Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Unbundled Access to Network Elements	)	WC Docket No. 04-313
	)	
Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers	)))	CC Docket No. 01-338

REPLY COMMENTS OF
DIALOG TELECOMMUNICATIONS, INC.

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SUMMARY

In these Reply Comments, Dialog refines the impairment test it described in its Comments and suggests that, rather than using a central office line count as a proxy for a rural wire center, the Commission should import its definition of a rural market from the *CLEC Access Charge Reform Order.* Notwithstanding evidence that facilities based competition is established in most markets, residential customers in rural areas are still vastly under-served by competitors of any type – both facilities based wireline and intermodal competition are scarce or non-existent.

The Commission should retain the impairment analysis it established in the *Triennial Review Order.* Based on Dialog's analysis of rural markets in Kentucky, the Commission will find that competitive carriers serving residential customers in rural markets are uniformly impaired without access to all elements of UNE-P at TELRIC rates. In addition to (and because of) economic barriers such as lack of economies of scale, large sunk costs and first mover advantages, none of the proposed triggers for overturning a presumption of impairment are found. There are rarely, if ever, other competitors with self-provisioned switching, nor are there likely to be wholesale switching providers. Overall, the current competitive environment for residential customers in rural markets is weak. Only by continuing UNE-P in the near term will competition be able to fully develop in rural markets.

In its Comments, Dialog suggested that the Commission establish a mass market line threshold under which a new entrant is impaired in a rural area. Based upon further analysis Dialog now proposes that any carrier serving mass market, and especially residential, customers in markets that meet the definition of a rural market from the *CLEC Access Charge Reform*

Order are impaired without access to all of the elements of UNE-P at TELRIC pricing, and further proposes an ongoing process for evaluating impairment.

Dialog also reiterates its proposal that a reasonable 36 month transition period is necessary to ensure that the competitor can migrate its customer lines to a facilities-based network without significant inconvenience to its customers nor undue burdens on its business operations once an area is determined to be no longer impaired.

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I. THE COMMISSION SHOULD ADOPT THE DEFINITION OF "RURAL AREA" FROM THE CLEC ACCESS REFORM ORDER.

In its Comments, Dialog suggested an end office line density threshold that would serve as a proxy for identifying rural areas.[1] This proxy can be dispensed with, however, if the Commission borrows the definition of a rural area that it adopted in its recent *CLEC Access Charge Reform Order*.[2] In the Order, the Commission defined rural areas as being all areas outside "(1) any incorporated place of 50,000 inhabitants or more, based on the most recently available population statistics of the Census Bureau or (2) an urbanized area, as defined by the Census Bureau."[3]

Dialog has applied this standard to both Kentucky and the entire country using a very conservative approach that designates a central office that serves *any* part of an urbanized area, no matter how small, as being wholly contained within that urbanized area, and therefore non-

[1] Dialog Comments at 11.

[2] *Reform of Access Charges Imposed by Competitive Local Exchange Carriers*, CC Docket No. 96-262, Eighth Report and Order and Fifth Order on Reconsideration, 19 FCC Rcd 9108 (2004).

[3] *Id.* para. 6.

rural.[4] The data to complete this analysis for the entire country is readily available. Based on this approach, out of a total of 178 BellSouth central offices in Kentucky, there are 149 (84%) that are considered rural, and yet these rural offices represent only 46% of the population in the BellSouth's territory. Applying this approach nationally reveals that about 65% of central offices nationwide are rural and these rural offices represent only 18% of the population.[5]

II. COMPETITION IN RURAL MARKETS IS IMPORTANT, EVEN IF IT IS NOT CURRENTLY FACILITIES-BASED.

The objectives of the Telecommunications Act, as administered by the Commission, include (1) fostering sustainable competition across the entire telecommunications sector and (2) ensuring that American consumers can choose among multiple reliable and affordable communications services. After eight years, the Commission recognizes that this has not been an easy task, noting that "[l]egal challenges, a depressed telecommunications sector, and technical and operational obstacles have been features of the competitive landscape to a far greater extent than could have been reasonably predicted in 1996."[6] Regarding residential customers in rural markets, the Commission has expressly recognized some of the challenges of promoting competition. In its Strategic Plan for fiscal years 2003-2008,[7] the Commission described its focus in regard to competition. Two concerns in particular are shared by Dialog. First, the Commission was concerned that not all geographic areas and demographic groups have the same

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[4] *See map,* "Kentucky Central Offices," attached hereto as Exhibit 1.

[5] *See map,* "Urbanized Areas and Affected COs," attached hereto as Exhibit 2.

[6] *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*, CC Docket Nos. 01-338, 96-98, 98-147, Report and Order and Order on Remand and Further Notice of Proposed Rulemaking, 18 FCC Rcd 16978 para. 6 (2003), corrected by Errata, 18 FCC Rcd 19020 (2003)(*Triennial Review Order*).

[7] *See* <http://www.fcc.gov/omd/strategicplan/strategicplan2003-2008.pdf>.

access to advanced communications services.[8] Second, it noted the disparity between the pace of competition developing in business and residential markets.[9] Dialog's business is at the intersection of these concerns, serving only mass market, and primarily residential customers in rural markets. Dialog is providing real value to these consumers and communities today, through traditional wireline means as evidenced by its continued growth.

According to the most recent USF monitoring report,[10] prices for local residential telephone service are up 23% since passage of the Telecom Act in 1996, while the incumbents' business rates are up only 1.4%. Long distance rates are down almost 30% and wireless rates are down almost 35%. The Commission has been very successful in fostering competition for business customers and for long distance and wireless services, but at the same time it must recognize that there is not yet robust competition for residential customers.

Competition, even UNE-P based competition, provides immediate benefits to customers through innovative products, new billing approaches, better customer service, and reduced retail prices. Of equal importance, UNE-P is an essential means to the development of facilities-based competition for residential customers in rural markets. In these markets, economic factors dictate a lengthier progression to a viable facilities-based operating model. In conjunction with the recent FTTH and FTTC orders, there is also clearly incentive for both the incumbent and each of the competitors to be the first to provide higher capacity access to the customers to meet their growing demand for broadband services

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[8] *Id.* at 12.

[9] Id.

[10] "Federal-State Joint Board on Universal Service, Universal Service Monitoring Report 2004, CC Docket No. 98-202," Report at 7-20 (available at http://www.fcc.gov/Bureaus/Common_Carrier/Reports/FCC-State_Link/Monitor/mr04-0.pdf>).

The Commission has clear direction from Congress and has recognized the challenges associated with creating an environment that fosters competition for mass market, and especially for residential, customers in rural markets. These markets and customers clearly demand alternatives, and there is no reason to extend the period that they must wait, most likely by years, for effective facilities based competition to be deployed when there is an appropriate solution available today that concurrently encourages the deployment of facilities to provide enhanced services.

III. THE COMMISSION SHOULD CONSIDER MARKETPLACE EVIDENCE OF IMPAIRMENT AS ESTABLISHED IN THE *TRIENNIAL REVIEW ORDER*, AND MAKE APPROPRIATE DECISIONS BASED ON THIS INFORMATION.

In the *Triennial Review Order*, the Commission wisely noted that "marketplace evidence is the most persuasive and useful kind of evidence" and that "[the Commission is] most interested in granular evidence that new entrants are providing retail services in the relevant market using non-incumbent LEC facilities."[11] In arriving at the conclusion that competitors are "impaired without access to the incumbent LEC's switch on a national level when serving the mass market,"[12] the Commission considered evidence provided by incumbents that purported to show that some 3,000,000 mass market lines were being switched by competitors.[13] The Commission debunked this evidence, showing instead that there was very little if any deployment of switches by competitors to serve the mass market.

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[11] *Triennial Review Order* para. 93.

[12] *Id.* para. 94.

[13] *Id.* para. 438.

Of the central offices in rural Kentucky, only one is served by a facilities based competitor, and that competitor is an incumbent monopoly.[14] There are, however, UNE-P competitors serving mass market customers from most BellSouth offices.

While many wish it to be otherwise, intermodal competition is not relevant to the analysis in rural Kentucky markets. Existing broadband penetration is low. The Commission has reported that, as of December 30, 2003, only 73% of zip codes with low population density had any broadband subscribers while 99% of the zip codes in high population density areas had broadband subscribers.[15] Without high broadband penetration rates, the entry price for VoIP is very high. VoIP over DSL is nonsensical in rural Kentucky, as DSL is only available, when it is available at all, bundled with BellSouth's voice service. VoIP over cable is not available from the cable operators in these rural markets, and while third-party VoIP is available to anyone with access to broadband, these providers do not offer access to 911 and local telephone numbers in rural markets. The Commission has reported that the cellular penetration rate is estimated to be only 30% to 40% in the economic area that includes most of rural Kentucky.[16] Additionally, VoIP and cellular are not acceptable substitutes for the majority of rural consumers because the entry prices (and usage charges, in the case of cellular) are too high to be economical choices for middle and lower income households.

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[14] In Murray, Kentucky the municipal power company has partnered with other firms to deliver a triple play over new HFC plant.

[15] "High-Speed Services for Internet Access: Status as of December 31, 2003" at 4, Report, Industry Analysis and Technology Division, Wireline Competition Bureau, June 2004 (available at <http://www.fcc.gov/Bureaus/Common_Carrier/Reports/FCC-State_Link/IAD/hspd0604.pdf>).

[16] *Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services*, WT Docket No. 04-111, Ninth Report, FCC 04-216, App. A Table 3 (rel. Sep. 28, 2004).

Dialog does not have access to information from the incumbents about the numbers of DS0s converted to competitor's switches since the *Triennial Review Order* or even since the incumbents announced that they had developed their bulk migration processes. Dialog is, however familiar with what all of the competitors in rural Kentucky are doing, and to the best of its knowledge, only one has deployed switching,[17] and none has deployed collocation facilities to serve residential consumers. While it is possible that the switches originally deployed by CLECs to serve enterprise customers are now being used to serve mass market customers in urban markets, there is no evidence of this in rural Kentucky. Instead, as the attached market survey for Kentucky shows, with the exception of Murray, Kentucky the only competitive alternatives for residential consumers of mass market telecommunications services in the rural areas are based on UNE-P.[18] Based on this marketplace evidence it is readily apparent that competitors would be impaired without access to all elements of UNE-P at TELRIC prices when serving mass market, and especially residential, customers in rural Kentucky.

IV. THE COMMISSION SHOULD CONSIDER, WHEN AVAILABLE, EVIDENCE OF IMPAIRMENT AND NON-IMPAIRMENT AS OUTLINED IN THE TRO AND MAKE APPROPRIATE DECISIONS.

In the *Triennial Review Order*, the Commission designed a four step process for deciding if a particular area is impaired without access to switching to serve mass-market customers:

1) **Define mass market customer**: "[a] state must determine the appropriate cut-off for multi-line DS0 customers as part of its more granular review. This cross over point may

[17] *See supra*, note 12.

[18] *See* "Kentucky Market Review," at 5. Attached hereto as Exhibit 3.

be the point where it makes economic sense for a multi-line customer to be served via a DS1 loop."[19]

2) **Define market areas**: "State commissions must first define the markets in which they will evaluate impairment by determining the relevant geographic area to include in each market."[20]

3) **Consider non-impairment triggers**: "[A] state must find 'no impairment' when three or more unaffiliated competing carriers each is serving mass market customers in a particular market with the use of their own switches."[21] "[C]arriers are not impaired without unbundled local circuit Switching [when] two or more competing carriers, not affiliated with each other or the incumbent LEC, offer wholesale switching service for that market using their own switch."[22]

4) **Conduct analysis of competitive potential** -"[W]here neither of the triggers described above have been satisfied, the state must conduct further analysis to determine whether the market in question is suitable for "multiple, competitive supply."

- Determine "whether competitors are using their own switches to serve enterprise or mass market customers in the market at issue."
- "[C]onsider the role of potential operational barriers, specifically examining whether incumbent LEC performance in provisioning loops, difficulties in obtaining collocation space due to lack of space or delays in provisioning by the

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[19] *Triennial Review Order* para. 497.

[20] *Id.* para. 494.

[21] *Id*. para. 501.

[22] *Id.* para. 504.

incumbent LEC, and difficulties in obtaining cross-connects in an incumbent's wire center, are making entry uneconomic for competitive LECs."

- "[C]onsider the role of potential economic barriers associated with the use of competitive switching facilities."[23]

Setting aside *USTA II*'s objections to the sub-delegation to the states, the court objected to the Commission's impairment analysis because it did not adequately consider some of the arguments of the incumbents about how to mitigate the impairment caused by the hot cut process and because the analysis was not market focused. All of the courts concerns can be addressed quite easily in a brief analysis of the rural Kentucky market area when serving mass market customers:

Mass market determinations: Dialog is neutral regarding the appropriate cutoff for a customer to be served by a DS1 rather than by a number of DS0s in its markets, since the issue is not relevant in rural Kentucky. As the market survey shows, there are an average of almost 7,000 business lines in each wire center in urbanized areas, while there is only an average of 733 business lines in the rural wire centers.[24] Dialog's proposal deals primarily with residential customers, and while there are businesses in the rural areas, the selection of a crossover between three lines and fifteen lines has no impact on the analysis in the rural areas.

Define market areas: As described above, Dialog is guided by the Commission's definition of a rural area in the *CLEC Access Charge Reform Order*. Under this definition, Dialog proposes that there are six distinct market areas in Kentucky; five urban areas defined by the census bureau and one rural area comprised of the remainder of the state. Dialog's analysis

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[23] *Triennial Review Order* paras. 506-7.

[24] *See* Exhibit 3.

deals only with the rural market area. As discussed above, Dialog defined urbanized areas much more aggressively than did the census bureau to both simplify the analysis and to make it more conservative (*i.e.* less likely to find impairment). Exhibit 1 shows the urbanized areas, as defined by the census bureau, in red, and the Dialog-expanded urbanized areas in pink. The expansion of the urbanized areas into the areas served by predominantly rural wire centers reduces the differences between the urbanized areas and rural areas, but the differences are still very readily apparent.

Consider non-impairment triggers: The first trigger is to determine if there are three competitors serving mass market customers in a market area. Based on information gathered in the rural Kentucky market area, there is only one carrier serving mass market customers from its own facilities. Given that this competitor is a municipal power company, with all the resources and access to customers that implies, it would be reasonable to discount the presence of this competitor as an indication that the market is not impaired. In fact, even if that carrier is included, there are clearly not three competitors serving mass market customers from their own facilities in *all* of rural Kentucky. Moreover, as Dialog's Comments and the attached market survey demonstrate, there is no viable facilities based intermodal competition in these markets either.

The second trigger is based on access to wholesale switching from two sources other than the incumbent ILEC. In Dialog's market evaluation, it found no carriers who are capable of providing such wholesale service. While there is a switch in Murray, Kentucky, it is providing service only on its own network, and the carrier has no facilities, procedures, or experience interconnecting with the incumbent ILEC to serve customers across the incumbent loops. In addition, Dialog has approached two rural independent telephone companies in western

Kentucky with a proposal to acquire wholesale switching from these carriers. Both carriers declined to provide such switching to Dialog. All other Class 5 switches in western Kentucky are owned by BellSouth. Consequently, it is clear that neither trigger has been met in the rural Kentucky market area.

Competitive potential: The Commission has stated that considering the availability of competitive switching serving the enterprise market is relevant because these resources could potentially be used to serve mass market customers once a batch cutover process was implemented. As stated above, with only one exception, there are no facilities based providers serving either enterprise or mass market customers in the rural Kentucky market area. While the Commission specifically stated that "the existence of even one such switch might in some cases justify a state finding of no impairment, if it determines that the market can support 'multiple, competitive supply,'"[25] the one switch deployed in Murray is isolated from the local telephone network and operated by a municipal power company that has not demonstrated the capability to become a wholesale provider; this is not the "one switch" scenario the commission contemplated.

The state commissions were also directed to "consider the role of potential economic barriers associated with the use of competitive switching facilities"[26] to determine "whether entry is economic."[27] This analysis is terribly complex and subject to manipulation to reach whatever outcome is desired, but Dialog can state emphatically that the density of customers in the rural Kentucky market is dramatically lower than in the urbanized market areas (4,100 total lines per rural central office vs. 25,000 lines per urban central office, and the urban central offices would

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[25] *Triennial Review Order* para. 510.

[26] *Id.* para. 506.

[27] *Id.* para. 517.

average 40,000 lines except for Dialog's expansion of the urbanized areas as described above), resulting in higher operating and capital costs per customer in the rural market area. It is also well known that the revenue stream from residential consumers is significantly less than from enterprise customers. Finally, it is prudent to assume that, in general, competitors are innovative in their business models and their financing, and are motivated to deploy their own facilities to provide additional services (including broadband) and higher quality service at lower costs than they can provide when dependent upon the incumbent. In this environment, competitors will deploy networks to serve these customers if they are not in some way impaired. It would be inappropriate to draw this conclusion when considering a single competitor who may simply be inefficient or poorly managed, but it is perfectly reasonable to draw this conclusion based on the behavior of a number of competitors.

Based on these definitions of markets and a review of the environment in the rural Kentucky market, it is clear that competitors serving residential customers in rural markets will be impaired without access to the entire UNE-P platform at TELRIC prices. Removal of any element at this time will reduce consumer choice, force customers back to the ILEC, and generate a financial windfall for the ILEC at the expense of the consumers and communities in the rural Kentucky market.

V. THIS ANALYSIS FOR RURAL KENTUCKY CAN BE APPLIED TO RURAL MARKETS IN OTHER STATES

Rural markets in disparate locations are treated similarly in the Act and Commission rules, and that same treatment is appropriate here as well. Central offices in rural Kentucky are similar in most respects (demographics, level of competition, level of broadband deployment, etc.), and the Commission should presume, as it did in the *CLEC Access Charge Reform Order*, that these markets are very similar across the country unless it considers evidence to the contrary.

VI. THE COMMISSION MUST ESTABLISH AN EFFICIENT PROCESS FOR REVIEWING IMPAIRMENT FINDINGS AND RESOLVING CHALLENGES TO IMPAIRMENT DETERMINATION

The ILECs have created an atmosphere of regulatory uncertainty that has chased investment dollars away from this sector. Whether intentional or not, this has boosted their stock values while cutting their competitors off from the capital they need to grow. The BOCs are certain to again challenge whatever order the Commission issues in this proceeding, but it would be beneficial to have an orderly review process to help reduce the level of judicial review beyond that. To that end, Dialog proposes that the Commission implement a biennial review process where ILECs and CLECs could petition the commission to evaluate impairment in specific central offices based upon the criteria for evaluating impairment described in the *Triennial Review Order* and other factors which any party may feel relevant. This process should be initiated in 2005, but no market would be evaluated more than once every two years, to ensure that all parties present for review only those areas where there are clear reasons to change the markets current status.

VII. COMPETITORS NEED A DEFINED TRANSITION PERIOD ONCE THERE IS A FINDING OF NO IMPAIRMENT.

In the *Triennial Review Order*, the Commission found that CLECs serving mass market customers were impaired without access to UNE-P at TELRIC pricing. Based on the analysis presented above, the Commission should find that CLECs serving mass market customers, and especially residential customers, outside of "urbanized areas" are impaired without access to UNE-P at TELRIC pricing in those areas.

Even if the Commission's finds otherwise, however, the CLECS that have invested significant resources and effort -- and which are delivering significant value to their customers and communities -- must be given the opportunity to smoothly transition from a UNE-P model to a facilities-based model. Given the opportunity, most CLECs will make this transition without any pressure from the Commission when it is economically feasible to do so. They will then demonstrate the advantages of operating their own network by reducing prices, offering new products, and generally wreaking havoc on the incumbent and the competitors that depend upon the incumbent. Each UNE-P CLEC is racing to be the first to be able to do this, because of the competitive pressures to do so.

As discussed in Dialog's comments, the length of this transition period is especially critical for CLECs that are small businesses because the regulatory uncertainty that the incumbents have so expertly created has effectively chased all investment from the sector. In its meeting with Commission staff on October 12, 2004, Dialog presented a timeline that was very aggressive; any shorter transition would either force Dialog to abandon many customers or pay BellSouth its so-called "market-based" rate (700% above TELRIC) for switching. In either case, this would be to Dialog's detriment and would give a substantial windfall for BellSouth while reducing competition in the market -- contrary to the intent of the act.

VIII. CONCLUSION

Accordingly, the Commission should adopt the impairment determination described herein.

Respectfully submitted,

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EXHIBIT 1

Kentucky Central Offices

EXHIBIT 2

Urbanized Areas and Affected COs

EXHIBIT 3

Kentucky Market Review