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September 29, 2004

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Ex Parte

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

Re: AT&T Petition for Rulemaking to Reform Regulation for Incumbent Local Exchange Carrier Rates for Interstate Special Access Services, RM No. 10593; 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

Dear Ms. Dortch:

On September 28, 2004, Sherry Ingram, Donna Epps, and the undersigned, on behalf of Verizon, met with Tamara Preiss, Deena Shetler, Jay Atkinson, Alvero Gonzalez, Jeremy Marcus, and Richard Kwiatkowski of the Wireline Competition Bureau to discuss material relevant to the above captioned proceedings. The attached document formed the basis of the discussion.

Please do not hesitate to contact me with any questions.

Sincerely,

/s/Joseph Mulieri

Attachment

cc: T. Preiss
J. Atkinson
A. Gonzalez
R. Kwiatkowski
J. Marcus
D. Shetler

THE ETI REPORT DISTORTS MARKET FACTS
ON HIGH CAPACITY COMPETITION

ETI argues there is no competition in the market for high capacity services and that as a result, ILECs have raised prices for special access services, resulting in harm to end user customers. ETI is wrong for two reasons.

- First, as described below, there is extensive competition to provide end user customers high capacity services both from competitors who have deployed their own facilities to serve these customers as well as from competitors who are using exclusively ILEC special access services or a combination of their own facilities and ILEC special access services.
- Second, because of this extensive market competition, the prices both carrier and end user customers are actually paying for special access services have actually declined.

ETI argues CLECs are dependent upon ILEC special access for "last mile" (local loop) connections to enterprise customers because CLECs have deployed their own facilities to only 1% of ETI's estimated 3-million commercial buildings in the United States. The truth is:

There Is Extensive Competition to Provide End User Customers High Capacity Services.

- Demand for high capacity facilities is highly concentrated in downtown business districts.
 - 80% of the special access demand is in just 8.5% of Verizon's wire centers.
 - Three-fourths of those wire centers are located in just Verizon's top 20 MSAs.
 - ETI distorts the percentage served by including thousands of small buildings that are not served by *any* high capacity facilities because there is no demand there.
- Competing providers have deployed high capacity facilities to meet that demand:
 - There is at least 1 competitive network in 98 of the top 100 MSAs in the country;
 - There is an average of 20 competitive networks in each of the top 50 MSAs.
- Competing providers have deployed 180,000 route miles of fiber including:
 - AT&T – 21,000 *local* route miles in 70 MSAs;
 - Time Warner – 21,247 local route miles in 41 MSAs;
 - XO – 23,800 total route miles in 34 MSAs;
 - MCI – 9,000 *local* route miles in 63 MSAs;
 - Cox – 9,500 total route miles in 23 MSAs;
 - TelCove – 8,700 *local* route miles in 48 MSAs.
- Competing providers, in fact, have connected to thousands of buildings including:

- AT&T – 6,400 on net;	KMC – 1,700 on net;
- Time Warner – 4,576 on net; 17,690 served;	Cox – 6,600 on net;
- XO – 2,434 on net;	TelCove – 2,500 on net.

- CLECS themselves, including AT&T, boast about the extensive reach of their networks:
 - Time Warner earns the “majority of [its] revenue ... exclusively through [its] own network facilities ...” and boasts that “[w]hile [RBOCs] have lots of fiber deployed, I don’t know that they have more buildings connected than we do in all cases.”
 - AT&T tells investors that its own network “touches virtually all Fortune 1,000 Companies,” and that its core network extends “all the way to the customer premises;”
 - Level 3 states that its “metro networks comprise almost one million miles of installed optical fiber and connect to 792 on-net buildings.”
- Demand for high capacity services is so concentrated that competitors have deployed their own facilities in markets that represent 80% of Verizon’s high capacity services.
 - Data Verizon purchased from GeoTel and physical inspections confirm that there are competing providers with their own fiber in each of Verizon’s top 20 MSAs.
 - Data purchased from GeoResults confirm that competing providers have extended the reach of the fiber networks to thousands of buildings in Verizon’s top 20 MSAs.
- ETI relies on maps created by Verizon that show the success of CLECs using special access, but fails to acknowledge maps from the same filing that demonstrate that other CLECs are using non-Verizon facilities to serve customers in the same locations.
 - Attachment 1 shows competitive fiber and lit buildings in the New York MSA.
 - Attachment 2 shows that competitors have deployed facilities and equipment to many of the same locations that other CLECs are serving using special access services.
- ETI also denies the scope of inter-modal competition from fixed wireless and cable.
 - Analysts report that 40% of large business (5,000+ employees) use fixed wireless or cable service for at least some high-capacity service. (In-Stat/MDR, Dec. 2003).
- Finally, independent analysts confirm that ETI has its basic facts wrong:
 - ETI ignores the fact that large carriers purchased major providers of high cap services:

“The large carriers made multi-billion dollar acquisitions (i.e. Teleport, MFS, Brooks Fiber) to improve their reach in local markets to improve their cost structures and lower their dependence on the Bells. As a result, we believe that roughly 25% of AT&T’s customer connections are on-net – utilizing their own facilities to reach customers. We believe this figure is between 10-20% for MCI. When these carriers are required to use off-net facilities they try to use third party connectivity (CLECS, utilities) when available to avoid Bell special access. These figures contrast with the white paper that suggested that the Bells control 98% of the special access market – a figure we believe is much too high.” (UBS, “Telecom Wake-Up Call”).
 - Royce Holland: “The large ... enterprise market . . . is all but irrelevant in the debate over competition policy because there are no bottleneck facilities.” (TR Daily 12/03).

Despite this overwhelming evidence, ETI argues there is a lack of competitive alternatives based on the "fact," according to ETI, that ILECs have raised prices for special access services. ETI makes its claim based on the monthly ("sticker price") rates in ILEC tariffs. The truth is:

Prices competing providers actually pay for special access services have declined *because of the availability of competitive alternatives in the high capacity market.*

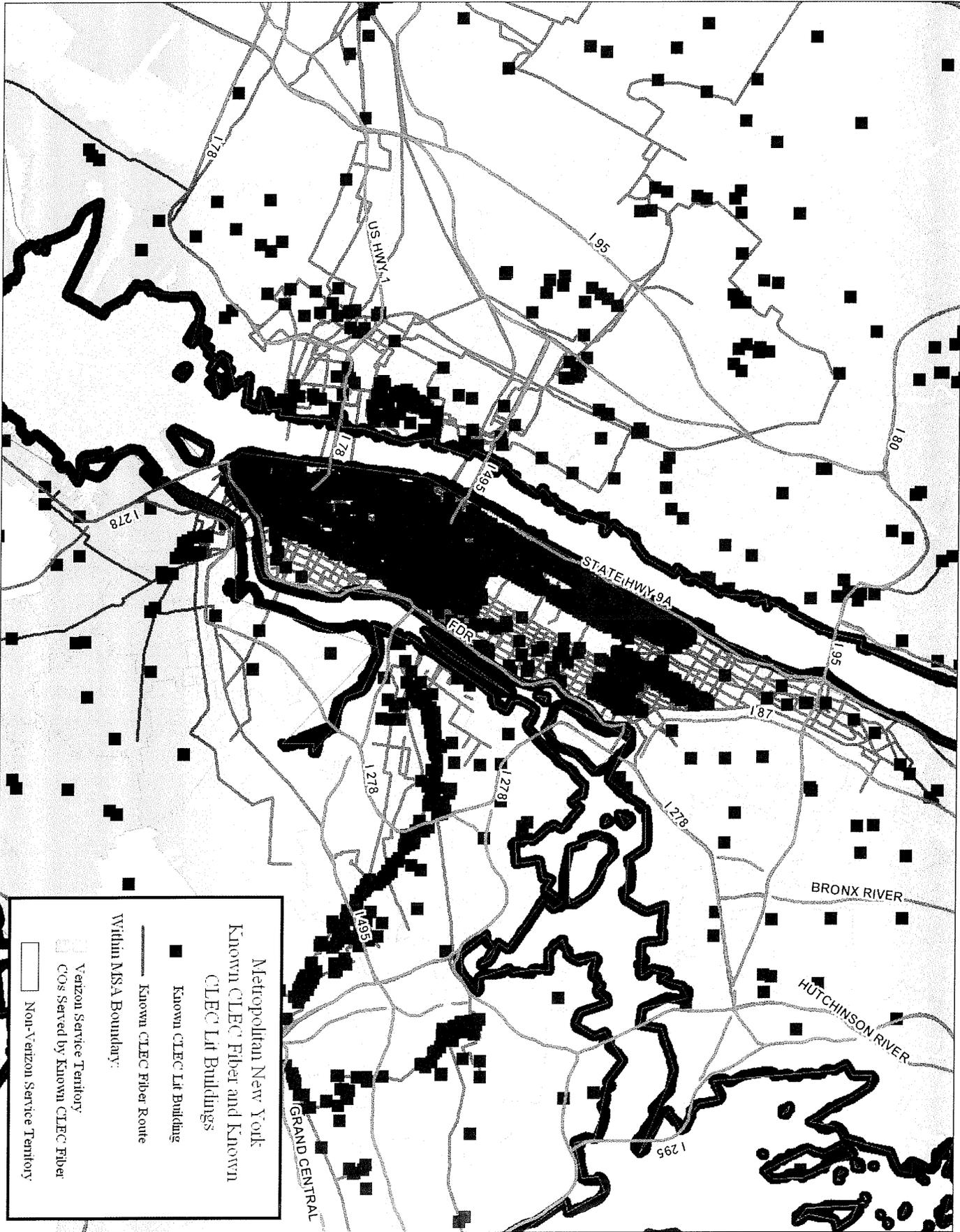
- Customers do not pay the monthly tariffed rates, but instead actually buy special access services at deep discounts of 25 to 40 percent off those monthly rates.
 - Attachment 3 shows the difference between the *monthly* tariffed rates for a DS-1 circuit (\$403) and the average price per DS-1 circuit customers are actually paying (\$254).
- Prices Verizon customers are actually paying for DS-1 special access circuits have declined by 9% since 2001, and the overall decrease in prices actually paid for all special access services was even higher.
- As Attachment 4 shows, even the ARMIS data relied on by ETI confirms that the average price per special access line sold by the RBOCs has fallen during the period of pricing flexibility, and that the price charged by Verizon has fallen even faster.
- This extensive competition in the market for high capacity services has changed dramatically the way both our wholesale and retail customers do business with us.
 - Some wholesale customers who have deployed or purchased facilities deeper into our network are migrating off Verizon's special access facilities onto their own facilities.
 - Others that are more aggressive make it clear that they prefer to build themselves and will do so unless Verizon provides more cost effective prices for the facilities they need.
 - Even customers who have not deployed their own facilities but instead rely almost exclusively on special access to compete report they have lots of other alternatives and threaten to take their business elsewhere if Verizon does not offer competitive prices.
 - As a result, retail customers receive bids for high capacity services from multiple vendors and, therefore, demand competitive pricing when purchasing these services.
- Verizon has responded to this competition and to customer-specific requests for price reductions both through volume and term discounts mentioned above and through contract tariffs offered in areas where we have pricing flexibility for high capacity services.
 - To encourage competing providers to continue to purchase entrance facility services from us, in May, Verizon offered an additional 8% off the already discounted 5-year term rates to customers who agreed to purchase a certain number of SONET¹ services.
 - To encourage competing providers to keep their high capacity transport services with us, Verizon previously offered additional discounts of between 15-21% off 5-year term rates to customers who renewed their already existing SONET services.
 - Verizon also filed contract tariffs, including more than 5 New Connect Plans, offering customers additional discounts of between 10%-20% off already low term rates when they order new SONET, DS-3s, DS-1s and Facility Management Services.

¹ SONET (Synchronous Optical Network) services allow customers to transport DS-1s, DS-3s, OCn, and now Ethernet services.

- While Verizon has lost some retail accounts because it did not have pricing flexibility for services the customer required and, therefore, could not match an un-regulated competitor's price, many retail customers have qualified for price flex offerings.
 - * One customer took advantage of an offer that provided a discount of nearly 25% off the 5-year term plan rates for DS-3 circuits and 16% off those rates for DS-1s.
 - * Another took advantage of an offer that provided 20% off new SONET rings (using the New Connect Plans), and 13% off our 5-year term rates for DS-1 services.
 - * One government agency took advantage of an offer that provided 20% off OC-192 IDSR rings and 30% off IOTS services, both high capacity transport services.
- Through volume and term discounts and these contract tariff offerings one carrier customer, which relies exclusively on special access services to serve enterprise customers, has achieved a 21% reduction in prices per circuit in just the last 18 months.

Relying on data from the FCC's ARMIS reports, ETI argues ILEC abuse of their market power is evident by their excessive rates of return. The truth is:

- The FCC has recognized that the category-specific data computations from ARMIS reports
 - are not reliable indicators of market power and “do[] not serve a ratemaking purpose.”
 - has referred to the cost-allocation rules as “outdated regulatory mechanisms that are out of step with today’s rapidly-evolving telecommunications marketplace”; and
 - has indicated that reducing “regulatory reliance on earnings calculations based on accounting data is essential to the transition to a competitive marketplace.”
- The problem of mismatches is particularly acute with respect to special access because the rules assign the growing *revenues* associated with DSL services and interstate packet-switched services to the special-access element, but assign a significant portion of the associated interstate *costs* to other elements.
- AT&T’s own experts agree:
 - “Because [a carrier’s] services use[] the same network, computers[,] and other facilities whatever the jurisdiction, determining the cost basis for calculating an economically meaningful rate of return is impossible.”
 - AT&T experts have acknowledged that, “fully allocated cost figures and the corresponding rate of return numbers simply have zero economic content” and “cannot pretend to constitute approximations to anything.”



Metropolitan New York
 Known CLEC Fiber and Known
 CLEC Lit Buildings

- Known CLEC Lit Building
- Known CLEC Fiber Route

Within MSA Boundary:

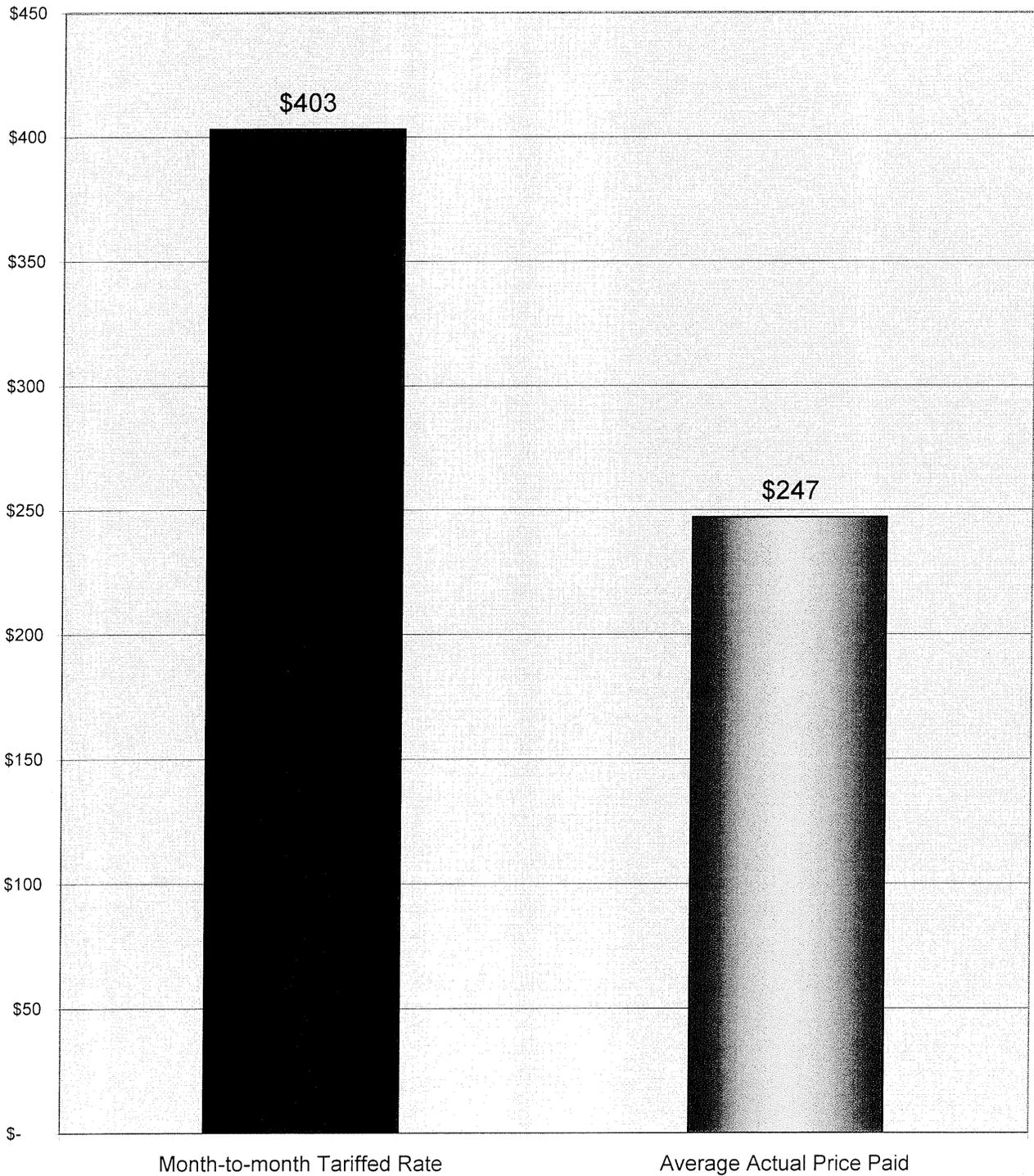
- ▬ Verizon Service Territory
- ▬ CECs Served by Known CLEC Fiber
- ▬ Non-Verizon Service Territory



**Downtown New York
Known CLEC Fiber and Known
CLEC Lit Buildings Overlayed on
Top of Special Access Data**

- ▲ Customers of 8 Select CLECs Served Using Verizon Special Access
 - Known CLEC Fiber Route
 - Known CLEC Lit Buildings
- Within MSA Boundary:
- Verizon Service Territory
 - Verizon COs Served by Known CLEC Fiber
 - Non-Verizon Service Territory

DS1: Tariffed Rate v. Average Actual Price Paid
(as of April 2004)



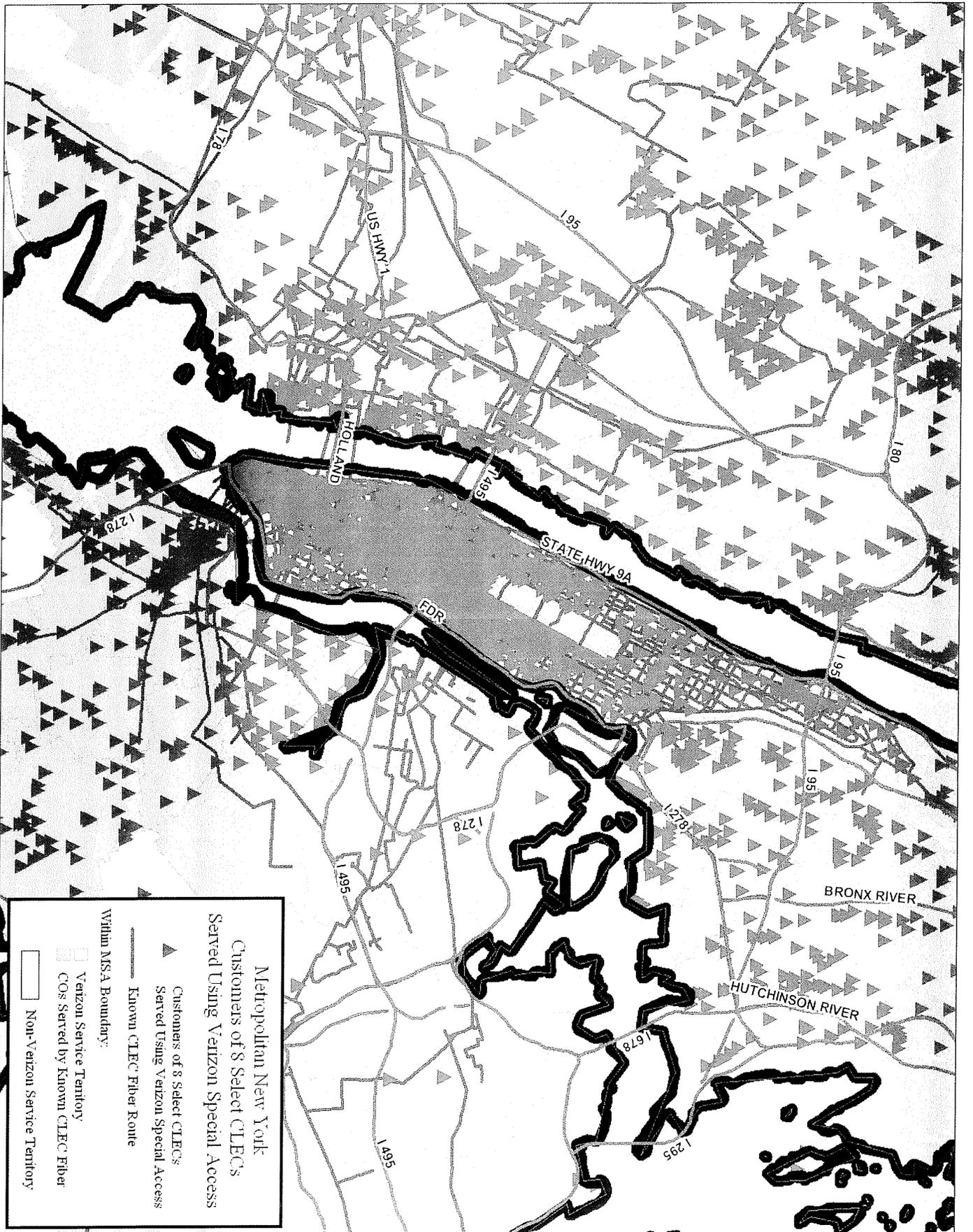
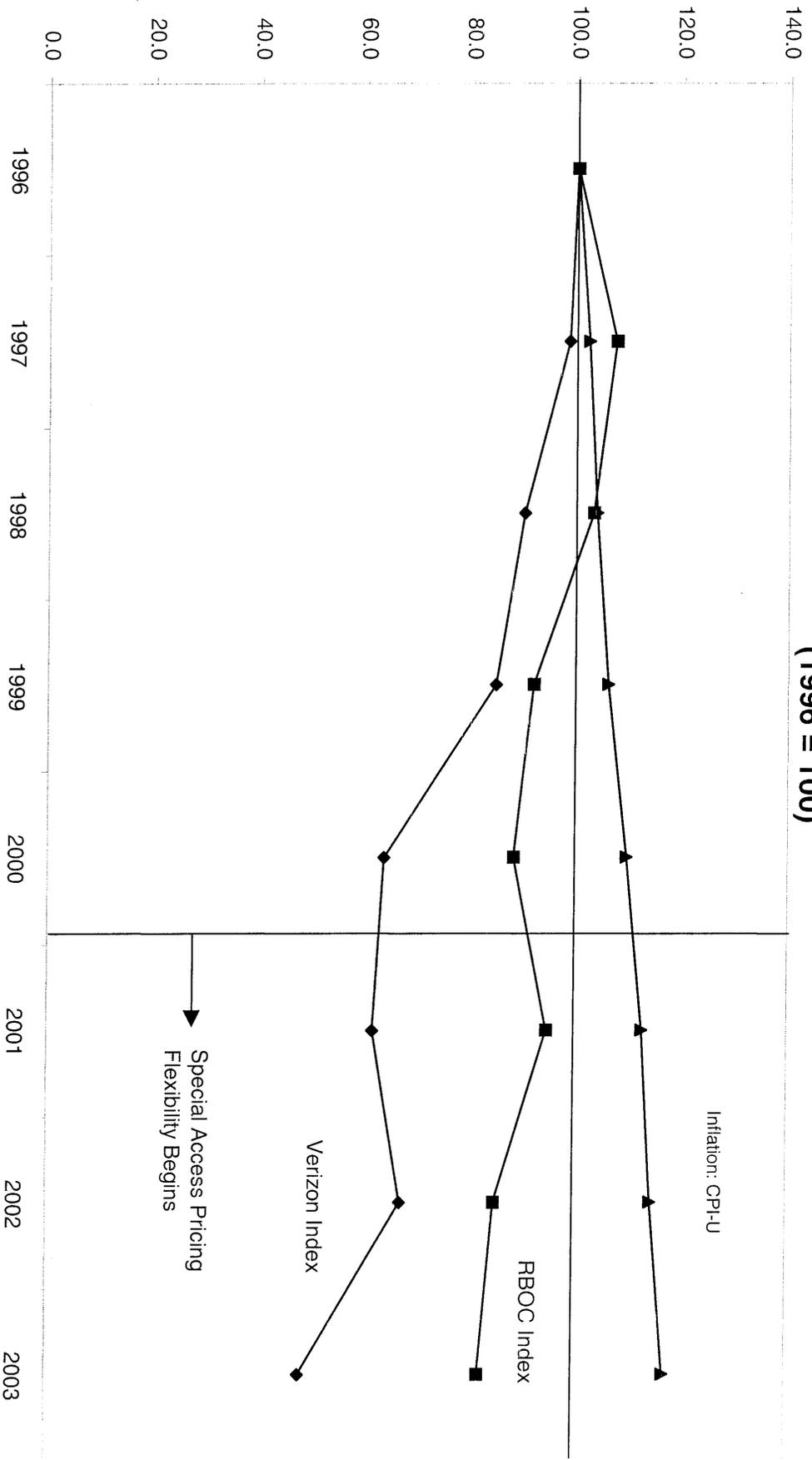


Figure 1
Nominal Special Access Revenue per
Special Access Voice Grade Equivalent
(1996 = 100)



Source: FCC ARMIS Report 43-08, 43-03; BLS