Mass-Market Switching

24. Dr. Pelcovits has proposed an incorrectly narrow definition of the product and geographic market in which CLECs that deploy their own circuit switches compete and an internally inconsistent rationale for that definition. First, he has defined the product to include only offerings that utilize traditional circuit switching—thereby assuming away the already great and rapidly increasing competitive significance of intermodal alternatives such as wireless, cable, and VoIP. Second, he has confined its geographic extent to individual ILEC wire centers. As we explained in our opening declaration and discuss in more detail below, the correct market definition clearly embraces intermodal options[23] and, for reasons analogous to the FCC's in its determinations for long-distances services, the geographic scope of these products is nationwide. Even if the Commission were to ignore the intermodal competitors, the proper geographic market would still be at least the metropolitan area, because that is the basis on which CLECs deploy their own switches and compete—not wire center by wire center.

25. A proper geographic market is the area in which sellers provide products or services that customers treat as substitutes for one another and which therefore compete against one another. As a leading text describes the same concept:

> The geographic limit of a market is determined by answering the question of whether an increase in price in one location substantially affects the price in another. If so, then both locations are in the same market.[24]

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[23] Dr. Crandall and Dr. Singer's reply declaration (Attachment H) supports this proposition in detail.

[24] D. W. Carlton and J. M. Perloff, *Modern Industrial Organization*, Second edition, (1994), New York: Harper Collins, at 807. Similarly, the *Horizontal Merger Guidelines* (Section 1.2.1) consider firms at different locations to be in the same market when a potential price increase by one firm (assuming other firms maintain

For example, carriers offering mass-market local telephone service using their own switches in the core of an urban area would be likely to be in a position to use those same switches to compete with carriers offering local service in a nearby suburb: for this reason, reductions in local exchange prices in the suburb would tend to lower prices in the core area and, conversely, an attempt by the local carrier to raise rates in the suburb would be limited by the ability of the lower-pricing carrier in each case to invade the higher-priced adjoining market, using their existing switches.

26. In determining the geographic reach of competing firms, a typical market definition analysis (e.g., under the DOJ *Merger Guidelines*) starts with the products of the firm in question and poses the question of whether customers would shift to the products of firms *at other locations* in the event it increases its price. That is, firms are viewed as having precise locations; consequently, considerations such as transportation costs come into play when determining whether customers would shift their purchases to the competing firms. If they would do so, then the locations of those other firms are part of the same geographic market. As we discuss further below, proper application of this standard leads to a nationwide market for switching because of the development of intermodal competition from sources such as VoIP and wireless. But even leaving such intermodal substitutes aside, Dr. Pelcovits' suggestion that the wire center is the appropriate geographic market is mistaken.

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their current prices) would be unprofitable, because customers would shift to the products of firms at other locations in the same geographic market.

27. Although Dr. Pelcovits purports to rely on the *Merger Guidelines* in support of his position, he turns them on their head. He reasons that, because (1) a user of circuit switched telephone services receives them over a subscriber loop and (2) services provided to other consumers at other locations are not substitutes *on the demand side*, each individual customer location is arguably a separate market. The similarity of certain economic factors within a wire center, however—such as that multiple customers can be served from the same collocation facilities and UNE loop rates are the same throughout the wire center—leads him to expand the scope of the geographic market from the customer location to the wire center.

28. Dr. Pelcovits asserts that (1) the fact that consumers use wireline telephone services at their specific locations is a unique feature of telecommunications[25] and (2) makes each customer location analogous to the plant locations used to define geographic markets under the *Merger Guidelines*.[26] In so doing, not only does he overstate the uniqueness of telecommunications, he draws the wrong analogy to the *Merger Guidelines* market definition exercise. In the case of the scope of a CLEC deploying circuit switching with UNE loops, viewing each customer location as an individual "plant" would be incorrect: instead, the competing firm can be thought of as located at its switch and able to offer the local exchange service product at that location to any customer that can be served by that switch—not simply those in a particular wire center. In order to reach customers throughout the market, the firm incurs "transportation costs" in the form of outlays for

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[25] MCI's Pelcovits Declaration at ¶ 39.

[26] MCI's Pelcovits Declaration at ¶ 38.

unbundled loops, transport of traffic between its switch and ILEC end-offices, certain non-recurring charges and the like. Nevertheless, customers at different locations would be in the same market, because the prices competing firms would offer to customers in a particular area would be influenced by what firms were offering in nearby areas (in part because the nearby firms could also provide service to those customers, using their switches). The immobility of the customer location and the consequent need of the service provider to incur costs to reach that location is not unique to telecommunications. For example, residential consumers would be equally reluctant to move to take advantage of lower-priced home remodeling services elsewhere. Yet clearly the geographic markets for such services are considerably broader than individual houses, because (and to the extent that) suppliers of those can offer them over a broader geographic area.

29. Dr. Pelcovits' reliance on the FCC's 2003 *TRO* market definition rule[27] is equally flawed. Proper application of the market definition rule promulgated in the *TRO* requires a fact-intensive investigation whose outcome would be a geographic scope at least as large as a metropolitan area (even ignoring intermodal competition). In contrast, Dr. Pelcovits has not only failed to provide the requisite factual information, he has also misinterpreted where those facts would lead. The FCC stated that the geographic market may not be so small that *it fails to reflect available scale and scope economies from serving a wider market.* In addition, its market-definition rule instructs the state to take into account the following considerations:

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[27] *TRO* at ¶ 495.

- Locations of customers actually being served (if any) by competitors;
- Variation in factors affecting competitors' ability to serve each group of customers; and
- The ability of competitors to target and serve specific markets economically and efficiently using currently available technologies.[28]

In paragraph 496 of the *TRO,* the FCC also listed additional considerations that a state commission may take into account. As Verizon's evidence demonstrates, CLECs are in fact serving mass-market customers throughout large portions of their service territories in large MSAs and have the capability to expand within these MSAs if they so choose. Therefore, even if intermodal competitors are ignored, considering all aspects of the FCC's rule together, the facts strongly support the MSA, not the wire center, as the proper geographic market.

30. As in any analysis of the scope of potential competitive entry, the locations of customers actually being served by competitors are a powerful indicator of the ability of competitors to offer services throughout a market. These locations are the outcome of business decisions that require real CLEC entrants to take into account some or all of the various considerations listed in the *TRO* and the FCC's rule. In its instructions on how states should analyze potential competition, the *TRO* states that "the existence of a competitor serving the mass market with its own switch provides evidence that the mass market can be

[28] 47 C.F.R. § 51.319(d)(2)(i); see also TRO ¶¶ 495-96.

served effectively."[29] By the same token, the locations of customers actually being served provide substantial evidence that they are part of the area that a CLEC's scale and scope economies allow it to serve economically, and in which CLECs would not be impaired by the unavailability to them of unbundled switching.

31. But the line cannot simply be drawn there, because a CLEC can expand use of its switches and other facilities where it makes sense to do so.[30] Just as the DOJ/FTC *Horizontal Merger Guidelines* (§ 1.2.1) recognize that geographic markets can be larger than the area currently being served, so too the FCC adopted additional criteria that can be used to define a geographic market larger than the locations of current customers. For example, suppose that a CLEC is currently using its own switch to serve mass-market customers in ILEC wire center A, and that the same switch could efficiently serve the contiguous ILEC wire center B but is not currently doing so. The prices and terms and conditions of mass-market services that a hypothetical monopolist could profitably offer in wire center B would surely be affected by the CLEC's prices and service offerings in wire center A. Hence, by the market-definition process in the *Horizontal Merger Guidelines* and the FCC's rule, wire centers A and B must in those circumstances be regarded as in the same geographic market.

32. The TRO geographic market definition rule properly ascribes considerable importance to scale economies when assessing the geographic scope of potential competitive entry. Other than a grudging acknowledgment that such economies may require the recognition of areas

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[29] *TRO* at ¶ 510.

[30] The second and third factors of the FCC's market-definition rule get at this same concept by examining variability in conditions and in the ability of CLECs to serve new areas.

larger than wire centers,[31] Dr. Pelcovits essentially ignores them in defining the market. In fact, the area served by a wire center is far too small to exhaust the economies of scope and scale in local switching, particularly for a CLEC that cannot expect to serve large numbers of customers in each ILEC wire center. Similarly, an individual wire center's area is too small to justify the fixed and sunk costs of mass-market advertising and of establishing sales, marketing, and customer-service organizations. Indeed, CLECs themselves (including MCI, Dr. Pelcovits's client) have described these economies. For example, last year, MCI (then WorldCom) observed that CLECs serve customers in multiple ILEC wire centers with a single switch.[32] And in the recent mass market switching proceeding in California, AT&T's economist testified:[33]

> [I]t is unlikely that the "efficient CLEC" would enter a state intending to serve only a single wire center. Rather, the model CLEC would likely map out a footprint that is large enough to permit it to realize necessary economies of scale and to market to a broad range of potential customers. In most cases, this will approximate an MSA, LATA or other similarly broad area, while in some very dense areas it may be only a portion of such an area, depending on the local demographics.

33. While the TRO's geographic market definition rule would take into account variations in factors such as retail rates across a geographic area and wire centers as convenient "units of analysis," they are relevant only to the extent they would enable the Commission "to

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[31] MCI's Pelcovits Declaration at ¶ 47.

[32] Letter from Donna Sorgi, Vice President, Federal Advocacy, WorldCom to William F. Maher, Chief of the Wireline Competition Bureau, Federal Communications Commission, CC Docket No. 01-338, January 8, 2002.

[33] Direct Testimony of Nicholas S. Economides, on behalf of AT&T, before the Public Utilities Commission of the State of California, Order Instituting Rulemaking on the Commission's Own Motion into Competition for Local Exchange Service. R.95-04-043 and Order Instituting Investigation on the Commission's Own Motion into Competition for Local Exchange Service, I.95-04-044, December 12, 2003 at p. 40.

distinguish among markets where different findings of impairment are likely" (TRO ¶ 495)—that is to say, the variations must be material. The mere fact that some of these may differ among areas does not, by itself, make those areas separate markets. While it is certainly conceivable that factors could vary within different parts of the overall market, the fact that the differences may in some cases coincide with wire center areas has no particular significance. Costs often vary within more traditional geographic markets (*e.g.*, because of differences in transportation costs). What matters for the economic definition of a geographic market is whether prices and services in one area are constrained by prices and services in another. Dr. Pelcovits' observations are mere speculations: he provides no information about actual variations within wire centers, and makes no attempt to show that any particular variations among wire centers in the MSAs are large enough to make different findings of impairment likely.

34. As we have already pointed out, consideration of *intermodal* alternatives, particularly VoIP offerings, fundamentally changes the analysis of the geographic scope over which the unavailability of ILEC circuit switching at TELRIC prices may impair competition. While the entry decisions of some firms with VoIP and wireless offerings may be on a metropolitan area basis,[34] the multitude of firms offering the former and the ubiquity of high-speed connections to the Internet creates the same similarity of competitive conditions as effectively groups smaller markets into a national one, in much the same way as the FCC has routinely done for years in the case of interLATA long-distance. Moreover, the use of

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[34] See, for example, AT&T, "AT&T CallVantage Service Expands to 21 New Markets in Seven States in Nationwide Deployment," Press Release, Aug. 19, 2004.

the Internet for voice transmission and the widescale presence of high-speed connections appear to allow providers to establish a national presence in short order: barriers to entry and expansion are small. For example, AT&T's senior vice president for Internet Telephony, Consumer Marketing, and Sales, Cathy Martine, reported: "Today's market entries place us in 39 states and Washington, D.C.—that's 121 major markets since we introduced the service in late March."[35] Similarly, Vonage describes 40 states as "active markets" and indicates it will expand into two more.[36]

35. This concludes our declaration.

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[35] *Ibid.*

[36] http://www.vonage.com/avail.php.

I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct.

Executed on October 15, 2004

Alfred Kahn

I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct.

Executed on October 15, 2004

Timothy J. Tardiff

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 DECLARATION OF RONALD H. LATAILLE, MARION C. JORDAN, AND JULIE K. SLATTERY

1. My name is Ron Lataille. I submitted a Declaration with Judy K. Verses, Marion C. Jordan, and Lynelle J. Reney in this proceeding on October 4, 2004. My qualifications are set forth in that Declaration. I have information and knowledge relating to the sources of data described specifically in paragraphs 4-34, 36-38, 49-56 of this reply declaration.

2. My name is Marion Jordan. I submitted a Declaration with Judy K. Verses, Ronald H. Lataille, and Lynelle J. Reney in this proceeding on October 4, 2004. My qualifications are set forth in that Declaration. I have information and knowledge relating to the sources of data described specifically in paragraphs 35, 39-42 of this reply declaration.

3. My name is Julie Slattery. My business address is 9 Gates Avenue, Montclair, New Jersey, 07042. I am a Director in Verizon's Wholesale Markets Group and have worked in the telecommunications industry since 1997. My current responsibilities include supporting Verizon's Wholesale Access Centers with internal performance reports to manage Verizon performance results and providing Verizon's wholesale customers business-to-business performance reports for special access services they purchase with Verizon. In this capacity, I

have information and knowledge relating to the sources of data described specifically in paragraphs 43-48 of this declaration.

4. The purpose of this reply declaration is to provide additional data in response to carrier claims that (i) demand for DS1 and DS3 special access services is not highly concentrated; (ii) they need access to UNEs to provide local and long distance services to business end users; (iii) they have been forced to purchase special access services where they would have rather purchased UNEs; and (v) ILEC performance in providing special access services is poor and subject to little or no quality assurance monitoring. In addition, we analyze the extent to which carriers are extending the reach of their networks using Verizon's special access services and are purchasing dark fiber UNEs. We also address one of the CLECs' impairment tests and concerns about CLEC viability in the absence of access to unbundled high-capacity loops and transport.

5. This reply declaration addresses these issues and the data sources upon which we rely in six sections. *First*, we further analyzed the extent to which demand for high-capacity services is concentrated, and we demonstrate here that demand for DS1 and DS3 special access services also is highly concentrated. *See infra* ¶¶ 6-10. *Second*, we conducted additional analysis of our carrier customers' use of special access to provide local service, and we identify examples of carriers whose purchases from Verizon are predominantly special access services and not UNEs and who are generating local minutes of use through these special access connections. We also refute carriers' claims that Verizon is using special access pricing and policies to undermine competition in the long distance market such that carriers now need access to UNEs and EELs to compete for long distance service. We demonstrate that carriers are using Verizon's special access services in local markets to extend the reach of or "fill in" their own

fiber facilities as well as those of alternative providers. *See infra* ¶¶ 11-32. *Third*, we demonstrate that, contrary to carriers' claims, taking into account UNE orders rejected because Verizon lacked facilities necessary to provision the service does not change significantly the balance between special access services and UNEs purchased by Verizon's carrier customers. We also show that Verizon's tariffed special access minimum service periods do not prevent carriers from converting special access circuits to UNEs and that carriers, in fact, have been converting their special access circuits to UNEs after holding them for only a few months in some instances. By the same token, other carriers have chosen to rely on special access for years before converting some circuits to UNEs. *See infra* ¶¶ 33-42. *Fourth*, we explain that carriers have the ability to monitor Verizon's special access ordering, provisioning, and maintenance performance and that Verizon's performance is good. *See infra* ¶¶ 43-48. *Fifth*, we show that carriers have made little use of dark fiber UNEs and verify that our previous analysis of carriers' use of special access instead of UNEs was not affected by carriers' conversion of special access circuits to UNEs. *See infra* ¶¶ 49-52. *Finally*, we evaluate the proposal put forth by the Loop and Transport Coalition for determining impairment for high-capacity loops and transport and address other concerns about CLEC viability in the absence of unbundled network elements. *See infra* ¶¶ 53-56.

I. Further Analysis of Verizon's Special Access Demand Concentration.

6. In our initial declaration, we demonstrated that demand for Verizon's high-capacity special access services is highly concentrated in a small number (only 8.5 percent) of Verizon's wire centers.[1] *See* Declaration of Judy K. Verses, Ronald H. Lataille, Marion C. Jordan, and Lynelle J. Reney ("Verses/Lataille/Jordan/Reney Decl."). Several parties argue that

[1] For measurement purposes, we have included in our definition of wire centers both stand-alone switching offices and other locations with their own CLLI (Common Language Location Identifier) codes.

this concentration exists only for the higher-capacity special access services and not for DS-1s or DS-3s. That is not true. Using the methodology described before, *see* Verses/Lataille/Jordan/ Reney Decl. ¶ 7, we determined that 80 percent of the demand for Verizon's DS1 special access services is located in 844 wire centers. These 844 wire centers represent just 12 percent of the roughly 7,000 wire center locations contributing to Verizon's special access revenue. Furthermore, 81 percent of these 844 wire centers are located in the 40 MSAs where total demand for Verizon's high-capacity special access services is greatest ("top 40 MSAs"). *See* Exhibit 1. Similarly, Verizon determined that 80 percent of the demand for its DS3 special access services is located in just 253 wire centers. These 253 wire centers represent just 4 percent of Verizon's wire center locations contributing to special access revenue. Of these 253 wire centers, 89 percent are located in Verizon's top 40 MSAs. *See* Exhibit 2.

7. In our prior declaration, we provided data demonstrating that competitive supply of high-capacity facilities is particularly concentrated for wire centers with 5,000 or more total business lines. *See* Verses/Lataille/Jordan/Reney Decl. ¶ 63. To verify that wire centers of this density have the concentrated business demand for high-capacity services that generates such competition, we looked at several indicia of economic activity. First, we found there is a strong correlation between wire centers with 5,000 or more total business lines and concentrations of business employees. Specifically, the industry data show that Verizon's wire centers with 5,000 or more total business lines are used to serve buildings with 72 percent of the total number of employees of all businesses in all of Verizon's service area. Second, we looked at business establishments in industry sectors that use a high level of telecommunications services. Within Verizon's service territory, we found that 69 percent of such businesses are located in these wire centers with 5,000 or more business lines.

8. To perform these analyses, we used information provided by Donnelley Marketing, (formerly American Business Institute) which compiles statistics of business activity. To compile such data Donnelley Marketing obtains the Yellow Page listing for each listed business in the United States (approximately 11 million). Each business is called and data is collected regarding the business. These items include both the number of employees and the Standard Industrial Classification ("SIC") code. SIC codes are determined by the Executive Office of the President's Office of Management and Budget and group businesses by product produced.

9. Verizon's Retail Market Analysis and Modeling organization matched the business telephone numbers provided by Donnelley Marketing with the Local Exchange Routing Guide ("LERG") database provided by the National Exchange Carrier Association. The LERG database provides a mapping of the Area Code and Prefix (NPA NXX) code for each business telephone number into a specific wire center. The data provided by Donnelley Marketing was then summed at the wire center level to obtain establishment counts and employment levels by SIC code.

10. To determine which SIC codes or industry sectors use a high level of telecommunications services, Verizon obtained the 1997 Benchmark Input-Output tables from the US Commerce Department's Bureau of Economic Analysis. These tables describe the dollar value of inputs required by an extensive list of industries (129 industry segments) to produce a dollar's worth of output for those industries. The dollar value of telecommunications input relative to the dollar value of labor inputs was calculated as a measure of telecommunications intensity in the production process. These 129 industries were then ranked by telecommunications intensity. These 129 industries were then mapped to SIC code, and SIC

codes with high rankings in distribution of telecommunications intensity were chosen for inclusion in the analysis as being industry sectors that use a high level of telecommunications services. These industry sectors consisted of the following: Finance-Banking; Finance-Insurance; Finance-Other; Services-Business; Services-Health; Services-Education; Services-Other; Transportation; Communication; Trade-Wholesale; and Government.

II. Carriers' Use of Special Access to Provide Local and Long Distance Service.

11. We conducted additional analysis in response to carrier claims that they need unbundled high-capacity loops and transport and enhanced extended links ("EELs") to provide local and long distance services to business end users.

A. Response to Carriers' Claims That They Need UNEs for Local Service.

12. In our initial declaration, we showed that carriers that use Verizon's network primarily use special access service and not UNEs to provide service to customers. *See* Verses/Lataille/Jordan/Reney Decl. ¶¶ 52-59. In response, carriers claim that they are not using Verizon's special access to provide local service and, therefore, that they still need access to UNEs to provide customers local service. While carriers themselves have the most direct data of the extent to which they are using special access to provide local service, our analysis shows that there are a number of carriers terminating local minutes of use on Verizon's network who appear to be providing this local service without using UNEs.

13. We started with the subset of carriers we previously identified as using predominately special access services, not UNEs, when they purchase services from Verizon to serve business end users within Verizon's top 40 MSAs. *See* Verses/Lataille/Jordan/Reney Decl. ¶¶ 45-50. For each of these carriers, we collected from Verizon's Carrier Access Revenue Data system terminating local minutes of use – minutes that Verizon bills these carriers for

terminating local calls on Verizon's network that originated on that carrier's network – for January through April 2004. These minutes of use were collected by carrier and by terminating end office wire center and summed for the 4-month period. Based on the address of the terminating wire center, the minutes were mapped to the appropriate MSA so that we could verify where this subset of carriers was terminating local traffic within the 40 MSAs Verizon studied.

14. Next, to determine whether these carriers were providing this local service within these 40 MSAs using special access service or UNEs purchased from Verizon, we collected from Verizon's access line database the DS1 and DS3 special access channel terminations and the voice grade (DS0), DS1, and DS3 UNE loops each of these carriers had in service with Verizon as of March 2004. We compared this data with the data showing significant local minutes of use for each carrier to identify instances in which a particular carrier had significant volumes of local minutes of use but appeared to have used only Verizon's special access services, and not UNEs, to connect with business end users within that MSA. Even working with data from only a subset of carriers, we found, for these 40 MSAs, numerous examples where carriers had significant local minutes of use and had Verizon's special access service as the only visible means of interconnecting and exchanging that volume of traffic with Verizon's network. *See* Exhibit 3. This included, among others, **[BEGIN CLEC PROPRIETARY]** **[END CLEC PROPRIETARY]** in the New York MSA; **[BEGIN CLEC PROPRIETARY]** **[END CLEC PROPRIETARY]** in the Boston MSA; **[BEGIN CLEC PROPRETARY]** **[END CLEC PROPRETARY]** in the Dallas MSA; **[BEGIN CLEC PROPRIETARY]** **[END CLEC PROPRIETARY]** in the Los Angeles MSA; **[BEGIN CLEC PROPRIETARY]**

[END CLEC PROPRIETARY] in the Seattle MSA; and **[BEGIN CLEC PROPRIETARY]** **[END CLEC PROPRIETARY]** in the Tampa MSA. *Id.* From this data it is reasonable to conclude that these carriers are relying upon Verizon's special access services either alone or in combination with their own facilities or facilities of other carriers, not UNEs, to provide local service to business end users.

B. Response to Carriers' Claims That They Need UNEs for Long Distance.

15. Despite the fact that carriers have successfully served long-distance customers for years without access to UNEs, some carriers now claim that they need access to high-capacity UNEs for loops and transport to compete successfully in the long-distance market. These carriers argue that, even if Verizon's prices for special access service have fallen, now that Verizon has authority to compete for long-distance service, Verizon will raise rates carriers must pay for special access facilities carriers need to provide long-distance service while lowering its own retail rates for long-distance service to levels carriers cannot match given the higher prices they will be paying for access services.

16. As an initial matter, Verizon has demonstrated that carriers are not dependent upon ILEC special access services to provide local or long distance services. Verizon has shown that, in areas where demand for high-capacity services is most heavily concentrated, carriers have deployed extensive networks of their own and, therefore, are capable of and, in fact, are competing to provide local and long distance services to customers of all types and sizes using their own facilities or facilities of alternative providers. *See* Verizon Comments at 41-54. To evaluate carriers' claims about Verizon's pricing behavior, we also analyzed the price carrier customers are paying for Verizon's special access service in states where Verizon has long had long distance authority. We demonstrate that, as was true for all Verizon customers, *see*

Verses/Lataille/Jordan/Reney Decl. ¶¶ 60-61, the average price per circuit that carrier customers are paying for DS1 special access service has declined since 2001. We also compared the DS1 special access volume growth of Verizon's wholesale business to that of Verizon's retail business to show that, contrary to carriers' claims, Verizon's retail business is actually declining while Verizon's wholesale business is growing.

17. First, we analyzed the average price per circuit that Verizon's wholesale customers are paying for DS1 special access circuits in New York and in the former GTE states, where Verizon has had authority to offer long-distance services since before 2001. Using the methodology previously described, *see* Verses/Lataille/Jordan/Reney Decl. ¶ 61, we determined that the average price per circuit that Verizon's carrier customers are paying for DS1 special access circuits in New York has declined in absolute terms by 17 percent since 2001, from $257 in 2001, to $214 as of April 2004. *See* Exhibit 4. Similarly, in the former GTE states (the Verizon West serving territory),[2] where Verizon has long been able to offer long-distance service, we determined that, between 2001 and April 2004, there has been a decline in absolute terms of 8 percent in the average price per circuit for DS1 special access service. *See* Exhibit 5. The decline is somewhat greater in real terms if inflation during this period is taken into account.

18. Using data from Verizon's access line database, we also compared DS1 special access volume growth for Verizon's wholesale and retail operations for a one-year period from July 2003 through July 2004. The data show that Verizon's year-over-year DS1 special access volume growth for this period for Verizon's wholesale division was **[VERIZON PROPRIETARY BEGINS]** **[VERIZON PROPRIETARY ENDS]** percent compared to

[2] The former GTE states, which Verizon refers to as the Verizon West serving territory includes Arizona, California, Florida, Hawaii, Idaho, Illinois, Indiana, Michigan, North Carolina, Nevada, Ohio, Oregon, Pennsylvania, South Carolina, Texas, Virginia, Washington, and Wisconsin.

[VERIZON PROPRIETARY BEGINS] **[VERIZON PROPRIETARY ENDS]** percent. *See* Exhibit 6. And as we previously showed, 85 percent of Verizon's high-capacity DS1s are sold to other carriers rather than end users. *See* Verses/Lataille/Jordan/Reney Decl., Ex. 9. This trend belies carriers' claims that Verizon's retail division is dominating the market for high-capacity services such that carriers now need DS1 UNEs to compete in providing long-distance services.

C. Response to Carriers' Claims With Respect to Term and Volume Discounts for Special Access Services.

19. Finally, some carriers argue that they need access to high-capacity UNEs and EELS at UNE rates, rather than as special access, to provide both local and long-distance service because the only way they can obtain special access facilities at rates that allow them to compete is to commit to onerous long-term special access pricing plans. These plans, they claim, require them to commit the majority of their high-capacity business to the RBOC for long periods of time, with no ability to opt out should they subsequently decide to build the facilities themselves or move the circuits to an alternative provider.

20. Again, putting aside the fact that RBOC special access is not the only option carriers have for obtaining high-capacity facilities, particularly in areas where business end user demand for high-capacity services is highly concentrated, *see* Verizon Comments at 41-54, none of the carriers' claims are true with respect to Verizon's term pricing plans. Carriers in Verizon's serving territory can choose between two types of special access term pricing plans, and neither type of plan prevents them from using their own facilities where they choose to do so.

21. In the Verizon East[3] serving territory, where special access demand is more concentrated, there are two types of long-term special access pricing plans that provide significant discounts of 5 to 40 percent off monthly or base special access rates to carrier customers who choose to participate in these plans. The first type of plan is strictly a term of years pricing plan that is circuit specific. A carrier who purchases a DS1 special access circuit (or other qualifying service) from Verizon may decide at the time of purchase whether to place the circuit under a plan for a term of years ranging from two to ten years, with discounts increasing as the term commitment increases. These term plans require no volume or revenue commitment at all – carriers purchasing special access services from Verizon can either place the circuits on term pricing plans (and obtain substantial discounts) or not, and can do so on a circuit-by-circuit basis.

22. To provide its carrier customers more flexibility and ease in managing their special access service, Verizon also offers a second type of term plan called a Commitment Discount Plan. Carriers can participate in this term plan if they purchase from Verizon at least 336 DS0s or their equivalent. Accordingly, a carrier purchasing only DS1s or DS3s from Verizon would need to purchase 14 DS1s or 1 DS3 to participate in this plan. If a carrier chooses to participate in the plan, the carrier also must agree to a minimum volume level, for DS1s and DS3s, equal to 90 percent of the total number of channel terminations for the service type that they have in service with Verizon when they subscribe to the plan. So, for example, a carrier who has 100 DS1s with Verizon and subscribes to the plan must agree to maintain at least 90 DS1s with Verizon for the term of the plan. The Commitment Discount Plan also requires a

[3] The Verizon East serving territory includes the former NYNEX states (Connecticut, Maine, Massachusetts, New Hampshire, New York, Rhode Island, and Vermont) and the former Bell Atlantic states (District of Columbia, Delaware, Maryland, New Jersey, Pennsylvania, Virginia, and West Virginia).

one-year minimum service period. But, unlike the circuit-specific term plans described above, carriers under the Commitment Discount Plan may remove individual circuits as they choose, without termination liability, as long as they meet the minimum service period and maintain their minimum volume level. This allows carriers that do reach a point where they can build some facilities themselves (or even to obtain them from another provider at a lower rate), to move individual circuits off of Verizon's special access services as they are able to do so. For example, this would allow a carrier to reduce the number of special access circuits in one area as it builds out its own facilities, while adding special access circuits in another area as it begins to build a customer base there in advance of deploying facilities there as well, and to continue the pattern in additional areas.

23. In exchange for the discounts and this flexibility, carriers participating in Verizon's commitment discount plans must agree to make up the difference or "shortfall" when they do not maintain their minimum volume level. The "shortfall" is equal to the difference between the amount Verizon would have received had the carrier met the minimum volume level for the service in question less the amount Verizon actually received. This "true up" process occurs at six-month intervals and is determined based on the average number of circuits in service over the six-month period, so that, even if a carrier falls below the minimum volume level during any particular month within that six-month period, there is no shortfall assessment as long as, on average, the carrier met its minimum volume level.

24. Carriers, therefore, have two types of term discount plans to choose from in Verizon's serving territory, each offering different advantages to the customer. For DS1 services, the discount rates are the same for both types of terms plans – *i.e.*, there is no benefit to choosing one plan over the other in terms of the available discount – and the conditions and

charges for early termination are similar. Under the basic circuit-specific term plans, liability for terminating a circuit prior to expiration of the term is equal to the *lesser* of (1) the difference between the rates for the selected term plan and the rates for the longest term plan period that could have been satisfied (or the month-to-month rates if no other commitment period could have been satisfied); or (2) 15 or 50 percent (depending on the plan) of the discounted monthly charges from the date of termination to the end of the term period. So, for example, if a customer places a circuit on a seven-year term plan and terminates after three years, under option "1," the most the customer would pay is the difference between the seven-year and three-year discount rates under those plans. The customer, therefore, receives the benefit of any time for which the service was placed under the plan.

25. Termination liability under the Commitment Discount Plan is calculated in a similar manner. Carriers terminating the Commitment Discount Plan prior to term are liable for the *lesser* of (1) the difference between what the customer paid under the Commitment Discount Plan and what the customer would have paid for the same service volume level under the longest term period that could have been satisfied or (2) 50 percent of the applicable monthly rates for each month (or fraction) remaining in the term period after the minimum service period less any credits the carrier may have received for circuits in service before subscribing to the plan. But termination charges apply under the Commitment Discount Plan only when a carrier terminates the plan entirely and removes all circuits for all service types from the plan.

26. The term plans for the Verizon East states, described above, are set forth in Verizon's interstate access tariffs FCC 1 and FCC 11. Relevant excerpts from those tariffs are attached as Exhibits 7-8 (Term Plans) and Exhibits 9-10 (Commitment Discount Plan). Similar

term plans are available in the Verizon West states under Verizon's interstate access tariffs FCC 14 and FCC 16.

27. Finally, to put the effect of Verizon's term plans in context, Verizon looked specifically at the current holdings of a carrier customer that makes use of both special access and UNEs, **[BEGIN CLEC PROPRIETARY]** **[END CLEC PROPRIETARY]** **[BEGIN CLEC PROPRIETARY]**

[END CLEC PROPRIETARY] and, in the past, has used its network in combination with Verizon's special access services to serve business end users. **[BEGIN CLEC PROPRIETARY]** **[END CLEC PROPRIETARY]** has been purchasing more UNE DS1s and DS3s than it had in the past and has indicated to Verizon that it will purchase special access services only where facilities are not available to provision its UNE orders and then will later convert even those special access circuits to UNEs.

28. Accordingly, Verizon reviewed **[BEGIN CLEC PROPRIETARY]** **[END CLEC PROPRIETARY]** account in its Verizon East territory to determine the financial impact to **[BEGIN CLEC PROPRIETARY]** **[END CLEC PROPRIETARY]** were it to convert its existing UNEs to special access services and place all of its special access services under Verizon's Commitment Discount Plan for a seven-year period. Our analysis showed that if **[BEGIN CLEC PROPRIETARY]** **[END CLEC PROPRIETARY]** converted its existing UNE circuits to special access and placed those special access circuits as well as its existing special access circuits under the Commitment Discount Plans available in the areas **[BEGIN CLEC PROPRIETARY]** **[END CLEC PROPRIETARY]** serves, it would actually achieve costs savings of nearly $500,000 a month compared to what it is currently

paying for its current special access and UNEs services mix. *See* Exhibit 11. And, as explained above, this type of Commitment Discount Plan preserves a carrier's ability to move circuits to its own network as it builds out facilities and to continue to use discounted special access services to build a customer base in additional areas.

29. Contrary to carriers' claims, therefore, Verizon's discount term plans offer substantial savings to carriers who take advantage of these plans, and neither type of plan "locks" carriers into maintaining service with Verizon or requires them to commit a major percentage of their total special access revenue spending with Verizon. There is no minimum volume to participate in Verizon's circuit-specific term plans, and the volume of high-capacity circuits required to participate in the Commitment Discount Plan is minimal, only 14 DS1s or 1 DS3. Carriers can terminate their service under either plan at any time by paying termination charges that are not particularly onerous and that give them the benefit of any discount for which they actually qualified.

D. Carriers' Use of Special Access to Supplement or Fill In Network Facilities.

30. We conducted further analysis to determine the extent to which carriers may be using Verizon's special access service to extend the reach of or "fill-in" their fiber networks or the networks of alternative fiber providers they may be using. First, within each of the 40 MSAs we studied, we used data we obtained from GeoTel, a leading provider of information related to alternative telecommunication provider networks, and our own physical inspections of collocation arrangements in a number of Verizon wire centers, *see* Verses/Lataille/Jordan/Reney Decl. ¶¶ 9-18, Exs. 3A-B and 4A-B, to identify wire centers where carriers have their own fiber facilities. Next, to identify carriers who were using Verizon's special access services to serve business end users from those same serving wire centers, we analyzed data we previously

collected for a subset of our carrier customers who purchase predominately Verizon's special access services, not UNEs, in instances where they use Verizon's facilities. Taken together this provides a wire center list of competitive fiber providers and carriers that reach customers using special access. *See* Exhibit 12.

31. The results show two things: (1) that in many wire centers within Verizon's top 40 MSAs, some carriers have both their own facilities and are using Verizon's special access services to serve business end users (Verizon has highlighted in Exhibit 12 instances where these "matches" of fiber facilities and special access use occur); and (2) that in many of the wire centers where this subset of carriers is using Verizon's special access services to serve business end users, there are also a number of alternative providers with fiber facilities. This means that some carriers with fiber presumably are using special access to extend the reach of that fiber and other carriers may be using competitive fiber in conjunction with special access.

32. We also sorted the data by wire center to identify wire centers with 5000 or more total business lines. We had previously determined that virtually all of these wire centers had carriers serving customers with Verizon's special access service. For this subset of Verizon wire centers within Verizon's top 40 MSAs, we now also identified and counted the number of carriers who had deployed their own fiber facilities. As Exhibit 13 shows, the wire centers with 5000 or more business lines within these MSAs have on average more than four alternative providers with their own fiber facilities.

III. Response to Carrier Claims That They Have Been Forced to Use Special Access.

33. In our initial declaration, we showed that carriers purchasing DS1 and DS3 services from Verizon are purchasing primarily Verizon's special access service and not UNEs. *See* Verses/Lataille/Jordan/Reney Decl. ¶¶ 52-59. In response, carriers claim that they have

purchased and retained Verizon's DS1 and DS3 special access services only because they were required to buy special access service when facilities were not available to provision the UNE circuits they requested and, therefore, the circuits had to be converted subject to the terms of Verizon's interstate access tariffs. This means, they argue, that Verizon's previous analysis, *see* Verses/Lataille/Jordan/Reney Decl. ¶¶ 52-59, overstates significantly the extent to which carriers have used special access instead of UNEs to serve customers. We demonstrate, however, that even taking into account UNE orders that have been rejected because Verizon lacked the facilities necessary to provision them, our previous analysis of the extent to which carriers are using special access instead of UNEs to serve customers does not change substantially. We also explain our special access minimum service period policies and show that carriers are able to and have been converting eligible special access circuits to UNEs.

A. UNE Orders Rejected for Lack of Facilities.

34. First, we found that even when UNE orders rejected for lack of facilities are factored into our previous analysis, carriers are still using overwhelmingly Verizon's special access service, not UNEs, to serve their customers.

35. We obtained from Verizon's ordering systems the number of DS1 and DS3 UNE orders for which a "no facilities" alert was generated when the order was placed for the period January through August 2004. A "no facilities" alert is issued when Verizon's ordering and provisioning systems cannot identify and assign facilities necessary to provision a UNE order. *See* Exhibit 14. We then determined the orders that actually were provisioned as UNEs despite having received a "no facilities" alert. *Id.* As Verizon has explained in the past, one reason this may occur is that Verizon's policy has been to provision UNE orders where construction of facilities necessary to fulfill the UNE order is in progress, even if the facilities are not available

when the order is placed. *See* Letter from William S. Randolph, Verizon, to Marlene H. Dortch, FCC, CC Docket Nos. 01-338 *et al.* (Oct. 18, 2002). Verizon determined that some of these circuits were provisioned as UNEs on that basis. *See* Exhibit 14.

36. We analyzed what effect the remaining UNE orders that were actually rejected for lack of facilities had on Verizon's previous analysis of carriers' use of special access services compared to UNEs. *See* Verses/Lataille/Jordan/Reney Decl. ¶¶ 52-59, Ex. 10A-D. Although our prior analysis was based on circuits in service as of March 2004, taking the most conservative approach, we assumed that each of the DS1 and DS3 UNE orders that were rejected from January through August 2004, were counted as special access circuits in our previous analysis. *See* Verses/Lataille/Jordan/Reney Decl., Ex. 10A-D. Using our previous analysis, we then overlayed the total number of rejected DS1 and DS3 circuits on the number in service as of March 2004, as reflected in Exhibits 11 and 12 of the Verses/Lataille/Jordan/Reney Declaration.

37. First, we counted the total number of DS1 and DS3 circuits that had been requested in the rejected UNEs orders and added the rejected DS1 UNEs to the UNE and EEL column in Exhibit 11 of the Verses/Lataille/Jordan/Reney Declaration, and the rejected DS3 UNEs to the UNE and EEL column in Exhibit 12 of that declaration. We then subtracted the same amounts from the respective DS1 and DS3 special access columns on Exhibits 11 and 12 of the Verses/Lataille/Jordan/Reney Declaration. As attached Exhibits 15 and 16 show, even if one assumes that carriers would have purchased these DS1 and DS3 circuits as UNEs instead of special access, the extent to which carriers are using special access service instead of UNEs to serve customers does not change significantly. The data show that carriers still would have purchased 93 percent of their DS1s as special access circuits compared to 7 percent as UNEs and 98 percent of their DS3s as special access circuits compared to 2 percent as UNEs. *Id.*