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June 24, 2004

Ex Parte

Ms. Marlene Dortch
Secretary
Federal Communications Commission
445 12th Street, SW
Washington, D.C. 20554

Re: *In the Matter of Review of Petition for Forbearance From the Current Pricing Rules for the Unbundled Network Element Platform*, WC Docket No. 03-157

Dear Ms. Dortch:

This letter responds to AT&T's June 18 ex parte, as well as to an inquiry from Commission staff regarding several issues relating to the above-captioned petition.[1/] Specifically, we show that while Verizon's petition and the TELRIC rulemaking (WC Docket No. 03-173) address similar issues, the Commission need not be concerned that the decision it reaches here would necessarily predetermine the outcome of that rulemaking. In addition, we demonstrate that an FCC order granting the access charge component of Verizon's forbearance petition would limit state authority to preclude

[1/] Letter from Joan Marsh, Director – Federal Government Affairs, AT&T to Marlene Dortch, Secretary, Federal Communications Commission, dated June 18, 2004 ("AT&T Ex Parte").

incumbents from collecting access charges in the context of UNE-P. We also show that claims by several CLECs that they would suffer a "price squeeze" if Verizon were permitted to collect access charges for interexchange calls to or from UNE-P customers are not credible. As we demonstrate, nothing in AT&T's recent ex parte changes the price squeeze analysis, nor does AT&T show that granting Verizon's petition with respect to access charges would result in double or over-recovery. Finally, we demonstrate that it is especially appropriate for the Commission to forbear from its rule permitting CLECs to collect access on UNE-P since there is no impairment with respect to the provision of long distance service to end users, and thus Verizon may not be required to unbundle switching for that purpose.

(1) The TELRIC rulemaking is procedurally and conceptually distinct from this forbearance proceeding, and the Commission can rule on the merits of forbearance without deciding the outcome of the broader policy questions at issue in the general rulemaking. As an initial matter, Verizon's forbearance request extends only to the application of TELRIC to UNE-P.[2/] As Verizon has shown and the D.C. Circuit recently reiterated, UNE-P is not a UNE required by the Act.[3/] In the TELRIC rulemaking, by

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2/ Staff asked which rules Verizon is seeking forbearance from in the TELRIC portion of its petition. To clarify, Verizon seeks forbearance from the application of rules 47 C.F.R. §§ 51.501-515 to UNE-P.

3/ *United States Telecom Ass'n v. FCC*, 359 F.3d 554, 589 (D.C. Cir. 2004) ("*USTA II*") ("neither *AT&T* nor *Verizon* holds that the § 251(c)(3) nondiscrimination requirement *mandates* the combination rules the FCC promulgated under that section; rather, those cases found the nondiscrimination language . . . ambiguous and deferred to the agency's reading of it."); *see also Powell Defends Stance on Telecom Competition*, Communications Daily (May 22, 2001) (UNE-P "wasn't in the statute. It was sort of a creative combination of the Commission.").

contrast, the Commission is considering what UNE pricing rules should apply to those UNEs that *are* in fact required by the Act.

To be sure, the analysis that should lead the Commission to forbear from applying TELRIC to UNE-P would also support substantial reform of the TELRIC pricing rules for all UNEs. But it is by no means unusual for decisions made in one docket to influence the outcome of another. And that is certainly not a legitimate ground to delay or deny the relief Verizon requests here. Nor is it significant that the Commission might decide, in the TELRIC rulemaking, to reform TELRIC and thus potentially provide Verizon with relief similar to what it seeks in this forbearance proceeding. As the D.C. Circuit has recognized, the fact that issues raised in a forbearance petition may be decided in a different proceeding is not a lawful basis to deny forbearance. *See AT&T Corp. v. FCC*, 236 F.3d 729, 737-38 (D.C. Cir. 2001). "Congress has established § 10 as a viable and independent means of seeking forbearance," and thus reference to "another, very different, regulatory mechanism," such as the TELRIC rulemaking, provides "no authority" for the Commission to fail to exercise its statutory responsibilities under section 10 — even where that rulemaking might allow the petitioner to "receive much [not all] of the relief they seek."[4/] *Id.*

[4/] Similarly, a decision not to forbear would not bar the Commission from granting similar relief in the rulemaking context. *See* Memorandum Opinion and Order, *Petition of Verizon for Forbearance from the Prohibition of Sharing Operating, Installation, and Maintenance Functions Under Section 53.203(a)(2) of the Commission's Rules*, 18 FCC Rcd 23525 (2003) (denying forbearance); Report and Order, *Section 272(B)(1)'s "Operate Independently" Requirement for Section 272 Affiliates*, 19 FCC Rcd 5102 (2004) (granting same relief in rulemaking).

(2) Forbearance by the FCC from its UNE-P access charge policy would preclude the states from imposing that rule. Under section 160(e) of the Act, "a state commission may not continue to apply or enforce any provision of this Act that the Commission has determined to forbear from applying under subsection (a)." Since the FCC rules require the UNE-P carrier (rather than the incumbent) to collect both state and federal access charges, incumbents should be permitted to collect both if the Commission forbears from that rule. Specifically, in adopting the access charge prohibition, the Commission made clear that the rule required that the states, too, permit CLECs to collect (and preclude the incumbents from collecting) access charges in the context of UNE-P. *See* First Report and Order, *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, 11 FCC Rcd 15499, 15868-69, 15651, 15683, ¶¶ 729-732, 362, 365 (1996) ("*Local Competition Order*"). The Commission found that while the states would be *permitted*, under a transitional mechanism, to allow the incumbents to collect intrastate access charges for a defined interim period, "[t]hese state mechanisms must end" by certain specified dates. *Id.* at 15869 ¶ 731. And the Commission found that it was authorized to dictate whether incumbents could collect intrastate access charges pursuant to its "authority under section 251(d)(1) of the 1996 Act, and section 4(i) of the 1934 Act." *Id.* at 15869 ¶ 732.

If the Commission forbears from its access charge prohibition, the states could no longer rely on that prohibition to preclude incumbents from collecting intrastate access charges when CLECs take UNE-P, or to permit the CLEC to collect those access charges instead. Forbearance also would necessarily preempt the states from reimposing that same rule under the guise of a *state* law requirement. As the Commission has explained and the courts have repeatedly recognized, the states are "precluded from enacting or maintaining a regulation or law pursuant to state authority that thwarts or frustrates the federal regime . . . ."[5/] A state law reimposing the access charge rule would necessarily "thwart or frustrate" federal policy. Forbearance would be founded on a determination that the incumbent is the entity providing access —not the UNE-P CLEC. The public interest therefore requires that the incumbent recover the access revenues, and that the CLEC not be given the artificial, competition-distorting advantage embodied by the access charge rule. Once the Commission has correctly concluded that the federal regulatory regime requires this result, it is impossible to see how a state could reach a contrary result that would not conflict with these federal findings and with the Commission's determinations concerning what competition and the public interest require. As the Supreme Court has made clear, the Commission's "statutorily authorized" determinations "will pre-empt any state or local law that conflicts with such regulations or frustrates the purposes thereof." *City of New York v. FCC*, 486 U.S. 57, 64 (1988).

Indeed, that rule holds even though the states retain authority over intrastate access charges under sections 251(d)(3) and 261 of the Act. As the Commission itself has recognized, "[e]ven where Congress has preserved some role for the states[,] the

[5/] Report and Order and Order on Remand and Further Notice of Proposed Rulemaking, *Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers; Implementation of the Local Competition Provisions of the Telecommunications Act of 1996; Deployment of Wireline Services Offering Advanced Telecommunications* Capability, 18 FCC Rcd 16978, 17099-100 ¶ 192 (2003) ("*Triennial Review Order*"), vac'd in part, *United States Telecomm. Ass'n v. FCC*, 359 F.3d 554 (D.C. Cir. Mar. 4, 2004). *See Geier v. American Honda Motor Co.*, 529 U.S. 861, 873 (2000) (Supremacy Clause nullifies state law that conflicts with purposes and objectives of federal law).

Supreme Court has found that 'state law is nullified to the extent that it actually conflicts with federal law.'" *Triennial Review Order* at 17100 ¶ 192 n.613 (citing *Fidelity Federal Savings & Loan Assoc. v. de la Cuesta,* 458 U.S. 141, 154 (1982)).[6] And even if that were not the general rule, it is clear from the face of these two "savings" provisions themselves: Section 251(d)(3) by its terms preserves state access regulations (and other state requirements) only to the extent they are "consistent with the requirements of this section" and do not "substantially prevent implementation of the requirements of this section and the purposes of this part." 47 U.S.C. §§ 251(d)(3)(B), (C). Section 261 likewise permits state law requirements only to the extent "not inconsistent with this part or the Commission's regulations to implement this part." 47 U.S.C. § 261(c). As the Supreme Court has held, therefore, the Act by its terms illustrates Congress's intention to "tak[e] the regulation of local telecommunications competition away from the States," and the Commission may therefore "draw the lines to which [the states] must hew," lest the industry fall into the "surpassing strange" incoherence of "a federal program administered by 50 independent state agencies" without adequate federal oversight. *AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 378 n.6 (1999).

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[6] As the Commission has clarified, since the Commission "is charged with implementing the Act and its purposes are fully consistent with the Act's purposes," a law that conflicts with the Commission's regulatory scheme is preempted as much as one that conflicts the provisions of the Act itself. *Triennial Review Order* at 17100 ¶ 193 n.614.

(3) Claims by AT&T, MCI and others that granting the access charge portion of Verizon's petition would create a price squeeze[7/] are demonstrably false. Staff has requested that Verizon provide an analysis using the same basic methodology that Verizon used in its 271 cases, which compared the difference between Verizon's average retail revenue per line[8/] and the average per-line cost to a CLEC for a UNE-P, and adjust that comparison to reflect the impact of granting Verizon's petition with respect to access charges. That analysis, which is provided in Attachment A, illustrates that, in four of the five states that have the most UNE-P lines where Verizon is the incumbent, a CLEC taking UNE-P would have gross margins of 50 percent or more. This is well over the $10 per line that AT&T and MCI have estimated as the internal costs of an efficient competitive carrier;[9/] indeed, in most cases it is nearly twice that amount. Moreover, as

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7/ *See, e.g.,* AT&T Ex Parte (June 18, 2004) at 8-9; AT&T Ex Parte (Feb. 25, 2004); MCI Comments at 8-9, 12; MCI Reply Comments at ; Pace Coalition Ex Parte (March 3, 2004). AT&T focuses its price squeeze analysis on the TELRIC portion of Verizon's petition, rather than the access charge portion, but typically does refer to access charge revenues in making its price squeeze arguments. *See, e.g.,* AT&T Ex Parte, "UNE-P v. 271 LD Entry" at 3 ("UNE-P Associated Revenue") (Sept. 24, 2002).

8/ The retail revenues included in this analysis are those earned by the Verizon ILEC in each state: "Local/SLC" includes local dialtone and usage, plus the SLC; "Toll" includes the toll services provided by the Verizon ILEC (intraLATA toll plus corridor services); "Access" includes inter- and intrastate access charges, including access charges paid by Verizon's long distance company when it provides interLATA and other toll services; "Other" includes a variety of miscellaneous revenues such as features and operator services. As noted below, we make an adjustment with respect to access revenues for purposes of the analysis we submit here.

9/ *See, e.g.,* Declaration of Steve Bickley on Behalf of AT&T Corp. ¶¶ 2-3, *attached as* Exhibit B to Comments of AT&T Corp., *Application by BellSouth Corporation Pursuant to Section 271 of the Telecommunications Act of 1996 to Provide In-Region, InterLATA Services in Alabama, Kentucky, Mississippi, North Carolina, and South Carolina*, WC Docket No. 02-150 (filed July 11, 2002); Comments of WorldCom, Inc., *Application by BellSouth Corporation, BellSouth Telecommunications, Inc. and BellSouth Long Distance, Inc., for Provision of In-Region, InterLATA Services in* discussed further below, nearly all of the UNE-P that AT&T and MCI purchase is used to sell bundles of services at rates that exceed the Verizon retail revenue used in this analysis.[10/] As a result, CLECs' real gross margin is even greater than that shown in Attachment A. It is clear, therefore, that no price squeeze would exist.

Attachment A contains Staff's requested analysis for five states that have the most UNE-P lines where Verizon is the incumbent.[11/] As noted, the analysis uses the same methodology as Verizon presented in connection with many of its applications for long distance authority, showing that price squeeze claims there were without merit.[12/]

Alabama, Kentucky, Mississippi, North Carolina, and South Carolina, WC Docket No. 02-150 at 19-20 (filed July 11, 2002). *See also* Memorandum Opinion and Order, *Application by Verizon New England Inc., Verizon Delaware Inc., et al., for Authorization To Provide In-Region, InterLATA Services in New Hampshire and Delaware*, 17 FCC Rcd 18660, 18748 ¶ 157 (2002) ("*NH/DE 271 Order*") (Commission noted claims by AT&T and MCI that potential margins must exceed their internal costs of more than $10.00 per line, but stated that relevant inquiry was sufficient profit margin for an efficient competitor).

10/ *See "AT&T Plans a Vonage-style Consumer VoIP Service,"* Converge Network Digest, Sept. 9, 2003, http://www.convergedigest.com/Bandwidth/newnetworksarticle.asp?ID=8669 (reporting that AT&T Chairman and CEO David Dorman told analysts that 90 percent of UNE-P customers choose a bundle of local plus long distance services); Huyard, W. (MCI Chief Operating Officer), *"Using UNE-P to develop a strong and profitable local presence,"* Speech to Goldman-Sachs Telecom Issues Conference, May 7, 2002, http://www.sbc.com/Large-Files/CA-LD/Appendix_A/Smith_J_G/Smith_J_G_Affidavit_Attachment_K.pdf (more than 80 percent of MCI's new customers buy a bundle of local and long distance services).

11/ These states are Maryland, Massachusetts, New Jersey, New York, and Pennsylvania. Verizon did not include Virginia in this analysis, because, as explained in an Verizon's May 20, 2004 ex parte, Verizon suggests that forbearance for Virginia be conditioned on Verizon's submission and any necessary regulatory approval of a proposal to identify the traffic sensitive costs that should be removed from the flat-rated port charge ordered by the Wireline Competition Bureau while it remains in effect.

12/ *See, e.g., NH/DE 271 Order*, 17 FCC Rcd at 18741-51 ¶¶ 142-162; Memorandum Opinion and Order, *Application by Verizon New Jersey Inc. for Authorization To Provide*

Specifically, for each state, Verizon first determined the average retail revenue per line. As noted above, the revenue per line reflects a composite of the revenues the Verizon ILEC receives from its residential and business customers for local services, including the SLC, intraLATA toll services, access services, and other services (such as features) based on 2003 revenues. Verizon then adjusted the retail revenue to remove the per-line equivalent of flat-rated transport revenues that it retains when a line is converted to UNE-P; since this portion of the retail revenue is not available to the CLEC, it is appropriate to exclude it from the retail revenues to which the CLEC's UNE-P costs are compared.[13/]

Second, Verizon determined the UNE-P costs using the UNE rates that are actually in effect.[14/] As it did in the analyses it presented in its 271 applications, Verizon calculated the switching costs by applying the UNE switching rates to the average number of Dial Equipment Minutes for each state as reported in ARMIS.[15/] The minutes were spread among types of usage (interstate, intrastate, and local calling) according to

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In-Region, InterLATA Services in New Jersey, 17 FCC Rcd 12275, 12359-62 ¶¶ 169-175 (2002); Memorandum Opinion and Order, *Application by Verizon New England Inc. for Authorization To Provide In-Region, InterLATA Services in Vermont,* 17 FCC Rcd 7625, 7661-65 ¶¶ 65-73 (2002).

13/ These transport services are not the subject of Verizon's forbearance petition. Rather, they reflect payments from interexchange carriers to Verizon for dedicated transport between the IXC's POP/POP serving wire center and Verizon's tandem or end office switch to or from which traffic is handed off. Although Verizon is losing access lines to UNE-P carriers, Verizon continues to provide dedicated transport to the interexchange carriers (in those cases where the carriers choose to purchase service from Verizon rather than using their own facilities or other alternatives). Verizon calculated the per-line amount represented by that access revenue.

14/ Verizon included charges for Loop; Port; Switching (including transport); and Other, such as features and operator services.

15/ As the Commission is aware, Verizon and other ILECs were not required to report DEMs after 2000. As a result, Verizon used reported 2000 minutes in its calculations.

average call patterns for each state.[16] Finally, Verizon determined the effect of granting the access charge portion of its petition. The "Forbearance Access Adjustment" is the per-line net impact of two components — (1) the reduced amount the CLEC would pay for UNE switching (because it would no longer pay per-minute charges for access minutes) and (2) the per-minute usage-related switched access revenue that would no longer be available to CLECs because it would be collected by Verizon if its petition is granted.[17] The "Forbearance Access Adjustment" is shown in Attachment A as an adjustment to the UNE-P cost.

Verizon then compared the adjusted ILEC retail revenue per line with the adjusted UNE-P cost per line to develop the gross margin — both as a dollar amount and as a percentage of the retail revenue. As shown in Attachment A, the gross margin in each state is more than sufficient to cover an efficient CLEC's own additional costs of offering service using UNE-P. In Massachusetts, CLECs would have a per UNE-P gross margin of **[BEGIN PROPRIETARY]** **[END PROPRIETARY]**; in Maryland, the gross margin would be **[BEGIN PROPRIETARY]** **[END PROPRIETARY]**. In New York, it would be **[BEGIN PROPRIETARY]**

[16] The Commission described this methodology in the *NH/DE 271 Order* ¶ 45: "State-approved rates for end office switching and transport are imposed on a MOU basis. We develop the per-line per-month overall demand for these usage-sensitive rate elements . . . by first dividing total state-specific switched access lines into state-specific total annual MOU, based on dial equipment minutes (DEM), divided by 12 months. We then apply to each of the usage sensitive rate elements a percentage of this overall demand that is based on state-specific traffic assumptions supplied by Verizon regarding originating versus terminating, local intra-switch versus inter-switch, and tandem-routed versus direct-routed MOU."

[17] This amount is calculated in the data Verizon submitted on June 15, 2004 in support of the Declaration of Patrick A. Garzillo, filed on May 20, 2004.

[END PROPRIETARY], while in New Jersey, it would be **[BEGIN PROPRIETARY]** **[END PROPRIETARY]**. Of the five states, the per month per UNE-P gross margin would be lowest in Verizon's former Bell Atlantic Pennsylvania (East) service area, and even there it is **[BEGIN PROPRIETARY]** **[END PROPRIETARY]**.

It is true that CLECs will incur marketing and other internal costs that would have to be deducted to determine the net margin for their retail services. As noted above, AT&T and MCI have estimated that their internal costs are on the order of $10 per line, and the costs of an "efficient" CLEC likely would be lower (and, because they have no network to operate, may be substantially so).[18/] Accordingly, UNE-P carriers enjoy substantial margins even after taking into account their own estimates of the internal costs they would incur.

Moreover, this analysis does not take into account all of the revenues that are available to UNE-P carriers. As AT&T notes, the Commission has concluded that price squeeze analyses must take into account the fact that a competitive carrier using UNE-P can also earn interLATA and intraLATA toll revenues. AT&T Ex Parte at 8-9. As noted above, nearly all of the UNE-P that AT&T, MCI, and other CLECs purchase is used to offer bundles of local and long distance services at monthly rates that significantly exceed the adjusted retail revenues shown in Attachment A. For example, Attachment B sets out on a state-by-state basis the prices that AT&T, which is the largest user of UNE-

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[18/] *See NH/DE 271 Order* ¶ 157 (providing examples of competitive LECs entering the local telephone market "even where they allege that the available margins are less than $10"; noting MCI data filed in another 271 proceeding "show[ing] that it has decided to enter markets where it will achieve a 'minimally acceptable' UNE-Platform margin that is substantially lower than $10 and falls between $5 and $7").

P arrangements, charges its own customers for the bundled service offering it markets using the UNE platform. These prices were taken from AT&T's web site and, for each of the five states included in the analysis in Attachment A, are significantly above Verizon's average retail revenue per line.[19/] Other CLECs also offer bundles of services at rates comparable to AT&T's.[20/] As shown in Attachment B, the UNE-P carriers enjoy even larger gross margins on the bundled offerings that have been the focus of their marketing efforts. For example, the gross margins shown in Attachment B (based on 2000 minutes per month) for the Verizon states with the most UNE-P lines are $45.08 (New York), $40.80 (Maryland), $38.71 (Massachusetts), $31.01 (New Jersey), and $36.15 (Pennsylvania).

As noted above, the UNE-P carriers do incur some internal costs in order to offer their services, which AT&T has estimated are on the order of $10. The UNE-P carriers also have argued elsewhere that, in addition to these internal costs, they incur other costs, such as long distance costs, where they offer bundled service offerings. And in its June 18 Ex Parte, AT&T argues that granting the access portion of Verizon's forbearance petition would "radically alter UNE-P carriers' costs." Ex Parte at 9. But even assuming that competitive carriers' costs for their bundled offerings were 50 to 100 percent higher

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19/ The UNE-P rates included in Attachment B are based on a widely used report compiled by the West Virginia consumer advocate and were computed using two standard minute of use assumptions (1,000 minutes per month and 2,000 minutes per month).

20/ *See, e.g.*, "The Neighborhood Calling Packages," http://consumer.mci.com/compare_plans.jsp (Neighborhood Complete package priced between $49.99 and $69.99, depending on state); https://www.getpva.com/eloa/ZLineHomeUnlimited.do (Z-Tel's ZlineHome Unlimited starting at $49.99).

(i.e., as much as $20), they still would enjoy substantial margins. In fact, as Attachment B demonstrates, they still would enjoy margins that typically are $10 to $20 or more per line *after* subtracting their additional internal costs. And this is equally true in the case of the Verizon states where they have the most UNE-P lines.

In order to account for both the additional inter- and intraLATA toll revenues competitive carriers can earn and for the reduced access revenues the competitive carrier would earn,[21] Verizon compared the bundled rates shown on Attachment B ("Monthly Rate + Line Charge") to the adjusted UNE-P costs shown on Attachment A ("Total UNE-P"). When the adjusted UNE-P costs are subtracted from AT&T's bundled rates, the gross margin in Massachusetts would be **[BEGIN PROPRIETARY]** **[END PROPRIETARY]**; in Maryland, the gross margin would be **[BEGIN PROPRIETARY]** **[END PROPRIETARY]**. In New Jersey, the gross margin would be **[BEGIN PROPRIETARY]** **[END PROPRIETARY]**; in New York, it would be **[BEGIN PROPRIETARY]** **[END PROPRIETARY]**; and in Pennsylvania (former Bell Atlantic service area), it would be **[BEGIN PROPRIETARY]** **[END PROPRIETARY]**. Even if AT&T's internal costs were $20 per line, subtracting that amount from these gross margins would leave *profit* margins ranging from more than

[21] As discussed above, Verizon's analysis in Attachment A reflects *both* the reduced UNE switching charges that a CLEC would pay (since it would no longer pay per-minute switching charges on access minutes), *and* the access revenues it would no longer receive if Verizon were permitted to collect per-minute switched access charges on calls to or from UNE-P customers. AT&T claims that granting Verizon's petition would "force UNE-P carriers to pay originating access charges for toll calls initiated by their customers." AT&T Ex Parte at 9. This is wrong. The interexchange carrier carrying the toll call would pay originating access charges to Verizon. Verizon's analysis takes this into account.

$13.00 to approximately $22.00 per line. Clearly, therefore, no price squeeze would exist.

(4) AT&T's attempt, in its recent ex parte, to show that forbearance from the access charge rule would result in double or over-recovery by Verizon is easily dismissed. The bulk of AT&T's argument rests on the erroneous statement that states "increasingly require the use of *fixed* UNE port charges to recover [switching] costs . . . ." AT&T June 18 Ex Parte at 5. But that is not true in Verizon's case: Leaving aside the Bureau's decision with respect to Virginia, none of the states in which Verizon provides service as an incumbent require Verizon to recover all UNE switching costs through a flat rated charge. As to Virginia, Verizon has proposed that "the Commission's forbearance order . . . make clear that in Virginia, forbearance is conditioned on Verizon's submission (and any necessary regulatory approval) of a proposal to identify the traffic sensitive costs that should be removed from the UNE-P port charge in connection with the access minutes for which Verizon would receive access charges."[22/]

Nor is there any merit to AT&T's effort to show over-recovery where usage sensitive UNE switching rates are in place. AT&T provides an illustration showing that, if Verizon is collecting only UNE switching charges and no access charges, it would, under AT&T's assumptions, collect $4.68, whereas if it could also collect the access charges, it would collect more — $9.18, according to AT&T. *See* AT&T June 18 2004 Ex Parte at 6. AT&T's claim that Verizon would collect $4.50 more per line is blatantly untrue — as Verizon has already demonstrated, the per-line revenue impact is about

[22/] *See* Verizon May 20 Ex Parte at 7 n.9.

$0.80 per UNE-P per month. *Garzillo Decl.* ¶ 16. And AT&T is patently incorrect in suggesting that this means the CLEC is paying 96% more for switching. As Verizon has shown, the CLEC's switching cost has actually *dropped*, because the CLEC pays nothing for toll minutes on the switch. And while the CLEC will earn less revenues because it does not collect access charges, as we have just shown, the CLEC will still enjoy a healthy margin.

(5) Finally, as Verizon previously has explained in detail,[23] UNE-P itself is not a requirement of the Act and the Commission has ample authority to grant forbearance from the access charge rule. Likewise, we previously have explained why section 10(d) poses no impediment to granting that relief. While we will not belabor those arguments again here, there is one point that warrants brief discussion in light of the D.C. Circuit's decision in *USTA II.*

Specifically, forbearance is especially warranted in the case of the Commission's access charge rule because there is no plausible basis for finding that competition for long distance services is impaired without access to UNE switching at TELRIC to originate or terminate long distance calls. On the contrary, the extensive competition in long distance services generally, as well as the extensive competition from cable, wireless, and VoIP providers who originate and terminate long distance traffic without using ILECs' circuit switches, demonstrates that competitors are not impaired from providing end users with access to long distance services without unbundled switching or the UNE-P. And this is

[23] *See, e.g.*, Petition for Expedited Forbearance at 12-18 (filed Jul 3, 2003); Reply Comments of Verizon, at 21-31 (filed Sept. 2, 2003); Letter from Donna Epps, Verizon, to Marlene Dortch, Secretary, FCC, WC Docket No. 03-157, at 7-13 (filed May 20, 2004).

true regardless of what conclusion the Commission may reach with respect to unbundled switching and the UNE-P generally. Accordingly, the Commission cannot require Verizon to provide access to unbundled switching for that purpose. And, of course, section 10(d)'s limitation on forbearance from the "requirements of section 251(c)" therefore would not apply to unbundled switching for exchange access for this additional reason as well.

In *Competitive Telecommunications Assoc. v. FCC*, 309 F.3d 8, 13 (2002) ("*CompTel*"), the D.C. Circuit upheld the Commission's determination that the impairment standard is properly applied on service-specific basis, and that any unbundling requirements must be "keyed to a specific 'service' of the requesting carriers." This is because, as the court and the Commission noted, section 251(d)(2) permits the Commission to "consider the markets in which a competitor 'seeks to offer' services and, at an appropriate level of generality, ground the unbundling obligation on the competitor's entry into those markets in which denial of the requested elements would in fact impair the competitor's ability to offer services." *Id.* (citation omitted). Accordingly, given the express terms of the statute, the Court emphasized that "it is far from obvious . . . that the FCC has the power, without an impairment finding as to nonlocal services, to require that ILECs provide EELs for such services on an unbundled basis." 309 F.3d at 14.

In *USTA II*, the D.C. Circuit emphatically reaffirmed its holding in *CompTel* that that the Commission appropriately has determined whether competition would be impaired for specific services, such as long distance or wireless, and that that there is no basis for finding impairment where competition has thrived without UNEs. As the Court explained, in *CompTel*, "[w]e held that the Commission acted reasonably in disaggregating the *impairment* issue, and in ordering unbundling only with respect to the service for which it found impairment." 359 F.3d at 591-92; *see also id.* at 575 (holding that the Commission had "failed to conduct the requisite impairment analysis for wireless providers"). The Court also pointedly noted that there is "no evidence suggesting that [carriers] are impaired with respect to the provision of long distance services." *Id.* at 592. On the contrary, in discussing the special access services that IXCs use to serve their customers, the Court held that "competitors cannot generally be said to be impaired by having to purchase special access services from ILECs, rather than leasing the necessary facilities at UNE rates, where robust competition in the relevant markets belies any suggestion that the lack of unbundling makes entry uneconomic." *Id.*; *see also id.* at 575 ("wireless carriers' reliance on special access has not posed a barrier that makes entry uneconomic").

Applying the "requisite impairment analysis" to the long distance market shows that there is no "impairment" with respect to that market that would support a requirement that incumbents provide CLECs with unbundled switching or UNE-P for long distance traffic. The long distance market is already marked by robust competition, much of which is intermodal competition that bypasses the PSTN entirely and thus does not use UNE-P at all.

Wireless providers compete with wireline carriers in two respects, both for lines and for minutes. From December 1999 to June 2003, the number of wireless subscribers in the former Bell Atlantic jurisdictions has more than doubled, from 16,891,215 to

35,442,248.[24/] And while wireless services increasingly are competing for and winning lines from wireline carriers, as shown above, the competition from wireless carriers for minutes is even more intense. This is especially true when it comes to long distance services. Industry analysts have noted that the bundled local and long distance calling plans that wireless carriers increasingly offer have "directly contributed to wireline traffic substitution . . . ."[25/] and are "displac[ing] traditional long distance calling . . . ."[26/] Indeed, one analyst estimates that U.S. households currently make 43% of their long-distance calls on wireless phones.[27/] Interexchange carriers have expressly acknowledged the threat from this intermodal competition in their financial reports.[28/]

24/ *Id.* at Table 5.

25/ S. Ellison, IDC, *U.S. Wireless Displacement of Wireline Access Lines, Forecast and Analysis, 2003-2007* at 7 (Aug. 2003).

26/ J.D. Power and Associates Press Release, *J.D. Power and Associates Reports: Customer Satisfaction Increases as Stiff Rate Competition and Bundling Causes Steep Drops in Long Distance Spending* (July 1, 2003) (*quoting* Steve Kirkeby, senior director of telecommunication research, J.D. Power and Associates), *at* http://www.jdpa.com/pdf/2003047.pdf. *See also* J. Bazinet, *et al.*, JP Morgan, *U.S. Telecommunications: The Art of War* at 13 (Nov. 7, 2003) ("In total, consumers have reduced the number of long-distance minutes of use per landline by 40% over the past five years. We think the source of the decline is that consumers are increasingly using fixed priced wireless plans to make 'free' long-distance voice calls. . . . We expect this trend to continue in the residential market. . . .")

27/ Yankee Group News Release, *U.S. Consumer Long Distance Calling Is Increasingly Wireless, Says Yankee Group* (Mar. 23, 2004), *at* http://www.yankeegroup.com/public/news-releases/news_release_detail.jsp?ID=PressReleases/news_03232004_cts.2.htm.

28/ AT&T admits that "consumer long distance voice usage is declining as a result of substitution to wireless services . . . ." AT&T Corp., Form 10-K at 2 (SEC filed Mar. 15, 2004). Similarly, MCI explains that its "competitors include...wireless telephone companies, such as Verizon Wireless, Cingular, Sprint PCS, AT&T Wireless, Nextel and T-Mobile, which have . . . gained market share from providers of wireline voice communications . . . ." MCI Inc., Form 10-K at 22 (SEC filed Apr. 29, 2004).

These reports are confirmed by reported traffic volumes. For example, the Commission's own data show that traditional wireline toll minutes are declining rapidly for the industry as a whole — from a peak of 149 for the average household per month in 1997, down to only 90 in 2002.[29]

Average Wireline Residential Monthly Toll Minutes (excluding wireless)

1995	1996	1997	1998	1999	2000	2001	2002
143	143	149	144	131	116	105	90

Source: Industry Analysis & Technology Division, Wireline Competition Bureau, *Statistics of the Long Distance Telecommunications Industry* at Table 20 (May 2003) (includes: IntraLATA-Intrastate, InterLATA-Intrastate, IntraLATA-Interstate, InterLATA-Interstate, International, Others (toll-free mins. billed to residential customers, 900 mins., and mins. for calls that could not be classified)).

Verizon's total switched access minutes of use have steadily declined approximately 7.7 percent between the first and fourth quarters of 2003, and by approximately 12 percent compared to the levels for the same quarters of 2002.[30] As noted above, this is largely driven by the fact that end users are increasingly using wireless and VoIP services for their long distance calls, neither of which rely on the incumbents' network (or UNEs) for exchange access. In contrast to the trend in wireline minutes, wireless carriers have seen their total minutes of use, as well as their average minutes per subscriber, increase several fold since 2000.

29/ Industry Analysis & Technology Division, Wireline Competition Bureau, *Statistics of the Long Distance Telecommunications Industry* at 35-36 & Table 20 (May 2003).

30/ *See* Letter from Dee May, Vice President, Federal Regulatory, Verizon, to Marlene Dortch, Secretary, FCC, Re: Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements, WC Docket No. 02-112 (filed May 19, 2004) at 2 & Table 3.

Wireless Use

	Analyst	2000	2001	2002	2003	2004E
Wireless MOUs (in billions)	Thos. Weisel Partners (Apr. 2004)	259	457	620	803	1,052
	Merrill Lynch (Mar. 2004)	259	456	620	837	1,054
Monthly MOUs per Subscriber	Thos. Weisel Partners (Apr. 2004)	221	320	384	444	525

Sources: N. Zachar, *et al.*, Thomas Weisel Partners, *Wireless Carrier Consolidation: Setting the Record Straight for the Tower Industry* at 3, Fig. 1 & at 4, Fig. 2 (Apr. 6, 2004); D. Janazzo, *et al.*, Merrill Lynch, *The Next Generation VIII: The Final Frontier?* at 42, Table 33 (Mar. 15, 2004).

VoIP providers also are increasingly displacing traditional wireline long distance: In the first quarter of 2004, each of the six major cable operators — whose networks reach 85 percent of U.S. households — has either begun commercial deployment of VoIP telephony service, or has announced aggressive plans to do so imminently.[31/]

[31/] J. Halpern, *et al.*, Bernstein Research Weekly Notes, *US Telecom and Cable: Faster Rollout of Cable Telephony Means More Risk for RBOCs, Faster Growth for Cable,* at Exh. 1 (Jan. 9, 2004) at 3 ("Nearly every major cable MSO has indicated over the past month that it will offer cable telephony service to every, or nearly every, household in its footprint by 2005, with Time Warner Cable and Cablevision targeting year-end 2004"); G. Campbell, *et al.*, Merrill Lynch, *3Q03 Broadband Update: The Latest on Broadband Data and VoIP Services in the U.S. and Canada,* at 9 (Nov. 3, 2003) ("In the third quarter, all of the major cable operators continued to push ahead with their VoIP plans and deployments"); G. Campbell, *et al.*, Merrill Lynch, *Everything over IP: VoIP and Beyond*, at 17 (Mar. 12, 2004) (Charter will deploy VoIP to 1 million homes by year-end 2004).

Each of these major cable operators also has concentrations of customers in Verizon's local service areas. For example, Cablevision already offers voice telephone service using VoIP to 100 percent of its 4 million cable homes passed in metropolitan New York and New Jersey. *March 2004 Broadband Update* at 13 (attachment to Letter from Dee May, Verizon to Marlene Dortch, FCC, CC Docket Nos. 01-337, 01-338 and WC Docket Nos. 02-33 and 02-52 (filed March 26, 2004)). Time Warner has already deployed VoIP in seven of its markets, and is "on track" to deploy service to "essentially all" of its cable systems – which pass a total of 18 million homes – "by the end of 2004." Time Warner News Release, *Time Warner Reports First Quarter 2004 Results* (Apr. 28, 2004) at 5 *at* http://www.timewarner.com/investors/quarterly_earnings/

Furthermore, consumers with access to *any* broadband connection can use VoIP from multiple providers, and thus avoid using their narrowband wireline service for any long distance calling. Between 85 and 90 percent of U.S. households are now able to obtain a broadband connection from a provider other than their incumbent local telephone company.[32]

Plainly, there is no "reasonable basis" for "thinking that competition" for long distance services "is suffering from [] impairment." *USTA I*, 290 F.3d at 422. Accordingly, the provision of unbundled switching or UNE-P for that service cannot be "required" under section 251(c). There accordingly is no justification for the Commission to allow the CLEC to collect access charges in connection with the exchange access the incumbents provide when the CLECs' customers make long distance calls. Furthermore, given that the incumbents already are losing a significant percentage of access charges even outside of the UNE-P context as a result of the intermodal competition described above, any such rule also is directly contrary to the public interest and basic principles of competitive neutrality.

Because UNE switching or the UNE-P for the provision of exchange access cannot lawfully be required under section 251(c) of the Act, an incumbent cannot be

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2004_1q/pdf/release.pdf. Comcast has told analysts it will have half of its 39 million homes passed "VoIP ready" by year-end 2004 and 95-percent VoIP ready by year-end 2005. John R. Alchin, Executive Vice President and Co-CFO, Comcast, Presentation to Bear Stearns 17th Annual Media, Entertainment and Information Conference at 16 (Mar. 9, 2004), *at* http://media.corporate- ir.net/media_files/irol/11/118591/presentations/ cmcsa_030904/sld001.htm.

[32] *See* NCTA, *Broadband Services*, *at* http://www.ncta.com/Docs/ PageContent.cfm?pageID=37; *see also* J. Halpern, *et al.*, Bernstein Research Call, *Broadband Update: DSL Share Reaches 40% of Net Adds in 4Q . . . Overall Growth Remains Robust,* at 7, Exhibits 1 & 6 (Mar. 10, 2004) (cable broadband available to 92.3 percent of total cable homes passed).

required to provide unbundled switching for that purpose under state law, as well. As the Commission noted in the *Triennial Review Order* at 17101 ¶ 195, "If a decision pursuant to state law were to require the unbundling of a network element for which the Commission has either found no impairment — and thus has found that unbundling that element would conflict with the limits in section 251(d)(2) — or otherwise declined to require unbundling on a national basis, we believe it unlikely that such decision would fail to conflict with and "substantially prevent" implementation of the federal regime, in violation of section 251(d)(3)(C)." As a result, states would be preempted from constructively requiring the unbundling of switching for exchange access by directing that CLECs retain intrastate access revenues in connection with the exchange access IXCs use when serving UNE-P-based end users.

Sincerely,

Donna Epps
JKC

Donna Epps

Attachments

cc: Tamara Preiss
Steve Morris
Julie Saulnier
Jeremy Marcus

ATTACHMENT A

REDACTED

ATTACHMENT B

AT&T's One Rate USA^{sm} Plan Availability

Includes unlimited local and long distance calling, choice of 4 calling features at one flat monthly rate.

(Grouped by Monthly Rate.)

	State	One Rate USA^{sm} Monthly Rate[A]	Monthly FCC Line Charge (1/04))[B]	Monthly Rate + Line Charge	UNE-P @1,000 MOU[C]	Margin (Rate-UNE-P @1000)	UNE-P @2,000 MOU[C]	Margin (Rate UNE-P @ 2000)	Margin Difference b/w 2000 and 1000 MOU
1	Kentucky	$ 59.95	$ 6.50	$ 66.45	$ 19.61	$ 46.84	$ 20.81	$ 45.64	$ (1.20)
2	Mississippi	$ 59.95	$ 6.50	$ 66.45	$ 24.63	$ 41.82	$ 25.66	$ 40.79	$ (1.03)
3	Montana	$ 59.95	$ 6.50	$ 66.45	$ 26.87	$ 39.58	$ 28.44	$ 38.01	$ (1.57)
4	South Carolina	$ 59.95	$ 6.50	$ 66.45	$ 18.69	$ 47.76	$ 19.74	$ 46.71	$ (1.05)
5	Alabama	$ 54.95	$ 6.50	$ 61.45	$ 18.51	$ 42.94	$ 19.21	$ 42.24	$ (0.70)
6	Delaware	$ 54.95	$ 6.48	$ 61.43	$ 16.18	$ 45.25	$ 18.10	$ 43.33	$ (1.92)
7	Florida	$ 54.95	$ 6.50	$ 61.45	$ 15.89	$ 45.56	$ 16.66	$ 44.79	$ (0.77)
8	Louisiana	$ 54.95	$ 6.50	$ 61.45	$ 19.47	$ 41.98	$ 21.34	$ 40.11	$ (1.87)
9	Maine	$ 54.95	$ 6.45	$ 61.40	$ 18.81	$ 42.59	$ 20.49	$ 40.91	$ (1.68)
10	New Hampshire	$ 54.95	$ 6.45	$ 61.40	$ 19.36	$ 42.04	$ 21.80	$ 39.60	$ (2.44)
11	New York	$ 54.95	$ 6.45	$ 61.40	$ 15.19	$ 46.21	$ 16.32	$ 45.08	$ (1.13)
12	North Carolina	$ 54.95	$ 6.50	$ 61.45	$ 17.96	$ 43.49	$ 19.86	$ 41.59	$ (1.90)
13	Northern Nevada	$ 54.95	$ 5.39	$ 60.34	$ 23.07	$ 37.27	$ 24.68	$ 35.66	$ (1.61)
14	Rhode Island	$ 54.95	$ 6.45	$ 61.40	$ 17.07	$ 44.33	$ 18.35	$ 43.05	$ (1.28)
15	Tennessee	$ 54.95	$ 6.50	$ 61.45	$ 16.62	$ 44.83	$ 17.42	$ 44.03	$ (0.80)
16	Vermont	$ 54.95	$ 6.45	$ 61.40	$ 19.44	$ 41.96	$ 23.44	$ 37.96	$ (4.00)
17	West Virginia	$ 54.95	$ 6.50	$ 61.45	$ 24.56	$ 36.89	$ 27.11	$ 34.34	$ (2.55)
18	North Dakota	$ 53.95	$ 6.50	$ 60.45	$ 19.03	$ 41.42	$ 20.51	$ 39.94	$ (1.48)
19	Georgia	$ 49.95	$ 6.50	$ 56.45	$ 14.33	$ 42.12	$ 14.94	$ 41.51	$ (0.61)
20	Idaho	$ 49.95	$ 6.50	$ 56.45	$ 22.89	$ 33.56	$ 24.23	$ 32.22	$ (1.34)
21	Iowa	$ 49.95	$ 4.92	$ 54.87	$ 18.65	$ 36.22	$ 20.21	$ 34.66	$ (1.56)
22	Maryland	$ 49.95	$ 5.77	$ 55.72	$ 13.75	$ 41.97	$ 14.92	$ 40.80	$ (1.17)
23	Massachusetts	$ 49.95	$ 6.45	$ 56.40	$ 16.92	$ 39.48	$ 17.69	$ 38.71	$ (0.77)
24	Missouri	$ 49.95	$ 5.27	$ 55.22	$ 19.27	$ 35.95	$ 21.46	$ 33.76	$ (2.19)
25	Nebraska	$ 49.95	$ 5.07	$ 55.02	$ 17.77	$ 37.25	$ 27.25	$ 27.77	$ (9.48)
26	New Jersey	$ 49.95	$ 6.31	$ 56.26	$ 12.61	$ 43.65	$ 13.79	$ 42.47	$ (1.18)
27	New Mexico	$ 49.95	$ 6.50	$ 56.45	$ 21.01	$ 35.44	$ 25.44	$ 31.01	$ (4.43)
28	Oregon	$ 49.95	$ 6.50	$ 56.45	$ 17.47	$ 38.98	$ 18.80	$ 37.65	$ (1.33)
29	Pennsylvania	$ 49.95	$ 6.10	$ 56.05	$ 18.19	$ 37.86	$ 19.90	$ 36.15	$ (1.71)
30	South Dakota	$ 49.95	$ 6.50	$ 56.45	$ 21.38	$ 35.07	$ 22.08	$ 34.37	$ (0.70)
31	Utah	$ 49.95	$ 6.50	$ 56.45	$ 15.58	$ 40.87	$ 17.21	$ 39.24	$ (1.63)
32	Virginia	$ 49.95	$ 6.37	$ 56.32	$ 17.26	$ 39.06	$ 17.26	$ 39.06	$ -
33	Washington	$ 49.95	$ 6.10	$ 56.05	$ 16.72	$ 39.33	$ 17.90	$ 38.15	$ (1.18)
34	Wyoming	$ 49.95	$ 6.50	$ 56.45	$ 26.95	$ 29.50	$ 27.87	$ 28.58	$ (0.92)
35	Arkansas	$ 48.95	$ 5.27	$ 54.22	$ 16.54	$ 37.68	$ 18.38	$ 35.84	$ (1.84)
36	Illinois	$ 48.95	$ 4.50	$ 53.45	$ 11.99	$ 41.46	$ 11.99	$ 41.46	$ -
37	Indiana	$ 48.95	$ 5.53	$ 54.48	$ 15.10	$ 39.38	$ 15.10	$ 39.38	$ -
38	Kansas	$ 48.95	$ 5.27	$ 54.22	$ 17.49	$ 36.73	$ 19.33	$ 34.89	$ (1.84)
9	Michigan	$ 48.95	$ 5.35	$ 54.30	$ 13.36	$ 40.94	$ 13.88	$ 40.42	$ (0.52)
40	Ohio	$ 48.95	$ 5.39	$ 54.34	$ 12.46	$ 41.88	$ 13.30	$ 41.04	$ (0.84)
41	Oklahoma	$ 48.95	$ 5.27	$ 54.22	$ 19.35	$ 34.87	$ 21.61	$ 32.61	$ (2.26)
42	Texas	$ 48.95	$ 5.27	$ 54.22	$ 18.63	$ 35.59	$ 20.21	$ 34.01	$ (1.58)
43	Wisconsin	$ 48.95	$ 5.07	$ 54.02	$ 13.01	$ 41.01	$ 13.01	$ 41.01	$ -
44	Arizona	$ 43.95	$ 6.50	$ 50.45	$ 15.53	$ 34.92	$ 16.50	$ 33.95	$ (0.97)
45	Minnesota	$ 43.95	$ 5.05	$ 49.00	$ 15.98	$ 33.02	$ 15.98	$ 33.02	$ -
46	California	$ 41.95	$ 4.49	$ 46.44	$ 11.39	$ 35.05	$ 12.13	$ 34.31	$ (0.74)
47	Alaska[D]		$ 6.50		$ 25.79				
48	Colorado		$ 6.50		$ 18.61		$ 20.22		
49	Connecticut		$ 5.78		$ 19.38		$ 22.96		
50	DC		$ 3.87		$ 13.04		$ 16.04		
51	Hawaii[E]		$ 6.50						

A) Source: AT&T website. Updated rates as of 3/10/04

B) Source: B.J. Gregg Analysis, Appendix 2, January 2004

C) Source: B.J. Gregg Analysis, Appendix 3, page 1, as of January 2004.

D) B.J. Gregg analysis includes only 1000 mou.

E) No state wide average provided for Hawaii, only individual rates on three islands included

NOTE: Includes 11 additional states entered by AT&T as well as updated rate changes to One Rate USA

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