

BEFORE THE
Federal Communications Commission
WASHINGTON, D.C.

In the Matter of)	
)	
Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers)	CC Docket No. 01-338
)	
Implementation of the Local Competition Provisions of the Telecommunications Act of 1996)	CC Docket No. 96-98
)	
Deployment of Wireline Services Offering Advanced Telecommunications Capability)	CC Docket No. 98-147
)	

REPLY COMMENTS OF ALLEGIANCE TELECOM, INC.

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Allegiance Telecom, Inc. ("Allegiance"), by its attorneys, hereby submits these reply comments in response to the Notice of Proposed Rulemaking¹ in the above-referenced proceeding.

I. INTRODUCTION AND SUMMARY

The focus of this Triennial Review proceeding has obviously changed somewhat as a result of the United States Court of Appeals for the D.C. Circuit's decision to overturn the *UNE Remand Order* in *USTA v. FCC*. But that decision should not result in a sea change in the Commission's approach to the ILECs' unbundling obligations.

It is important to emphasize at the outset that the *USTA v. FCC* decision is profoundly flawed, most importantly because it is flatly inconsistent with the Supreme Court's opinion in

¹ See *Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers; Implementation of the Local Competition Provisions of the Telecommunications Act of 1996; Deployment of Wireline Services Offering Advanced Telecommunications Capability*, Notice of Proposed Rulemaking, 16 FCC Rcd 22781 (2001) ("NPRM").

Verizon v. FCC in many respects and because the D.C. Circuit failed to apply the deferential standard of review required in appeals of agency rulemaking decisions. The Commission has correctly described these and other problems with the D.C. Circuit's reasoning in the Commission's petition for rehearing of the *USTA v. FCC* case. If the D.C. Circuit does not itself revise its decision, the Commission must seek review by the Supreme Court.

But even assuming the D.C. Circuit's decision remains good law, on remand the Commission is free to assess the extent to which the court's opinion was based on an incorrect factual predicate. At its most basic level, the court's opinion stands for the proposition that the Commission must only require ILECs to continue to provide UNEs where the benefits of unbundling outweigh the costs. The Commission is surely bound by this standard, but it is not bound by the court's inaccurate assessment of the relative costs and benefits. For example, the court viewed the costs of unbundling to be very high because it assumed that requesting carriers could obtain access to UNEs at prices near or at those that would prevail in a fully competitive market. Based on this assumption, the court indicated that unbundling obligations were likely to have a chilling effect on investment and innovation. It accordingly suggested that a high threshold must be met before unbundling could be required. But the court's estimation of the costs incurred by CLECs to obtain UNEs is inconsistent with the Supreme Court's findings regarding TELRIC, and it ignores the very substantial costs (also recognized by the Supreme Court) CLECs incur in addition to paying TELRIC-based prices (primarily costs caused by ILEC anticompetitive behavior). The true costs incurred by CLECs to obtain UNEs are actually far above any definition of "cost-based" prices. Unbundling therefore has a much less significant effect on investment incentives than the D.C. Circuit assumed.

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Furthermore, the court had no opportunity to assess the impact of the extraordinarily high cost of capital faced by CLECs. For almost every competitor, selling equity and debt is simply too costly to contemplate, and there is no indication that this situation will change in the foreseeable future. The ILECs' costs of capital are generally much lower, as reflected in their higher bond ratings and stock prices. This means that the benefits of unbundling, allowing CLECs to obtain access to facilities that cannot be efficiently duplicated, are much greater than the court could have known.

These facts, among others, justify the adoption of an impairment standard under which unbundling obligations remain in place except where there is clear marketplace evidence that CLECs are unimpaired without a particular UNE. The standard proposed by Allegiance in its initial comments is fully appropriate under the circumstances. As Allegiance explained, the Commission should adopt a simplified standard for determining whether ILECs continue to have substantial market power in the provision of a particular UNE in the relevant geographic market. Specifically, the Commission should define the relevant product and geographic markets for UNEs and eliminate unbundling obligations for a network element for which four or more competitive network facilities have been deployed in the relevant market.

In adopting this framework, or indeed any impairment standard, the Commission must be careful to establish appropriate market definitions. For example, separate product markets should be established for voice grade loops, loops used in the provision of mass market (primarily residential) broadband such as ADSL and cable modem, DS1 loops, and loops of capacity above the DS1 level. Transport should be similarly disaggregated according to the capacity of the transport circuit. In defining geographic markets, the Commission must

distinguish between UNEs that consist of point-to-point circuits and those for which larger geographic markets are appropriate. Most importantly, each loop and each point-to-point transport link must be viewed as a separate product market. It is not enough for non-ILEC sources of supply to be available on only one end of a point-to-point route. For example, it must be demonstrated that non-ILEC sources of supply actually carry traffic between two wire centers before an ILEC can be relieved of its obligation to unbundle interoffice transport between those two wire centers. Other UNEs can support larger geographic markets. For example, it would be appropriate to adopt a national market for SS7 signaling.

Once the Commission has established the relevant product and geographic markets, it must allocate responsibility for determining whether an ILEC has met the trigger for eliminating unbundling obligations. In the case of loops and transport, this task must be delegated to the states. The Commission simply lacks the resources to determine the extent to which non-ILEC sources have been deployed along specific point-to-point routes. For those UNEs for which the relevant product market is larger than a single state (such as SS7), the Commission should assume responsibility for assessing the availability of substitutes to UNEs.

The standard proposed by Allegiance fully comports with the underlying logic of the USTA decision, when that logic is considered in light of the factual record. But regardless of the specific manner in which the Commission measures impairment, the underlying analysis must turn on whether the ILECs continue to possess substantial market power in the provision of a network element. There should be no question that they do with regard to loops, transport, and SS7. This is most obviously the case with regard to voice grade loops. Intermodal voice grade connections will not be significant until well into the future (a future too uncertain and distant to

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be relevant for this proceeding), and there are essentially no non-ILEC sources of intramodal voice grade loops. The situation with regard to DS1 level capacity loops is similar. There are no intermodal competitors for these inputs. In addition, the intramodal wholesale and self-deployment of DS1 loops is minimal and scattered. Allegiance itself has found that it is not possible to self-deploy DS1 loops.

Moreover, the Commission must reject the ILECs' attempt to refuse to provide high-capacity loops based on false no facilities claims. The Commission should clarify in this proceeding that ILECs are required to modify loops, for example by adding electronics needed to increase the capacity of a loop facility, to the same extent that the ILEC would to fulfill a request for one of its own retail or special access customers.

Similarly, there is simply no basis in the record for removing transport from the list of UNEs in any geographic market. In the so-called "UNE Fact Report," the ILECs offer only generalized statistics regarding competitive fiber deployment and collocation. But the fiber deployment data does not distinguish between fiber deployed for local and long-haul transport and statistics regarding the number of collocators in an end office say nothing about the geographic points to which the collocators' networks are connected. None of this data therefore offers any basis for concluding that there has been significant actual deployment of interoffice transport by non-ILECs, let alone whether alternatives have been deployed along specific point-to-point routes.

Furthermore, there is every reason to believe that a close examination of the actual deployment of substitutes for interoffice transport would yield the conclusion that the ILECs retain substantial and persisting market power over these inputs. This is because the entry

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barriers, in the form of (among other things) very substantial sunk costs, the difficulty of achieving scale economies over a particular point-to-point route, the need to obtain access to rights-of-way, and the exorbitant cost of capital for competitors, all make deployment by non-ILECs impossible in almost every case.

Nor can it be said that the ILECs have relinquished their market power over SS7 needed by competitive providers of local exchange service. In the *UNE Remand Order*, the Commission concluded that, while several non-ILEC sources of SS7 signaling have been deployed, those sources did not constitute true substitutes for ILEC SS7. This is because the Commission found that non-ILEC SS7 networks rely on only a handful of STP pairs. This limited deployment of STP pairs exposes purchasers of SS7 from non-ILECs to far more extensive network outage when problems occur with a single pair than is the case with the ILECs' SS7 networks, which generally include one STP pair per LATA. Nothing has changed since the time of the *UNE Remand Order* to alter this conclusion. Non-ILEC sources of SS7 continue to rely on far too few STP pairs to limit the consequences of network failure. There is therefore a complete absence of any true substitutes for unbundled ILEC SS7 service.

Finally, the Commission should continue its policy of reviewing its unbundling regime every three years. In no event should the Commission require unbundling to sunset after an arbitrary period of time, as the ILECs suggest. Section 251(d)(2) permits the elimination of unbundling obligations *only* when it determines that competitors are not impaired in the absence of a UNE. A sunset rule would therefore violate the statute. Furthermore, the three year time period for revisiting the unbundling rules is the minimum amount needed to establish some stability in the unbundling regime.

II. THE COMMISSION SHOULD ADOPT A SIMPLIFIED MARKET POWER TEST AS ITS STANDARD.

A. The *USTA v. FCC* Decision

In the *UNE Remand Order*, the Commission held that a requesting carrier is impaired if, taking into consideration sources of supply other than the ILEC, the absence of the UNE “materially diminishes a requesting carrier’s ability to provide the services it seeks to offer.”² This analysis was to be based on cost, effect on timeliness of entry, quality, ubiquity, and the impact on network operations of the absence of the UNE in question. In addition to the impairment standard, the Commission stated that it would consider whether unbundling would (1) lead to rapid introduction of competition, (2) promote facilities-based competition, investment, and competition, (3) reduce regulatory obligations, (4) promote certainty in the market, and (5) be administratively practical. See *UNE Remand Order* ¶¶ 101-116. In applying this framework, the Commission adopted a largely national list of UNEs (the main exceptions being the carve out for unbundled local switching and the limited availability of packet switching and DSLAMs).

In *USTA v. FCC*,³ the D.C. Circuit ruled that, in adopting the impairment standard in the *UNE Remand Order*, and in applying that standard in the *Line Sharing Order*,⁴ the Commission

² *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, Third Report and Order and Fourth Further Notice of Proposed Rulemaking, 15 FCC Rcd 3696, ¶ 51 (1999) (“*UNE Remand Order*”), remanded, *United States Telecom Ass’n v. FCC*, 290 F.3d 415 (D.C. Cir. 2002).

³ *United States Telecom Ass’n v. FCC*, 290 F.3d 415 (D.C. Cir. 2002).

⁴ *Deployment of Wireline Services Offering Advanced Telecommunications Capability and Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, Third Report and Order in CC Docket No. 98-147 and Fourth Report and Order in CC Docket No. 96-98, 14 FCC Rcd 20912 (1999) (“*Line Sharing Order*”).

had failed to properly balance the costs and benefits of unbundling. As seen by the court, the benefits of unbundling are that it allows a CLEC to purchase ILEC facilities where it is not practical or efficient for parties other than the ILEC to deploy those facilities. The costs of unbundling identified by the court consist primarily of disincentives for ILEC and CLEC investment and innovation that may be created by unbundling, but also of the costs of administering the unbundling regime. When describing the cost side of the analysis, the court placed special emphasis on the role of the prices competitors pay to acquire UNEs. Under the court's analysis, the lower the costs of obtaining UNEs, the greater the likelihood that such unbundling will prevent ILECs and CLECs alike from investing in new facilities and innovation. *See USTA v. FCC*, 290 F.3d at 427. Based on its assumption that the Commission had set UNE prices close to ILECs' costs (or indeed "below true cost," *id.* at 424), the court concluded that the Commission had failed to demonstrate that its impairment standard ensured that unbundling would be imposed in circumstances where the benefits would be substantial enough to outweigh the costs.

In order to balance these factors adequately, the court held that the impairment analysis must take into consideration differences in impairment for CLECs in the relevant product and geographic markets for UNEs. For example, the court indicated that the Commission should consider whether unbundling would promote investment and innovation in markets in which end-user rates are purportedly set artificially high (since such "high" rates would permit competitors to justify investment in their own facilities and unbundling rules might only serve to dampen the incentive to do so) or indeed even in markets where rates are purportedly set artificially low (since there might be no chance for investment and innovation in any event in

these markets, thus making unbundling unhelpful). *See id.* at 422-23. As to the former markets, the court held that the Commission must assess whether actual deployment by competitors of network facilities indicates that the costs of unbundling are outweighed by any benefits. The court did not, however, specify the number of non-ILEC sources of supply that would be needed to demonstrate that competitors are unimpaired in a particular market.

Furthermore, again based on its underlying conviction that the Commission had established extremely low UNE prices and that the resulting costs of unbundling are significant, the court ruled that the Commission must use a very precise method for a CLEC's costs with and without unbundling. Under the circumstances, the court held that the relevant comparison must not be (as the Commission had assumed in the *UNE Remand Order*) between a CLEC's average costs of providing service in the early stages of entry when relying on non-ILEC sources of supply and its average costs when relying on UNEs. Rather, the court held that the Commission should consider the extent to which a CLEC has a reasonable prospect of accumulating enough market share that its average costs of providing service using non-ILEC facilities resemble the average costs it would incur when purchasing UNEs.⁵

⁵ *See id.* at 427. This does *not* mean that the Commission may only require unbundling for an element that qualifies as a natural monopoly (*i.e.*, a facility for which duplication would be wasteful, regardless of how efficient the competitor is that seeks to build it) or that the Commission must apply the essential facilities doctrine. The court in *USTA v. FCC* discussed the economic theories underlying natural monopoly and the essential facilities doctrine only for the purpose of illustrating the general considerations that would be relevant to what it considered to be a proper analysis of cost, one that considers scale economies. The court merely stated that the Commission's analysis of cost must be "linked (in some degree)", *USTA v. FCC*, 290 F.3d at 427, to the theory of natural monopoly and that the essential facilities doctrine "offer[s] useful concepts for agency guidance." *Id.* at n.4. In fact, the Commission has substantial discretion to choose at what point the market share needed to achieve economies of scale for a particular facility constitutes an entry barrier significant enough to mandate unbundling. Furthermore, the Commission has recently recognized that use of an essential facilities or natural monopoly doctrine as the basis for the impairment standard conflicts with *Iowa Utilities Board v. FCC* and the language of Section 271. *See Respondents' Petition for Rehearing or Rehearing En Banc* at 12-13, *USTA v. FCC*, Nos. 00-1012 & 00-1015 (D.C. Cir. Jul. 8, 2002) ("*Respondents' Pet.*").

Finally, in overturning the *Line Sharing Order*, the court held that the impairment analysis must include consideration of the presence of intermodal competitors. *See USTA v. FCC*, 290 F.3d at 428. Thus, when considering whether ILECs must unbundle the high-frequency portion of copper loops to allow competitors to provide ADSL and similar services to the mass market, the D.C. Circuit seemed to say that one must assess the extent to which ILECs already face competition in the relevant *retail* market from intermodal competitors such as cable modem service providers (and to a lesser extent satellite providers) that do not need UNEs. This ruling seems to reflect the court's underlying judgment that the impairment analysis must be rooted in an assessment of the ultimate benefits to consumers of a particular unbundling obligation. Thus, the court seems to require that the impairment analysis look at whether an ILEC would have the ability to harm end users by raising prices (ignoring end-user rate regulation for these purposes) or stunting innovation by restricting access to UNEs. If there is enough competition from intermodal competitors that the ILEC's ability to engage in this kind of conduct by limiting access to UNEs is small, then the court's analysis suggests that "impairment" should not be found. The court did not indicate, however, how much competition from intermodal competitors must be present to justify the elimination of unbundling obligations for a particular UNE.

B. The Court's Decision In *USTA v. FCC* Was Based On A Fundamental Misunderstanding Of The Underlying Factors That Must Be Considered In A Cost-Benefit Analysis.

At its most fundamental level, the *USTA v. FCC* decision stands for the proposition that the Commission failed to engage in an adequate cost-benefit analysis to justify national

unbundling obligations. The court did suggest some issues that the Commission should logically consider in such an analysis, but it did not establish an exclusive and comprehensive list of factors to be considered. Thus, the Commission is free to exercise its substantial discretion⁶ to consider all factors that are relevant to the cost-benefit analysis, including factors that undermine the validity of the court's conclusions. *See Competitive Enter. Inst. v. NHTSA*, 45 F.3d 481 (D.C. Cir. 1995).

There are several critically important factors that the court in *USTA v. FCC* either misunderstood or to which it did not give adequate weight. First, the court's decision was based on a vastly overstated estimate of the costs of unbundling. The court assumed that CLECs can obtain UNEs at "prices that *seem* to equate to cost." *USTA v. FCC*, 290 F.3d at 424 (emphasis in original). But this assumption is inconsistent with the Supreme Court's conclusions regarding the true nature of TELRIC-based prices and the record in this proceeding.

Prices equate to costs where a market is subject to perfect competition. Yet as the Supreme Court concluded (and the Commission recently recognized)⁷, "TELRIC does not assume a perfectly efficient wholesale market or one that is likely to resemble perfection in any foreseeable time." *Verizon Communications v. FCC*, 122 S.Ct. 1646, 1669 (2001). This is because "the Commission ... qualified any assumption of efficiency by requiring ratesetters to

⁶ In assessing the implications of *USTA v. FCC*, it is critical to emphasize that the Commission has a great deal of discretion to implement reasonable rules. Even the D.C. Circuit recognized the "extraordinary complexity of the Commission's task." *USTA v. FCC*, 290 F.3d at 421. The court explained that "Congress sought to foster competition in the telephone industry" by requiring that ILECs unbundle network elements when competitors are impaired in the absence of UNEs, yet Congress "gave no detail as to either the kind or degree of impairment that would qualify." *Id.* at 421-22. Moreover, as Justice Breyer recognized in his separate opinion in the *AT&T v. Iowa Utilities Board* case, "the law gives the FCC considerable leeway in the exercise of its judgment" to establish unbundling requirements. *AT&T v. Iowa Utils. Bd.*, 525 U.S. 366, 430 (1999) (Breyer J. dissenting in part, concurring in part).

⁷ *See Respondents' Pet.* at 9.

calculate cost on the basis of ‘the existing location of the incumbent[’s] wire centers.’ This means that certain network elements, principally the local-loop elements, will not be priced at their most efficient cost and configuration to the extent, say, that a shorter loop could serve a local exchange if the incumbent’s wire centers were relocated for a snugger fit with the current geography of terminal locations.” *Id.* (citation omitted). In addition, “TELRIC rates in practice will differ from the products of a perfectly competitive market owing to built-in lags in price adjustments.” *Id.* Those lags, between state TELRIC proceedings, can be as long as four years (or even longer).

Moreover, as the Supreme Court also recognized, requesting carriers incur many substantial costs beyond simply paying TELRIC rates. The Court explained that “[i]nefficiencies built into the scheme may provide incentives and opportunities for competitors to build their own network elements, perhaps for reasons unrelated to pricing (such as the possibility of expansion into data-transmission markets by deploying ‘broadband’ technologies, or the desirability of independence from an incumbent’s management and maintenance of network elements).” *Id.* at 1670 (citation omitted). The latter point cannot be overemphasized. For as the Commission has repeatedly recognized, ILECs have powerful incentives to deny, delay, and degrade CLEC access to UNEs.⁸ There is virtually no limit to the ILECs’

⁸ See *Applications of Ameritech Corp. and SBC Communications Inc. for Consent to Transfer Control of Corporations Holding Commission Licenses and Lines Pursuant to Sections 214 and 310(d) of the Communications Act and Parts 5, 22, 24, 25, 63, 90, 95, and 101 of the Commission’s Rules*, Memorandum Opinion and Order, 14 FCC Rcd 14712, ¶ 107 (1999), *vacated on other grounds, Ass’n of Communications Enterprises v. FCC*, 235 F.3d 662 (D.C. Cir. 2001) (“[ILECs], which are both competitors and suppliers to new entrants, have strong economic incentive to preserve their traditional monopolies over local telephone service and to resist the introduction of competition that is required by the 1996 Act.”) (citation omitted); *Application of GTE Corp., Transferor, and Bell Atlantic Corp., Transferee, for Consent to Transfer Control of Domestic and International Sections 214 and 310 Authorizations and Application to Transfer Control of a Submarine Cable Landing License*, Memorandum Opinion and Order, 15 FCC Rcd 14032, ¶ 176 (2000).

opportunities to act on this incentive. Those opportunities in many cases force CLECs to pay a price even above TELRIC, as is the case with regard to high-capacity loops that Verizon refuses to provide based on meritless no-facilities claims (discussed *infra*). In other cases, CLECs receive degraded service quality, in the form of inexcusably slow provisioning times and shoddy service that in turn harms CLECs' reputations for service quality. In all cases, however, a firm such as Allegiance must incur the substantial recurring costs of paying for numerous employees and outside counsel to monitor ILEC behavior and to dispute (in some cases litigate) the endless unreasonable ILEC provisioning, maintenance, and repair practices for UNEs.

All of these expenses are in addition to the costs users of UNEs incur to initially negotiate and arbitrate interconnection agreements (sunk transaction costs) and to deploy and master electronic interfaces used solely for the purpose of ordering UNEs (also sunk costs).⁹ Users of UNEs must also disclose competitively sensitive information to their most important market competitors. *See id.* ¶ 55. They must absorb the risk that regulators or courts will change the nature of the ILECs' unbundling obligations based on factors unrelated to a competitor's ability to construct facilities or obtain them from third parties. *See id.* ¶ 57. Furthermore, more generally, requesting carriers must incur much more substantial marketing and promotional costs (on a per customer basis) to overcome the ILECs' entrenched position in the market (their first mover advantage). *See id.* ¶¶ 47-48, 50.

It is also worth emphasizing that the D.C. Circuit's analysis of costs in terms of disincentives to invest associated with unbundling contradicts the Supreme Court's decision in *Verizon v. FCC*. *See Respondents' Pet.* at 8. The Supreme Court, in sharp contrast to the D.C.

⁹ *See* AT&T Comments, Attachment F ¶¶ 48, 53 (Declaration of Robert D. Willig).

Circuit, held that the Commission could reasonably conclude that unbundling at TELRIC rates would encourage investment by both incumbents and new entrants. *See Verizon v. FCC*, 122 S.Ct. at 1668 n.20, 1672 & n.27, 1675-76 & n.33. The Supreme Court reasoned that the availability of costly-to-duplicate elements at TELRIC prices could “[avoid the] risk of keeping more potential entrants out,” while at the same time “induc[ing] them to compete in less capital-intensive facilities.” 122 S.Ct. at 1672 & n.27. Rejecting the notion embraced by the D.C. Circuit, the Supreme Court concluded that, so long as the regime “brings about some competition, the incumbents will continue to have incentives to invest and to improve their services to hold on to their existing customer base.” *Id.* at 1676 n.33.

Second, the court was unable to consider the significance of the broader financial crisis facing the telecommunications industry, and competitive carriers in particular. The cost any competitive telecommunications carrier must incur to raise capital, whether in the form of equity or debt, is far too high to make facilities deployment rational. Investors are simply leaving the sector and capital expenditures have dropped accordingly.¹⁰ One leading analyst is advising potential investors that every existing competitive provider of telecommunications service could end up in bankruptcy.¹¹ Moreover, recent revelations that WorldCom overstated cash flow by more than \$3.8 billion during the past five quarters¹² have only made a bad situation worse. As

¹⁰ See Scott Cleland, *What's Preventing Telecom's Return to Growth?*, Precursor Group (June 21, 2002) (“*What's Preventing Telecom's Return to Growth?*”) (describing 50 percent drop in industry-wide capital expenditures from 2000 to 2002).

¹¹ See Scott Cleland, *The ‘Insolvency Zone’: the Bankrupting of the U.S. Telecom Sector*, Precursor Group (May 20, 2002) (“*Insolvency Zone*”).

¹² See Simon Romero & Alex Berenson, *WorldCom Says It Hid Expenses, Inflating Cash Flow \$3.8 Billion*, N.Y. Times (June 26, 2002).

the New York Times reported, this “disclosure is expected to add to the problems of telecommunications companies to arrange financing.” *Id.*

The problems obviously affect both attempts to raise equity and debt. Selling equity is almost impossible for CLECs. Among competitors in general, stock prices have lost most of their value, causing many CLECs that have avoided bankruptcy to be delisted from NASDAQ, thus further harming companies by limiting their liquidity. Secured debt is usually less expensive for firms to sell than equity because it is generally viewed as less risky. But investors view telecommunications carriers’ debt as extraordinarily risky. Debt held by smaller CLECs such as Time Warner Telecom, Focal, and Choice One have been graded as B3, Caa3, and Ca respectively.¹³ Even some of the largest firms, such as WorldCom and Qwest, have had their bonds classified as junk grade.¹⁴ Moody’s Investors Service recently downgraded AT&T Corp. debt, which has cable assets that can at least somewhat differentiate its credit rating until they are sold to Comcast, to just two notches above “junk” status. *See id.*

There is also no indication that this will change any time in the foreseeable future for competitors. The Precursor Group has explained that “the sector is not going to rebound in the foreseeable future”¹⁵ and that “telecom is not even close to bottoming.” *Insolvency Zone* at 1. Another leading analyst recently concluded that “[t]he bottom line is we haven’t seen the bottom.

¹³ See *Time WarnerTelecom, Inc.*, Moodys.com (visited July 16, 2002) (rating Time Warner Telecom, Inc. Senior Unsecured debt as B3); *Focal Communications Corp.*, Moodys.com (visited July 16, 2002) (rating Focal Communications Corp. Senior Unsecured debt as Caa3); *Choice One Communications, Inc.*, Moodys.com (visited July 16, 2002) (rating Choice One Communications, Inc. Senior Secured Bank Credit Facility debt as Ca). These ratings indicate investments that are “highly speculative,” “in poor standing,” and “extremely speculative” respectively. See *Long Term Bond Ratings*, bondsonline.com (visited June 19, 2002) (explaining bond ratings).

¹⁴ See Jonathan Stempel, *AT&T Cut to Two Notches Above ‘Junk’*, Reuters Business Report (May 29, 2002).

¹⁵ See *What’s Preventing Telecom’s Return to Growth?*.

It's the worst time in telecoms in history."¹⁶ The growing consensus is that the telecommunications sector will not begin to pull out of this downward cycle until the latter part of 2004 at the earliest.

Critically, the BOCs that, unlike Qwest, have stayed away from investing in CLEC entry outside their regions have maintained relatively high stock prices and credit ratings. For example, SBC and BellSouth have bond ratings of Aa3.¹⁷ Thus, while even these BOCs have been harmed by the depressed state of telecommunications, their cost of capital is obviously far lower than competitors', and there is every indication that the trend will continue for the foreseeable future.

The D.C. Circuit emphasized that the Commission must consider whether it is reasonable to expect that a competitor can build its own facilities and establish economies of scale similar to the ILEC's. In assessing whether such a prospect is reasonable, the Commission must consider all of the costs that a competitor would incur today. If the cost of raising the necessary capital to build facilities is high enough, and there should be no question that it is, no competitor will have a reasonable prospect of constructing its own network facilities. Except perhaps for the few intermodal competitors in the residential market that only place limited and narrowly targeted competitive pressure on the ILECs (see *infra*), only the ILECs have the ability to raise money to invest in new facilities. In most cases, therefore, there is simply no basis for believing that

¹⁶ See Ben Klayman, *Telecom sector will be cut down to smaller size*, Reuters (June 27, 2002) (quoting Jeff Kagan).

¹⁷ See *SBC Communications, Inc.*, Moody's.com (visited July 16, 2002) (rating SBC Communications, Inc. Senior Unsecured debt as Aa3); *BellSouth Corporation*, Moody's.com (visited July 16, 2002) (rating BellSouth Corporation Senior Unsecured debt as Aa3). These ratings indicate investments that are "high grade high quality." See *Long Term Bond Ratings*, bondsonline.com (visited June 19, 2002) (explaining bond ratings).

CLECs have any reasonable prospect of building facilities and eventually achieving economies of scale possessed by ILECs. Similarly, it is almost absurd to try to quantify the “costs” of unbundling in the form of foregone CLEC investment in this environment, since there is no real possibility of such investment.¹⁸

Third, the D.C. Circuit failed to consider just how administratively burdensome it would be for regulators to conduct the kind of analysis of CLEC costs that the court seemed to contemplate. In the *UNE Remand Order*, the Commission listed administrative practicality as one reason why it adopted national unbundling rules. The D.C. Circuit concluded, however, that administrative practicality was an insufficient rationale for national rules where the Commission had abandoned the national approach in the case of switching and offered no basis as to why a similar approach was precluded for other UNEs. *See USTA v. FCC*, 290 F.3d at 423. To be sure, the requirements of Section 251(d)(2) do seem to require some recognition of the differences among geographic and product markets for UNEs. *See* 47 U.S.C. § 251(d)(2). But, a full, detailed analysis of each geographic and product market to determine whether enough CLECs could reasonably be expected to acquire the economies of scale possessed by the ILEC would be simply impossible for the Commission (or even the states) to administer. This is especially true with regard to UNEs for which the relevant geographic market should be very small (*e.g.*, loops and transport), as discussed *infra*. Moreover, the court seemed to believe that such an onerous undertaking was necessary to be sure that significant costs imposed by low-

¹⁸ It is for this reason that the Commission must reject SBC’s argument that CLECs and ILECs are in the same position to construct new facilities. *See* SBC Comments at 14.

priced unbundling obligations were not incurred. That underlying predicate is, as explained, inaccurate.

C. On Remand, The Commission Should Require The ILECs To Continue To Provide UNEs Except In Those Markets In Which Four Or More Non-ILEC Facilities-Based Substitutes Have Been Actually Deployed.

In its initial comments in this proceeding, Allegiance explained that the Commission's traditional market power analysis provides an analytical framework for determining whether competitors are impaired without access to a particular UNE and serves as a limiting principle to the impairment standard. *See* Allegiance Comments at 6-11. Under this approach, the Commission must define the relevant geographic and product markets for UNEs and then assess the extent to which substitutes for those UNEs have actually been deployed in the relevant markets. As Allegiance explained, it would make sense for the Commission to adopt a simplified trigger that unbundling obligations would continue to apply except in those markets in which four non-ILEC sources of supply had been deployed. The Commission should adopt this approach on remand. The Allegiance approach offers an administratively practical standard to a market-specific impairment standard that fully comports with the *USTA v. FCC* decision.

As mentioned, *USTA v. FCC* requires that the Commission engage in the impairment analysis on a market-by-market basis, since the costs and benefits will be different in different markets. The Allegiance approach satisfies this requirement by removing unbundling in any market in which the costs of unbundling (such as they are) are no longer worth incurring because enough non-ILEC sources of supply have been deployed to discipline ILEC behavior.

The D.C. Circuit seemed to suggest that the Commission assess on a *de novo* basis whether CLECs could reasonably be expected to achieve the economies of scale possessed by

the ILEC for a particular UNE. But as explained, a more accurate assessment of the costs of unbundling renders such a level of precision and such a costly administrative process unnecessary. Moreover, as the D.C. Circuit held with regard to pricing flexibility triggers for special access, the Commission may adopt reasonable, simplified triggers designed to eliminate ILEC regulatory requirements in a particular market. *See WorldCom v. FCC*, 238 F.3d 449 (D.C. Cir. 2001).

Furthermore, a test under which unbundling obligations are eliminated only where non-ILEC sources of supply are deployed is sound policy because of the substantial entry barriers associated with deploying network elements. The entry barriers for all investments in telecommunications facilities are very significant, since the ILECs possess very significant first mover advantages and the cost of capital for competitors is too high to justify deployment of facilities. Entry barriers are especially high for loops and transport in that competitors must incur very substantial sunk costs to build those facilities. Sunk costs increase substantially the likelihood that the incumbent will engage in strategic anticompetitive behavior.¹⁹ This is because the presence of sunk costs makes entry less likely and thus the presence of potential competitors has far less disciplining effect on the incumbent's behavior. It makes sense therefore to adopt a standard based on the extent to which firms have actually cleared the entry barriers associated with deploying UNEs as the measure for determining whether unbundling is necessary.

¹⁹ *See Implementation of Section 19 of the Cable Television Consumer Protection and Competition Act of 1992; Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, First Report, 9 FCC Rcd 7442, App. H ¶¶ 36-37 (1994).

In addition, the choice of four as the number of non-ILEC sources that should trigger the elimination of unbundling is designed to promote consumer welfare and is also consistent with the underlying logic of the *USTA v. FCC* decision. As Allegiance explained in its comments, where there are fewer than five total providers of a particular service, the risk of coordinated anticompetitive behavior is 100 percent, while the introduction of a fifth competitor reduces that likelihood down to 22 percent. *See* Allegiance Comments at 10-11. As the ILECs have repeatedly asserted in the context of the long distance market,²⁰ competitors in a concentrated market with high entry barriers are likely to keep prices well above cost. Such high prices diminish the likelihood that firms that must purchase the high priced inputs to compete in a downstream market will enter or expand entry. Rate regulation under Section 252(d)(2) therefore delivers substantial consumer benefits where there are only four sources of supply. *See* 47 U.S.C. § 252(d)(2).

In addition, the Allegiance standard accounts for the presence of intermodal competitors as required by *USTA v. FCC*. As an initial matter, it is important to emphasize that the D.C. Circuit's apparent conclusion that the Commission consider intermodal competitors as part of an impairment standard that is purportedly based on an assessment of consumer welfare is flatly inconsistent with the language of Section 251(d)(2). Under that provision, the Commission must consider whether failure to provide access to a UNE "would impair the ability of the telecommunications carrier seeking access to provide the services that it seeks to offer."

²⁰ *See, e.g., Application by New York Telephone Company (d/b/a Bell Atlantic -- New York), Bell Atlantic Communications, Inc., NYNEX Long Distance Company and Bell Atlantic Global Networks, Inc., for Authorization to Provide In-Region, InterLATA Services in New York, Declaration of Paul W. MacAvoy in Support of Bell Atlantic's Petition to Provide In-Region, InterLATA Telecommunications Services, CC Docket No. 99-295 (Sept. 29, 1999).* By citing this declaration, Allegiance does not intend to suggest that this theory can reasonably be applied to the long distance market, but only that it is applicable to UNE markets where entry barriers are very high.

47 U.S.C. § 251(d)(2). The focus of this language is on whether a requesting carrier can obtain the network inputs it needs to provide “the services that it seeks to offer.” The presence of intermodal competitors that provide retail service in competition with the requesting carrier but that have no desire and/or ability to supply the requesting carrier with a substitute for an ILEC UNE should have no relevance to the impairment inquiry. Intermodal competitors should only be relevant to the inquiry if they offer wholesale substitutes for ILEC UNEs.

Nevertheless, assuming the Commission is forced to consider all intermodal competition that competes with ILECs in retail markets under the impairment standard, the Allegiance standard takes those carriers into consideration. It does so by giving them the same weight as other sources of UNE supply. Again, the significance of an intermodal competitor in this regard is that it can provide some limit on the extent to which the ILEC could (in the absence of regulation governing end-user rates) harm consumers in retail markets. If there are enough intermodal competitors for a particular end-user service, then an ILEC would theoretically not be able to harm consumers by denying competitors access to UNEs. The ILEC would not, in other words, gain the ability to raise prices by restricting output to end users by denying access to UNEs because the numerous intermodal competitors would underprice the ILEC in the retail market and make such behavior unprofitable. But the fundamental rules governing the likelihood of coordinated anticompetitive behavior apply to intermodal competitors. A single or even three intermodal competitors will have the incentive to keep prices well above cost by tacitly cooperating with the ILEC. Thus, until there are four intermodal competitors (assuming no intramodal competitors), the ILEC would continue to have the ability to harm consumers by denying competitors access to UNEs. The Allegiance standard simply aggregates the number of

intermodal competitors in a retail market and the number of other non-ILEC sources of UNEs (generally intramodal competitors) because they all have the same ultimate effect on consumer welfare (again, assuming that is the relevant inquiry). Insufficient numbers of such competitors allow ILECs to retain their inefficient incentives, a situation in which there are substantial benefits to retaining the unbundling requirements.

Finally, the Allegiance standard fully accounts for the effects of any purported implicit subsidies that might exist in local rates. To begin with, putting aside the question of whether ILECs are in fact required to charge below cost prices for any significant number of customers (a questionable proposition when one considers charges for such things as vertical features), there is every reason to believe that UNE-based competition delivers substantial consumer welfare benefits even in areas where retail prices are set relatively low. As explained, there is almost no risk that a requesting carrier can obtain UNEs at prices that are actually below the ILEC's costs. Thus, anytime a CLEC is able to compete by using UNEs, it can do so either because (1) the ILEC's retail prices are in fact far enough above cost to allow the competitor to take market share by charging prices between the (above-cost) UNE prices and ILEC retail prices, and/or (2) the CLEC is able to introduce lower costs by deploying more efficient pieces of its own network that it combines with UNEs. Either way, introducing lower retail rates delivers substantial consumer welfare benefits.²¹

Moreover, in those markets in which ILECs are purportedly required to charge relatively high prices to compensate for lower rates charged to other end users (again, a questionable

²¹ See *Ex Parte* Letter from Robert H. Bork, Counsel to AT&T, to Michael Powell, FCC, CC Docket Nos. 01-338, 96-98, 98-147 at 4 n.4 (filed June 10, 2002).

description of most state rate regimes), the issue is again easily addressed. If competitors have truly been beneficiaries of artificially high ILEC rates in a particular geographic market, experience shows that competitors will have deployed their own facilities in those markets. Thus, the establishment of an appropriate trigger for removing unbundling addresses the question of whether competitors have been in impaired in any relevant market.

In any case, reading the *USTA v. FCC* discussion of implicit subsidies to require a dispositive role for the presence or absence of implicit subsidies in the Commission's analysis conflicts with the statute, as explained by the Commission in its rehearing petition. *See Respondents' Pet.* at 14-15. Therefore, this conclusion could not have been intended by the court.

D. Regardless Of The Market-Specific Standard Adopted By The Commission, It Must Be Sure To Define The Relevant Product And Geographic Markets In A Reasonable Way.

Even if the Commission decides not to adopt the Allegiance standard, it must adopt a standard that accounts for differences in geographic and product markets. In so doing, the Commission must be very careful to use reasonable product and geographic market definitions.

To begin with, assuming that the Commission is forced to consider intermodal competitors as discussed *supra*, it must be very careful to define the extent to which an intermodal carrier actually competes with an ILEC in retail markets. For example, cable companies that have upgraded their facilities to provide cable modem service offer competition with ILEC mass market broadband services, targeted to residential customers using ADSL. However, as Allegiance has explained, cable modem service does not constitute a substitute for broadband services demanded by businesses with more substantial and sophisticated data

requirements. *See* Allegiance Reply Comments, CC Docket No. 01-337 at 6-7 (filed April 22, 2002). Those firms increasingly demand the kind of reliability and capacity (both upstream and downstream) that can only be delivered by such products as Allegiance’s integrated access service. Cable end-user connections cannot therefore be considered intermodal substitutes for the high-capacity loops Allegiance and other CLECs need to provide integrated access service.

As this example illustrates, the Commission must establish clear rules defining the proper means of determining whether a particular non-ILEC source of supply counts as a “substitute” for purposes of the impairment analysis. It makes no sense to analyze all loops as a single product market or all transport as a single product market. To the extent that an intermodal competitor may compete in the provision of a particular end-user service, it makes sense to treat UNEs used to provide that service as a separate “product” market for purposes of the impairment analysis. Thus, the available evidence regarding both the existence of intermodal competitors and the demand patterns for different UNE substitutes suggest that, for loops, the following different loop categories should be analyzed separately: voice grade loops, loops used for the provision of mass market broadband (*e.g.*, ADSL, cable modem), DS1 loops, and loops of capacity above the DS1 level each warrants separate treatment. For transport, differences between DS1, DS3, and transport circuits above the DS3 level warrant differential treatment. SS7 signaling seems to warrant a single “product” market.

In addition, difficult issues regarding geographic market definition must be addressed with specificity. Most importantly, it is clear that, from a technical perspective, the geographic market for loops and transport is the relevant point-to-point route served by a particular loop or transport circuit. *See UNE Remand Order* ¶ 333 (discussing transport). The only reliable way to

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be sure that multiple non-ILEC sources of supply can be efficiently deployed for a particular point-to-point route is if such deployment has actually occurred. That is, a circuit should only be considered a substitute for an ILEC point-to-point UNE (loop or transport) if the non-ILEC source actually carries traffic between the two points served by the UNE. In the case of transport, this means that the non-ILEC transport circuit must carry traffic between collocated equipment located in the wire centers at either end of a transport UNE to qualify as a substitute for that transport UNE.

Furthermore, deployment of multiple non-ILEC facilities over one point-to-point route cannot be relied upon as evidence that similar deployment is efficient for another point-to-point route. In order to make such inferences, it would be necessary to examine all of the relevant entry barriers and market opportunities associated with a particular point-to-point circuit to determine whether it resembles the route for which multiple sources of supply were actually deployed. For example, in the case of a DS1 capacity loop needed to serve a particular business customer, a prospective supplier of a non-ILEC source of supply would need to consider whether it could obtain access to the building in question and under what terms and conditions. Such considerations vary dramatically from building to building and make generalizations as to the viability of deploying loop facilities impossible. Of course, other factors are equally relevant to this analysis, such as the volume of traffic to be carried over a particular route, the length of the loop in question, and costs associated with obtaining access to rights-of-way (discussed further below), all of which differ for each point-to-point route. It is simply not practical for regulators to analyze all of these issues for each point-to-point route.

Similarly, each point-to-point route for transport is different. That several non-ILEC sources of transport may have been deployed along one route does not indicate that such deployment will be efficient on another route. It is simply too difficult to make generalizations regarding, among other considerations, (1) the volume of traffic that would be carried over a particular circuit, (2) whether one or more firms that have deployed transport have been able to do so because of economies of scope that may or may not apply on a different route, (3) whether collocation space needed to accommodate multiple transport providers, while available along one route, would be available in central offices on either end of another route, or (4) the extent to which costs and delays associated with obtaining access to public and private rights-of-way needed for construction differ from city-to-city and even from point-to-point route to point-to-point route.²²

Other UNEs can be examined using larger geographic markets. For example, it makes sense to use a national geographic market for SS7. While it may be that customers' demand for SS7 is location-specific (a CLEC demands signaling for the particular geographic markets in which it operates), it is possible for an SS7 provider to make the functionalities performed by its STP pairs accessible to virtually any geographic market in the country by transmitting the signals between the STP pairs and the customer's switch over long haul transport facilities. As

²² See *Localities Hit U.S. ROW Action But May Buy Mich.-Style Approach*, State Telephone Regulation Report at 5-6 (June 7, 2002) (describing differing rights-of-way regulations among localities and their opposition to harmonization). While the ILECs offer data regarding the number of end offices in which fiber-based providers have collocated, that data is essentially a red herring. See, e.g., SBC Comments, Attachment A at III-1-6 ("UNE Fact Report 2002"). That a fiber-based transport provider may have collocated in an ILEC end office to provide a DS3 capacity circuit to an unspecified location does not demonstrate that adequate number of such facilities could be efficiently provided over a different point-to-point route. For example, it may be that four competitive fiber-based transport providers have collocated in an end office in a densely populated downtown metropolitan area. But if those four carriers provide DS3 circuits connecting different destination points (likely IXC POPs), this fact offers no basis for concluding that multiple non-ILEC sources of transport can be efficiently constructed over any particular route, especially a point-to-point route not even served by one of the collocators.

explained in more detail below, it is critically important to examine (among other things) whether a particular SS7 vendor has deployed enough STP pairs for its service offerings to constitute a viable alternative to ILEC service sold on an unbundled basis. However, it does not in theory matter where those STPs are geographically located, so long as they can be connected to a CLEC's switches using long haul transport at an affordable price. Thus, a national market appears to be reasonable for SS7.

Once the Commission has defined the relevant product and geographic markets, it should then determine whether unbundling obligations apply based on the number of non-ILEC sources of supply that have been deployed in those markets. With regard to loops and transport, it seems clear that this analysis must be performed by the states. This is simply too onerous a job for the Commission. Instead, the Commission should set clear guidelines and then leave implementation to state commissions. The states have responsibility for regulating smaller geographic areas and, especially because of their work in Section 271 proceedings and in arbitrating interconnection agreements, the state commissions generally have a more detailed understanding of the market within their jurisdictions. They are therefore in a far better position to study the location of non-ILEC facilities and what services those facilities are being used to provide. Of course, the Commission would need to assume the responsibility for performing this analysis in those states in which the regulatory commission lacks the statutory authority to perform the analysis or, for whatever reason, is unwilling or unable to perform the analysis. The Commission should also take responsibility for assessing the extent to which substitutes have been deployed in product markets, such as SS7, for which the geographic market is national.

E. ILEC Arguments That The Commission Should Adopt An Impairment Standard Under Which UNEs Would Be Less Readily Available Should Be Rejected.

In their initial comments, the ILECs asserted that the Commission should adopt an impairment standard that resulted in a flash-cut reduction in the availability of UNEs. No doubt the ILECs will take an even more aggressive approach in light of the *USTA v. FCC* decision. While it is impossible to anticipate all of the pretexts the ILECs will dream up to try to support the elimination of UNEs now in light of that decision, they are likely to repeat at least some of the arguments raised in their initial comments. Many of those are fully refuted by the arguments presented above, but some further arguments are addressed in this section.

First, there is no basis for excluding newly deployed facilities from the unbundling regime, as the ILECs urge. *See, e.g.*, SBC Comments at 13-20; Qwest Comments at 46-50. The ILECs are no less likely to have market power over a network facility deployed sometime in the future than over a network facility built in the past. Quite the contrary, given the differences in the cost of capital available to most ILECs and their competitors, it is likely that ILECs will be in a far better position to invest in next generation network facilities for the foreseeable future. Competitors will simply lack access to the capital to invest efficiently on any widespread basis. Circumstances in which only the ILEC can invest in facilities efficiently are exactly those in which, under *USTA v. FCC*, unbundling must be required.

There is also no basis in the language of Section 251(d)(2), Section 251(c)(3), or Section 153(29) (the definition of network element) for concluding that the date of deployment should affect whether a particular part of the ILEC network should be deemed a UNE. *See* 47 U.S.C. §§

251(d)(2), 251(c)(3), 153(29). Given that Congress did in fact provide for the sunset of numerous ILEC obligations imposed under the 1996 Act (such as separate affiliate requirements for interLATA telecommunications services and information services), it is clear that Congress knew how to place a temporal limit on ILEC obligations when it wanted to do so. The absence of a statutory provision limiting unbundling to network elements constructed in the past therefore reflects an affirmative Congressional intent that the impairment analysis would apply in the same way regardless of when a network element is constructed.

Second, the ILECs again repeat their tired argument that the Commission should consider the availability of a tariffed offering, mainly special access, that resembles a UNE as relevant to whether a requesting carrier is impaired in the absence of the UNE. The Commission should, as it has numerous times in the past, reject this argument.²³ To begin with, tariffed services cannot be considered to be substitutes for UNEs in the impairment analysis because they are provided over the same facilities as UNEs. The point of the impairment analysis is to determine whether the ILECs have enough market power as a result of their control over inputs of production needed by their competitors. Unbundling, then, is required to ensure that ILECs do not deny, delay, and degrade CLEC access to the inputs they need. But regardless of whether CLECs purchase the input as a UNE or (because the ILEC has violated or found some way around its unbundling obligation) as a tariffed offering, the market power analysis is exactly the same. The analysis must focus on whether competitors are impaired without access to the *facilities* at the statutory cost-based pricing standard. In addition, where impairment exists, the 1996 Act

²³ See *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service Providers*, First Report and Order, 11 FCC Rcd 15499, ¶ 287 (1996) (“*Local Competition Order*”); *UNE Remand Order* ¶ 354.

mandates that the facilities in question be available to CLECs as UNEs under Sections 251(c) and 252(d), not as tariffed services. The intent of Congress could not be clearer on this point, since the 1996 Amendments included new and specific pricing requirements applicable to UNEs that are different from those included in the 1934 Act provisions.

Third, contrary to the ILECs' assertions, there is no heightened burden of proof on competitors to justify unbundling. *See Verizon Comments* at 42. The review of UNE requirements takes place in the context of a rulemaking in which the Commission must use its judgment as an expert agency to come to a reasonable application of the statutory standards based on the record.²⁴ As explained, that record points strongly toward a presumption that unbundling obligations should continue to apply in all markets except where at least four non-ILEC sources of supply have actually been deployed. The closest analogy for the proper application of the impairment standard is therefore a non-dominance proceeding. In such proceedings the carrier that has been historically treated as dominant, in this case the ILEC, effectively bears the burden of proof to demonstrate that it no longer has market power.²⁵ This is the appropriate approach here.

III. UNBUNDLING REMAINS A CRITICAL COMPONENT OF COMPETITION POLICY.

As explained, the most appropriate approach to the impairment standard is for the Commission to define the relevant UNE product and geographic markets and then (in

²⁴ *See Chevron U.S.A. Inc. v. Natural Resources Defense Council*, 467 U.S. 837 (1984); *Motor Vehicle Manufacturers Ass'n v. State Farm Mutual Automobile Ins. Co.*, 463 U.S. 29, 43 (1983) (“[T]he agency must examine the relevant data and articulate a satisfactory explanation for its action including a ‘rational connection between the facts found and the choice made.’”).

²⁵ *See Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier*, Order, 11 FCC Rcd 3271, ¶ 163 (1995).

conjunction with the state commission) determine whether there is an adequate number (four) of competitors.²⁶ There is no basis in the record in this proceeding for concluding that four non-ILEC sources have been deployed in any relevant geographic market for loops, transport, or SS7. But even if the Commission were to adopt a different impairment standard, the underlying analysis should similarly seek to determine the extent to which ILECs continue to have market power in the provision of a particular UNE. The ILECs could not possibly meet this standard either.

When determining whether products belong in the same market, whether they are substitutes, the Commission focuses on consumer demand.²⁷ That is, if a firm introduces a “small but significant and non-transitory increase in price” in a product, the question is whether buyers shift their purchases to a second product.²⁸ If the answer is yes, the two products are substitutes. However, quantitative evidence of demand cross-elasticities between two services is often unavailable. As a result, courts and the Commission have generally relied on qualitative evidence of whether two services are “reasonably interchangeable” in their use.²⁹ For example,

²⁶ As also explained, the proper way to read Section 251(d)(2) is to require that the impairment analysis focus on whether an adequate number of alternative sources of supply for a particular network element are available to a particular CLEC. Nevertheless, if the Commission reads the *USTA v. FCC* decision to require consideration of intermodal competitors that do not provide wholesale inputs to CLECs in the impairment analysis, then the Commission should count intramodal and intermodal competitors in its determination of whether the ILEC faces adequate discipline in the market in the manner discussed *supra*.

²⁷ See *Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC’s Local Exchange Area; Policy and Rules Concerning the Interstate, Interexchange Marketplace*, Second Report and Order in CC Docket No. 96-149 and Third Report and Order in CC Docket No. 96-61, 12 FCC Rcd 15756, ¶¶ 28, 40 (1997) (“*ILEC Classification Order*”) (explaining that product markets should be defined based on demand substitutability).

²⁸ See Dept. of Justice/Federal Trade Comm’n, *1992 Horizontal Merger Guidelines*, 57 F.R. 41552, 41555-56 (1992) (rev. Apr. 8, 1997); *ILEC Classification Order* ¶ 28.

²⁹ See *Brown Shoe Co. v. United States*, 370 U.S. 294, 325 (1962) (“The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it.”); *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 404 (1956) (“The

“high correlation in the prices or price movements of two products presumptively indicates a single market.”³⁰ Evidence that a producer views another’s product as a close competitor may also indicate that the products are substitutes. *See id.* Differences or similarities in qualities such as utility, efficiency, reliability, responsiveness, and continuity may indicate whether two products are appropriately considered to be reasonably interchangeable in the market. *See United States v. Grinnell Corp.*, 384 U.S. 563, 573-75 (1966); Areeda ¶ 562b. In defining the relevant market, the regulators should consider these and other types of qualitative evidence to determine how broad or narrow the relevant product market is.

A. Loops

1. Voice-Grade Loops

As persuasively demonstrated by commenters, in no case is the ILECs’ market power over the provision of inputs greater than in the case of voice-grade loops. *See Allegiance Comments* at 24-25. Nothing has changed since the Commission concluded that “without access to unbundled loops, competitive LECs would be required to sink a large initial investment in loop facilities before they had a customer base large enough to justify such an expenditure, thereby increasing the risk of entry and raising the competitive LEC’s cost of capital.” *UNE Remand Order* ¶ 182. ILEC arguments to the contrary rely heavily on data -- largely predictions -- regarding intermodal competition. Intermodal competition for customers served by voice-

‘market’ which one must study to determine when a producer has monopoly power will vary with the part of commerce under consideration, but the tests are constant, and the market is composed of products that have reasonable interchangeability for the purposes for which they are produced, with price, use and qualities considered.”); *Applications of NYNEX Corp. Transferor, and Bell Atlantic Corp. Transferee, for Consent to Transfer Control of NYNEX Corp. and Its Subsidiaries*, Memorandum Opinion & Order, 12 FCC Rcd 19985, ¶ 37, n.88, ¶ 50, n.110 (1997).

³⁰ Phillip E. Areeda and Herbert Hovenkamp, *Antitrust Law: An Analysis of Antitrust Principles and Their Application*, ¶ 562a (1995) (“Areeda”).

grade loops is in the very early stages of halting development and remains far too meager to constrain ILEC market power over voice-grade end-user connections.

As the Commission suggested in the NPRM, “evidence of actual marketplace conditions [is] more probative than other kinds of evidence.” NPRM ¶ 17. Nonetheless, ILEC arguments regarding possible alternative sources of supply for voice-grade loops are based primarily on predictions. While the ILECs quote some impressive statistics about anticipated growth of intermodal technologies (again, assuming that these are even relevant under Section 251(d)(2)), these predictions are speculative at best and should carry no weight in an impairment analysis. For example, while explaining that only two major cable operators are actively deploying circuit-switched cable telephony, the UNE Fact Report 2002 suggests that the Commission should also consider Comcast’s promises of future deployment following its merger with AT&T.³¹ Moreover, it asks the Commission to weigh the “imminent deployment of IP cable telephony,” citing analyst predictions that cable operators will deploy primary-line IP cable telephony sometime after 2006. *See id.* All the while, it glosses over the current lack of deployment in areas where many small business customers are located and the severe technical shortcomings of current IP technologies including, critically, difficulties with reliable access to E911 services.³²

³¹ *See* UNE Fact Report 2002 at IV-10. Not only should the Commission not consider speculative promises of future performance, it should be highly skeptical of promises made in merger proceedings given that similar promises made in previous merger proceedings have gone unfulfilled.

³² *See Inquiry Concerning the Deployment of Advanced Telecommunications Capability to all Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996*, Third Report, 17 FCC Rcd 2844, ¶ 45 (“*Broadband Report*”) (explaining that cable systems are largely deployed in primarily residential areas); Wylie Wong, *Net2Phone Unveils New Net-phone Service*, CNET News.com (June 6, 2001) (explaining that Net2Phone marketed its Internet telephony service as second line service only because it could not provide access to 911 services).

The analysis of mobile wireless substitution suffers from similar flaws. The report acknowledges that the number of customers that have “abandoned wireline in favor of wireless entirely ... ‘could be as high as 5 percent.’”³³ Yet, it asks the Commission to rely on analysts’ predictions of wireless substitution in 2005, 2006, and beyond. *See UNE Fact Report 2002* at IV-12. Moreover, it baldly asserts that “wireless is now fully competitive with wireline,” avoiding any mention of the technical disadvantages that limit wireless substitutability. *See id.* at IV-13. While there is no doubt that wireless pricing and quality have improved in recent years, the Fact Report denies that inferior sound quality and lack of E911 services are of concern to consumers.³⁴ These unproven market predictions, little more than guesswork, tell little about the current state of competitor impairment with regard to voice-grade loops.³⁵

Actual marketplace evidence tells a very different story from the Fact Report. The Commission’s own data refutes the ILEC assertions. For example, only about one percent of local telephone lines terminated over coaxial cable at the end of June 2001.³⁶ Estimates of CMRS substitution for primary wireline service using voice-grade loops are only about three to

³³ See *UNE Fact Report 2002* at IV-13 (quoting *Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993, Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services*, Sixth Report, 16 FCC Rcd 13350, 13381 (2001) (citing Yankee Group survey cited in J. Sarles, *Wireless Users Hanging Up on Landline Phones*, Nashville Bus. J. (Feb. 2, 2001))) (emphasis added).

³⁴ See Michelle Kessler, *18% See Cellphones as Their Main Phones*, USA Today at 1B (Feb. 1, 2002) (“A 911 system that automatically sends a caller’s location to police and fire departments should be in place by 2005. *** U.S. cellphone service has other drawbacks ...: spotty service, dropped calls and overburdened networks. Most people won’t rely on cellphones ‘until we see quality of service begin to match’ regular phones, says Chris Murray of Consumers Union.”).

³⁵ See *UNE Remand Order* ¶ 152 (noting the difficulty of predicting future market conditions).

³⁶ See *Local Telephone Competition: Status as of June 30, 2001*, Industry Analysis Division, Common Carrier Bureau at 2 (Feb. 2002) (“*Local Competition Report*”).

five percent of mobile telephone subscribers.³⁷ Finally, the Commission's most recent data indicates that less than one percent of lines terminate over fixed wireless facilities. *See Local Competition Report* at 2. Indeed, even this data may overstate substitution. A recent Forrester Research report concludes that actual substitution by all of these technologies combined is only 1.7 percent at present.³⁸ Accordingly, the Commission should reject ILEC attempts to use unproven predictions of future competitive developments to displace actual market evidence that CLECs are currently impaired without unbundled access to voice-grade loops, the element most vulnerable to ILEC market power abuses.

2. High-Capacity Loops

Despite the recent remand of the *UNE Remand Order*, the Commission's conclusion that "[b]uilding out any loop is expensive and time-consuming, regardless of its capacity" should be beyond dispute. *UNE Remand Order* ¶ 184. ILECs continue to possess overwhelming market power in the provision of high-capacity loops. Few non-ILEC loop facilities are available to serve business customers using DS1 level services and above. This is especially true for the customers Allegiance seeks to serve -- small- and medium-sized enterprises. Indeed, in many cases, replicating the vast ILEC network with loop facilities that each serves only a single customer would be impossible. As the Supreme Court recently explained, "entrants may need to

³⁷ See *Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993, Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services*, Seventh Report, FCC 02-179 at 32 (rel. July 3, 2002) (citing *Carriers Said to Need New Tactics to Combat LD Substitution*, Communications Daily (Mar. 15, 2002) (citing Yankee Group Analyst Knox Bricken's estimate of 3 percent)). Moreover, the Commission could improve wireless substitution for wireline services by setting a firm deadline for implementation of wireless number portability.

³⁸ See Paul Kirby, *Analysts: Wireless Displacement of Wireline Services Will Rise*, Telecommunications Reports at W-2 (May 6, 2002) ("According to Forrester Research, 1.7% of U.S. households have turned to new communications options such as mobile telephones and cable- or digital subscriber line (DSL)-delivered telephony and broadband Internet access in place of basic wireline telephony.").

share some facilities that are very expensive to duplicate (say, loop elements) in order to be able to compete in other, more sensibly duplicable elements....”³⁹

As Allegiance demonstrated in its comments, there is no intermodal competition for high-capacity service (DS1s and above). *See* Allegiance Comments at 20-21. As a result, the only competition in the provision of these services is intramodal. These intramodal competitors remain critically dependent on ILEC high-capacity end-user facilities. As an initial matter, the Commission should reject ILEC attempts to obscure the issue through incorrect market definitions. For example, Verizon argues that there is significant intermodal competition for mass market (primarily residential) customers, but it states that large business customers are served by ATM and frame relay service providers other than the ILECs. Although Allegiance agrees that these are distinct product markets, this analysis totally ignores the significant segment of business customers in between the mass market and large business market -- small- and medium-sized enterprises that use DS1 capacity services for products such as integrated access service. *See* Allegiance Comments, CC Docket No. 01-337 at 2-8 (filed Apr. 22, 2002). For these DS1 level services, there are not sufficient alternative facilities available to limit ILEC market power.

Moreover, the Commission should carefully scrutinize the data regarding high-capacity loops presented in the UNE Fact Report 2002 before relying on it. Many of the ILECs’ conclusions are based on flawed methodology and obvious gaps in reasoning. In the Fact Report, the ILECs purport to demonstrate that CLECs are not impaired without access to

³⁹ *See Verizon v. FCC*, 122 S.Ct. at 1672 n.27; *see also* Letter from Chairman Michael K. Powell, to Senator Ernest F. Hollings (Mar. 5, 2002) (“[L]oops are probably the most difficult network element for competitors to duplicate and, thus, the most critical asset.”).

unbundled high-capacity loops by showing that CLECs provision services to their business customers using unbundled high-capacity loops in only a small percentage of cases. *See* UNE Fact Report at IV-6. From this, the Fact Report concludes that “CLECs are able to serve the vast majority of their high-capacity customers with *their own high-capacity facilities.*” *See id.* (emphasis added). This analysis makes a leap of logic that is not only misleading but intentionally distorts the truth. ILECs are well aware that in many (perhaps most) cases, CLECs do not provide high-capacity service over their own facilities, but instead use ILEC special access services because they cannot obtain unbundled loops. Verizon, for example, rejects up to 30 percent of CLEC UNE DS1 orders on the grounds that it has no facilities available to provision the orders.⁴⁰ Regardless of whether they purchase UNEs or special access, CLECs remain critically dependent upon ILEC facilities for access to the customer.

Moreover, the number of unbundled high-capacity loops indicated in the Fact Report is artificially low due to the ILECs’ relentless refusal to comply with their legal obligation to provide unbundled high-capacity loops. Thus, they deny competitors critical inputs to which CLECs are legally entitled and then attempt to use that fact to demonstrate that those competitors are not impaired. In fact, most CLECs are forced to pay a premium for special access only because ILECs have impeded their access to and use of UNEs at every turn.⁴¹

⁴⁰ In the Virginia Section 271 proceeding, Verizon testified that it rejects up to 30 percent of CLEC UNE DS1 orders for no facilities. *Inquiry into Verizon Virginia’s Compliance with the Conditions Set Forth in 47 U.S.C. § 271(c)*, Transcript of Hearing at 824, Case No. PUC 200200046 (Virginia State Corp. Comm’n June 19, 2002).

⁴¹ For example, many ILECs refuse to make minor modifications to unbundled loops to make them usable for competitors, such as adding line cards, thereby forcing competitors to obtain the high-capacity loop as an access service.

Allegiance's experience illustrates this point. Its business model calls for it to use its own switching with unbundled high-capacity loops, usually DS1s, to provide innovative integrated access services to small- and medium-sized enterprises. Allegiance has found that it is simply not possible to self-provision DS1 level loops. Nonetheless, Allegiance has frequently been forced to obtain these end-user connections as tariffed special access services rather than unbundled loops due to the intransigence of ILECs, especially Verizon. For example, between January and June of this year, Verizon rejected 16.8 percent of Allegiance's orders for UNE DS1 loops in Massachusetts due to "no facilities." In New York and New Jersey, Verizon rejected 14.6 percent and 27.7 percent respectively, again for no facilities reasons. In January alone, Verizon rejected 53.5 percent of Allegiance's orders for UNE DS1 loops claiming that no facilities were available. Even more striking is Allegiance's experience in Portland, Oregon. In the part of Portland served by Qwest, Allegiance has been able to obtain unbundled DS1 loops for all of its integrated access customers. In the part of Portland served by Verizon, Allegiance has been unable to obtain *any* unbundled DS1 loops, and has instead resorted to ordering special access service so that it may serve its high-capacity end-user customers.

Because the record demonstrates that insufficient alternatives exist to constrain ILEC market power over high-capacity end-user connections, the Commission should reaffirm that ILECs must provide high-capacity loops on an unbundled basis. But it is equally important that the Commission clarify ILEC obligations to unbundle high-capacity loops so that CLECs are able to use UNEs to compete and are no longer coerced into purchasing above-cost special access circuits needlessly. Specifically, the Commission should clarify that ILECs, as part of

their duty to unbundle the loop, have an affirmative duty to make minor modifications to make the loop usable for the requesting carrier. The Commission has concluded that

the loop includes attached electronics, including multiplexing equipment used to derive the loop transmission capacity [with the exception of DSLAMs]. The definition of a network element is not limited to facilities, but includes features, functions, and capabilities as well. Some loops, ... are equipped with multiplexing devices, without which they cannot be used to provide service to end users. Because excluding such equipment from the definition of the loop would limit the functionality of the loop, we include the attached electronics ... within the loop definition.

UNE Remand Order ¶ 175 (footnotes omitted). Moreover, the Commission has held -- and the Eighth Circuit has affirmed -- that Section “251(c)(3) requires ILECs to provide modifications to their facilities to the extent necessary to accommodate access to network elements.”⁴²

Nevertheless, Allegiance has increasingly encountered problems obtaining UNE DS1s from Verizon because Verizon refuses to make minor modifications that would enable Allegiance to use the “features, functions, and capabilities” of the loop.⁴³ Once Verizon has rejected an order, Allegiance’s options are limited. First, it may cancel the order and resubmit it at a later date on a “hit or miss” basis hoping that facilities may have become available. This is clearly an unworkable option, since Allegiance must be responsive and accountable to its customer for a timely and reliable installation. Second, Allegiance may cancel the order and resubmit it as an order for special access services. These orders, by contrast to UNEs, are more promptly and efficiently fulfilled, even if modifications are required. But this process leaves

⁴² *UNE Remand Order* ¶ 173 (citing *Iowa Utils. Bd. v. FCC*, 120 F.3d 753, 813, n.33 (8th Cir. 1997) (citing *Local Competition Order* ¶ 198)).

⁴³ No other BOC rejects UNE orders for “no facilities” with the frequency or for the wide variety of reasons cited by Verizon. Verizon stands out among BOCs in the number and variety of circumstances it characterizes as “no facilities” for purposes of rejecting UNE loop orders. Pacific Bell, for example, will not reject UNE orders for “no facilities” except where there are no copper lines or the copper lines are defective.

Allegiance with little alternative than to pay above-cost special access rates and to forgo the cost-based UNE rates to which it is entitled under the Act. It bears repeating that the facilities used to provide ILEC retail high-capacity service are exactly the same as the facilities purchased by CLECs as high-capacity unbundled loops. There is no principled basis therefore for treating these same facilities differently depending on whether they are purchased as special access or as UNEs.

In many of these cases, the cause of the “no facilities” status could be easily corrected without construction and for a relatively modest cost. But Verizon refuses. For example, Verizon will reject an order for “no facilities” reasons when the loop needs only the addition of a repeater shelf or an apparatus/doubler case. Verizon makes these modifications in the normal course to fulfill retail or special access orders. Verizon’s refusal to accord its CLEC wholesale customers treatment comparable to that it provides its retail and special access customers is discriminatory and deprives CLECs of the ability to offer their own customers competitively priced service. Indeed, as NewSouth explained, this practice allows CLECs to compete for existing ILEC high-capacity customers only with no ability to compete for new customers of high-capacity service without ILEC high-capacity facilities already in place. *See* NewSouth Comments at 36 (public version).

The Commission should take the opportunity afforded by this proceeding to unequivocally reject Verizon’s most recent attempt to thwart competition. This practice is merely an abuse of the ILEC’s market power over high-capacity loops. Accordingly, the Commission should clarify that ILECs have an existing duty, as part of the obligation to

unbundle the loop facility, to modify loops, including adding electronics, to the same extent that the ILEC would to fulfill a request for one of its own retail or special access customers.⁴⁴

Finally, the Commission should soundly reject the SBC proposal that unbundling for all DS-3 loops be eliminated and that unbundling be eliminated for DS1 loops in those wire centers that meet any of the following requirements: (1) two or more fiber-based collocations have been established; (2) the wire center serves 15,000 or more business lines; or (3) the wire center serves customers representing \$150,000 or more per month in special access revenues. *See SBC Comments* at 101. SBC's DS1 test in particular should be rejected. As the Commission has concluded, collocation is not an especially reliable proxy for determining where end-user connections have been deployed.⁴⁵ In any event, as explained *supra*, the only reliable way to determine whether non-ILEC sources of a loop can be provided is if carriers have actually deployed them over the point-to-point route in question. Moreover, SBC's own data demonstrates that the vast majority (just under 80 percent and over 85 percent respectively) of wire centers with 15,000 business lines or more and special access revenues of \$150,000 or more have either one or zero collocators. *See SBC Comments* at 91-92. As the Commission has itself recognized by retaining dominant carrier tariffing requirements for ILECs that have received special access pricing flexibility, the ILECs remain dominant where they face only a single

⁴⁴ *See NewSouth Comments* at 31 (public version); *see also id.* at 32-35 (discussing state decisions finding a duty to modify). The Commission relied on similar reasoning in requiring ILECs to condition DSL-capable loops. *See UNE Remand Order* ¶¶ 172-173. Although this was at issue in the appeal of the *UNE Remand Order*, the D.C. Circuit declined to address loop conditioning. *See USTA v. FCC*, 290 F.3d at 428.

⁴⁵ *See Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers; Petition of US West Communications, Inc. for Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA, Fifth Report and Order and Further Notice of Proposed Rulemaking*, 14 FCC Rcd 14221, ¶¶ 100-03 (1999) (“*Pricing Flexibility Order*”), *aff'd*, *WorldCom, Inc. v. FCC*, 238 F.3d 449 (D.C. Cir. 2001).

competitor. *See generally Pricing Flexibility Order.* So long as ILECs remain dominant, they wield market power over loop facilities that impairs competitors. SBC's test for unbundling relief says nothing about impairment as the statutory standard requires, and accordingly, should be rejected.

B. Transport

Commenters in this proceeding have not provided sufficient evidence for the Commission to conclude that there are adequate substitutes for UNEs in the interoffice transport market to constrain ILEC market power on the vast majority of point-to-point routes. For example, the UNE Fact Report does not demonstrate that either CLEC self-provisioning or third-party sources offer sufficient alternatives to ILEC UNE interoffice transport to justify removing unbundling obligations. In fact, the UNE Fact Report says nothing about a competitor's impairment on any point-to-point interoffice transport route. It relies heavily on generalized statistics regarding total route miles of competitive fiber deployment and the number of competitive fiber networks deployed in particular geographic markets from which the Commission can draw no conclusions about deployment on particular routes. *See UNE Fact Report 2002 at III-6-8.* Indeed, even the Fact Report acknowledges that it is unable to determine how much of the fiber deployment it cites is actually local instead of long-haul. *See id.* at III-6.

In addition, the Fact Report argues that "fiber-based collocation is now widespread" and that "[i]t is clearly economical for competitors to deploy fiber in an even larger share of wire centers than they currently serve." *Id.* at III-2-3. Yet, the ILEC data merely confirms that there are few wire centers where there are sufficient alternatives to limit the market power ILECs continue to hold over those facilities. For example, according to the Fact Report's own numbers,

a mere seven percent of wire centers in the 25 largest MSAs have four or more fiber based collocators. *See id.* at III-3. But of course, as explained above, even for those wire centers with four or more collocators, this data tells nothing about whether there are sufficient competitors on a particular point-to-point route originating or terminating at that wire center. Again, each fiber could be provisioned for an entirely different route, conceivably leaving each route with only a single alternative, not enough to effectively control the ILEC's behavior through market forces.

Moreover, the Fact Report ignores the market conditions facing many CLECs and competitive interoffice transport providers. Many of the competitive providers cited by the Fact Report have already filed for bankruptcy or are on the brink. The UNE Fact Report, for example, describes the collocation-based business models of a number of CLECs to support their proposition that fiber-based collocation demonstrates that competitors are no longer impaired with respect to interoffice transport. *See id.* at II-2 n.5. What it fails to note is that three of the five CLECs have filed for bankruptcy.⁴⁶ Furthermore, the Fact Report provides a long list of third-party interoffice transport providers, without mentioning that many of these have filed for bankruptcy or have been reported to be in financial trouble. Indeed, it is still to be seen whether wholesale business models are viable at all.⁴⁷ In addition, there are significant risks associated with purchasing transport from third-party providers of transport that could slip into bankruptcy

⁴⁶ See Melanie Austria Farmer, *Winstar Files for Bankruptcy, Sues Lucent*, CNET News.com (Apr. 18, 2001); Sam Ames, *Adelphia Files for Bankruptcy*, CNET News.com (Mar. 27, 2002); *Another Telecom Firm Files for Bankruptcy*, Reuters (Feb. 5, 2002) ("Voice and data communications provider Network Plus on Tuesday became the latest telecommunications company to file for protection under Chapter 11 of the U.S. Bankruptcy Code.").

⁴⁷ See, e.g., Sam Ames, *Metromedia Files for Bankruptcy*, CNET News.com (May 20, 2002); *Dominion Telecom Closes on Purchase of Long-Haul, Metro Fiber Networks from Telergy*, PR Newswire (Apr. 11, 2002) ("Dominion Telecom Inc., an affiliate of Dominion that provides facilities-based broadband services, announced that on April 10 it closed on the purchase of the upstate New York long-haul and metro-fiber network facilities of Telergy Inc., a Syracuse, N.Y., telecommunications provider in liquidation."); Wylie Wong, *Yipes Files for Chapter 11 Bankruptcy*, CNET News.com (Mar. 22, 2002).

at any time. As Allegiance explained in its comments, this means that the financial status of any such third-party provider must be deemed fully stable before it can be considered a provider of substitute transport services. *See* Allegiance Comments at 11.

The CLEC Comments persuasively show that competitors remain impaired without access to unbundled interoffice transport on an overwhelming number of point-to-point routes. Both economic considerations and practical impediments prevent competitors from deploying transport facilities on interoffice routes. First, because interoffice transport facilities connect only two specific points, competitors can expect to achieve the scale necessary to justify the high fixed cost required to self-deploy transport only on a small number of routes. *See* AT&T Comments at 125-31 (public version). ILECs enjoy scale efficiencies and incremental cost advantages that CLECs do not, severely limiting competitors' opportunities to deploy their own fiber efficiently. *See id.* at 135. Without access to unbundled interoffice transport, CLECs would not only be impaired, but would likely be unable to ever build the scale needed to deploy their own transport facilities on all but the highest demand routes.⁴⁸

Moreover, even if economic realities could be overcome, practical obstacles to deployment remain. It is an oversimplification to view the "buy or build" decision based purely on the cost of capacity. Obtaining and using municipal rights-of-way has become an expensive,

⁴⁸ *See* AT&T Comments at 135 (public version) ("As a rule of thumb, a CLEC must have multiple DS-3s of traffic before it will consider extending a fiber facility to an LSO. That is the *minimum* level of traffic necessary to begin contemplating the deployment of a fiber facility comparable in scale to an ILEC's fiber, which, as noted, typically operates at an OC-48 level. But given the small number of customers that most CLECs can expect to serve from a single LSO, there are only a few LSOs that by themselves have sufficient demand to justify a CLEC's construction of alternative fiber transport. *** AT&T currently has special access circuits to approximately 11,500 of the over 14,000 ILEC LSOs. For fully 70% of these LSOs, AT&T has insufficient traffic to fill a *single* DS-3 facility to reasonable levels of utilization to carry its substantial long distance traffic. Most CLECs, of course, do not have the long distance traffic that AT&T does and would therefore have even less ability to self-deploy fiber to any given LSO.") (emphasis in original) (citations omitted).

contentious, and time-consuming procedure that creates a sometimes insurmountable barrier to constructing facilities for already cash-strapped competitors. Meanwhile, an ILEC that needs additional transport has a substantial competitive advantage in that it can light a strand or upgrade electronics as needed on its fiber deployed long ago and paid for by ratepayers in a monopoly market. *See id.* at 142-43. In addition to the well-documented high fees and unreasonable delays associated with municipal construction permits, municipalities impose a wide range of onerous conditions that further burden competitors and often discourage them from deploying facilities at all. Municipalities have imposed such unreasonable conditions as requiring pre-notification of the introduction of new service, requiring most favored community status, demanding free fiber and conduit, regulating service offerings, and imposing unrelated employment provisions.⁴⁹ Some municipalities have even imposed moratoria on new construction, denying any opportunity to build. *See AT&T Comments* at 143-44 (public version). As a result, competitors are impaired as a practical matter on a large number of point-to-point interoffice routes even if the economics could justify deployment.

Next, the Commission should reject the ILEC argument that interoffice transport unbundling obligations should be eliminated where they have been granted pricing flexibility. *See, e.g., Qwest Comments* at 35-36. The Commission clearly held in the *Pricing Flexibility Order* that ILECs remain dominant even after receiving Phase II pricing flexibility. *See Pricing Flexibility Order* ¶ 151. As the Commission has already explained,

⁴⁹ *See Ex Parte* Letter from Traci Bone, Metromedia Fiber Network Services, Inc., *et al.* (on behalf of the Industry Rights-of-Way Working Group), to Magalie Roman Salas, FCC, CC Docket Nos. 98-146, 96-98, and WT Docket No. 99-217, Attachment 2 at 1-4 (filed Jan. 25, 2002).

we recognize that the Commission has established a framework for incumbent LEC pricing flexibility in areas where competition for dedicated transport and most special access services has developed. Competition evidenced by the satisfaction of certain triggers, to the extent they are met, however, does not demonstrate that a requesting carrier is not impaired without access to unbundled dedicated transport. The Commission's pricing flexibility rules provide for flexibility where one requesting carrier is collocated in a serving wire center. These rules allow incumbent LECs to meet competitive transport entry with pricing flexibility. They do not, however, describe market conditions where requesting carriers would not be impaired without access to unbundled transport. Furthermore, even in those areas where competition for special access services is present and where, presumably the triggers for pricing flexibility have been met, the price differentials between TELRIC-priced transport and special access may persist for an indefinite period of time because the differential between unbundled transport and retail special access services are significant.

UNE Remand Order n.673. Pricing flexibility triggers have been set too low to serve as a reasonable basis for concluding that an ILEC is no longer able to exercise market power over the routes in question,⁵⁰ and therefore, the Commission should not consider pricing flexibility as support for the ILECs' assertions that competitors are no longer impaired with respect to interoffice transport facilities where they have been granted pricing flexibility.

Finally, the Commission should reject SBC's argument that its proposed standard discussed above for high-capacity loops should be also used to determine whether transport should be unbundled. *See SBC Comments at 89-93*. There is simply no basis for concluding that ILECs no longer have market power in the provision of transport of DS-3 capacity or above. In order to determine the extent of ILECs' market power in the provision of such services, the

⁵⁰ *See AT&T Comments at 139-40 (public version)* ("The purpose of granting such pricing flexibility was to enable ILECs to lower their access rates to meet lower priced retail service offers from nascent competitors. But the actual market results of this pricing flexibility have been quite the opposite of what was intended. First, *none* of these incumbent LECs has decreased its special access rates in the affected cities.... Second, and most perversely, BellSouth and Verizon have actually *increased* their special access rates, which has resulted in cost increased to AT&T alone of \$25 million and \$24 million, respectively. As a result of these and other exercises of the ILECs' market power, ILEC special access charges are now nearly *twice* their economic costs.") (emphasis in original) (citations omitted).

Commission must examine the actual existence of alternative sources of supply in the marketplace. Only where it has been demonstrated that four or more alternatives exist can the ILECs be deemed to have lost their market power. Moreover, as discussed above with regard to loops, SBC's proposed standard for eliminating UNEs of DS1 capacity should be easily rejected.

C. Signaling

As the comments in this proceeding demonstrate, competitors continue to be impaired without unbundled access to SS7 signaling because they are unable to achieve the scale of the ILECs' ubiquitous SS7 networks through either self-provisioning or third-party providers. The Commission previously concluded that, taking into consideration the availability of alternatives outside the ILEC networks, competitors are impaired without unbundled SS7 "because alternative providers' signaling networks lack the ubiquity of the incumbent LECs' networks, and that larger portions of a requesting carrier's network would likely be affected by a single point of failure on the signaling network." *UNE Remand Order* ¶ 397. Today, competitors and third-party providers are still unable to achieve the scale necessary to create a ubiquitous SS7 alternative that would mitigate the elevated risks of network failures on currently-deployed competitive networks.

While some CLECs have deployed their own SS7 networks, this strategy has often proven to be an inefficient investment and has contributed in part to the subsequent bankruptcies of these carriers.⁵¹ Indeed, market evidence demonstrates that even third-party providers have been unable to aggregate sufficient levels of competitive traffic to achieve the scale needed to

⁵¹ See, e.g., ICG Communications, Press Release, *ICG Communications Files Voluntary Petitions for Chapter 11 Bankruptcy Protection* (Nov. 14, 2000); Time Warner Telecom, Press Release, *Time Warner Telecom Executes Purchase Agreement for GST Assets* (Sep. 11, 2000) (describing the assets of bankrupt GST as including its SS7 networks).

deploy SS7 networks as ubiquitously as the ILECs have.⁵² In contrast, as WorldCom explains, it has been able to deploy its own signaling network, but only because the needed scale was achieved through its long-established long distance business. *See* WorldCom Comments, Decl. of Bernard Ku at 3.

Notably, Illuminet -- the leading independent SS7 network provider that potentially stands to be the largest beneficiary of a decision to remove SS7 from the UNE list -- agrees that SS7 unbundling may well continue to be necessary. *See* Illuminet Comments at 8-9. Indeed, ILEC arguments that their networks are less ubiquitous or that competitive SS7 networks are more ubiquitous than at the time of the *UNE Remand Order* actually prove the case. Even though competitive networks are likely more widespread than they were in 1999, they still cannot provide the redundancy and reliability of a network with large numbers of STP pairs -- ILEC networks. BellSouth, for instance, argues that the Commission based its *UNE Remand Order* decision to unbundle SS7 on the fact that ILECs had at least one STP pair per LATA. In the intervening period, BellSouth explains, it has reduced STP pair deployment by 50 percent, and therefore, the *UNE Remand* reasoning no longer applies. *See* BellSouth Comments at 107. Regardless of LATA boundaries, the large gap between STP pair deployment in independent networks and ILEC networks -- the real basis of the Commission's decision -- remains a critical factor in the reliability and redundancy of a network. For example, even with reduced deployment, BellSouth has approximately 22 STP pairs in its region.⁵³ By contrast, Illuminet,

⁵² *See* WorldCom Comments, Decl. of Bernard Ku at 2-3; Illuminet Comments at 5 (describing Illuminet's network, the largest unaffiliated SS7 network, as including only 14 STP pairs nationwide).

⁵³ Assuming that BellSouth previously maintained only a single STP pair per LATA, it would have had one STP pair for each of its 44 LATAs. After a fifty percent reduction, that would yield at least 22 remaining STP pairs

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the largest independent SS7 provider, has 14 STP pairs to cover the whole nation.⁵⁴ As a result, the Commission should again conclude that larger areas of competitors' networks are at risk from outages on competing SS7 networks, and therefore, competitors continue to be impaired without unbundled access to the ubiquitous ILEC SS7 networks.

IV. THE COMMISSION SHOULD CONTINUE TO REVIEW UNE OBLIGATIONS EVERY THREE YEARS.

The Commission must soundly reject ILEC efforts to escape unbundling obligations through proposals to set a sunset for the UNE rules on a date certain.⁵⁵ The Commission correctly came to the same conclusion in the *UNE Remand Order*. See *UNE Remand Order* ¶ 152. Just as the statute provides no basis for treating newly deployed facilities differently under the impairment standard (as discussed above), the statute provides no basis for sunseting unbundling obligations that currently apply. Again, it would be contrary to the statute for the Commission to sunset unbundling obligations if it has not yet determined that the elements have met the statutory standard for removal from the list. The Commission is obligated to make the determination required by Section 251(d)(2) and may not abdicate its responsibility by setting a date-certain sunset based on some predictive judgment about future competitive conditions. As the Commission has recognized, predictions about future market conditions are inherently unreliable. See *id.* Furthermore, as WorldCom notes, "an automatic sunset date would provide incumbent LECs with an incentive to strategically delay the availability of UNEs until the sunset

for its region. See *CCMI National LATA Map*, Center for Communications Management Information (13th ed., rev. Jan. 2002).

⁵⁴ See Illuminet Comments at 5. Indeed, only eight of Illuminet's STP pairs are owned by Illuminet. The remaining six are obtained through capacity leases. See *id.*

⁵⁵ See Verizon Comments at 70-71 (advocating a three-year sunset); BellSouth Comments at 66 (advocating a two-year sunset of unbundling for POTS loops).

date arrives.” WorldCom Comments at 64-65. Accordingly, the Commission should again reject this proposal.

Instead, the Commission should maintain a cycle of at least three years for review of unbundling obligations. *See UNE Remand Order* ¶ 152. This approach will create needed market certainty for carriers making competitive decisions based on the Commission’s action. In adopting the *Triennial Review*, the Commission emphasized the importance of “a measure of certainty to ensure that new entrants and fledgling competitors can design networks, attract investment capital, and have sufficient time to attempt to implement their business plans.” *Id.* ¶ 150. It remains critical to competition that the obligations come to rest for some period of time in between reviews so that competitors may act based on those obligations. In fact, it is even more critical now as competitors struggle to survive the financial crisis currently strangling much of the competitive telecommunications industry. Moreover, three years is frequent enough to respond to competitive developments that would diminish an ILEC’s reluctantly-relinquished market power over network elements. Finally, any review interval shorter than three years would be administratively burdensome and wasteful of Commission resources insofar as, given the length of time needed for notice and comment proceedings, the Commission would be continually engaged in reviewing the UNE obligations.

V. CONCLUSION

For the reasons described herein and in Allegiance's initial comments, the Commission should adopt unbundled network element rules in accordance with Allegiance's recommendations.

Respectfully submitted,

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