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October 24, 2003

Ex Parte

Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Re: Review of the Commission's Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Service by Incumbent Local Exchange Carriers, WC Docket No. 03-173; Petition for Expedited Forbearance of the Verizon Telephone Companies, WC Docket No. 03-157

Dear Ms. Dortch:

Yesterday, on behalf of Verizon, Karen Zacharia, Donna Epps, and the undersigned met with Lisa Zaina, Legal Advisor to Commissioner Jonathan Adelstein to discuss the above captioned proceedings. The discussion focused on the effects of the Commission's current pricing rules on competition and Telecom investment. The attached slides were used during the meeting.

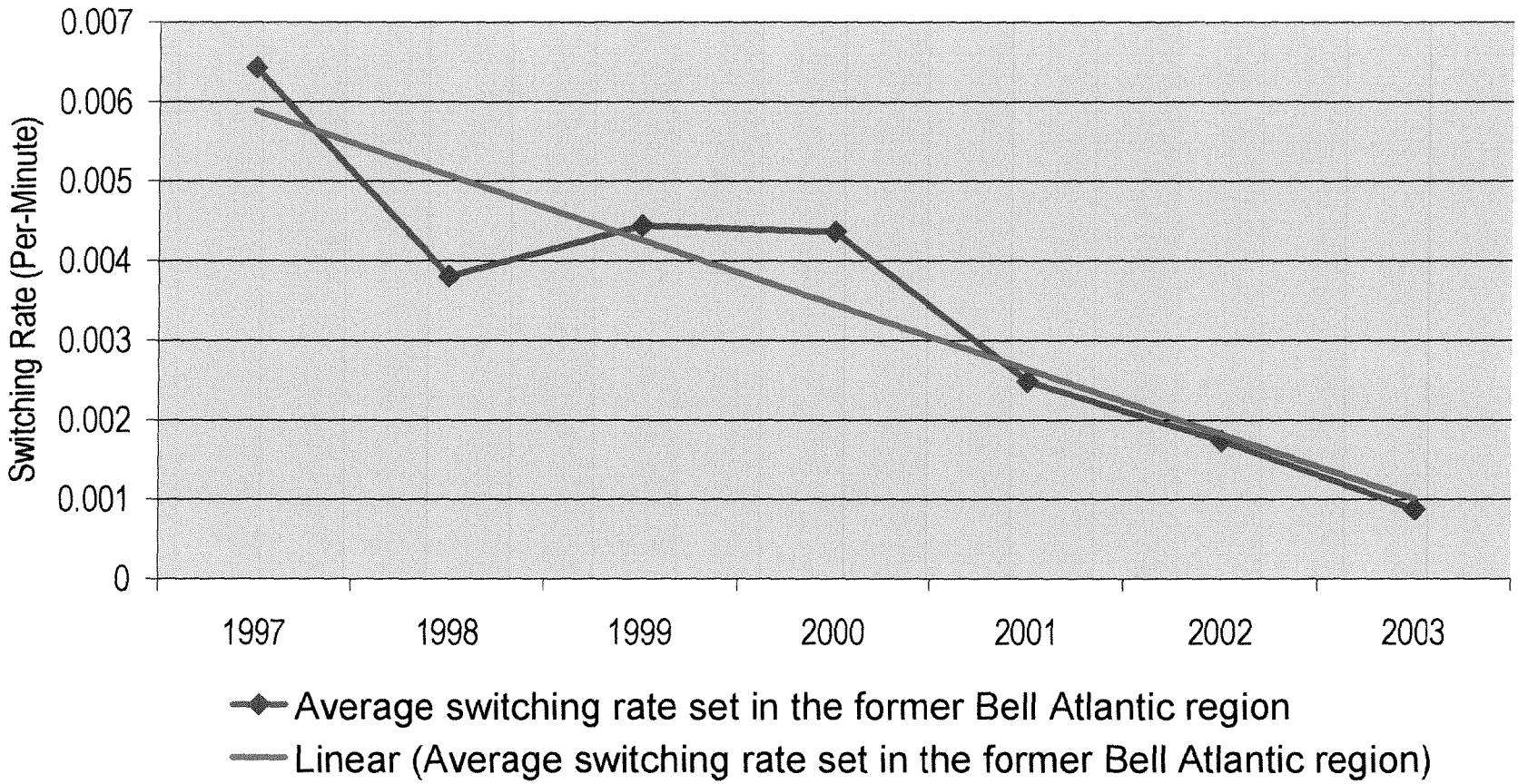
Should you have any questions regarding this material, please do not hesitate to contact me.

Sincerely,

Attachment

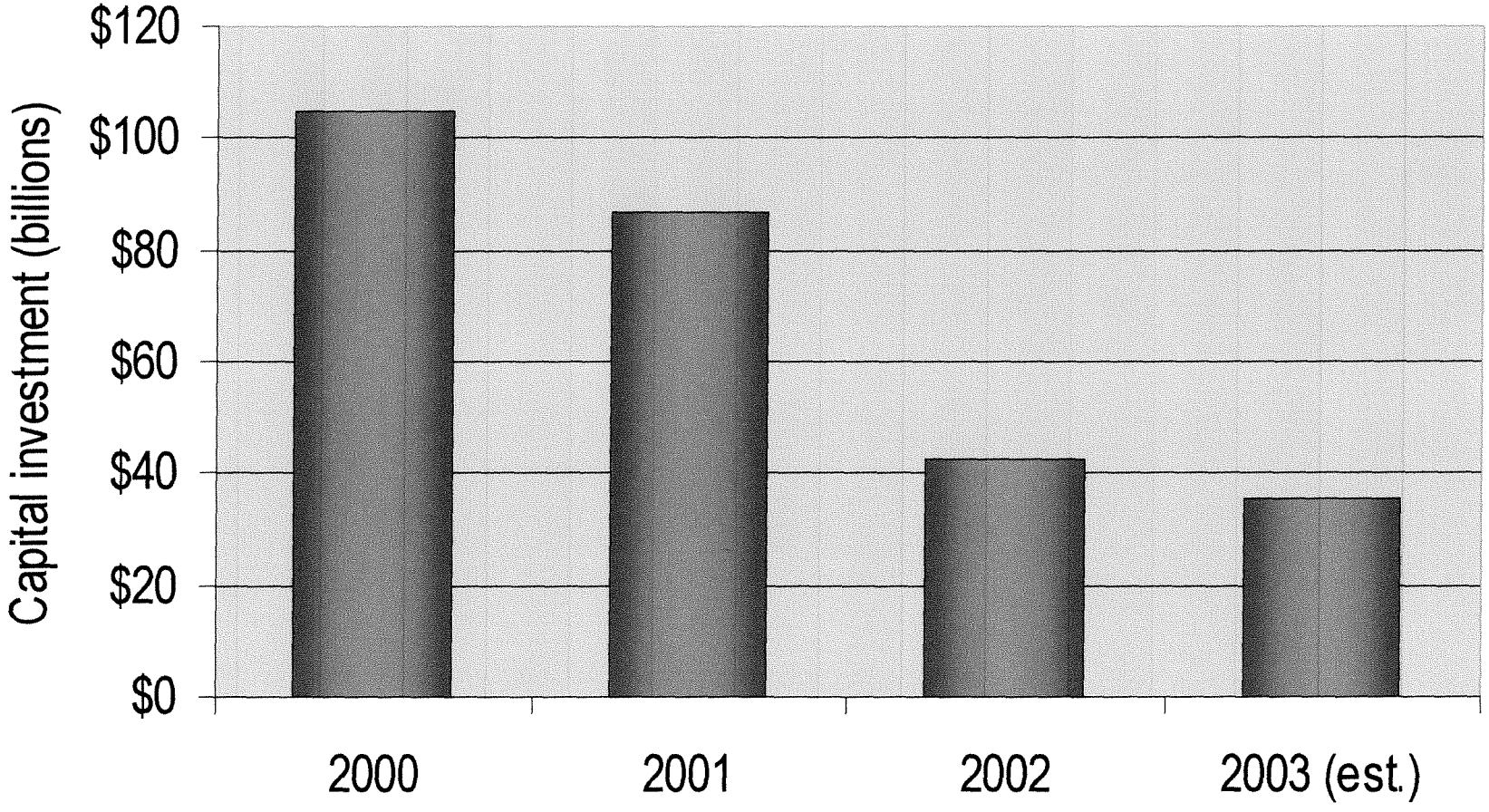
cc: L. Zaina

UNE rates based on TELRIC have declined significantly



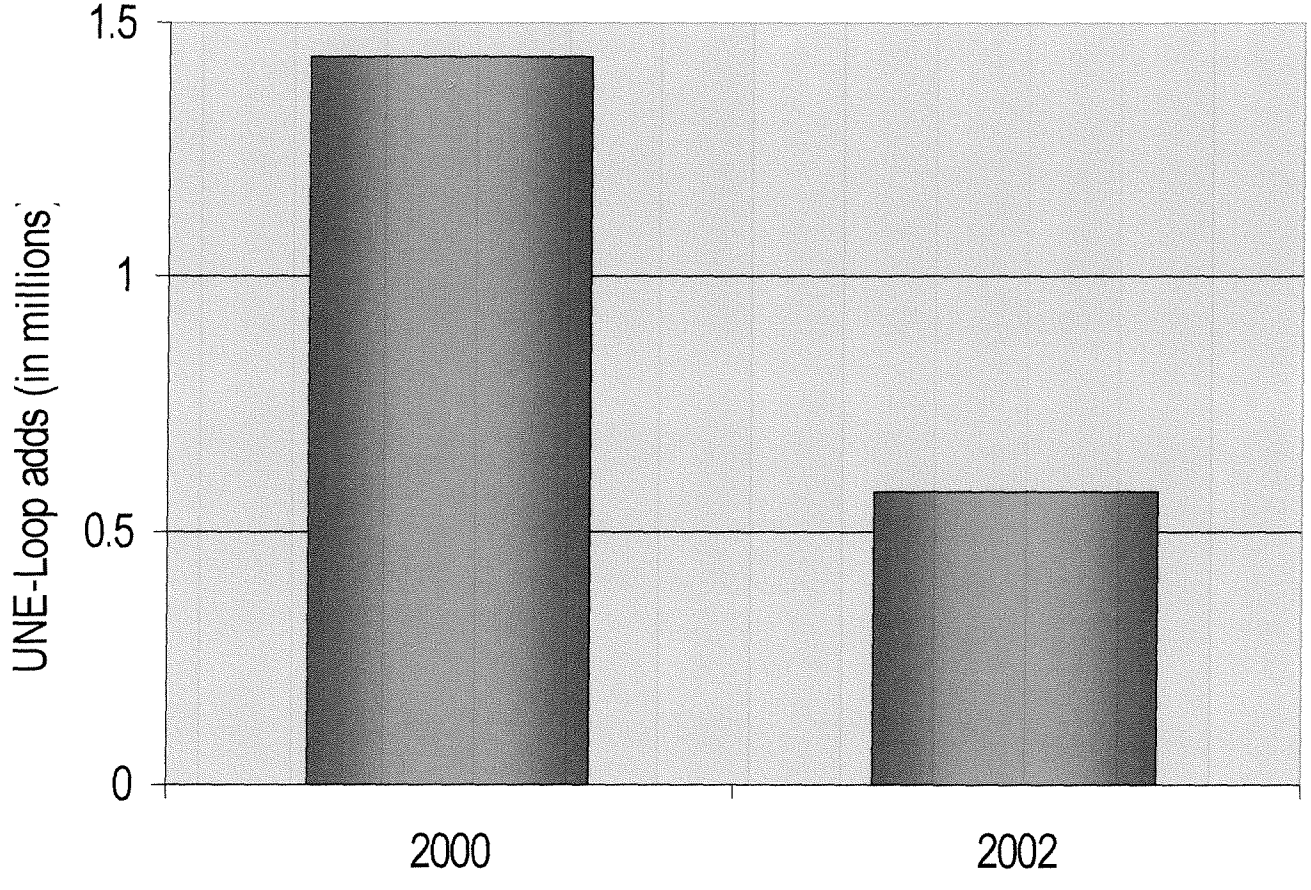
[Source: Verizon data]

As TELRIC rates have been reduced, telecom investment has declined significantly



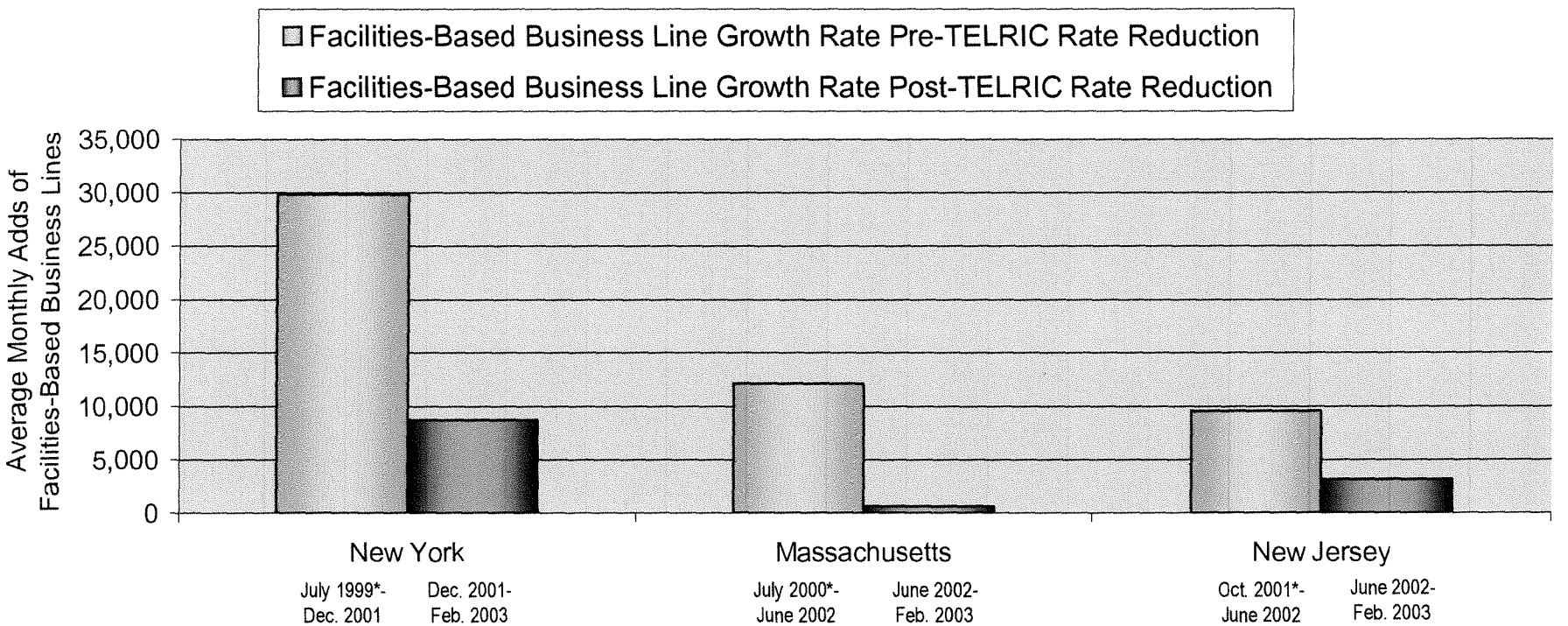
[Source: Skyline Marketing Group, *CapEx Report: 2002 Annual Report*, June 2003]

TELRIC rates curtailed competing carriers' use of their own switches



[Source: FCC, *Local Telephone Competition: Status as of December 31, 2002*]

Growth of facilities-based business lines has slowed significantly following TELRIC rate reductions



*Start date is based on earliest available data. Middle date is date closest to TELRIC rate reduction (within three months) for which data are available. End date is most currently available data.

[Source: Verizon data]

- Independent analysts have repeatedly concluded that TELRIC rates fail to fairly compensate incumbents for their costs and undermine facilities-based competition.

"[F]or all RBOCs, UNEs are priced below cash operating cost, and radically below total operating cost including depreciation and amortization. The discounts from total cost are 50%-60% below total cost even when total cost does not include the cost of equity, a component that is allowed under TELRIC." A. Kovacs, et al. Commerce Capital Markets, Inc., The Status of 271 and UNE-Platform in the Regional Bells Territories at 15 (May 1, 2002).

"[W]hile the Bells lose roughly 60% of the revenues when they lose a line to a UNE-P based competitor, we estimate that they retain 95% of the costs." M. Crossman, et. al, J.P. Morgan Securities, Inc., IndustryUpdate – No Growth Expected for Bells in 2003 at 15 (July 12, 2002).

- Independent analysts have also concluded that TELRIC's below-cost rates discourage facilities-based investments.

"[N]o company will deploy and scale facilities if it can achieve similar economics immediately by renting network elements from the ILECs – all with little up-front investment." McKinsey & Co. and JP Morgan H&Q, *Broadband 2001, A Comprehensive Analysis of Demand, Supply, Economics, and Industry Dynamics in the U.S. Broadband Market* at 18 (Apr. 2, 2001).

"[W]hy overbuild if one can lease it more cheaply than one can build it? We strongly suspect that the success of the UNE-P resale will adversely affect the incentive for facilities-based competition." Hearings before the Subcomm. On Telecommunications Trade & Consumer Protection of the House Commerce Comm., 106th Cong. 2 (May 25, 2000) (Written statement of Scott Cleland, Managing Director, The Precursor Group); *see also* S. Cleland, Precursor Group, *Why UNE-P Is Going Away: Telecom Competition's Changing Trajectory* (Oct. 2, 2002).