

August 24, 2005

**Ex Parte**

Ms. Marlene H. Dortch  
Secretary  
Federal Communications Commission  
445 12th Street, S.W.  
Washington, DC 20554

**Re: Applications for Consent to Transfer of Control Filed by Verizon Communications Inc. and MCI, Inc., WC Docket No. 05-75**

Dear Ms. Dortch:

We are writing to respond briefly to the ex parte submission of Cox Communications and the accompanying paper by Dr. Gerald W. Brock, in which Cox raises the same “vertical” concerns that we have repeatedly addressed elsewhere.<sup>1/</sup> Cox’s analysis is based on a series of hypothetical and counterfactual assumptions that are unrelated to market realities. Further, the concerns it attempts to raise are not even merger-specific but pertain to issues facing the industry generally. As a result, Cox’s submission offers no basis to impose the “remedies” it seeks.

Much of Dr. Brock’s paper (at 1-8) is devoted to a general discussion of economic theory and then a series of hypothetical scenarios that are irrelevant to this transaction. Indeed, the fundamental premise of this discussion – that the transaction “[r]epresent[s] a major change in industry structure” because it collapses traditional market segments such as local and long distance (at 1-2) – misses the fact that these fundamental changes are already occurring wholly independent of this transaction. The growth of intermodal competition from cable companies like Cox itself, wireless companies, and providers of VoIP and other technologies, as well as market developments such as the offering of all-distance services, already are transforming the industry and will continue to do so regardless of this transaction.

When Dr. Brock finally turns to applying his theoretical points to the transaction at issue here, he makes a series of assumptions that are plainly counterfactual and raises issues that are not merger-specific. *First*, Dr. Brock’s discussion of the voice market segment (at 8-9) is premised entirely on a hypothetical abuse of terminating access charges charged to unaffiliated long distance carriers “[i]n the absence of regulation” of such charges. But, of course, terminating access charges *are* regulated, and various provisions of the Act guard against the type of abuse Dr. Brock posits. *See, e.g.*, 47 U.S.C. §§ 201, 202, 272(e)(3). In any case, Dr.

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<sup>1/</sup> *See* Letter from J. G. Harrington, Counsel for Cox Communications, Inc. to Marlene Dortch, Secretary, FCC, WC Docket No. 05-75 (July 28, 2005) (“*Cox Letter*”) & Gerald W. Brock, Vertical Integration with Network Effects (July 21, 2005) (“*Brock Paper*”).

Brock's hypothetical is not a new possibility that arises from the merger: Verizon itself is already "vertically integrated" in that it provides both terminating access and retail long distance services, and it has not engaged in the tactics that Dr. Brock hypothesizes. Particularly given the declining state of MCI's mass market business, *see, e.g.*, Public Interest Statement at 46-51, the merger would not alter the incentives or ability of Verizon to engage in the practices Dr. Brock conjures.

Indeed, as Dr. Brock concedes (at 9), his hypothetical depends on the percentage of voice customers the combined company would serve, and that percentage is *decreasing* as a result of increased intermodal competition and other factors unrelated to this transaction. For example, the most recent data confirms that cable companies are rapidly gaining voice telephony customers. Time Warner added over 240,000 net new customers in the second quarter of 2005, about sixty percent more than the number they added in the first quarter.<sup>2/</sup> Cablevision added more than 100,000 voice telephony customers in the second quarter of 2005 and now has approximately 478,000 customers.<sup>3/</sup> And Comcast remains on track to make cable telephony available to 15 million subscribers by year end and expects to add 1 million VoIP customers next year.<sup>4/</sup> Moreover, these same companies, including Cox itself, increasingly use their own network facilities to provide VoIP service. *See* Reply at 69.

*Second*, Dr. Brock's discussion of vertical integration in the context of the Internet (at 9-10) fares no better. As an initial matter, Dr. Brock concedes (at 10) that his hypothetical harms will not occur in the present market because a backbone operator such as MCI could not credibly threaten to cut off interconnection with other backbone operators since MCI's customers "need to reach web sites or customers served by other backbone providers." But, given that Verizon has a very small Internet backbone, the transaction will not significantly alter the status quo for backbone services. *See, e.g.*, Public Interest Statement at 61-65; Reply at 70-74. And it certainly will remain the case that the combined company's customers will demand the ability to reach users and content and application providers served by other backbone operators. Indeed, as we have explained in detail, because the combined company will carry less than 10% of North American Internet traffic, if it were to cut off all other backbone operators (or all other backbones other than SBC/AT&T), it would also be cutting off its own customers from the large majority of traffic and customers on the Internet, while competitors' customers would lose connectivity only to a small fraction of traffic. *See* Letter from Dee May, Verizon and Curtis Groves, MCI to Marlene Dortch, Secretary, FCC, WC Docket No. 05-75, at 3-5 (Aug. 8, 2005) ("*Applicants' Response to Earthlink*").

Dr. Brock's hypothetical "high quality Internet" example (at 10) is just a variant of the same argument made by Earthlink and others that we have already rebutted. He posits that

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<sup>2/</sup> Time Warner Inc., Presentation of Wayne Pace, CFO, *Time Warner Inc.: Second Quarter 2005 Results* (Aug. 3, 2005).

<sup>3/</sup> Cablevision Press Release, *Cablevision Systems Corp. Reports Second Quarter 2005 Results* (Aug. 9, 2005).

<sup>4/</sup> Thomson StreetEvents, *Q2 2005 Comcast Corporation Earnings Conference Call*, Conference Call Transcript at 5 (Aug. 2, 2005).

Verizon-MCI and SBC-AT&T could form a new high quality Internet to carry their VoIP and video conferencing services and only exchange such traffic with one another, but not any backbone operator using the general Internet.<sup>5/</sup> But such an action would effectively cut off Verizon-MCI's customers from the majority of other users whom they would expect to be able to reach through VoIP or video conferencing services. As a result, Verizon-MCI would lose its retail broadband customers to cable modem or other broadband access operators, and their wholesale customers to other backbone operators, which would allow them to reach far more other users with unimpeded interconnections. Furthermore, as Dr. Brock notes, other backbone operators could develop such a network as well so that customers would obtain a higher quality of service by switching from Verizon-MCI. Nor would such a competitive response require a "coordinated effort" among backbone providers as Dr. Brock claims (at 10). Particularly given that cable companies serve large numbers of broadband customers, if one or more of them began migrating to backbone operators with such a "high quality" network or otherwise demanding such quality, operators would have every reason to respond unilaterally by developing such networks in order to gain their business.

*Third*, Dr. Brock speculates (at 11) that, because the "regulatory treatment" of what he terms "hybrid services" is "in flux," they may be subject to "strategic manipulation" in the future. As he acknowledges, however, the regulatory policy issues are "unrelated to the proposed mergers." And the only concrete examples he gives – terminating access for VoIP and connections for 911 services – themselves do not give rise to merger-specific concerns since Verizon's incentives and ability to deny terminating access or 911 connection are unaffected by the transaction. In any case, as we have previously noted, the Commission already has demonstrated that it can move quickly in response to attempts to prevent the termination of VoIP calls.<sup>6/</sup>

Given that the concerns Dr. Brock raises are based on counterfactual assumptions and/or are not merger-specific, the remedies he suggests (at 12) are both unnecessary and unjustified. His suggestion that the Commission essentially rewrite the Act's interconnection provisions is both needless and in conflict with settled principles. For example, Section 252 already permits carriers to opt-in to existing interconnection agreements, and Dr. Brock offers no rationale for why a carrier operating in one state should be permitted to opt-in to an agreement that was negotiated or arbitrated in another state, particularly given that many terms of an interconnection agreement (e.g., UNE prices) are state-specific and unrelated to the interconnection concerns raised by Dr. Brock. Likewise, his assertion that Verizon and MCI should be required to keep in

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<sup>5/</sup> In this example, Dr. Brock appears to assume that Verizon/MCI would remain interconnected with other backbone operators to exchange all other Internet traffic, presumably because he recognizes that Verizon/MCI's customers otherwise would be cut off from myriad application and content providers. He does not explain, however, how the combined company could overcome the numerous practical and technical obstacles to filtering traffic in this manner so as to block the exchange of VoIP and video conferencing traffic. *See, e.g., Applicants' Response to Earthlink* at 10.

<sup>6/</sup> *See Order, Madison River Communications, LLC and affiliated companies*, File No. EB-05-IH-0110, DA 05-543 (rel. March 3, 2005) (consent order stopping telephone company from interfering with service of independent VoIP provider).

place for two years all existing agreements for backbone peering and for some undefined “provision of services” is both vague and unnecessary. As we have explained, the transaction will not alter the existing characteristics of the Internet backbone business, which is highly competitive and dynamic and promotes economically rational peering and transit agreements. *See, e.g.*, Reply at 69-81. Similarly, wholesale services – whether for long distance or for use by cable companies and others in their provision of VoIP – will remain highly competitive with numerous providers other than the combined company. *See* Reply at 65-69.

In sum, Cox’s submission offers no new argument or basis for imposing conditions on the transaction. Instead, it is based on hypothetical assumptions that are contrary to the market facts and raises concerns that are not merger-specific.

Please let us know if you require any additional information.

Sincerely,



Dee May  
Verizon



Curtis Groves  
MCI

cc: Julie Veach  
William Dever  
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