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May 24, 2005

BY HAND AND VIA ECFS

REDACTED – FOR PUBLIC INSPECTION

Marlene H. Dortch
Secretary
Federal Communications Commission
c/o Natek, Inc.
236 Massachusetts Ave., NE
Suite 110
Washington, DC 20002

Mr. Gary Remondino
Wireline Competition Bureau
Federal Communications Commission
c/o Natek, Inc.
236 Massachusetts Ave., NE
Suite 110
Washington, DC 20002

Re: WC Docket No. 05-75, DA 05-762 – In the Matter of Verizon Communications Inc. and MCI, Inc. Applications for Approval of Transfer of Control

Dear Secretary Dortch and Mr. Remondino:

Advance/Newhouse Communications, by its attorneys and pursuant to the Commission's *Public Notice* (DA 05-762) and *Order Adopting Protective Order* (DA 05-647) in the above-referenced proceeding, hereby submits to the Secretary two copies of its redacted, public Reply Comments, and one copy of same to Mr. Remondino. Advance/Newhouse will also submit its redacted, public Reply Comments via ECFS in this proceeding.

Each page of Advance/Newhouse's redacted public version of its Reply Comments is marked as required under the *Order Adopting Protective Order*. Inquiries regarding access to Advance Newhouse's Confidential submission should be addressed to the undersigned.

Please feel free to contact me if you have any questions regarding this filing.

Sincerely,

Robert G. Kidwell

Enclosures

cc: G. Remondino
G. Cohen
B. Dever
M. Schultz
J. Tobias
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J. Bird
J. Levy
N. Victory
G. Strobel

REDACTED – FOR PUBLIC INSPECTION

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

In the Matter of	)	
	)	
Verizon Communications, Inc. and MCI, Inc. Applications for Consent to Transfer of Control	)	WC Docket No. 05-75
	)	DA 05-762
	)	

REPLY COMMENTS OF ADVANCE / NEWHOUSE COMMUNICATIONS

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SUMMARY

In many communities, approval of this transaction could retard the emergence of true facilities-based voice telephony competition of the type being introduced by Bright House Networks. The combination of assets described in the Application would allow Verizon to drive up its competitors' costs for long distance access, interconnection, and other back office services as well as access to the Internet backbone. At the same time, the transaction would enable Verizon to engage in anti-competitive behavior such that true "competition" in either the voice telephony or HSD markets would be delayed or made more costly. Verizon's suggestion that competition from IP-enabled telephone providers such as Bright House Networks negates any competitive concerns arising from this merger must be viewed from a post-merger standpoint, when the only available independent, full-service providers of transport, interconnection and termination (MCI and AT&T) are gone, and three of the six remaining Tier I Internet backbone providers are ILECs. In such a world, providers such as Bright House Networks will have no choice other than to purchase long distance and access to the PSTN from their primary voice telephony and HSD competitor, who in turn would possess the power to extract monopoly rents for those services and for Internet backbone peering.

Verizon's rollout of video programming services provides an additional incentive and greater ability for Verizon to act anticompetitively toward its competitors, to raise their cost of doing business, or to undermine the quality of their offerings. Advance/Newhouse therefore urges the Commission, if it decides that approval of this transaction serves the public interest, to condition its approval upon Verizon's provision of long distance access, PSTN interconnection, and Internet backbone peering – in short,

to deal with its facilities-based competitors – on reasonable, equitable, and non-discriminatory terms and at reasonable and non-discriminatory rates.

Consumer harm arising from Verizon's post-merger ability to "price squeeze" its primary (and in many cases, sole) competitor in many of the markets served by Bright House Networks would be further aggravated if Verizon is allowed to continue tying its DSL service to its voice telephony service. Verizon's anticompetitive tying practice has already had a significant deleterious effect on competition and consumer choice in central and western Florida. Because the practice of tying voice and HSD service will have a much more pernicious effect on consumers when combined with this merger's other anti-competitive effects, the Commission should condition its approval by requiring Verizon to offer unbundled, "naked" DSL to consumers at a reasonable price.

REDACTED – FOR PUBLIC INSPECTION

Before the
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WASHINGTON, D.C. 20554

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

REPLY COMMENTS OF ADVANCE / NEWHOUSE COMMUNICATIONS

Advance/Newhouse Communications ("Advance/Newhouse") respectfully submits these comments in reply to the comments submitted in the Commission's above-captioned inquiry.[1] Advance/Newhouse manages Bright House Networks, which is a full-service broadband provider for more than 2.2 million subscribers in and around Tampa Bay and central Florida, Indianapolis, IN, Birmingham, AL, Bakersfield, CA, and Detroit, MI, along with several smaller systems in Alabama and the Florida panhandle. Bright House Networks provides high-quality digital (including high-definition) television and high-speed data service ("HSD"), and is also (through its wholly-owned subsidiaries in multiple states) a facilities-based local exchange carrier offering voice telephony services to its residential customers. As such, Advance/Newhouse and Bright House Networks have a vested interest in the outcome of this proceeding.

Bright House Networks competes head-to-head with Verizon Communications, Inc. ("Verizon") in the western and central Florida voice telephony market, and Verizon

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[1] *Commission Seeks Comment on Applications For Consent to Transfer of Control Filed By Verizon Communications Inc. and MCI Inc.*, WC Docket No. 05-75, DA 05-762 (2005).

is beginning to compete head-to-head with Bright House Networks in the western Florida video programming market.[2] As a facilities-based telephony provider, Bright House Networks does not rely upon Verizon for any unbundled network elements. Bright House Networks does not resell any Verizon services, and has no collocation arrangements with Verizon. However, Bright House Networks purchases call termination, long distance access, and other "back office" services from MCI, Inc. ("MCI") (collectively with Verizon, "Applicants").[3] Integrated with these services, Bright House Networks also purchases Internet backbone access for its IP-enabled telephone service from MCI's UUNET affiliate. Because of this heavy reliance upon MCI services for which no real substitutes will exist post-merger, the Applicants' request for consent to transfer control of MCI will have a significant effect on Bright House Networks and upon competition in the markets it serves.

In addition to the comments already received in this proceeding, Advance/Newhouse urges the Commission to examine the "situation on the ground" in Florida as a real-world case study of the competitive problems likely to arise from the unrestricted combination of Verizon and MCI. Because the transaction, if approved as proposed, would provide Verizon with an opportunity to hamstring its major facilities-based competitor in western and central Florida (and, undoubtedly, in other markets as well), and thereby drive up prices and limit consumer choice, the Commission should condition its approval of this transaction – if it finds approval to be in the public interest –

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[2] *See* Linda Haugsted, "Fla. City OKs Verizon Franchise," *Multichannel News*, May 18, 2005.

[3] See Affidavit of Arthur C. Orduna ("Orduna Affidavit"), attached hereto, at ¶¶ 6-7.

in order to mitigate certain substantial, identifiable, and merger-specific competitive harms.

INTRODUCTION

The Applicants claim that the traditional regulatory distinction between local telephone service and long distance service has become antiquated due to the evolution of voice over Internet protocol ("VoIP") and wireless services, and that therefore "[t]he decision by Verizon and MCI to combine represents the next logical step in this industry transformation."[4] But Verizon's further accretion of market power in local markets up and down the eastern seaboard represents neither a foregone conclusion nor a healthy evolution of the communications industry.[5] In many of the communities served by Bright House Networks, this transaction could well retard the emergence of true facilities-based voice telephony competition of the type being introduced by Bright House Networks.[6]

The combination of assets described in the Application would allow Verizon to drive up its competitors' costs for long distance access, interconnection, and other back office services as well as access to the Internet backbone. At the same time, the transaction would enable Verizon to engage in further anti-competitive behavior such that

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[4] Applicants' Public Interest Statement at 1-3.

[5] *See* Petition to Deny of Qwest Communications International, Inc. at 4 (rebutting Applicants' statement that this transaction is natural and "inevitable" consolidation).

[6] *See, e.g.*, Comments of Cox Communications, Inc., at 10-12 ("Post-merger, Verizon would have greater capabilities and incentives to increase the interconnection costs of its remaining competitors."); CompTel/ALTS Petition to Deny at 22 ("The merged company will have the ability to severely harm consumers by raising wholesale prices for essential local facilities to service providers attempting to compete with Verizon/MCI"); Comments of The Independent Alliance at 3-4 ("The proposed merger of Verizon and MCI, two very large companies that control tandem and transport facilities, raises questions as to how smaller carriers might obtain fair access to facilities that are controlled by a single vertically integrated entity.").

true "competition" in either the voice telephony or HSD markets would be delayed or made more costly.[7] Verizon's suggestion that competition from IP-enabled telephone providers such as Bright House Networks negates any competitive concerns arising from this merger must be viewed from a post-merger standpoint, when the only available independent, full-service providers of transport, interconnection and termination (MCI and AT&T) are gone, and three of the six remaining Tier I Internet backbone providers are incumbent local exchange carriers ("ILECs").[8] In such a world, providers such as Bright House Networks will have no choice other than to purchase access to the public switched telephone network ("PSTN") from their primary voice telephony and HSD competitor, who in turn would possess the power to extract monopoly rents for those services and for Internet backbone peering.

In addition, Verizon has chosen to launch its "FiOS" video programming service in certain of the communities served by Bright House Networks, thereby providing an

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[7] *See, e.g.*, Opposition of Broadwing Communications, LLC, and SAVVIS Communications Corporation to the Merger Application Filed by Verizon Communications, Inc. and MCI, Inc. ("Broadwing Comments") at 28 ("With its ILEC footprint, Verizon will have every incentive and the ability to engineer a price squeeze that benefits the newly integrated MCI operations."); Comments of PAETEC Communications, Inc., at 5 ("Applicants can eliminate competitors by utilizing price squeeze techniques through the vertical integration of their operations."); CompTel/ALTS Petition to Deny at 22; Comments of Cox Communications, Inc., at 10-12.

[8] *See, e.g.,* Broadwing Comments at 2-3 ("the proposed merger would (1) further reduce the already limited competition in the special access market and increase prices for consumers; and (2) likely result in the collapse of the current competitive market for Internet backbone services and replace it with a market dominated by two companies.") (citations and parentheticals omitted). This statement assumes approval of SBC's acquisition of AT&T, another existing Tier I access provider. If Verizon's acquisition of MCI is indeed the industry's "next logical step," then it is only logical that one of the two remaining ILECs will propose to acquire Sprint, thereby making the count four out of six.

additional incentive and greater ability for Verizon to act anticompetitively toward Bright House Networks, to raise its costs of doing business, or to undermine the quality of Bright House Networks' offerings. This dynamic can only be bad for consumers. Advance/Newhouse therefore urges the Commission, if it decides that approval of this transaction serves the public interest, to condition its approval upon Verizon's provision of long distance access, PSTN interconnection, and Internet backbone peering – in short, to deal with its facilities-based competitors – on reasonable, equitable, and non-discriminatory terms and at reasonable and non-discriminatory rates.

Consumer harm arising from Verizon's post-merger ability to "price squeeze" its primary (and in many cases, sole) competitor in many of the markets served by Bright House Networks would be further aggravated if Verizon is allowed to continue tying its digital subscriber line ("DSL") service to its voice telephony service. Competition is thwarted when consumer choices are artificially limited, and Verizon's practice of tying DSL with its voice telephony service is a stark example of an anti-competitive, artificial constraint on consumer choice imposed solely for the purpose of leveraging its market power in the voice market into the HSD market and imposing costs on consumers' ability to choose a competitive telephone service provider. As discussed in detail below, Verizon's anticompetitive tying practice has already had a significant deleterious effect on competition and consumer choice in central and western Florida. Because the practice of tying voice and HSD service will have a much more pernicious effect on consumers when combined with this merger's other anti-competitive effects, the Commission should condition its approval by requiring Verizon to offer "naked" DSL to consumers at a reasonable price.[9]

LEGAL STANDARD GOVERNING THIS PROCEEDING

Under 47 U.S.C. §§ 214(a) and 310(d), the burden is on the Applicants to demonstrate that the proposed transaction serves the public interest, as measured by four factors: (1) whether the transaction would result in a statutory violation, (2) whether the transaction would result in a violation of Commission rules, (3) whether the transaction would "substantially frustrate or impair" the Commission's implementation or enforcement of the Act, or would interfere with statutory objectives, and (4) whether the transaction promises to yield affirmative public interest benefits net of any public interest harms, including harms identified through antitrust analysis.[10]

To apply the fourth prong of its merger review standard here, the Commission can approve this transaction only upon reasonable conditions imposed to mitigate the merger-specific public interest harms described below.

[9] *See, e.g.*, Comments of Vonage Holdings Corp. at 10-11 (discussing Verizon's history of interfering with consumers' number porting rights and the related problem of DSL tying); Petition to Deny of Qwest Communications International, Inc. at 42 (urging the Commission to impose a "naked DSL" condition, as "announcements of willingness to begin to provide stand-alone DSL are meaningless if the terms are not sufficient to allow competitive service offerings by non-Verizon VoIP providers and others."); Comments of Eliot Spitzer, Attorney General of the State of New York, at 7-12 (discussing need for unbundled DSL access if intermodal competition is to provide a competitive check on Verizon).

[10] *See, e.g., Ameritech Corp., Transferor, and SBC Communications, Inc., Transferee, Application For Consent to Transfer of Control*, 14 FCC Rcd 14712, 14736-37 ¶¶ 46-49 (1999) ("*SBC/Ameritech*").

I. ABSENT REASONABLE CONDITIONS, THE MERGER HAS THE POTENTIAL TO ALLOW VERIZON TO INCREASE ITS COMPETITORS' COSTS, THEREBY DRIVING UP PRICES AND DECREASING COMPETITION IN BOTH VOICE TELEPHONY AND HSD MARKETS

If approved without condition, Verizon's acquisition of MCI has the potential to drive up the prices paid by consumers for telephone service and HSD (and potentially, for video programming service) and at the same time decrease the likelihood that other facilities-based competitors will be able to provide a competitive check on such conduct. The deal will eliminate as an independent entity and as a check upon Verizon's market power[11] Bright House Networks' primary supplier of back office service, long distance access, and interconnection – and replace that supplier with Bright House Networks' primary telephone and HSD competitor – just as Bright House Networks is establishing its telephone service as a true competitor to Verizon. In markets such as those in Florida where Bright House Networks competes head-to-head with Verizon for voice, HSD, and video programming customers, the transaction presents an even broader set of public interest harms. The Commission should take steps to mitigate these harms, and should impose reasonable and merger-specific conditions toward that end.

A. The Transaction Will Drive Up Prices

Bright House Networks offers facilities-based, digital IP-enabled telephony to all of the over 3 million homes passed by its facilities in western and central Florida. By the end of 2005, Bright House Networks is on schedule to roll out its Digital Phone service to the Birmingham, AL, Detroit, MI, Bakersfield, CA, and Indianapolis, IN markets, for a

[11] *See* Petition to Deny of Qwest Communications International, Inc. at 1 ("After the merger, MCI no longer will act as an independent source of wholesale supply, or as a restraint on Verizon's access pricing.").

total of REDACTED homes passed by Digital Phone by the end of 2005. For $49.95 a month,[12] Bright House Networks Digital Phone customers may make unlimited local and long distance calls to the continental U.S., Alaska, Hawaii, Puerto Rico, Guam and the North Marianas, and Canada. Vertical services for which Verizon imposes additional fees, such as voicemail, call waiting, and caller ID, are included with Digital Phone at no charge, as is Bright House Networks' exclusive 24-hour "611" customer care line. Bright House Networks Digital Phone is fully E-911 and CALEA compliant and offers a selection of blocking services at its customers' request.

In order to "hand off" its voice traffic to the PSTN, Bright House Networks purchases interconnection and call termination services from MCI. Under contract, MCI also provides back office and other services such as domestic long distance, international long distance, directory assistance, and operator assistance.[13] UUNET, an affiliate of MCI, connects Bright House Networks IP-enabled voice service to the Internet backbone and to the PSTN.[14] Bright House Networks' ability to partner with MCI has been essential to its timely rollout of cost-competitive telephone service due to the expense and delay associated with constructing duplicative back office facilities, and because of MCI's proven expertise in handling number porting requests quickly and efficiently.[15] MCI has been the only available "one stop" vendor for Bright House Networks, as its

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[12] This price is for free-standing telephone service. Bright House offers its customers a discount for purchase of additional services such as cable television and/or HSD.

[13] *See* Orduna Affidavit at ¶¶ 6-7.

[14] *See* Declaration of Vinton G. Cerf at ¶ 11; *see also* Orduna Affidavit at ¶¶ 6-7.

[15] *See* Orduna Affidavit at ¶¶ 6-11.

experience with Verizon in the central and western Florida markets has not been a positive one.

Bright House Networks also offers cable modem-based HSD in all of the markets it serves. In order to connect its HSD customers with the Internet, Bright House Networks also purchases Internet backbone access from non-ILEC carriers. Bright House Networks' ability to purchase Internet backbone access in an unconcentrated market has been essential to its ability to compete with Verizon DSL (particularly given Verizon's bundling and tying practices).

Post-merger, Bright House Networks will be forced to rely upon its principal retail competitor for provisioning of long distance service, interconnection/call termination and back office services. Additionally, with its acquisition of MCI's Internet backbone assets, Verizon will be positioned to drive up Bright House Networks' costs directly (through its UUNET subsidiary) and through manipulation of its peering relationships with other backbone providers.[16] The Applicants gloss over these facts in their Public Interest Statement:

> MCI supports the Internet offerings of certain cable operators, including Time Warner Cable, Bright House Networks, Susquehanna

[16] *See, e.g.*, Comments of Cox Communications, Inc. at 13-14 ("the merged company would have an increased capability and incentive to raise or maintain its [Internet backbone] transit rates at supra-competitive levels or engage in other anticompetitive conduct, because such actions would have the external effect of raising the costs for Cox and other IP service providers to compete against Verizon's core retail services."); Comments of Eliot Spitzer, Attorney General of the State of New York, at 13-19 (discussing potential harm resulting from Verizon's acquisition of MCI Internet backbone assets, and recounting past divestitures ordered by FCC to avoid excessive Internet backbone concentration); Broadwing Comments at 44-55 (discussing harms presented by concentration in the Internet backbone market and its pernicious effect when combined with market power in wholesale access markets).

> Communications, and Armstrong Group of Companies. *See* Cerf Decl. ¶ 11. MCI picks up the cable operator's traffic at the softswitch or media gateway (which MCI may operate or own), and terminates the traffic over its network, as well as handling other administrative and provisioning tasks. *See id.*
>
> The transaction would not have a material effect on competition to provide these services. First, MCI provides these services pursuant to long-term contracts, which Verizon plans to honor. *See* Lew/Lataille Decl. ¶ 12. Second, MCI's contracts are nonexclusive, and a number of other providers provide comparable services, including Sprint and Level 3, many of which began offering these services around the same time as MCI. Indeed, AOL recently chose Level 3 as its wholesale provider for its new VoIP service. As the success of these other recent entrants demonstrates, MCI does not possess any unique capabilities in providing these services.[17]

In support of their claim that this transaction will have "no effect" on the competitors for whom MCI's wholesale services are essential, the Applicants cite the declaration of two Verizon officers, but that declaration states only that "we will continue to offer these services to our carrier customers."[18] The concern raised by this merger is not that Verizon will stop providing wholesale access and related services to other carriers; rather, the concern is that Verizon will drive up its competitors' costs of purchasing long distance service, interconnection, Internet backbone access, and other services needed to compete. Neither the Applicants nor their numerous declarants address this harm.

The Applicants point out that Sprint and Level 3 both provide similar services in many areas; however, neither of these firms represents a realistic long-term alternative to MCI for Bright House Networks. Sprint is the incumbent LEC in several of the markets served by Bright House Networks, and therefore cannot provide a competitive check on

[17] Applicants' Public Interest Statement at 66.

[18] *Id.*; Lew/Lataille Declaration ¶ 12.

Verizon's pricing of these services since both Verizon and Sprint will have an incentive to set the prices they charge Bright House Networks at supracompetitive levels.[19]

Level 3 Communications is as well an unattractive alternative to MCI for provision of wholesale services. Bright House Networks considered partnering with Level 3 when initially developing its telephone product, but Level 3 could not provide access to the rate centers required to serve Bright House Networks' customers. Furthermore, Level 3 has ceased providing business-class wholesale services, and is generally retreating from the provision of residential wholesale services as well. Much like Sprint, Level 3 is not an effective long-term alternative to MCI.[20]

The Applicants also claim that "[a]s the success of these other recent entrants [referring to Sprint and Level 3] demonstrates, MCI does not possess any unique capabilities in providing these services."[21] But even if true, this assertion does not change the fact that this transaction will eliminate the primary independent provider of these services from the market, leaving behind only incumbent LECs whose desire to compete with Verizon in wholesale markets is uncertain, and a single independent provider – Level 3 – whose limited ability and declining willingness to offer such services on the necessary scale renders it practically unavailable as a substitute to MCI.

The Applicants further state that "[c]ustomers now view cable and wireless as viable alternatives to wireline telephone service, and that acceptance will only grow going forward. Other services such as VoIP, e-mail, and instant messaging impose still

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[19] *See* Orduna Affidavit at ¶ 12.

[20] *See* Orduna Affidavit at ¶ 13.

[21] Applicants' Public Interest Statement at 66.

further discipline on the market. . . . This transaction does not affect this intermodal competition in the slightest."[22] The Applicants' suggestion that VoIP/IP-enabled telephony, E-mail, and instant messaging are and would remain serious competitors to a post-merger Verizon, absent conditions, is without merit.

E-mail and Instant Messaging Competition. The Applicants suggest that E-mail and Instant Messaging ("IM") have taken ten percent of voice traffic that would have otherwise been carried over their systems, and suggest that these services therefore provide a competitive check on the merged firm's ability to raise prices.[23] The two sources cited by the Applicants and their economists may or may not support the ten percent diversion rate that they assert (it is unclear whether they do or not), but in any case this statistic alone provides no support whatsoever for the Applicants' implication that E-mail and IM provide any sort of price constraint on Verizon. Despite the Applicants' submission of multiple expert declarations with their Application, nowhere do they offer even the most rudimentary analysis of consumer product substitution or cross-elasticity of demand between voice telephony and either E-mail or IM. Such an analysis is essential if the Commission is to consider this argument in its public interest analysis,[24] and therefore the Applicants' failure to even allege such cross-elasticity renders their discussion of E-mail and IM irrelevant.

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[22] Applicants' Public Interest Statement at 38-39.

[23] Applicants' Public Interest Statement at 45; Hassett *et. al.* Declaration at ¶¶ 88-89.

[24] The Commission's inquiry should include traditional antitrust analysis when appropriate. *SBC/Ameritech*, 14 FCC Rcd at 14737 ¶ 49. Here, the Applicants attempt to make a standard antitrust product substitutability argument; therefore, the Commission should be guided by traditional antitrust principles. In this case, even a cursory antitrust analysis requires evidence of cross-elasticity of demand based on real-world facts. *See,*

Even were the Applicants to demonstrate real cross-elasticity of demand between voice telephony and E-mail and IM, the ten percent diversion rate cited by the parties would have to be discounted substantially to account for a substantial portion of E-mail and IM traffic that will be routed, at least in part and frequently end-to-end, over Verizon's facilities post-merger. Such an analysis is pointless, however, as the suggestion of significant cross-elasticity itself is simply ridiculous.

Cable/VoIP Competition. The Applicants rely upon certain of their supporting economist declarations to describe the growth of cable firms' voice telephony service offerings, and argue that these intermodal offerings will provide a significant competitive check on the post-merger firm.[25] Bright House Networks is proud to count itself among the growing list of cable operators providing IP-enabled digital voice telephony to its subscribers as cited by the Applicants. However, neither the Applicants nor their economists address the heavy reliance placed by Bright House Networks and other cable operators on the competitive, nondiscriminatory long distance access, PSTN interconnection, and Internet backbone access made available to them by non-incumbent providers such as MCI. Without the benefit of competitively priced services delivered in a timely manner that meet the quality objectives of a reputable company like MCI, cable

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e.g., Merit Motors, Inc. v. Chrysler Corp., 417 F. Supp. 263, 269 (D.D.C. 1976) (discussing necessity of evidence of demand cross-elasticity for product market definition). The Applicants provide no more than unfounded conjecture that consumer demand for E-mail and IM are cross-elastic with their demand for voice telephony.

[25] Applicants' Public Interest Statement at 39; Hassett *et. al.* Declaration at ¶¶ 30-56.

and VoIP competitors' ability to provide choice and a competitive check to Verizon will be severely hampered.[26]

The Applicants argue that cable and VoIP provide a competitive check on its market power because they provide a separate "pipe" into the home; it is true that cable operators are facilities-based providers, but the transaction at issue here goes well beyond last-mile pipes, as Verizon is in effect purchasing the river itself – upon completion of this transaction, if left unchecked, Verizon will be able to set the price of water regardless of whose pipes deliver it.[27]

It is tautological that two firms cannot engage in aggressive price competition in a downstream market when one of those firms holds a monopoly on upstream inputs essential for both firms; indeed, this is one of the most pernicious competitive problems in evolving telecommunications markets in the U.S. and abroad.[28] Unless its power over

[26] *See* Comments of ACN Communications Services *et al.* at 14-12 (describing IP-enabled providers' need for competitively priced wholesale inputs for true intermodal competition); Comments of Cox Communications, Inc. at 4 ("facilities-based competitive LECs and VoIP service providers cannot provide service without efficient collocation and interconnection with the incumbents' networks to exchange calls between their customers and those of the incumbents."); Comments of Vonage Holdings Corp. at 4 ("In order for VoIP providers like Vonage to offer competition in the retail marketplace for communication services, they must have access to the access tandem switches – the access ramps to and from the PSTN – controlled by local exchange carriers, and, to an increasing extent, the backbone facilities that represent the Internet itself."); *id.* at 9 ("The market dominance of the combined Verizon MCI also presents concerns about their ability to discriminate in the quality of the broadband connection they offer end-users" and will enable packet discrimination).

[27] *See, e.g.*, Petition to Deny of Qwest Communications International, Inc. at 27 ("Verizon also ignores the fact that intermodal competitors depend on wholesale inputs from Verizon itself in order to provide their services.").

[28] *See generally* Damien Geradin and Robert O'Donoghue, *The Concurrent Application of Competition Law and Regulation: The Case of Margin Squeeze Abuses in the Telecommunications Sector*, Global Competition Law Centre Working Paper No. 04/05;

price and terms is checked, the upstream monopolist may in effect set the downstream competitor's price. It was this dynamic that led to the breakup of AT&T over twenty years ago, when AT&T's monopoly over local exchange service allowed it to exclude competitors from complimentary markets such as long distance service by raising rivals' costs of interconnection and, therefore, gaining power over the price ultimately paid by consumers.[29] Now no less than then, Verizon's post-merger market power in the markets for long distance access, interconnection, back office services, and Internet backbone access will likely retard, if not destroy, competition, and will almost certainly result in higher costs for consumers unless conditions are placed upon its exercise of that market power. Quite simply, this merger will roll back the clock to "the bad old days" for consumers of voice telephony, and will make today the "bad old days" for consumers of HSD.

There can be no question that this transaction will consolidate the voice telephony market to pre-divestiture levels. However, the Commission has determined that the market for Internet backbone services as well is a distinct product market for purposes of

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see also Covad Communications Co. v. BellSouth Corp, 299 F.3d1272, 1290-92 (11th Cir. 2002) (reversing dismissal of CLEC price squeeze allegation against ILEC), *cert. granted, remanded,* 540 U.S. 1147 (2004), *aff'd on reh'g*, 374 F.3d 1044 (11th Cir. 2004); *City of Kirkwood v. Union Electric Co.*, 671 F.2d 1173, 1176 n.4 (8th Cir. 1982) ("A price squeeze occurs when a vertically integrated company which has monopoly power at the wholesale level but faces competition at the retail level sets its wholesale rates so high that its wholesale customers will be unable to compete with it in the retail market.").

[29] *United States v. AT&T*, 552 F. Supp. 131, 162 (D.D.C. 1982) *aff'd sub nom. Maryland v. United States*, 460 U.S. 1001 (1983) ("it was because of its ownership and control of the local Operating Companies – whose facilities were and are needed for interconnection purposes by AT&T's competitors – that AT&T was able to prevent these competitors from offering [their] services. Similarly, AT&T was able to deter competition by manipulating prices for access to the Operating Company networks.").

competitive merger analysis.[30] With its acquisition of MCI, Verizon will instantly become one of the largest Internet backbone service providers in the world. The effect of this development cannot be overstated – with a single purchase, Verizon will essentially guarantee that its decades-old monopoly over traditional, circuit-switched local telephone service will be transplanted wholesale into the once-virgin soil of IP-enabled communication services. With this acquisition, years of speculation and hopeful anticipation about new hi-tech services dethroning incumbent telephone monopolies will be proven wrong once and for all, and consumers will see the effect in terms of higher prices and fewer choices. Because its telephony and HSD services rely on access to services that will be controlled by Verizon post-merger, Bright House Networks will be competitively disadvantaged and its subscribers will face increased costs as a result.

B. Bright House Networks' Experience in Florida is Illustrative of the Harms Presented by this Transaction

The perspective that Bright House Networks brings to this proceeding is its own, but the competitive problems that are presented by this transaction in the markets served by Bright House Networks will become more common as Verizon introduces its video programming service to other areas. Verizon's rollout of video programming in Bright House Networks service areas[31] will provide the merged entity with the increased

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[30] *See Application of WorldCom, Inc. and MCI Communications Corporation for Transfer of Control of MCI Communications Corporation to WorldCom, Inc.*, 13 FCC Rcd 18025, 18107 at ¶ 148 (1998) ("*MCI/WorldCom*").

[31] *See, e.g.*, Linda Haugsted, "Fla. City OKs Verizon Franchise," *Multichannel News*, May 18, 2005; Verizon Press Release, "Verizon Poised to Deliver First Set of Services to Customers Over its Fiber-to-the-Premises Network," July 19, 2004, available at <http://newscenter.verizon.com/proactive/newsroom/ release.vtml?id=86053>.

incentive and ability to impose anti-competitive costs on Bright House Networks and other facilities-based competitors beyond that which exists today.

First, Bright House Networks relies heavily upon its relationship with MCI for provision of its voice telephony services, and there are no good substitute providers of these services in the areas Bright House Networks serves. As a consequence of this transaction, in the Florida market Verizon will be able to increase Bright House Networks' cost of acquiring necessary inputs for both its HSD and voice telephony services, thereby increasing the price of those services and making Bright House Networks a less attractive option for consumers seeking a bundle of services from a single provider. The benefits of such a strategy to Verizon are obvious. As discussed below, Verizon is already using anti-competitive tying methods (rather than competitive actions such as price cuts or service enhancements) to impose direct costs on consumers wishing to cancel their Verizon telephone service and switch to Bright House Networks Digital Phone service. Furthermore, Verizon's rollout of its video programming service in the same area has resulted in destructive behavior on the part of Verizon resulting in service outages to hundreds of Bright House Networks telephone, HSD, and video programming customers.[32] In such an environment, Verizon has everything to gain and consumers have everything to lose from the anticompetitive pricing behavior that will be enabled by this transaction.

Second, the monopoly rents extracted by the merged firm will provide Verizon with the ability and incentive to cross-subsidize its nascent video programming offering

[32] *See* Linda Haugsted, "Bright House Complains About Verizon Cut," *Multichannel News*, April 18, 2005.

with monopoly rents extracted from Bright House Networks and others, with the effect being Bright House Networks' subsidization of Verizon's video programming startup costs at the same time as Verizon imposes additional startup costs on Bright House Networks' Digital Phone service. Once again, this state of affairs can only be harmful to consumers.

Third, Bright House Networks' experience in Florida telephony markets demonstrates the degree of competitive harm that can be caused by seemingly minor (and easily hidden or denied) decreases in service levels. Between August 2004 and February 2005, MCI fell behind on its ability to process Bright House Networks service orders and meet its performance commitments, sometimes delaying number porting and similar requests by thirty days or more. During this period, Bright House Networks experienced a projected growth shortfall of REDACTED, amounting to a loss of REDACTED subscribers in addition to a spate of bad press and a ten-fold increase in the number of customer complaints.[33] This situation was remedied only because MCI became highly motivated to resolve its service issues and maintain its business relationship with Bright House Networks. Once Verizon takes control of MCI's assets, it will have no motivation to resolve such issues, and is likely to leave services and facilities sold to competitors at the bottom of the repair list when such issues arise in the future.[34] In addition, any decision by Verizon to purposefully degrade the level of service provided to wholesale

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[33] See Orduna Affidavit at ¶ 8.

[34] *See, e.g.*, Comments of ACN Communications Services, Inc. *et al.* at 53-54 (describing potential harm from service quality discrimination and seeking conditional performance measures).

customers such as Bright House Networks would be more difficult to detect and more difficult to remedy than would other types of anticompetitive conduct.

In order to combat these foreseeable anti-competitive effects of the proposed merger, the Commission, if it finds approval of the transaction to be in the public interest, should impose reasonable conditions that address these merger-specific harms. The Commission should require that Verizon provide long distance, interconnection, and Internet Backbone access with reasonable, equitable, and non-discriminatory terms and rates. For any such condition to be meaningful, it is essential that Verizon's *internal cost allocation* be used as a benchmark for "reasonableness" when determining acceptable rates. Otherwise, the merged firm will simply be able to extract similarly anti-competitive rents from all buyers, all the while asserting its equitability and non-discrimination.

II. ABSENT REASONABLE CONDITIONS, THE MERGER WILL SIGNIFICANTLY AGGRAVATE THE ANTICOMPETITIVE EFFECTS OF VERIZON'S PRACTICE OF TYING DSL WITH LOCAL TELEPHONE SERVICE

It is no secret that Verizon, like other ILECs, has established a practice of tying its DSL offering to consumers' purchase of local exchange service and thereby of erecting roadblocks to consumer number portability.[35] As a result, Verizon enjoys a significant "lock-in" effect due to consumers' desire to keep their telephone number and E-mail address when changing carriers. Numerous commenters in this proceeding, including

[35] *See* Comments of Eliot Spitzer, Attorney General of the State of New York, at 10-12 (discussing Verizon's tying of its DSL service to its voice service and the impact of tying on number porting requests, and seeking a "naked DSL" condition). *See also, e.g.,* Ted Hearn, "FCC TO Bells: No Stalling," *Multichannel News*, April 4, 2004.

service providers (both incumbent and competitive) and regulators alike, have documented this effect in this proceeding.[36]

DSL tying is a weapon that Verizon has wielded against Bright House Networks as well. In the communities that Bright House Networks serves, Verizon has aggressively discouraged competition by refusing to allow its voice customers to port their number to Bright House Networks if those voice customers also subscribe to Verizon DSL. To date, Verizon's anti-competitive tactics have proven extremely effective, and have convinced a quarter or more of Bright House Networks' first-time telephone subscribers to cancel their Bright House Networks service order and stay with Verizon.[37] Competition is thwarted when consumer choices are artificially limited, and Verizon's practice of tying DSL with its voice telephony service is a stark example of an anti-competitive, artificial constraint on consumer choice imposed solely for the purpose of leveraging its market power in the voice market into the HSD market.

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[36] *See, e.g.*, Petition to Deny of Qwest Communications International, Inc. at 42 (urging the Commission to impose a "naked DSL" condition, as "announcements of willingness to begin to provide stand-alone DSL are meaningless if the terms are not sufficient to allow competitive service offerings by non-Verizon VoIP providers and others."); Comments of Vonage Holdings Corp. at 10-11 (discussing Verizon's history of interfering with consumers' number porting rights and the related problem of DSL tying); Comments of Eliot Spitzer, Attorney General of the State of New York, at 7-12 (discussing need for unbundled DSL access if intermodal competition is to provide a competitive check on Verizon).

[37] *See Bright House Networks Information Services, LLC v. Verizon Florida, Inc.*, Complaint and Request for Declaratory Ruling of Bright House Networks Information Services, LLC, at 1 n.1, 3, and 6 (filed September 30, 2004). *See also* Linda Haugsted, "MSO: Verizon Numbers Aren't Porting Over," *Multichannel News*, October 25, 2004. *See also Cable, Phone Carriers Wage High-Speed Battle*, ST. PETERSBURG TIMES, October 4, 2004, at 3.

Under traditional antitrust analysis, Verizon's tying of DSL and voice services raises serious antitrust concerns. There are four elements to a *per se* tying violation: (1) the tying and tied goods are two separate products; (2) the defendant has market power in the tying product market; (3) the defendant affords consumers no choice but to purchase the tied product from it; and (4) the tying arrangement forecloses a substantial volume of commerce.[38] In this case, DSL and voice telephony are clearly separate products, and Verizon clearly possesses market power in the areas it serves.[39] Verizon is the sole provider of DSL services in many of the markets it serves, and its tying practice forecloses a substantial volume of commerce – in western and central Florida alone, as mentioned above, Verizon's tying practice has stifled a whopping 25 percent of consumers' attempts to switch their service to Bright House Networks. The Commission cannot ignore this behavior, particularly since it is the primary enforcer of the antitrust laws in the telecommunications industry.[40]

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[38] *See United States v. Microsoft Corp.*, 253 F.3d 34, 85 (citing *Eastman Kodak Co. v. Image Tech. Servs., Inc.*, 504 U.S. 451, 461-62 (1992)).

[39] In case there was any doubt that Verizon possesses market power in the voice telephony market, it is telling that, in the short time since the FCC effectively lifted its network element unbundling requirements, Verizon has raised its wholesale rates charged to competitors substantially. *See* Thomson StreetEvents VZ – Q1 2005 Verizon Earnings Conference Call, April 27, 2005, at 6 and 11 (disclosing substantial profit gains from wholesale price increases following UNE deregulation).

[40] *See Verizon Communications Inc. v. Law Offices of Curtis V. Trinko*, 540 U.S. 398, 412 (2004) ("One factor of particular importance is the existence of a regulatory structure designed to deter and remedy anticompetitive harm. Where such a structure exists, the additional benefit to competition provided by antitrust enforcement will tend to be small, and it will be less plausible that the antitrust laws contemplate such additional scrutiny.").

The Commission has recently re-affirmed that "carriers may not impose non-porting related restriction on the porting-out process."[41] Verizon's pattern and practice of refusing to port consumers' numbers, upon request, to Bright House Networks when those consumers also subscribe to Verizon DSL service violates both the Communications Act and the antitrust laws. Consumer harm arising from Verizon's post-merger ability to "price squeeze" its primary (and in many cases, sole) competitor would be further aggravated if it is allowed to continue tying its DSL service to its voice telephony service. Because the practice of tying voice and HSD service will have a much more pernicious effect on consumers when combined with this merger's other anti-competitive effects, the Commission should condition its approval by requiring Verizon to offer "naked" DSL to consumers at a reasonable price.

[41] *BellSouth Telecommunications, Inc. Request For Declaratory Ruling that State Commissions May Not Regulate Broadband Internet Access Services By Requiring BellSouth to Provide Wholesale or Retail Broadband Services to Competitive LEC UNE Voice Customers, Memorandum Opinion and Order and Notice of Inquiry*, WC Docket No. 03-251 at ¶ 36 (2005).

CONCLUSION

For the reasons stated above, should the Commission find approval of this transaction to be in the public interest, it should condition its approval of the parties' Application on Verizon's provision of long distance service, PSTN interconnection, and Internet backbone access on reasonable, equitable, and non-discriminatory terms benchmarked to Verizon's internal cost allocations, on Verizon's unbundling of its DSL product from its voice telephony product at reasonable and affordable rates for consumers, and upon such other conditions as may be necessary to ensure fair and effective competition.

Respectfully submitted,

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May 24, 2005

CERTIFICATE OF SERVICE

I, Robert G. Kidwell, do hereby certify that, on May 24, 2005, a copy of the foregoing Reply Comments of Advance/Newhouse Communications was served upon the Secretary, counsel for Applicants, and FCC staff in the following manner:

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

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

AFFIDAVIT OF ARTHUR C. ORDUNA

I, Arthur C. Orduna, hereby state:

1. I am Vice President, Strategic Initiatives, for Bright House Networks, LLC (hereinafter "BHN"). My responsibilities include, among other things, overseeing the strategic direction of BHN's Digital Phone product, which is a residential voice telephony service offering. BHN utilizes IP-enabled technology to deliver its voice traffic to the public switched telephone network.

2. BHN is a facilities-based local exchange carrier currently offering local, long-distance, and international long distance services to customers in the Tampa Bay and Central Florida markets. BHN launched Digital Phone in the Tampa Bay area on or around July 2004. We launched the service in Central Florida in October 2004. BHN will complete the roll out Digital Phone service to the Birmingham, Detroit, Bakersfield, and Indianapolis markets by the end of 2005.

3. In addition to basic local and long distance service, our Digital Phone product also includes features such as call waiting, call forwarding, and free voicemail. We also offer directory assistance (411), operator assistance, 611 services, and the necessary subscriber information for a printed telephone directory. Our public safety features include E911 and 711 support, and our network is "CALEA" compliant. BHN also contributes to the Universal Service Fund and other FCC-controlled funds supported by traditional telecom providers. In sum, BHN's Digital Phone acts as a replacement to the traditional voice service offered by the incumbent LECs.

4. Currently, BHN Digital Phone service passes REDACTED homes in central Florida and the Tampa area, with REDACTED active Digital Phone subscribers. With the addition of Birmingham, Detroit, Bakersfield, and Indianapolis this year, BHN will offer Digital Phone service to almost REDACTED of the homes passed by BHN facilities in the United States. Aside from the period of service disruption discussed below, BHN is experiencing Digital Phone subscriber growth of approximately REDACTED subscribers per week, which is expected to grow to between REDACTED subscribers per week as Digital Phone is rolled out in remaining BHN markets. BHN's Digital Phone architecture is designed to serve over REDACTED new voice customers in 2005, and we expect subscriber growth to match that projection.

5. In addition to our current offering, BHN intends to offer our customers the following value-added features: multiple telephone lines, a local-only service, seasonal rates, bulk

rates for multi-dwelling units, and a host of other calling features that will offer customers an enhanced and expanded telephony experience.

6. BHN competes head-to-head in the local Florida voice telephony market and the high-speed data market with Verizon Communications, Inc. ("Verizon"). In the Tampa area, Verizon has announced plans to compete in the video programming market as well. As a facilities-based carrier, BHN does not resell the services of the incumbent LEC, nor do we rely on or purchase unbundled network elements. However, we rely heavily on the services offered by MCI, Inc. ("MCI). In order to effectively and aggressively enter the Florida voice services market, BHN elected to partner with MCI to provide a variety of voice-related capabilities. Specifically, MCI provides the following services in support of our voice services product:
   a. **Local network connectivity** – MCI provides connectivity to the ILEC tandems, PSAP tandems and other local traffic terminating points. MCI is responsible for securing the necessary interconnection agreements with each incumbent LEC within BHN's footprint.
   b. **Long distance network connectivity** – MCI provides connectivity to their long distance transport network for delivery of intra- and inter-LATA calling traffic.
   c. **Traffic backhaul** – Through its UUNET affiliate, MCI provides network connectivity of signaling, voicemail and other associated traffic between our main network operating center and the other BHN divisions located in Birmingham, Detroit, Bakersfield, and Indianapolis.

d. **SS7 support** – MCI provides support for signaling protocol and other messaging related to call set-up, tear-down, and in-call feature manipulation.

e. **Telephone number management** – MCI provides BHN subscribers with telephone numbers acquired from the North American Numbering Plan Administrator (NANPA).

f. **Service order processing** – MCI provides BHN with the systems, personnel, and processes to support voice services order processing. This activity is further detailed below:

   i. New Service Orders- MCI processes all BHN orders for both native telephone numbers as well as customers who wish to port their number from their current provider. MCI's unique expertise in handling number porting requests was an important selling point for BHN and remains an essential aspect of the service.

   ii. Moves, Adds, and Change Orders – MCI processes all move, add, and change orders that require either changes in their network or LEC changes (such as directory listing changes)

   iii. Disconnect Orders – MCI processes all disconnect orders for removing voice services from BHN and MCI systems, including porting out numbers for customers moving to another carrier.

g. As part of the order processing capability, MCI performs the following functions:

   i. LEC CSR Access -- MCI pulls the relevant customer service report from the porting carrier, to confirm order entry information necessary to process a ported order.

ii. MSAG Validation – MCI ensures that the street address provided for the customer conforms to addressing standards to support full E911 capability.

iii. Ported Number FOC – MCI coordinates with the porting carrier to establish a date for porting the number of a new customer.

iv. TN Activation – MCI activates the new telephone number, both with regard to its network as well as in our network.

v. ALI Update – MCI updates the address lookup information for the telephone number to ensure proper E911 routing and response

vi. LIDB Update – MCI updates the line information database with relevant customer information as required.

vii. CNAM Update – MCI updates caller ID information as required.

viii. CARE Update – MCI updates the long distance carrier information to reflect MCI as the long distance provider.

h. **Domestic Long Distance** – As part of the service bundle, MCI provides unlimited domestic long distance service for BHN customers.

i. **International Long Distance** – MCI offers a discounted rate plan for calls to locations around the world. REDACTED

j. **Operator and Directory Assistance Services** – MCI provides our operator support system and directory assistance/411 services.

7. These services as provided by MCI are critical services in support of our voice product. Most notable are the network connection, network capacity and order processing services, including MCI's proven expertise in number porting.

8. We have already experienced one business slow down due to MCI's failure to meet performance commitments, so we have a painful awareness of just how essential their continued good performance is to our business overall. Between August of 2004 and February of 2005, MCI experienced difficulty meeting its service level obligations, and was unable to process BHN service orders in a timely manner. The result of this slowdown was redacted shortfall from projected Digital Phone subscriber growth during this period, which translates into a loss of nearly REDACTED potential subscribers.

9. Given our experience with service level interruptions, it is clear that a decrease in service by a Verizon-owned MCI could seriously affect our business performance in a number of dimensions. For example, if MCI does not properly size its network and telephone number capacity, we will not be able to sell or install at the rate driven by market demand. If MCI does not invest in improved or enhanced processes and systems, the amount of customer orders rejected or reworked will negatively impact our business. In addition, if MCI does not invest in the proper resources to monitor and address call and network quality and otherwise meet service levels, the perception of our product will be diminished in the eyes of our customers.

10. Moreover, if MCI loses its incentive to expand and grow its business as it has traditionally done, then our ability to rapidly acquire and install new customers, as well as respond to their service requests, would be severely diminished.

11. Finally, we are highly dependent on MCI to provide these services in a cost-effective manner. BHN's financial model for Digital Phone service is based on the competitive availability of wholesale services as MCI provides them today. If MCI begins to alter

the current financial model to favor of its parent Verizon, it could have a negative impact on the value of our product versus that of competitors.

12. There are two other known providers of the services MCI offers us today: Sprint and Level 3. Sprint is an incumbent LEC in our Central Florida market, and thus one of our primary competitors. This presents certain competitive problems similar in type to those we face with the proposed MCI/Verizon merger.

13. BHN considered Level 3 when it began development of its Digital Phone service and found Level 3 an unattractive alternative due to its poor rate center coverage in BHN markets. Since that time, Level 3 has exited the business services provisioning market and is in the process of retreating from the residential wholesale provisioning market altogether. BHN does not view Level 3 as a reliable long-term provider of wholesale services required to support Digital Phone service.

14. As neither of those providers is a workable alternative, BHN would have to construct redundant capabilities to replace those that MCI provides today independently. This option would significantly impact on our business plan in at least the following ways:

    a. Customer impact – Transitioning from one service provider to another (or a host of others) could result in our customers being impacted by service outages, improperly processed orders, and diminished service availability and performance.

    b. Slow down in product evolution – rather than evolving the product portfolio forward, business resources will be focused on re-creating existing capabilities and services.

    c. Cost – Transitioning would impose substantial costs on BHN and would amount to, at a minimum, several millions of dollars, and more likely would run into the tens of millions. Transition costs include the cost of purchasing duplicative services during the transition period, the costs of new construction and substantial extra labor, and substantial startup costs with the new providers, in addition to significant lost revenues due to inevitable customer service problems resulting from the complete overhaul of a network relied upon by over 200,000 subscribers on a day-to-day basis. Perhaps the most substantial cost would be BHN's inability to aggressively pursue and add new Digital Phone subscribers, as the task of simply maintaining service to the installed base during the transition period would make new customer adds a lower priority. BHN estimates that such a transition would result in a redacted month delay in projected subscriber growth and a concomitant substantial decrease in revenue growth.

I affirm under penalty of perjury that, to the best of my knowledge, the foregoing paragraphs are true and correct, and that I am qualified to so affirm.

Arthur C. Orduna
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5/24/05
Date