as VoIP) in place of wireline service. The threat of such defections serves to constrain the pricing behavior of traditional wireline providers.

Further competition is provided by cable companies that provide circuit-switched telephony, as well as by other modes of communication such as e-mail and instant messaging.[55] Considering the state of competition using these alternative forms in late 2003 and early 2004, the Commission found that more than "85% of Verizon's access lines are located in wire centers that have [a competition] index of at least 2.75," which the Commission found "reflects a suitably robust mixture of alternatives."[56] There can be no doubt that, in the last 18 months, competitive alternatives have increased, as cable, VoIP and wireless providers have made aggressive competitive inroads into the mass market.

Verizon is losing tens of thousands of lines per month in New York, with intermodal competitors the primary beneficiaries. Verizon's Wholesale Markets group has examined the shift of consumers away from UNE Platform lines and to alternatives, in New York and across the Verizon East footprint. Over the first five months of 2005, there has been a substantial reduction in the number of new UNE Platform lines in New York, dropping from nearly **[BEGIN CONFIDENTIAL]** **[END CONFIDENTIAL]** in January 2005 to just over **[BEGIN CONFIDENTIAL]** **[END CONFIDENTIAL]** in May 2005, a reduction of 45

[55] *See Intermodal Services Proceeding Order* at 5 & n.3, 6-7. Consistent with its failure in other respects to take a forward-looking view, Staff acknowledged the "growing evidence that consumers increasingly view these new [Internet] technologies as substitutes for wireline voice service," but ignored them in analyzing the effect of this transaction on competition for mass-market consumers. White Paper at 24. Like wireless service, e-mail and instant messaging are undoubtedly substituting for wireline voice minutes, as "[c]onsumers are using e-mail and instant messaging in place of a phone call." In-Stat/MDR, *State of the U.S. Carrier Market* at 6 (Oct. 2003).

[56] *Intermodal Services Proceeding Order* at 9. The competition index considered each Verizon wire center and assigned varying weights based on the presence of different types of competitors. The maximum index value was 3.25, which would be assigned to a wire center where circuit-switched cable telephony (1), residential UNE loop service (1), wireless service (0.5), and VoIP (0.75) are all available. *See id.*

percent.[57] Over that same period, the number of customers moving from UNE-P back to Verizon's retail service in New York has remained stable, at about **[BEGIN CONFIDENTIAL]** **[END CONFIDENTIAL]** per month. Thus, in May 2005, Verizon line losses to UNE-P in New York roughly equaled its returns from UNE-P. However, total UNE-P lines in service for May 2005 shows a *net loss* of **[BEGIN CONFIDENTIAL]** **[END CONFIDENTIAL]** access lines. That is because nearly **[BEGIN CONFIDENTIAL]** **[END CONFIDENTIAL]** customers in New York left their UNE-P provider and moved off of Verizon's network, presumably to an intermodal competitor. This figure has stayed roughly constant from January through May 2005, with an average of more than **[BEGIN CONFIDENTIAL]** **[END CONFIDENTIAL]** customers per month in New York moving off of and not returning to Verizon's network in New York. And this figure understates Verizon's total line losses in May 2005 – which are estimated at more than **[BEGIN CONFIDENTIAL]** **[END CONFIDENTIAL]** – as it does not include customers that are switching directly from Verizon retail (rather than from UNE-P) to VoIP or wireless, or moving to New York and signing up with one of those providers in the first instance.

c. The Flaws In Staff's HHI Calculations

Calculation Based on FCC Form 477 Data. Staff's first calculation is based on data submitted to the FCC twice each year using its Form 477. The primary flaw in Staff's use of this data set is that the data are from June 2004. In the 14 subsequent months, the communications industry has undergone substantial changes. These include legal changes, such as the Supreme Court's decision to deny petitions for a writ of certiorari from the D.C. Circuit's *USTA II*[58]

[57] "New" UNE-P lines are existing Verizon retail customers that moved to a UNE-P provider and customers not currently served by Verizon retail or a CLEC using resale, UNE-P, or UNE-L that move to a UNE-P provider.

[58] *USTA v. FCC*, 359 F.3d 554, 594 (D.C. Cir.) ("*USTA II*"), *cert. denied*, 125 S. Ct. 313, 316, 345 (2004).

decision, the FCC's release of the *Interim Rules Order*,[59] the release of the *Triennial Review Order*,[60] this Commission's approval of tariff revisions reflecting those legal changes, and the release of the FCC's decision regarding porting of numbers between wireline and wireless carriers. There have also been substantial technological changes, as both cable companies and other competitors have moved aggressively and successfully to offer VoIP service throughout New York and the nation, and wireless providers have continued to take wireline customers and wireline minutes away from incumbents and traditional IXCs. In this rapidly changing industry, where even the recent past is not prologue, there is no basis for drawing any meaningful conclusions from data that are 14 months old. Cablevision, for example, more than tripled its total number of voice customers between the second quarter of 2004 (115,050) and May 5, 2005 (400,000), with net gains of nearly 130,000 customers through May 5, 2005 alone.[61]

The data on which Staff relied, moreover, are plainly incomplete. As even Staff acknowledges, wireless carriers do not fill out Form 477, nor do VoIP providers.[62] And, although cable telephony providers can submit Form 477, Staff admits that the data on which it relied did not include "*any* voice grade lines" for the "largest cable VoIP provider in New York."[63] As explained above, any analysis that does not include the extensive (and growing) intermodal competition in the mass market is flatly inconsistent with this Commission's

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[59] Order and Notice of Proposed Rulemaking, Unbundled Access to Network Elements; Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers, 19 FCC Rcd 16783 (2004) ("Interim Rules Order") (subsequent history omitted).

[60] Report and Order and Order on Remand and Further Notice of Proposed Rulemaking, *Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, 18 FCC Rcd 16978 (2003) ("*Triennial Review Order*") (subsequent history omitted).

[61] *See* Cablevision Presentation at the Deutsche Bank Securities Media Conference at 29 (June 6, 2005), available at http://library.corporate-ir.net/library/10/102/102703/items/154595/deutsche_final.pdf.

[62] *See, e.g.*, White Paper at 22.

[63] *Id.* (emphasis added).

precedent, as well as the policies it has implemented to foster facilities-based, intermodal competition, and Staff provides no justification for this inconsistency. In addition, carriers that serve fewer than 10,000 lines in a given state are not required to file a Form 477, and the FCC has explained that, while it is not "certain about the extent to which . . . lines . . . as reported by CLECs are understated as a result" of this cut-off, it "expects such understatement to be larger, on a percentage basis, than for [independent] ILECs."[64] These omissions render the Form 477 data unsuitable for assessing the effects of this transaction on a "Wireline Voice Market" – as if there were such a market – let alone in the actual, intermodal mass market where Verizon is "losing over 75,000 [lines] a month" – nearly double its losses a year earlier, and despite the elimination of the UNE Platform.[65] Indeed, Staff explicitly recognized, albeit with considerable understatement, that the omissions from the Form 477 data "may overstate the mass market concentration."[66]

Finally, the predictions Staff made of the effect of this transaction on market concentration are based on the same Form 477 data as Staff's HHI calculation for the June 2004 data.[67] Therefore, the predictions suffer from the same flaws as discussed above. In addition, Staff did not factor in the more recent competitive trends, making no effort to adjust the prediction to account for the fact that New York cable companies recently completed their network upgrades, and are making steady gains in their subscriber base, the current and likely future dramatic gains by VoIP providers, the trends in wireless substitution for wireline lines and

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[64] FCC Wireline Competition Bureau, Local Telephone Competition: Status as of June 30, 2004, at 1 n.3 (Dec. 2004) ("*June 2004 FCC Report*").

[65] White Paper at 53.

[66] *Id.* at 22. Because of the difficulty in obtaining reasonably accurate data with which to estimate forward-looking shares of all meaningful competitors in the mass market, Verizon has not attempted to recalculate HHIs for the mass market.

[67] *See id.* at 21-22 (Figure 1).

usage, or the decline of MCI that began before the transaction and would have continued regardless of the transaction.

Calculation Based on PAP Data. The Staff also performed HHI calculations on data from Verizon's April 2005 Performance Assurance Plan ("PAP") report. Although these four-month-old data are more recent than the June 2004 Form 477 data, they are equally incomplete. The PAP data Staff used were limited to considering competition through UNE-P, resale, and UNE loops. Accordingly, these data do not even reflect all wireline competition, let alone the extensive intermodal competition that exists today from cable providers, wireless providers, VoIP providers and others. Recognizing this flaw, Staff modified the PAP data to include "a single Cable/VoIP provider with a 5% [market] share."[68] This assumption, however, does not track the actual entry of numerous cable and unaffiliated VoIP providers.[69]

Because the base calculation using the PAP data provides no meaningful information on the likely effects of this transaction on the mass market, there is no reason to consider Staff's "Scenario 2," where it assumed that MCI's (and AT&T's) UNE-P customers would have migrated to Verizon and other competitors.[70] In any event, Scenario 2 is based on the inexplicable assumption that MCI would retain one-third of its mass-market customers, while AT&T would lose *all* of its customers – half to Verizon and half to other CLECs.

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[68] *Id.* at 24-25.

[69] Staff states that its 5 percent adjustment is "conservative" because Cablevision reported that at year-end 2004, "it had almost 273,000 customers, or 6% of our homes passed," and Time Warner served 1.9% of homes passed in its territory. Staff Response to Verizon's July 20, 2005 White Paper Questions at 3. Staff overlooks, however, that both of these companies' voice services have been growing extremely rapidly. Cablevision was up to 364,000 customers or 8% of homes passed by the end of the first quarter 2005, adding customers at the rate of 7,100 per week. *See* Cablevision Press Release, *Cablevision Systems Corporation Reports First Quarter 2005 Results,* (May 5, 2005). In addition, Time Warner reported 614,000 Digital Phone subscribers by the end of the second quarter of 2005, a 4% penetration of serviceable homes passed, and a quarterly growth rate of 65%. *See* Time Warner 2Q 05 Presentation, *available at* http://ir.timewarner.com/downloads/Q205presentation.pdf. Ignoring such tremendous growth is anything but conservative.

[70] *See* White Paper at 25 & n.63.

d. The Remedies Offered For Consideration Are Unnecessary And Should Not Be Adopted As Conditions To Approval

Because there is no basis on which to conclude that this transaction will have a material, negative effect on competition for mass-market customers, there is no legal or factual basis for adopting any of the remedies that Staff proposes for consideration. Indeed, although Staff stated that it has "attempt[ed] to comport with the[] principles" for remedies set forth by the DOJ,[71] two of the three remedies Staff has suggested are squarely at odds with those principles because they are entirely unrelated to this transaction. The FCC has likewise held that it "will impose conditions only to remedy harms that arise from the transaction" and "will not impose conditions to remedy pre-existing harms or harms that are unrelated to the transaction."[72]

1. Stand-Alone DSL. Staff seeks comments on whether it would be appropriate to require Verizon to offer an "unrestricted" stand-alone DSL product to mass-market customers. It would not be appropriate to do so for several reasons. First, Staff's suggestion that Verizon might be required to offer stand-alone, or "naked," DSL has nothing to do with this transaction. Whatever the benefits for intermodal competition that might result from Verizon's offering of stand-alone DSL, those benefits are entirely unrelated to this transaction. Similarly, whatever impediments some might claim exist when customers seek to switch among intermodal competitors will not change upon the completion of this transaction. Accordingly, it would be inappropriate (and unwarranted) for this Commission to consider either requiring Verizon to provide stand-alone DSL or to take steps that purport to facilitate customers' switching among intermodal competitors.

[71] *Id.* at 17.

[72] AT&T Wireless-Cingular Order ¶ 43.

Second, Staff's suggestion takes no account of the fact that more than 90 percent of U.S. households are now able to obtain a broadband connection from a provider other than their incumbent local telephone company, principally cable modem service. Consumers can use those broadband connections to obtain VoIP either from cable companies or independent providers such as Vonage, regardless of the availability of naked DSL.

Third, as Petitioners explained in their May 13 Reply Comments, Staff's suggestion is largely moot because Verizon is already offering in New York several forms of "stand-alone DSL" services now and expects to be able to offer nearly all varieties in New York by September. Verizon realizes that offering such a product is imperative as a business matter, as customers are increasingly relying on broadband services to communicate and, in the process, are rapidly subscribing to VoIP services provisioned over broadband lines.[73] Verizon has moved to respond to this demand and is working on overcoming the technical issues that have thus far prevented it from offering stand-alone DSL service to all customers, as it wants to do.

In April 2005, Verizon began offering stand-alone DSL service to existing New York customers who port their voice line to a facilities-based carrier (including a VoIP provider) or wireless carrier but who want to retain their DSL service without the voice service. In June, Verizon expanded its offering to New York customers who have never had voice service with Verizon.[74] Therefore, for example, Verizon's DSL customers can cancel voice service from Verizon, obtain voice service from an independent VoIP provider such as Vonage, and retain their DSL line provided by Verizon. And new customers who do not currently have Verizon

[73] Thomson StreetEvents, VZ – Q2 2005 Verizon Earnings Conference Call, Final Transcript at 7 (July 26, 2005) ("In the next few months we will be more actively marketing 'DSL over dry loop,' or 'naked DSL.' We believe this presents a significant new opportunity for us to provide a data solution for the large number of wireless-only households.") (statement of Doreen Toben, Verizon CFO).

[74] *See* FCC Tariff No. 1, Access Services, § 16.8(D)(4)(b); FCC Tariff No. 20, Communications Services, § 5.1.2(D)(2).

voice service can purchase stand-alone DSL and, for example, obtain service from an independent VoIP provider. The last principal type of stand-alone service – for those using the commercial replacement for UNE Platform – should be implemented by September.

As discussed in the Petitioners' Reply Comments, it would be inappropriate (and unlawful) for the Commission to use its regulatory authority to interfere with Verizon's diligent efforts to offer stand-alone DSL to the remaining group of customers who cannot currently obtain stand-alone DSL service and to require Verizon to make the service available sooner than it is operationally possible to do so. The market is already motivating Verizon to provide the service to all customers and the Commission should allow Verizon to continue its efforts to do precisely that without imposing an artificial deadline. Such an approach is consistent with Commission's own thinking, as articulated in its Order initiating the "Comp III" proceeding:

> New York has long been on record stating its strong preference for competitive markets as the most effective approach to ensure the provision of reasonably priced and reliably provided telecommunications services... Where competition is robust, regulatory restraint is the best approach; where it is not, some intervention may be required to restrain the exercise of market power and ensure adequate consumer protections.[75]

Given that there is clearly strong, intermodal competition for mass market customers and Verizon is responding to it by, among other things, expanding its stand-alone DSL offering as soon as it is operationally possible to do so, it would be contrary to the Commission's stated goals to increase regulation at this time.

Finally, requiring Verizon to offer stand-alone DSL service would violate federal law. Just today, the FCC adopted an order declaring wireline broadband Internet access to be an

[75] See Case 05-C-0616, Proceeding on Motion of the Commission to Examine Issues Related to the Transition to Intermodal Competition in the Provision of Telecommunications Services, Order Initiating Proceeding and Inviting Comments (June 29, 2005) at 2.

unregulated information service.[76] And this Commission has no jurisdiction to regulate the rates, terms, and conditions on which Verizon offers this *interstate* service, including regulation of whether Verizon offers this service separate from its retail voice product.

Furthermore, to the extent Staff contemplated requiring Verizon to provide retail DSL service on the same line over which an end-user customer obtains voice service from a CLEC, such an obligation would be unlawful for still another reason. In the *BellSouth Preemption Declaratory Ruling*, the FCC explicitly held that states violate federal law to the extent they require incumbents to provide DSL service to customers that purchase voice service from CLECs that use unbundled loops.[77] That is because such a requirement would impose on incumbents an obligation to "do exactly what the [FCC] expressly determined was not required by the Act" – namely, to provide DSL service over the high-frequency *portion* of a loop – and is "therefore inconsistent with federal law."[78]

2. Switching Among Intermodal Service Providers. Staff seeks comment on whether there exist any "impediments which impair a cust[o]mer's ability to switch between wireline, DSL and cable modem based telephone service providers."[79] As an initial matter, any such impediments would not be specific to this transaction and, therefore, it is inappropriate to consider this question in the context of this proceeding. In any event, there are no meaningful issues – certainly none that must be overcome by additional regulation, rather than market-based solutions. More than 70 percent of New Yorkers with broadband connections subscribe to *cable modem* providers, so these customers need do little more than sign up for VoIP – provided by

[76] FCC News Release, *FCC Eliminates Mandated Sharing Requirement on Incumbents' Wireline Broadband Internet Access Services* (Aug. 5, 2005).

[77] *See id.* ¶¶ 17, 25-26.

[78] *Id.* ¶ 27.

[79] White Paper at 26.

either their cable company or one of many other firms – to switch from their existing wireline service.[80] And 95 percent of New Yorkers have access to broadband service from the dominant cable modem providers or from other providers, and could obtain broadband service and switch to a VoIP provider as well.[81] Verizon's voluntary retail, stand-alone DSL offering will also enable consumers easily to switch from wireline service to VoIP-over-DSL. In short, there are no meaningful impediments for those customers that wish to switch from wireline service to VoIP service, as evidenced by the rapid penetration of VoIP into the residential market. Finally, imposing conditions solely on Verizon's DSL product – which provides a distinct minority of broadband services in the state – would only alter the competitive landscape by further strengthening cable's (unregulated) broadband lead in New York.

3. Freezing MCI's Rates, Terms, and Conditions. Staff also questions whether it would be appropriate to "freez[e] MCI's rates, terms and conditions for MCI mass market customers for 12 months from the date of the merger."[82] Staff suggests this might be appropriate to "insulate [these] customers from the short term negative effects of the merger."[83] But Staff does not explain what those effects could be. In any event, it would not be appropriate to freeze MCI's rates as suggested.

The condition that Staff tentatively suggests is tantamount to rate regulation of a competitive carrier without the corresponding benefit of a guaranteed rate of return. This is flatly contrary to the regulatory regime and policies the Commission has long applied to

[80] *See* FCC Wireline Competition Bureau, *Local Telephone Competition: Status as of June 30, 2004* at Table 7 (July 2005) (reporting data as of December 31, 2004). This compares to less than 23 percent of New Yorkers having chosen DSL.

[81] Intermodal Services Proceeding Order at 8.

[82] White Paper at 26.

[83] Id.

competitive carriers, and ignores the fact that MCI's mass-market customers have freely chosen MCI (instead of Verizon or another competitor) and remain free to choose a different provider in the future. The concern animating Staff's tentative proposal is a vestige of monopoly regulation that has no place in a competitive market, where protection to consumers comes in the form of services offered by facilities-based and intermodal competitors. And a proposed governmentally mandate "rate freeze" ignores the fact that MCI will face increases in the costs of providing service to mass market customers.

Moreover, because MCI's existing retail packages include bundles of intra- and *inter*state services, this Commission lacks jurisdiction over all of MCI's rates, terms, and conditions for those packages.[84] For these reasons, there is no basis for the Commission to impose additional regulation on MCI's current plans.

2. Enterprise Customers – Retail

a. This Transaction Will Not Reduce The Intense Competition For Enterprise Customers Or For The High-Capacity Facilities Used To Serve Those Customers

Petitioners have demonstrated that the combination of their highly complementary operations would have significant benefits for large enterprise and other commercial and institutional customers by creating a strong new competitor with the network reach and financial resources to compete in this market segment nationwide. The two companies have highly complementary – rather than overlapping – core competencies, with MCI a primary provider of global business communications services and IP-based services and Verizon a provider of local

[84] *See, e.g.*, *Dreamscape Design, Inc. v. Affinity Network, Inc.*, ___ F.3d ___, No. 04-3035, 2005 WL 1560330, at *9 (7th Cir. July 5, 2005) ("state law cannot operate to invalidate the rates, terms, or conditions of a long-distance service contract"); *Boomer v. AT&T Corp.*, 309 F.3d 404, 417-24 (7th Cir. 2002) (holding that 47 U.S.C. §§ 201 and 202 "demonstrate a congressional intent that individual long-distance customers throughout the United States receive uniform rates, terms and conditions of service" and that state law regulation of such interstate services is preempted).

bandwidth, CPE and related services, and network integration. Indeed, in more than 96 percent of the more than 800 instances between October 1, 2004 and April 20, 2005 in which MCI bid on enterprise contracts, Verizon was not among the competing bidders.[85]

Although MCI and Verizon rarely compete head-to-head in bidding for the business of enterprise customers, there is extensive competition for all different types and sizes of such customers, and for various services they purchase. There are large numbers of providers competing for these customers today, none of which has a dominant share, including traditional interexchange carriers such as AT&T, Sprint, and Qwest; CLECs like XO and Level 3; cable companies such as Time Warner and Cablevision; systems integrators and managed service providers like IBM, EDS, Accenture, Northrop Grumman, and Lockheed Martin; major global telecommunications providers such as Equant, British Telecom, Deutsche Telekom, COLT, KPN Telecom, and NTT; equipment vendors like Lucent and Nortel; and, most recently, major application providers such as Microsoft. The combined company will be just one among many other competitors in this segment of the industry, which is widely recognized as the most competitive.[86]

b. The Flaws In The Staff's HHI Calculations

In reaching the contrary conclusion, Staff again relied exclusively on HHI calculations. And, again, Staff relied on incomplete and out-of-date data. Staff also made numerous errors in its HHI calculations and drew the wrong conclusions from the results of those calculations. For these reasons, and as set forth in further detail below, nothing in the White Paper supports the

[85] *See* Ex Parte Letter from Verizon and MCI to FCC, WC Docket No. 05-75, at 2-3 n.5 (filed July 1, 2005) ("July 1, 2005 Ex Parte Letter").

[86] *See* Petitioners' Reply Comments at 34-38.

view that this transaction will result in any material concentration in the market for retail enterprise services.

Calculation Based on FCC Form 477 Data. Staff first used the June 2004 FCC Form 477 to calculate an HHI for the "Wireline Voice Market" for enterprise customers. As explained above, the data are both outdated and incomplete – because there is no "*wireline voice*" market for enterprise customers – which necessarily means that any calculations of HHIs from the data is not probative. Indeed, the Form 477 data measures only "*Switched* Access Lines" obtained by enterprise customers, and only from those ILECs and CLECs required to submit Form 477.[87] Enterprise customers, however, do not merely purchase switched access services. Instead, these customers purchase a wide array of communications services, including voice (domestic and international), data (Frame Relay, ATM, IP/VPN), CPE, ancillary services, and network integration services. Large enterprise and other commercial and institutional customers now spend more on data and wireless than they spend on wireline voice, and data and wireless are growing considerably, while wireline voice spending is declining.[88] Enterprise customers also obtain voice services through other technologies, such as VoIP, without obtaining switched access lines. Any analysis of competition for this customer segment, therefore, must analyze the full array of services and facilities that large enterprise customers and medium businesses purchase, and cannot focus solely on switched access, wireline services.[89]

[87] *June 2004 FCC Report* at Table 2 (emphasis added).

[88] See Kneko Burney, InStat/MDR, Share of Wallet?: Telecom Trends and Expenditures in the US Business Market; Part One: US Enterprises (1,000+ Employees) at Table 7 (Aug. 2004); Kneko Burney, InStat/MDR, Share of Wallet?: Telecom Trends and Expenditures in the US Business Market; Part Two: Mid-Sized Businesses (100-999 Employees) at Table 7 (Sept. 2004).

[89] For these same reasons, Staff's prediction of HHIs after this transaction provides no meaningful data on the consequences of this transaction. *See* White Paper at 32. In addition, as explained above, Staff's projection is based on a simple time series extrapolation that ignores technological trends and the expected growth of various alternatives.

Calculation Based on Lehman Brothers Data. Staff also performed HHI calculations on Lehman Brothers' estimations of the share of national enterprise revenues.[90] As Staff recognized, these data indicate that this transaction "only would result in a relatively unconcentrated market that might not warrant further review."[91] It is only by considering both this transaction and the proposed combination of SBC and AT&T that Staff could find a "change in HHI" that it contends means this transaction "warrants further review" – even while reaching no such conclusion with respect to the combination of SBC and AT&T.[92] In fact, using the Lehman Brothers data, it is the AT&T-SBC merger that increases the national HHI by 414 – from 764 to 1,178 – while this transaction on its own increases the HHI by only 231 points from 764 to 995. Even if one were to assume that the base is one where the AT&T-SBC merger has been completed, the Lehman Brothers data would show this transaction as increasing the HHI by only 231, from 1,178 to 1,409, which is a far cry from the HHIs in transactions that DOJ or the FTC have recently challenged. The 645 point increase shown in the last column of Staff's Table 5 is premised on the erroneous assumption that the two mergers should be considered as a single transaction.

Apparently recognizing that no serious case can be made that this transaction will materially reduce competition for enterprise customers nationwide, Staff attempts to construct an analysis of competition for enterprise customers within Verizon's region. As an initial matter, this approach is erroneous. There is no "regional" market for enterprise customers, which often have locations in the territory of more than one incumbent carrier. The largest of these customers operate internationally. Thus, the enterprise market is national, if not international, in

[90] *See id.* at 29.

[91] Id.

[92] *Id.*; *see id.* at 73.

scope. Indeed, the FCC has found that the relevant geographic market for enterprise customers is "a single national market."[93] Accordingly, the approach of calculating HHIs based on a Verizon-region enterprise market is mistaken from the outset.

In addition, Staff's efforts to translate Lehman Brothers' nationwide revenue and share estimates into Verizon-region estimates resulted in numerous calculation errors. These range from the trivial to the fatal. On the minor side, Staff failed to use the same revenue figures for the pre- and post-transaction HHI calculation.[94] In a proper HHI calculation, the pre- and post-transaction shares of the non-combining companies should remain constant. Far more serious was Staff's decision to exclude entirely the "Other" category, which included all companies serving enterprise customers other than the *nine* specifically identified by Lehman Brothers, and which account for more than 30 percent of the nationwide revenues from sales to enterprise customers.

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[93] E.g., Memorandum Opinion and Order, Application of WorldCom, Inc. and MCI Communications Corporation for Transfer of Control of MCI Communications Corporation to WorldCom, Inc., 13 FCC Rcd 18025, ¶ 30 (1998); Memorandum Opinion and Order, Applications of NYNEX Corp. and Bell Atlantic Corp. For Consent to Transfer Control, 12 FCC Rcd 19985, ¶ 54 (1997).

[94] For example, Staff derived pre-transaction revenues of $3.86 billion for AT&T, but set AT&T's post-transaction revenues at $3.62 billion. *See* White Paper at 30. Similar reductions occurred for Sprint, Level 3, and XO. *See id.* In any event, Staff's derivations of companies' enterprise revenue within Verizon's region are fraught with error. Staff attempted to derive the revenue figures by using data from a Verizon SEC filing and extrapolating based on the Lehman Brothers market share estimations and an estimate of Verizon's share of switched access lines. Staff apparently did not realize that the actual Lehman Brothers report contained nationwide revenue figures. *See* Declaration of Eric J. Bruno & Shelley Murphy, Exhibit 1 (Attachment 3 to Application for Transfer of Control, WC Docket No. 05-75 (FCC filed Mar. 11, 2005)). In addition, in converting from nationwide to regional figures, Staff used "the percentage of RBOC customer access lines in Verizon's territory." White Paper at 29-30. But because Verizon's service territory is widely regarded to be more competitive than that of other RBOCs, using Verizon's share of RBOC lines as the basis for assigning revenues to different RBOC regions will understate the amount of competition in Verizon's service area. *See* Wachovia Capital Markets, LLC, Equity Research Department, *Verizon Communications* (Mar. 2, 2005) ("The core Verizon region (northeast U.S.) has been one of the primary battlegrounds since the beginning of telecommunications deregulation in 1984. Home to many of the Fortune 500 and particularly the telecommunications-intensive financial services industry; it has always been the first stop for competitors that target business customers."); Banc of America Securities, *Setting the Bar, Establishing a Baseline for Bell Consumer Market Share* (June 14, 2005) ("Among our conclusions divvying up market share loss between wireless and VoIP, we believe Verizon is suffering outsize losses relative to the rest of the Bells."). Assuming that Verizon has lost a larger percent of its lines to competitors than other RBOCs, it is clear that Staff's approach would understate the fraction of enterprise competition taking place in Verizon's area.

Petitioners understand that, based on the discussion of the Lehman Brothers data in the Crandall/Singer declaration Petitioners' submitted to the FCC, Staff concluded that none of the companies in the "Other" category operate in New York or in other Verizon territories.[95] But the Crandall/Singer declaration was not providing an exclusive list of the competitors for enterprise customers "other" than those identified by name in the Lehman Brothers report. Instead, that declaration was providing examples of the numerous companies that operate in the national enterprise market, including in New York. The fact that some of the companies named "were not immediately recognizable to Staff as New York competitors"[96] is hardly reason for presuming, as Staff did, that AT&T, MCI, Verizon, Sprint, Level 3, and XO account for anywhere near 100 percent of the sales to enterprise customers in Verizon's region, let alone in New York. In fact, as this Commission well knows and analysts confirm, New York and the rest of Verizon's northeast region "has always been the first stop for competitors that target business customers."[97]

Nonetheless, Petitioners have identified numerous carriers that compete for enterprise customers in New York that were not identified by name in the Lehman Brothers report. One such competitor is Cablevision, which as far back as 2000 beat out *twelve* other competitors (including then-Bell Atlantic) to win a multi-million dollar contract to serve Westchester County.[98] British Telecom offers ATM and other enterprise services in New York and has

[95] *See* Staff Response to Verizon's July 20, 2005 White Paper Questions at 4.

[96] Id.

[97] Kevin M. Moore, Wachovia Capital Markets, LLC, *Verizon Communications* at 3 (Mar. 2, 2005).

[98] *See* Brian Quinton, *Scoring in the Suburbs*, Telephony Online (Mar. 13, 2000), *available at* http://telephonyonline.com/ar/telecom_scoring_suburbs/. Cablevision also has won contracts to serve Long Island University and Lenox Hill Hospital. *See* Cablevision Lightpath Press Release, *Lightpath Links Long Island University* (Mar. 8, 2004), *available at* http://www.lightpath.net/Interior33-8.html; Cablevision Lightpath Press Release, *Lenox Hill Hospital Switches to Lightpath for Voice, Data, and Internet Services* (Aug. 11, 2003), *available at* http://www.optimumlightpath.com/Interior187-11.html.

acquired a "New York-based financial services extranet provider."[99] Both British Telecom and AboveNet have won contracts to serve the New York Mercantile Exchange.[100] Broadwing has won a contract to serve Petry Media, which is headquartered in New York City.[101] WilTel has won a contract to provide services to the New York State Education and Research Network.[102] These are just a handful of examples Petitioners were able to glean from press releases and other public sources, which demonstrate that in New York, as across the nation, there are numerous carriers successfully competing to serve enterprise customers, which fit within the "Other" category in the Lehman Brothers data. Therefore, it was plain error for the Staff to exclude the "Other" category in its entirety in its analysis.

Although, as explained above, there is no basis for calculating "Verizon-region" HHIs for enterprise customers, when Staff's calculation is corrected for these errors, using conservative assumptions – as well as the error of assigning SBC and Qwest $0 in enterprise revenue from customers in Verizon's territory[103] – the re-calculated HHI, per the Staff's approach, would have led Staff to conclude that this transaction raises no issues warranting additional consideration.[104]

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[99] *See* BT: Availability, *available at* http://www.btglobalservices.com/business/global/en/products/atm/availability.html; BT:News, *available at* http://www.btglobalservices.com/business/global/en/business/business_zone/issue_04/news_acquisitions.html.

[100] See AboveNet Press Release, New York Mercantile Exchange Selects MFN for Secure, High-Speed Private Optical Network (May 19, 2003), available at http://www.abovenet.com/news/pr051903.html; BT Press Release, New York Mercantile Exchange Upgrades Trading Floor with Digital Voice Trading Technology from BT (Feb. 1, 2005), available at http://www.btplc.com/News/Articles/Showarticle.cfm?ArticleID=1a019352-8e03-4ec8-8e54-9efc75d52ab2. AboveNet has also won a contract to provide service to Cantor Fitzgerald in New York. See AboveNet Press Release, Cantor Fitzgerald Selects AboveNet to Provide Critical Network Services Over Its Private Optical Network (Jan. 18, 2005), available at http://www.abovenet.com/news/pr011805.html.

[101] *See* Broadwing Press Release, *Petry Media Selects Broadwing Communications IP VPN Services* (Apr. 5, 2005), *available at* http://www.broadwing.com/bwngcorp/pressreleases/pr481.html.

[102] *See* WilTel Press Release, *NYSERNet Selects WilTel to Provide Network Solution for Research, Education Institutions in New York* (Dec. 13, 2004), available at http://www.wiltel.com/overview/content/pressreleases/2004/12-13.htm.

[103] SBC and Qwest both successfully compete for enterprise customers in Verizon's region. For example, SBC has recently won contracts to provide services to Bob Evans Farms, Inc., Martiz Inc., and Pillsbury Winthrop LLP in numerous locations, including New York. *See* SBC Press Release, *SBC Communications Announces New*

(continued . . .)

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Contract with Bob Evans Farms Inc. (Dec. 7, 2004), *available at* http://www.sbc.com/gen/press-room?pid=4800&cdvn=news&newsarticleid=21491; Bob Evans, Location Guide, *available at* http://www.bobevans.com/; SBC Press Release, *SBC Communications Announces Three-Year, Multimillion-Dollar Contract with Maritz Inc.* (Aug. 13, 2004), *available at* http://www.sbc.com/gen/press-room?pid=4800&cdvn=news&newsarticleid=21298; SBC Press Release, *SBC Communications Announces New Voice and Data Networking Services Contract with Pillsbury Winthrop LLP* (Jan. 11, 2005), *available at* http://www.sbc.com/gen/press-room?pid=4800&cdvn=news&newsarticleid=21544. Qwest has won contracts to serve Grubb & Ellis, Scotttrade, Hagemeyer North America, and Burlington Coat Factory, including at their locations in New York. *See* Qwest Press Release, *Grubb & Ellis Awards Qwest Communications Network Services Agreement* (Apr. 24, 2003), *available at* http://www.qwest.com/about/media/pressroom/1,1281,1254_archive,00.html; Grubb & Ellis, *Office Locations*, *available at* http://www.grubb-ellis.com/offices/; Qwest Press Release, *Scottrade Signs Multi-Year, Multimillion Dollar Contract with Qwest Communications* (June 17, 2003), *available at* http://www.qwest.com/about/media/pressroom/1,1281,1289_archive,00.html; Scottrade, *Branch Locator*, *available at* http://www.scottrade.com/frame_branchlocator.asp; Qwest Press Release, *Qwest Awarded Multimillion Dollar Contract Renewal by Hagemeyer North America* (Feb. 23, 2004); Hagemeyer North America, *HNA Locator: Branch Locator: New York State*, *available at* http://www.hagemeyerna.com/; Qwest Press Release, *Burlington Coat Factory Expands Contract with Qwest Communications for Advanced Network Services* (June 8, 2004); Burlington Coat Factory, *Find a Store: New York State*, *available at* http://corporate.burlingtoncoatfactory.com/cgi-bin/mqinterconnect?screen=find&smap=map&link=results&closestprox=1&closestn=5&miles=250&streetaddress=&city=&state=NY&zip=&country=US&x=65&y=3.

[104] The corrections of the errors Staff made in its analysis include: using the national revenue data from the Lehman Brothers report as a basis for deriving so-called "Verizon region" data; including the revenue that Lehman Brothers assigns to "Other" carriers; using the more realistic, but still conservative, estimate that 38.9% of AT&T's, MCI's, Sprint's, Level 3's, XO's, and the Other's national revenue is attributable to Verizon's region (*see supra* note 94); using the ratio of the special access lines that SBC and Qwest purchase from Verizon to the sum of their enterprise customer loops from ARMIS data plus those special access lines to determine the SBC and Qwest revenue to allocate to Verizon's region (*see supra* note 103); using the same revenue figures for the pre-transaction and post-transaction HHI calculations.

*** REDACTED VERSION ***

Adjusted Staff Enterprise Market Share Analysis

		Change in HHI		=	**660**			
		Before Merger			**After Merger**			
Market Total	154.80	57.28		1,220	57.28		1,880	
Company	**National Revenues**	**Revenues**	**Share**	**HHI**	**Revenues**	**Share**	**HHI**	
AT&T	24.50	9.54	16.6%	277	9.54	16.6%	277	
SBC	20.20	0.65	1.1%	1	0.65	1.1%	1	
MCI	18.30	7.12	12.4%	155				
Verizon	15.20	15.20	26.5%	704	22.32	39.0%	1,519	
Sprint	9.30	3.62	6.3%	40	3.62	6.3%	40	
Qwest	8.70	1.65	2.9%	8	1.65	2.9%	8	
Bell South	8.50	-	0.0%	-	-	0.0%	-	
Level 3	1.80	0.70	1.2%	1	0.70	1.2%	1	
XO	1.20	0.47	0.8%	1	0.47	0.8%	1	
Others	47.10	18.33	32.0%	32	18.33	32.0%	32	
Total	154.80	57.28	100.0%	1,220	57.28	100.0%	1,880	

Sources:
R. Dale Lynch and Blake Bath, *Enterprise Telecom; A Comeback Begins*, Lehman Brothers Equity Research Report, Nov. 11, 2003.
FCC, *Trends in Telephone Service*, as *of April 2005*, Table 7.3 and *Local Telephone Competition: Status as of December 31, 2004,* Tables 6 and 11.
SBC and Qwest Special Access Purchases.
Verizon Lines by State.

	Staff Original	With Changes
Pre-Merger HHI	2,924	1,220
Post-Merger HHI	4,679	1,880
Change in HHI	1,755	660

As shown in the tables above, on Staff's approach, it should have calculated a post-transaction HHI of no more than 1,880, rather than 4,679. Indeed, Staff's figure should have been less than 1,880, as the above table does not allocate any of Verizon's enterprise revenue to out-of-region customer locations and does not account for any enterprise revenue that SBC and Qwest obtain using their own facilities, rather than special access purchased from Verizon. For the same reasons, Staff should have calculated a change in HHI of no more than 660, rather than 1,755. As shown above, HHI numbers such as these are well within the range where the antitrust enforcement agencies do not challenge transactions as a practical matter. And because, as discussed, HHI calculations, when used, are only the beginning of an analysis of competitive effects of a transaction, consideration of other factors – such as the national characteristics of the enterprise segment, the heterogeneity and sophisticated nature of enterprise customers, the complex procurement practices followed in the segment, and the importance of non-price elements of competition for enterprise customers – leads to the conclusion that this transaction will not adversely affect competition for enterprise customers.

Analyst Reports. Staff also pointed to two analyst reports, which it asserted "suggest that the[] mergers [of AT&T and SBC and Verizon and MCI] will cause falling prices in the telecommunication[]s industry to slow."[105] In fact, there is no reason to think that this transaction will result in any lessening of existing vigorous competition for enterprise customers. On the contrary, because both this transaction and the SBC/AT&T transaction will result in significant savings through synergies, and because a core purpose of both transactions is to enhance the ability of the entities to compete aggressively for the business of enterprise customers, there is every reason to think that prices will fall even faster in the future.

c. Staff Correctly Concluded That No Remedies Are Warranted

Despite Staff's erroneous HHI calculations, it reached the correct conclusion that "direct retail based remed[ies] [are] not required."[106] Nor, as explained below, is there any need for indirect remedies that address wholesale services. There is robust retail competition to serve enterprise customers today, and this transaction will do nothing to lessen that competition.

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[105] White Paper at 30.

[106] *Id.* at 33.

3. Transport – Wholesale

a. This Transaction Will Not Reduce The Significant Competitive Deployment And Availability Of High-Capacity Transport Facilities

As discussed in Petitioners' May 13 Reply Comments, MCI's local fiber facilities have a very limited overlap with Verizon's facilities in New York and, more important, where they do overlap numerous other providers have deployed facilities as well. As Petitioners have explained, the overlap occurs in only seven wire clusters (totaling 48 wire centers) in New York, virtually all of which have fiber deployed by multiple additional carriers, at both the cluster and individual wire center level.[107] Indeed, there is an average of 12 additional competitors per cluster and 10 additional competitors per wire center where MCI has deployed local fiber networks in New York.[108] The extensive competition in the areas where MCI has deployed fiber should not be surprising, because MCI has focused its fiber deployment on the areas with the greatest demand for high-capacity services and the greatest potential for revenues – factors that obviously also attract other carriers.

The data available to Petitioners about other carriers' fiber deployment, however, are necessarily limited and, therefore, certainly understate the extent of fiber deployment in the areas in which MCI has deployed fiber. Nonetheless, the maps included in Exhibit 2 demonstrate the extensive fiber deployment by carriers other than MCI in the wire center clusters where MCI has local fiber networks in New York.[109] These maps also show that there are extremely few areas

[107] *See* Petitioners' Reply Comments at 29-31.

[108] See id.

[109] The maps are based on data from MCI regarding its fiber network, Verizon's inspection of its central offices to identify fiber-based collocation, and data obtained from a third-party (GeoTel) which has an incomplete list of fiber deployed by other carriers. The maps show fiber in the entire state, as well as detailed sections in the New York Metro, Albany, Buffalo, and Syracuse MSAs. The maps depict fiber deployed by 35 carriers in addition to MCI in the New York Metro MSA, and by 7 carriers in addition to MCI in each of the other three MSAs.

where MCI has deployed fiber that does not overlap with fiber routes deployed by at least one other carrier. In addition, where MCI's fiber does not directly overlap with other carriers' fiber, it is located very close to fiber that is currently deployed by at least one other carrier and that economically could be extended to serve the areas where MCI found it made economic sense to deploy its own fiber. And, again, the maps understate the extent of other carriers' fiber deployment, because Petitioners do not have access to maps of all other carriers' fiber networks.

Moreover, these other carriers offer access to their fiber networks on a wholesale basis. Indeed, operators of competitive fiber networks routinely offer high-capacity services over those networks on a wholesale basis to other carriers, from the DS1 level all the way up to the highest capacity OCn levels. For example, of the seven carriers with fiber networks shown on the map of the Albany MSA, at least five advertise their wholesale services. Thus, MCI is not a unique provider of wholesale access to fiber networks in any part of New York. This transaction, therefore, will have no material effect on the availability of fiber transport in New York.

b. The Flaws In Staff's HHI Calculations And Overlap Analysis

All of the evidence detailed above demonstrates that the combination of Verizon and MCI will not have a material effect on the availability of high-capacity transport facilities in any area in New York. Staff reached the contrary tentative conclusion because it relied on an outdated and incomplete set of data to determine the extent of fiber deployment in New York: the self-reported data obtained in late 2003 and early 2004 in response to the *Triennial Review Order*.[110] As an initial matter, many carriers with fiber networks in New York – including Looking Glass and Neon, among others – were not parties to that proceeding and did not respond to the Staff's requests for data. Indeed, only 17 carriers submitted data in response to Staff's

[110] *See* White Paper at 34.

request.[111] The maps Verizon has attached, however, include more than 20 fiber providers in addition to those that submitted data to Staff. In addition, as even Staff recognized, the data that the carriers submitted "contained numerous inconsistencies," and some companies did not submit data but instead "indicated that they do not maintain data in such a way as to be able to answer [Staff's] questions" or "claimed that answering [Staff's] questions . . . would be cost prohibitive."[112] Because Staff's transport analysis is entirely based on this fundamentally flawed data set, no meaningful conclusions can be drawn from the calculations it conducted, which are discussed in further detail below.

Calculation of Transport HHIs. Staff conducted three HHI calculations.[113] Petitioners understand that, for each calculation, Staff first determined the number of mathematically possible intraLATA transport routes between Verizon's wire centers.[114] Staff then assumed that Verizon has deployed transport on each possible route. Staff then considered the self-reported data from other carriers on their transport routes, considering a route to exist only if the carrier stated that it actually had deployed transport directly between two wire centers. In other words, if a carrier stated that it had deployed transport between points A and B and B and C, but did not state that it had a transport route between A and C, Staff did not count the carrier as having transport on the A to C route. This is in stark contrast to Staff's assumption with respect to Verizon, which often can transport traffic between two wire centers only indirectly, routing it

[111] *See* Case 03-C-0821, Descriptive Summary of Department of Public Service Staff's Preliminary Data Collection Effort (Nov. 17, 2003), at 4 ("Descriptive Summary").

[112] Descriptive Summary at 4.

[113] *See* White Paper at 34-35.

[114] That number is calculated using the formula n!/[(n-2)!2!], where n is the number of Verizon wire centers in a LATA. Therefore, if Verizon has 5 wire centers in one LATA and 7 wire centers in another LATA, the number of mathematically possible intraLATA routes is 31, with 10 possible in the first LATA (5!/[3!2!]) and 21 possible in the second LATA (7!/[5!2!]).

through other wire centers. Finally, Petitioners understand that Staff used this data to assign "shares" of a "transport market" based on the number of routes it had calculated.

The errors in this approach are many. The primary one is the reliance on the extremely limited self-reporting of transport routes from a more than 15-month-old proceeding. As the maps in Exhibit 2, the data Staff collected dramatically understate the extent of the fiber networks that other carriers have deployed in New York, and of course provide no information on where competitors would be able to provide competitive fiber if MCI's fiber network were no longer available on a wholesale basis. Therefore, regardless of whether Staff performed its calculations on all conceivable routes in Verizon's territory in New York, or only those routes in LATA 132 where two carriers had self-reported that they had deployed transport, or only those routes where Verizon no longer has an obligation to provide DS1 or DS3 transport as a UNE, the results of the calculations are meaningless because they exclude both significant fiber deployment and potential deployment.

Transport Overlap Analysis. Staff also sought to call into question Petitioners' demonstration that MCI's local fiber networks overlap with Verizon's to only a limited extent and that numerous other providers have deployed fiber in the limited areas where there is overlap.[115] To conduct its analysis, Staff reviewed Appendix E of Verizon's PSC NY No. 10 tariff, which lists a total of 41 wire centers: 30 that are "Tier 1" wire centers under the criteria the FCC established in the *Triennial Review Order* and 11 that are "Tier 2" wire centers under those same criteria.[116] There are 487 mathematically possible intraLATA routes between these

[115] *See* White Paper at 35-37 & Table 8.

[116] Verizon is not obligated to provide UNE DS1 or DS3 dedicated transport on routes between two Tier 1 wire centers. *See TRRO* ¶¶ 126, 129. Verizon is not obligated to provide UNE DS3 dedicated transport on routes between a Tier 2 wire center and a Tier 1 or Tier 2 wire center, but must provide UNE DS1 transport on those routes. *See id.*

wire centers: 465 in LATA 132 (New York Metro), 21 in LATA 140 (Buffalo), 1 in LATA 134 (Albany), and 0 in LATA 136 (Syracuse), where there is only one Tier 1 wire center and no Tier 2 wire centers, and therefore no intraLATA routes where Verizon is not required to provide UNE DS1 and DS3 transport.[117]

Staff then asserts – based on the same self-reported data it used to calculate the HHIs – that MCI, AT&T, and/or SBC are the *only* carriers to provide transport on roughly 70 percent of those routes.[118] But an analysis of the fiber-based collocators in the wire centers that make up these 487 routes demonstrates the flaws in relying on that self-reported data set.[119] In fact, 82 percent of the 487 routes have at least one fiber-based collocator on each end of the route other than MCI; more than 55 percent of those routes have at least *three* fiber-based collocators on each end other than MCI. Moreover, there are only 72 routes (15 percent) where AT&T, SBC, or MCI are the only fiber-based collocators on each end of a route – a far cry from the 70 percent figure arrived at using Staff's incomplete data.[120] As the FCC determined, this fiber-based collocation enables carriers to transport traffic to and from that wire center, and demonstrates that competition is possible along those routes without the use of unbundled network elements.[121]

But even if the analysis were limited to routes where the *same* carrier has fiber-based collocation on both ends of the route – and therefore can use its own network to transport traffic

[117] Because Staff lumped the Tier 1 and Tier 2 wire centers together, it ignored that, on more than 200 of the routes, the FCC's rules continue to require Verizon to provide UNE DS1 transport.

[118] *See* White Paper at 36.

[119] The fiber-based collocation, moreover, understates the likely extent of alternative transport available. Many carriers that have deployed fiber networks do not collocate in Verizon's central offices.

[120] MCI is the only carrier with fiber-based collocation on both ends of only 8 routes, or just over 1.5 percent of the routes. And, the six wire centers that comprise these 8 routes have at least one fiber-based collocator other than MCI and an average of five fiber-based collocators other than MCI. Indeed, of the **[BEGIN CONFIDENTIAL]** **[END CONFIDENTIAL]** of the 487 routes where MCI has fiber-based collocation on both ends, 74 percent of the routes have 2 or more carriers other than MCI with fiber-based collocation on both ends.

[121] *See TRRO* ¶¶ 96-98.