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1501 K STREET, N.W.
WASHINGTON, D.C. 20005
TELEPHONE 202 736 8000
FACSIMILE 202 736 8711
www.sidley.com
FOUNDED 1866

LOS ANGELES
NEW YORK
SAN FRANCISCO
SHANGHAI
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TOKYO
WASHINGTON, D.C.

WRITER'S DIRECT NUMBER
(202) 736-8088

WRITER'S E-MAIL ADDRESS
dlawson@sidley.com

April 15, 2004

Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Re: *In the Matter of Petition for Forbearance of the Verizon Telephone Companies*, CC Docket No. 01-338; *In the Matter of SBC Communications Inc.'s Petition for Forbearance Under 47 U.S.C. § 160(c)*, WC Docket No. 03-235; *In the Matter of Qwest Communications International Inc. Petition for Forbearance Under 47 U.S.C. § 160(c)*, WC Docket No. 03-260

Dear Ms. Dortch:

This *ex parte* letter addresses Verizon's March 26, 2004 *ex parte* letter in support of its forbearance petition in the above-captioned proceeding.¹ Despite its great length, the *ex parte* says very little and largely fails to respond to the showings of AT&T and others that Verizon cannot satisfy any of the three independent criteria for forbearance imposed by section 10(a) of the Communications Act.² Moreover, Verizon pointedly continues to ignore the showings that its petition is categorically foreclosed by sections 10(d) and 271(d)(4) of the Communications Act. Verizon's petition should be denied.

Section 10(a)(1). Under section 10(a)(1), Verizon's burden is to demonstrate that the section 271 unbundling obligations from which it seeks forbearance are unnecessary to

¹ *Ex Parte* Letter from Dee May, Verizon, to Marlene H. Dortch, FCC (filed in WC Docket Nos. 01-337, 01-338, 02-33 and 02-52 (March 26, 2004)) ("Verizon *ex parte*").

² *See Ex Parte* Letter from David Lawson, AT&T, to Marlene H. Dortch, FCC, WC Docket Nos. 01-337, 01-338, 02-33 and 02-52 (March 3, 2004) ("AT&T *ex parte*"); *Ex Parte* Letter from Jonathan Askin *et al.*, to Marlene Dortch, FCC, (filed in WC Docket Nos. 03-260, 03-235, 03-220, 03-157, 03-189, and CC Docket No. 03-338 (March 1, 2004)).

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ensure just, reasonable, and nondiscriminatory terms and conditions for the services (or carriers) at issue – e.g., Bell operating company provision of broadband “local loop transmission.”³ Verizon does not even attempt to argue that there is meaningful “wholesale” competition that would ensure just, reasonable, and nondiscriminatory terms and conditions for these telecommunications services. As Verizon concedes, the Commission in the *Triennial Review Order* found that competitive carriers would be *impaired* without access to the full capabilities of hybrid fiber-copper loops.⁴ Under the Commission’s impairment test, impairment exists when natural monopoly and sunk cost entry barriers generally make it uneconomic for competitive carriers to deploy their own hybrid fiber-copper loops.⁵

This should be the end of the issue, and the end of Verizon’s petition. Absent the section 271 regulations that Verizon seeks to evade, Verizon would have the ability to charge supracompetitive prices for wholesale access to broadband loops – or deny access altogether – because it is economically infeasible for competitive carriers to self-deploy their own broadband loops. Competitive carriers could not turn to alternative providers for such access, because none exist. Most cable facilities do not currently have voice capabilities (and thus could not even theoretically be used by competitive carriers to offer voice and data services) and, in all events, cable companies do not offer such wholesale access.

Verizon responds with word play. Verizon contends that it is seeking forbearance from an unbundling obligation, rather than regulation of a telecommunications “service,” and therefore, if “there should be no such unbundling obligation to begin with, section 10(a)(1) can impose no barrier to forbearance on the grounds that the rates for *that* ‘service’ need to be regulated to ensure they are just and reasonable.”⁶ This circular argument has no basis in the language of the statute, which applies in a straightforward manner here. Verizon is seeking forbearance from “enforcement of” a statutory “provision” that requires wholesale unbundling. Either Verizon is asking the Commission to “forbear from applying” that provision to a “telecommunications service” – e.g., “local loop transmission,”⁷ – in which case the Commission may only grant forbearance if it finds that failure to “enforce[] . . . such” provision will not result in rates “by, for or *in connection with that*” “telecommunications service” that are unjust or unreasonably discriminatory.⁸ Or Verizon is asking the Commission to “forbear from applying” that provision to a “telecommunications carrier” (e.g., Verizon), in which case the Commission

³ 47 U.S.C. § 271(c)(2)(B)(iv).

⁴ Verizon *ex parte* at 23.

⁵ *Triennial Review Order*, 18 FCC Rcd. 16978, ¶¶ 75-78 (2003).

⁶ Verizon *ex parte* at 23-24 (emphasis in original).

⁷ 47 U.S.C. § 271(c)(2)(B)(iv).

⁸ *Id.* § 160(a)(1).

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may only grant forbearance if it finds that failure to “enforce[] . . . such” provision will not result in rates “by, for, or in connection with *that*” “telecommunications carrier” – *any* rates for that telecommunications carrier – that are unjust or unreasonably discriminatory.⁹ *There are no other section 10 forbearance options*; Verizon must either ask the Commission to forbear from applying the section 271 provisions to telecommunications services or to telecommunications carriers, and it cannot meet the section 10(a)(1) standard in either case.¹⁰ And because Verizon clearly intends to eliminate all unbundling of broadband facilities post-forbearance, its argument is, in truth, merely another way of stating that Verizon would charge an *infinite* rate for unbundling – which, by definition, would be an unjust and unreasonably discriminatory rate.

Alternatively, Verizon argues that even if forbearance would lead to market power harms, the Commission should weigh those harms against potential benefits of forbearance, such as investment incentives, as the Commission did in conducting its *Triennial Review Order* section 251 impairment analysis.¹¹ Verizon notes that the Commission considered section 706 of the Act in conducting its section 251 “impairment” analysis and found that the impairment suffered by competitive carriers with respect to hybrid loop facilities was outweighed by the need to provide incumbents with greater incentive to deploy broadband facilities.

But as AT&T has previously explained, such balancing is foreclosed by the plain language of section 10(a).¹² Section 10(a) requires three *conjunctive* showings. The first two showings – that enforcement of the regulation at issue is not necessary to ensure just and reasonable rates and conditions and that enforcement is not necessary to protect consumers – are absolute and do not permit the balancing permitted under section 251(d)(2)’s “at a minimum language.”¹³ And while the third showing – that forbearance is consistent with the “public

⁹ *Id.*

¹⁰ See 47 U.S.C. § 160(a) (granting the Commission authority to “forbear from applying any regulation or any provision of this Act to a telecommunications carrier or telecommunications service, or class of telecommunications carriers or telecommunications services, in any or some of its geographic markets,” if the three section 10(a) criteria are satisfied); *id.* § 10(a)(1) (Commission may grant forbearance only if it determines that “enforcement of such regulation or provision is not necessary to ensure that the charges, practices, classifications, or regulations by, for, or in connection with *that* telecommunications carrier or telecommunications service are just and reasonable and are not unjustly or unreasonably discriminatory”) (emphasis added).

¹¹ Verizon *ex parte* at 23.

¹² AT&T *ex parte* at 9.

¹³ 47 U.S.C. § 160(a)(1), (2).

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interest”¹⁴ – is broader in scope, the Commission cannot grant forbearance unless *all three* showings are satisfied.

Thus, Verizon is left to argue that section 706 somehow trumps the plain language of section 10(a). The Commission, however, has repeatedly held that section 706 grants it *no* “independent” authority.¹⁵ Thus, even if section 706 can be considered under the section 10(a)(3) public interest analysis, section 706 plainly does not authorize the Commission to rewrite sections 10(a)(1) and 10(a)(2) to allow trade-offs of market power harms against investment incentives.

Verizon’s reliance on *Consumer Electronics Association v. FCC*, 347 F.3d 291 (D.C. Cir. 2003), is badly misplaced.¹⁶ *Consumer Electronics* did not involve the Commission’s forbearance authority. In *Consumer Electronics*, the court reviewed a Commission order establishing a prospective rule of general applicability pursuant to the All Channel Receiver Act (“ACRA”), 47 U.S.C. § 303(s), which grants the Commission authority to require that televisions “be capable of adequately receiving all frequencies allocated by the Commission to television broadcasting.” The challenged Commission order required all televisions with display of 13 inches or greater to include a tuner capable of receiving and decoding digital television signals. The court upheld the Commission order as a rational means of accomplishing Congress’s “unambiguous command” that analog television broadcasting be phased out by 2007.¹⁷ The court recognized that the order forces some consumers to purchase digital tuners that they do not want, but held that “the very nature of the authority conferred by ACRA assumes that the Commission may impose costs on consumers for features they do not want.”¹⁸

Consumer Electronics quite clearly does not support Verizon’s position here. First, while ACRA authorizes the Commission to establish general rules that impose costs on some consumers in order to benefit the public overall, nothing in section 10(a)(1) permits comparable balancing in the context of forbearance requests. Second, even if such cost-benefit balancing were permissible in the forbearance context, *Consumer Electronics* would not support Verizon’s position. The court held that the Commission’s costly digital tuner requirement was reasonable on balance, because it “would necessarily increase production volumes and, through economies of scale, lower the price of digital tuners for all television purchasers,” which in turn

¹⁴ *Id.* § 160(a)(3).

¹⁵ *Triennial Review Order* ¶ 176 (citing precedents).

¹⁶ *See Verizon ex parte* at 16-17.

¹⁷ *Consumer Electronics*, 347 F.3d at 301.

¹⁸ *Id.*

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would facilitate the Congressionally-mandated transition to digital television.¹⁹ Here, in contrast, the Commission's findings in the *Triennial Review Order* establish that allowing Verizon to deny access to its network will not promote the deployment of hybrid fiber-copper loops by competitive carriers because it is uneconomic for them to do so.

Sections 10(a)(2) and 10(a)(3). Verizon contends that broadband unbundling is unnecessary to promote the public interest and protect consumers because the Bells already face effective broadband competition. Verizon, however, has failed to offer any concrete evidence in *any* actual relevant market, instead relying solely on an economically meaningless hodge podge of "national share" information. Further, Verizon concedes, as it must, that there are, in fact, local markets – and the market at issue are undeniably *local* markets – in which it has broadband monopolies, and contests only the extent of its monopolies (by arguing that it ordinarily is subject to duopoly "competition").²⁰

It is Verizon's burden in this proceeding to present empirical evidence enabling the "painstaking analysis of market conditions" that section 10(a) demands.²¹ Absent such market-specific evidence, the Commission cannot determine the extent of Verizon's monopolies or the ability of duopoly "competition" to protect consumers and ensure just and reasonable rates – and, therefore, cannot make the findings necessary to justify forbearance. What little empirical information Verizon does provide is shockingly inaccurate. For example, Verizon provides no hard figures about actual cable modem penetration in local business markets, but instead relies primarily on *2002 predictions* from the Yankee Group (and others) about the ability of cable to expand into business markets.²² Verizon fails to disclose, however, that the Yankee Group itself has now concluded that these predictions were, to say the least, wildly optimistic. "We projected cable modem would surpass DSL in this [the small business] segment by year-end 2003. However, cable modem penetration *dropped precipitously* in the small business market, or businesses with between 20 and 99 people. Cable operators also achieved limited success in the

¹⁹ *Id.*

²⁰ Verizon *ex parte* at 24-25. In this regard, Verizon mindlessly recycles its argument that cable companies "lead" DSL providers in overall subscribership. Verizon *ex parte*, Broadband Competition Report at 1-8. Duopoly "competition" is problematic not just because the firm with the larger market share may exercise market power, but because *both* participants are likely to have the incentive and ability to maintain prices above competitive levels rather than attempting to ruthlessly compete with the other, as they would need to do in a market with multiple firms. See United States Department of Justice/Federal Trade Commission, *Horizontal Merger Guidelines*, Section 2 (rev. Apr. 8, 1997).

²¹ *WorldCom, Inc. v. FCC*, 238 F.3d 449, 459 (D.C. Cir. 2001); *AT&T Corp. v. FCC*, 236 F.3d 729, 735-37 (D.C. Cir. 2001).

²² See Verizon *ex parte* at 24 & n.31.

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remote office market, reaching only 4.2 percent of the market in 2003").²³ As the Yankee Group now recognizes, "*DSL operators dominate* the U.S. [small business] broadband and enterprise remote-office broadband market."²⁴

Verizon has no response to the fundamental economic point that duopoly conditions are insufficient to produce competitive outcomes, as the Department of Justice and the Commission have repeatedly recognized.²⁵ Nor does Verizon attempt to explain how the Commission could conclude that a duopoly is sufficient to protect consumers in light of its recent holding in the *Mass Media Ownership Order* that "both economic theory and empirical studies" indicate that "five or more relatively equally sized firms" are necessary to achieve a "level of market performance comparable to a fragmented, structurally competitive market."²⁶

Instead, Verizon cites anecdotal evidence of some price competition between cable and DSL.²⁷ By definition, this alleged evidence of recent price reductions, to the extent it exists in some markets, hardly demonstrates that Verizon's DSL prices are the cost-based prices that would obtain in fully competitive markets with multiple competitors. In any event, Verizon is simply making up the facts when it claims that recently "each of the Bell companies has cut its national DSL prices considerably."²⁸ Verizon's "price war" timeline conspicuously stops at the end of 2003.²⁹ Since that time, DSL prices have increased significantly. SBC announced a sharp increase in its DSL prices last month.³⁰ And contrary to Verizon's claim that its rates have "plummeted," Verizon, in *virtual unison* with BellSouth, followed SBC's lead and announced a

²³ Yankee Group, *Cable and DSL Battle for Broadband Dominance* (February 2004), at 4-5 (emphasis added).

²⁴ *Id.* at 4 (emphasis added).

²⁵ AT&T *ex parte* at 11.

²⁶ Report and Order, *2002 Biennial Regulatory Review – Review of the Commission's Broadcast Ownership Rules and Other Rules Adopted Pursuant to Section 202 of the Telecommunications Act of 1996*, 18 FCC Rcd. 13620, ¶ 289 (2003).

²⁷ Verizon *ex parte* at 25-27.

²⁸ *Id.* at 27.

²⁹ *Id.*, Broadband Report at 7.

³⁰ See, e.g., *BellSouth and SBC Raise Prices, Slap Powell in the Face*, dslprime.com (March 18, 2004) (reporting SBC's and BellSouth's recent price increases); Merrill Lynch, *Everything over IP*, at 11 (March 12, 2004) ("We note that SBC raised prices on its entry-level DSL service (by \$3 to \$29.95) and said that it would not lower prices further.").

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stiff price increase for its own DSL service.³¹ In short, the most recent pricing evidence only confirms the existence of a “cozy duopoly.”

It is also notable that these most recent price hikes came after the Commission announced the end of line sharing obligations and that important source of intramodal competition.³² Thus, the market place evidence, rather than “vindicat[ing]” the Bells’ positions,³³ damns them.

Verizon also has no answer to AT&T’s showing that continued unbundling of broadband loops is necessary to protect competition for consumers that increasingly demand *bundles* of voice and data services. Verizon asserts that the Commission has defined “the” relevant market as the *broadband* market,³⁴ but the paragraphs of the *Triennial Review Order* that Verizon cites do not suggest, let alone hold, that the standalone broadband market is the *only* relevant market with respect to broadband services. In any event, even if the Commission focused on broadband markets in analyzing unbundling obligations under section 251(d)(2), section 10(a)(2) expressly forbids the Commission from forbearing where regulation is necessary for the “protection of consumers.” Verizon does not – and cannot – dispute that consumers are increasingly demanding voice-data bundles. Indeed, the Bells are moving aggressively to meet and exploit this demand.³⁵ Thus, under the plain language of section 10(a)(2), the Commission must ensure that such bundled services are available on competitive terms.

Alternatively, Verizon contends that it has no unique ability to offer voice-data bundles, because some cable companies offer cable telephony in some markets.³⁶ The very authorities that Verizon cites, however, confirm AT&T’s claim that the market penetration of this type of service is small – cable telephony is *available* to only 15% of mass market consumers and is not available at all in most local markets.³⁷ And, as Verizon concedes in its

³¹ Matt Richtel, *Verizon to Add Internet Surcharge*, New York Times (Apr. 14, 2004).

³² *Cf. Verizon ex parte* at 26.

³³ *Id.*

³⁴ *Id.* at 27

³⁵ *See, e.g.*, Merrill Lynch, *Everything over IP*, at 49 (March 12, 2004) (“Bundling remains a key element in SBC strategy. Management noted on 4Q03 call that 44% of customers have a ‘key product bundle’ including one or more of LD, DSL or wireless, up from 36% last quarter and 19% a year ago.”).

³⁶ *Id.*

³⁷ *See Verizon ex parte* at 27.

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“Broadband Report,” only 16% of those households subscribe – for an overall penetration rate of 2.4%.³⁸

Nor can the Commission take comfort in VoIP as an alternative so long as the Bells believe that they are free to disconnect the DSL service of any consumer that chooses an alternative voice provider. Thus, at this time, the Bells remain free to thwart VoIP competition by requiring customers to purchase Bell local voice services as a condition of retaining their DSL connections. Under such conditions, no subscriber would want to pay additional money for VoIP service that is, at best, an alternative for local telephone service.³⁹

Unable to show that competition today is sufficient to protect consumers, Verizon’s claim is that future competition – from, for example, satellite and fixed wireless providers – may eventually provide meaningful competition.⁴⁰ But Verizon is requesting immediate forbearance relief today. These technologies have been much hyped, but still have no meaningful customer bases.⁴¹ As the Chairman recently remarked, the “ground is littered with failed predictions.”⁴² Under section 10(a), the relief that Verizon seeks can only be based on a

³⁸ *Id.*, Broadband Report, at 11.

³⁹ Indeed, the primary VoIP offers in the marketplace today require that the subscriber have an underlying broadband connection. *See, e.g.,* http://vonage.com/learn_tour.php; <http://att.com/voip/>.

⁴⁰ *Id.* at 29-30 & Broadband Report at 13-26.

⁴¹ Even Verizon acknowledges today that these technologies have attracted only a handful of customers. For example, despite years of effort, fixed wireless service providers have attracted only 600,000 subscribers and are capable of reaching only a small fraction of the population. *Id.* at 15. Verizon also is forced to concede that to date satellite broadband has attracted few customers and has been a financial disaster for investors. *Id.* at 22. And broadband-over-power lines (“BPL”) is still at the trial stage and still years away from being a full fledged competitor to DSL. The Southern companies – which together constitute a principal potential deployer of BPL – state that commercial deployment of BPL will not commence until 2005, and, even then, BPL will generally be offered on a very limited basis. Reply Comments of AT&T at 9 (filed in ET Docket No. 03-104, Aug. 20, 2003). Indeed, Verizon concedes that BPL is available commercially on a limited trial basis in only two discrete locations and that it is not clear whether these trials have attracted any customers. *See Verizon ex parte*, Broadband Report at 19-20.

⁴² *See Powell Calls “Digital Migration” Critical to U.S. Competitiveness*, Communications Daily (Apr. 14, 2004).

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finding that Verizon lacks market power now, not speculation that competitive conditions may exist in some places at some unknown points in the future.⁴³

Sections 10(d) and 271(d)(4). Finally, Verizon's filing is telling for what it does not address. AT&T and others have demonstrated that even if Verizon could satisfy the three specific requirements for forbearance contained in section 10(a), the petition is categorically foreclosed by two separate provisions of the Communications Act: sections 10(d) and 271(d)(4). Section 10(d) states that "the Commission may not forbear from applying the requirements of section 251(c) or 271 . . . until it determines that *those requirements* have been fully implemented."⁴⁴ Section 271(d)(4) is an express "[l]imitation on [the] Commission,"⁴⁵ which provides that the Commission "may not," either by rule "or otherwise," "limit the terms used in the competitive checklist." That, of course, is precisely what Verizon seeks in its forbearance petition. These provisions stand as insurmountable barriers to the requested relief, notwithstanding any of the issues discussed in Verizon's *ex parte*.

Sincerely,

/s/ David L. Lawson

David L. Lawson

cc: Pamela Arluk John Stanley
Michelle Carey Debra Weiner
Jeffrey Dygert
Trey Hanbury
Thomas Navin
Austin Schlick
Paula Silberthau

⁴³ First Report and Order, *Forbearance from Applying Provisions of the Communications Act to Wireless Telecommunications Carriers*, 15 FCC Rcd. 17414, ¶ 13 (2000) ("In determining whether to forbear from applying specific statutory or regulatory provisions, our goal, consistent with sound public policy and Congressional intent, is to deregulate whenever the operation of competitive market forces is capable of rendering regulation unnecessary. At the same time . . . the decision to forbear from enforcing statutes or regulations is not a simple decision, and must be based upon a record that contains more than broad, unsupported allegations of why the statutory criteria are met"); *WorldCom*, 238 F.3d at 459 (A request that seeks "the forbearance of dominant carrier regulation under Section 10" demands "a painstaking analysis of market conditions" supported by empirical evidence).

⁴⁴ See 47 U.S.C. § 160(d) (emphasis added).

⁴⁵ *Id.* § 271(d)(4).