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

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

REPLY COMMENTS OF FOCAL COMMUNICATIONS CORPORATION AND PAC-WEST TELECOMM, INC.

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SUMMARY

The incumbent local exchange carriers ("ILECs") have seized upon this proceeding as an opportunity to press for complete deregulation of their broadband service offerings. They make a variety of wildly inflated claims as to the competitiveness of the broadband market today, asserting that dominant carrier regulation of their broadband offerings is no longer needed and, in fact, is hindering their roll-out of broadband.

On close examination, however, the ILECs' claims crumble. The economic "analysis" which forms the linchpin of their position is riddled with methodological and factual errors – ranging from the misapplication of Commission precedent, through the misdefinition of markets, through the use of a price-elasticity "study" that is built on a flimsy structure of non-representative, incomplete and misleading data.

The truth of the matter is that the ILECs retain market power in the broadband market. They have used this market power even under existing regulation to beat back emerging intramodal competition from competitive local exchange carriers ("CLECs") and data local exchange carriers ("DLECs"). Nor does intermodal competition promise to restrain ILECs from behaving monopolistically. Neither cable modem service, satellite nor wireless is a good enough substitute for DSL to restrain the ILECs in the "mass market." The best possible scenario if regulation is lifted would be the emergence of a duopoly, which – as the Commission has consistently recognized for years – allows both participants to exercise market power, and hence does not justify the lifting of dominant carrier regulation. And ILECs' control over essential bottleneck facilities will allow them easily to dominate the larger business market as well.

The ILECs' claims that existing regulation has discouraged their deployment of broadband services are also baseless. In fact, under existing regulation, their deployment of DSL

services has boomed – a fact of which they boast to investors and analysts but which they soft-pedal before this Commission. Their deployment has been more than adequate to meet actual demand for these services. Moreover, they have stage-managed their deployment in such a way as to stymie CLEC and DLEC competition and to protect to the extent possible their profitable second-dial-up line services. These factors, not overburdensome regulation, account for the manner in which DSL has been deployed to date.

As a final appeal, some ILECs hold out the possibility of a gold-plated network that would provide services at many times the speed of today's services. They do not, however, show that demand exists or is developing for such services. They also make no showing as to whether the offering of such services is likely to be subject to competition. Indeed, the whole tenor of their argument is that only they can build these networks. In other words, the ILECs are asking this Commission to lift its regulations so that they can proceed to extend their monopoly power well into the 21st century. The Commission should repel this attempt. It should peremptorily dismiss this proceeding. Failing that, it should issue a new notice to cure the fundamental analytical and definitional flaws of the original *NPRM*.

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Focal Communications Corporation and Pac-West Telecomm, Inc. ("Commenters") submit these reply comments in response to initial comments filed in response to the Commission's Notice of Proposed Rulemaking in the above-captioned proceeding,[1] concerning regulation of incumbent local exchange carriers' ("ILECs") provision of broadband telecommunications services.

I. INTRODUCTION

It comes as no surprise that the independent local exchange carriers ("ILECs"), led by the regional Bell operating companies ("RBOCs"), have come out with guns blazing in favor of essentially complete deregulation of their broadband service offerings. Lining up behind the standard of SBC's petition for declaratory ruling,[2] the ILECs bewail the regulatory "asymmetry" that assertedly keeps them from being able to compete fairly with cable modem providers in the

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[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] 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, filed Oct. 3, 2001 ("SBC Petition").

"mass market" and with the IXCs in the "larger business market." They assert that unless the burdensome yoke of dominant carrier regulation is lifted, they will have no incentive to continue developing broadband services and thus U.S. consumers will not have access to advanced services in the 21st century. They state further that dominant carrier regulation is not necessary in this area, contending that the market for broadband services is already fully competitive and indeed that they have already been outrun by their competitors.

Put simply, none of this is true. In fact, as Commenters showed in initial Comments in this proceeding and further show herein, the ILECs have been fully able to compete in the market as it exists today under current regulation. Their deployment decisions have been driven, not by the vagaries of regulation as they claim, but by their determination to pinch off the nascent competitive threat posed by the competitive local exchange carriers ("CLECs"), the better to allow the development of a duopoly in the mass market with cable providers if not an outright ILEC monopoly. As shown herein, the ILECs' arguments to the contrary are not only unsupported by evidence, they are in fact wrong – and indeed are internally incoherent.

The issuance of the *NPRM* was well-intentioned but ill-advised. The Commission should peremptorily dismiss this proceeding. Failing that, the Commission should not act without a further notice to address the fundamental definitional and analytical problems identified by the Commenters in initial Comments.[3]

II. CONTRARY TO THE ILECS' CLAIMS, THEY RETAIN MARKET POWER IN THE MARKET FOR BROADBAND SERVICES.

Central to the ILECs' position is one fundamental claim: that they do not possess market power in the market for broadband services. They expend a great deal of effort in an endeavor to

demonstrate this premise. In the end, this effort is wasted. Their economic presentations are woefully deficient. They ignore the glaring reality that they, and they alone, control bottleneck facilities, access to which is essential for true competition to arise in this market. Finally, even if everything they say were true, in the mass market, the best outcome under their scenario would be a classic duopoly, allowing both providers to engage in monopolistic practices.

A. The ILECs' Economic Presentations Are Fraught With Factual and Methodological Error.

The centerpiece of the ILECs' economic arguments is the Crandall/Sidak declaration provided with the SBC Petition and recycled with SBC's comments herein.[4] In their declaration, Messrs. Crandall and Sidak assert that there are two relevant submarkets in the broadband market – the "mass market," consisting of residential and small business users,[5] and the "larger-business" market.[6] They also conclude that the relevant geographic market for each of these product markets is the ILEC's entire service area, whether or not there is actual competition for the ILEC's offerings within any particular portion of the service area.[7] Finally, they conclude that in each of the relevant product and geographic markets, the ILECs lack market power in the provision of broadband services. As to the "mass market" in particular, they assert that cable

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[3] As Commenters noted (Comments at 2-4), in the *NPRM,* the Commission inexplicably declined to take up the fundamental prerequisite to any analysis of the market for "broadband services" in that it expressly disclaimed any intent to define what "broadband services" *means.*

[4] Declaration of Robert W. Crandall and J. Gregory Sidak ("CS Declaration") attached to SBC Petition, which in turn is attached to SBC's Comments at Attachment A.

[5] CS Declaration at 15-21. Crandall and Sidak (Declaration at 1) unreflectively adopt the definition of advanced services established by the Commission in *Application of Ameritech Corp, Transferor, and SBC Communications Inc., Transferee, for Consent to Transfer Control of Corporations Holding Commission Licenses and Lines Pursuant to Section 214 and 310(d) of the Communications Act and Parts 5, 22, 24, 25, 63, 90, 95 and 101 of the Commission's Rules*, 14 F.C.C. Rcd 14,712 (1999) ("SBC/Ameritech Merger Order") Appx. C., Merger Conditions, at para. 2. They provide no analysis as to whether this is in fact a separate product market from the services excluded by the Commission in that proceeding. *See also* SBC Comments at 19-22.

[6] CS Declaration at 45-49; *see also* SBC Comments at 22-29.

[7] CS Declaration at 21-24, 49-51; *see also* SBC Comments at 32-35.

modem providers, not ILECs, are dominant.[8] With minor variations, all the RBOCs echo these contentions.[9]

The attached Declaration of Lee L. Selwyn ("Selwyn Declaration") thoroughly refutes the claims of the ILECs, with particular attention to the conclusions of Messrs. Crandall and Sidak. As Dr. Selwyn points out, Crandall/Sidak "apply" a four-part standard previously used by the Commission to determine whether carriers have market power in provision of interexchange services. Under this test, the Commission is to assess, for the relevant product and geographic markets: (1) the carriers' market share and changes therein; (2) demand elasticity; (3) supply elasticity; and (4) any disparity in size, resources and costs between the carriers and other providers.[10] According to Crandall and Sidak, all four of these factors weigh in favor of a conclusion that ILECs do not possess market power in the broadband "mass market." But, as Dr. Selwyn shows, they are in error as to all four.

1. The ILECs Have Misdefined the Relevant Product and Geographic Markets, With the Effect of Vastly Understating the ILECs' True Market Share.

First, the market definitions adopted by Crandall and Sidak and endorsed by the ILECs are inappropriate, and are arrived at without accounting for the critical differences between the interexchange market (from which Messrs. Crandall and Sidak have taken their analytical framework) and the market for broadband services. Unlike the interexchange market, in which any IXC could access any customer on the public switched telephone network by simply establishing appropriate points of presence (POPs), the broadband market contains a privileged

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[8] CS Declaration at 25-29; *see also* SBC Comments at 35-37.

[9] *See, e.g.,* Qwest Comments at 15-23 (mass market), 23-24 (larger business market), 24-31 (geographic market), 31-56 (market power); BellSouth Comments at 30 (product and geographic markets), 31-45 (market power); Verizon Comments at 9-12 (product markets), 22-24 (geographic markets), 13-22 (market power).

[10] CS Declaration at 11-12.

competitor – the ILEC – who alone as against most potential competitors controls the "last mile" to the customer. This means that the broadband market is a true point-to-point market, and cannot be aggregated into a single national or service-area-wide market, as was done with interexchange services. Crandall and Sidak assert that the broadband market for SBC's services is SBC's entire 13-state region, by analogy to the long distance market. But, as Dr. Selwyn shows, this analogy is fatally flawed, and the extension of the long distance model to the broadband marketplace is directly contrary to the Commission's approach in the *BOC Classification Order.*[11]

Moreover, the Crandall/Sidak definition of the relevant product market is erroneous. They assert that the relevant product market for the "mass market" in broadband includes not only DSL, but cable modem service, satellite and fixed wireless. But they offer no substantial evidence that consumers actually view these services as substitutes for one another – as they must if they are to constitute a single product market. As Commenters pointed out in their initial Comments herein, and as Dr. Selwyn elaborates,[12] satellite and wireless services cannot be considered even arguably close substitutes for DSL given their severe technical and availability constraints. Moreover, cable modem services do not have the security and reliability characteristics sought by most business users and hence are not close substitutes as far as those users are concerned.[13] Finally, in the many areas not served by both DSL and cable modems, the two are obviously not substitutes at all.[14] For all of these reasons, the Crandall/Sidak conclusion

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[11] Selwyn Declaration at 17-21, 31-35.

[12] Selwyn Declaration at 25-26.

[13] Selwyn Declaration at 26-27, 39.

[14] Selwyn Declaration at 27. As Dr. Selwyn points out, if the data used in Crandall and Sidak's price elasticity study are to be believed, as few as 12 percent of homes have a choice between DSWL and cable modems. Selwyn Declaration at 40-42. While these data are, as shown, of dubious reliability, it appears clear from various data (footnote continued on next page)

seriously underestimates ILEC market share when the relevant product and geographic markets are defined properly.

Crandall and Sidak underestimate market share for another reason: empirical evidence supports the conclusion that for many users, a second dial-up line is an adequate solution for Internet access. The ILECs provide all of these lines either at retail or wholesale. When they are taken into account, the ILECs' total market share is much higher than that arrived at by Messrs. Crandall and Sidak and the other ILEC estimates.[15]

Moreover, Crandall and Sidak (and the ILECs generally) fail to adequately account for the ILECs' control over wholesale as well as retail DSL. As Dr. Selwyn notes, even under dominant carrier regulation and with line-sharing requirements, the ILECs have gamed the system in a manner that has allowed them to hold the CLEC/DLEC share of the retail DSL market to as low as seven percent today – a share that may well shrink further as the ILECs have succeeded in driving some CLECs and DLECs from the market altogether.[16]

Finally, the ILECs' assertions as to current market share are, as pointed out in Commenters' initial Comments, largely irrelevant because the structure of the nascent market as it exists today may well not be reflective of the structure the market will assume as it matures. As Dr. Selwyn states, "it is simply too early to tell" whether the ultimate state of the market will be competitive enough to allow for some easing of regulatory constraints. The potential for irreparable harm arising from the premature lifting of dominant carrier regulation is real and substantial. Regulatory caution in such contexts has long been a policy given. For example,

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submitted by the parties that the degree of overlap between the two services is far smaller than the ILECs might have one believe.

[15] Selwyn Declaration at 28-31.

[16] Selwyn Declaration at 36-38.

AT&T was still considered dominant in long distance services long after it had divested the wholesale facilities (loops) that had allowed it to create and guard such dominance; it was only when the interexchange market had achieved a state of considerable maturity and it became clear that competition was real and lasting that the regulatory constraints on it were eased. Similarly, GTE was forced to enter into a consent decree with the Department of Justice in order to enter the long distance market even though it had essentially *zero* percent of that market at the time, because its potential for achieving dominance using its bottleneck facilities was high.

2. The Only Evidence in the Record of Demand Elasticity Between DSL and Cable Modem Service Is Fatally Flawed.

In assessing the ILECs' market power, most of the ILECs simply state in a conclusory manner that there is elasticity of demand in the broadband market, and in particular that there is cross-elasticity between cable modem and DSL services. But the only attempt to provide any serious empirical evidence for this proposition is the "study" performed for SBC by Crandall and Sidak of certain consumer bills and survey data. Unfortunately, the Crandall/Sidak study is so flawed as to be unusable.[17]

At the outset, the Crandall/Sidak study includes only residential customers. It ignores the small-business segment altogether. As noted above, there are strong qualitative reasons – supported by the comments of actual business users – to believe that cable modem service is not viewed as a substitute for DSL by business users. Crandall and Sidak simply ignore this important issue.[18]

Second, the Crandall/Sidak study throws out a full *seven-eighths* of the respondents to the TNS billing survey on which the study is based – using only those 12 percent of respondents that

[17] *See generally* Selwyn Declaration at 39-50.

indicated they had access to both DSL and cable modems at the time the survey was taken. This is a problem because it completely ignores the extent of own-price-elasticity for DSL for the remaining 88 percent of respondents. In addition, because the 12 percent is so far below other estimates (including Crandall and Sidak's own) of the number of consumers having access to both services that its representativeness is highly suspect.[19]

Third, even as to the fraction of consumers which it considers, the Crandall/Sidak study fails to account for the fact that many early adopters of technology will have adopted cable modem or DSL *depending on which was first available in their area* regardless of whether a second technology had become available by the time of the survey. By ignoring this factor, the study misleadingly implies an affirmative choice by users between two competing technologies and wrongly assumes that consumers' choices were based on price. Even as to customers who may have had a choice at the time they made their initial purchase decision, the Crandall/Sidak study does not even attempt to determine what the relative pricing of the services was at the time that decision was made. Rather, the study only addresses pricing at a later period – a time irrelevant to the initial purchasing decision. Thus, the study cannot rule out or otherwise control for purchasing decisions made on the basis of service characteristics such as realized speed or other non-price considerations.[20]

Finally, the study fails in that it does not consider the extent to which customers view dial-up 56 kbps modem service as a substitute for DSL at an appropriate price point. This is important because, in areas where there is no cable modem service, ILECs have a strong

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[18] Selwyn Declaration at 39.

[19] Selwyn Declaration at 40-42.

incentive to avoid rolling out DSL or to make it hard to get, so as to avoid cannibalizing their higher-margin second-line dial-up market. To the extent ILECs have been successful in driving DLECs from the marketplace, this "slow-roll" strategy is facilitated.[21]

To cut to the chase, Dr. Selwyn adduces substantial *direct* evidence of market performance demonstrating that, contrary to Crandall and Sidak's conclusions, demand for DSL is highly *inelastic:* the ILECs have been able to raise DSL prices by large amounts without suffering significant customer defections to other technologies. In fact, their DSL subscribership has substantially increased.[22]

3. Contrary to the ILECs' Position, Supply Elasticity is Low and Entry Barriers Are High in the Broadband Market.

Through Messrs. Crandall and Sidak, SBC also alleges that supply is elastic in the broadband market, a claim joined by the other ILECs. Significantly, as Dr. Selwyn points out, they focus entirely on *intermodal* competition. It is self-evident that the ILECs control over bottleneck facilities gives them the ability to prevent CLECs from increasing supply to provide intramodal competition. The record of this proceeding – as well as other proceedings before this Commission – is replete with evidence of the ILECs use of delaying tactics, denial of service, withholding of information and degradation of service to weaken CLECs and thwart any ability they might have to provide such supply.[23]

Similarly, as to the larger business market, ILECs' control over last-mile facilities gives them the ability to engage in price squeezes and thwart competing IXCs' ability to meet demand

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[20] Selwyn Declaration at 42-46. Dr. Selwyn also notes that the comparative price data used by Messrs. Crandall and Sidak are incomplete and that they have used "inferred" rather than actual prices for technologies other than the one subscribed to by the user. Selwyn Declaration at 43-44.

[21] Selwyn Declaration at 46-47.

[22] Selwyn Declaration at 48-49.

caused by customers leaving ILEC services. As AT&T has noted, excess capacity in packet switching and intercity transport are irrelevant if, as is the case here, there is no excess capacity in the last-mile bottleneck.[24]

Messrs. Crandall and Sidak also ignore that entry barriers are very high, even for providers using ILEC underlying facilities. Dr. Selwyn describes these barriers in detail at pages 53-54 of his Declaration.

4. ILECs Possess Substantial Size, Resource and Cost Advantages Over Their Competitors.

The ILECs argue that the ILECs do not possess any significant size or resource advantages over their competitors. They base this contention solely on the fact that a number of large cable companies provide cable modem services in some areas. Messrs. Crandall and Sidak also cite cost figures that, they claim, show that the ILECs' average cost of serving a DSL customer is $86 per month, while cable modem providers' average cost is only $55. As Dr. Selwyn notes, there are two fundamental flaws in their argument.

First, as to competitors other than cable modem providers – i.e, CLECs and DLECs offering intramodal competition, there is no question that ILECs dwarf their competitors in size and resources. Moreover, their control over the bottleneck facilities which are necessary inputs for the CLECs and DLECs gives them a whip hand over these competitors and in particular allows them to engage in price squeeze tactics.[25]

Second, if the Crandall/Sidak figures are accurate, *both* ILECs and cable modem providers have been engaging in cross-subsidization of their broadband offerings – as much as

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[23] Selwyn Declaration at 51-52.

[24] Selwyn Declaration at 52-53.

[25] Selwyn Declaration at 56.

$38 per month in the case of ILECs. This massive cross-subsidization is in itself strong evidence that deregulation of the ILEC service offerings is at best premature.[26]

B. The ILECs' Arguments At Best Demonstrate The Potential Emergence Of A Broadband Duopoly, Which Will Allow The ILECs To Engage In Monopolistic Practices Absent Continued Dominant Carrier Regulation.

Even viewed in the most charitable light, the ILECs' reliance on cable modem providers to show that the broadband "mass market" is competitive fails because at most it proves that a duopoly exists in the broadband market. As noted in Commenters' initial Comments (at 10-11), even taking the ILECs' market share claims at face value, the market concentration in the broadband "mass market" is far in excess of that which the Justice Department considers acceptable in assessing mergers. Dr. Selwyn's Declaration demonstrates why a market dominated by two enormous providers – a duopoly – is characterized not by effective competition, but by *both* providers being able to engage in monopolistic behavior. As he shows, the ILECs and cable providers have engaged in lockstep pricing and have raised rates with impunity, hardly the behavior of participants in a highly competitive market.[27]

The Commission has in the past been well aware of the dangers of duopoly. Over and over it has noted that duopolistic markets are not truly competitive. For example in the recent order in *In The Matter Of Applications For Consent To The Transfer Of Control Of Licenses And Section 214 Authorizations By Time Warner Inc. And America Online, Inc., Transferors, To AOL Time Warner Inc., Transferee,* 16 F.C.C. Rcd 6547, para. 163 (2001) the Commission stated:

> From among all entrants into the IM business, AOL points especially to Microsoft as a significant rival. AOL claims that Microsoft's presence, and especially its recent growth in the market, demonstrates that AOL does not dominate IM. . . . However, Microsoft has not always been able to leverage its control of the Windows desktop into dominance of

[26] Selwyn Declaration at 55-56.

[27] Selwyn Declaration at 58-65.

> other applications. In addition, in IM today, AOL benefits from network effects and first mover advantages; and, as we discuss below, the proposed merger would give AOL significant, additional advantages over Microsoft, Yahoo!, and smaller IM providers. *And even if Microsoft's NPD did grow to rival AOL's, the result would be merely a duopoly, not the healthy competition that exists today in electronic mail and that we hope will exist in new IM-based services and AIHS in particular.* [Citations deleted; emphasis added.]

Similarly, in *In The Matter Of Interconnection And Resale Obligations Pertaining To Commercial Mobile Radio Services*, 17 Communications Reg. (P&F) 518, para 69 (1999) the Commission recognized that the existence of a duopoly did not provide sufficient competition to justify the lifting of regulatory obligations designed to promote competition:

> We agree with those opposing PCIA's petition for reconsideration that competition in the wireless telephony market is not yet at a state where the resale obligation should be eliminated, and conclude that it should be retained for the remainder of the transitional period, until it sunsets on November 24, 2002. We addressed the forbearance issues raised by PCIA just last year. Since that time, competition in CMRS industries has continued to grow. However, we do not view competitive conditions in the CMRS marketplace as qualitatively different from those that obtained one year ago; i.e., competition continues to be a "work in progress," as the marketplace evolves from the tight duopoly that prevailed only a few years ago to a state of full competition, which we anticipate will prevail in a few years. The situation has not changed so dramatically in the last year to cause us to reverse course on the continued utility of the resale rule in this market. *Rather, we see the gradual, but steady, growth of competition in these markets as confirming our decision to maintain the rule at present,* but sunset it at a specific time in the future, based on our expectations that competition will develop in these markets over time sufficient to support the elimination of the rule. [Citations deleted; emphasis added.]

In this instance, indeed, the Commission noted that the prior duopoly no longer existed but determined to maintain the rule because the transition to a fully competitive market was not yet complete.

That the distance between a duopoly and a fully competitive market is wide – and that the problems posed by duopoly are not cured by the mere potential for entry by others – is further borne out by the Commission's discussion in *In The Matter Of 1998 Biennial Regulatory Review Spectrum Aggregation Limits For Wireless Telecommunications Carriers Cellular*

Telecommunications Industry Association's Petition For Forbearance, 15 FCC Rcd. 9219, para. 32 (1999):

> There is little dispute in the record that considerable progress has been made toward the goal of promoting competition in CMRS markets, but many commenters question whether an adequate array of competitive options is now available to all of the nation's wireless consumers. While commenters generally agree that the creation of the spectrum cap rule helped competition in mobile voice markets develop out of a duopoly environment, disagreement exists regarding the extent to which competition has been achieved. Several commenters contend that with the initial licensing of PCS spectrum now largely completed, our objectives have essentially been accomplished. Some commenters argue that with the completion of the recent supplemental auction of C-block licenses, even further progress toward our goals has been achieved. We cannot agree, however, that merely making spectrum available completes the task of promoting competition. [Citations deleted.]

See also, e.g., In The Matter Of Implementation Of Section 11(C) Of The Cable Television Consumer Protection And Competition Act Of 1992, 14 FCC Rcd. 19,098 at para. 51 (1999) ("Although a 50% limit could lead to a more even duopoly, the weaknesses of such competition are well established. The probability of tacit collusion is higher with 2 competitors than 3 competitors."); *1998 Biennial Regulatory Review — Spectrum Aggregation Limits for Wireless Telecommunications Carriers,* Report and Order, Separate Statement of Commissioner Powell, 15 FCC Rcd9219, 9296 (1999) (regulatory caution regarding spectrum aggregation limits is warranted because of "lingering concerns left over from the vestiges of the original cellular duopoly.") It should be noted that the Commission's analysis applies even when the providers' products are more or less perfect substitutes for each other. As Dr. Selwyn points out, the fact that there is differentiation between DSL and cable modem service will only facilitate the arising of leader/follower behavior.[28]

[28] Selwyn Declaration at 61, 63-64.

The current regulatory scheme is ineffective in restraining the ILECs' anticompetitive behavior, as detailed in Commenters' initial Comments herein. Ceding the regulatory field in the hopes that competition between duopolists will be sufficient to protect consumers from monopolistic behavior would be disastrous. The Commission must maintain, and even strengthen, the current dominant carrier regulatory regime.

C. The ILECs' Focus on the Retail Market Ignores the Fact That the Wholesale Broadband Market is Unquestionably a Monopoly.

The ILECs' arguments regarding the alleged competitiveness of the "mass market" for broadband – meritless as they are – do not even attempt to address the wholesale market.[29] They assert that CLECs provide and will continue to provide substantial intramodal competition.[30] But at the same time, they advocate regulatory changes that would effectively put an end to this competition, in contravention of the policies behind the Telecommunications Act of 1996 and of all articulated Commission policy to date.

In fact, the wholesale market from which CLECs obtain essential inputs into the services they provide their customers remains for all intents and purposes an ILEC monopoly. Even if some reduction in dominant carrier regulation were justified (which it is not) in the retail market, the sweeping deregulation called for by the ILECs must not be extended to the wholesale market. Existing line-sharing and unbundling requirements must be maintained and strictly enforced in this market. If not – if the ILECs "trust us" approach is adopted – they will be at liberty to contunue and extend the exclusionary tactics they have used to meet and repel CLECs'

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[29] It is obvious that the state of competition in the retail market is not dispositive of the state of the wholesale market. Microsoft's power in the retail market for PC operating systems tells us nothing about whether operating system architects and programmers are readily available. Similarly, Intel's power in the CPU market explains nothing about the extent of competition in the market for personal computers.

[30] *See, e.g.*, BellSouth Comments at 8; Qwest Comments at 52.

competitive advances to date. The tide of the war of attrition they have been fighting will be turned conclusively in their favor. Freed from the nettlesome threat posed by CLECs, they will be able to turn their full attention to managing the duopoly they seek to establish. Ultimately, indeed, if the ILECs are in fact, as they claim, the only entities able to build the futuristic broadband networks they tout, they would be left in the enviable position of unencumbered, unregulated monopolists, and the entire purpose for which the original Communications Act was adopted would be vitiated. This result cannot be allowed to take place.

III. THE ILECS HAVE FAILED TO DEMONSTRATE THAT REDUCED REGULATION IS NECESSARY TO FOSTER BROADBAND DEPLOYMENT.

The ILECs all sing the same refrain: that existing dominant carrier regulation has retarded their deployment of broadband services. Yet they offer no meaningful proof of this claim. Instead, they harp on the truism that regulation imposes costs,[31] while studiously ignoring the benefits of regulation in constraining ILECs' anticompetitive behavior in this market.

As the Selwyn Declaration shows, the ILECs' contention that current regulation has prevented them from investing in broadband services is a canard – and is directly contrary to what these same ILECs have been telling Wall Street. For example, as Dr. Selwyn notes, Verizon has told investors that it has deployed DSL to central offices serving 79 percent of its access lines and that it has cut installation times nearly in half.[32] Dr. Selwyn also details the intensive marketing efforts the RBOCs have devoted to their DSL rollout. And these marketing efforts have been explosively successful: the four RBOCs' *average* growth in DSL subscribership in the year 2001 was well over *100 percent*.[33]

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[31] *See, e.g.*, SBC Comments at 59-60.

[32] Selwyn Declaration at 5-6.

[33] *Id.* at 6-8.

This growth has occurred despite the fact that no "killer application" has yet emerged that would drive mass market demand past the "early adopters" and those who have specialized needs for high speed access. As Commenters pointed out in our initial Comments (at 17):

> [T]here are simply no services not already available to consumers that would make broadband particularly desirable. Video programming is available from several sources including over-the-air broadcast, cable, satellite, videocassettes and DVDs. High speed web browsing is already available through DSL and cable modem service, although these services are not necessarily substitutes for each other. Businesses are already able to obtain the high speed services they need from ILECs.

As Dr. Selwyn notes (Selwyn Declaration at 10-11), the RBOCs themselves have recognized that their current pace of development is commensurate with, if not in excess of, demand. Other commenters, as well, have noted that demand for broadband services does not justify extraordinary measures to speed their rollout.[34]

Undeterred by this market reality, some of the ILECs acknowledge that DSL deployment has taken place but assert that the real need is for fiber to the home. BellSouth, for example, characterizes DSL as an "infant" technology[35] and states that the true imperative in the "mass market" is to achieve 100-megabit-per-second connections to 100million homes by 2010.[36] According to BellSouth, it will not make the investment needed to attain this result so long as current regulation would apply.

It is here that the ILECs' logic is most patently fallacious. They argue first that the presence of other providers means that sufficient competition exists. But then they argue that if

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[34] *See, e.g.,* DirecTV Comments at 15; Information Technology Association of America ("ITAA") Comments at 24.

[35] BellSouth Comments at 8.

[36] In support of this "imperative," BellSouth cites a report of TechNet, a "national network of senior executives of the nation's leading technology companies," as though it were national policy. Comments at 8. Whatever one thinks of this goal in the abstract, it must not be achieved at the cost of allowing a duopoly – or even a monopoly – to arise.

the ILECs do not build this 100-megabit-per-second network, there are no other entities which will, and therefore American consumers will be denied the benefits of such a network![37] This smacks of the old "natural monopoly" concept, yet the ILECs stop short of the ultimate conclusion their arguments imply: that dominant regulation of such offerings would then be if anything even more essential than it is today.

The ILECs also argue that line-sharing and UNE requirements, if applied to broadband, discourage ILECs and CLECs alike from investing in the facilities needed to make this dream a reality, as though the situations of ILECs and CLECs are the same. While this issue is not directly before the Commission in this proceeding, it bears addressing. Contrary to the ILECS' contention, in fact, it is the ILECs that control the huge embedded infrastructure on which such investment would piggyback. No CLEC can justify investment in facilities needed to provide broadband services if the ILECs are permitted to deny CLECs the unbundling and interconnection needed to allow CLECs to provide these services in an efficient and cost-effective manner. The effect of the relief the ILECs request would not be to motivate the CLECs to invest the hundreds of billions of dollars the ILECs claim is necessary but to drive them from this market altogether.

IV. CONCLUSION

The ILECs have failed to show that the removal of dominant carrier regulation from their broadband offerings is warranted. In fact, the maintenance of such regulation is essential to ensure that nascent competition in this market is not snuffed out. Accordingly, the Commission

[37] It is noteworthy that in all their analyses of the "mass market," not a single ILEC has focused on the ability of other providers to provide broadband services at speeds anything like 100 mbps. They address only the extent to which other providers offer services at speeds comparable to DSL, though as Commenters have shown, satellite and wireless services in particular do not stack up to DSL in terms of speed and reliability. Commenters Comments at 11-12.

should peremptorily terminate this proceeding. If the Commission determines to proceed nevertheless, then, as stated in Commenters' initial comments, the Commission must first issue a further notice of proposed rulemaking to define the market(s) it is analyzing.

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