

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

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

REPLY COMMENTS OF SBC COMMUNICATIONS INC.

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SBC Communications Inc. (SBC), on its own behalf and on behalf of its affiliates, files these reply comments in support of its position that the Commission should remove all dominant carrier regulation of incumbent local exchange carrier (LEC) broadband telecommunications services.¹

I. Introduction

Last month, the Commission issued a declaratory ruling in which it confirmed the deregulated status of cable modem service.² Resolving long simmering disputes over the appropriate classification of cable modem service, the Commission ruled that: (1) cable modem service is neither a cable service nor a telecommunications service, but rather an interstate information service; and (2) cable modem service need not be provided on a stand-alone basis to unaffiliated Internet service providers (ISPs) irrespective of whether the cable operator is also providing telephone service to end-user customers.³ The Commission thereby simultaneously freed cable modem service both from Title VI of the Act and Title II. Although the Commission issued a Notice of Proposed Rulemaking to consider whether to impose some form of “multiple

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

² *Inquiry Concerning High-Speed Access to the Internet Over Cable and Other Facilities; Internet Over Cable Declaratory Ruling; Appropriate Regulatory Treatment for Broadband Access to the Internet Over Cable Facilities*, GN Docket No. 00-185 and CS Docket No. 02-52, Declaratory Ruling and Notice of Proposed Rulemaking, FCC 02-77 (rel. Mar. 15, 2002) (*Cable Broadband Declaratory Ruling*).

³ *Id.* at ¶ 33.

ISP access” on cable modem providers, the Commission offered no hint that it would require cable modem providers to offer an unbundled transmission component, much less that it would subject any such offering to dominant carrier regulation.⁴

The Commission’s actions in the *Cable Broadband Declaratory Ruling* stand in stark contrast to its current treatment of incumbent LEC broadband services. Unlike cable operators, incumbent LECs may not offer their customers broadband Internet access without first creating a stand-alone DSL transport service offering for unaffiliated ISPs. They are not free to negotiate individualized contractual arrangements with ISPs, much less private carriage arrangements and they are subject to dominant carrier tariff and price regulation.

The regulatory disparity between incumbent LECs and their competitors is equally striking in the larger business segment of the market. IXCs are deregulated in their provision of broadband services to business customers. They are free to enter into individualized arrangements, respond to customer requests for proposals (RFPs), and respond quickly to any incumbent LEC offering in the market. An incumbent LEC, by contrast, must file a tariff for each customer arrangement and does not have the ability to respond quickly or effectively to competition. In addition, an incumbent LEC cannot offer customers information services, such as data storage and protocol conversion, without creating a stand-alone transmission service and making available comparably efficient interconnection (CEI) to competing providers. The combination of these regulatory burdens and the inability of incumbent LECs to offer interLATA services in most areas of the country ensures that IXCs remain entrenched in their dominant position in the market.

⁴ The Commission stated that its decision should be guided by three principles: (1) fulfilling its statutory obligations to encourage the widespread deployment of broadband services and to “preserve the vibrant and competitive free market that presently exists for the Internet and other interactive computer services, unfettered by Federal or State regulation”; (2) ensuring that broadband services exist in a “minimal regulatory environment that promotes investment and innovation in a competitive market”; (3) creating a “rational framework for the regulation of competing services that are provided via different technologies and network architectures.” *Cable Broadband Declaratory Ruling* ¶ 4-6.

This regulatory disparity is indefensible, particularly given that in both sub-markets, incumbent LECs are dwarfed by their much larger rivals. In the mass market segment of the broadband market, the Commission expressly recognized in the *Cable Broadband Declaratory Ruling* that:

- cable operators are the “leading providers” of residential broadband services;
- almost 70 percent of residential broadband subscribers use cable modem service, while only about 29 percent use DSL service; and
- in the past year, some incumbent LECs have scaled back their DSL deployment plans and cable’s lead over DSL has grown.

In the larger business segment of the market, the story is much the same. After more than a decade of competing against the “Big Three IXCs” — AT&T, WorldCom and Sprint, which have always been the dominant providers of broadband services to larger business customers — incumbent LECs have captured less than 15 percent of the market. The notion that the incumbent LECs will be able to acquire market power from these much larger service providers — each of which has an established base of lucrative business customers and national broadband networks with hundreds of points of presence (POPs) nationwide — is patently absurd. The difficulty of wresting market share away from the IXCs is evidenced by the fact that, despite having received interLATA authority in seven states, SBC has captured only a *de minimis* amount of interLATA Frame Relay and ATM business. Even when the incumbent LECs have received interLATA authority in all states, the limited reach of their local and regional networks will leave them at a significant competitive disadvantage compared to the Big Three IXCs, which can offer many larger business customers end-to-end service over their nearly ubiquitous nationwide networks.

Dominant carrier regulation applies, by its terms, only to firms that have market power — that is, the ability to control price by restricting output — in the provision of a service. As SBC and others have shown, and as the Commission itself has effectively recognized, no serious argument could be made that incumbent LECs have market power in the provision of broadband services. To the contrary, their dominant status is strictly a product of their regulatory legacy.

Not surprisingly, some of the incumbent LECs' largest deregulated competitors in the broadband market, including AT&T, AOL Time Warner, and DIRECTV, seek to preserve the current asymmetrical regulatory regime from which they benefit so much. As shown below, though, their arguments are sheer hypocrisy:

- **AT&T argues that incumbent LECs have market power in the provision of mass-market broadband services.**⁵

AT&T argues this despite the fact that, after its proposed merger, Comcast/AT&T will be the country's largest provider of mass-market broadband services and that cable modem service is the clear "market leader," with twice as many customers as DSL service.⁶

- **AT&T argues that incumbent LECs control bottleneck facilities in the broadband market.**⁷

AT&T argues this even though cable modem service is much more widely available than DSL service and the cable industry association has acknowledged that there is no bottleneck in the provision of broadband services.

- **AT&T argues that there is a wholesale market for DSL service that justifies the continuation of regulation.**⁸

AT&T makes this argument while also taking the position that competing cable modem service providers should have the right to operate closed networks with no obligation to do business with unaffiliated ISPs.

⁵ AT&T p. 19.

⁶ In their December 19, 2001, press release, AT&T and Comcast stated that "AT&T Comcast Corporation will be the world's leading provider of broadband video, voice and data services with annual pro forma revenue of approximately \$19 billion."

⁷ AT&T pp. 14-15.

⁸ AT&T p. 49-50.

- **AT&T argues that the Commission cannot deregulate incumbent LECs on a service-specific basis.**⁹

Yet AT&T has argued for years that the Commission could and should deregulate particular segments of the long distance market.

- **AT&T argues that the incumbent LECs are dominant in the provision of Frame Relay and ATM service.**¹⁰

AT&T argues this despite the fact that AT&T is the nation's largest provider of both services with more than 600 POPs and more than 51,000 miles of fiber nationwide.¹¹

- **AT&T argues that incumbent LECs can leverage market power in the local market.**¹²

AT&T makes this argument despite the fact that the incumbent LECs largest competitors provide inter-modal competition and do not depend at all on incumbent LEC facilities, and despite the fact that incumbent LEC local services remain highly regulated and, in most cases, under price caps. AT&T and other cable operators have been cross-subsidizing their cable modem deployment with an on-going rise of cable television price increases, to the point that Sen. John Mc Cain has sought a review of them.¹³

- **AT&T downplays the costs that dominant carrier regulation imposes on incumbent LECs and end-user customers.**¹⁴

AT&T contends this even though AT&T spent years filing comments and economic analyses that documented the various costs and customer harms imposed by dominant carrier regulation and the social costs of asymmetric regulatory regimes.

⁹ AT&T p. 23.

¹⁰ AT&T p. 23-26.

¹¹ See <http://www.ipservices.att.com/brochures/atm.pdf>.

¹² AT&T, p. 32.

¹³ Sen. John Mc Cain, Republican-Arizona, sent a letter on Tuesday, April 16, 2002, asking the General Accounting Office to review rising cable television rates. Sen. Mc Cain expressed concern that cable rates continue to rise much faster than the rate of inflation. Dow Jones Newswires.

¹⁴ AT&T p. 67-76.

Clearly, competitors, such as AT&T, have no credibility in this proceeding, and the Commission should disregard their transparent attempts to maintain an artificial competitive advantage in the broadband market.

As SBC discussed in its initial comments, removing dominant carrier regulation of incumbent LEC broadband services will benefit customers by forcing *all* providers to compete more vigorously in the market. That step will accordingly help to fulfill the Commission's mandate under section 706 of the Act to promote the deployment of broadband services and ensure that such services are offered at competitive terms and conditions that are attractive to customers.

Classifying incumbent LECs as non-dominant in their provision of broadband services is just a first step, however. In addition to classifying incumbent LEC broadband services as non-dominant in this proceeding, the Commission must implement a comprehensive regulatory framework that promotes competition and investment in the broadband market. That means the Commission also must eliminate the potential for "regulatory creep" by making clear that burdensome unbundling requirements that were designed for the legacy circuit-switched network will not extend to incumbent LEC broadband investment. It also means that the Commission must regulate the broadband market in a manner that is competitively and technologically neutral for all providers, regardless of the platforms they have deployed. The Commission's parallel *Wireline Broadband* and *Cable Broadband* proceedings must eliminate the illogical regulatory disparities that currently exist and produce a unified regulatory framework that will encourage investment in new broadband products and services that will benefit end user customers.

II. Mass Market Segment

Recent events — both in the marketplace and in regulatory and judicial arenas — underscore the importance of finding that incumbent LECs are not dominant carriers in the provisioning of mass-market broadband services. In the marketplace, cable operators continue to increase their market share, outpacing growth by competing platforms. In the regulatory and

judicial arenas, cable operators are gaining new freedoms and rights that will strengthen their dominant position in the mass-market market for broadband services.¹⁵ In the first round of comments, some commenters tried to mask these gains and to depict cable operators as disadvantaged. Other commenters have attempted to blur the distinctions between narrowband and broadband services. Still others argue that the mass-market market includes a wholesale component dominated by incumbent LECs. These attempts to cloak the overwhelming fact that the mass-market market is dominated by cable operators and that incumbent LECs are unfairly disadvantaged in the marketplace should not deter the Commission from finding that incumbent LECs are non-dominant and that regulatory relief should follow.

A. Product Definition

1. Narrowband vs. Broadband

Many commenters in this proceeding agree with the Commission's earlier determination in the *AOL/Time Warner Merger Order* that high-speed Internet access services occupy a market separate from narrowband services.¹⁶ Several findings supported that determination. Those findings included the access to high-bandwidth content and applications with broadband, the associated costs of switching from narrowband to broadband, the "always-on" feature of broadband, and preliminary quantitative studies, which indicated separate markets for these two

¹⁵ See Cable Broadband Declaratory Ruling, ¶ 38, finding that cable modem service is an information service and not a cable service; and, *National Cable & Tel. Ass'n v. Gulf Power Co.*, ___ U.S. ___, 122 S.Ct. 782, 151 L.Ed.2d 794 (2002) ("Cable television systems that also provide Internet service are still covered by §§ 224(a)(4) and (b) [of the Act] — just as they were before 1996") (*Gulf Power*). **N.B.:** In the *Cable Broadband Declaratory Ruling*, the Commission acknowledged the *Gulf Power* ruling and reassured cable operators that "[t]hat decision is not affected by [the Commission's] categorization of cable modem service[as an information service]." ¶ 109.

¹⁶ *Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations by Time Warner Inc. and American Online, Inc., Transferors, to AOL Time Warner Inc., Transferee*, CS Docket No. 00-30, *Memorandum Opinion and Order*, 16 FCC Rcd. 6547 ¶¶ 69-73 (2001) (*AOL/Time Warner Merger Order*).

services.¹⁷ None of these findings has changed, and there is no basis for the Commission to reconsider this determination.

Recent studies show that the Commission's original thinking was right. These studies confirm that the distinguishing aspects of broadband identified by the Commission — such as speed, the always-on connection — not only draw users to broadband services but also alter their use of the Internet:

Up to now, narrowband users have wanted to upgrade to broadband mainly because of its speed and because it offers a constant connection to the Internet, but more and more people are being motivated by the desire to use specific applications.¹⁸

Broadband users are staying online four times as long, shopping online almost twice as much, and using the Internet more frequently.¹⁹ Moreover, broadband has increased the number of people who use the Internet's online multi-media features and has led to a shift from portals and Internet service providers (ISPs) to news and entertainment sites.²⁰

When users of broadband were asked how it changed or would change their online behavior, 79 percent said that they were having more fun on the Internet; 58 percent that they were downloading more audio, video, and software; and 41 percent that they were purchasing more products and services online.²¹

AT&T's suggestion that narrowband and broadband offerings are “reasonably substitutable services”²² thus not only flies in the face of the Commission's previous

¹⁷ *Id.*, ¶ 71. Add cites from note 36

¹⁸ R. Carrière, et al, BROADBAND CHANGES EVERYTHING, McKinsey & Co (2000)(Carriere Report).

¹⁹ Carriere Report.

²⁰ The McKinsey Quarterly 2001 No. 1, "What Users Think of Broadband." (McKinsey Quarterly No. 1).

²¹ McKinsey Quarterly, No. 1.

²² AT&T p. 39. In a similar vein, Covad broaches the subject of dial-up Internet access and second lines in its comments. Covad p. 9. Almost as quickly as it mentions narrowband, Covad abandons it in favor of arguing that the *Broadband Internet Access* proceeding has rendered the instant proceeding “moot.” Covad pp. 9 – 12.

determination, but also these more recent studies.²³ In the face of this, AT&T purports to dismiss the value of broadband services.²⁴ It claims that most people do not need broadband speed because they “use the Internet primarily for email, instant messaging, and shopping.”²⁵ But this claim *presumes* that their primary use of the Internet is dictated by their preferences. In fact, their primary use of the Internet may be dictated by speed — slow speed to be exact. Their attempts to access other applications may have been frustrated by download times and other time-consuming actions, leaving these users little choice of how to best use the Internet.

In any event, AT&T ignores broadband’s potential. Commenters recognize the chicken-and-the-egg issue of whether broadband facilities need to be constructed before “killer applications” will be developed or vice versa.²⁶ Even at this stage, it is clear that, as broadband use expands in the mass-market, more and more bandwidth-consuming sites and applications arise. As that occurs, the differences between broadband and narrowband will become even more pronounced.

Along this same line, AT&T argues that narrowband services are reasonably substitutable for broadband because they are available “at similar prices” and because “a 56 kbps always-on service is expected to be available soon.”²⁷ In support of its claim that the services are priced

²³ “Narrowband access is generally perceived as qualitatively inferior, and is unsuitable for many applications (*e.g.* downloading of large files that may, increasingly, contain musical or video content). At the same time, empirical studies indicate little if any actual cross-elasticity of demand between narrowband and broadband services.” J. Haring and H. Shoosan, *ILEC Non-dominance In The Provision of Retail Broadband Services*, Strategic Policy Research (March 1, 2002), attached to BellSouth’s Comments.

²⁴ AT&T even claims that “the ILECs’ narrowband monopolies — and their control over the facilities used to provide *both* broadband and narrowband services — give them market power over residential broadband services even where there is competition from cable.” AT&T p. 7. AT&T makes this absurd claim even though competitors to DSL — cable, wireless, and satellite — do not use ILEC facilities to provide their service and even though narrowband facilities will remain regulated if incumbent LECs are found to be non-dominant in the broadband arena.

²⁵ AT&T p. 39.

²⁶ *E.g.*, BellSouth p. 18-19.

²⁷ AT&T pp. 39-40.

similarly, AT&T relies on a chart in a Commission report released in 1999, which relies on 1998 data. The analysis in the *AOL/Time Warner Order* provides a more recent and nuanced comparison of prices. In that Order, the Commission concluded that “[c]onsumers switching to high-speed service from dial-up (or between high-speed services) experience costs significantly higher than those involved in switching between dial-up providers.”²⁸ Moreover, it is indisputable that the recurring costs (monthly fees) are also higher:

DSL				
	PROVIDER	DSL SERVICE WITH ONE LINE²⁹	DIAL-UP SERVICE WITH ONE LINE³⁰	DIAL-UP SERVICE WITH TWO LINES³¹
	SBC	\$61.44	\$31.44	\$48.27
CABLE				
		CABLE MODEM SERVICE WITH CABLE-TV SERVICE³²	CABLE MODEM SERVICE WITHOUT CABLE-TV SERVICE	
	AT&T	\$49.95	\$59.95	
	Comcast	\$44.95	\$54.95	
	Cox	\$44.95	\$54.95	
	Time Warner/AOL	\$44.95	\$49.95	

As for the potential 56 kbps always-on service, the addition of the always-on feature to narrowband will not be in and of itself sufficient to make narrowband a reasonably substitutable service for broadband. Speed, in conjunction with the always-on feature, distinguishes

²⁸ *AOL/Time Warner Order*, ¶ 20.

²⁹ Price represents the price of one residential telephone line, plus the price of DSL service (which includes Internet access). The price of the residential line is a 13-state average, which includes the end-user common line (EUCL) charge, but does not include other fees or taxes.

³⁰ Price represents the price of one residential telephone line, plus the price of Internet access (\$19.95). The price of the residential line is a 13-state average, which includes the end-user common line (EUCL) charge, but does not include other fees or taxes.

³¹ Price represents the price of two residential telephone lines, plus the price of Internet access (\$19.95). The price of the residential line is a 13-state average, which includes the end-user common line (EUCL) charge, but does not include other fees or taxes.

³² Price includes broadband Internet access and modem rental, but does not include the price of cable-TV service.

broadband in the mass-market. Speed makes the mass-market broadband experience enjoyable and compelling and speed facilitates access to and use of alternative applications.³³

In the final analysis, however, AT&T's argument is irrelevant. As SBC pointed out in its Non-Dominant Petition and in its Comments, even if narrowband and broadband were sufficiently substitutable to comprise a single market — a contention SBC continues to dispute — that would only strengthen the case for removing dominant carrier regulations of broadband offerings because it would mean that consumers would continue to have available to them a fully regulated substitute.

2. Wholesale vs. Retail

Commenters generally agree that, at present, there are four different technology platforms used to provide broadband services to the mass-market; these are: DSL, cable modem, satellite, and wireless.³⁴ As noted in SBC's comments, and as confirmed by many other commenters, these broadband services for the mass market are part of a single product market with no relevant submarket. This is so because, from a functional point of view, they are substantially similar and because users see these services as substitutable and providers see these services as competitive.

Other than the technologies used to support these different platforms, what distinguishes these platforms most is the regulatory environment in which they operate. Under the present

³³ Carriere Report. *See also* STRATEGIC POLICY RESEARCH, p. 6 (“In making their initial decision to acquire broadband, 80 percent gave very high priority to faster speed [citing page 24 of *Broadband Users: Cable vs. DSL, 2002*], Other cited considerations include freeing up the phone line and always-on capability. In choosing between technologies, 86 percent of users cited ‘speed of performance’ as the key choice-determining factor, followed by the technology’s reputation and (only) then price.”) And, *see also, Cable Broadband Declaratory Ruling*, & 10: “Because of the broadband capability of the cable plant, however, cable modem service subscribers can access the Internet at speeds that are significantly faster than telephone dial-up service. As a result of that faster access, subscribers can often send and view content with much less transmission delay than would be possible with dial-up access, utilize more sophisticated ‘real-time’ applications, and view streaming video content at a higher resolution and on a larger portion of their screens than is available via narrowband.”

³⁴ Alcatel, p. 7; BellSouth, p. 30; Qwest, p. 12; Sprint, p. 3; USIIA, p. 6; Verizon, p. 13.

regulatory regime, only incumbent LECs are required to provide open access to non-affiliated ISPs and to sell telecommunications services under tariff on a wholesale basis for the provisioning of broadband transport services.³⁵ Some commenters — almost exclusively ISPs — seek to exploit that difference in regulatory regimes to argue that there is a separate wholesale market for broadband transport services in which incumbent LECs are dominant.³⁶ They are wrong.

First, as SBC explained in its Non-Dominant Petition, through reliance on the *Merger Guidelines*, the Commission deems two services to be in the same product market “if a small but non-transitory price increase by a monopoly provider of one of these services would cause enough buyers to shift their purchases to the second service as to render the increase unprofitable.”³⁷ Here, ISPs argue that there is a separate wholesale market in which incumbent LECs are dominant because incumbent LECs, like SBC, sell their DSL transport service to ISPs, rather than directly to mass-market consumers. Consequently, the ISPs assert that cable modem pricing does not constrain SBC’s DSL transport. This is nonsense. To succeed in selling DSL transport services to ISPs, incumbent LECs must offer service on terms that permit ISPs to compete with cable modem providers. Any substantial price increase for DSL transport service

³⁵ Only AOL/Time Warner is obligated to provide choice of provider “in accordance with conditions imposed on the merger by the FTC.” Some cable operators are providing limited choice with certain specific ISPs, but are under not compulsion to do so. *Cable Broadband Declaratory Ruling*, & 26.

³⁶ ALTS p. 7-8; Direct TV p. 5-7; EarthLink p. 3; ITAA, p. 3-4. WorldCom argues that “several factors make cable broadband services an inadequate alternative to incumbent LEC DSL.” WorldCom p. 11. These “factors” result almost entirely from regulatory obligations imposed on telephony, but not cable broadband. As it pointed out in its comments, SBC notes that the justification for regulating wholesale relationships is the concern that the market may not function properly if a provider has exclusive control over bottleneck facilities. Such is not the case with mass-market broadband. In this market, the various competitors — cable operators, telephone companies (wireline and wireless), electric companies, satellite operators — do not rely on each other’s facilities to provide their service. In short, there is no bottleneck control over Internet access. Absent a bottleneck to complain about, ISPs are forced to fall back on the artificial distinction imposed by regulation. SBC p. 30.

³⁷ Non-Dominant Petition, p. 12. *See also* BOC Classification Order, ¶ 28; *Crandall/Sidak Declaration*, ¶ 32. *Merger Guidelines*, § 1.0.

would ultimately result in an increase in the price of DSL Internet access (assuming ISPs are not making excess profits when they sell DSL service). If that price were to make DSL Internet service non-competitive with cable modem providers' broadband service, then both the DSL Internet and transport provider would be harmed. Thus, it is easy to see that the retail price of cable modem service constrains SBC's DSL transport prices, no less than its DSL Internet service prices.

Antitrust case law supports this argument. The antitrust laws were "especially intended to serve" consumers,³⁸ and market power must be identified from their perspective.³⁹ From that perspective, the ultimate market power issue is whether SBC has "the ability to raise prices above those that would be charged in a competitive market."⁴⁰ Because of retail competition from cable modem and other services, it does not.

The antitrust laws support the view that downstream retail price competition may constrain the ability of sellers of the related wholesale input to exercise market power at the wholesale level. If the wholesale input prices rise to a point where they deprive resellers of the ability to earn a profit in the competitive downstream market, then they will be forced to cease reselling this input, and thereby deprive the wholesaler of sales at the higher price.⁴¹ This view is consistent with the basic policy of the antitrust laws, which were "especially intended to serve" consumers,⁴² and market power must be identified from the consumers' perspective.⁴³

³⁸ *Jefferson Parish Hosp. Dist. v. Hyde*, 466 U.S. 2, 15 (1984).

³⁹ *United States v. E. I. duPont de Nemours & Co.*, 351 U.S. 377, 395 (1956).

⁴⁰ *NCAA v. Board of Regents*, 468 U.S. 85, 109 n.38 (1984).

⁴¹ *See e.g., New York Citizens Comm. on Cable TV v. Manhattan Cable TV, Inc.*, 651 F.Supp. 802 (S.D.N.Y. 1986), in an antitrust action brought against a cable TV distributor and upstream cable TV programming companies for allegedly monopolizing the market for pay cable movie and non-sports entertainment in lower Manhattan, court found that wholesale pricing was constrained by impact of wholesale price increases on retail sales.

⁴² *Jefferson Parish Hosp. Dist. v. Hyde*, 466 U.S. 2, 15 (1984).

⁴³ *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 395 (1956).

Second, the Commission has held, consistent with the *Merger Guidelines*, that if “production substitution among a group of products is nearly universal among the firms selling one or more of those products,” it may consider that group of products to be in the same product market. In other words, if the facilities of most competitors are *capable* of providing a group of services, those services may be considered, for purposes of administrative convenience, to be in the same product market.⁴⁴ As the facilities of cable operators are undeniably capable of providing wholesale services to ISPs those wholesale services can and should be considered to be in the same market as retail broadband services.

Third, the issue in this proceeding is whether the Commission should maintain dominant-carrier regulations on incumbent LECs in a market presently dominated by cable operators and fully open to alternative services — wireless and satellite — none of which are dependent upon incumbent-LEC facilities. If the Commission is concerned about the choices available to ISPs, it would be odd indeed — and patently arbitrary — for the Commission to address that concern through dominant carrier regulation of incumbent LECs, rather than through open access requirements for cable modem providers. The issue of multiple ISP access has been set for comment in other proceedings, specifically in both the *Cable Broadband Declaratory Ruling* and *Broadband Title I* proceedings.⁴⁵ The ISPs’ argument pertaining to multiple ISP access should and will be addressed in those proceedings.⁴⁶ Regardless of how the Commission ultimately resolves this issue, all providers of mass-market broadband services ought to be similarly

⁴⁴ Non-Dominant Petition p. 13. See *Application of WorldCom, Inc. and MCI Communications Corp. for Transfer of Control of MCI Communications Corporation to WorldCom, Inc.*, 13 FCC Rcd 18025 (1998) (*WorldCom/MCI Merger Order*), ¶ 27.

⁴⁵ *Cable Broadband Declaratory Ruling; In the Matter of Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, CC Docket No. 02-33, Notice of Proposed Rulemaking, FCC 02-42 (Released Feb. 15, 2002) (*Title I*).

⁴⁶ WorldCom seems to be making a similar argument in favor of multiple ISP access. WorldCom p. 20-21.

regulated and, if the Commission decides for policy reasons to require open access, incumbent LECs should not be the only providers to which that policy applies.⁴⁷

3. Smaller Businesses

Some commenters claim that there is a separate smaller-business broadband market and that cable operators are not competing in this market, leaving incumbent LECs dominant carriers.⁴⁸ This issue is a red herring. Dominant carrier regulation is only appropriate in instances in which a carrier has market power, which the FCC has defined as the ability to raise price by restricting output. But when SBC sells DSL transport service to an ISP, SBC does not vary the price of that service, depending on whether the ultimate end user is a business or residential customer; the price is the same, irrespective of the type of customer. Thus the vigorous competition faced by SBC for the provision of DSL transport for use by residential customers effectively constrains SBC's pricing of DSL transport services used by smaller business customers.

In any event, those commenters who claim that cable modem providers do not offer services to smaller businesses are wrong. As pointed out in SBC's comments, cable operators are today marketing cable modem services to small business customers.⁴⁹ While it is true that their cable facilities tend to be located in residential neighborhoods, they can and do serve smaller businesses by extending those facilities to nearby businesses. Cox, for example, "realized that there were 300,000 small businesses within 50 feet of their coaxial drops, easily reachable... That

⁴⁷ SBC notes that, like cable modem service, DSL "[s]ubscribers typically have 'click-through' access to any and all content and services available on the Internet. That is, a subscriber can access the service or content of his choice by typing in the Uniform Resource Locator ('URL') of, or clicking on a hyperlink to, the desired service or content, using the web browser chosen by the subscriber or included with the subscriber's [Internet access] service." *Cable Broadband Declaratory Ruling*, ¶ 11.

⁴⁸ AdHoc, p. 17-19; Covad p. 14-15; Comptel p. 11.

⁴⁹ SBC p. 31 n98. *See also* <http://www.charterbusinessnetworks.com/smbusinessinternet.html>.

could greatly expand the networks revenue-generation potential.”⁵⁰ And, the Vice President and General Manager of Time Warner Cable in Minneapolis, Minnesota recognized that 50,000 businesses were located within range of the company’s cable service area — although, with respect to one-third of the businesses Time Warner signed up, Time Warner needed to build out more network. He is quoted as saying that “[i]t made a lot of sense to expand into the business sector.”⁵¹ These observations are not atypical.⁵² Competition spurs this kind of expansion.

This expansion of cable modem services is not surprising, given the demand for broadband services and the added revenue opportunity created by “the advent of next-generation Voice-over-Internet-protocol technology.”⁵³ The only thing standing between cable operators and some small businesses is the need to extend facilities a short distance.⁵⁴ There are no other barriers to entry. When markets are allowed to work — as they will be when incumbent LECs are declared non-dominant — pressure will build on all providers of broadband services to seek out more and more businesses and opportunities.

As noted in the BROADBAND FACT REPORT, satellite providers also have designed services “targeted at small business customers.”⁵⁵ Hughes Network Systems is reported to offer

⁵⁰ BROADBAND FACT REPORT, p. 9.

⁵¹ *Id.*

⁵² See STRATEGIC POLICY REPORT, p. 14: “We note also that cable has the ability to expand its existing capacity for cable modem service by assigning additional bandwidth and/or by increasing the number of local ‘nodes’ in its backbone network. Indeed, in our opinion, cable can more quickly — and cheaply — expand its capacity than can DSL providers.”

⁵³ BROADBAND FACT REPORT, p. 5.

⁵⁴ Businesses with fewer than eight POTs lines “represent the best growth opportunity for DSL service — voice needs are not sufficient to justify a dedicated line, and the data needs do not necessitate a more secure and reliable dedicated means of access. However, alternatives to DSL do exist. As cable providers eventually increase focus on the SMB market, it is also this low end of the market that presents the best opportunity for cable MSOs. Essentially, DSL is caught between two encroaching alternatives — T1s and cable.” — The Yankee Group SMB Report.

⁵⁵ BROADBAND FACT REPORT, p. 6.

an Internet access service called “DirecWay,” which purportedly gives small businesses “access to the same advanced technology that powers global enterprises.”⁵⁶ WorldCom is reselling this service, re-branded with WorldCom’s name.⁵⁷ StarBand offers its “StarBand Small Office” package,⁵⁸ described as “world-class, high-speed, two-way Internet access.” This service will allow “five networked PCs to share an always-on, high-speed Internet connection.”

Competitive LECs, as well, provide alternatives to smaller businesses. Indeed, they target business customers, as opposed to residential customers, with their DSL offerings.⁵⁹

Other alternatives also are available to business customers for whom larger business offerings, like frame relay service, are not viable. Many such customers use T-1 service, prices for which are constrained not only by growing competition in the special access sector, but by price cap regulation. In addition, the Yankee Group recently issued a report indicating that, for businesses with between “2 and 499 employees” — there is a shift away from DSL and POTs lines to *integrated access*, which is defined as voice and Internet access over a T1 line.⁶⁰ The Yankee Group predicts that this service will grow in popularity as prices for T1s and integrated access devices continue to decline.⁶¹ Even without integrated access, this report confirms that T1s are an excellent product for businesses with 20 to 49 employees:

⁵⁶ *Id.*

⁵⁷ *Id.*, p. 7.

⁵⁸ *Id.*, p. 6.

⁵⁹ In its comments, Time Warner Telecom notes that because ADSL provides higher speed downstream than upstream, ADSL has limited appeal to medium and large business customers. Time Warner Telecom p. 4. But if SBC’s DSL service (ADSL) is of limited appeal to certain business customers, that would only confirm that SBC is not dominant in the business sector. The reality is that SBC’s DSL deployment is primarily a mass-market deployment — something one would think the Commission would applaud given that so many carriers focus on the more lucrative business market. SBC could hardly be dominant in a market it barely serves.

⁶⁰ The Yankee Group: “DSL & POT Lines and Integrated T1s: Understanding Their Place in the SMB Market,” Report Vol. 5, No. 17 (Nov. 2001) (Yankee Group SMB Report).

⁶¹ Yankee Group SMB Report:

Given the infamous distance and *technical* limitations of DSL, T1 service will fill the market need of this segment. Declining T1 prices, as well as a sales emphasis on T1 service from carriers that offer both T1 and DSL, will further accelerate this. For example XO and Birch Telecom make it clear that T1 service is promoted over DSL, citing superior customer satisfaction, less churn, and higher margins.⁶²

In sum, small businesses, depending on their size and composition, enjoy a variety of broadband services developed for the mass-market and larger-business markets. These services are provided over different platforms and by a variety of providers. The competition among these platforms and providers underscores the fact that incumbent LECs are not dominant in the provisioning of these services.

B. Geographic Market

In its comments and its *Non-Dominance Petition*, SBC showed that the relevant geographic market for purposes of the Commission's non-dominance analysis is each ILEC's in-region service area. SBC noted that while, technically speaking, each point-to-point route constitutes a separate geographic market, there are no such routes in which incumbent LECs could exercise market power in their provision of mass market broadband services.⁶³ Thus,

Companies that are ready for an integrated access solution are those with 8 to 18 lines. Today, 684,000 SMBs [small and medium business], or 11% of the SMB market, are ready for integrated T1s. When only looking at businesses with 10 to 249 employees, the integrated access segment fulfills the requirement of 28% of the segment. . . .The sweet spot for integrated access is the 50-to-249-employee segment as the value proposition of DSL weakens. Not only do firms with 50 to 249 employees present the greatest opportunity today, but this segment also presents the greatest future growth. . . .As the wholesale cost of T1s and the price of IADs fall, the opportunity for integrated T1 service will only expand and will allow T1s to compete more effectively for companies that have fewer than eight POT lines.

⁶² *Id.* XO Communications website — XO T1 Dedicated Internet Access: <http://www.xo.com/xofferings/internet/dedicated/t1/index.html>. And, Birch Telecom website — Products & Service, Complete T-1 Internet Access: <http://www.birch.com/products/T1.shtml>. *See also* Covad website — Covad TeleXtend Service: <http://www.covad.com/businessservices/telextend.shtml>.

⁶³ *Non-Dominance Petition* at 34-38; Comments at 32.

under clear Commission precedent, the Commission should treat each incumbent LEC's in-region service area as a discrete geographic market.

Some parties nevertheless argue that there are some areas in which DSL service, but not cable modem service, is available and that incumbent LECs can exercise market power in these areas. These arguments are specious for several reasons. *First*, like arguments that there is a separate small business market, these arguments ignore the way in which incumbent LECs sell DSL service. When incumbent LECs sell DSL transport service to an Internet service provider, they do not vary the price based on the location of the ultimate end user to whom the ISP provides Internet access service; they do not even know to whom the ISP will provide Internet access service. What they do know is that in order to sell DSL transport service they must offer that service on terms that permit their ISP customers to compete with cable modem providers. That is true wherever they sell DSL transport service.

It is particularly ironic that AT&T would argue that there are geographic submarkets within which incumbent LECs have market power. When the Commission was considering deregulation of AT&T's long-distance services, it was pointed out that there were areas in which AT&T faced no facilities-based competition. AT&T responded — and the Commission agreed — that AT&T could not exercise market power in those regions because geographic rate averaging requirements would ensure that rates for all customers (including customers with no choice of facilities-based competitors) would be constrained by the competition that existed in many areas. The same, of course, is true here. While there may be a few areas in which DSL service is available, but cable modem service is not, the rates for DSL service in those areas are no different from the rates in areas where cable modem service is available.

Second, there are many more areas in which cable modem service is available, but DSL service is not, than vice versa. DSL is available to only approximately 40 percent of U.S. homes — see the addressability discussion below.⁶⁴ In contrast, cable operators report that, as of

⁶⁴ BROADBAND FACT REPORT, p. 5.

December 31, 2001, there were approximately 70 million U.S. homes passed by cable modem service.⁶⁵ As SBC pointed out in its Comments, the National Cable and Television Association (NCTA) reported in September 2001 that 83 percent of all U.S. households passed by cable would be upgraded for cable modem service by the end of 2001.⁶⁶ The reach of cable modem service far exceeds DSL.⁶⁷

Third, these commenters conveniently ignore the actual and potential penetration of wireless and satellite. StarBand and Hughes began offering two-way broadband satellite services in late 2000.⁶⁸ And other two-way broadband satellite services using the Ka-band should be online in the relatively near future.⁶⁹ Satellite service has great potential and is practically ubiquitous. Such services are available to 90 percent of U.S. households.⁷⁰ This compares favorably to both cable modem services and DSL. Interestingly, those customers already using DBS for their television service are precisely the chief targets of wireless and satellite Internet access service providers. As these customers are already accustomed to using a satellite system for television, they will be most comfortable with the satellite or wireless option for Internet access, too. SBC realizes that wireless and satellite penetration in the mass-market market for broadband services is not great; yet, even in their infancy, these alternative services act as a viable option and protect against supra-competitive prices.

⁶⁵ NCTA Press Release.

⁶⁶ Non-Dominant Petition, p. 32: citing to National Cable Television Association web site dated Sept. 25, 2001.

⁶⁷ “In economic terms, a firm can hardly dominate a market it is barely in, especially one in which its technology (*i.e.*, DSL), in general, precludes it from supplying, let alone *restricting*, the *marginal unit* of output — the *sine qua non* for exercise of market power and dominance.” J Haring and H. Shoosan, *ILEC Non-dominance In The Provision of Retail Broadband Services*, Strategic Policy Research (March 1, 2002), attached to BellSouth’s Comments.

⁶⁸ BROADBAND FACT REPORT, p.6.

⁶⁹ *Id.*

⁷⁰ *Id.*, p. 15.

B. Market Power

1. Market Share: DSL vs. Cable Modem Service

It is now beyond dispute that cable operators have the lion's share of the mass-market for broadband services. In earlier filings, as well as these reply comments, SBC has shown that cable modem service has a commanding lead in market share — a lead that has recently widened. In the fourth quarter 2001, cable operators added more than 800,000 new cable modem subscribers, giving cable operators over 7.2 million cable modem subscribers by the end of 2001.⁷¹ At the end of 2001, cable operators had captured 66 percent of the market.⁷² Residential DSL had only 33 percent.⁷³ Records from the third quarter 2001 indicate that cable operators not only signed up more broadband subscribers, they signed them up at a slightly higher rate. Cable-modem providers⁷⁴ added approximately 624,000 new subscribers, compared to DSL providers⁷⁵ who only added 392,000 new subscribers.⁷⁶ This represented a 14 percent growth in subscribers for the cable operators and a 13 percent growth for DSL.⁷⁷ Even the Commission, in its recently

⁷¹ NCTA Press Release; Cable Datacom News, "Cable Modem Market Stats & Projections, March 1, 2002, reported similar findings; however, the figures in that report included Canadian subscribers.

⁷² Cable Datacom News.

⁷³ In the *Cable Broadband Declaratory Ruling*, the Commission found similar market-share analysis: "Throughout the brief history of the residential broadband business, cable modem service has been the most widely subscribed to technology, with industry analysts estimating that approximately 68% of residential broadband subscribers today use cable modem service. Analysts estimate that about 29% of residential broadband subscribers use DSL service, and about 3% of subscribers use various radio-based technologies." ¶ 9

⁷⁴ Time Warner, AT&T Broadband, Comcast, Cox, and Charter.

⁷⁵ Covad, BellSouth, Qwest, SBC, and Verizon.

⁷⁶ Network Fusion News, "Cable Net's Demise Raises New Worries," (Dec. 10, 2001).

⁷⁷ *Id.* These reported growth rates conflicts with AT&T's unsubstantiated claim that "DSL is thriving and growing much faster than cable modem service," AT&T p. 3.

released *Cable Broadband Declaratory Ruling*, acknowledges cable modem's substantial grip over this market.⁷⁸

These figures are consistent with the Joint Industry Study prepared by McKinsey & Co. and J.P. Morgan, which compares just cable modem services and DSL. This study, which did not address wireless or satellite, reported that cable modem service was available to approximately 71 percent of the 105 million U.S. households — compared with DSL's reach, which was approximately 43 percent.⁷⁹ The study showed that 38 percent of U.S. households had access to cable modem services alone; whereas only 10 percent were limited to DSL services.⁸⁰

⁷⁸ *Cable Broadband Declaratory Ruling*, ¶ 9:

“Industry analysts estimate that high-speed Internet access service is now available to approximately 75-80% of all the homes in the United States via DSL or cable modem service, and approximately 11% of all households subscribe to these services today. While there are several types of high-speed access (DSL, cable, satellite, fixed wireless), not every home has access to every type of service. Throughout the brief history of the residential broadband business, cable modem service has been the most widely subscribed to technology, with industry analysts estimating that approximately 68% of residential broadband subscribers today use cable modem service. Analysts estimate that about 29% of residential broadband subscribers use DSL service, and about 3% of subscribers use various radio-based technologies. In the past year, some incumbent LECs have scaled back their DSL deployment plans; cable's lead over DSL has grown; and several incumbent LECs and cable operators have raised their prices for high-speed Internet access services.”

⁷⁹ NCTA Press Release. *See also* STRAGETIC POLICY REPORT, p. 13, reporting that 80 percent of U.S. residence households have access to cable modem service.

⁸⁰ *Id.* *See also* STRAGETIC POLICY REPORT, p. 13 (“The Yankee Group 2001 Survey indicates that the suburban parts of MSAs account for about 50 percent of all broadband users. These are precisely the areas where DSL suffers its greatest technical limitations due to the more typical long distances from ILECs' central offices; at the same time, this is naturally where cable companies have concentrated their network upgrades.”) Surprisingly, DIRECTV argues:

[C]able broadband service is often not available to homes that can be reached by DSL. Only 1/3 of American homes can currently choose between wireline and cable broadband services. That means 2/3 of homes are stuck with monopoly access, if they have any access at all. DIRECTV p. 6.

DIRECTV disingenuously gives the impression that DSL, and not cable modem service, is the “monopoly access” that most people are stuck with. In fact, as shown in these reply comments and as depicted in the authority cited by DIRECTV (McKinsey & Co. and J. P. Morgan H&Q, *Broadband 2001: A Comparative Analysis of Demand, Supply, Economics, and Industry Dynamics in the U.S. Broadband Market*, April 2001, pp. 40-43), while 33 percent of U.S.

This fact — that cable modem service has the lion’s share of the mass-market for broadband services — is dispositive of the issue of whether incumbent LECs are dominant in this market. As SBC explained in its Petition, antitrust recognize that “while a large market share does not, in itself, show market power, a low market share generally indicates a *lack* of market power. That is because firms with low market share usually cannot affect the price of a product by restricting their output.”⁸¹ Even so, Verizon is certainly correct when it notes that the incumbent LECs’ low market share figures overstate the strength of incumbent LECs in the broadband market:

Market share is an inherently backward-looking measure, and market power is better evaluated by considering the extent to which competing service offerings are available in the market or likely to become available in the near term. The recent debut of two-way satellite broadband, plus the promise of significant growth in terrestrial wireless services suggest that unregulated competitive offerings are likely to increase, so that existing market shares are not especially reliable predictors of future market success. Any price increase by the telephone companies would lead to defections of DSL customers to cable modem service, satellite, and fixed wireless operators.⁸²

Faced with market share data from multiple sources, including the Commission, that demonstrates conclusively that DSL providers are nondominant in the broadband Internet access market, cable operators and ISPs resort to the only ploy that is available to them: they attempt to change the numbers by redefining the market.. Each of these arguments was addressed above, and SBC will not repeat its responses here. Suffice it to say that these arguments fly in the face of Commission precedent and market realities and have no credibility whatsoever. That is perhaps why none of these commenters can point to a single independent source that places cable modem’s market share at anything less than 65 percent and DSL’s market share at anything more than 33 percent.

homes can choose between cable and DSL, 38 percent cannot choose DSL (this authority showing cable modem service is available to 72 percent of U.S. homes).

⁸¹ SBC Non-Dominant Petition, p. 42.

⁸² Verizon p. 17.

2. Demand Elasticity

As explained in SBC's comments, demand elasticity is a measure of the "the propensity of . . . customers to switch carriers or otherwise change the amount of services they purchase . . . in response to relative changes in price and quality."⁸³ Demand elasticity is relevant to a non-dominance analysis insofar as high demand elasticity can offset the significance of a high market share. Simply put, even a firm with a high market share does not have the ability to sustain excessive rates if such rates would cause customers to switch to alternative providers in large numbers. Conversely, low demand elasticity would suggest that a firm with high market share may indeed possess market power since customers would be more or less "locked-in" to that provider. Demand elasticity is not particularly relevant, however, to an assessment of whether a firm with low market share has market power. In that context, far from demonstrating the existence of market power, low demand elasticity only underscores the lack of market power such firms have because it indicates that they will have a difficult time *increasing* their market share.

In its comments, EarthLink nevertheless argues that demand is not as elastic as SBC contends.⁸⁴ Briefly stated, EarthLink asserts that consumers in the mass-market market may be constrained from exercising a competitive choice between DSL and cable modem service. EarthLink cites five reasons:

- Locked-in package commitments with penalties;
- Up-front equipment investment;
- The costs and inconvenience of being disconnected from broadband;⁸⁵
- Consumer perception that the two services are not substitutable; and
- The alleged existence of buy-through policies.⁸⁶

EarthLink greatly exaggerates these alleged constraints.

⁸³ *AT&T Streamlining Order* at n. 29.

⁸⁴ EarthLink, p. 16.

⁸⁵ WorldCom makes a similar argument. WorldCom p. 14.

⁸⁶ EarthLink, pp. 16-17.

Locked-in package commitments with penalties. According to EarthLink, “many consumers may be ‘locked-in’ under one-year or more package commitments, which carry heavy penalties if they are breached.”⁸⁷ EarthLink, however, does not even purport to estimate the percentage of DSL subscribers who have entered into such commitments, much less explain how a one-year term commitment (which is typical) could give rise to market power. SBC notes, in this regard, that the Commission has long recognized that competition for telecommunications services is most intense in the larger businesses sector notwithstanding that larger businesses *typically* seek contracts that carry term commitments, often three years or more. SBC notes, further, that, while some customers may choose term plans, no customer is forced to — certainly not by SBC’s affiliated Internet service provider which offers one or more month-to-month options in each of its servicing markets. Rather, term plans are offered so that customers may allay the up-front costs of subscribing to DSL service, such as the cost of a modem. Without some term commitment from the consumer, providers could not recoup their investments. Indeed, when and if consumers do desire to migrate from one platform to another, the other providers will be standing by to offer similar packages. Such packages actually facilitate migration because they eliminate the consumer’s concern about up-front installation and equipment charges (see EarthLink’s second reason).

Up-front equipment investment. EarthLink also argues that consumers are constrained from switching from DSL to cable modem service because “the consumer will have already invested in DSL modem equipment and installation fees and set-up time, which would be a total loss if the consumer were to abandon DSL due to a rate hike.”⁸⁸ But customers who see these up-front costs as significant can take advantage of promotional offers to waive them. While those offers may require a one-year commitment, as noted above, those commitments, which are made by some customers, but not others, hardly convert an otherwise competitive market into a

⁸⁷ EarthLink, p. 16.

⁸⁸ *Id.* at 16-17.

non-competitive market. Of course, all the speculation in the world cannot refute the facts, and the fact is that SBC's churn rate for DSL service is extremely high. Whether customers switch back to narrowband or to cable modem service is beside the point. When they abandon their DSL service, they strand whatever up-front costs they have incurred to obtain that service. Obviously, up-front costs are not a significant deterrent to switching or SBC's churn rate would not be so high.

The costs and inconvenience of being disconnected from broadband. EarthLink also argues that "in switching from one delivery platform to another, a consumer would bear the enormous cost and inconvenience of being disconnected from broadband for considerable lengths of time, because consumers oftentimes have to ensure considerable waiting periods for the broadband service to be installed."⁸⁹ This is simply untrue. SBC is unaware of any evidence of excessive waiting periods for cable modem service, much less that consumers are deterred from switching from DSL to cable modem service because of any such waiting periods. In any event, any consumer who wishes to switch from DSL service to cable modem service can retain his/her DSL service until the cable modem service is installed.

Consumer perception that the two services are not substitutable. EarthLink next argues that "consumers may not view the characteristics of the two platforms as completely substitutable or competitive[.]"⁹⁰ Again, it cites no evidence to support its speculation, although one would assume that, as one of the leading ISPs, EarthLink certainly would be privy to such evidence if it did exist. Instead, EarthLink simply throws out the possibility that some consumers may prefer one platform over the other. But studies show that this is not generally the case, and that consumers view cable modem and DSL service as substitutable.⁹¹ Moreover, as SBC previously demonstrated, the providers of these platforms see themselves as competitors.

⁸⁹ *Id.*, p. 17.

⁹⁰ WorldCom p. 17.

⁹¹ Non-Dominant Petition, p. 25.

Even more to the point, though, is that, if DSL service were perceived as so superior to cable modem service, cable modem subscribers would not so vastly outnumber DSL subscribers, nor would cable providers be *expanding* their lead.

The alleged existence of buy-through policies. EarthLink claims finally that “DSL and cable modem services are generally only available to the consumer if the consumer also purchase both related services — voice telephony from the Incumbent LEC and cable television service from the cable operator — creating a ‘buy-through’ obstacle to consumer choice.”⁹² EarthLink might have a point if local telephone service were only available to consumers who also purchased DSL service. Whether a LEC provides DSL service only to consumers who purchase its local service, however, is irrelevant. As for alleged cable “buy-through” policies, EarthLink offers no evidence that such policies are widespread or that they have any impact on competition whatsoever. And if such policies did confer market power on DSL providers, cable operators themselves could eliminate that alleged power by getting rid of their own buy-through policy — making it easier for DSL customers to switch to cable. If all this were not enough, EarthLink simply ignores competition from wireless and satellite providers. If cable operators and incumbent LECs create obstacles to consumer choice between those two platforms, it only enhances the competitive opportunities for wireless and satellite. The history of wireless telephony shows — if nothing else — that, in a competitive market, these perceived limitations on consumer choice only become sales opportunities for competitors.

As SBC pointed out in its Non-Dominant Petition, the fact that mass-market users of broadband services show highly elastic demand for such services confirms that SBC does not have market power in its provision of DSL services.⁹³ SBC believes this to be true of incumbent

⁹² EarthLink, at 17.

⁹³ Non-Dominant Petition, p. 44.

LECs generally. Some commenters, however, have suggested that SBC “recent price increase” disproves this point.⁹⁴ They are incorrect.

First, it is important to recognize that the “price increase” of February 1, 2001, actually represented the end of a year-long promotion. It was not so much a matter of raising prices as it was of returning to the pre-promotion list price of \$49.95. Second, SBC’s experience with the return to the list price supports SBC’s direct quantitative evidence in the Non-dominant Petition.

In the petition, SBC offered the testimony of Robert W. Crandall and J. Gregory Sidak. In their declaration, they showed that, for every one percent increase in the price of DSL service, demand drops by an amount between 1.184 and 1.462 percent.⁹⁵ As a result of this February 2001 return to the list price, SBC’s initial estimate is that its price elasticity was approximately – 1.2, well within the range described by Crandall and Sidak.

In its comments, AT&T suggests that the crucial question with churn rates is “What happened to SBC’s lost DSL customers?”⁹⁶ Then, AT&T proposes an answer: “[I]t is likely that *a substantial percentage of them returned to narrowband dial-up access.*”⁹⁷ In support of this assertion, AT&T cites the declaration of its own economist, Robert Willig. Yet, Professor Willig’s testimony does not support AT&T’s assertion. In his declaration, Professor Willig merely speculates as to what happens with these customers and opines: “it is likely that some of these customers switched to cable, and it is likely that some of them returned to narrowband dial-up access.”⁹⁸ Thus AT&T has cited the bald speculation of its hired economist — and a misrepresentation of this speculation at that — as fact. The truth is — and AT&T know this —

⁹⁴ CITATIONS TO RECORD.

⁹⁵ Non-Dominant Petition, p. 44. *See also* Crandall/Sidak Declaration, ¶¶ 63-67.

⁹⁶ AT&T p. 47.

⁹⁷ *Id.*

⁹⁸ Declaration of Robert Willig, attached to the Comments of AT&T Corp., ¶ 111, p. 54-55.

highly elastic demand for mass-market broadband services shows that incumbent LECs, like SBC, do not have market power and are not dominant carriers.

3. Cost, Structure, Size, and Resources

AT&T argues that SBC is in error when it contends that cable operators are deregulated. AT&T asserts that cable companies are merely “differently regulated.”⁹⁹ In support of this, AT&T cites cable operators’ obligations to comply with local franchising requirements, pay franchising fees, creation of “institutional networks” for franchising authorities, as well as “must-carry,” PEG, and other regulations. This argument misses the point. Of course, SBC recognizes that cable service is not completely deregulated, but cable *pricing* is largely deregulated, and cable operators have been taking advantage of their pricing freedom to increase substantially the price of basic cable service.¹⁰⁰ Moreover, cable operators are subject to none of the cost allocation, accounting, and audit requirements that apply to incumbent LECs. They can use monopoly revenues from their basic cable service to cross-subsidize their cable modem service to their hearts content.

More to the point, cable operators’ *broadband* service is completely deregulated. The Commission has just held that it is neither a cable service nor a telecommunications service, but rather an interstate information service.¹⁰¹ The Commission has issued a Notice of Proposed Rulemaking¹⁰² to consider whether any regulation of cable modem service under Title I is necessary, but until an order is issued, cable modem service *completely* deregulated, and the Commission has not in any event, sought comment on *price* regulation of that service.¹⁰³

⁹⁹ AT&T p. 77.

¹⁰⁰ See earlier footnote reporting Sen. John McCain’s efforts to have the rise in cable-TV prices investigated by the GAO.

¹⁰¹ *Cable Broadband Declaratory Ruling*, ¶ 33.

¹⁰² *Id.*,

¹⁰³ AT&T whines about its franchise fees and its obligations under 47 U.S.C. § 541(a)(3). Yet, as a result of the *Cable Broadband Declaratory Ruling*, neither of these cable-TV obligations now apply to AT&T’s cable modem service. Assuming for the sake of argument that

In its Petition, as well as in its comments, SBC chronicled the advantages cable operators possess in their competition for broadband customers. It noted among other things, a study by J.P. Morgan and McKinsey showing that cable operators enjoy significant cost advantages over DSL providers. This finding is echoed in another analysts report issued by Salomon-Smith-Barney's (SSB). The SSB report, "The Battle for the High-Speed Data Subscriber,"¹⁰⁴ offers a laundry list of cost and other advantages that cable modem providers enjoy over DSL providers and predicts that cable modem service will maintain a 59% to 34% market share advantage over DSL service in 2005 among the advantages it describes are:

- *Technical advantages:* A considerable number of homes are not eligible to receive DSL service and must employ alternative broadband delivery platforms (i.e., cable, satellite, fixed wireless, and wireless cable).
- *Regulatory advantages:* Regulatory developments continue to favor MSOs and the restraints on RBOCs are increasing.
- *Superior retail distribution:* In retail stores where DSL and cable modem services are both available, cable modem services are outselling DSL by seven times.
- *Cost advantages:* The incremental cost associated with offering DSL service is "extremely high" compared to that for cable modem service, which is described as "relatively modest."

The report elaborates some detail on these cost advantages. The report noted that "[b]ecause the costs of a cable plant upgrade are shared across so many revenue streams, the dedicated capital expenditures for providing cable modem service are relatively modest and the

47 U.S.C. § 541(a)(3) would otherwise pertain to cable modem service, the provision merely prohibits cable operators from engaging in public-utility "redlining." (To "redline" normally means "[t]o refuse home mortgages or insurance to areas or neighborhood judged to be poor financial risks." NEW RIVERSIDE UNIVERSITY DICTIONARY, The Riverside Publishing Co., 1984.) Does AT&T think incumbent LECs are entitled to redline? It seems reasonable to contend that, presently, incumbent LECs are prohibited from redlining, as well, under section 202 of the Act. Incumbent LECs, after all, are often *carriers of last resort*. Surely cable operators do not think they are more "burdened" in this regard than are incumbent LECs. If the Commission were to decide that DSL service is not a Title II service, then the question of dominant carrier regulation would be rendered moot in any event.

¹⁰⁴ SalomonSmithBarney, Cable and Telecommunications Services, "The Battle for the High-Speed Data Subscriber: Cable vs. DSL," August 20, 2001. (SSB Report).

returns on capital for the service are extremely high.” SSB expects cable operators to complete plant upgrades by the end of 2002, at which time SSB expects “85%-90% of the plant will be at least 750 MHz and two-way capable.”¹⁰⁵

SSB paints a far bleaker picture of DSL:

In contrast, for the RBOCs, putting fiber deep into the network, eliminating digital loop carriers (DLCs) and load coils, putting in remote terminals, etc. entail expenditures largely associated with DSLConsequently, the hurdle rate for DSL is clearly higher than it is for cable modems since the capital costs of a cable plant upgrade is shared with other services to a much greater degree than is true for DSL.¹⁰⁶

As pointed out in the Petition, the Commission, under its traditional dominant-carrier analysis, considers whether a firm enjoys advantages in the market by virtue of, *inter alia*, its size, financial strength, resources, or cost structure.¹⁰⁷ The Commission has repeatedly emphasized that the issue is not whether the firm under examination has advantages in the relevant market, but “whether any such advantages are so great as to preclude the effective functioning of the competitive market.”¹⁰⁸ Clearly incumbent LECs, like SBC, do not enjoy such advantages, especially when compared to the market leader, cable modem service, in the mass market segment.

III. Larger Business Segment

A. Market Definition.

In its initial comments, SBC defined the product market for the larger business segment as various high-speed services that transmit and route packetized data. The products in this market segment include established packet-switched services, such as Frame Relay and ATM,

¹⁰⁵ SSB Report.

¹⁰⁶ SSB Report. This same report notes that “even if a central office is DSL-ready it is not obvious that widespread provisioning is possible. This is because there are still issues with port capacity at the switch and often issues with outside plant and copper being substandard.”

¹⁰⁷ Non-Dominant Petition p. 49.

¹⁰⁸ *AT&T Reclassification Order*, ¶ 73; *AT&T Streamlining Order*, n.187. See also *COMSAT Non-Dominance Order* at 14130.

and optical transport services (*i.e.*, above DS3). It also includes Ethernet and other “next generation” packetized transport services that are capable of transmitting a wide variety of protocols, and services that use emerging technologies such as Packet Resilient Ring and optical switching and transport. SBC’s definition of the product market for the larger business segment is similar to Verizon’s definition, which includes services that use a packet switch or successor technology, as well as services that include the capability of high-speed transmission and are not circuit switched.¹⁰⁹ Both SBC’s and Verizon’s product definitions reflect the fact that a larger business customer may use a packet service to transmit data among various locations or between two points. Accordingly, the Commission should define the product market broadly to encompass the existing universe of substitutable services, as well as future packet and optical services that provide business customers with similar functionality.¹¹⁰

Commenters do not question the presence of a distinct larger business market segment or the substitutability of services such as Frame Relay, ATM and Ethernet.¹¹¹ Time Warner, for example, agrees that the larger business market and the mass market are distinct segments of the broadband market and that there is no basis for revisiting the Commission’s prior conclusion to that effect in the *WorldCom/MCI Merger Order*.¹¹² WorldCom argues that SBC has not defined the larger business market broadly enough. It argues that the Commission has not defined separate voice and data markets, and it points out that packet-switched services are merely

¹⁰⁹ Verizon p. 10.

¹¹⁰ AT&T attempts to make an issue of the fact that some Frame Relay service is provided at 56 kbps capacity, but this should not affect the Commission’s definition of the product market. AT&T p. 20. Frame Relay service at any speed is a broadband service because it is packet switched and is used by customers to transport data. Further, a relatively small and shrinking percentage of Frame Relay service is provided at 56 kbps capacity. This trend should continue, as Frame Relay service faces increasing competition from Ethernet and other next generation packet transport services.

¹¹¹ AT&T p. 22.

¹¹² Time Warner p. 3-4.

alternative technologies (as are DS1s and DS3s) for “moving large amounts of data on behalf of corporate customers.”¹¹³

WorldCom’s blanket statement that the Commission has not recognized a distinction between the voice and data markets is demonstrably incorrect. Shortly after the incumbent LECs began offering packet-switched services in the early 1990s, the Commission recognized that such services were provided over brand new networks and should be regulated differently than services provided over the legacy circuit-switched telephone network. Accordingly, the Commission held that incumbent LECs should not be required to file detailed cost-support information for “packet-switched services” given that “[t]he packet switching services market is . . . highly competitive.”¹¹⁴ It likewise justified the decision not to investigate an incumbent LEC’s packet-switching rates on the fact that the incumbent LEC was “a new entrant in the *packet switching market*, which is currently dominated by a relatively small number of well-established service providers.”¹¹⁵ The Commission’s holdings reflect the reality that the legacy circuit-switched telephone network is not well suited to carrying large amounts of data. As a result, the market has responded with packet networks and broadband services that are specifically designed for high-speed data transmission.

WorldCom is correct that a variety of services are available to meet the needs of business customers for transmitting large amounts of data and that DS1s and DS3s are used for high-speed data transport. However, SBC recognizes that it may be difficult, as a practical matter, to determine the particular instances where a DS1 or DS3 is being used in the provision of a

¹¹³ WorldCom p. 9.

¹¹⁴ *Open Network Architecture Tariffs of Bell Operating Companies*, Order, 9 FCC Rcd 440 (1993), ¶ 68 (emphasis added). See also *Southwestern Bell Protocol Conversion Waiver Review Order*, ¶ 19 (1990) (finding that detailed cost support rules of section 61.38 should not apply to Southwestern Bell’s MicroLink II a packet switching service, because “Southwestern entered the [packet switching] market with a zero share of the business and strong established competitors.”)

¹¹⁵ *Bell South Corporation on Behalf of Southern Bell Telephone and Telegraph Company, Petition for Waiver of Section 64.702 of the Commission’s Rules and Regulations To Authorize Protocol Conversion Offerings*, 3 FCC Rcd 6961, ¶ 9 (1988) (emphasis added).

broadband service. SBC also recognizes that a bright-line approach to deregulation is easier to administer and provides regulatory certainty in the market. Accordingly, SBC is taking a conservative approach and is not seeking to be declared non-dominant in the provision of any DS1 and DS3 transport services. The fact that the Commission is not deregulating the total universe of services that may be part of the broadband market certainly does not justify failing to deregulate those services that can be clearly identified as part of the product market. To the contrary, it provides additional assurance for the Commission that customers will have the option of purchasing the incumbent LECs' regulated and tariffed special access and transport services as an alternative to deregulated broadband services. It also means that the incumbent LECs' regulated and tariffed special access and transport services will continue to be available to broadband competitors for use as inputs in their service offerings.

With respect to the geographic market, AT&T attempts to argue that the Commission must conduct a market-by-market analysis of the larger business market. AT&T's argument focuses, not on broadband services themselves, but on special access and transport services that are inputs for some of these services. It takes the position that an incumbent LEC should be required to "demonstrate on a market-by-market basis that its high-capacity loops and transport facilities do not give it market power in the provision of retail services."¹¹⁶ In effect, AT&T claims that the Commission must regulate the incumbent LECs' broadband services because of their purported ability to leverage market power in the market for special access and transport services.

AT&T's argument is contrary to the Commission's established precedent. As SBC demonstrated in its initial comments, the Commission has considered and resolved a similar concern about the use of "local bottleneck facilities" as part of its determination that incumbent LECs are non-dominant in the provision of in-region, long-distance service.¹¹⁷ In the *BOC*

¹¹⁶ AT&T p. 23.

¹¹⁷ *BOC Classification Order*, ¶ 134.

Classification Order, the Commission held that applying dominant carrier regulation to the BOCs' long-distance services is "at best a clumsy tool for controlling vertical leveraging of market power by the parent, if the parent can be directly regulated instead."¹¹⁸ As SBC previously explained, this is a much easier case for the Commission than the long distance market. The incumbent LECs' primary competitors in the broadband services market have deployed their own networks and thus do not rely on incumbent LEC facilities inputs for their broadband service offerings in many cases. Another important factor is that the incumbent LECs' ability to discriminate or raise their rivals' costs is severely constrained by pervasive regulation of their exchange and exchange access services. In addition, as discussed further below, the market for special access and transport services is more competitive than the local services market at issue in the *BOC Classification Order*.

If anything, the availability of the incumbent LECs' special access and dedicated transport services as inputs provides additional justification for deregulating broadband services in all markets nationwide. Even if there is a geographic area where AT&T or another broadband competitor currently is not providing service to a larger business customer, the barriers to entry for it to do so is very low. AT&T has the option of extending its own extensive broadband network out to serve the business customer or purchasing the incumbent LEC's special access and dedicated transport services — at regulated, federally tariffed prices — as an input for its broadband service. In either case, the business customer has a competitive alternative to meet its broadband services needs. Thus, the availability of the incumbent LECs' tariffed services as inputs for competitors' broadband service offerings strengthens, not weakens, the case for deregulating broadband services on a nationwide basis.

B. Market Power.

SBC's Non-Dominant Petition and its initial comments demonstrated that the market for broadband services, such as Frame Relay and ATM, continues to be dominated by the large

¹¹⁸ *Id.*, ¶ 91 (citing DOJ Reply Comments at 27).

IXCs. In particular, the “Big Three” providers (AT&T, WorldCom and Sprint) collectively account for 70 percent of the market for these services nationwide, whereas the incumbent LECs entered the market with zero market share and still account for only about 14 percent of the market.¹¹⁹ The incumbent LECs’ small share of the market alone provides sufficient evidence to warrant non-dominant treatment. SBC, however, presented additional evidence showing that: (i) larger business customers are highly demand elastic with significant buying power; (ii) supply elasticity is equally impressive and competitors have deployed thousands of packet switches nationwide; and (iii) the incumbent LECs are new entrants in the market competing against much larger competitors with a large embedded base of lucrative business customers and nearly ubiquitous nationwide broadband networks.

1. Evidence of Competition in the Market.

Commenters such as AT&T and WorldCom do not challenge SBC’s market share data. Instead, they attempt to create an artificial distinction between the “local” market for larger business services and the interLATA market for such services.¹²⁰ Based on this distinction, AT&T argues that the incumbent LECs dominate the local market and that the incumbent LECs will “expand their dominance, first regionally and then nationally.”¹²¹ These claims are preposterous.

There are not separate local and interLATA markets for broadband services provided to larger business customers. The IDC Frame Relay and ATM studies cited by SBC do have breakdowns for local and interLATA services, but they also include aggregated nationwide data.¹²² Other analysts such as Stratecast focus exclusively on nationwide market share data and

¹¹⁹ *Crandall/Sidak Declaration* at ¶¶ 110-12.

¹²⁰ AT&T pp. 24-25. WorldCom makes a similar argument that there is a distinct market segment for “exchange and exchange access” broadband services. WorldCom p. 23. WorldCom’s analogy is misplaced because it ignores the fact that the incumbent LECs’ ATM and Frame Relay services are not inputs to the IXC’s ATM and Frame Relay services.

¹²¹ AT&T p. 25.

¹²² *Crandall/Sidak Declaration* at ¶¶ 110-12

do not include any breakdown of local and interLATA revenues.¹²³ There is a good reason that SBC relied on aggregate nationwide market share data in its Non-Dominant Petition. By citing only local market share figures, AT&T's presents a distorted picture of the market that masks a critical aspect of the market — revenues from ATM and Frame Relay services are overwhelming weighted in favor of the IXC's interLATA services. That is why the Big Three IXCs “own the U.S. frame relay market, have scale economies and are best positioned to influence users and move the market,” as one analyst observed.¹²⁴

The grossly disproportionate amount of revenues generated by interLATA ATM and Frame Relay services also explains why the IXCs have not focused on serving business customers that have only local needs. As analysts have noted, the IXCs generally have made no serious attempt to capture local business customers and, instead, have chosen to price themselves out of the market for many such customers.¹²⁵ There are indications, however, that the IXCs are increasingly willing to market to business customers with more localized data needs. WorldCom, for example, claims that its Metro Frame Relay Service offers the same reliability and scalability of WorldCom's standard Frame Relay service offerings, “but offers the advantages of discounted pricing traditionally only available” from LECs.¹²⁶ AT&T markets local ATM and Frame Relay services and allows business customers to include local service in their existing contracts for national services and to count local service revenues toward the customer's national revenue commitments, which “may even make greater discounts

¹²³ ATM and Frame Relay Market Assessment: Data/Internet Services Growth Strategies, Stratecast Partners (September 2001).

¹²⁴ *Id.*, at 12.

¹²⁵ See IDC Study at 36 (“Carriers such as AT&T and WorldCom have introduced local frame relay offerings through their CLEC units, but the IXCs are not focusing on the “local-only” market specifically.”).

¹²⁶ See <http://www1.worldcom.com/us/products/datanetworking/framerelay/metro/>.

possible.”¹²⁷ In any event, the incumbent LECs cannot be held hostage to the business decisions of the IXC to price their services in a manner that preserves their revenue stream from interLATA ATM and Frame Relay services and to target their services to more lucrative national business accounts.

Regardless of their past marketing and pricing decisions, AT&T and WorldCom have not and cannot demonstrate that competitors are incapable of providing ATM and Frame Relay service to any category of business customer. The UNE Fact Report 2002 that was recently submitted in the *Triennial Review* proceeding shows that the installed base of packet switches deployed by IXCs and CLECs has jumped from 860 to at least 1,700 in just three years.¹²⁸ In the top 100 MSAs, where most larger business customers are located, the average number of packet switches per MSA has grown by nearly 150 percent during that same time period.¹²⁹ But there also has been extensive deployment of packet switches in smaller markets such as Cotati, California; Lisle, Illinois; Evansville, Indiana; Springfield, Missouri; and Amarillo, Texas.¹³⁰ It is not surprising, therefore, that analysts have noted increasingly intense competition for local ATM and Frame Relay services from both IXCs and CLECs.¹³¹

AT&T’s and WorldCom’s marketing of their ATM and Frame Relay services also belies any claim that there is a distinct local services market in which they are not competitive. AT&T touts its local ATM and Frame Relay services as offering “unparalleled services for any-distance communications” with the convenience of one-stop shopping.¹³² According to AT&T, it has the

¹²⁷ See <http://www.ipservices.att.com/brochures2/atm1.pdf>.

¹²⁸ See UNE Fact Report 2002, prepared for and submitted by SBC, BellSouth, Qwest and Verizon in CC Docket Nos. 01-338, 96-98 and 98-147, at II-23 (April 2002). SBC incorporates the UNE Fact Report 2002 by reference into this proceeding.

¹²⁹ *Id.*

¹³⁰ *Id.*, at Appendix E (CLEC Packet Switches).

¹³¹ See, e.g., Stratecast Report at 18.

¹³² See <http://www.ipservices.att.com/brochures2/atm1.pdf>.

industry's largest fiber network, with more than 51,000 miles of fiber optic lines, more than 60 interconnected SONET fiber rings across the country, and over 620 POPs across the country.

AT&T describes the advantages of its extensive broadband network as follows:

With AT&T, you can leverage our unique "any distance" solutions to meet your local, national and global Frame Relay and ATM networking needs. With AT&T's High Speed Packet Services, you'll have a single services provider. AT&T can provide competitive offers for customers who have all their sites located in one city or who have sites located around the world.¹³³

Thus, contrary to AT&T's advocacy in this proceeding, AT&T characterizes its ATM and Frame Relay service offerings as providing business customers with "any distance" service availability.

Likewise, WorldCom offers ATM and Frame Relay services to more than 350 metropolitan areas served by 700 POPs across the nation.¹³⁴ WorldCom claims that it is uniquely qualified to deliver ATM and Frame Relay services "as part of an overall, reliable, wholly-owned, local-to-global-to-local service," and it also touts its ability to provide "seamless end-to-end connectivity between local/metro and IXC locations."¹³⁵ As with AT&T, therefore, WorldCom characterizes its ATM and Frame Relay service as offering business customers the benefits of local and national capabilities.

In addition to more established ATM and Frame Relay services provided by IXCs and CLECs, there are a number of emerging services in the larger business market segment. For example, Time Warner Telecom and other CLECs are selling Internet Protocol virtual private network services as an alternative to Frame Relay service.¹³⁶ Similarly, Ethernet services providers — such as Yipes, Time Warner Telecom and Telseon — are competing head-to-head with ATM services.¹³⁷ These competing services represent actual competition that exists in the

¹³³ See <http://www.ipservices.att.com/brochures/atm.pdf>.

¹³⁴ See <http://www1.worldcom.com/us/products/datanetworking/>.

¹³⁵ *Id.*

¹³⁶ Stratecast Report at 13.

¹³⁷ *Id.*, at 17.

market today, but they also illustrate the rapid pace of technological change in the broadband market. In this evolving market, it is inconceivable that the incumbent LECs would ever be able to acquire market power.

Moreover, the incumbent LECs continue to be disadvantaged in the broadband market. The IXCs and CLECs can and do provide “any distance” broadband services to larger business customers, but SBC and the other BOCs continue to be prohibited from competing in the market for interLATA broadband services in most areas of the country. The competitive advantage that this creates for the Big Three IXCs cannot be understated. For more than ten years, the IXCs have been constructing nationwide broadband networks and establishing longstanding relationships with large business customers. The notion that the incumbent LECs will be able to acquire market power from these much larger service providers, each of which has an established base of lucrative business customers and national broadband networks with hundreds of POPs nationwide, is patently absurd.

The difficulty of wresting market share away from the IXCs is evidenced by the fact that SBC has captured only a *de minimis* amount of business in the interLATA Frame Relay and ATM services market, despite having received interLATA authority in five states. Even when the incumbent LECs have received interLATA authority in all states, the limited reach of their local and regional networks and will leave them at a significant competitive disadvantage compared to the Big Three IXCs, which can offer many larger business customers an end-to-end service over their nearly ubiquitous nationwide networks. Therefore, it should not be surprising that analysts believe “it will be a challenge” for the BOCs to gain market share from the IXCs for ATM and Frame Relay services.¹³⁸

Of course, IXCs continue to aggressively exploit their competitive advantage in the market at the same time they are claiming the incumbent LECs are dominant in the market. As previously discussed, WorldCom markets the advantages of one-stop shopping for both local and

¹³⁸ *Id.*, at 13.

national connections and the “seamless end-to-end connectivity” between local/metro and IXC locations. In a direct reference incumbent LECs, WorldCom also makes the following misleading statement:

LECs can offer (interLATA) service, but can’t cross LATA boundaries or move into other Regional Bell Operating Company (RBOC) territories. WorldCom Metro ATM Service offers an aggressive price position compared to LECs in the marketplace. In addition, our nationwide reach provides both interLATA (IXC) and intraLATA ATM service.¹³⁹

Similarly, AT&T tells customers, “Your business communications are too important to be limited by the borders of your LATA. Now AT&T will take you any distance you want to go.”¹⁴⁰

Not only does AT&T trumpet the superior reliability of the “largest Frame Relay network in the World,” but it also tells customers they will not be “saddled with the limitations” of Network-to-Network Interfaces (NNIs).¹⁴¹ In fact, AT&T refuses to enter into NNIs with other carriers. The incumbent LECs will continue to be disadvantaged in the market because of their reliance on NNIs to serve customers beyond their existing networks, even as they slowly obtain interLATA relief. AT&T’s refusal to enter into NNI agreements will just make it that much more difficult for incumbent LECs to expand their service offerings.

2. Leveraging Market Power

AT&T and WorldCom, lacking any response to the overwhelming evidence of competition in the larger business market segment, attempts to shift the focus to special access and dedicated transport services uses as inputs in broadband services. As an initial matter, the Commission should recognize the obvious: this proceeding has nothing to do with deregulating traditional special access and dedicated transport services. Competitors will continue to have the same access to the incumbent LECs’ regulated and tariffed special access and dedicated

¹³⁹ See <http://www1.worldcom.com/us/products/datanetworking/atm/metro/>.

¹⁴⁰ See <http://www.ipservices.att.com/brochures2/atm1.pdf>.

¹⁴¹ *Id.*

transport services that they have today. Further, as previously discussed, the Commission has consistently recognized that concerns about a carrier leveraging market power from one market into other competitive markets should be addressed directly, not through dominant carrier regulation of a competitive market.

Although the regulation of special access and dedicated transport services is not at issue in this proceeding, SBC must respond to the grossly distorted description of the market for these services. AT&T and WorldCom attempt to create the impression that there is virtually no competition or self-provisioning of special access and dedicated transport used with broadband services.¹⁴² These blanket statements do not comport with reality. Indeed, the Commission recently granted SBC new or additional pricing flexibility relief in 17 markets based on SBC's showing of facilities-based competition in those markets. That means SBC now has been granted some level of flexibility in a total of 45 markets. Moreover, the UNE Fact Report 2002 demonstrated that, based on a highly conservative count of lines that CLECs provide over their own facilities, CLECs now supply at least 20 percent and likely closer to 28 percent of all business lines nationwide.¹⁴³ They also account for between 28 and 39 percent of all special access revenue.¹⁴⁴ The ability of CLECs to serve business customers over their own facilities is facilitated by the fact that business customers tend to be highly concentrated in multi-tenant units and in the largest MSAs.¹⁴⁵

In addition to generalized statements about the special access and dedicated transport market, AT&T makes a number of specific claims that are flatly incorrect. Specifically, AT&T claims that there are numerous (unidentified) areas where the incumbent LEC's special access

¹⁴² See AT&T pp. 26-30; WorldCom pp. 23-24.

¹⁴³ UNE Fact Report 2002 at IV-2.

¹⁴⁴ *Id.* at IV-3.

¹⁴⁵ *Id.*

charges are higher than the incumbent LEC's retail price for ATM and Frame Relay service.¹⁴⁶ Clearly, that is not the case anywhere in SBC's region. As the Commission is aware, SBC continues to provide broadband services, including ATM and Frame Relay services, through a structurally separate affiliate that must obtain special access services at tariffed prices. If anything, AT&T probably pays *less* than SBC's affiliate for special access and transport services because it receives significant volume discounts.

AT&T also raises unfounded service quality issues that are the subject of a separate proceeding pending before the Commission. This is just another attempt to distract the Commission from the real issue involved in this proceeding — the regulation of incumbent LEC broadband services. If the Commission concludes that there is a problem with special access service quality, and AT&T has provided no legitimate evidence that there is, then the Commission should address those issues directly in the appropriate proceeding. AT&T's tortured argument — that the primary basis for dominant carrier regulation of incumbent LEC broadband services is special access services — proves that there is no legitimate justification for such regulation.

IV. Regulatory Relief

As with broadband services in the mass-market segment, the Commission should remove dominant carrier tariff and pricing regulation of incumbent LEC broadband services in the larger business market segment. The Commission has repeatedly recognized that forbearance from tariff requirements is appropriate for services provided on a non-dominant basis. It has held that the application of section 203 tariff requirements to such services offers no public benefits, while imposing significant social costs. Conversely, it has held that detariffing of competitively provided services promotes competition and offers other significant benefits to consumers.

¹⁴⁶ AT&T pp. 32-33.

Indeed, the Commission has gone so far as to prohibit non-dominant carriers from filing tariffs.¹⁴⁷

Most commenters recognize that the mandatory tariffing requirements imposed on dominant common carriers are at best inappropriate in a competitive market.¹⁴⁸ These commenters seek forbearance of these requirements. Predictably, the commenters who urge that the Commission retain mandatory tariffing requirements also contend that LECs are dominant in the marketplace. These commenters extol the virtues of mandatory tariffing even though they themselves are not now nor ever have been required to file tariffs or have struggled mightily to free themselves of that obligation.

In contrast, AT&T, which worked so hard to rid itself of mandatory tariffing, now argues, incredibly, that the costs of dominant carrier regulations, which include mandatory tariffing, are “*de minimis*.”¹⁴⁹ That AT&T has the audacity to make this claim, given its long history of arguments to the contrary, is nothing short of astonishing and raises serious questions about its creditability. Of course, the Commission has rejected this argument in an unbroken line of cases beginning with the *Competitive Carrier* decisions in the early 1980s. For example, in the *IXC Forbearance Order* the Commission recognized that there are real world costs associated with the tariffing process:

Even under existing tariff filing procedures, requiring nondominant interexchange carriers to file tariffs for interstate, domestic, interexchange services impedes vigorous competition in the market for such services by: (1) removing incentives for competitive price discounting; (2) reducing or taking away carriers’ ability to make rapid, efficient responses to changes in demand and cost; (3) imposing costs on carriers that attempt to make new offerings; and (4) preventing consumers

¹⁴⁷ See *In the Matter of Policy and Rules Concerning the Interstate, Interexchange Marketplace; Implementation of Section 254(g) of the Communications Act of 1934, as Amended*, Second Report and Order, 11 FCC Rcd 20730, 20760 (1996)(IXC Forbearance Order); and *Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities, Authorization Therefor*, Sixth Report and Order, 99 FCC 2d1020 (1985), vacated *MCI Telecommunications Corp. v. FCC*, 765 F. 2d 1186 (DC Cir. 1985).

¹⁴⁸ BellSouth p. 52, Sprint p. 8, Verizon p. 28.

¹⁴⁹ AT&T p. 5.

from seeking out or obtaining service arrangements specifically tailored to their needs.¹⁵⁰

Any one of these negative effects is enough to justify the elimination of mandatory tariffing requirements for non-dominant carriers. All of these negative effects are potential evils that need to be avoided in this competitive broadband market.

In its discussion of mandatory tariffing, DIRECTV takes the opportunity in its comments to repeat a number of baseless allegations regarding SBC's DSL service. In particular, DIRECTV claims that SBC raised its rates by 15 percent in the tariff that it filed in September 2001. As SBC previously explained in responding to the same allegation months ago, the tariff clearly grandfathers all existing contracts between SBC and non-affiliated ISP customers, so many ISP customers are completely unaffected by the tariff. Further, the tariff allows an ISP customer to obtain a DSL price of \$39 with no commitment and a price of \$35 with a commitment of only 250 DSL lines for one year. For most ISP customers, these prices are equal to or lower than the price they previously were paying.

DIRECTV also claims that incumbent LECs such as SBC have implemented a requirement to use Point-to-Point Protocol over Ethernet (PPPoE) as a way of blocking the provision of voice-over-Internet-protocol (VoIP) services.¹⁵¹ This claim also is incorrect. At present, only SBC's ASI-North is presently requiring PPPoE; however, as VoIP will work on PPPoE, DIRECTV is incorrect to contend that this requirement was engineered to block the provisioning of VoIP services.¹⁵² If anything the unfounded and grossly distorted allegations that DIRECTV and others have raised about SBC's DSL service shows how companies can seek to gain leverage or a competitive advantage in the market by using the dominant carrier tariff process to their advantage.

¹⁵⁰ *IXC Forbearance Order* at 20760-61, ¶ 53.

¹⁵¹ DIRECTV Comments at 10-11, 17.

¹⁵² In any event, PPPoE is not incompatible with VoIP services, as DIRECTV claims. While the use of PPPoE with VoIP services may not be common yet, customers can use VoIP services over SBC's existing DSL service offering.

The Commission also should remove outdated *Computer Inquiry* requirements that are inhibiting the provision of broadband services to mass-market and larger business customers. SBC recognizes that the Commission is presently considering the future of the Computer II/III regulations in the *Computer III Further Remand Proceedings* and in the *Title I* matter.¹⁵³ Yet, other commenters correctly note that LEC non-dominance in these markets is another reason to eliminate these unnecessary and burdensome regulations.

In its comments filed last year in the *Computer III Further Remand Proceedings*, SBC noted that the Commission's rules regulating the provisioning of information services by the Bell Operating Companies (BOCs) date back more than 30 years. Times have changed. The Commission, in its recently released Notice of Proposed Rulemaking in the *Title I* proceeding, recognized this fact in its reiteration of the history of the *Computer Inquiry* decisions.¹⁵⁴ When these rules were first enunciated, the incumbent LECs had exclusive control over the bottleneck facilities needed to provide many information services. This is no longer the case. Certainly, in the mass-market segment, where the incumbent LECs' competitors are no longer use the incumbent LECs' facilities in the provision of broadband services, basis for the *Computer Inquiry* regulations is no longer applicable. In this proceeding, the Commission should make clear that Computer II/III requirements are not applicable to incumbent LECs' broadband services.

While SBC contends that these requirements should be repealed, it is clear that tariffing requirements, which are integral to the *Computer II/III* requirements, are inconsistent with a finding that a carrier is non-dominant in a market. Non-dominant carriers need not file tariffs

¹⁵³ *In the Matter of Computer III Further Remand Proceedings: Bell Operating Company Provision of Enhanced Services; 1998 Biennial Regulatory Review — Review of Computer III and ONA Safeguards*, CC Docket Nos. 95-20, 98-10 (*Computer III Further Remand Proceedings*); *In the Matter of Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, CC Docket No. 02-33 (*Title I*).

¹⁵⁴ *Title I* ¶ 35. "We note at the outset that the *Computer Inquiry* line of decisions was initiated at a time when very different legal, technological and market circumstances presented themselves to the Commission."

because it is presumed that a competitive market will establish just and reasonable prices for the carrier's services. As far as these proceedings go, SBC seeks to be placed on a par with all other non-dominant telecommunications carriers — such as competitive LECs. SBC's *Computer II/III* requirements should be no greater than or less than theirs. Specifically, the Commission should eliminate the ONA and CEI requirements applied to incumbent LECs because they are inconsistent with the tariffing relief given to non-dominant carriers. As noted by Verizon in its comments: "It would make no sense to remove mandatory tariffing for a service under Title II only to reimpose it under the guise of the *Computer Inquiries*."¹⁵⁵

In short, as the Commission has long recognized, removing dominant carrier regulation of services provided by carriers that lack market power in the provision of those services offers numerous public benefits, not the least of which is increased competition.¹⁵⁶ Accordingly, it would be in the public interest for the Commission to classify incumbent LECs as non-dominant in the highly competitive broadband market, to forbear from applying section 203 tariffing requirements to such services, and to repeal the application of the *Computer II/III* requirements to them.

V. Conclusion

There is overwhelming evidence that incumbent LECs are non-dominant in the provision of broadband services for use by mass-market customers and larger businesses. For the reasons discussed above and in SBC's Non-Dominant Petition, the Commission should expeditiously classify incumbent LECs as non-dominant in the broadband services market and forbear from applying dominant carrier regulation, including tariff, pricing and *Computer Inquiry* requirements, to incumbent LEC broadband services.

¹⁵⁵ Verizon p. 44.

¹⁵⁶ This latter benefit can itself be a basis for concluding that forbearance would be in the public interest.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Regina Ragucci, do hereby certify that on this 22nd day of April 2002, Reply Comments of SBC Communications Inc. in CC Docket No. 01-337, was served first class mail - pre-paid postage to the parties attached.

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