federal Communications Commission
445 Twelfth Street, S.W.
Washington., DC 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Please deliver to:

236 Massachusetts Avenue, N.E.
Suite 110
Washington, D.C. 20002

Re: *In the Matter of Review of Regulatory Requirements for Incumbent LEC
Broadband Telecommunications Services, CC Docket No. 01-337*

Dear Mr. Caton:

Enclosed for filing in the above-referenced proceeding pursuant to the Commission's December 20, 2001 Notice of Proposed Rulemaking are an original and four paper copies of the Comments of US LEC Corp.

Please date stamp and return the enclosed extra copy of this filing. Should you have any questions concerning this filing, please do not hesitate to call us.

Respectfully submitted,



Harisha J. Bastiampillai

Enclosures

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

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of)
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Review of Regulatory Requirements for)
Incumbent LEC Broadband) CC Docket No. 01-337
Telecommunications Services)
)

COMMENTS OF US LEC CORP.

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March 1, 2002

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SUMMARY

In this proceeding, the Commission seeks to determine what regulatory treatment should be accorded to the provisioning of broadband services by incumbent local exchange carriers (“ILECs”). Specifically the Commission seeks to determine if ILECs should be granted non-dominant carrier status in the provisioning of broadband services. The Commission, however, defers the most crucial component of such a determination, the definition of broadband service, to another proceeding. The Commission then asks to address the ILECs’ market power in regard to broadband services. Determining the proper regulatory treatment for provisioning of broadband services begs the question of how broadband services is defined. By not addressing this question, and by seeking to determine policy without defining broadband services, the Commission is putting the cart before the horse.

Before the Commission can proceed with this rulemaking, it must first define what broadband services are. This is not an easy question, but the complexity of the task does not support deferring it. In fact, in determining the definition of broadband services the Commission will see that contrary to its pre-conceived notion that broadband service is distinct from traditional voice service, the two services are inextricably linked. The Commission will also see that broadband and voice service rely on many of the same facilities, and it is the ILECs’ control over these facilities, particularly last mile facilities, that precludes a finding of non-dominant status for ILEC provisioning of broadband service. At any rate, the Commission’s failure to address this threshold definitional issue renders its approach in this proceeding fatally flawed and counsels for the termination of the proceeding.

The Commission should, prior to terminating the proceeding, reject the proposition that ILECs should be accorded non-dominant status, and that such status would promote the

provisioning of advanced services. The ILECs' control over the underlying facilities to provide voice and broadband services gives them tremendous market power. This power will only increase as ILECs deploy next-generation loop architecture capable of supporting both traditional voice service and advanced services. Already ILECs are succeeding in impeding CLEC access to these facilities; granting ILEC non-dominant status will enhance the ILECs ability to preclude access by lessening regulatory scrutiny over the services they provide over these facilities. ILECs will be able to evade unbundling obligations under the guise that the services they are providing are "broadband" services. The failure of the Commission to define such services from the outset will only aid the ILEC cause.

It would be far too premature to accord ILECs non-dominant status in regard to broadband services. The broadband services market is too new and small to determine how market dynamics will play out. Already ILECs are succeeding in dampening competition from CLECs and independent Internet service providers seeking to use ILEC facilities. While ostensibly there may appear to be intermodal competition from cable, satellite and wireless providers currently cable is the only truly significant form of intermodal competition and that is only in the mass market. As new technologies roll out, such as fiber-to-the-curb, ILECs may be able to squeeze out cable competition. Even if such a scenario does not occur, the market will be a duopoly which will necessitate more regulation instead of less regulation.

According ILECs' non-dominant status would also mean the Commission would have to ignore the mandate of the 1996 Act to promote intramodal competition in regard to advanced services. Already ILEC customer growth in the advanced services market is outpacing CLEC growth. Allowing the ILECs a greater ability to leverage their control over their facilities would only heighten this market disparity. Plus intramodal competition is the only competition in the business market and the Commission would be imperiling this competition.

The not-so-subliminal ILEC threat that it will stop deploying new technology without deregulation speaks volumes about their market power. The fact that such a threat has fueled both this proceeding and action in Congress shows how ILECs are pulling the strings in the marketplace. The threat is a transparent one, however. ILEC investment, particularly in state-of-the-art facilities, has burgeoned since the 1996 Act. One of the great successes of the Act is that it has spurred investment both on the part of ILECs and new market entrants. Previously content to provide their traditional services, CLEC market entry spurred ILECs to invest in new facilities and services. The beneficiary of this investment was the marketplace in general. Protecting and enhancing this competition is crucial to continuing the advancement of the advanced services market. Deregulating ILEC provisioning of such services, particularly in the context of diminishing competition, will allow ILECs to return to their old ways. This is already seen in ILEC plans to scale back deployment and raise DSL prices. It is a lack of competition that is fueling the ILEC actions. Thus, if the Commission truly wants to spur deployment in the advanced services market it must promote competition and not imperil it through premature deregulation.

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In the Matter of)
)
Review of Regulatory Requirements Review)
of Regulatory Requirements for Incumbent) CC Docket No. 01-337
LEC Broadband Telecommunications)
Services)

US LEC Corp. ("US LEC") submits these comments in response to the Commission's notice of proposed rulemaking concerning regulation of incumbent local exchange carriers ("ILECs") provision of broadband telecommunications services.¹ As discussed in these comments, the Commission should terminate this proceeding in light of basic flaws in the approach and framework for analyzing market power set forth in the *NPRM*. The Commission, however, should prior to terminating the proceeding, unequivocally reject the ILECs' assertion that non-dominant status would promote the provisioning of broadband services.

I. THE COMMISSION'S FRAMEWORK FOR ANALYSIS OF MARKET POWER IS FUNDAMENTALLY FLAWED

A. The Commission Must Define "Broadband" Services.

In this proceeding, the Commission intends to determine the extent to which the ILECs retain market power in "broadband services." The Commission asks whether the ILECs' broadband service offerings are now subject to a sufficient degree of competition as to warrant streamlining the regulation of these service offerings.² The Commission, however, by failing to

¹ *Review of Regulatory Requirements for Incumbent LEC Broadband Telecommunications Services*, Notice of Proposed Rulemaking, CC Docket No. 01-337, FCC 01-360, released December 20, 2001 ("*NPRM*").

² *NPRM* at ¶ 7.

define what it means by “broadband services” renders the inquiry a non-starter. It does not even propose to define “broadband services” as an outcome of this rulemaking. The Commission expressly avoids the issue here and defers such definitional considerations to an entirely separate proceeding noting:

By using the term broadband services, we intend to avoid statutory-based definitional issues and instead focus on addressing the relevant markets in which these services participate. We will be addressing these issues in the forthcoming Title I broadband proceeding....”³

US LEC appreciates the difficulty in defining “broadband,” and it is the nebulous nature of such a definition that demonstrates why it is imprudent to consider deregulating ILEC provisioning of broadband services at this stage, particularly before even determining what such services are. Unless the Commission defines what it means by “broadband services,” it cannot determine that the ILECs are non-dominant in the provision of such services. As the Commission notes, “incumbent local exchange carriers are treated as dominant carriers, absent a specific finding to the contrary for the particular market.”⁴ It is uncontroverted that ILECs maintain bottleneck control over the facilities used to provide local exchange and exchange access services. The Commission recognizes that “broadband” services are often provided over these very same facilities over which the ILECs retain a stranglehold.⁵ It is hard then, if not impossible, to see how the Commission can segment out a particular class of services provided over these bottleneck facilities for non-dominant treatment without even defining the class of services.

³ *NPRM* at ¶ 17, n.37, referring to *Appropriate Framework for Broadband Access to the Internet Over Wireline Facilities*, Notice of Proposed Rulemaking, CC Docket No. 02-33, FCC 02-42, released February 15, 2002.

⁴ *NPRM* at ¶ 5.

⁵ *NPRM* at ¶ 6.

US LEC also cannot identify from the NPRM the relevant product market in which these services are bought and sold or explain any relationship with other product markets without defining what is a “broadband” service. Yet such a definition is, as the Commission acknowledges, fundamental to the question of whether the ILECs should be regulated as dominant carriers in their provision of these services. An even more basic problem is this: whatever form of regulation the Commission might decide to adopt for these services, how can it draft appropriate regulations if it does not face the question of exactly what services these regulations apply to? The Commission states: “While we recognize that parties’ identification of the relevant product markets may vary depending on the definition of ‘broadband services,’ our goal is to rigorously define the relevant markets so as to include all reasonably substitutable services.”⁶ Nevertheless, nowhere does the Commission state how it will determine which products are “reasonably substitutable” for a class of services which it declines to define in the first place.

It is crucial that the Commission address and dispense with any definitional hurdles prior to proceeding with this rulemaking. The folly of the Commission’s proposed approach is seen in the problems the Commission has had in implementing its reciprocal compensation policy without first cementing the proper definitional treatment for ISP-bound traffic. The U.S. Court of Appeals for D.C. Circuit panel addressing the appeal of the Commission’s reciprocal compensation order intimated that another remand might be in order because the definition of ISP-bound traffic was not properly grounded in the Telecom Act. The panel queried the Commission as to the basis for making forward-looking policy changes based on a “holding

⁶ *NPRM* at ¶18

clause” in the Act.⁷ Here the Commission states its intent to “avoid any statutory-based definitional issues” and defer these issues to another proceeding.⁸ Setting policy without addressing threshold definitional issues is putting the proverbial cart before the horse and is an infirm approach not only as a matter of policy, but also precludes any lawful resolution in this proceeding of “broadband” market power issues.⁹

As the Commission concedes, the issues raised in this proceeding are “more challenging” than its prior attempts at deregulation.¹⁰ For instance, when deciding to deregulate long distance service, the Commission had already surmounted definitional issues. The definition of a LATA provided a bright line definition of what constituted long distance service, and the facilities used to provide interLATA transport of calls were not the domain of one provider. Here there is no bright line between “broadband” and traditional voice service. In fact, broadband facilities can support a myriad of services including basic voice service. ILECs also control most of the vital facilities to provide “broadband” service. This is all the more reason why the threshold definitional issue be addressed first, and then only, a proceeding be initiated to consider the proper regulatory treatment for ILECs in regard to broadband services.

The Commission intimates that there is a distinction between the broadband services market and analog voice services “in which traditional common carrier regulation arose.”¹¹

Broadband service is still, however, inextricably linked to telephone service. Broadband is not

⁷ Edie Herman, *Judges Warn Remand Is Possible on FCC Reciprocal Compensation Order*, Communications Daily, Vol. 22, No. 30, at 1 (Feb. 13, 2002).

⁸ *NPRM* at ¶ 17, n. 37.

⁹ *See Motor Vehicle Manufacturers Ass'n of the U.S, Inc. v. State Farm Mutual Automobile Insurance Company*, 463 U.S. 29, 43 (1983) (“Normally, an agency rule would be arbitrary and capricious if the agency has relied on factors which Congress has not intended it to consider, *entirely failed to consider an important aspect of the problem*, offered an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it could not be ascribed to a difference in view or the product of agency expertise.”) (Emphasis added.)

¹⁰ *NPRM* at ¶ 6.

some new and distinct line of service divorced from traditional phone service. As economists

Robert Hall and William Lehr note in their paper, *Promoting Broadband Investment and*

Avoiding Monopoly:

If a Bell wanted to enter the breakfast cereal business, there would be no need for unbundling provisions on its activities in that business. Broadband is not breakfast cereal. Nearly all of the proposed broadband investments by the Bells represent incremental upgrades to the existing infrastructure. These investments are fully integrated with the Bell business plans and operations, and are closely coupled to the existing investment in the Bells' local networks.¹²

As they add:

it is difficult to draw a clear boundary between what constitutes investments in new infrastructure rather than the standard infrastructure. The whole vision is to migrate to a broadband platform that is capable of supporting integrated services.¹³

An example of this is Project Pronto which is perhaps the prototype of network investment that ILECs seek to remove from traditional dominant carrier regulation. This investment was sold to SBC's investors, however, as something that not only would allow for the greater deployment of DSL, but that would produce savings in operating costs for current services and savings on future facilities expansion.¹⁴ Provision of voice service is an integral part of the Project Pronto offering. The line where broadband begins and voice service ends is nebulous, if in fact there is any line at all.

For all of these reasons, the Commission's failure to consider the definition of broadband services in this proceeding precludes any rational or lawful determination of the extent to which

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¹¹ *NPRM* at ¶ 5.

¹² Robert E. Hall and William H. Lehr, *Promoting Broadband Investment and Avoiding Monopoly*, at 12 (Feb. 21, 2002). A copy of the paper may be found at:

<http://www.sandhillecon.com/Broadband.PDF>.

¹³ *Id.*

¹⁴ *Id.*

ILECs have market power in the provision of “broadband” services. Any record developed herein will therefore be insufficient by definition to support any determination of whether ILECs remain dominant in the provision of “broadband” services. Moreover, while the Commission may craft a definition of “broadband” based on the record, it will need to issue a further NPRM in light of that definition before it could lawfully establish any regulatory framework for it.

If the Commission establishes a regulatory framework before defining broadband services it embarks on a slippery slope that could undermine all the market-opening aspects of the 1996 Act. As Hall and Lehr note:

Deregulating prospective broadband investment assures the sunset of open access provisions of the Telecom Act. If granted, the Bells may be able to classify nearly all of its investment opportunistically as intended for broadband data services to avoid pro-competitive unbundling and interconnection obligations. In a converged network, voice can be carried as data (Voice-over-IP services) raising the possibility that even facilities used for legacy services would avoid unbundling obligations. As increasing portions of the network become “broadband” – and hence unregulated – it will become increasingly difficult to implement unbundling and interconnection rules for the rest of the Bells’ local access networks.¹⁵

The dangers of premature deregulation are more acute in the local exchange context than they were in the long distance context. When AT&T was given non-dominant status, the long distance market was thriving and had many market participants. Today in both the local exchange market and the advanced services market, competition is tenuous, and premature deregulation could dim the prospects for competition.

B. The Commission Must Not Underestimate The Tremendous Leveraging Power of the ILECs.

The framework for assessing ILEC market power described in the *NPRM* fails to take into account the interdependence of the various described “broadband” services with each other and with the ILECs’ local exchange service. As a result of this interdependence, any declaration

that the ILECs have become non-dominant in the provision of broadband services would be unsupportable.

The Commission suggests¹⁶ that at least two relevant product markets may exist. In one, the “mass market,” the only ILEC offering it cites is xDSL.¹⁷ By contrast, in the other relevant product market tentatively identified by the Commission, the “larger business” market, the Commission identifies several ILEC offerings as being potentially included. These include Frame Relay, Asynchronous Transfer Mode (“ATM”), Gigabit Ethernet (“GigE”), Switched Multimegabit Data Service (“SMDS”) and Remote Local Area Network (“RLAN”) service.¹⁸

The Commission suggests that it could find ILECs non-dominant in one or more of these markets *notwithstanding the fact that the ILECs continue to have market power with respect to basic local exchange service and that all these services are provided over the same local exchange and exchange access facilities.*¹⁹

The failure of the *NPRM* to recognize the importance of this interdependence between “broadband” services and the facilities that support such services is fatal to the deregulation the *NPRM* espouses. Even if ILEC broadband offerings taken on a stand-alone basis are potentially subject to competition (*e.g.*, from cable modems, as the Commission suggests), the ILECs’ ability to pursue this market stems from their ability to piggy-back the construction of broadband

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¹⁵ Hall and Lehr at 14.

¹⁶ *NPRM* at ¶¶ 19-22

¹⁷ The Commission identifies cable modem, fixed wireless and satellite services – all non-ILEC services – as other products that might provide “intermodal” competition in the mass market. *NPRM* at ¶ 21.

¹⁸ The Commission states that it will not consider whether traditional special access services (and by implication, traditional data private line services) belong in the larger business market “as these services are governed by the Commission’s pricing flexibility regime.” *NPRM* at ¶ 22. But this is a non sequitur. The issue of whether these services are in this market has to do with the degree to which customers see them as substitutes for each other, not with how they are classified for regulatory purposes. Of course, leaving them out of the analysis will also have the effect of significantly understating the ILECs’ market share.

facilities upon the core voice telephone network.²⁰ This gives the ILECs a significant economic advantage of integration that is unavailable to competing, non-integrated providers. Inevitably, they will be able to leverage this integration in a manner that effectively excludes CLECs from significant segments of the market, and they are doing so today. Even cable providers, for whom cable telephony is a nascent offering, cannot offer the power of the integrated package that ILECs are able to offer.

As economists Hall and Lehr argue:

But the on-ramps to the information highway remain in the hands of the monopolists. The last mile of the telecom network lacks the competition that has invigorated the rest of the network. The last mile remains in the hands of the traditional phone companies, the Bells. Bell control of the last mile means that continuing regulation is essential. Because homeowners and small businesses rarely have ways to gain access to the telecom network apart from the Bells' last mile connections, the Bells could extract full monopoly value of the network if they were not regulated. As competitive service providers add value to telecom products, the Bells would absorb that value through higher prices for the last mile, and consumers would be denied the benefit of added value.²¹

One illustration of this problem is the ILECs' practices with regard to deployment of next-generation loop architecture, which has an enormous impact on competition in what the Commission would refer to as the mass market. The tales of the preclusive impact the deployment of such architecture will have on competition has filled the records of numerous proceedings conducted by the Commission. US LEC directs the Commission to the record in

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¹⁹ As Chairman Powell notes in his separate statement (at page 1) the ILECs remain "clearly dominant" in local exchange service.

²⁰ For instance, Project Pronto is an overlay of the existing SBC network meaning it will not displace existing network facilities.

²¹ Hall and Lehr at 3.

Docket Nos. 96-98, 98-141, and 98-147 as to the ability of ILECs to be able to preclude access to customers through use of next-generation loop deployment.²²

ILECs are rapidly extending fiber into feeder plant and are deploying DSLAMs at remote terminals (“RTs”), where the fiber is cross-connected with copper distribution plant, in each of the various neighborhoods served by the same central office wire center building, bypassing CLEC interconnections and/or collocated facilities at the central office. This hybrid fiber/copper loop plant is used jointly to provide ordinary telephone service as well as xDSL services, yet the ILECs refuse to allow CLECs either to interconnect with the DSLAMs at the RTs or to collocate their own facilities at those network points. This effectively denies CLECs access to the copper loop and precludes them from providing xDSL services to end users served by the RTs. Thus, if left unchecked, ILECs can eliminate CLECs as a competitor in the “mass market.” Such practices can also preclude competition in the business market.

There is a concern that “ILECs will extend their monopoly power over local telephony to advanced services by operating and controlling next-generation networks in a manner that ensures that only the ILECs (and their data affiliates) will be able to recognize the full benefits of new network technology and architecture.”²³

²² See *Deployment of Wireline Services Offering Advanced Telecommunications Capability and Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket Nos. 98-147, 96-98, Third Report and Order on Reconsideration and Third Further Notice of Proposed Rulemaking in CC Docket No. 98-147, and Fourth Report and Order on Reconsideration and Sixth Further Notice of Proposed Rulemaking in CC Docket No. 96-98, FCC 01-26 (January 19, 2001) (“*Line Sharing Recon. Order & FNPRM*”); *In the Matter of Ameritech Corp., Transferor, and SBC Communications, Inc., Transferee, for Consent to Transfer Control of Corporations Holding Commission Licenses and Lines Pursuant to Sections 214 and 310(d) of the Communications Act and Parts 5, 22, 24, 25, 63, 90, 95, and 101 of the Commission Rules*, CC Docket No. 98-141, ASD File No. 99-49, Second Memorandum Opinion and Order, FCC 00-336 (Sept. 8, 2000) (“*Project Pronto Order*”); *In the Matters of Deployment of Wireline Services Offering Advanced Telecommunications Capability and Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket Nos. 98-147, 96-98, Order on Reconsideration and Second Further Notice of Proposed Rulemaking in CC Docket No. 98-147, and Fifth Further Notice of Proposed Rulemaking in CC Docket No. 96-98, FCC 00-297 (August 10, 2000) (“*Collocation Reconsideration Order and NPRM*”).

²³ *In the Matters of Deployment of Wireline Services Offering Advanced Telecommunications Capability; Implementation of the Local Competition Provisions of the Telecommunications Act of 1996; Application for*

(continued....)

By this stratagem, ILECs can effectively block CLECs from competing in the “mass market” for broadband services unless the CLECs are prepared to overbuild the *entire* ILEC feeder *and* distribution network. The Bell infrastructure is already immense, approximating \$333 billion of historical investment. Getting to the next generation of networks will require billions of additional dollars of additional investment.²⁴ It goes without saying that such an overbuild could not be justified as an economic matter. As Hall and Lehr contend:

It appears likely to be inefficient for competing suppliers to entirely duplicate fiber last-mile networks. If each home should have only one all-fiber broadband circuit, then suppliers of other services such as local and long distance transport and Internet services and products, should compete to use the single pipe to the home. Even in the local network, regardless of the last-mile fiber economics, competition is the right model for local switches, backhaul facilities, and additional equipment such as web servers, DSLAMs, or other equipment specifically intended to support broadband services. And it goes without saying that competition should remain where it is flourishing already, in medium and long-distance transport and in Internet services and products.²⁵

While Chairman Powel suggests that this proceeding will not detrimentally impede the unbundling obligations of the ILECs,²⁶ ILECs, in a deregulatory environment, can manipulate their relationships with their affiliates to preclude competitive access to these vital last mile facilities. For instance, SBC offers a Gigabit Ethernet service on its web site. Gigabit Ethernet is one of those services that the *NPRM* suggests may be part of a “larger business market” for broadband services.²⁷ SBC describes the product as follows:

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Consent to the Transfer of Control of Licenses and Section 214 Authorizations from Ameritech Corporation, Transferor to SBC Communications, Inc., Transferee; Common Carrier Bureau and Office of Technology Announce Public Forum on Competitive Access to Next-Generation Remote Terminals, CC Docket Nos. 98-147, 96-98, 98-141, and NSD-L-00-48, Reply Comments of AT&T Corp. at p. 12 (July 10, 2000)(“AT&T ALTS Petition Reply Comments”).

²⁴ Hall and Lehr at 5-6.

²⁵ Hall and Lehr at 5.

²⁶ *NPRM*, Separate Statement of Chairman Michael K. Powell at 1.

²⁷ *NPRM* at ¶ 22.

Gigabit Ethernet Service is a logical extension of Native LAN Services at a cost that is 70% below ATM (according to Business Communications Review). Gigabit Ethernet Service provides up to a 10 gigabit LAN/WAN extension of your customer premise equipment (CPE) gigabit switches between two locations. This transport service operates over single-mode fiber optic cables connected to fiber extender equipment located at or near your premises. Gigabit Ethernet service supports and complies with the IEEE 802.3z Ethernet LAN standard.²⁸

This product is offered not by SBC but through SBC Global. As with SBC's relationships with its other affiliates such as Southwestern Bell Internet Services and SBC-ASI, the precise relationship between SBC Global and SBC is unclear.²⁹ It is clear, however, that SBC is marketing telecommunications services which would normally be subject to Section 251(c) obligations if it was offered by SBC. Through deregulation, SBC would be able to leverage its control over vital last mile facilities to benefit exclusively its affiliate, and by extension, itself.

Tariffs are an especially vital part in policing against such nefarious activities. Requiring ILECs and their affiliates to tariff its product offerings with an adequate notice period and with adequate cost support will enable competitors to examine these offerings to ensure that the affiliate or its parent are not attempting to evade Section 251(c) requirements. For instance, the ILEC could use a one day notice period or contract tariffs to mask a product that it would otherwise be required to provide on a resale or unbundled basis to competitors. Allowing the ILEC or its affiliate the ability to offer services without cost support would also enhance the ability of ILECs to evade the requirements of the Act. The parent may offer the service at a below cost price to its affiliate and without cost support this discriminatory treatment could not be discerned.

²⁸ <http://global.sbc.com/content/0,4109,13,00.html#gigabit>

²⁹ SBC explained that ASI and SBIS are affiliates within the same corporate family and do "not necessarily reflect the strict separation between the responsibilities of a wholesale telecommunications provider and the 'consumer-oriented tasks' of a retail information service provider . . ." CC Docket No. 01-194, Comments of WorldCom at 9 (September 10, 2001).

These are but some examples of the anticompetitive behavior that the ILECs are already engaged in, and the potential for further anticompetitive behavior, which demonstrates that ILECs control of the facilities used to provide dominant local exchange services and broadband services is a circumstance that by itself precludes any finding of nondominance for broadband services even if there is some competition in provision of the end product to consumers. On this basis alone, the most useful step the Commission could take at this point would be to promptly terminate this proceeding.

C. The Broadband Market Is Too New and Small to Permit Deregulation.

The ILECs argue, in effect, that their ability to leverage control of local exchange facilities ability does not actually exist because, so far anyway, they have not succeeded in monopolizing the broadband market. In its petition for non dominant treatment,³⁰ for example, SBC argues that it cannot possibly be dominant in broadband in the mass market, because, to date, there are more cable modem users nationwide than there are xDSL users. But this is hardly conclusive. Current mass market penetration for broadband services remains extremely low.³¹ It is simply not possible to extrapolate what the ultimate market structure will be from market shares that exist at this nascent stage. And even if one believes that intermodal competition from cable modems, satellite and fixed wireless is real, premature deregulation of the ILECs could snuff it out as the market size increases and ILECs take more and more advantage of their leveraging opportunities.

The ability of ILECs to leverage their market power in the advanced services market cannot be underscored enough. This power is already seen in the successful attempts of the

³⁰ SBC Petition for Expedited Ruling That It Is Non-Dominant In Its Provision of Advanced Services And For Forbearance From Dominant Carrier Regulation of Those Services, p. 38.

ILECs to stifle competition from independent Internet Service Providers. The Office of Public Utility Counsel of Texas (“OPUCT”) noted in the Commission’s Intercarrier Compensation proceeding, that “ILECs have consistently been at war with ISPs and when given the opportunity will discriminate against this class of customers.”³² To demonstrate ILEC unwillingness to serve ISPs, OPUCT quotes from a brief filed by Texas Internet Service Provider Association in which that organization stated:

ISPs have been fortunate that competitive carriers have sought to provide service to them – at reasonable prices and terms. SWBT never competed for service to ISPs; rather the ILEC has been *hostile, unyielding, and antagonistic*. SWBT has refused to provide PRI service to ISPs in many areas, despite Commission rules requiring statewide availability. SWBT favors the SBC Internet affiliate in numerous ways, for dial-up and DSL service. SWBT has continually sought to leverage its continued dominance in the local market into a large share of the enhanced services market and has done everything it can to harm ISPs. At every turn, ISPs throughout the state have discovered that SWBT perceives them to be competitors; a group that must be driven from business, and certainly not deserving of high-quality, reliable and affordable local service.³³

Last year, Verizon implemented new policies which impinged on the ability of small and mid-size ISPs to provide broadband service. Verizon implemented a policy for carriers that plan to use its network for advanced services that requires them to contract, at a minimum, for an OC-3 line.³⁴ An OC-3 is a large and costly facility that will impede the ability of small and medium-sized competitors to utilize Verizon’s network.³⁵ Normally, the minimum requirement starts at a

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³¹ The various sources cited by SBC are widely disparate in their estimates of xDSL and cable penetration. Nevertheless, they agree that only a few million households have either of these services or other broadband services today.

³² CC Docket 01-92, Comments of The Office of Public Utility Counsel of Texas at 27 (Aug. 21, 2001).

³³ *Id.*, quoting Proceeding to examine Reciprocal Compensation Pursuant to Section 252 of the Federal Telecommunications Act of 1996, Public Utility Commission of Texas, Docket No. 21982, TISPA *Amicus Curiae* Brief at 3.

³⁴ Jim Wagner, *Verizon Ups Ante for Small ISPs*, http://www.internetnews.com/isp-news/article/0,,8_581301,00.html.

³⁵ *Id.*

T-1 and scales upward to a DS-3, and only later, an OC-3. Many carriers who are purchasing Verizon's wholesale service already experience "stalled installation times and bungled billing procedures," and will now be required to have a high threshold of traffic to "qualify" for this substandard service.³⁶ Since Verizon controls these vital facilities, it can manipulate the terms of access to such facilities to impede competition. This is a further example of how ILECs can leverage their control over facilities to dominate the advanced services market. It is ironic that as cable providers are evolving to a more open access model,³⁷ ILECs are setting the table such that their affiliated ISP will be sole provider of advanced services over their facilities.

In short, it is far too early in the development of provision of "broadband" services for the Commission to make any generalizations about the market power of ILECs. In light of this, the Commission should also promptly terminate this proceeding.

D. The NPRM Does Not Adequately Consider Intramodal Competition.

In the Commission's and SBC's focus on intermodal competition, the Commission overlooks the continuing vital role of the CLECs in this market. It is clearly part of the fundamental policy of the Telecommunications Act that *intramodal* competition, from competing carriers such as CLECs that rely in part on interconnection with ILEC facilities, is to be fostered. The Commission must be careful to ensure that its focus on intermodal competition does not result in a regulatory structure that facilitates the ILECs' continuing efforts to eliminate intramodal competition. Intramodal competition is already suffering. Of the 2.7 million high-speed DSL lines, about 93% of these lines were reported by incumbent local exchange carriers (LECs); about 86% of these lines were reported by the Regional Bell Operating Companies

³⁶ *Id.*

³⁷ Time Warner and Comcast have both announced plans to have multiple ISPs access their facilities. See Birgitte Greenberg, *FCC's 'Tentative Conclusion' Spawns Cable Industry Scramble*, Communications Daily, Vol. 22, N0.

(continued...)

(RBOCs); and about 7% of these lines were reported by non-ILECs.³⁸ ILEC DSL customer

growth rates are now fast outstripping CLEC customer growth rates.³⁹ The Commission should

be wary of what deregulation will mean for intramodal competition. As Hall and Lehr warn:

Current policymaking needs to consider the implications of today's decisions for the future. If the policy regime adopted today excludes rivalry in broadband services over the Bells' last mile facilities, the Bells will become the single entrenched provider of broadband service over the existing copper and hybrid fiber/copper loops; the only rivals in broadband will be cable companies. Thus broadband will have only two sellers, and a duopoly with a Bell and a cable provider may fail to offer vibrant competition. Either broadband customers will pay high prices or regulation will need to be extended to broadband services.⁴⁰

Thus, by deregulating now, the Commission may be planting the seeds for even more permanent regulation in the future.

E. The ILECs' Argument That Only They Can Provide Widespread Broadband Development Underscores the Fact That They Retain Market Power.

There should be no doubt that the elimination of potential competition from CLECs in provision of broadband services is the ILECs' goal. They have been arguing in a variety of arenas that their Section 251 and 252 obligations to provide CLECs with access to facilities, as well as dominant carrier regulation itself, cause them not to make the necessary investments to allow the widespread deployment of broadband services – and so, they assert, these burdens should be lifted. But it is here that their argument reveals its internal inconsistency. For the ILECs go on to claim that if they don't make this investment then nobody else will either, and that the nation will therefore be deprived of this valuable resource. Yet this argument flies in the

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33 at 2 (Feb. 19, 2002). (“AOL TW in recent months has been speaking out publicly about benefits of such a business model, saying that offering several ISPs over pipe would draw more customers to overall product.”)

³⁸ *FCC Releases Report on the Availability of High Speed and Advanced Telecommunications Capability*, FCC Press Release (Feb. 6, 2002)

³⁹ *Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996*, CC Docket No. 98-146, Third Report at ¶ 51 (Feb. 6, 2002).

face of their other claim: that the market is *already competitive* – which could only be true if other parties have in fact made investments toward providing such services. The truth is that the ILECs need to maintain the fiction of a robustly competitive market in order to justify the regulatory freedoms they are seeking, but also need to hold the club of a refusal to invest altogether and thus to deny the nation a broadband network in order to pressure the Commission to give them what they want. ILECs' arguments are in reality no more than the traditional argument of dominant carriers, *i.e.*, promises to provide new services in exchange for permitting them to keep their monopoly. The Commission should recognize that this argument verifies that they are dominant carriers and so find in this proceeding.

F. Intermodal Competition Is Insignificant.

Finally, the *NPRM* greatly exaggerates the extent of intermodal competition in the provision of “broadband” services. Upon closer review, it is clear that intermodal competition is far too insignificant to justify a conclusion that it constrains ILECs' market power. As Hall and Lehr observe:

Preferential regulatory treatment of the Bells' broadband operations also cannot be justified on the basis that they face adequate competition already. It is true that the Bells account for less than half of current broadband subscribers. Cable modem services have a larger share of current residential broadband services, but this does not lead to the conclusion that the Bells lack substantial market power with regard to those services. The Bells control the copper loops that are an essential input for the provision of DSL services and the Bells are the largest providers of DSL-based broadband services. We have noted earlier that cable operators, as half of a duopoly structure could not be expected to be vigorous broadband customers.⁴¹

It is also, as noted above, too early to anoint cable as a viable competitor to ILEC provisioning of advanced services. If the technology of choice for next generation access

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⁴⁰ Hall and Lehr at 9.

⁴¹ Hall and Lehr at 13.

networks turns out to be fiber-to-the-home, it will almost certainly be a single-circuit natural monopoly, and undoubtedly one controlled by the ILECs.⁴²

As to the “larger business” market, the Commission has identified no intermodal competition at all. All the services cited as examples in this market – Frame Relay, ATM, GigE, SMDS and RLAN – are offered by ILECs. A competitive analysis of broadband needs to consider the total local access market for data services which remains dominated by Bell-provided leased line and other data services. The ILECs, however, are only motivated to provide such services when competitors begin to offer services. In the 1980s, Teleport’s provisioning of DS3 access services prompted the RBOCs to enter that market. It was the growth of competition from market entrants offering DSL service over Bell facilities that spurred the Bells to accelerate their own deployment of DSL services. The Bells were influenced by a desire to protect their substantial data service revenues from competitors.⁴³ Thus, in this part of the market, intramodal competition is all there is. But the *NPRM* fails to set forth any effective method for protecting this market from the ILECs’ leveraging their control over bottleneck facilities and eliminating intramodal competition as well.

As to the “mass market,” the Commission identifies three “service platforms” as intermodal competitors for the ILECs’ xDSL offerings: cable modem service, satellite and fixed wireless. But none of these is a serious competitor for xDSL at this point in time. First, while cable is touted as the most important competitor for xDSL, only a third of American homes can currently choose between wireline and cable broadband services. That means that, for two thirds of homes, no intermodal competition between cable and xDSL exists at all.⁴⁴ Should an ILEC

⁴² Hall and Lehr at 15.

⁴³ *Id.* at 14.

⁴⁴ McKinsey & Co. and J.P. Morgan H&Q, *Broadband 2001: A Comprehensive Analysis of Demand, Supply, Economics, and Industry Dynamics in the U.S. Broadband Market* (April 2001), pp. 40-43.

raise xDSL prices, the vast majority of its subscribers would *not* have a cable alternative. Thus, there is no viable intermodal competition from cable.

Second, satellite services pose no significant competitive threat to xDSL, for several reasons. First, some of these services are really just a subset of somewhat improved dial-up services.⁴⁵ Moreover, to date they are being priced in the range of \$70 per month,⁴⁶ hardly competitive with the pricing of xDSL, at \$50 per month.⁴⁷ In terms of market power, this means that an ILEC could raise its xDSL rates by *forty percent* and still not fear losing customers to the satellite providers – and there would be some significant premium it could collect even above that for its faster service. The Commission cannot base a finding of intermodal competition on the satellite services market.

Fixed wireless providers are no greater a competitive threat due in part to the logistical difficulties and technical limitations that constrain its roll-out.⁴⁸ These include difficulty in obtaining access to rooftops to install antennas, line-of-sight requirements, spectrum scarcity (which also affects satellite services), small cell sizes for some bands, and weather issues. In fact, during the latter half of 2001, a number of companies offering innovative wireless services either went bankrupt or scaled back their investments in wireless alternatives to local loops.⁴⁹ Small wonder, then, that satellite and fixed wireless together only accounted for a paltry 73,476 lines as of June 2001, barely one percent of the market. It is clear that fixed wireless providers are not providing intermodal competition.

⁴⁵ *Third Advanced Services Report*, Appendix B, ¶ 47.

⁴⁶ Hughes pricing at <https://register.earthlink.net/cgi-bin/wsisa.dll/broadband/satellite/pricing.html?drm=9cd9e606ce965ab8b7856265874157fb>; StarBand pricing at <http://www.starband.com/faq/starbandfacts.htm#cost>.

⁴⁷ See, e.g., Verizon “Pricing and Packages,” http://www22.verizon.com/foryourhome/dsl/order/NLF_vzolproductsprequalify.asp

⁴⁸ *Third Advanced Services Report*, Appendix B, ¶ 34 *et seq*

⁴⁹ Hall and Lehr at 15.

It is evident that none of the intermodal competitors identified by the Commission seriously constrains the ILECs' market power. The regulatory "relief" they request would enable them to wipe out the possibility that CLECs or other future market entrants or technology improvements could ever provide effective intramodal competition, and diminish – and probably eliminate – the possibility that effective intermodal competition could ever arise.

II. ILEC DEREGULATION WILL NOT FURTHER THE GOAL OF WIDESPREAD PROVISION OF BROADBAND TELECOMMUNICATIONS SERVICES AND MAY IMPEDE FURTHER DEPLOYMENT

A. ILECs Are Already Rapidly Deploying Broadband Capability

Assuming there were any basis for finding ILECs' nondominant in provision of "broadband" services, which there is not, there is no reason to believe that such treatment would promote their construction of because ILECs are already building them. For example, only 7 months ago, in June 2001 Verizon informed the New York Public Service Commission that the "unprecedented and unpredictable demand" for high speed data circuits required increased capital spending and the deployment of new technologies.⁵⁰ In 2000, Verizon's capital spending for special access services was nearly 4 times the amount spent just 3 years earlier. In 1999, SBC launched "Project Pronto," a \$6 billion investment in high-speed residential broadband services to residential consumers. Despite the fact that they had previously ignored DSL, SBC and other ILECs proclaimed that it and other advanced services were "strategic growth driver[s]."⁵¹ More recently, in a January 24, 2002, "Investor Briefing" SBC announced that it had expanded its DSL-capable footprint by 37% in 2001 and that it had the "industry's largest

⁵⁰ See Opinion and Order Modifying Special Services Guidelines for Verizon New York Inc., Conforming Tariff, and Requiring Additional Performance Reporting, Cases 00-C-2051 and 92-C-0665, Opinion No. 01-1, NYSPSC, June 15, 2001, p. 10.

⁵¹ SBC Investor Briefing No. 226, http://www.sbc.com/Investor/Financial/Earning_Info/docs/2Q_IB_FINAL_Color.pdf, at 5 (July 25, 2001) ("SBC Second Quarter Briefing").

DSL Internet customer base.”⁵² SBC’s public pronouncements regarding data services provided to enterprise customers were equally glowing. SBC announced growth for data services of between 14.4% and 27.9% in 2001 and 16.9% in the fourth quarter of 2001 for high-speed data transport services.⁵³ For its part, BellSouth announced 25% growth in data revenues and a 189% increase in DSL subscribers in 2001, which BellSouth noted was “the fastest growth of any DSL or cable provider in the country.”⁵⁴ BellSouth claimed that it had “the most aggressive DSL deployment strategy in the industry” and that it had increased its DSL coverage from 45% to 70% of households in 2001.⁵⁵

Obviously, these ILECs deployed the broadband facilities, including fiber in the loop, and made these impressive gains possible under dominant carrier regulation.⁵⁶ Therefore, apart from any other reason, there is no reason to believe that dominant carrier regulation has, or will, inhibit to any degree ILECs’ investment in broadband infrastructure.⁵⁷ Since the 1996 Act, the Bells have cumulatively invested \$100 billion which is 22% higher than the four year period

⁵² SBC Investor Briefing No. 228, http://www.sbc.com/investor_relations/financial_and_growth_profile/investor_briefings/1,5869,253,00.html, at 2 and 5 (Jan. 24, 2002) (“SBC Fourth Quarter Briefing”).

⁵³ SBC Second Quarter Briefing, at 4; SBC Third Quarter Briefing, at 4; SBC Fourth Quarter Briefing, at 4.

⁵⁴ BellSouth investor news, “BellSouth Reports Fourth Quarter Earnings,” http://www.bellsouth.com/investor/pdf/4q01p_news.pdf (Jan. 22, 2002).

⁵⁵ *Id.* Qwest, while lagging behind the other ILECs, nevertheless had impressive growth as well. In January 2002, Qwest announced that DSL customers increased by 74% and revenues from DSL services by 66% in 2001. “Qwest Communications Reports Fourth Quarter, Year-End 2001 Results,” http://media.corporate-ir.net/media_files/NYS/Q/q_1_28_02earnrel.htm (Jan. 29, 2002).

⁵⁶ For a time, SBC and Verizon provided advanced services through affiliates that the Commission had determined were presumptively nondominant. However, the cited network investments were made by the parent companies.

⁵⁷ The ILECs also were able to compete effectively for DSL and other data customers. Verizon, for example, reported a 122% increase in DSL subscribers and a 21.2% increase in data transport revenues in 2001. “Verizon Communications Reports Solid Results For Fourth Quarter, Provides Outlook for 2002,” http://investor.verizon.com/news/VZ/2002-01-31_X263602.html (Jan. 31, 2002). Verizon also announced that it had deployed DSL to central offices serving 79% of Verizon’s local access lines and that its total number of data circuits in service had increased 53% from 2000. News Release, “Verizon Communications Second Quarter Earnings Highlighted by Strong Long-Distance and Wireless Sales,” <http://newscenter.verizon.com/proactive/newsroom/release.vtml?id=59168> (July 31, 2001).

preceding passage of the Act.⁵⁸ The sustained high market valuations of the incumbents even through the current slump in the telecom sector provide potent evidence that investors believe that ILECs are getting a fair return on their investments so competitive access to ILEC facilities has not dampened their market prospects.⁵⁹

B. Competition Is The Best Incentive For Infrastructure Investment For All Industry Players

Apart from the fact that ILECs' previous and ongoing substantial broadband infrastructure investments refute ILEC claims that dominant carrier regulation inhibits such investment, it is also evident that the threat of competition provides the best incentive for ILECs to invest in broadband networks. In fact, the ILEC's pattern of deployment of DSL capable networks perfectly illustrates that competition is the best way to encourage ILECs to deploy broadband networks.

In a nutshell, ILECs ignored DSL until CLECs began to deploy it. As President Clinton's Council of Economic Advisers stated in early 1999:

Although DSL technology has been available since the 1980s, only recently did [the ILECs] 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-competition provisions of the Telecommunications Act of 1996 to provide DSL over the incumbents' facilities.⁶⁰

Or, as stated more succinctly by James Glassman, the ILECs "kept cheaper DSL on the shelf for a decade" to protect their higher revenue services.⁶¹ Bells were slow to deploy DSL because of

⁵⁸ Hall and Lehr at 5.

⁵⁹ Hall and Lehr at 10.

⁶⁰ ALTS New Economy Analysis at 4 (citing Council of Economic Advisers, Economic Report of the President, February 1999, pp. 187-188, <http://w3.access.gpo.gov/usbudget/fy2000/pdf/erp.pdf>)

⁶¹ James Glassman, "Best Remedy for Recession? Break Up the Bells," <http://www.techcentralstation.com/NewsDesk.asp?FormMode=MainTerminalArticles&ID=131> (December 10, 2001).

its affect on their ability to sell second lines and alternative high-priced, high-speed services such as T1s to business customers.⁶² That decision is unsurprising and perhaps even economically rational from the ILECs' point of view, but consumers and businesses were required to bear the higher costs and poorer quality of the ILECs' actions earlier "high speed" services. Competition from CLECs thus was pivotal in furthering the deployment of DSL and other advanced services. Even today, Bells will resist providing Internet-based videophone or even Internet-based standard phone service because it "cannibalizes their existing products."⁶³ Absent the spur of competition, ILECs will reduce their own investment commitments to avoid cannibalizing lucrative revenues from leased line and other data services to businesses and second lines to consumers.⁶⁴

As described in the previous section, ILECs responded by increasing their capital spending and the coverage of their DSL-capable networks. Prior to the introduction of commercial DSL services by competitors, the ILECs did little or nothing to encourage the development or deployment of new advanced services, preferring to focus on their existing, and more lucrative, data services. Thus, it was the threat of competition of CLECs, particularly since DSL holds the promise some day of providing competition in voice service, that stimulated ILEC infrastructure investments necessary to provide this broadband service.

Moreover, it is not coincidental that after two of the "big three" CLEC DSL providers terminated operations and the third filed for bankruptcy that some ILECs announced they were scaling back somewhat DSL investment, although this did not prevent them from making the record-breaking growth discussed above so that they now control 90% of customers. Thus, in

⁶² Hall and Lehr at 3.

⁶³ Hall and Lehr at 3.

⁶⁴ Hall and Lehr at 9.

October 2001, SBC quietly scaled back its original deployment plan for Project Pronto and reduced capital spending by 20% in 2002.⁶⁵ In short, to the extent any diagnosis other than the general recession is needed to explain these modest scalebacks, it is that ILECs no longer needed to make the investment in light of the diminished threat of competition from CLECs. It also worth noting that some ILECs substantially raised prices for DSL service, which never would have happened in a competitive market. Thus, in October 2001, SBC raised its wholesale prices for DSL services by approximately 15% (while admitting that its cost to provide DSL connectivity was declining).

As a group of distinguished economists explained in a December 2001 letter to Commerce Secretary Donald Evans: “both history and economic theory have taught us [that] deregulating a monopoly without genuine prospects for competition does not induce it to deploy more infrastructure, only to exploit more severely the infrastructure that it has already in place by limiting its use and raising its price.”⁶⁶ Thus, in a perfect illustration of this point, SBC reduced investment and raised prices as soon as the threat of broadband competition diminished.

C. Regulation Is Not Impeding The Rapid Deployment of “Broadband”

The Commission recently concluded that the deployment of advanced telecommunications capability was occurring on a reasonable and timely basis.⁶⁷ Therefore, there is no reason to find that nondominant status or any other possible ill-advised steps under consideration in other proceedings are necessary to promote deployment of advanced telecommunications capability. Nonetheless, to the extent that the Commission concludes that

⁶⁵ SBC Advanced Solutions, Inc., Tariff FCC No. 1, pp. 60-69 (eff. Sept. 10, 2001); SBC Second Quarter Briefing, at 5.

⁶⁶ Letter from William J. Baumol et al. to Hon. Donald L. Evans et al., dated December 11, 2001, at 3.

⁶⁷ *Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996*, Third Report, CC Docket No. 98-146, FCC 02-33, released February 6, 2002, at para. 1.

broadband is not being deployed rapidly enough, it is clear that there are circumstances other than ILEC complaints about regulation that fully explain the current pace of deployment of broadband. As Hall and Lehr conclude, “recent disappointments in DSL are the result of the collapse of many of the new rivals, the subsequently higher prices charged by Bells once they no longer face competition, and because of the poor quality of service offered by the Bells that have turned many would-be consumers away.”⁶⁸ Deregulating ILEC provisioning of advanced services will only heighten this downturn, and not alleviate it.

For these reasons, there is no rational basis for the Commission to conclude that nondominant treatment of ILECs’ provision of broadband services would promote broadband networks. In reality, ILEC arguments on this issue and promises to develop broadband networks are no more than self serving efforts to manipulate policy makers and should be rejected as such.

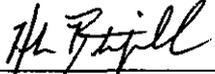
⁶⁸ Hall and Lehr at 8.

III. CONCLUSION

For these reasons, the Commission should promptly terminate this proceeding after concluding that deregulation of ILECs would not promote the goal of widespread deployment of broadband services to all Americans.

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March 1, 2002

CERTIFICATE OF SERVICE

I, Harisha Bastiampillai, hereby certify that on March 1, 2002, I caused to be served upon the following individuals the Comments of US LEC Corp. in CC Docket No. 01-337:



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