

**Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, D.C.**

In the Matter of	)	
	)	
Verizon Communications, Inc. and	)	WC Docket No. 05-75
MCI, Inc. Applications for Approval	)	
of Transfer of Control	)	

**COMMENTS OF  
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## INTRODUCTION

The proposed merger of Verizon Communications Inc. (“Verizon”) and MCI, Inc. (“MCI”), along with the pending merger of SBC Communications Inc. (“SBC”) and AT&T Corporation (“AT&T”), portends a tremendous consolidation in the vital and changing telecommunications industry, which will shape the world for a long time. Predictably, Verizon and MCI project in their filing a dynamically competitive outlook, and see the proposed merger as affording opportunities for them to innovate, to compete more efficiently, and to offer consumers greater product choices. However, there is great potential for this merger to cause significant competitive harm, which may prevent telecommunications markets from developing competitively in the fashion that Verizon and MCI predict.<sup>1</sup> For that reason, the Commission should not approve this merger unless and until it is satisfied that the merger’s potential anticompetitive impacts can be avoided and that the proposed combination is in the public interest.

In asserting that the proposed merger is in the public interest, the Application for Transfer of Control (“Application”) states that:

The transaction will marry Verizon’s best-in-class broadband, wireless, and local wireline networks with MCI’s Internet backbone and global reach. This combination will benefit large enterprise customers by creating a strong new competitor with the network reach and financial resources to compete in this technologically intensive and highly competitive market segment. . . . The transaction will also benefit mass-market consumers, by establishing the nation’s most advanced broadband platform, capable of delivering next-generation multimedia services in markets across the country.<sup>2</sup>

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<sup>1</sup> The pendency of the proposed SBC/AT&T merger exacerbates the potential for post-merger mischief to the public interest.

<sup>2</sup> Application at 3.

But this very same marriage – and the leverage it would create – threatens significantly to hinder the opportunities for future competition. It is these opportunities that the Commission needs to protect and encourage.

Based on the Application and other publicly available materials, the New York Attorney General’s Office has two primary areas of concern that must be addressed before the Commission could find this transaction to be in the public interest. First, the Federal Communications Commission (“FCC” or “Commission”) must require that, post-merger, Verizon offers stand-alone Digital Subscriber Line (“DSL”) service to all customers. Second, the Commission must take steps to ensure that competitors have non-discriminatory access to the Internet backbone that MCI controls, which will be combined with Verizon’s own backbone and network. The expected concentration of the nationwide Internet backbone – which is an integral part in the transformation of the telecommunications industry – is particularly significant. For, post-merger, SBC/AT&T and Verizon/MCI would control over half of the backbone assets.<sup>3</sup>

It is, at the very least, essential to protect consumers and competitors from diminished or degraded services that depend on the Internet background. The Commission similarly must ensure that nascent technologies are able to mature into true competition for the bundled services that a combined Verizon/MCI will offer.

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<sup>3</sup> See Nicholas Economides, *The Economics of the Internet Backbone*, NYU Law and Economics Working Papers, Paper 4, p. 6 (2004).

## **DESCRIPTION OF THE VERIZON / MCI MERGER**

Verizon Communications Inc. is a Delaware corporation, with its principal office at 1095 Avenue of the Americas, New York, New York 10036. MCI, Inc. is also a Delaware corporation, with its principal office at 22001 Loudoun Parkway, Ashburn, Virginia 20147.

On February 14, 2005, MCI and Verizon announced a proposed plan of merger pursuant to which MCI will become a direct, wholly owned subsidiary of Verizon. MCI and Verizon believe that the merger will create “a strong, U.S.-based globally competitive Internet protocol communications network and services provider, positioned to put an American company in a leadership role in the globalization and expansion of advanced IP [Internet protocol] communications and services.”<sup>4</sup>

Under the merger agreement, MCI shareholders will receive a combination of cash and shares of Verizon stock. The Proxy Statement is being distributed to MCI shareholders as they must vote to approve or reject the transaction. The shareholder vote is expected to take place in June 2005. Assuming shareholder and regulatory approval, Verizon expects the merger to close in the first half of 2006.

On March 11, 2005, Verizon and MCI filed an Application for Transfer of Control, seeking the FCC’s approval.

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<sup>4</sup> Proxy Statement filed by Verizon Communications Inc. with the U.S. Securities and Exchange Commission on April 12, 2005 (“Proxy Statement”).

## THE NEW YORK ATTORNEY GENERAL'S INTEREST

The Attorney General is charged with enforcing state and federal antitrust and consumer protection laws. The Attorney General advocates in Commission proceedings on behalf of New York State, consumer and small business interests, and the public interest generally.

Through Verizon New York Inc., Verizon Communications Inc. provides regulated telecommunications services in New York. MCI's subsidiaries provide telecommunications services on a regulated and unregulated basis in New York.

Telecommunications is vital to New York's information-intensive economy. Competition in telecommunications is the driving force behind fair prices, high quality, innovative offerings and greater access to services in the industry. Accordingly, in reviewing whether telecommunications transactions are in the public interest, the Commission plays an essential role in ensuring that competition remains robust.

The Attorney General submits these comments in response to the Commission's request for comments addressing the proposed merger's potential public interest impact.<sup>5</sup>

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<sup>5</sup> WC Docket No. 05-75, In the Matter of Verizon Communications, Inc. and MCI, Inc. Applications for Transfer of Control, *Commission Seeks Comment on Applications for Consent to Transfer of Control Filed by Verizon Communications, Inc. and MCI, Inc.*, issued March 24, 2005.

## DISCUSSION

### 1. The Commission's Review Standard.

The Commission's task in this proceeding is to weigh the proposed merger to verify that approval would be in the public interest. In evaluating a prior merger between Bell Atlantic Corporation and GTE Corporation, the Commission described this test as follows:

Before approving the transfer of control of licenses and lines in connection with the proposed merger, the Commission must determine, pursuant to sections 214(a) and 310(d) of the Communications Act, that the proposed transfers serve the public interest. In accordance with the Act's public interest standard, we must weigh any potential public interest harms of the proposed transaction against the potential public interest benefits to ensure that, on balance, the merger serves the public interest, convenience, and necessity. In doing so, we examine, *inter alia*, possible competitive effects of the proposed transfers and measure the effect of the merger on both the broader aims of the Communications Act and federal communications policy.<sup>6</sup>

The Applicants bear the burden of proving by a preponderance of the evidence that, on balance, the proposed transaction serves the public interest. In applying this public interest test, the Commission considers four questions: (1) whether the transaction would result in a violation of the Communications Act; (2) whether the transaction would result in a violation of the Commission's rules; (3) whether the transaction would substantially frustrate the Commission's ability to implement or enforce the Communications Act; and (4) whether the merger promises to yield affirmative public interest benefits that could not be achieved without the merger.<sup>7</sup>

The Commission must make an independent public interest determination that includes an evaluation of the merger's likely effect on future competition. Because Congress has determined that additional competition in telecommunications markets will better serve the public interest, **in order to conclude that a merger**

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<sup>6</sup> CC Docket No. 98-184 - In re Application of GTE Corporation, Transferor, and Bell Atlantic Corporation, Transferee For Consent to Transfer Control of Domestic and International Sections 214 and 310 Authorizations and Application to Transfer Control of a Submarine Cable Landing License, *Memorandum Opinion and Order* (Adopted: June 16, 2000 Released: June 16, 2000) at 20 (footnotes omitted), 15 FCC Rcd 14032.

<sup>7</sup> *Id.* at 22.

**is in the public interest, the Commission must be convinced that it will enhance competition, not merely [sic] lessen it.<sup>8</sup>**

Where necessary, the Commission can attach conditions to a transfer of lines and licenses to ensure that the public interest is served by the transaction. Section 214(c) of the Act authorizes the Commission to attach to the certificate "such terms and conditions as in its judgment the public convenience and necessity may require." Similarly, section 303(r) of the Communications Act authorizes the Commission to prescribe restrictions or conditions, not inconsistent with law, that may be necessary to carry out the provisions of the Act. Indeed, unlike the role of antitrust enforcement agencies, the Commission's public interest authority enables it to rely upon its extensive regulatory and enforcement experience to impose and enforce conditions to ensure that the merger will yield overall public interest benefits.<sup>9</sup>

**2. Absent the imposition of conditions by the Commission, the proposed merger would not serve the public interest.**

In addition to the proposed Verizon/MCI merger, the Commission is also reviewing a proposed merger of SBC and AT&T. The combined potential impact of these two transactions upon the state of competition nationally – and in every region of the country – warrants heightened Commission concern over the future competitive landscape of the telecommunications industry. For example, if both mergers are consummated without divestitures and conditions, SBC and Verizon would gain control of half of the nationwide Internet backbone (currently held by AT&T and MCI).<sup>10</sup> Their combined share probably would be even higher because SBC and Verizon already operate their own Internet backbone elements. When combined with other network elements and services offered by these companies, the post-merger Verizon and SBC companies will dominate the telecommunications market.

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<sup>8</sup> *Id.* at 23 (emphasis added).

<sup>9</sup> *Id.* at 24.

<sup>10</sup> See Economides, *The Economics of the Internet Backbone*, at 6.



Verizon asserts that it faces numerous competitors across business lines, and “[t]he combination of Verizon and MCI will also enhance the ability of the combined firm to develop innovative services.”<sup>11</sup> However, consumer access to some of Verizon’s telephone service competitors, such as other Voice over Internet Protocol (“VoIP”) providers, will be limited to the degree that consumers do not have free and unfettered access to broadband internet connections, including Verizon’s DSL service. The post-merger Verizon would be in a position to stifle such access and, in so doing, to hamper innovation and competition.

Thus, the Commission should not approve the merger without requiring Verizon to provide unbundled, stand alone DSL service to all customers and not to discriminate in favor of its own services in the use of its Internet backbone. Imposing these limited conditions on the merger will ensure that there is, in fact, greater opportunity for competitive access, future innovation and improved services.

**a. Unbundled DSL is Necessary to Maintain Competition.**

Verizon offers consumers access to the Internet through broadband connections known as Digital Subscriber Lines (“DSL”). As provided by Verizon, DSL service is a dedicated high speed digital connection to the Internet that is provided over traditional copper telephone lines, and that does not interfere with customers’ telephone service supplied over the same line.

Verizon offers DSL service to its small businesses and residential customers over its standard wireline connection.<sup>12</sup> As explained below, DSL service allows customers to access Internet-

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<sup>11</sup> Application, Attachment 1 (Bamberger, Carlton, Shampine Declaration) at ¶ 7.

<sup>12</sup> While other variations of DSL, used primarily by medium and larger business customers, do not share a telephone line with voice traffic, the focus of these comments is on the residential and small business DSL market.

based telephone services, as well as other products that compete with telephone and other services offered by Verizon.

**i. High-speed Internet Access is Necessary for a Number of Internet-based Services.**

The Application states that “intermodal alternatives such as cable, wireless, and VoIP already provide significant and intensifying competition for mass-market customers, particularly in Verizon’s service territory. This transaction will not in any way reduce this intermodal competition.”<sup>13</sup> However, the Application fails to note that these competitive services rely upon broadband access – such as that provided by Verizon’s DSL service, typically, on a bundled basis with Verizon’s voice service.

For instance, VoIP holds out the potential to become a major competitor to wireline telephone services. But VoIP requires customers to secure broadband access from another provider. By selling its DSL service bundled with its monopoly voice service, Verizon discourages its DSL customers from using VoIP competitors. Verizon customers wishing to use competitors’ VoIP, instead of Verizon’s wireline service, will have to choose between securing broadband services from a local cable operator, typically at a higher cost than DSL service – or else continuing to purchase the bundled Verizon wireline/DSL product, and adding the cost of a competitor’s VoIP on top of that.<sup>14</sup>

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<sup>13</sup> Application, at 34-5.

<sup>14</sup> An additional impediment that can arise when a customer moves to VoIP is porting the customer’s telephone number to the new service provider. Customers are reluctant to try these new, innovative voice services absent assurance that they can keep their phone number. FCC regulatory orders therefore require local service carriers to port customers’ numbers. *See, e.g.* CC Docket No. 95-116 - In the Matter of Telephone Number Portability, *Second Further Notice of Proposed Rulemaking* (released September 16, 2004). Only with the recent change in Verizon

Verizon is acutely aware of losses in wireline services to competitive VoIP and other services. As Verizon's 2004 Quarterly Report summarizes, "our emphasis is on. . . devoting more resources from traditional services, where we have been experiencing access line losses, to the higher premium growth markets such as wireless, digital subscriber lines (DSL), long distance and other data services."<sup>15</sup> Indeed, Verizon introduced its own nationwide VoIP product, VoiceWing,<sup>16</sup> in 2004 and, thus, has further incentives to hinder competitive VoIP products through means other than competition on the merits. MCI likewise offers a VoIP product, marketed under the MCI Advantage name.<sup>17</sup>

Until recent regulatory changes altered the pricing structure whereby Competitive Local Exchange Carriers ("CLECs") lease Verizon's local facilities, both MCI and AT&T had made significant inroads as competing local telephone providers using Verizon's facilities, especially in New York. Since those regulatory changes became final, however, these two largest of the CLECs announced that they have ceased marketing to new customers and, as a result, the prospect of mass market telephone service competition using unbundled network elements is dim. As a result, Verizon's only remaining competition for telephony is from cable and DSL-based VoIP providers. Given Verizon's monopoly of wireline services, Verizon has little incentive to open its network to those offering competitive services.

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practices, described below, are customers able to port their wireline telephone numbers to a VoIP or facilities-based voice provider, and still keep their existing DSL service.

<sup>15</sup> Verizon Communications Inc., 2004 Quarterly Report (for the period ending September 30, 2004), p.20 (2004).

<sup>16</sup> *Id.*

<sup>17</sup> MCI, Inc., 2003 Annual Report 9 (2004).

**ii. Verizon Offers Stand-Alone DSL Only on a Limited Basis.**

In early April 2005, the Federal Communications Commission ordered Verizon and other carriers to allow their existing customers who subscribe to the carriers' voice and DSL service to port their phone numbers to a new voice carrier.<sup>18</sup> In response, Verizon informed competing voice carriers that such customers should be advised that porting the number, and thus terminating their Verizon voice service, would cause their Verizon DSL service to be disconnected as the services were not separable. More recently, on April 18, 2005, Verizon publicly expressed a willingness to allow existing customers in the former Bell Atlantic service territories to maintain their Verizon DSL service in the event that they discontinue Verizon's telephone service.<sup>19</sup> However, even this option is not available to new Verizon customers or those outside the former Bell Atlantic service territories.

Before announcing these recent changes, Verizon claimed that customer identification issues prevented it from offering wireline and DSL services independent of each other. By contrast, Qwest Communications International Inc., the smallest regional phone company, has

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<sup>18</sup> Memorandum Opinion and Order and Notice of Inquiry in response to BellSouth's Petition regarding issues stemming from the Triennial Review Order (FCC Docket Number WC 03-251). *See also, Verizon Offers a Deal on DSL*, The Atlanta Journal-Constitution, May 28, 2004 ("customers in 12 states who are moving their local phone numbers to wireless devices can keep their high-speed Internet service. . . spokeswoman Briana Gowing said").

<sup>19</sup> Matt Richtel, *Some Verizon Customers to Get Stand-Alone D.S.L.*, N.Y. Times, April 19, 2005, at C7. In conjunction with the April 18, 2005 announcement, in a notice to CLECs, Verizon explained that CLECs no longer had to alert customers that porting *would* result in disconnecting their DSL service. Instead, Verizon said that CLECs should alert customers that DSL service *might* be disconnected, and that the customer should contact Verizon to determine how to handle the service. There still seems to be some ambiguity whether every existing Verizon customer seeking stand-alone DSL will actually be able to do so. Moreover, Verizon has also not disclosed whether its stand-alone DSL will be priced at a premium or at a price comparable to that of the DSL component of the bundled product.

offered stand-alone DSL for quite some time.<sup>20</sup> The inference is inescapable that Verizon's stalling is designed to hinder competition from other VoIP providers.

Meanwhile, Verizon seeks to expand its fiber-to-the-premises (FTTP) network, which will replace its DSL service and allow Verizon to offer a broader array of products to better compete with the highspeed broadband services offered by cable providers. Thus far, however, FTTP is available only in limited areas.<sup>21</sup> While the roll-out of FTTP progresses, Verizon has little incentive to offer stand-alone DSL – particularly when refraining from doing so hinders VoIP providers from competing against Verizon's monopoly voice product.

Verizon's Annual Report indicates that offering unbundled services is not likely to be a high priority for Verizon at all, as the bundles themselves give Verizon a competitive advantage over other service providers. Verizon's 2004 Annual Report highlights the company's "continuing initiatives to more effectively package and add more value to our products and services. Innovative product bundles include local wireline services, long distance, wireless and DSL for consumer and business retail customers. . . . These efforts will also help counter the effects of competition and technology substitution that have resulted in access line losses in

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<sup>20</sup> Yuki Noguchi, *Merger Critics Seek Telecom Regulation*, Wash. Post., April 20, 2005, at E5.

<sup>21</sup> News Release, Verizon Communications, Inc., *Verizon Brings Blazing-Fast Computer Connections to 5 Long Island Communities*, (April 11, 2005) at <http://newscenter.verizon.com/proactive/newsroom/release.vtml?id=90318> ("Verizon customers in Massapequa, Wantagh, Franklin Square, Port Washington and Oyster Bay now can experience breathtaking high-speed Internet access as the company begins to offer its Verizon FiOS<sup>sm</sup> (FYE'-ose) Internet Service to homes here.").

recent years.”<sup>22</sup>

While many consumers like bundled services, others prefer to choose their services *a la carte*. Unbundled service offers allow competitors to compete on a product-by-product basis – and consumers benefit accordingly. The continued availability of *a la carte* offerings as well as bundled services allows consumers to maximize the benefits of competition.

**iii. The Commission Should Require that Verizon Offer Stand-Alone DSL.**

The public interest should not depend on whether Verizon decides on its own volition to offer stand-alone DSL (or FTTP broadband). Verizon and other ILECs failed to exploit DSL technology for over a decade, and when faced with attempts by COVAD, Northpoint and others to introduce DSL, Verizon raised a host of obstacles to this new competitive service. It was only after much resistance that Verizon allowed Internet Service Providers (“ISP”) to purchase and resell DSL access at all.<sup>23</sup> Recognizing the advantage that Verizon derives from limiting its DSL

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<sup>22</sup> Verizon Communications Inc., 2004 Quarterly Report (for the period ending September 30, 2004), pp. 20-21 (2005) (emphasis added). *See also* Verizon Communications Inc., 2003 Annual Report, Exhibit 13 (2004) (noting that decreases in certain revenue streams were “partially offset by increased demand for our DSL services”). Last year, Verizon noted that “[a]s of year-end 2003, approximately 48% of Verizon’s residential customers have purchased local services in combination with either Verizon long distance or Verizon DSL, or both.” Verizon Communications Inc., 2003 Annual Report, p. 6 (2004). By September 30, 2004, that number had increased to 53%. Verizon, 2004 Quarterly Report (for the period ending September 30, 2004), p. 26 (2005).

<sup>23</sup> *See* NYSPSC Case 00-C-0127 - Proceeding on Motion of the Commission to Examine Issues Concerning the Provision of Digital Subscriber Line Services, *Opinion and Order Concerning Verizon’s Wholesale Provision of DSL Capabilities* (issued October 31, 2000) (after many months of industry collaborative negotiations failed to resolve key issues, the NYSPSC instituted a litigation proceeding to determine when, and on what terms, DSL providers would be able to serve customers over Verizon’s lines); *see also* 14 FCC Rcd. 20,912, CC Docket 98-147 - In the Matter of Deployment of Wireline Services Offering Advanced Telecommunications Capability and CC Docket No. 96-98 - Implementation of the Local Competition Provisions of

service to a bundled product, the Commission may fairly infer that Verizon is unlikely to act expeditiously to expose its DSL product to competition on the merits.

Thus, in order to ensure the competitive environment that most benefits consumers, the Commission should condition the merger on the combined Verizon/MCI offering stand-alone DSL service to all customers, existing or otherwise, not later than 30 days following Commission approval.

**b. The Commission Should Assure Nondiscriminatory Access to the Internet Backbone Post-Merger.**

**i. The Internet Backbone.**

A basic understanding of how the Internet works is central to appreciating the competitive implications of a Verizon/MCI combination. The primary Internet infrastructure in the U.S. has approximately ten major backbones – often referred to as “Tier 1 providers”– plus independent Internet Service Providers. MCI is a Tier 1 provider. The Internet backbone is relatively concentrated. According to In Stat-MDR, a market research firm, “[a]t the end of 2000, 10 backbone providers generated 92 percent of all wholesale ISP revenues” in the U.S.<sup>24</sup> The three top providers were:<sup>25</sup>

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the Telecommunications Act of 1996, *Third Report and order in CC Docket No. 98-147 and Fourth Report and order in CC Docket No. 96-98.*

<sup>24</sup> ISP-Planet Staff, *ISP Backbone Market Forecast: Flat Through 2002* at [http://isp-planet.com/research/2002/backbone\\_020123.html](http://isp-planet.com/research/2002/backbone_020123.html).

<sup>25</sup> *Id.*

	<u>%</u>
WorldCom (MCI)	44.0
Genuity	12.5
Sprint	9.4

The vast majority of Internet users in the United States access the Internet infrastructure through ISPs.<sup>26</sup> While AOL is by far the largest ISP, many smaller ISPs exist, some of whom have customers only in limited regions.<sup>27</sup>

The network backbone comprises: (a) high speed hubs, to which customer data packets, including electronic mail and voice services, are sent by ISPs, and (b) high speed circuits that connect the hubs to move data from one location to another. Thus, the Internet backbone provides data transport and routing services, moving the data to the appropriate destinations with a minimum of loss and delay. In most instances, the data is broken up into smaller packets to speed delivery. As a result, the data packets usually flow over multiple providers' backbones before reaching their final destinations; therefore, backbones must interconnect to exchange customer traffic.<sup>28</sup>

Tier 1 Internet providers achieve interconnection of their backbones through what is

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<sup>26</sup> Nicholas Economides, *The Economics of the Internet Backbone*, NYU Law and Economics Working Papers, Paper 4, p. 4 (2004).

<sup>27</sup> One example of a local New York ISP is Bestweb, based in the Hudson Valley and serving Downstate New York ([www.bestweb.net](http://www.bestweb.net)).

<sup>28</sup> Nicholas Economides, *The Economics of the Internet Backbone*, p. 3-7. For a more detailed understanding of the Internet backbone see Michael Kende, *The Digital Handshake: Connecting Internet Backbones*, FCC Office of Plans and Policy Working Paper No. 32 (September 2000) and Nicholas Economides, *The Economics of the Internet Backbone*, NYU Law and Economics Working Papers, Paper 4 (2004).



known as “peering.” Through peering, Tier 1 providers agree to afford each other the ability to freely move data across networks without fees, in mutually beneficial arrangements. Smaller backbones, on the other hand, are frequently considered free riders, as they generate too little traffic to be peering partners.<sup>29</sup> Because Tier 1 providers generally do not consider peering with small providers sufficiently beneficial, to move data, smaller providers usually must enter into fee-based agreements - called “transit” arrangements - with Tier 1 providers.

These fee-based arrangements for interconnection are not necessarily problematic in a competitive market. However, if only a few providers control backbone access, the resulting opportunity for these few to hinder the operations of smaller backbones by refusing to interconnect with them, or by imposing onerous fees or conditions on interconnecting, has significant public interest implications. Those Tier 1 providers in control would have both the ability and incentive to, for example, charge significantly higher fees, prioritize their own data packets, block certain ISP transmissions, or end entirely their cooperative relationships with smaller backbones.<sup>30</sup>

Consequently, regulatory action has been necessary to preserve competition when the Internet backbone was threatened by prior corporate combinations and mergers. In 1998, WorldCom, the owner of Internet backbone assets, proposed to acquire MCI, then the owner of UUNet backbone assets. To avoid increased concentration of Internet backbone assets as a result of the merger, as a condition to the WorldCom/MCI transaction, the FCC required WorldCom to

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<sup>29</sup> Nicholas Economides, *The Economics of the Internet Backbone*, NYU Law and Economics Working Papers, Paper 4, p. 4 (2004).

<sup>30</sup> Kende, *The Digital Handshake: Connecting Internet Backbones*, pp. 18-23.

divest its backbone assets to Cable & Wireless.<sup>31</sup> Similarly, in considering the merger application of Bell Atlantic and GTE (which resulted in the formation of Verizon), the FCC weighed the public interest ramifications of the merger's impact on the Internet backbone, concluding that the merging parties had "not demonstrated any merger-specific benefits to the market for Internet backbone services."<sup>32</sup> Accordingly, the Commission conditioned its approval of the GTE/Bell Atlantic merger in part on GTE's divestiture of its Internet backbone.

As these transactions reflect, there is a strong public interest in preventing increased concentration in ownership of Internet backbone assets. The Verizon/MCI merger, too, requires regulatory vigilance.

**ii. Verizon and MCI's Internet Backbones.**

MCI, by its own acknowledgment, owns "one of the most extensive Internet protocol backbones."<sup>33</sup> One estimate of MCI's market share of the national Internet backbone was 32% in 2003, with AT&T representing the closest competitor, at 19%.<sup>34</sup> More recently, MCI has

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<sup>31</sup> CC Docket No. 97-211 - Application of WorldCom, Inc. and MCI Communications Corporation for Transfer of Control of MCI Communications Corporation to WorldCom, Inc., *Memorandum Opinion and Order*, FCC 98-225 (rel. Sept. 14, 1998).

<sup>32</sup> CC Docket No. 98-184 - In re Application of GTE Corporation, Transferor, and Bell Atlantic Corporation, Transferee For Consent to Transfer Control of Domestic and International Sections 214 and 310 Authorizations and Application to Transfer Control of a Submarine Cable Landing License, *Memorandum Opinion and Order*, released June 16, 2000, at ¶ 215.

<sup>33</sup> MCI, Inc., 2003 Annual Report 2 (2004).

<sup>34</sup> Economides, *The Economics of the Internet Backbone*, at 6. If SBC acquires AT&T, SBC and Verizon, by virtue of the backbone control currently held by AT&T and MCI, respectively, would control half of the nationwide Internet backbone (and possibly more, given that SBC and Verizon may operate their own Internet backbone elements acquired prior to the two pending mergers).

reported that its backbone network “has been recognized for the fourth consecutive year. . . as the world’s most connected Internet backbone playing a critical role in the movement of Internet traffic. Our expansive IP footprint, coupled with our direct interconnections, enables our customers to reach more destinations directly through our global Internet backbone than any other communications provider.”<sup>35</sup>

MCI’s extensive backbone thus represents an attractive, strategic asset. According to MCI’s 2003 Annual Report, MCI occupies:

a strategically important position within the communications market. . . due to the extremely rapid growth of Internet usage resulting from the increasing availability of high speed broadband access, the decreasing cost of all types of Internet access, the expanding volume of informative and entertaining content, the continued improvement in email and instant messaging, and the ever increasing number of personal computers, and other devices for accessing the Internet. Corporations and government entities have responded by developing additional applications to run over the Internet that allow communications and e-commerce transactions with customers, communications with employees and the transfer of data among offices and operating units.<sup>36</sup>

Although public information regarding Verizon’s current Internet backbone ownership is incomplete, there can be no doubt that the opportunity to amass a dominant Internet backbone position is a significant feature of the MCI merger:

The Verizon/MCI combination of product offerings will provide a stronger, and geographically broader, converged solution for large enterprises. Verizon currently has strong IP-based offerings, but they have limited reach within its area footprint and Verizon is not a major provider of IP-based services. MCI’s core strength is its global Internet backbone, which provides global IP connectivity today, and will be able to provide next-generation VoIP and other IP-based

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<sup>35</sup> MCI, Inc., 2004 Quarterly Report (for the period ending September 30, 2004) 33 (2004).

<sup>36</sup> MCI, Inc., 2003 Annual Report 15 (2004).

services worldwide tomorrow.<sup>37</sup>

Verizon – whose objective is, of course, to secure merger approval – showcases potential procompetitive benefits: “The combined company will thus be able to offer converged IP-based solutions to large enterprise customers with nationwide and global needs, as well as grow its application services on a broader scale.”<sup>38</sup>

But there are also significant risks of adverse consequences to competition and innovation. Despite this, the Joint Petition fails to identify: (1) whether Verizon already controls a share of the Internet backbone, (2) the share of the Internet backbone held by MCI, and (3) the combined share of the Verizon/MCI assets. These omissions are striking. As noted, the FCC previously expressed concern about concentration in the Internet backbone market when it had before it the Bell Atlantic/GTE merger:

Although we agree with the Applicants that the Internet backbone market is highly concentrated, we nonetheless conclude that the Bell Atlantic and GTE have presented insufficient evidence regarding how their proposed merger would alleviate such concentration and benefit consumers of long-haul data services.<sup>39</sup>

Here too, evidence of the effect of this combination on backbone ownership concentration is lacking.

In consequence, the Commission should direct Verizon to provide the information needed to make an informed decision regarding the extent to which backbone concentration will increase as a result of the proposed merger with MCI. Based on that information, together with further

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<sup>37</sup> Application, p. 17 (citations omitted).

<sup>38</sup> *Ibid.*

<sup>39</sup> CC Docket 98-184, *supra*, at ¶ 215 (footnote omitted).

public comments evaluating it, the appropriateness of divestiture of backbone assets should be assessed.

There is, however, a need for Commission to do more than address concentration concerns. As a combined Verizon/MCI moves to offer more bundled product packages over its backbone – such as combining VoIP and video – the increased need for bandwidth may strain its existing system, encouraging Verizon to give priority to its own products to the detriment of consumers whose information must travel across the Internet backbone, but who use non-Verizon providers. A Verizon-MCI combination would also have the ability adversely to impact other Internet backbone providers who lack the capacity to offer the same panoply of services. Vital public policy, therefore, requires that a Verizon acquisition of MCI's internet backbone, when combined with Verizon's current internet backbone holdings, not diminish either consumers' or competitors' equal and unfettered access to the Internet.

This is, indeed, a concern that some stand-alone service providers have already voiced. As Jeffrey Citron, the CEO of Vonage, a major VoIP provider, testified before a United States Senate Committee, "Vonage's service is dependent upon reasonable and non-discriminatory access to the network infrastructure . . . ." <sup>40</sup> That access, Mr. Citron further explained, is jeopardized from transactions such as this merger, which "consolidat[e] ownership and control over the communications infrastructure on which Vonage and other competitors . . . rely to provide service to end users." <sup>41</sup> Similarly, the head of the Consumers Union has stated that if the

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<sup>40</sup> Written Statement of Jeffrey Citron, *United States Senate Committee on the Judiciary, Antitrust Subcommittee*, April 19, 2005.

<sup>41</sup> *Id.*

Verizon/MCI and SBC/AT&T mergers are approved, “Verizon and SBC are well-positioned to dominate and make it more difficult for other backbone providers to offer packages of services.”<sup>42</sup> In other words, the concentration of Internet backbone owners could have anti-competitive effects on service providers and, in turn, on their customers.

The core risk in this regard is that, post-merger, Verizon will have an Internet backbone that carries its own products in first class, while competitors ride in coach – or, indeed, never get to ride at all. As noted above, Verizon plans to utilize the Internet backbone to provide “IP connectivity for VoIP services today and other IP-based services tomorrow.”<sup>43</sup> This approach dovetails with MCI’s own pre-merger strategy of “converging Internet, data, and voice traffic onto a common IP backbone.”<sup>44</sup> MCI’s convergence strategy was driven by “technological and market trends and on the strong competitive position of our IP network. The common IP backbone we envision will integrate our IP network and our existing frame relay, ATM and voice networks modified to operate under a unified standard IP protocol.”<sup>45</sup> In addition to voice communications being handled as VoIP, MCI’s strategy calls for data, video and software applications traffic to be converted to digitized packets for routing across IP networks. Accordingly, MCI believes that “[t]hrough our strategy of integrating our network onto a common IP backbone and enhancing its capabilities, we are seeking to position ourselves as a

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<sup>42</sup> Jonathan Krim, *Mergers Raise Concerns Over Internet Access*, Wash. Post, Feb. 16, 2005 at E1.

<sup>43</sup> Application, at 12.

<sup>44</sup> MCI, Inc., 2003 Annual Report 15 (2004).

<sup>45</sup> *Id.*

provider of emerging services such as grid computing and web services.”<sup>46</sup>

The sort of products envisioned by this Verizon/MCI strategy consume relatively large amounts of Internet bandwidth. And a combined Verizon/MCI entity would be well positioned to create an Internet infrastructure that could severely diminish the capacity available to competitive providers of these services that need to use Verizon’s Internet backbone. By way of example, there exists today a process known as “tagging,” which allows a provider to use rule-based and policy-based filtering to limit the flow of data packets. If packets are “tagged,” the network recognizes the class of service and priority assigned it for real-time delivery to ensure a high quality of service. Using tagging, Verizon could assign a higher transit priority – first class status – to data packets originating on its own system, while relating a lower priority – coach status – to the data packets from outside traffic that needs to access to Verizon’s Internet backbone. But discriminating against content from outside the network creates an artificial impediment to the flow of data and other information, thereby impairing the integrity and volume of the Internet for all users.<sup>47</sup>

These Internet control mechanisms are available today, and can be expected to evolve going forward. In a recent incident, the FCC fined an incumbent local telephone provider for

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<sup>46</sup> *Id.*

<sup>47</sup> Even if certain traffic was treated preferentially with priority ratings, there has to be some prioritization and limit on how many packets can drop or go into a buffer zone overflow. Eventually, bandwidth demands may require prioritization for all packets sent over the Internet backbone. The challenge is to create a workable system that routes data in a non-discriminatory fashion over the Internet backbone without creating buffering delays or poor quality.

blocking its customers' access to a VoIP provider.<sup>48</sup>

**iii. The Commission Should Act to Protect Innovation and Competition.**

We do not today have evidence that Verizon tags its own content, or uses other techniques to the detriment of non-Verizon users of the Internet backbone. Our concern is that post-merger, the combined Verizon/MCI entity will have enhanced ability and incentive to adopt these devices, as the bundled services envisioned in the Joint Petition consume more of the available bandwidth than do the currently available unbundled offerings. Now is the time for the Commission to guard against this risk.

To ensure the competitive environment that most benefits consumers and Verizon/MCI competitors, the Commission needs more information. The Commission must determine how to guard against discrimination in the flow of information across the Internet backbone that Verizon owns or controls post-merger.

The Commission has substantial experience in fashioning appropriate performance measures and monitoring processes to prevent anti-competitive discrimination. In an analogous context, the Commission adopted carrier-to-carrier wholesale performance metrics and standards and integrated these standards into a self-executing penalty enforcement mechanism:

The performance measures we use here, and the related voluntary payment provisions, are a carefully tailored enforcement response to the specific difficulties experienced by Bell Atlantic in complying with a statutory checklist element that is a condition of its section 271 authorization to provide long distance service in the State of New York.<sup>49</sup>

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<sup>48</sup> File No. EB-05-IH-0110 - In the Matter of Madison River Communications, LLC and affiliated companies, Consent Decree issued March 3, 2005.

<sup>49</sup> FCC 00-92 - In the Matter of Bell Atlantic-New York Authorization Under Section 271 of the Communications Act to Provide In-Region, InterLATA Service In the State of New York, March 9, 2000 at ¶ 6, 15 FCC Rcd 5413.



The Commission should apply its expertise to this transaction as well.

As a condition to approving the proposed merger, Verizon should file proposed performance standards to ensure that the combined company does not favor its own products and customers, or discriminate against competitors. Verizon's filing should include proposed mechanisms to verify parity between Verizon/MCI and its competitors that use Verizon/MCI's Internet backbone facilities in such categories as number porting, data transfer speeds, and other quality of service criteria. Based on this submission and subsequent comments from interested persons, the Commission will be able to adopt forward-looking performance standards designed to protect the public interest post-merger.

#### **CONCLUSION**

It is imperative that the Commission not give Verizon and MCI "a pass" on the basis of the Joint Petition. This proposed merger is too important for too many people and businesses nationally, as well as in New York and regional sections of the country.

The Commission can not conclude that this transaction to be in the public interest unless , at a minimum, it imposes conditions sufficient to ensure both that Verizon offers stand-alone DSL service to all customers, and that the combined Verizon/MCI does not discriminate in access to the Internet backbone.

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Respectfully Submitted,

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