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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

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

In the Matter of:	)	
	)	
Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements	)	WC Docket No. 02-112
	)	
2000 Biennial Regulatory Review Separate Affiliate Requirements of Section 64.1903 Of the Commission's Rules	)	CC Docket No. 00-175

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COMMENTS OF VERIZON[1]

BOCs and independent local exchange carriers providing in-region, interstate, interexchange long distance services on an integrated basis should not be subject to dominant carrier regulation, separate affiliate requirements, or other unique obligations. The long distance market is vigorously competitive, and any such burdens are unnecessary, anticompetitive, and detrimental to consumers. Incumbent local exchange carriers (ILECs) should be treated the same as all other long distance competitors, including traditional interexchange carriers, competitive LECs (CLECs), wireless providers, cable companies, and Information Service Providers (ISPs).

I. SUMMARY

As the *NPRM* recognizes, there have been "significant changes in the competitive landscape" for long distance services over the past several years.[2] For one thing, BOC entry into the interLATA market in 42 states has intensified competition and lowered rates. Even more striking, however, is the substantial shift in usage away from wireline networks toward wireless

[1] The Verizon companies ("Verizon") are the affiliated local and long distance telephone companies of Verizon Communications Inc. These companies are listed in Attachment A.

[2] *Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements, 2000 Biennial Regulatory Review Separate Affiliate Requirements of Section 64.1903 of the Commission's Rules*, Further Notice of Proposed Rulemaking, WC Docket No. 02-112 and CC Docket No. 00-175, FCC 03-111, ¶ 8 (rel. May 19, 2003) ("*NPRM*").

services, e-mail, and instant messaging – all of which are potent substitutes for traditional long distance services and none of which relies heavily (or in some cases, at all) on access services provided by ILECs. As AT&T itself has told its investors, "the rapid expansion of usage of wireless and e-mail services has contributed to an overall decline in traffic volume on traditional wireline networks." In fact, based on a very conservative estimate, wireless long distance now accounts for almost *one-third* of all long distance minutes – the most relevant measure of long distance calling habits, since it directly accounts for usage (in a way that presubscribed lines does not). And e-mail and IM likely replace (again, using very conservative assumptions) roughly one-third of voice traffic that otherwise would flow over the public network, including a very significant portion of long distance minutes.[3]

Regulators should not intervene in such a competitive market. In particular, the Commission should resist calls to impose on ILECs the burdensome tariffing and cost support requirements inherent in dominant carrier regulation (let alone even more burdensome separation requirements under Section 272 of the Act or Section 64.1903 of the Rules). As the Commission has recognized, "regulations associated with dominant carrier regulation can … stifle price competition and marketing innovation when applied to a competitive industry."[4] Such regulation would "adversely affect competition" by "discourag[ing] the introduction of innovative service offerings," would "prevent consumers from enjoying lower prices resulting from real efficiencies," and would "encourage … interLATA competitors to challenge the [ILECs'] interLATA rates in order to impede [their] ability to compete." *LEC Classification Order*, ¶¶ 89-90.

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[3] The basis for these statistics is presented in Section II, *infra*.

[4] *Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area*, 12 FCC Rcd 15756, 15806 (1997) ("*LEC Classification Order*").

The Commission's last concern is particularly perceptive: dominant carrier regulation traditionally has been used to ensure that rates are not excessive – a measure of government intervention that is patently unnecessary in the competitive long distance market. Here, however, dominant carrier regulation would be employed by the ILECs' long distance competitors to enlist the Commission's aid in assuring that rates are not "too low" – that is, to prevent consumers from enjoying the natural rewards of a vigorously competitive market. Plainly, "[i]f tariffs or price caps were to deter firms from reducing prices … there would be obvious anticompetitive consequences of discouraging legitimate price competition." Declaration of Dennis W. Carlton, Hal S. Sider, and Allan L. Shampine, Attachment B hereto ("Carlton/Sider/Shampine Decl."), ¶ 77.

With this caution in mind, the issue here is narrow: in the absence of separation requirements, is it necessary to restrain competition in order to save it? The answer, beyond any reasonable dispute, is no. No ILEC can leverage its control of local exchange and exchange access facilities to gain market power in the long distance market, whether or not it offers such services through a separate affiliate. *First*, ILECs have provided a plethora of competitive services on an integrated basis for years with no evidence that they have ever sought to engage in such strategies, let alone been successful. It would be arbitrary in the extreme to impose dominant carrier regulation here based on speculation that is belied by the facts on the ground. *Second*, to succeed in an attempted predation, price squeeze, or discrimination scheme, an ILEC would have to drive from the marketplace the incumbent national IXCs, dozens of regional facilities-based long distance carriers, hundreds of resellers, five unaffiliated nationwide wireless providers, and the major ISPs. Moreover, having done so, it would have to prevent potential entrants from making use of the massive available capacity. And, it would have to accomplish

all this while somehow stopping its customers and competitors from substituting local exchange and access services provided by the multitude of new competitors that have entered those markets. This is ludicrous. *Third*, in what must be considered belt, suspenders, and an elastic waistband, there are a multitude of regulatory and statutory obligations that deter or prohibit price manipulation and discrimination and punish any ILEC foolish enough to try it.

Nor can ILECs be considered dominant under the factors comprising the Commission's traditional market power analysis. Demand and supply substitutability are high, no ILEC's market share is within an order of magnitude of AT&T's share when it was declared non-dominant, and the ILECs enjoy no cost structure or size advantage over competitors such as AT&T, Sprint, a nearly debt-free WorldCom, the major wireless operators, and Internet goliaths such as Microsoft, IBM, Yahoo!, and AOL Time Warner. Dominant carrier regulation therefore is inimical to fair competition and entirely unwarranted.

II. THE INTEREXCHANGE MARKET IS DYNAMIC, VIGOROUSLY COMPETITIVE, AND IMMUNE TO EFFORTS BY ANY COMPETITOR TO ACQUIRE AND EXERCISE MARKET POWER.

The *NPRM* properly recognizes that the Commission's actions in this proceeding "must be guided by a full understanding of the existing market dynamics" for in-region, interstate, interexchange services. *NPRM*, ¶ 8. Put another way, any market analysis must include "all firms whose participation in provision of a service significantly constrains the price under analysis." Carlton/Sider/Shampine Decl., ¶ 14.

As the Commission's *Long Distance Report* recently noted, "long distance service" now encompasses far more than traditional interexchange carrier services:

> Historically, this report has tracked data for wireline long distance. One of the challenges for the future will be to track developments in an evolving marketplace, where carriers (such as wireline, wireless and cable) are offering consumers bundled packages of local and long distance service, and buckets of minutes that can be used to call anyone,

anywhere, and anytime. *Statistics of the Long Distance Telecommunications Industry*, 2 (May 2003) ("*Long Distance Report*").

Simply put, as a result of wireless substitution, an explosion of instant messaging ("IM") and e-mail traffic, and BOC entry into the interLATA market in the vast majority of states, competition in the provision of long distance services has intensified well beyond the point where concerns about the exercise of market power by any competitor are even remotely tenable.

The dramatic impact of cross-platform competition on wireline long distance – that is, the substitutability of wireless and Internet-based services for traditional landline toll calls – is illustrated by the fact that wireline toll minutes are plummeting. According to the Commission's statistics, the average number of monthly residential toll call minutes fell from 147 (in 1997) to 90 last year. *Long Distance Report*, Table 20. Similarly, one analyst just reported that "the average [monthly] long-distance usage per household has declined from 180 minutes to 100 minutes due to wireless and e-mail substitution ...."[5] CIBC World Markets, "Opportunities for Flat Rate Pricing and Bundling," June 26, 2003, at 3.

Plainly, customers have not cut back on their total long distance communications. Rather, as CIBC concluded, and as AT&T recently told investors and the SEC, "the rapid expansion of usage of wireless and e-mail services has contributed to an overall decline in traffic volume on traditional wireline networks." AT&T Corp. SEC Form 10-K, at 17 (filed Mar. 28, 2003).[6] In fact, analysts estimate that 70 percent of the $3.5 billion decline in AT&T's consumer

[5] Indeed, not only are consumers making fewer wireline long distance calls, but call durations have been getting shorter. Carlton/Sider/Shampine Decl., ¶ 33 (citing a Merrill Lynch report).

[6] More specifically, AT&T's "[c]alling volumes declined at a low-teen percentage rate in 2002, and a low double-digit percentage rate in 2001 as a result of competition and wireless and Internet substitution." *Id.* at 39.

long distance revenues between 2001 and 2002 was due to wireless and Internet substitution. Carlton/Sider/Shampine Decl., ¶ 34 (citing a Lehman Brother report).

As AT&T's experience shows, wireless long distance services are direct substitutes for traditional wireline toll services.[7] In fact, using very conservative assumptions, wireless calls account for almost one-third of all long distance minutes,[8] and that percentage has been increasing rapidly. This is hardly surprising, since wireless calling plans routinely include free nationwide long distance and a bucket of minutes, encouraging customers to replace their wireline long distance usage with wireless phone usage.[9] ***See*** *Seventh CMRS Competition Report*, 17 FCC Rcd 12985, 13014, 13018 (2002).

Wireless substitution, moreover, is not just a mass market phenomenon. The nationwide carriers are aggressively marketing their "free long distance" calling plans to businesses,[10] and

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[7] The *NPRM* (at ¶ 28) asks "how [the Commission] should factor the BOCs' and independent LECs' interests in their respective mobile telephony operations into [its] analysis." There is no reason to do so. First, in virtually every in-region market, there will be five nationwide wireless carriers that are unaffiliated with the ILEC – in Verizon's region, for example, AT&T Wireless, Sprint PCS, Nextel, Cingular, and VoiceStream all compete to provide wireless services. Second, given the intense competition in the provision of CMRS services, a BOC's affiliated wireless carrier cannot afford to pull its competitive punches in-region. Third, the majority of wireless all-distance plans are the same nationwide, so that Verizon Wireless goes after long distance usage in Verizon's region as aggressively as it does elsewhere in the country.

[8] Carlton/Sider/Shampine Decl., ¶ 31.

[9] An IDC survey estimates that one-third of wireless calls are long distance. ***See*** Dana Thorat, IDC, *Soaring Wireline Displacement and Highest Interest in Location-Based Services: U.S. Wireless Household Survey Results*, at 7 (2002).

[10] All of the major wireless carriers advertise business calling plans with "free nationwide long distance" or "no long distance charges." For example, Nextel promotes business calling plans with "Free Nationwide Long Distance, ***see*** http://www.nextel.com/phones_plans/promos/promo_free_incoming.shtml?id1=bb2&id2=free_incoming&id3=home. Cingular's "business solutions" include its Cingular Nation plan, with which the carrier advertises the ability to "pay the same low rate for all of your calls, with no roaming or nationwide long distance charges." ***see*** http://www.cingular.com/business/calling_plans. Verizon Wireless likewise markets the ability for its small/medium and enterprise business customers to call "with no long distance charges."

industry analysts have concluded that, for enterprise customers, "when the budgetary constraints are lifted, the primary areas of incremental spend will likely be more in wireless than in wireline capabilities." Morgan Stanley, *Wireline Telecom Services, Ice Age II: The Return of the Scenario Analysis*, May 12, 2003, at 17. Similarly, the near-ubiquity of Blackberry devices, Palm-powered devices, and similar equipment permitting users to send and retrieve messages from anywhere at any time inevitably replaces a significant portion of landline business long distance voice and data traffic.

Internet-based services such as e-mail, instant messaging, and voice over IP are another major source of competition for traditional landline long distance voice services. ***See*** *Sizing U.S. Consumer Telecom*, The Forrester Report, at 19 n.5 (Jan. 2002) ("[a]lternate forms of communication, such as email and instant messaging, [] reduce long-distance minutes of use."). The extent of this substitution, while difficult to measure precisely, is staggering:

> consumers in the U.S. are sending approximately 3.2 billion e-mail messages and approximately 1 billion IM messages per day. If only 10 percent of the 4.2 billion daily e-mail and instant messages substitute for a voice call, that is equivalent to about 750 billion minutes per year, or roughly one-third of all voice traffic that passes through ILEC networks. 2002 UNE Fact Report 2002, at I-10 (attached to Verizon's comments in CC Docket No. 01-338, filed April 5, 2002).

And, as with wireless, the use of e-mail and IM to replace landline long distance calling it not limited to mass market consumers. E-mail is ubiquitous in the business world, and it is routinely used as a direct substitute for long distance (as well as local) calling. Instant messaging – which has been a mammoth success among residential customers and indisputably replaces long distance (as well as local) calling – also is taking hold in the enterprise market. Indeed,

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(Continued . . .)
See http://www.verizonwireless.com/jsp/business_svcs/sm_md_business.jsp; http://www.verizonwireless.com/jsp/business_svcs/enterprise.jsp.

IBM, Oracle, Sun MicroSystems, Microsoft, AOL Time Warner, and Yahoo! are aggressively promoting the use of IM in business applications.

Yahoo!, for example, markets Yahoo! Messenger Enterprise Edition by noting that "employees can instantly identify who is online and exchange information in order to get answers, share ideas and collaborate on projects" – "[t]hey can connect across departments, companies, networks, *and geographies*." And Yahoo! expressly touts that this service enables companies to "reduce ... phone and network costs, such as storage and bandwidth." ***See*** http://enterprise.yahoo.com/products/msg (emphasis added).[11] For its part, Microsoft just announced that it will unveil a new integrated IM/telephony/video conferencing server software package this summer. Not only will this package offer a powerful enterprise IM tool, but it will include "Session Initiation Protocol" (SIP), which "allows many different forms of real-time data exchange, such as [VOIP] voice calls, video conferences, and instant messaging to interact with one another." Jim Hu, "Is Ma Microsoft Calling?," http://news.com.com/2102-1037_3-1-16355.html?tag=ni_print (June 12, 2003) (listing IBM's Lotus SameTime product as the market leader and noting that Sun, Oracle, AOL Time Warner, and Yahoo! all compete against Microsoft in offering integrated enterprise IM/telephony applications).

Likewise, e-commerce (*e.g.*, placing orders on a business's web site) is replacing 800 traffic. ***See*** *AT&T Corp.*, Jefferies Telecom Services Group, at 2 (June 13, 2003). For example, for some industries that historically have been heavy users of toll-free inbound calling services, such as airlines and hotels, the use of both owned and third-party Internet-based reservation services (such as Orbitz and Travelocity) is causing a sharp decline in 800 usage. In the same

[11] Yahoo! references a study showing that 65 million people use IM at work, and that this number is expected to grow to 250 million by 2005. http://enterprise.yahoo.com/pdf/ymee.pdf. ***See also*** Christopher Saunders, "Yahoo! IM Expands Conferencing," www.instantmessagingplanet.com/enterprise/article.php/2220541 (June 11, 2003).

vein, catalogue companies such as LL Bean, which traditionally have been intensive users of 800 services, are encouraging people to order on-line at the companies' web sites, dramatically reducing both 800 traffic and telecommunications costs.

Cable telephony is yet another direct substitute for traditional interexchange service. The Commission's most recent *Local Competition Report* indicates that there are now approximately three million cable telephony subscribers nationwide, and the service is available to 14 million households. ***See*** *Local Telephone Competition: Status as of December 31, 2002* (Industry Analysis and Technology Division, June 2003), at 2 ("*Local Competition Report*"); Merrill Lynch, "Voice over Broadband: The Challenge from VOIP in the Residential Phone Market," Appendix B, Table 9A (June 24, 2003). And cable modem service – which is now available to 85 million households and has garnered 12 million subscribers – continues to enjoy an almost two-to-one lead over DSL services. ***See*** http://www.ncta.com/industry_overview/indStat.cfm?indOverviewID=2; *High-Speed Services for Internet Access: Status as of December 31, 2002* (Industry Analysis and Technology Division, June 2003) at 2 (6.5 million ADSL subscribers as of year-end 2002). Both residential and business customers use cable modem service to send and receive e-mails and IM, to engage in electronic commerce, and increasingly, to transmit VOIP calls. In fact, a recent survey of 300 Chief Technical Officers found that 13 percent of medium-sized enterprises (50-249 employees) and 19 percent of large enterprises (more than 250 employees) use cable modem service for at least some portion of their data communications. *Annual Telecom Services Survey Part 3: Competition* (Morgan Stanley June 17, 2003), Exhibit 24 ("*Telecom Competition Survey*").

Even looking just at the provision of traditional wireline long distance service, the Commission's most recent statistics reveal that there are more than *one thousand* toll carriers

today – a number that has increased by more than 50 percent since 1999, notwithstanding a stagnant economy, a reeling telecommunications industry, and the BOCs' entry into the market. *Long Distance Report*, Table 4. These entities include numerous facilities-based IXCs – with AT&T and WorldCom remaining far and away the largest – hundreds of resellers, the long distance affiliates of BOCs and independent LECs, and dozens of niche players such as prepaid calling card providers.

Finally, and not surprisingly, given the intensity of competition in the market, rates have been declining significantly for several years. For domestic calls, the average revenue per minute declined from 11 cents to 9 cents between 1999 and 2000 and from 9 cents to 8 cents between 2000 and 2001 (the latest year for which the Commission has released information). Id., Table 5. By all accounts, rates are continuing to decline for all categories of users.[12]

* * *

Given the dynamic nature of the long distance market, a focus on traditional, wireline interexchange services is indefensibly narrow. Nonetheless, whatever market definition the Commission uses, the sheer number and variety of entrenched competitors and the intensity of competition preclude any argument that an ILEC could exercise market power. Indeed, that conclusion would hold true even in the absence of *any* regulatory safeguards.

No further inquiry should be necessary to find that the ILECs cannot restrain long distance competition. Even so, the next section of these comments applies the relevant analytical framework to the facts at hand, and demonstrates the ILECs' non-dominance beyond any reasonable dispute.

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[12] One recent study indicates that consumer rates are approaching the 4-5 cents-per-minute range and that rates for small and medium-sized business customers also are close to 4 cents per minute. *Telecom: Three Year View* (Lehman Brothers, June 17, 2003) at 8, 17 ("*Telecom: Three Year View*").

III. ILECS ARE NON-DOMINANT IN THE PROVISION OF INTEREXCHANGE SERVICE ON AN UNSEPARATED BASIS.

The Commission has stated that "dominant carrier regulation should be imposed on a carrier only if it could unilaterally raise and sustain prices above competitive levels and thereby exercise market power by restricting its output or by its control of an essential input." *NPRM*, ¶ 5 (footnotes omitted). Under neither theory – control of an essential input or restriction of output – could an ILEC providing long distance service on an integrated basis even arguably exercise market power.

A. ILECs Have No Ability To Raise Rivals' Costs or Restrict Output Through Control of an Essential Input To Long Distance Service.

The *NPRM* asks whether ILECs could "leverage market power from their local exchange and exchange access markets into the markets for interstate and international interexchange services." *NPRM*, ¶ 29. Years of experience, the growth of local exchange and exchange access competition, and the existence of effective non-structural safeguards demonstrate that this concern is unfounded.

1. History confirms that ILECs are unable to gain market share in downstream markets by "leveraging" control over essential facilities.

Local exchange and exchange access services and facilities are inputs into a wide range of competitive downstream services and products: interLATA telecommunications services, intraLATA toll services, interLATA "corridor" services, interLATA and intraLATA information services, wireless services, customer premise equipment ("CPE"), and inside wire, to name the most obvious examples. In virtually every case (except for the non-corridor, interLATA telecommunications services at issue here), ILECs can provide the downstream service or product on an integrated basis, and without being saddled by dominant carrier regulation. (Indeed, many of the downstream markets involve non-Title II services that could not be subject

to such regulation in any event.) And, as discussed below, in every case, not only has there been no evidence of "leveraging" of market power, but competition in the downstream market has thrived.

Because the theoretical risk of predatory pricing, price squeezes, and discrimination is the same for in-region long distance services as for these other products and services, there is overwhelming evidence that ILECs will not be able to exercise market power in the long distance market when providing that service on an integrated basis. In the face of this evidence, the Commission must find that dominant carrier regulation is unwarranted. A contrary conclusion unquestionably would be arbitrary. ***See*** *Illinois Pub. Telecomm. Ass'n v. FCC*, 117 F.3d 555, 564 (D.C. Cir. 1997) ("The FCC's *ipse dixit* conclusion, coupled with its failure to respond to contrary arguments resting on solid data, epitomizes arbitrary and capricious decisionmaking"); *Alltel Corp. v. FCC*, 838 F.2d 551, 561 (D.C. Cir. 1988) ("'a regulation perfectly reasonable and appropriate in the face of a given problem may be highly capricious if that problem does not exist'").

IntraLATA toll. Providing an exact parallel for the issues at stake in this proceeding, ILECs have always provided intraLATA toll service on an unseparated basis, yet competition in that market is robust. At divestiture, the BOCs had a 100 percent market share (as did the independent telcos in their territories). By 1995, even in the absence of dialing parity, IXCs had taken more than 20 percent of the market. ***See*** Declaration of Timothy J. Tardiff at 6, attached to Reply Comments of Verizon, CC Docket No. 96-149, filed Sept. 24, 2002. And, following full implementation of intraLATA toll dialing parity in early 1999, the RBOCs' collective market share has fallen dramatically to 38.8 percent of residential minutes (and an undoubtedly smaller, but unreported, share of business minutes). ***See*** *Long Distance Report*, at 4 & Table 16. The

rapid growth of vigorous competition in this market is even more striking given that IXCs initially depended heavily on ILEC facilities for access to subscribers, competed against inexpensive local calling within the LATA, and had to educate subscribers that they had a choice of providers. Tardiff Decl. at 5-6. Plainly, if ILECs had the incentive and ability to "leverage" control of bottleneck facilities to prevent competition, they would have been far better able to do so in the intraLATA toll market (where they started with a 100 percent market share) than in the interLATA market (where they started with a zero percent share).[13]

InterLATA corridor services. As further confirmation that the ILECs cannot leverage their control of exchange and exchange access facilities, the BOCs have provided interLATA services in certain "corridor" areas (such as between Northern New Jersey and New York, or between Camden and Philadelphia) on an integrated basis for years with no harm to competition. In fact, competition in this market is so robust that the FCC removed these services from price cap regulation in 1999. *Access Charge Reform*, Fifth Report and Order and Further Notice of Proposed Rulemaking, 14 FCC Rcd 14221, ¶ 56 (1999). In doing so, the Commission found that "price cap LECs may now be non-dominant in the provision of corridor and interstate intraLATA toll services" and that "developments in the markets for interexchange services make it unlikely that price cap LECs will be able to exploit over a sustained period any individual market power in their provision of corridor and interstate interLATA toll services." Id. ¶ 53.[14] The same must hold true here.

[13] Notably, in the significant majority of Verizon states, intraLATA toll services are considered competitive and thus not subject to cost support or lengthy advance notice requirements.

[14] The Commission did not make a non-dominance finding because it found the record was insufficient to conduct the requisite analysis. Id. ¶ 53.

InterLATA information services. InterLATA information services depend on the same access facilities, services, and processes as interLATA telecommunications services. Consequently, if ILECs had the ability to leverage market power to restrain long distance competition, they would have the same ability to restrain competition in the provision of interLATA information services. Three years ago, however, the Commission permitted the Section 272 separate affiliate requirements to sunset for interLATA information services, explicitly finding that the numerous other non-structural safeguards in the Act are sufficient to prevent any exercise of market power by ILECs in the in-region, interLATA information services market. ***See*** *Request for Extension of the Sunset Date of the Structural, Nondiscrimination, and Other Behavioral Safeguards Governing Bell Operating Company Provision of In-Region, InterLATA Information Services*, 15 FCC Rcd 3267, ¶ 3 (2000).[15] The same conclusion is required in this proceeding because the supposed opportunities to acquire and exercise market power are identical.

IntraLATA information services. In theory, ILECs have just as much incentive and ability to engage in predatory pricing or to discriminate against competitors in the provision of intraLATA information services as they do in the provision of interLATA telecommunications services. Yet, ever since the 1986 *Computer III* decision, the BOCs have provided intraLATA information services pursuant to non-structural safeguards (which do not include "dominant carrier"-type regulation of these non-Title II offerings) – and in the intervening 17 years, competition in the downstream market has thrived and consumers have enjoyed an explosion of innovative services at ever-declining rates. The BOCs, moreover, have hardly come to dominate

[15] In fact, interLATA information services are subject to even fewer safeguards than interLATA telecommunications services, since the information services themselves are not subject to Sections 201 and 202.

the market. For example, they hold a collective share of just over 15 percent of revenues for voice messaging services (one of the most popular intraLATA information services) and are essentially non-players in the provision of dial-up Internet access. ***See*** Tardiff Decl. at 8.

Wireless services. On January 1, 2002, the Commission permitted the rule requiring ILECs to offer CMRS services through a separate affiliate (47 C.F.R. 20.20(f)) to sunset. In imposing the separation requirement five years earlier, the Commission stated that it would allow the rule to sunset unless it determined that "competitive conditions in the local exchange market are such that continuation of these safeguards is in the public interest." *Amendment of the Commission's Rules to Establish Competitive Service Safeguards for Local Exchange Carrier Provision of Commercial Mobile Radio Services*, 12 FCC Rcd 15668, ¶ 99 (1997) ("*LEC-CMRS Safeguards Order*"). CMRS carriers, like long distance carriers, must interconnect with the ILECs' networks, so the same theoretical opportunities to manipulate price and discriminate against competitors arise in the CMRS context. Yet there has been no allegation, let alone any finding, that ILECs have discriminated in favor of their CMRS operations in the eighteen months since sunset of the separate affiliate requirement. The Commission's refusal to extend the separate affiliate requirement (let alone to impose dominant carrier regulation on the ILECs' CMRS services), coupled with marketplace experience, thus further compels a finding of non-dominance with respect to integrated, in-region, landline long distance services.[16]

[16] Other examples abound: The BOCs have provided CPE on an unseparated basis for nearly 20 years, with no ill effect on competition. Notwithstanding the theoretical ability to cross-subsidize, engage in predatory pricing, and discriminate, the BOCs are minor players in the CPE market. Likewise, ILECs always have provided inside wire installation and maintenance on an integrated basis, and that market is vigorously competitive as well. Similarly, ILECs have been losing payphone market share for years, even though they began with almost complete control of the payphone market. If ILECs were able to exert market power through their control of local bottleneck facilities, they should have been able to prevent competitors from gaining any share of these markets.

2. Competition in the exchange and exchange access markets provides further assurance against leveraging.

Even if concerns about leveraging of control over local exchange and exchange access facilities into competitive markets had any merit in 1997, when the *LEC Classification Order* was adopted (which they did not), they undeniably lack foundation today, given the tremendous growth in both local and access competition over the past six years. Any effort by an ILEC to shift costs to its local customers, manipulate access prices, or engage in discrimination would be met with a swift and effective penalty imposed by the marketplace, as customers would desert the ILEC in favor of other suppliers. ***See*** *NPRM*, ¶ 29.

Looking first at the local market, in 1997, the Commission found that BOCs earned approximately 99.1 percent of local exchange service revenues. Today, the competitive picture is dramatically different. ILEC switched access lines have declined from 181 million in December 1999, to 162 million in December 2002. ***See*** *Local Competition Report*, Table 1. During the same period, CLEC end user lines more than tripled, from 8 million to 25 million. Id. In 2002, CLECs served 13.2 percent of local exchange lines, compared to 10.3 percent a year earlier. Public Notice, *Federal Communications Commission Releases Data on Local Telephone Competition*, June 12, 2003, at 1. Many of these customers are served using the CLECs' own facilities, in whole or in part. This is true even in the residential market, where cable telephony providers serve three million lines over their own facilities (and the service is available to almost five times that many households),[17] numerous CLECs have overbuilt existing ILEC networks and wired new developments, and many others have deployed their own switches and leased

[17] One industry analyst just predicted that cable telephony will capture 15-20 percent of the residential local phone market within the next five years. Fulcrum Global Partners, "Wireline Communications: We Believe the Industry Is Sick – Regulation is Making it Sicker," May 16, 2003, at 4.

loops from the ILEC. For purposes of the instant proceeding, however, the means through which the CLECs provide service is irrelevant. All CLECs provide competitive discipline against efforts by an ILEC to increase local rates in order to subsidize long distance service (assuming, contrary to fact, that any rational ILEC would try such a strategy).

Moreover, these numbers do not even include competition from wireless services, which have siphoned untold billions of minutes off the wireline network, replaced wireline service entirely for an estimated 3-5 percent of customers, and displaced at least ten million second phone lines. ***See*** *2002 UNE Fact Report*, sections II.C, IV.B.2. Nor do they include competition from instant messaging and e-mail, which likewise take billions of minutes from the ILECs' switched networks. Such inter-modal competition provides a further check against misguided efforts to shift costs.

Competition in the access market is even better established than in the local exchange market. ***See*** *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, Supplemental Order Clarification, 15 FCC Rcd 9587, ¶ 18 (2000) ("Competitive access, which originated in the mid-1980s, is a mature source of competition in telecommunications."). Every provider of local service is a competitive provider of switched access, whether it uses its own facilities, third-party alternatives, or UNEs.

Moreover, there has been an explosion of alternative special access capacity just in the last four years. Competitive fiber networks have grown more than 80 percent—from approximately 100,000 route miles to at least 184,000 route miles—and most of this fiber is local rather than long-haul. ***See*** Competition for Special Access Services, at 1, attached to Opposition of Verizon, RM 10593 (filed Dec. 2, 2002) ("*2002 Special Access Report*"). During the same period, the number of competitive networks in the 150 largest MSAs, which contain nearly 70

percent of the U.S. population, has grown by more than 60 percent, from approximately 1,100 to nearly 1,800. Id. With these facilities, competitive carriers are gaining a significant share of the revenues from special access. In 2001, competing carriers earned approximately $10 billion in special access and private line revenues – more one-third of all special access revenues. Id. at 2. In Verizon's territory, competitive access providers have established 7,000 collocation facilities in wire centers serving 78 percent of Verizon's access lines. Indeed, competition is so pervasive in the special access market that, under the Commission's competition-based triggers, Verizon has received pricing flexibility in MSAs accounting for roughly two-thirds of its interstate special access revenues, with MSAs accounting for more than half of those revenues subject to Phase II pricing flexibility. ***See*** AT&T Opposition to Verizon Petition for Pricing Flexibility, WCB-Pricing 02-33, filed Dec. 30, 2002, Declaration of Charles E. Stock, ¶ 2 (63 percent of Verizon's special access revenues derive from MSAs subject to Phase II pricing flexibility). This competition assures that no ILEC could price access at uneconomic levels or discriminate in the provision of access services.

3. Existing non-structural safeguards short of dominant carrier regulation assure against speculative risks of anticompetitive pricing and unreasonable discrimination.

a. Pricing issues

The *NPRM* (at ¶¶ 29-30) asks whether ILECs could engage in predatory pricing (by misallocating costs to their local exchange or access services) or place competitors in a price squeeze (by raising access charges). For good reasons, however, the Commission already has dismissed such concerns, both as a matter of practicality (given the existence of entrenched competitors in the interexchange market) and because of the existence of various regulatory and statutory safeguards (principally, price cap regulation). ***See*** *LEC Classification Order*, ¶¶ 107 ("even if a BOC were able to allocate improperly the costs of its affiliate's interLATA services,

we conclude that it is unlikely that a BOC interLATA affiliate could engage successfully in predation"), 129 ("a price squeeze strategy would give a BOC interLATA affiliate the ability to raise price by restricting its own output only if it is able to drive competitors from the market," which is "unlikely"). Indeed, as the Commission noted, the Supreme Court has recognized that "predatory pricing schemes are rarely tried, and even more rarely successful." Id. n.293 (***quoting*** *Matsushita Elec. Ind. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 589 (1986)). This is particularly true in an industry such as telecommunications, where "[m]uch industry investment consists of fixed assets" that will "remain available to a new entrant, even if existing long distance companies are driven from the market." Carlton/Sider/Shampine Decl., ¶ 55.

The elimination of separate affiliate requirements does not make a successful predation or price squeeze strategy any more realistic. Even apart from the evident futility of trying such a scheme (given robust and inter-modal interexchange, local exchange, and exchange access competition and the continued availability of competitive assets even if individual competitors exit the market), the Commission consistently has found that price cap regulation "reduces the BOCs' incentive to allocate improperly the costs of their affiliates' interLATA services." *LEC Classification Order*, ¶ 106; ***see*** id. ¶ 126 ("price cap regulation of the BOCs' access services sufficiently constrains a BOC's ability to raise access prices to such an extent that the BOC affiliate would gain, upon entry or soon thereafter, the ability to raise prices of interLATA services above competitive levels"). The deterrence effect of price cap regulation is equally strong regardless of whether an ILEC provides interLATA services through a separate affiliate: "[i]f shifting costs from long distance to local operations does not enable firms to generate higher revenue through higher prices of regulated services, there is no incentive to do so," whatever the corporate structure. Carlton/Sider/Shampine Decl., ¶ 64.

In fact, the effectiveness of price cap regulation in preventing cost-shifting is even stronger than in 1997, now that (1) sharing obligations have been eliminated (removing any theoretical incentive to shift costs in order not to reach the sharing thresholds) and (2) implementation of the CALLS plan has sharply reduced switched access rates. ***See*** *Local Competition Order*, ¶ 126 ("[t]o the extent that access charges are reformed to more closely reflect economic cost ... the potential for a price squeeze should be further mitigated"); Carlton/Sider/Shampine Decl., ¶ 65 (noting that CALLS has reduced large ILECs' access charges to $.0055 per minute).

All large ILECs are subject to price cap regulation of their interstate access services (except for those that have been effectively deregulated due to the existence of sufficient competition to satisfy the Commission's judicially-endorsed triggers). In addition, the large ILECs generally are subject to price cap or other forms of non-cost based regulation for their intrastate exchange and exchange access services.[18] Price cap regulation accordingly fully addresses any residual concerns about anticompetitive pricing – and, it is backstopped by the Commission's continued reliance on imputation of access charges, which further assures against attempted predation. Finally, a competitor that believes a particular rate for an interLATA service is unreasonably low or discriminatory can present its claims in a complaint alleging violations of Sections 201 and 202 of the Act. ***See*** *LEC Classification Order*, ¶ 128. This holds true whether the services are provided by the ILEC itself or by an affiliate.

b. Discrimination

The *NPRM* (¶ 31) also asks whether ILECs providing long distance service on an integrated basis could discriminate against their rivals. Such a prospect is, if anything, even

[18] For example, 91 percent of Verizon's access lines are subject to non-rate base regulation.

more remote than the risk of predatory pricing or a price squeeze. After all, not only do the same marketplace factors preclude such conduct, but any such discrimination would have to be effective enough to enable an ILEC to "gain the ability to raise prices by restricting its own output," *LEC Classification Order*, ¶ 111, yet subtle enough to escape the notice of competitors and regulators.[19] Nonetheless, should any ILEC try to discriminate in a way that violates Sections 202(a) and 251, it would be punished either at the FCC or in court pursuant to Sections 206-209 of the Act, further deterring any attempt to acquire and exercise market power in the long distance market.

Finally, with respect to the BOCs, Section 272(e)(1) bars non-price discrimination,[20] and Section 272(e)(3) bars price discrimination.[21] These provisions thus establish additional bases to sanction attempted discrimination.

B. ILECs Are Non-Dominant Under the Analysis Used in the *AT&T Non-Dominance Order*.

The restriction-of-output prong of the non-dominance inquiry focuses on four factors identified in the *AT&T Non-Dominance Order*: supply substitutability, demand substitutability, market share, and cost structure and size.[22] In the *LEC Classification Order*, the Commission

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[19] ***See also*** Carlton/Sider/Shampine Decl., ¶ 47 ("In order for discrimination to succeed, it must be effective enough to cause customers to switch to ILEC long distance services ... but ... must avoid detection by regulators and sophisticated rivals, such as AT&T, Sprint and MCI. These firms operate nationally and thus have numerous benchmarks available to evaluate whether an individual ILEC is engaging in non-price discrimination.").

[20] Under Section 272(e)(1), a BOC must "fulfill any requests from an unaffiliated entity for telephone exchange service and exchange access within a period no longer than the period in which it provides such [service] to itself."

[21] Section 272(e)(3) requires that, in the absence of a separate affiliate, a BOC "impute to itself ... an amount for access ... that is no less than the amount charged to any unaffiliated interexchange carriers for such service."

[22] *Motion of AT&T Corp. To Be Reclassified as a Non-Dominant Carrier*, 11 FCC Rcd 3271 (1996) ("*AT&T Non-Dominance Order*"); ***see*** *NPRM*, ¶ 27 ("In assessing the first type of market power, the Commission traditionally has focused on certain well-established market features,

found that "each of the traditional market factors ... supports a conclusion" that the ILECs' separate long distance affiliates "will not have the ability to raise price by restricting their output ...." *LEC Classification Order*, ¶¶ 96-97 (BOCs' affiliates), 157 (independent LECs' affiliates).

The elimination of separate affiliate requirements does not alter this conclusion. To the contrary, the Commission's finding in this regard was based solely on its consideration of structural factors in the long distance market; the provision of service through a separate affiliate was irrelevant to its analysis. ***See*** id.

1. Supply substitutability

In assessing supply substitutability, the Commission considers whether alternative suppliers have sufficient capacity to handle increased demand and whether there are significant barriers to entry. *AT&T Non-Dominance Order*, ¶ 57. In the *LEC Classification Order*, the Commission found that "AT&T and its competitors, which currently serve all interLATA customers, should be able to expand their capacity sufficiently to attract a BOC interLATA affiliate's customers if the affiliate attempts to raise its interLATA prices." *LEC Classification Order*, ¶ 97; ***see also*** id., ¶ 157 ("the same high supply and demand elasticities that the Commission found constrained AT&T's pricing behavior also apply to independent LECs").

Today, supply substitutability is even higher than at the time of the 1997 *LEC Classification Order*.[23] As the Commission is well aware, there is tremendous excess capacity in

(Continued . . .)
including market share, supply and demand substitutability, the cost structure, size, and resources of the firm.").

[23] Supply substitutability certainly is greater than in 1995, when AT&T was declared non-dominant. At that time, the Commission found that MCI and Sprint could "absorb overnight as much as fifteen percent" of AT&T's total switched demand and, within ninety days, "using their existing equipment, could absorb almost one-third of AT&T's total switched capacity." *AT&T Non-Dominance Order*, ¶ 59. Here, competitors likely could "absorb overnight" *all* of the ILECs' long distance demand.

the interexchange market, ***see*** Carlton/Sider/Shampine Decl. ¶¶ 37-40, so there are no appreciable barriers to entry, and any long distance customers leaving an ILEC could be served immediately by other carriers. (Indeed, as the Commission noted in the *LEC Classification Order*, the vast majority of the ILECs' long distance customers originally were served by an IXC.) In addition, wireless carriers and ISPs already handle hundreds of billions of minutes of long distance traffic (or "long distance" messages) and could soak up substantial additional demand if called upon to do so. Finally, because the same interexchange capacity is used to provide retail service to mass market and enterprise customers and wholesale service to other carriers, there is no need to draw distinctions among customer classes.

2. Demand substitutability

As the *LEC Classification Order* recognizes, "purchasing decisions of most customers of domestic interexchange services are sensitive to changes in price, and customers would be willing to shift their traffic to an interexchange carrier's rival if the carrier raises its prices." *LEC Classification Order*, ¶ 97. This holds equally true today. Indeed, as the rapid rise in wireless long distance traffic, e-mail, and instant messaging demonstrates, customers will use whatever means of long distance communications they believe offers the best value.

Moreover, as the Commission held in the *AT&T Non-Dominance Order*, high demand elasticity typifies both mass market and large business customers. *AT&T Non-Dominance Order*, ¶ 65. The ILECs are fighting hard to gain a foothold in the enterprise long distance market, which remains dominated by AT&T and WorldCom, and they would have no prospect of doing so if they tried to raise prices. In this regard, the *Telecom Competition Survey* (at 2) found that, for those enterprise customers willing to consider switching long distance carriers, 82 percent listed price as the most significant reason. The next highest reason (billing problems) was identified by only 36 percent of respondents. Id. at 8. Without a doubt, an ILEC – whether

or not it provides long distance service through a separate affiliate – could not charge supra-competitive interLATA rates without its customers fleeing to other competitors.

3. Market share

The Commission has been appropriately skeptical of the value of market share statistics in determining regulatory policy. In finding AT&T non-dominant notwithstanding its then-60 percent market share, for example, the Commission observed that

> [i]t is well-established that market share, by itself, is not the sole determining factor of whether a firm possesses market power. Other factors, such as demand and supply elasticities, conditions of entry and other market conditions, must be examined to determine whether a particular firm exercise market power in the relevant market. As we noted in the *First Interexchange Competition Order*, "[m]arket share alone is not necessarily a reliable measure of competition, particularly in markets with high supply and demand elasticities." *AT&T Non-Dominance Order*, ¶ 68.

In today's dynamic long distance market, moreover, any effort to consider market share must consider wireless and Internet services in addition to traditional wireline long distance. Verizon is not aware of any publicly reported statistics that endeavor to do so. For example, although the Commission's *Long Distance Report* makes an effort to include toll revenues reported by wireless carriers, ***see*** *Long Distance Report* at Table 1, n.13, it does not include the many billions of minutes of long distance traffic handled by wireless carriers under flat-rate, any-distance plans. Nor does it encompass revenues attributable to e-mail, instant messaging, and VOIP. Nonetheless, given the estimate that wireless long distance accounts for almost a quarter of total long distance minutes, and the reality that e-mail, IM, and e-commerce must substitute for a very large portion of long distance messages, market share statistics focusing solely on wireline (or wireline plus wireless toll) calling likely overstate any individual company's share by fifty percent or so.

Even putting on blinders to the reality of cross-platform competition, the ILEC-specific statistics reported by the Commission do not reveal market shares that come remotely close to

raising market power issues. Verizon's share of the total nationwide toll market (intrastate and interstate, including wireless toll traffic but not wireless flat-rate long distance) is only 3.4 percent, and its share of interstate toll revenues is only 2 percent. ***See*** *Long Distance Report*, Tables 1 and 2.[24]

Looking at the residential sub-market, Verizon has a roughly 5.6 percent share of nationwide residential interLATA minutes (an extremely conservative proxy for revenues, since it excludes wireless and Internet long distance minutes/messages), and the BOCs collectively account for only 10.6 percent of these minutes. *Long Distance Report*, Table 14 (2002 figures). Moreover, the BOCs' 10.6 percent share of residential interLATA minutes is only two-thirds of their share of households (which is 15.8 percent). *Long Distance Report*, Table 14 (2002 figures). This is so because the ILECs serve a disproportionate number of low-volume customers – hardly what one would expect to find if they could exercise market power.

The ILECs' business long distance market shares are not reported by the Commission, but undoubtedly are far lower. The *Telecom Competition Survey* found that only six percent of the 300 medium-sized and large enterprises surveyed identified Verizon as their primary long distance provider (for other BOCs, the numbers ranged from two percent (for BellSouth and SBC) to nine percent (for Qwest, which had an existing long distance business before acquiring U S WEST)). In fact, the survey found that AT&T, WorldCom, and Sprint actually have a stronger lock on the enterprise market this year (61 percent of responses) than they did in 2002 (53 percent of responses). *Telecom Competition Survey*, Exhibit 7. Another analyst likewise has

[24] Table 1 shows that Verizon's total (ILEC plus long distance affiliates) toll revenues are $3.361 billion, which is 3.4 percent of the $99.3 billion total interstate and intrastate toll revenues reported in the table. The Verizon long distance affiliates' revenues of $1.373 billion are 2 percent of the total interstate (including international) toll revenues of $69.77 billion shown on Table 2.

concluded that the RBOCs will "compete most effectively within the small and medium enterprise (SME) portion" of the commercial long distance market, but even there will attain a share of less than nine percent by 2005. *Telecom – Three Year View* at 17, 21. That same analyst stated that "[t]he incumbent IXCs, particularly AT&T and WorldCom, should find the RBOC competition manageable and are expected to continue to dominate the long distance commercial market, and particularly the Enterprise segment of that market, with minimal challenges from new entrant competition." Id. at 18. AT&T's CEO agrees, having just stated that the "Bells don't cover robustly" the large enterprise market, from which AT&T derives a "significant percentage" of its long distance revenues. "Dorman: AT&T Has Long-Distance Future," http://www.forbes.com/2003/06/18/0617chat_transcript.html.

In short, no individual ILEC has a market share within an order of magnitude of AT&T's market share when it was declared non-dominant; even collectively, the ILECs can muster a total share barely a quarter of AT&T's when it was relieved of dominant carrier regulation. And, in any event, there is no evidence that the ILECs' relatively rapid initial gains in serving mass market customers are in any way ill-gotten. To the contrary, those gains stem from favorable brand recognition, savvy marketing, and the availability of simple, easy-to-understand, inexpensive calling plans. The market share information – however the market is defined – thus further confirms that ILECs are non-dominant in the provision of long distance services on an integrated basis.

4. Size and cost structure

In the *LEC Classification Order* (at ¶ 97), the Commission found that the existence of well-established, incumbent IXCs made it unlikely that the BOCs' interLATA affiliates could raise prices to supra-competitive levels. The Commission also pointed out that ILECs suffered certain cost disadvantages relevant to the large IXCs, given their lack of nationwide, facilities-

based networks. Id. ¶¶ 97, 157. This analysis is still valid; nothing about the BOCs' and independent LECs' size and cost structure – whether or not they provide long distance service through a separate affiliate – suggests that they could exercise market power in the in-region, interexchange market.

As was true at the time of the *LEC Classification Order*, the major IXCs remain well-established players with considerable technological and cost advantages over the BOCs' and independent LECs' own long distance operations, stemming from their ownership of ubiquitous, nationwide long distance networks. Indeed, WorldCom – notwithstanding its massive and pervasive fraud – seems poised to emerge from bankruptcy in the next several months largely shorn of debt, giving it a substantial and wholly unwarranted cost advantage. In addition, there are five nationwide wireless providers of long distance services unaffiliated with the ILEC in each relevant geographic market, each of which is financially stable and likely capable of reaping significant economies of scale in providing long distance services. Further competition comes from instant messaging and e-mail services provided by corporate giants such as Microsoft, Yahoo!, and AOL Time Warner, among others.

In 1995, the Commission rejected arguments that AT&T, despite being significantly larger than all of its competitors combined, could exercise market power by virtue of its size and cost structure. ***See** AT&T Non-Dominance Order*, ¶ 73 ("the issue is not whether AT&T has advantages, but 'whether any such advantages are so great to preclude the effective functioning of a competitive market'"). Given the far greater number of entrenched competitors today, the much smaller size disparities, and the fact that no ILEC has a long distance network as ubiquitous as those of the major IXCs, the Commission must reach the same conclusion with respect to the ILECs' long distance operations.

IV. DOMINANT CARRIER REGULATION AND OTHER INTRUSIVE REQUIREMENTS ARE INIMICAL TO FULL AND FAIR COMPETITION.

In addition to being utterly unnecessary, dominant carrier regulation would be anticompetitive and harmful to consumers. The Commission has "long recognized" that dominant carrier regulation – namely, tariffing and cost support obligations – "ha[s] undesirable effects on competition" and is "'at best a clumsy tool for controlling vertical leveraging of market power ....'" *LEC Classification Order*, ¶¶ 88, 90, 91 (citing reply comments of the Department of Justice). There are several persuasive reasons for the Commission's concern:

- First, "advance notice periods for tariff filings can stifle price competition and marketing innovation when applied to a competitive industry." Id. ¶ 88. Indeed, the substantial advance notice and cost support requirements inherent in dominant carrier regulation "would impose even more significant costs and burdens ... than the one-day notice period formerly required of non-dominant carriers *and would adversely affect competition.*" Id. ¶ 89 (emphasis added).

- Second, "such requirements would impose significant administrative burdens on the Commission and [the ILECs'] interLATA affiliates, particularly to the extent they encourage the affiliates' interLATA competitors to challenge the affiliates' interLATA rates in order to impede the affiliates' ability to compete." Id. ¶ 90.

- Third, providing cost support data "can also discourage the introduction of innovative new service offerings, because it requires a carrier to reveal its financial information to its competitors." Id.

- Finally, although a price floor might help prevent predatory pricing, such a floor, "if set too high, could prevent consumers from enjoying lower prices resulting from real efficiencies." Id.

No meaningful benefits outweigh these harms. As the Commission found in the *LEC Classification Order* (¶ 92), dominant carrier regulation is "not well-suited to prevent the risks associated with" ILEC provision of in-region, interLATA services. The elimination of separate affiliate requirements for BOCs and independent LECs neither diminishes the anticompetitive impact of dominant carrier regulation nor makes such regulation any better tailored to address alleged risks of discrimination and price manipulation. ***See*** *NPRM*, ¶ 38; ***see also***

Carlton/Sider/Shampine Decl., ¶¶ 75-78 (explaining that "tariffs and price caps would not address concerns about non-price discrimination" and "would not address predation concerns").

For the same reasons, the Commission should not adopt any "alternative regulatory approaches" following the sunset or elimination of separate affiliate requirements. ***See generally*** *NPRM*, ¶¶ 45-49. Any form of "272-lite" separation requirements would impose significant, unwarranted costs on ILECs that no other competing provider of long distance services need bear, inevitably distorting competition and decreasing efficiency and innovation.[25] ***See Third*** *Computer Inquiry*, 104 FCC 2d 958, ¶ 3 (1986) ("structural separation requirements impose significant costs on the public in decreased efficiency and innovation that substantially outweigh their benefits").

Verizon has estimated that Verizon Global Networks, Inc. (the section 272 affiliate that provides underlying network services to Verizon's retail section 272 affiliates), would save roughly $ 247 million from 2002 through 2006 if separate affiliate requirements were discontinued. Verizon's retail section 272 affiliates would save almost another $ 100 million. Comments of Verizon, WC Docket No. 02-112, at 9-10 (filed Aug. 5, 2002). Merely substituting less stringent separation requirements still would leave the ILECs at a serious and unwarranted competitive disadvantage. For example, replacing the Section 272 requirements with Fifth Report and Order-type safeguards would continue the prohibition on joint ownership of transmission and switching facilities. Verizon estimates that it was forced to waste $ 195 million between 1998 and 2002 building duplicate facilities needed to comply with this ban. Id.

[25] Such requirements also would contravene Congress's intent that structural separation be a transitional mechanism that would be eliminated within three years after a BOC received in-region interLATA authority, absent unanticipated developments (of which there have been none).

at 13-14. Without a doubt, elimination of these costs would result in lower rates, greater (and more efficient) investment, more innovation, and increased competition.

Likewise, the Commission should not continue the Fifth Report and Order safeguards for independent LECs. The ban on joint ownership of transmission and switching facilities, in particular, creates serious inefficiencies that impair the ability of independent LECs to compete against the likes of AT&T, WorldCom, Sprint, the national wireless companies, major cable MSOs, and the dominant ISPs, all of which are free to integrate their operations as they see fit. These safeguards initially were imposed based on speculation that independent ILECs "could potentially" discriminate against long distance rivals or price predatorily. ***See LEC Classification Order***, ¶¶ 160-161. As demonstrated above, such speculation is patently without foundation in today's dynamic and vigorously competitive long distance market.

Nor can the Commission determine that Sections 272(e)(2) and 272(e)(4) continue to apply once the separate affiliate requirements sunset. ***See NPRM***, ¶ 46. The Commission already has found that "the plain language of the statute compels us to conclude that sections 272(e)(2) and 272(e)(4) can be applied to a BOC after sunset only if that BOC retains a separate affiliate." *Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act*, First Report and Order and Further Notice of Proposed Rulemaking, 11 FCC Rcd 21905, ¶ 270 (1996). The plain language of the statute has not changed, and there is no basis for the Commission to reconsider its earlier conclusion. And, in any event, other, less intrusive safeguards sufficiently address the alleged harms these provisions seek to prevent, and these additional constraints would uniquely and unduly constrain the BOCs' competitive flexibility.

V. CONCLUSION

For the foregoing reasons, the Commission should state that BOCs and independent LECs providing in-region, interstate, interexchange service on an unseparated basis are non-dominant, and should reject the inevitable calls for imposition of additional regulatory obligations on ILECs.

Respectfully submitted,

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