Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

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| In the Matter of | ) | |
| | ) | |
| Annual Assessment of the Status of | ) | MB Docket No. 03-172 |
| Competition in the Market for the | ) | |
| Delivery of Video Programming | ) | |

# COMMENTS OF
# <u>QWEST COMMUNICATIONS INTERNATIONAL INC.</u>

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TABLE OF CONTENTS

SUMMARY

Through its corporate affiliate Qwest BSI, Qwest currently provides advanced multi-channel video and high speed Internet access service in several markets within the United States using VDSL technology, and competes head-to-head with incumbent cable providers. These services have been well received by Qwest BSI's customers. This success demonstrates that there is a strong demand for telephony-based video services, and also shows that VDSL has the potential for being a viable alternative to traditional methods of delivering multi-channel video services such as cable television.

In regulatory terms, however, Qwest currently faces a lose-lose situation. Qwest BSI's expansion has been slowed by regulatory uncertainty as to whether certain of its services will be regulated as "telecommunications services" under Title II of the Communications Act as well as be regulated as cable services under Title VI. Since cable providers are able to provide telephony services with less regulation, the service packages that Qwest and cable providers use to compete for customers are regulated in a highly disparate manner. Operating under heavier regulatory burdens increases Qwest BSI's costs and sharply reduces its competitiveness. Qwest BSI also experiences a disadvantage in accessing programming, since it is a new market entrant.

It should therefore be clear that while the 1996 Act purported to remove barriers to competition in the video and telecommunications services markets, there is still a great deal of work to be done. Specifically, the Commission must resolve the current regulatory uncertainty under which incumbent LEC-affiliated companies like Qwest BSI are operating, reduce the asymmetric regulatory burdens that disadvantage them against their competitors, and take steps to prevent anticompetitive abuses by vertically-integrated cable providers in areas such as

programming access. All of these steps are going to be necessary if the 1996 Act's goal of promoting inter-modal competition is to be fulfilled.

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**COMMENTS OF**
**<u>QWEST COMMUNICATIONS INTERNATIONAL INC.</u>**

Qwest Communications International Inc. ("Qwest") respectfully submits these Comments in response to the Federal Communications Commission's ("Commission") *Notice of Inquiry* soliciting data, information, comments, and analyses pertaining to the status of competition in the market for the delivery of video programming.[1]

The Telecommunications Act of 1996 ("1996 Act") removed barriers to entry by telecommunications providers into the multi-channel video market and by traditional cable companies into the market for telecommunications services.[2] In some extent, that desired competition has begun. Qwest, through various of its affiliates, provides local exchange service, interexchange services, Internet access services and cable services. Specifically, Qwest provides advanced multi-channel video and Internet access service in several markets within the United States, using very-high speed digital subscriber line ("VDSL") technology. In these markets, Qwest has overbuilt incumbent cable television networks and now competes head-to-head as a new market entrant with these incumbent cable providers. Qwest's video services depend, in part, on its local telephone infrastructure to provide cable and Internet services in a way that is

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[1] *In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, MB Docket No. 03-172, *Notice of Inquiry*, FCC 03-185, rel. July 30, 2003 ("*Notice*").

analogous to the manner in which cable providers use their cable infrastructure to provide both telephony and cable modem services.

However, the 1996 Act has not (and will not) achieve the inter-modal competition intended by Congress without radical changes in the underlying regulation of cable and telecommunications providers. Although Qwest's broadband services have been well received by its customers, the expansion of these services to additional geographic markets has been slowed by regulatory uncertainty and the asymmetrical regulation that interfere with true market-based competition. Qwest's multi-channel video unit has been forced to operate in a vacuum of information regarding which type of regulation will apply to its high speed Internet services, which are otherwise comparable to cable modem service, due to Qwest's use of the local telephone infrastructure. These regulatory uncertainties are not shared by Qwest's direct competitors in the video market, and they place Qwest at a significant competitive disadvantage. These disadvantages are further magnified by the vertical integration of video content and retail cable services enjoyed by the major cable providers, and the corresponding inability of smaller buyers of video content to obtain programming at competitive prices.

To achieve the 1996 Act's intended purpose of increased inter-modal competition, the Commission must take action -- where it has authority -- to permit the development of real inter-modal competition and to prevent the misuse of market power by vertically integrated cable providers. And to the extent there are statutory barriers, the Commission must work with Congress and local franchising authorities to ameliorate additional asymmetrical burdens. Without such leadership, local exchange carriers ("LEC") will be unable to become a viable source of competition in the market for video services.

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[2] *See* Part V of Title VI of the Communications Act of 1934 as amended, 47 U.S.C. §§ 571

## I. QWEST'S VIDEO OPERATIONS

The *Notice* seeks data concerning the state of competition in the video marketplace, as well as information concerning the impact of regulations and a description of barriers to competition. Qwest takes this opportunity to describe the data and video services that it currently offers in several markets, the type of network and the technology that it is using, and the consumer demand that has been demonstrated for its broadband services.

In its cable franchised areas in the Phoenix metropolitan area, Denver and Boulder, Qwest Broadband Services, Inc. ("Qwest BSI") provides advanced multi-channel video and high speed Internet access services, over a VDSL infrastructure.[3] In all locations, Qwest BSI provides video services under the terms of cable franchise agreements with local franchising authorities, and its cable services are regulated under Title VI of the Communications Act of 1934, as amended ("Communications Act").

Qwest BSI provides its customers with traditional multi-channel video service, which is branded as "Qwest Choice TV," as well as broadband Internet access service which is functionally the same as cable modem service, and which is branded "Qwest Choice OnLine."

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through 573.

[3] Qwest BSI offers video service pursuant to its franchise in Omaha using a hybrid system of fiber and coaxial copper cable, and the broadband services it offers are cable modem service, identical to the architecture of the traditional cable operators on upgraded systems. It is only the VDSL architecture that Qwest wishes to bring to the Commission's attention in these comments, because VDSL relies on portions of the local telephone network, begetting the issues that are addressed herein.

In addition, customers may buy packages of services that include video, high speed Internet access, local telephone service, Caller ID, voice messaging, and long distance service in locations where Qwest is authorized to provide it.

Qwest BSI began offering its broadband services in Phoenix in approximately 1997 and began its build-out in parts of Denver and Boulder in 1999. Qwest BSI currently has approximately 40,000 subscribers in Phoenix, 2,000 subscribers in Denver and Boulder, and 14,000 subscribers in Omaha. Customers in Qwest BSI's service areas rate the value of their service significantly higher than digital cable subscribers, and judge the quality of the video service provided by Qwest BSI to be better than that of their previous (cable) provider. Packages including telephony services such as Caller ID that can work in conjunction with the set-top box and the customer's television set, and are accessible using the television remote, have also proved very popular with Qwest BSI's customers.

While Qwest BSI provides Internet access service using the same equipment it uses to distribute video programming, it has had to constantly worry whether its Internet access service will also be subjected to regulation as a telecommunications service under Title II or whether Qwest BSI might be found to be a common carrier under Title II. This concern arises principally because of its corporate affiliation with Qwest Corporation ("QC"), which is an incumbent LEC, and because Qwest BSI leases certain of its network facilities from QC. The facilities that Qwest BSI uses to provide video services to end users -- including the video head-end, the asynchronous transfer mode ("ATM") switches and other equipment, including the VDSL digital subscriber line access multiplexers ("DSLAM") -- all belong to Qwest BSI. However, Qwest BSI leases dark fiber from its head end to QC's central offices, rents space for its equipment in QC's central offices and also obtains the fiber feeder and line sharing on QC's subloop from the remote terminal to the customer's premises. Qwest BSI pays QC for this infrastructure and these facilities in accordance with the Commission's affiliate transaction rules.

The Ninth Circuit's decision in the *City of Portland*[4] case which held that transmission facilities used to provide cable modem service are subject to regulation under Title II, as well as the ongoing litigation, lack of clarity, and flux in the Commission's rules, have created regulatory uncertainty for Qwest BSI and QC. Qwest had taken a very conservative approach to compliance, and whenever QC permits Qwest BSI to construct and locate its VDSL equipment in its outside plant, QC has treated that location as a remote terminal with respect to which QC must stand ready to provide collocation and interconnection to any competitive carrier requesting those benefits under Title II of the Communications Act. As described below, this approach has added substantial cost to Qwest BSI's video distribution operations because it pays for build-out and the excess capacity.

## II. QWEST'S AFFILIATES ARE BURDENED BY REGULATORY UNCERTAINTY AND BY ASYMMETRIC RULES

The *Notice* seeks comment on the factors that have either facilitated or impeded changes in the competitive environment for video programming. It is therefore appropriate to review the regulatory costs that currently hinder Qwest BSI's ability to compete in the marketplace for video services, as well as the asymmetry of the regulations under which Qwest BSI competes in the video marketplace.

As the Commission is aware, incumbent LECs -- such as QC -- are permitted to operate on a fully integrated basis with video providers such as Qwest BSI.[5] These interoperations are critical to Qwest BSI, both as a new market entrant and as an overbuilder. However, in light of

[4] *See AT&T v. City of Portland*, 216 F.3d 871 (9th Cir. 2000), *reversing* 43 F. Supp. 2d 1146 (D. Ore. 1999) ("*City of Portland*").

the regulatory uncertainties caused by *City of Portland* and the lack of guidance in digital subscriber line ("DSL") by the Commission, Qwest has chosen to act, in many respects, as if its Qwest BSI affiliate is providing "telecommunications" under Title II. As a result, QC must plan on meeting the demands of unaffiliated carriers that might insist on parity under Title II. This situation results in much higher regulatory uncertainty and costs than Congress intended when it authorized telephone companies to provide video programming services on an integrated basis. It certainly adds a layer of complexity and cost not faced by Qwest's cable competitors, resulting in harm to Qwest BSI's ability to compete and slowing its ability to enter new markets.

There is an irony to this. As the Commission is aware, wireline LECs are comparative newcomers to the market for broadband services, and have a market share that is still far behind their competitors.[6] However, due to regulatory uncertainty regarding DSL and due to their status as LECs and as incumbent carriers under Section 251 of the Communications Act, LECs are finding it difficult to invest what is necessary to compete in the video market. This overlay of common carrier regulation has raised the facilities and operating costs of LEC-affiliated video providers such as Qwest BSI significantly, and has hindered their ability to enter the market as a VDSL provider, particularly when facing established incumbent cable television competitors.

Moreover, Qwest's affiliates operate under the double burden of being a new market entrant with regard to broadband and video services, while simultaneously bearing the regulatory burdens of being an incumbent LEC. Qwest BSI pays for the deployment of fiber optic feeder to neighborhoods in which it will offer cable services. Such facilities overbuild both the incumbent video provider's coaxial network and QC's own copper facilities. Qwest BSI's operations, as a

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[5] *See* 47 U.S.C. § 571(b).

[6] *See*, *e.g.*, various *ex partes* Qwest filed in the Broadband proceeding, CC Docket No. 02-33, on Aug. 8, 2003, June 30, 2003, June 26, 2003, June 25, 2003 and June 19, 2003.

new market entrant, do not allow it the economies of scale enjoyed by its established competitors. There is considerable uncertainty over whether Qwest BSI might be treated as an incumbent LEC by state and local regulators. At the same time, Qwest BSI is treated as a cable provider by local franchising authorities, which impose aggressive facilities build-out requirements, franchise fees and provision of dedicated public access channels. All of these costs add to Qwest BSI's capital requirements.

Particularly in the wake of *City of Portland*, the treatment of network plant that is used for Title VI operations has been unclear. In light of this uncertainty, Qwest has taken a conservative approach and kept ownership of the fiber feeder with QC. Consequently, while Qwest BSI pays for this fiber build-out, those facilities are subject to QC's unbundling and collocation obligations. This approach has added significant costs to the deployment of Qwest BSI's new broadband facilities. For example, when QC has deployed remote terminals that are equipped for its DSL service or for Qwest BSI's high speed Internet service, QC currently reserves an additional 15 percent space to accommodate a competitive LEC. This extra 15 percent space, plus engineering to permit multiple power feeds, adds $4,400 to the cost of each remote terminal used for broadband deployment. QC currently has approximately 1,500 remote terminals with DSL or high speed Internet services, and plans to deploy approximately 500 more remote terminals. Consequently, in deploying these existing remote terminals, QC incurred approximately $9.2 million in additional expense to accommodate potential collocation by competitive LECs.

In regulatory terms, operating both as a new market entrant for video services and as an incumbent LEC is truly the worst of both worlds, and is the result of a mismatch between the competitive nature of the broadband marketplace and the legacy regulations that threaten Qwest

BSI because of its corporate affiliations.[7] This situation violates the long-standing Commission principle that like services ought to be regulated in like ways.

## III. QWEST BSI HAS DIFFICULTY ACCESSING VIDEO PROGRAMMING

The *Notice* also requests comment on the effectiveness of the Commission's current program access rules, including information on the extent to which terrestrially-delivered programming services owned by, operated by, or affiliated with a programming distributor are available to other video service providers.[8] The simple answer to this inquiry is that Qwest BSI pays more to access programming than its larger, incumbent cable television providers. This is due to the manner in which the 1992 Cable Act permits programmers to differentiate their rates for selling and delivering programming to new market entrants such as Qwest BSI.[9] The net effect is that Qwest BSI is once again placed at a disadvantage in the market, which further reduces the profitability of its video services.

The incumbent cable television providers enjoy a distinct cost advantage to Qwest BSI when negotiating program access contracts with vendors. As a new market entrant, Qwest BSI does not have access to the content discounts and economies of scale that its cable television competitors enjoy. Qwest BSI is also disadvantaged by preferential treatment under the current laws. As the Commission is aware, while Section 628(c)(2)(B) of the 1992 Cable Act, 47 U.S.C. § 548(c)(2)(B), officially prohibits vertically-integrated cable programmers from discriminating against competitors with respect to the prices, terms and conditions of sale or delivery of programming, it simultaneously contains an exception that swallows the rule. Under Section

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[7] *See* Comments of Qwest Communications International Inc., CC Docket No. 02-33 *et al.* at 18-21, 21-32 (filed May 3, 2002).

[8] *See Notice* ¶ 18.

[9] 47 U.S.C. § 521, *et seq*.

628(c)(2)(B), programmers may charge new market entrants and overbuilders, such as Qwest BSI, higher prices for content than the rates paid by "similarly situated" cable television competitors on the basis of economies of scale, differences in delivery and transmission costs, expected viewership and advertising revenues, and the small size of the new entrant's subscribership. As a net result, Qwest BSI estimates that it pays approximately 20 percent more to access programming than the incumbent cable television providers with which it competes.[10] As the agency that has primary regulatory responsibility to implement the Communications Act, the Commission should take advantage of this *Notice* to develop a record and report to Congress detailing these inequities.

Qwest BSI experiences another, separate competitive problem derived from the market power of its cable television competitors. In areas where it provides video and broadband services, Qwest BSI's cable television competitors have refused to permit Qwest BSI to purchase advertising for its services on their networks. This anticompetitive behavior has prevented Qwest BSI from being able to reach potential customers on a targeted, regional basis, which is necessary due to the limited geographic areas in which Qwest BSI currently provides services. These actions have created entry barriers for Qwest BSI and raised its costs, because Qwest BSI is forced to either engage in national advertising campaigns for its services or forgo certain advertising avenues altogether. Either choice is unpalatable. The deliberate blocking of Qwest BSI's advertising perpetuates the incumbent cable television providers' dominance of the video market. It is yet another example of asymmetric regulation: cable television competitors are not

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[10] Qwest BSI's problem in accessing programming is common. For example, the Small Cable Business Association has cited a 50 to 100% cost differential between small, independent cable operators and large multi-system operators. Moreover, as a purchasing agent for a large number of small cable systems, the National Cable Television Cooperative pays approximately 40%

subject to market-opening obligations, and are free to provide telephony on a lightly-regulated basis in Qwest BSI's market.

As it stands, the current regulatory system perpetuates preferences in favor of incumbent cable television providers. This is neither workable nor sustainable in the long term if the Congressional intent to foster inter-modal competition is to be achieved. When coupled with additional regulatory uncertainty and consequent higher costs, the high price that Qwest BSI pays to access programming increases its costs above those of its incumbent cable television competitors, and seriously reduces Qwest BSI's already thin margin of profitability. If the Commission does not act to resolve the current tangle of legacy regulations and outdated service classifications, and lend certainty and order to the current system, companies such as Qwest BSI will simply not be able to compete in the open market.

## IV. STEPS THAT THE COMMISSION CAN TAKE TO CORRECT THESE PROBLEMS

Qwest is pleased that the Commission's recent decision in the *Triennial Review Order* acknowledged the importance of broadband issues, and exempted certain new, fiber-to-the-home broadband facilities from regulation under Section 251 of the Communications Act. Qwest also expects, however, that the *Triennial Review Order* will be subject to several years of appellate challenges in the federal courts, and the practical effect may not be known for several years. In the continued absence of regulatory certainty and stability, Qwest will be forced to continue to reserve space for broadband collocation on its facilities, and will continue to incur the additional regulatory costs that are discussed above.

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more for programming than TCI or Time Warner. *See* Comments of the Small Cable Business Association, CS Docket No. 97-248 at 2 (filed Feb. 2, 1998).

Qwest believes that in any event, the Commission must go further than the reforms made in the *Triennial Review Order,* and take specific steps to remove the hurdles that prevent incumbent LECs and their affiliates from being vigorous competitors in the video market.

- As Qwest has pointed out in a separate rulemaking, the continued distinction between cable modem service and LECs' DSL Internet services no longer makes sense, from either a policy or technical standpoint, and has become a serious barrier to open competition.[11] The current rules rest on decades-old legacy regulatory classifications that arose at a time when telephone companies and cable companies were both regulated monopolists, in separate markets, that never competed against each other. Given the increasing convergence of different types of broadband services, particularly in the residential broadband market, the Commission must actively find ways to reduce or eliminate these regulatory disparities between LECs and cable television providers. Because of the proven demand for video services provided over broadband facilities, and the promise of these services if the current regulatory hurdles are removed, Qwest BSI suggests that the Commission should open a rulemaking proceeding and examine ways in which this can be done, through forbearance and deregulation. At a minimum, the terminal that is established for such DSLAMs must not be considered a "premises of an incumbent local exchange carrier" under Title II.

- It is an established principle that "like" services should be regulated equally. The recent entry of many cable television providers into the telephony market underscores the need for regulatory symmetry between cable television providers and incumbent LECs. One example of reform would be further distinguishing video services from telephony in terms of unbundling requirements under Section 251, in an extension of the logic used in the *Triennial Review Order.*

- The Commission needs to resolve that the *Computer II* and *Computer III* rules have no valid application to the transmission component of bundled broadband services, such as DSL or cable modem service. This clarification would treat DSL in a like manner to cable modem services, since the Commission has affirmed that cable modem services are <u>not</u> subject to these rules.[12]

- Deregulation is the best course. Incumbent LECs and cable television providers should be regulated as equals when they provide equivalent services. The history of each sector and the nature of the facilities that are used should not lead to disparate regulatory results.

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[11] *See* Comments of Qwest Communications International Inc., CC Docket Nos. 02-33, 95-20 and 98-10 (filed May 3, 2002); *see also* Reply Comments of Qwest Communications International Inc., CC Docket Nos. 02-33, 95-20 and 98-10 (filed July 1, 2002).

[12] *See In the Matter of High Speed Access to the Internet Over Cable and Other Facilities, Declaratory Ruling and Notice of Proposed Rulemaking*, 17 FCC Rcd 4798, at ¶¶ 43-47 (2002).

## V. CONCLUSION

The positive customer response to Qwest BSI's VDSL offerings shows that strong demand for telephony-based video services exists, and that these services may potentially be a viable alternative to traditional methods of delivering multi-channel video services. It should be clear that these offerings will become truly competitive only if the Commission takes clear, active steps to establish regulatory parity. Today, however, Qwest currently faces a lose-lose proposition. It is regulated more heavily than the incumbent cable television providers with which it competes, but it is simultaneously disadvantaged as a new entrant to the video market in terms of programming access. Continuation of this asymmetry can only serve to discourage LECs from making further investments in broadband facilities or providing a robust, inter-modal and widespread challenge to cable modem providers. In recognition of the market convergence between different sources of broadband services, in the interest of competition, and for the long-term benefit of consumers, Qwest therefore encourages the Commission to undertake a serious and systematic reform of its regulations, so that like services are treated similarly and the artificial disadvantages under which incumbent LECs currently operate are reduced.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Richard Grozier, do hereby certify that on this 11th day of September, 2003, I have caused a copy of the foregoing COMMENTS OF QWEST COMMUNICATIONS INTERNATIONAL INC. to be filed with the FCC via its Electronic Copy Filing System, and served via e-mail on the parties listed below

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