Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of:	)	
	)	
Application for Consent to Transfer of Control filed by Verizon Communications, Inc. and MCI Inc.	)))	WT Docket No. 05-75

COMMENTS OF THE TEXAS OFFICE OF PUBLIC UTILITY COUNSEL ON VERIZON COMMUNICATIONS, INC. AND MCI INC. APPLICATIONS FOR APPROVAL OF TRANSFER OF CONTROL

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COMMENTS OF THE TEXAS OFFICE OF PUBLIC UTILITY COUNSEL

Pursuant to Public Notice DA-05-762, released March 24, 2005, the Texas Office of Public Utility Counsel (OPC) hereby submits these comments concerning Verizon Communications Inc.'s (Verizon) and MCI Inc.'s (MCI) Application for Consent to Transfer of Control.

I. INTEREST OF OPC

OPC is the Texas State agency designated by its state laws specifically to represent residential and small commercial utility interests of the state. It is responsible for representing these interests before Texas and federal regulatory agencies, as well as the courts. In Texas, MCI provides local and long distance service to both residential and small business customers. Verizon provides wireless services in Texas through its majority ownership in Verizon Wireless and also provides local and long distance service to Texas customers formerly served by GTE.

II. OPC'S COMMENTS

The proposed merger between Verizon and MCI will be detrimental to the public interest unless both Companies are required to adhere to several conditions and performance standards that will protect consumers and enhance competition in the telephone sector. This merger will bring together the largest RBOC with the second largest long distance provider, and has the potential to stifle the already limited amount of competition present in the U.S. telephone service market. MCI is also the second largest CLEC carrier serving enterprise customers in the U.S., and both MCI and Verizon are two of the largest providers of broadband and VOIP services.

Verizon and MCI claim that the merger is necessary in order to create a stronger and more efficient competitor in a multi-nodal communications market. The applicants claim that the merger will enhance investment in the national and international telecommunications infrastructure to the benefit of national security interests, federal and state agencies, large enterprise and mass market customers, as well as generate cost savings and enhanced revenue opportunities. The applicants allege that the benefits of the merger will outweigh any potential lessening of competition in any segment of the broad communications marketplace. The companies do not view each other as competitors, but rather as companies with "complementary assets," with MCI providing a global long-distance voice and data and a top-of-the-line Internet backbone that will mesh with Verizon's dense in-region local wireline network and wireless network. The two companies characterize themselves as merely two "not most significant" competitors among a sea of many other competitors.

OPC has previously provided comments in WT Docket No. 05-65, regarding the merger of AT&T and SBC Communications. The Verizon/MCI merger will have similar anti-competitive economic effects as the SBC merger. The two mergers viewed together, however, will result in the elimination of competition far greater than for each merger viewed individually. Therefore, it is important for the Commission to consider and analyze the combined merger affects for residential and business customers. Both MCI and AT&T directly compete with SBC and Verizon in the provision of local, long distance and broadband services. In the merger application, Verizon characterizes MCI as a declining company that is "a shadow of its former self" in the provision of mass market services and small business services. Verizon cites MCI's "long ago" decision to exit the mass market as evidence that mass market competition will not be harmed by the merger. Verizon also cites the fact that the number of MCI's small business customers purchasing long distance service has declined nearly 25% in the last year alone. The applicants also note that MCI is not a significant competitor with respect to residential broadband Internet services. However small MCI's operations may seem to be compared to Verizon's and the telephone market in general, the fact remains that MCI is the second largest CLEC service provider in the U.S., the second largest provider of Internet backbone service, as well as a significant competitor in the VOIP and broadband market. When viewed in conjunction with the SBC/AT&T merger, a somewhat different picture evolves. The post merger RBOC's will have near monopoly control of the local and long distance markets in their geographic service areas. As noted by Consumers Union and the Consumer Federation of America[1], both SBC and Verizon currently have about an 80% share for residential local telephone service and about a 40% share in the residential long-distance market within their service regions. After the merger, both Verizon and SBC will have about a 90% share for residential local service and a long distance market share of close to 70% in their respective service regions. Additionally, Verizon and SBC will have about a 40-50% market share in the wireless market, and perhaps even a higher market share in their respective geographic regions due to aggressive market efforts in conjunction with their wireless affiliates. As noted by the National Association of State Utility Consumer Advocates (NASUCA), the two mergers would go a long way to reestablishing dominant carriers in the local and long distance markets that will reverse the trend away from the total market dominance held by AT&T prior to the divestiture of the RBOCs.[2]

Through a series of successive RBOC mergers in the last eight years, SBC and Verizon have expanded their service territories and utilized their 271 authority to capture the dominant share of the consumer/small business market. As OPC previously noted, MCI is characterized as a declining competitor in the mass market and small business market. However, both Verizon

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[1] Statement of Gene Kimmelman on Behalf of Consumers Union and the Consumer Federation of America *On SBC, AT&T and Verizon Mergers, Remaking the Telecommunications Industry, Part II,* Senate Judiciary Committee, April 19, 2005, pp. 6-8.

[2] Comments of the National Association of State Utility Consumer Advocates before the FCC, *In the Matter of Application for Consent to Transfer of Control filed by Verizon Communications, Inc. and MCI Inc.*, WT Docket No. 05-75, May 9, 2005, pp. 2-3.

and SBC are largely responsible for the declining revenues and market share of MCI, AT&T and other CLECs. At the repeatedly urging of the RBOCs, the D.C. Court of Appeals vacated the FCC's initial determination that competition is impaired without CLEC access to mass market switches unless state regulatory agencies found otherwise.[3] On remand, the RBOCs' advocacy efforts were rewarded with an FCC determination that CLEC access to ILEC mass market local switches at Total Element Long Run Incremental Cost methodology (TELRIC) pricing was no longer required.[4] Both MCI and AT&T's response to the FCC and Court rulings was to discontinue aggressive marketing of telephone services to residential and small business customers, with the additional intent of migrating their customers to other CLEC or ILEC service providers. In Texas, for instance, the potential for increases in UNE-P prices at market based rates has and will continue to have a chilling effect on competition. Over 75% of Texas CLEC customers are served via UNE-P.[5] Substantial price increases for UNE-P network elements will cause formerly viable local exchange and other telephone service competitors to cease providing service to residential and other customers, close sales offices and liquidate their capital investments. For MCI and AT&T, the solution to their declining customer base was to merge with their two largest competitors.

Consumers Union, the Consumer Federation of America and NASUCA describe the current bleak competitive landscape in the telecommunications industry.[6] The 1996 Telecommunications Act, and the promise of vibrant new competition for telephone services, has

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[3] *United States Telecom Association v. FCC*, 359 F2d 554, 571 (D.C. Cir. 2004). See also *In the Matter of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers, et. al*, FCC 03-36, 66 Docket No. 01-338, ¶ 419-428 (August 21, 2003).

[4] *In the Matter of Unbundled Access to Network Elements, Review of Section 251 Unbundling Obligation of Incumbent Local Exchange Carriers*, FCC 04-290, WC 04-313, ¶ 199 (February 4, 2005).

[5] Report to the 79th Texas Legislature, *Scope of Competition in Telecommunications Market of Texas*, Public Utility Commission of Texas, January 2005, p. 11.

[6] Op. Cit, Comments of the National Association of State Utility Consumer Advocates before the FCC, pp. 7-11 and Statement of Gene Kimmelman, pp. 2-5.

been turned on its head by the removal of affordable unbundled network services for CLECs. Furthermore, the 30 and 21 market entry strategies that were developed as conditions for the SBC/Ameritech and Bell Atlantic/GTE mergers have not brought the expected benefits to consumers. More than five years after the mergers, significant competition by SBC or Verizon outside their geographic footprints has not occurred. Since 2001, SBC has not marketed to new customers in its initial six out-of-region cities, and the Company only maintains the minimal network presence it believes is required in the remaining 24 markets.[7] Verizon's voluntary commitment to target 21 cities outside its territory has had similar results. Neither SBC nor Verizon have been active CLECs outside their geographic territories, nor has there been the retaliatory entry by the RBOCs into other RBOC territories.

Significant bottlenecks and other competitive problems exist in the industry. Verizon and MCI discuss in their application the broad array of intermodal telephone alternatives that exist in the market, surmising that the merger will not affect the rapid growth of these competitive alternatives in the slightest. The applicants, similar to SBC and AT&T, contend that traditional wireline services are in decline, and the rapid changes in the telecom industry have erased the distinction between local and long distance services and between voice and data services. The applicants contend that the merger is necessary to bring a full range of "one stop shopping" telephone services to the public. However, Verizon and MCI are incorrect in their assessment that significant intermodal telephone competition exists as a countervailing measure to the merger. The applicants cite cable and wireless services as the most significant competition going forward. However, neither cable or wireless are currently formidable competitors to landline

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[7] *Petition to Deny of Cbeyond Communications, Conversant Communications, Eschelon Telecom, Nuvox Communications, TDS Metrocom, XO Communications and Xspedius Communications before the FCC, In the Matter of SBC Communications Inc. and AT&T Corp. Applications for Approval of Transfer of Control*, April 25, 2005, pp. 169-170.

telephone services, particularly in view of the fact that both services are highly dependent on the provision of local loop service by the RBOCs. In 2004 cable systems only provided basic local service to 3.34 million customers nationwide, despite the fact that cable is currently available to 107.1 million homes.[8] Furthermore, over 70% of U.S. households don't have the broadband Internet service necessary for cable VOIP service. Cost considerations are an important factor here. Most cable providers require VOIP users to subscribe to a basic cable TV package in order to have access to cable broadband service. The combination of cable TV and cable broadband range from $80 - $100 a month, with the VOIP services costing an additional $10 to $30 a month. If the customer forgoes cable services in favor of alternative broadband providers, the combination of broadband and VOIP can cost anywhere from $40 - $70 a month, which is not competitive with traditional wireline voice service. If the customer chooses broadband service offered by its local ILEC, the costs could be considerably higher since most ILECs refuse DSL service unless the customer also subscribes to basic local telephone service. Most ILECs also refuse to sell wholesale DSL service to competitors. Furthermore, VOIP quality is not reliable over DSL lines, and most VOIP providers do not have reliable access to 911 services. As noted in the *Confronting Telecom Industry Consolidation* report, ILECs and cable companies effectively maintain a duopoly with respect to the "last mile" high speed Internet access services that are essential for VOIP customers. ILECs now provide about 35% of all high speed Internet lines, and 57% are provided by the incumbent cable provider.[9] This strongly duopolistic market will give ILECs and cable companies a powerful incentive to profit maximize through tacit price collusion, resulting in higher prices for high speed Internet services.

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[8] *Confronting Telecom Industry Consolidation*, prepared for NASUCA by Economics and Technology Inc., April 2005, p. 25

[9] Op. cit., p. 29

Wireless telephone services are subscribed to by 70% of U.S. households. However, wireless is not competing with landline phone services to any great extent. Currently, only 3.7% of households are wireless only, and 94% of all wireless households have a landline phone. Similar to VOIP service, wireless is not a perfect substitute for wireline services. Wireless service does not provide reliable 911 service, and wireless customers are plagued with frequent service quality issues. Furthermore, wireless Internet access is prohibitively expensive (about 10 cents a minute), and currently does not have a broad customer base. While affordable broadband and wireless Internet services are currently provided by several municipalities in the U.S., further growth in the public provision of high speed Internet access is being aggressively thwarted by impending state legislation. State legislators are increasing banning the creation of publicly owned networks, largely at the urging of the RBOCs. Since SBC, Verizon and Bell South control 63% of the major national wireless service providers, and other ILECs own an additional 6%, the wireless "competition" cited by the applicants is largely occurring from its own customers, implying the wireless services may be merely replacing, not eliminating, wireline revenues.

NASUCA discusses the numerous findings and conclusions of the FCC in the SBC/Ameritech merger, noting the potential for the increased ability to discriminate against rivals in retail markets where the merged SBC will be the dominant carrier, as well as the decreased competition that would result from the elimination of Ameritech as an SBC rival.[10] The MCI/Verizon merger poses the same risks to competition. The two entities are direct competitors, and the merger will significantly decrease the potential for competition and will provide the incentives and the ability to discriminate against competitors in the provision of advanced services, interchange services, and circuit switch local exchange services.

[10] Op. cit., pp. 11-17.

Additionally, both MCI and AT&T were vigorous proponents of pro-competitive telecommunications policy presenting countervailing positions to the RBOC policy positions. The proposed merger will eliminate MCI as a competitor and public policy advocate for open competition.

The combined market presence of MCI and Verizon is particularly troublesome for the provision of special access services and Internet backbone services. Opportunities for discrimination against other market competitors are numerous. Both AT&T and MCI are the number one and number two largest providers of Internet backbone services. Verizon and SBC are the largest two customers of Internet backbone services. At this point in time, the market for Internet backbone services consists of numerous comparably sized "peers." The mergers would provide both combined companies with a dominant position in the backbone market; the existence of two dominant comparably sized backbone providers would likely result in a duopolistic market that would facilitate discrimination against the smaller backbone providers. The two merged companies, for instance, may be in a position to collusively recognize only each other as peers, and could unilaterally impose transit fees or peering fees on the other competitors, and/or degrade the quality of traffic exchange they offer other competitors. If SBC and Verizon should see a significant portion of their wireline voice services move to VOIP, their share of Internet traffic could increase dramatically, which would also facilitate their ability to price discriminate and service quality discriminate against competitors.

AT&T and MCI are also among the largest purchasers of special access from the RBOCs. AT&T also provides special access in several markets through its acquisition of TCG. The loss of both of these competitors could be devastating for the remaining providers of fiber-based services. AT&T and MCI, by virtue of their size, have been able to exercise some pricing discipline over Verizon's and SBC's special access rates. The merger will foreclose other telephone competitors buying special access circuits from AT&T and MCI from receiving more favorable special access rates. AT&T and MCI are the RBOC's primary, and in many cases, only competitors in the special access market, and the loss of pricing discipline they exert over the RBOCs will result in price increases for the vast majority of special access customers. As a result of the mergers, the number of potential special access providers will drop from three to two within most portions of the SBC and Verizon service regions. If SBC and Verizon fail to compete with each other outside their primary service regions after the merger, this number might decrease to one. Given the previous failure of competitive entry that was mandated or agreed to in prior mergers, competition is not likely. SBC and Verizon will have an economic incentive to tacitly agree to be non-competitors if the pending mergers are approved. Alternatively, SBC and Verizon could discriminate in their special access service offerings to non-affiliates and/or the two companies could offer each other heavily discounted special access in their out-of-region territory, making it difficult for non-affiliated telephone service providers to compete on both a service quality and price basis. The applicants' dominance over the special access market will also require the overwhelming majority of business customers in the two service territories to connect to the public Internet using RBOC facilities. Thus, Verizon and SBC will have almost complete control over both the Internet backbone and bottleneck facilities needed by competitors.

OPC does not believe the merger is in the public interest and will result in a substantial reduction in telephone competition. If the Commission approves the merger, OPC supports the implementation of several conditions in order to ameliorate the merger's anticompetitive results. As discussed by NASUCA, one of the most important conditions would be the requirement that

Verizon make UNE-P and HFPL available to competitors at TELRIC rates. The high frequency portion of the loop should also be made available without requiring customers to subscribe to basic local service. Verizon and MCI should be required to divest themselves of duplicative long-distance and Internet backbone capacity. The wholesale service quality conditions of the Bell Atlantic/GTE merger should be reinstated, and the Applicants should agree to cease any efforts that restrict municipalities and other government entities from investing in broadband networks that will be made available to consumers. Verizon should also be required to provide ubiquitous broadband capabilities throughout the Verizon territory within five years.[11]

Verizon should be required to repeat the Bell Atlantic/GTE out-of- territory competition strategy. As OPC has previously noted, the voluntary market entry strategy that ensued from the Bell Atlantic/GTE merger was not successfully pursued by Verizon. The Commission should not only require an aggressive out-of-market entry strategy for Verizon, it should also vigorously enforce the requirement and monitor the market entry on a continuous basis to ensure active and enduring entry into other markets.

OPC also recommends the adoption of the California Bill of Rights (CBOR) as a merger condition. Verizon/MCI should be subject to the CBOR for all its wireline, wireless and broadband operations, with the Commission retaining enforcement jurisdiction if a state regulatory authority is unable to enforce CBOR standards. Verizon/MCI should be required to flow merger synergies and savings back to consumers. The Commission should reinstate several regulatory controls to the re-emerged RBOC market dominance that will occur with this merger and the proposed SBC/AT&T merger. This would include reviewing and reformulating price cap and other alternative regulation plans to conform to current competitive conditions,

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[11] Op. cit., pp. 22-24.

reinstating earnings sharing, as well as reinstating financial and affiliate transactions reporting requirements.

III. CONCLUSION

OPC urges the Commission to find that the merger petition is not in the pubic interest convenience and necessity, and the Commission should not grant the necessary approvals for the merger. Alternatively, the Commission should impose conduct and performance standards on the merged entities that will limit the harm to competition resulting from the merger, and provide benefits to residential and small commercial customers. OPC further urges the Commission to keep in mind the potential anticompetitive effects of the impending merger of SBC and AT&T. When the two mergers are considered together, telephone competition will be harmed to a much greater extent than described by OPC in these comments.

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