

the combined entity would have the ability to disadvantage competitors in Verizon's traditional service territory by raising special access rates, it would have no ability to affect special access rates in two-thirds of the country where Verizon is not the incumbent provider. Thus the competitive advantage to be gained from increasing special access rates is uncertain, particularly when (as discussed below) the combined entity has every reason to prefer lower special access rates out of region.

Finally, the enterprise customers who buy the services that use special access are extremely sophisticated and have demonstrated their ability to nurture independent special access suppliers in order to reduce prices. In the past, enterprise customers have supported competitive efforts to deploy alternatives to incumbent facilities to ensure network redundancy and to maintain long-term competitiveness of downstream markets. For example, in the 1980s, CAPs had substantial success attracting large enterprise customers that were eager to promote telecommunications competition. The first CAP – Teleport Communications Group (“TCG”) – was in fact a joint venture funded in large part by its customer Merrill Lynch.<sup>156</sup> Some customers include price protection clauses in their agreements that allow them periodically to renegotiate contract terms if prices fall in the marketplace, and employ benchmarking to ensure that they are receiving the most competitive prices. It is thus unrealistic to suggest that retail customers would accept foreclosure due to uneconomic increases in special access rates without turning to alternative suppliers.

2. Just as important, claims that the combined entity would manipulate special access rates to foreclose downstream competition ignore the fact that provisions of the Communications Act and existing FCC regulations are specifically designed to prevent

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<sup>156</sup> See R.G. Tomlinson, *Tele-Revolution: Telephone Competition at the Speed of Light* at 10 (Penobscot Press 2000).

incumbent providers from placing unaffiliated purchasers of special access at a disadvantage.<sup>157</sup>

At the most basic level, because Verizon must provide special access to all customers on a common carrier basis, regulations directly prohibit the combined entity from withholding capacity.

In addition, special access is subject to rate regulation that permits incumbent providers pricing flexibility only in those MSAs where competitive special access providers are firmly established. *See* Section II.E, *supra*. In areas where it does not have pricing flexibility, Verizon is subject to price cap regulations that establish annually declining caps on special access rates, calculated based on a formula designed to reflect expected increases in productivity.<sup>158</sup> As Verizon has explained in the FCC's Special Access proceeding, the FCC's deregulatory efforts have led to reduced prices, increased output, and growing competition. Special access rates pose no obstacle to competitive success in downstream retail markets – and, in any event, the FCC is actively re-examining the proper regulatory (or deregulatory) treatment of such services.

Furthermore, existing regulations directly prohibit discrimination by incumbent local exchange carriers in favor of affiliated providers – that is, the type of discrimination that could raise rivals' costs or lead to a "squeeze" on retail service rates.<sup>159</sup> In those areas where Verizon is a BOC, Section 272(e) requires it to provide special access to unaffiliated providers on terms and conditions that are at least as good as those made available to affiliated providers.

Furthermore, the BOC must impute to itself special access rates that are at least as high as those

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<sup>157</sup> *See Trinko*, 540 U.S. at 411 ("Antitrust analysis must always be attuned to the particular structure and circumstances of the industry at issue. Part of that attention to economic context is an awareness of the significance of regulation.").

<sup>158</sup> *See Special Access NPRM*, ¶¶ 9-15 (describing history of special access pricing regulation).

<sup>159</sup> *See Trinko*, 540 U.S. at 412 ("One factor of particular importance is the existence of a regulatory structure designed to deter and remedy anticompetitive harm.").

charged to unaffiliated providers.<sup>160</sup> Comparable regulatory requirements are in place in the FCC's regulations to govern non-BOC ILECs.<sup>161</sup> These requirements – along with the price regulation described above – prohibit Verizon from raising rivals' costs, relative to its own costs, and thus from executing any type of price squeeze.

To the extent that some opponents of this transaction point to the possibility of evasion of these regulatory requirements, they founder initially on the record to date: there is no evidence of any such regulatory avoidance by Verizon.

Indeed, Congress has already reached a judgment in the 1996 Act that concerns over vertical integration and discrimination against unaffiliated providers did not justify either the exclusion of BOCs from interLATA service markets or the imposition of intrusive regulatory safeguards. Thus, after a relatively brief period of structural separation, BOCs are permitted to provide interLATA services subject only to non-structural and accounting safeguards comparable to those that apply to the provision of any unregulated service. The 1996 Act thus reflects a legislative judgment that these regulatory mechanisms are sufficient to guard against anticompetitive leveraging of BOCs' local market position. MCI can claim only a relatively small share of retail enterprise spending – on the order of 15 percent. The combined entity will have less than 25 percent. No one would argue that if Verizon had won a comparable percentage of enterprise spending through internal growth that the FCC would change the regulatory structure governing special access. There is accordingly no reason to believe that existing regulation is insufficient to address any competitive issue related to vertical integration.

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<sup>160</sup> In practice, Verizon frequently charges itself *more* for special access than it charges the largest unaffiliated providers, because the volume of Verizon's requirements is smaller.

<sup>161</sup> See 47 C.F.R. § 64.1903.

**B. The Transaction Would Not Enhance the Combined Entity's *Incentives To Attempt To Foreclose Retail Competition***

The claim that the combined entity would attempt to exclude competitors from providing downstream retail enterprise services necessarily depends on the claim that the combined entity would be willing to sacrifice profits from the sale of special access in the hope of reaping greater profits in the downstream retail market as a result of the exclusion. Such a sacrifice would make no business sense for several reasons.

As an initial matter, the relevant question again is whether the combination with MCI will significantly alter the combined entity's incentives. Verizon has had regulatory permission to provide interLATA services in former GTE territories since 1996 and in former Bell Atlantic states beginning as early as 1999. Yet there is no evidence that Verizon has found it profitable to increase retail enterprise sales by raising special access rates (despite the loss of special access revenues). To the contrary, retail enterprise competition has intensified, and Verizon's impact in the retail enterprise market has been limited. If Verizon's goal were to foreclose retail competitors by raising special access rates, it would have had no reason to acquire MCI, which does not meaningfully enhance Verizon's ability to execute such a strategy.

Indeed, while the transaction will give the combined entity a broader range of communications service capabilities, vertical integration for the combined company will remain minor in comparison both to Verizon's *sales* of special access to unaffiliated retail providers and MCI's purchases from unaffiliated wholesale providers. Although MCI is Verizon's second largest single customer for special access, special access revenues from MCI account for a small percentage – approximately [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] percent – of Verizon's overall wholesale special access revenues. Thus the combined entity will not face fundamentally different incentives in this regard than Verizon as it exists today: unaffiliated

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purchases will still account for a significant majority – better than [BEGIN  
CONFIDENTIAL] [END CONFIDENTIAL] percent – of Verizon's special access sales.  
The combined entity stands to lose substantial revenues and profits by sacrificing special access  
sales to unaffiliated retail providers.

Furthermore, if the combined entity were to attempt to foreclose downstream  
competitors, it would risk retaliation. No service provider can fulfill the needs of large enterprise  
customers entirely over its own facilities. No telecommunications carrier in the United States,  
including Verizon and MCI, has ubiquitous high-capacity telecommunications facilities that are  
capable of serving all the needs of commercial and institutional customers. As a result, all retail  
service providers must depend, to a greater or lesser degree, on multiple facilities-based carriers  
to create a network that can serve all of the needs of commercial and institutional customers.  
Although the combined entity will benefit from an increased degree of vertical integration, like  
its competitors, it will have to purchase special access from third parties to serve the needs of  
large enterprise customers. Reflecting this, MCI estimates that of [BEGIN  
CONFIDENTIAL] [END CONFIDENTIAL] in spending on special access in  
2004, approximately [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] (28  
percent) was spent with Verizon. The combined entity thus has a strong incentive to ensure that  
special access rates remain competitive nationwide.

In all events, the claim that the combined entity could harm competition in retail  
enterprise services ignores the robustness of existing competition. Verizon and MCI compete  
today with numerous other companies to serve large enterprise and other commercial and  
institutional customers of all shapes and sizes. Market participants include traditional  
interexchange carriers, such as AT&T, Sprint, and Qwest, newer network operators such as

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Global Crossing, Level 3, and Wiltel, competitive local exchange carriers, such as XO and Time Warner Telecom, network integrators and managed service providers, such as EDS, IBM, Accenture, and Lockheed, international carriers such as British Telecom, France Telecom/Equant, and Deutsche Telekom, and equipment manufacturers and value-added resellers, such as Lucent and Nortel. *See* Section IV, *supra*. Such competitors will not willingly cede the field to any competitor, and they have the resources to weather any temporary increases in special access pricing while investing in independent capacity.

In sum, raising prices for special access will not confer any long-term advantage on the combined entity and will simply reduce special access revenues in the short and long term – and potentially assist competitors to achieve greater efficiencies of scale and scope.

**IV. THE COMBINATION OF VERIZON'S AND MCI'S RETAIL BUSINESS UNITS WILL NOT SUBSTANTIALLY LESSEN COMPETITION FOR RETAIL SERVICES THAT USE SPECIAL ACCESS AS AN INPUT**

As demonstrated in Sections I.A.2 & I.B.2 above, both Verizon and MCI provide to business customers a wide range of retail services that rely on special access as an input. Although Verizon and MCI do occasionally compete head-to-head, their retail businesses are largely complementary; the two companies compete for the same retail opportunities to only a limited extent. In any event, the competition for retail services that use special access is intense, with multiple providers that will remain following the transaction, including many with significant scale. Moreover, following the transaction Verizon would not be able to increase prices for retail services that rely on special access because the areas of MCI fiber overlap represent only a small fraction of the locations where retail customers typically demand service. Thus, the combination of Verizon's and MCI's retail business units will not substantially lessen competition for retail services that rely on special access as an input.

**A. There Is Limited Overlap Between Verizon's and MCI's Provision of Retail Services that Use Special Access**

To the extent that both Verizon and MCI provide retail services that rely on special access, they largely compete for different retail opportunities. As a result, the transaction will not result in significant concentration for any of the customer segments or retail services that are provided using special access.

First, with respect to the large business customers that account for the bulk of special access revenues earned from retail customers, Verizon and MCI rarely compete for the same business opportunities from these customers. Whereas large enterprise customers form the core of MCI's retail business, Verizon is a minor player with respect to such customers. Large enterprise customers account for more than [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] percent of MCI's revenue from serving all commercial and institutional customers. By contrast, and as discussed below, Verizon is just one of many firms with a single-digit share in the large enterprise customer segment. Indeed, Verizon is rarely, if ever, a competing prime bidder against MCI on large enterprise contracts. Based on an analysis of hundreds of bids by Verizon and MCI between October 1, 2004 and May 1, 2005, the two companies competed for the same bid in a very small minority of cases.<sup>162</sup> Specifically, in the 539 instances in which Verizon submitted a bid in response to an RFP during that period, MCI also submitted a bid in only 31 instances. And this may overstate the degree of retail competition between the two companies, because Verizon and MCI have not been able to determine how many times the two companies were actually competing against each other to provide the same services in response to the same RFP.

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<sup>162</sup> See Verizon Response to FCC Specification 4 & Exhibit 4.1; Ex Parte Letter from Dee May, Verizon, to Marlene Dortch, FCC, WC Docket No. 05-75 (July 8, 2005), Attachment at 3-6 & Supplemental Exhibit 4.1.

According to other independent analyst studies and Verizon's own internal market-share analysis, Verizon and MCI's combined share of large enterprise and mid-sized business revenues will be no more than 16-22 percent following the transaction.<sup>163</sup> Lehman Brothers has estimated carrier shares of local and long-distance voice and data revenues provided to what it terms "enterprise" customers, which it defines as a \$152 billion market segment that includes large enterprise customers, wholesale services, and small and medium enterprises.<sup>164</sup> Lehman estimates that, for 2005, AT&T's share will be 15.5 percent; SBC's 13.1 percent, MCI's 11.8 percent, Verizon's 10.1 percent, Sprint's 5.9 percent; Qwest's 5.7 percent; BellSouth's 5.5 percent; Level 3's 1.2 percent; XO's 0.9 percent; and the rest of the industry, including systems integrators and CLECs, 30.4 percent.<sup>165</sup>

Verizon also compiles internal data that are consistent with these estimates. Verizon's data include revenues for the full range of services that large enterprise and other commercial and institutional customers purchase – voice, data, CPE, and integration services – with the exception of wireless services.<sup>166</sup> These data show that, as of the end of 2004, [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] is the largest single provider serving these customers, with a [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] percent

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<sup>163</sup> A *New York Times* survey estimated shares of a "corporate telecommunications market" that places Verizon's and MCI's respective shares at 15 and 12 percent, respectively. M. Richtel, *Valuing MCI in an Industry Awash in Questions*, N.Y. Times at C1 (Feb. 9, 2005). This survey appears to take a more restrictive view of the relevant market than those discussed below.

<sup>164</sup> See R. Dale Lynch & Blake Bath, Lehman Brothers, *Enterprise Telecom Services; A Comeback Begins* at 3 (Nov. 11, 2003) ("*Enterprise Telecom Services*") (attached as Exhibit 1 to Declaration of Eric J. Bruno and Shelley Murphy ("Bruno/Murphy Decl."), attached to Public Interest Statement, WC Docket No. 05-75 (FCC filed Mar. 11, 2005)).

<sup>165</sup> See *Enterprise Telecom Services* at 15, Fig. 12; see also Declaration of Robert W. Crandall & Hal J. Singer ¶ 36, attached to Public Interest Statement, WC Docket No. 05-75 (FCC filed Mar. 11, 2005).

<sup>166</sup> See Declaration of Jeffrey E. Taylor ¶¶ 4-6, attached to Public Interest Statement, WC Docket No. 05-75 (FCC filed Mar. 11, 2005).

share of the revenues.<sup>167</sup> No other single provider is in double digits. [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] is the next largest provider, at [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] percent.<sup>168</sup> [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] each has [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] percent, while [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] have [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] percent each.<sup>169</sup> Other CLECs, equipment providers, and systems integrators and IP applications providers have the remaining 49 percent.<sup>170</sup>

While some merger opponents have disputed these data on the grounds that Verizon's share of enterprise revenues within its region is significantly higher than its nationwide share, the Department of Justice ("DOJ") has previously concluded that the appropriate geographic markets for many of the major retail services that use special access as an input – including interLATA private line, ATM, Frame Relay, interLATA data services, and Custom Network Services – are national in scope.<sup>171</sup> The DOJ focused on the fact that these services tend to be purchased by "high-end" customers that have "extensive and complex telecommunications needs for both internal and external voice and data communications" as well as needs for the "provision and maintenance of diverse customer premises equipment."<sup>172</sup> The DOJ also recognized that these

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<sup>167</sup> See id. ¶ 9.

<sup>168</sup> See id.

<sup>169</sup> See id. ¶ 9 & Exhibit 2.

<sup>170</sup> See id. ¶ 9 & Exhibit 2.

<sup>171</sup> Complaint ¶¶ 124, 143, *United States v. WorldCom, Inc. and Sprint Corp.*, No. 1:00-cv-01526-RMU (D.D.C. filed June 27, 2000) ("WorldCom/Sprint Complaint"). The FCC has made similar findings. *Application of WorldCom, Inc. and MCI Communications Corporation for Transfer of Control of MCI Communications Corporation to WorldCom, Inc.*, Memorandum Opinion and Order, 13 FCC Rcd 18025, ¶ 30 (1998); *Applications of NYNEX Corp. and Bell Atlantic Corp. for Consent To Transfer Control of NYNEX Corp. and Its Subsidiaries*, Memorandum Opinion and Order, 12 FCC Rcd 19985, ¶ 54 (1997).

<sup>172</sup> WorldCom/Sprint Complaint ¶ 148.

large business customers “typically purchase a substantial majority of their telecommunications services” from a single provider that customizes those services to meet their needs.<sup>173</sup>

Significantly, however, the DOJ did not identify the ownership or operation of local fiber or other special access facilities as an element that was relevant in defining either the scope of competition or the viability of entry.

Second, Verizon and MCI largely concentrate on providing different types of retail services to business customers. Verizon’s core strengths lie in provision of consumer voice and broadband services, wireless services, and local connectivity, equipment, and professional services to local or regional business customers. MCI, by contrast, is a leading primary provider of large enterprise services with a national and global reach.

**B. Following the Transaction There Will Be Many Other Competitors for Retail Services that Use Special Access as an Input**

To the extent that Verizon and MCI do compete head-to-head in the provision of retail services that rely on special access, there are many other competitors that provide these services as well.<sup>174</sup> Even some of the competing carriers opposing this transaction have conceded that “CLECs, interexchange carriers (IXCs), and data companies compete to provide services to business customers;” that these various competitors “offer differentiated products;” and that their prices “accurately reveal buyers’ valuations and sellers’ costs.”<sup>175</sup> The transaction will not significantly reduce the number of these firms or give Verizon a dominant market position.

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<sup>173</sup> WorldCom/Sprint Complaint ¶ 149.

<sup>174</sup> Declaration of Simon Wilkie ¶ 10 (“Wilkie Decl.”), *attached to Petition To Deny of Cbeyond Communications, Conversent Communications, Eschelon Telecom, TDS Metrocom, NuVox Communications, and XO Communications*, WC Docket No. 05-75 (FCC filed May 9, 2005); Simon Wilkie, *Proposed Mergers of SBC/AT&T and VZ/MCI: Preliminary Analysis of Competitive Effects* at 24-25 (June 15, 2005), *attached to Ex Parte Letter from Brad Mutschelknaus, Kelley Drye & Warren, to Marlene Dortch, FCC, WC Docket Nos. 05-65 & 05-75* (June 15, 2005) (“Wilkie June 14 Pres.”).

<sup>175</sup> Wilkie May 9 Decl. ¶ 10; Wilkie June 14 Pres. at 24-25.

## 1. *Market Participants*

A wide variety of competing carriers currently provide retail services that use special access as an input. Such competitors include traditional interexchange carriers, such as AT&T, Sprint, and Qwest, newer network operators such as Global Crossing, Level 3, and Wiltel, competitive local exchange carriers, such as XO and Time Warner Telecom, network integrators and managed service providers, such as EDS, IBM, Accenture, and Lockheed, international carriers, such as BT and France Telecom/Equant, and equipment manufacturers and value-added resellers, such as Lucent and Nortel.<sup>176</sup>

As this list makes clear, it is possible to compete in the provision of retail services that use special access as input without actually owning special access facilities themselves. Because such services are most often sold in combination with other retail services, special access facilities themselves are just one of the factors that determine the competitive availability of these retail services. Other competitive facilities – voice and data switches, long-haul fiber backbones, and various types of customer premises equipment – must be used to provide these services as well. Furthermore, given that no one provider has ubiquitous network facilities, customers typically must be served by aggregating the facilities of multiple providers, which can be accomplished by companies that do not own any traditional telecom facilities at all.<sup>177</sup> The competitive success of network integrators, who combine the facilities of other providers into unified networks, reflects that demand. MCI itself serves the vast majority of its retail customers using third-party facilities rather than its own. Nationwide, MCI provides such services to

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<sup>176</sup> See Public Interest Statement at 24-30, WC Docket No. 05-75 (FCC filed Mar. 11, 2005); Bruno/Murphy Decl. ¶¶ 14-30; Declaration of Ronald J. McMurtrie ¶¶ 8-20 (“McMurtrie Decl.”), attached to Public Interest Statement, WC Docket No. 05-75 (FCC filed Mar. 11, 2005); see also Bruno et al. Reply Decl. ¶¶ 9-13, 33-35.

<sup>177</sup> See Bruno/Murphy Decl. ¶ 15; Lew/Lataille Decl. ¶¶ 8-10; McMurtrie Decl. ¶ 27.

approximately [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] locations  
whereas MCI has only [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] fiber-lit  
buildings.

Interexchange Carriers. IXCs have historically provided both voice and data services for commercial and institutional customers and have showed particular strength as the primary providers for large enterprise customers. Among these carriers, AT&T has emerged as the largest competitor.<sup>178</sup> AT&T boasts that it has an “unrivaled base of enterprise customers” and that “100% of S&P 500 are AT&T customers.”<sup>179</sup> Ninety-five percent of Fortune 1000 companies rely on Sprint for combinations of voice, data, Internet, and wireless services.<sup>180</sup> Level 3 offers a comprehensive range of communications services designed to meet the needs of the top global bandwidth customers, including large enterprise customers.<sup>181</sup> Global Crossing offers a full range of managed data and voice products to more than 40 percent of the Fortune 500 companies.<sup>182</sup> Broadwing owns an advanced fiber-optic network connecting over 100 cities

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<sup>178</sup> See J. Bazinet, *et al.*, J.P. Morgan, *AT&T: Fundamental Pressures Too Hard to Overcome* at 3 (Nov. 7, 2003) (AT&T’s “brand and client roster are unmatched, and its network, sales force, global presence and product breadth give the company a meaningful advantage over competitors.”); J. Halpern, Bernstein Research Call, *U.S. Telecom: Superior Growth Prospects Make Enterprise Market a Key Battleground for U.S. Service Providers* at 2 (Jan. 6, 2005) (“AT&T is currently the leader in the enterprise market, not only in market share but in mind-share as well.”); S. Flannery, *et al.*, Morgan Stanley, *Strong Showing for Bells in Annual Corporate Survey* at 6 (June 22, 2004) (“AT&T is the leader in being: (1) the highest-quality telecom provider, (2) the best integrated voice and data provider, and having (3) the best customer support. The surveyed CTOs also chose AT&T as having the most visible sales force.”).

<sup>179</sup> AT&T News Release, *AT&T Response Statement – DJIA* (Apr. 1, 2004); Bill Hannigan, President, AT&T, *AT&T Business Overview: The Networked Enterprise*, presentation at the AT&T Analyst Day, at 14 (Feb. 25, 2004).

<sup>180</sup> Sprint, *The PGA of America*, <http://www.sprint.com/business/products/whySprint/cs-PGA.jsp>.

<sup>181</sup> Level 3 Communications, *Services*, <http://www.level3.com/3383.html>; Level 3 Communications Corp., Form 10-K (SEC filed Mar. 15, 2004). These service offerings include: Softswitch based services including managed modem for the dial-up access business, business-oriented VoIP services, IP and data services and broadband transport services such as wavelengths, dark fiber, private line services including transoceanic, backhaul, intercity, metro and unprotected private line services, field technical services and collocation services.

<sup>182</sup> Global Crossing Press Release, *Global Crossing Brings Converged IP Solutions to Financial Services Customers* (July 1, 2004).

in the United States.<sup>183</sup> Savvis Communications was recently ranked as the #2 provider in the provision of IP-VPNs, trailing only AT&T.<sup>184</sup>

Systems Integrators. In recent years there has been a dramatic increase in competition from systems integrators – such as Electronic Data Systems Corp., IBM Global Services, Accenture, Cap Gemini Ernst & Young, Northrup Grumman, General Dynamics, and Computer Sciences Corp. With the increasing complexity and utilization of IT and communications systems, large businesses are increasingly turning to network integrators to assess, plan, and manage their telecommunications systems. The need for network integrators is heightened by the need for extensive planning and management needed to create converged systems without having to create new physical networks from scratch. Network integrators thus provide managed services to large business customers, such as network design and operation.

Systems integrators have shown that they can compete successfully against traditional telecommunications providers. One Yankee Group study showed that 10 percent of surveyed businesses reported that a system integrator was its primary communications service provider in 2004.<sup>185</sup> Likewise, in the government sphere, systems integrators have emerged as leading competitors, with General Dynamics and CSC trailing only AT&T and MCI as prime contractors.<sup>186</sup> Integrators have recently won many major contracts. For example, in October 2004, Lockheed Martin teamed up with AT&T, Hewlett-Packard Co., Hughes Network Systems Inc., and large local exchange carriers to become the comprehensive provider of managed

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<sup>183</sup> Corvis Corp., Form 10-K (SEC filed Mar. 15, 2004).

<sup>184</sup> See WAM!NET Press Release, *IDC and In-Stat/MDR Rank Savvis as Second Largest Hosting Services and IP VPN Services Provider, Respectively* (July 27, 2004). Savvis uses its network to offer a comprehensive array of data and voice communications services, including voice, Internet access and data networking, to multi-location large enterprise customers.

<sup>185</sup> S. Hackett, The Yankee Group, *The State of the Enterprise* at 28 (Nov. 30, 2004).

<sup>186</sup> Federal Sources, Inc., <http://www.fedsources.com/index.asp>.

network services to over 37,000 U.S. Postal Service locations. The \$3 billion contract was awarded principally to Lockheed Martin.<sup>187</sup> Harris Corp. won a \$1.7 billion contract for the nationwide FAA network;<sup>188</sup> EDS and Lockheed Martin won HUD contracts worth \$400 million each;<sup>189</sup> EDS won the Navy's \$8.8 billion NMCI networking contract;<sup>190</sup> General Dynamics won the contract for Pentagon renovation;<sup>191</sup> CSC won the \$2 billion WIN-T contract in connection with the Army's Warfighter Information Network project;<sup>192</sup> and Northrop Grumman won the Air Force's \$9 billion NetCENTS contract.<sup>193</sup> IBM Global Services won a recent contract with Lloyd's TSB bank to provide that company with converged voice and data systems, including 70,000 VoIP telephones.<sup>194</sup>

The central role that systems integrators now play in the provision of retail services that use special access is further evidenced by the partnerships that Verizon has formed with these entities. Verizon has decided to partner with a number of integrators so that it will be able to remain a partial supplier to end-user customers who decide to use an integrator as their primary telecommunications supplier. In addition, these partnerships also help Verizon become the

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<sup>187</sup> J. Miller, *USPS Taps Lockheed Martin for \$3 Billion Telecom Contract*, Gov't Computer News (Oct. 14, 2004), [http://www.gcn.com/vol11\\_no1/outourcing/27505-1.html](http://www.gcn.com/vol11_no1/outourcing/27505-1.html).

<sup>188</sup> Harris Corp., *2002 Annual Report*, <http://www.harris.com/harris/ar/archived-annualreports.html>.

<sup>189</sup> U.S. Department of Housing and Urban Development, *HUD Awards Information Technology Contracts Totaling \$800 Million to Electronic Data Systems and Lockheed Martin Corporation*, <http://www.hud.gov/offices/cpo/primes/hits.cfm>.

<sup>190</sup> J. Perez, *EDS CEO: Navy Contract Under Control*, InfoWorld (Feb. 18, 2004).

<sup>191</sup> F. Tiboni, *General Dynamics wins Pentagon Contract*, Federal Computer Week (Aug. 13, 2004).

<sup>192</sup> CSC News Release, *CSC Wins \$500 Million Forscom Aviation Support Contract* (Aug. 24, 2004) ("The aggregate ceiling value for all four contracts is \$2 billion.").

<sup>193</sup> W.D. Gardner, *USAF To Dole Out \$9 Billion On Beefed Up Network*, Networking Pipeline (Sept. 14, 2004).

<sup>194</sup> IBM Release, *At £500m IBM Voice and Data Services Deal To Enable Lloyds TSB's Next Generation Business Solutions* (Dec. 6, 2004).

primary vendor in a few cases, by giving Verizon the missing piece in its own service portfolio.

Since 2003, Verizon has formed partnerships with IBM, EDS, EMC, CMC, and BT.

Competitive Local Exchange Carriers. CLECs are significant providers of retail services that use special access services, particularly to medium-sized business customers. XO provides an extensive array of voice, data, Internet access, security solutions, and integrated and managed services to Fortune 500 companies.<sup>195</sup> US LEC Corp. is a super-regional telecommunications carrier providing integrated voice, data and Internet services to medium and large businesses and enterprise organizations throughout 15 Eastern states and the District of Columbia.<sup>196</sup> PAETEC Communications, Inc., a national communications solutions provider specializing in IP-based services, has installed over 675,000 access line equivalents on its network as of September 30, 2004.<sup>197</sup> Other CLECs operating in Verizon's region include 360networks,<sup>198</sup> Electric Lightwave,<sup>199</sup> Con Edison Telecom,<sup>200</sup> Covad,<sup>201</sup> ITC^DeltaCom,<sup>202</sup> Telephone & Data Systems,<sup>203</sup> and Broadwing.<sup>204</sup>

International Carriers. The provision of international telecommunications is also increasingly important service for large enterprise customers, as more of them expand overseas. Because of the growth in multinational operations, foreign telecommunications carriers are

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<sup>195</sup> XO Communications, *XO Products and Programs*, <http://www.xo.com/products/>.

<sup>196</sup> US LEC News Release, *US LEC Expands in Virginia* (Jan. 20, 2005).

<sup>197</sup> PAETEC News Release, *PAETEC Exceeds 675,000 Access Lines* (Oct. 14, 2004).

<sup>198</sup> 360networks, *About Us*, [http://www.360.net/About\\_Us/](http://www.360.net/About_Us/).

<sup>199</sup> Electric Lightwave, *About Us*, <http://www.electricleightwave.com/about.html>.

<sup>200</sup> Con Edison Communications, *Business Services*, <http://www.conedcom.com/businessservices.cfm/>.

<sup>201</sup> Covad, *Covad Corporate Brochure*, <http://www.covad.com/companyinfo/docs/CovadCorpBrochure.pdf>.

<sup>202</sup> ITC^DeltaCom, *Company Information*, [http://www.itcdeltacom.com/Company\\_info.asp](http://www.itcdeltacom.com/Company_info.asp).

<sup>203</sup> Telephone & Data Systems, *About TDS Telecom*, <http://www.teldta.com/tds-tele/index.html>.

<sup>204</sup> Broadwing, *Optical Network Story*, <http://www.broadwing.com/about-b6.html>; Broadwing, *Maps*, <http://www.broadwing.com/about-b4.html>.

increasingly becoming significant competitors for the business of large enterprises, including those based in the United States. France Telecom/Equant serves over 3,700 large business customers, including two-thirds of the top 100 companies in Business Week's "Global 1000" list for 2003.<sup>205</sup> British Telecom's global network, bolstered by, among other things, its recent acquisitions of InfoNet and Radianz (the former Reuters financial data network) operates in over 200 countries across five continents, and it owns POPs in 20 major U.S. metropolitan areas.<sup>206</sup> In January 2005, BT announced that Bristol-Myers-Squibb had awarded BT a multi-year contract estimated at approximately €500 million to provide managed services and to migrate Bristol-Myers's world-wide LAN and WAN infrastructure to a new IP-based global MPLS infrastructure.<sup>207</sup> British Telecom and Reuters just announced that "BT will become Reuters supplier of network services in a contract under which Reuters is expected to spend in the region of \$3 billion over eight and a half years."<sup>208</sup> Deutsche Telekom, Europe's largest telecommunications company, is also a major competitor in the United States through its T-Systems and T-Mobile subsidiaries. Last year, T-Systems entered into a partnership with Level 3 Communications to provide T-System's MPLS-based service to customers across Level 3's entire network.<sup>209</sup> Other foreign carriers competing in the U.S. include COLT, KPN, NTT, and SingTel.

*Equipment Vendors.* Because all communications services depend in part on customer premises equipment, one trend for enterprise customers is the development of increasingly

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<sup>205</sup> Equant, *About Equant*, [http://www.equant.com/content/xml/who\\_we\\_are.xml](http://www.equant.com/content/xml/who_we_are.xml).

<sup>206</sup> British Telecom, *Our Network*, [http://www.btglobalservices.com/business/global/en/about\\_us/around\\_the\\_world/americas.html](http://www.btglobalservices.com/business/global/en/about_us/around_the_world/americas.html).

<sup>207</sup> See *Look Out Bells, Here Come the Brits*, Red Herring (Feb. 7, 2005), <http://redherring.com/Article.aspx?a=11231&hed=Look+out+Bells%2C+here+come+the+Brits#>.

<sup>208</sup> BT Group Press Release, *BT and Reuters Sign Major Contract* (Mar. 10, 2005).

<sup>209</sup> T-Systems Press Release, *T-Systems Expands Reach of MPLS-Based Network* (Mar. 4, 2004).

sophisticated on-site communications capability to replace services that were previously provided through the network.<sup>210</sup> In part for this reason, a variety of equipment manufacturers are also competing for large business customers. Siemens offers a variety of converged communications solutions, including real-time IP systems, security systems, customer interaction solutions, and voice, data, and messaging systems, for enterprise customers.<sup>211</sup> Lucent provides a host of telecommunications services for business customers, including, among other things, its IP Centrex product, which is a fully managed service that combines the functionality of Centrex with the benefits of VOIP.<sup>212</sup> Lucent also provides managed data services including ATM, Frame Relay, and Ethernet-over-Sonet to business customers.

Cable Operators. The nation's major cable operators are now actively pursuing commercial and institutional customers. Cable operators originally focused on small businesses, but they have broadened their reach to offer individualized services to medium-sized businesses and even to large enterprise customers. Cable operators are providing high-capacity services to business customers both by deploying fiber to office buildings, and by extending their hybrid fiber-coax networks to business districts in order to provide cable modem services to business customers.<sup>213</sup> Time Warner Communications is "delivering cost effective, high capacity access solutions to several Fortune 500 customers," and in the past year has "enjoyed a \$60 million gain

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<sup>210</sup> See T. Valovic, *et al.*, IDC Research, *U.S. Hosted IP Voice Forecast and Analysis, 2002-2007* at 1, 19 (Feb. 2003).

<sup>211</sup> Siemens Enterprise Networks, *Products, Solutions & Services*, <http://enterprise.usa.siemens.com/products.html>.

<sup>212</sup> Lucent Technologies, *IP Centrex Service for Enterprises*, [http://www.lucent.com/solutions/ip\\_centrex.html](http://www.lucent.com/solutions/ip_centrex.html).

<sup>213</sup> See *UNE Fact Report 2004* at III-36 to III-38 & Table 19, WC Docket No. 04-313 & CC Docket No. 01-338 (FCC filed Oct. 4, 2004) ("*2004 Fact Report*").

in business sector revenue . . . boosting their overall commercial take by 70%.”<sup>214</sup> Time Warner Cable has signed on companies such as L.L. Bean and Fairchild Semiconductor International (FCS).<sup>215</sup> Cox Communications has “launched . . . a new integrated marketing campaign to inform and drive demand among Enterprise and Fortune 500 companies;” the company generated \$287 million in commercial sales in 2003, and has launched a new marketing effort to “boost commercial revenue by more than 20% this year, a jump of more than \$50 million.”<sup>216</sup> In 2004, Cox announced that it had signed contracts to provide telecommunications services to business customers including MGM Mirage (MGG) resorts and Chesapeake Energy Corp. (CHK).<sup>217</sup> Cablevision Systems Corp. “has been in the business services market longer than most,” and boasts “4,800 business customers concentrated in the health-care, financial services and government sectors.”<sup>218</sup> The company recently announced that “[d]uring the fourth quarter, we continued our roll-out of Metro Ethernet and optimal transport services to corporations, financial firms and educational institutions. Looking ahead to 2005, we expect commercial data sales will continue to drive revenue growth and Metro Ethernet, our all IP service, will be a key

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<sup>214</sup> Time Warner Cable Commercial Services, *Road Runner Business Class*, <http://www.twcbroadband.com/solutions/rrbc.cfm>; A. Breznick, *Cable Operators Show They Really Mean Business*, Cable Datacom News (Sept. 2004), <http://cabledatacomnews.com/sep04/sep04-2.html>.

<sup>215</sup> E. Sheng, *Cable-Baby Bell Competition Heats Up in Business Services*, Dow Jones News Service (Mar. 31, 2004), available at <http://www.optimumlightpath.com/Interior33-4.html>.

<sup>216</sup> Cox Business Services Press Release, *Enterprise Presents Even “Bigger” Opportunity for Cox Business Services in 2004* (Mar. 29, 2004); A. Breznick, *Cable Operators Show They Really Mean Business*, Cable Datacom News (Sept. 2004), <http://cabledatacomnews.com/sep04/sep04-2.html>.

<sup>217</sup> E. Sheng, *Cable-Baby Bell Competition Heats Up in Business Services*, Dow Jones News Service (Mar. 31, 2004), available at <http://www.optimumlightpath.com/Interior33-4.html>.

<sup>218</sup> *Id.*

focus for Lightpath's service offering."<sup>219</sup> Charter Cable is also moving "'up-market' to compete in Enterprise RFP environment."<sup>220</sup>

## 2. *Evidence of the Success of Competitive Providers*

As described above, competing providers other than Verizon and MCI already account for a significant share of revenues for the various retail services that use special access. This is corroborated by multiple additional sources of evidence.

First, competing carriers are winning large numbers of major contracts for services that use special access. Attachment 6 to this paper is an index of the recent contracts these competitive providers have won. When a competing carrier wins a major contract, it sometimes reports that information by issuing a press release. The index was compiled by canvassing the press releases of 148 competing providers that claim to serve enterprise customers, and by searching for similar reports in the trade press. Unfortunately, only 57 of those providers actually issue press releases reporting their successes; we were able to find information about an additional 12 providers in the trade press. Many of these carriers appear to report only a small subset of their contract wins, however. The index nonetheless identifies *over 1,200* contracts won by competing carriers since the beginning of 2003 alone.

With respect to the over 1,200 contracts identified in the index, competing carriers reported the value of the contracts only about a quarter of the time (293 contracts in total). The total value of these 293 contracts is more than *\$66 billion*. This includes eleven contracts valued at over \$1 billion, nine contracts valued at between \$500 million and \$1 billion, and 35 contracts valued at between \$100 million and \$500 million. In addition to those contracts with a specified

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<sup>219</sup> Cablevision Systems Corp., 4Q 2004 Earnings Conference Call (Feb. 23, 2005).

<sup>220</sup> D. Chang, EVP, Finance & Strategy, Charter Communications, presentation before the JP Morgan High Yield Conference, at 23 (Feb. 2, 2004).

value, 96 contracts were described as multi-million dollar contracts, and one was described as a multi-billion dollar contract. These 97 contracts are not part of the \$66 billion.

The contracts include the provision of services to both carrier and non-carrier customers. Of the over 1,200 contracts identified, 1051 appear to be for non-carrier customers (representing nearly \$65 billion), while 153 were for carrier customers (representing nearly \$1.5 billion). Competing carriers reported the length of the contract for only 42 percent of the 1,200 contracts (503 in total). These contracts range in duration from six months to 20 years. Of those for which duration was reported, the bulk – approximately 68 percent – had three- to five-year terms. For the most part, the contracts involve large enterprise or government contracts; competing carriers generally did not report contracts signed with small and medium business customers.

While this index represents only a small portion of total contract wins, it nonetheless proves that there are a wide variety of retail competitors in the marketplace that are successfully competing in the provision of retail services that use special access. As noted above, we have been able to identify 57 competing carriers that report such wins. In addition, the total volume of these contracts – \$66 billion – is enormous and indicates that competing carriers are succeeding in winning the business of the very largest and most demanding customers.

Second, research on customers that have moved from Verizon provides additional confirmation of these results. With respect to private line services, an analysis of three years of data shows that a wide variety of competing carriers are winning retail customers in Verizon's territory, and that MCI is winning only a small percentage of the time. Customers report switching to a total of 30 suppliers, including IXCs and CLECs such as [BEGIN

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CONFIDENTIAL]; cable companies such as [BEGIN CONFIDENTIAL]

[END CONFIDENTIAL]; utilities such as [BEGIN CONFIDENTIAL]

[END CONFIDENTIAL]; and others. Of the instances in which customers reported their preference to switch to a competitive provider, MCI was listed as one of the customer's choices in only [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] out of [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] total instances – only [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] percent of the time.

The results are similar for local voice and data services. Customers report switching to IXCs such as AT&T, Sprint, and Qwest; CLECs such as PAETEC, Focal, XO, and ATX; cable companies such as Cablevision Lightpath, Adelphia, Time and Warner, Cox, and Comcast; foreign competitors such as France Telecom/Equant; equipment suppliers such as Cisco, Siemens, Avaya, Lucent, and Nortel; ILECs such as SBC; and others. Of the instances in which customers reported their preference to switch to a competitive provider, MCI was listed as one of the customer's choices only [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] percent of the time for local voice and only [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] percent of time for local data (out of [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] and [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] instances, respectively).

Third, Verizon's experience demonstrates that, even when Verizon successfully bids to become the retail provider for commercial and institutional customers, Verizon often obtains only a small portion of the overall telecommunications business from these customers. Using year-end 2004 data available either publicly or through documents published or filed by enterprise customers, discussions with these customers' internal telecommunications teams or

analysts in the industry, Verizon examined the telecommunications spending practices of 10 of the largest users of telecommunications services in Boston, New York City, Philadelphia, and Washington, D.C. In 2004, Verizon earned only a small portion of the revenue expended by these customers for telecommunications services. See Table 4.

**[BEGIN CONFIDENTIAL]**

<b>Table 4. Verizon's Share of Revenues from 10 Largest Telecom Users</b>			
<b>City</b>	<b>Total Telecommunications Spending for 2004</b>	<b>Verizon Share of Telecommunications Spending</b>	<b>% of Telecommunications Services Customers Purchased from Verizon</b>

**[END CONFIDENTIAL]**

**C. The Transaction Will Not Enable Verizon To Increase Prices for Retail Services that Use Special Access as an Input**

As demonstrated above, following the transaction, there will continue to be a large list of significant competitors providing retail services that use special access, and there is accordingly no realistic prospect of unilateral or coordinated anticompetitive effects. If Verizon/MCI were to raise prices to large enterprise customers, it would lose customers to the established providers such as AT&T and Sprint, as well as the other entrants that have achieved success serving this segment. This is particularly true in light of the unique characteristics of the customers and demand in this market segment.

First, the majority of retail services that use special access as an input are purchased by larger business customers that are highly sophisticated.<sup>221</sup> In the case of Verizon, for example, the [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] customers served by ESG account for [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] percent of Verizon's retail special access revenues, whereas the more than [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] customers served by Retail Markets account for only [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] percent of such revenues. These large customers have the ability to negotiate effectively with even a small number of suppliers (which is not the case here).<sup>222</sup> There is also a large number of outside consultants who help such corporations design and issue RFPs and negotiate with the respondents of such proposals. Customers can engage the assistance of consulting firms throughout their entire procurement process, from assessing the providers in the market for a particular service to evaluating bids and negotiating contracts. Many customers also rely on consulting firms to perform periodic reviews of their existing contracts to ensure they receive competitive rates across all of their telecommunications purchases.

Second, these retail services that use special access are often highly heterogeneous. As described above, customers are increasingly seeking converged network solutions that integrate with their on-premises information technology, which requires a high degree of customization. Different customers also demand services at multiple locations with different services at each, which further increases the variation between the demand of individual customers. The demand

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<sup>221</sup> See also 2A Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 404c7, at 18 (2002) (“*Areeda*”) (“sellers will find it more difficult to maintain supracompetitive prices when tempted to discount in order to win large orders from sophisticated buyers”).

<sup>222</sup> See Declaration of Gustavo E. Bamberger, Dennis W. Carlton, and Allan L. Shampine ¶¶ 70-72, 79, attached to Public Interest Statement, WC Docket No. 05-75 (FCC filed Mar. 11, 2005); Bruno/Murphy Decl. ¶ 62; McMurtrie Decl. ¶¶ 6, 28.

for these heterogeneous services has not only facilitated a great deal of new entry from systems integrators, equipment suppliers, and the like, but also helps ensure competitive pricing. As Professor Areeda explains: "Product heterogeneity multiplies the avenues of rivalry and can thus impede tacit or even actual price coordination. Quality variations among the products of competing sellers generally produce price disparities, which will complicate the sellers' judgments about the proper cartel or oligopoly price, as well as output allocation."<sup>223</sup>

Third, the major customers of retail services that use special access operate over wide geographic areas. Large enterprise customers buy network services for their business locations, which frequently span global, national or regional geographies. For example, Verizon's largest ESG customers (those spending over \$10 million annually on communications services) average [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] sites, and even Verizon's smallest ESG customers (those spending less than \$250,000 annually) average [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] sites. It would be impractical and inefficient for such large customers to contract separately for service at each site. More important, such a disjointed aggregation of services would not serve their demand for unified, integrated systems. The competitive success of network integrators, who combine the facilities of other providers into unified networks, reflects that demand. Competition for such customers forces prices to competitive market levels in all geographic areas, irrespective of the degree of competition in each individual wire center or building. Large enterprise retail customers can accordingly drive special access prices to competitive levels even where there may not be multiple competitors from which to choose.

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<sup>223</sup> Areeda ¶ 942b.

Moreover, in light of the fact that the relevant retail customers typically demand services at multiple geographic locations, any increased ability to raise special access prices that Verizon would gain by obtaining MCI's local fiber facilities would not have an economically meaningful effect on the overall price that customers pay for retail services. With respect to any one large enterprise customer, MCI is typically able to provide service at only a small fraction of that customer's locations using its own facilities. Even assuming that Verizon was able to selectively discriminate in the special access prices at those locations, it would likely have no more than a minimal effect on that customer's total expenditures on special access, and an even less significant effect on the customer's total communications expenditures. As demonstrated in Section I.A.2 above, special access constitutes only a small fraction of the communications services that ESG and Retail Markets customers purchase. In 2004, special access accounted for only about [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] percent of total revenues generated by ESG customers (or [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] out of [BEGIN CONFIDENTIAL] [END CONFIDENTIAL]), and only about [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] percent of total revenues generated by Retail Markets customers (or [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] out of [BEGIN CONFIDENTIAL] [END CONFIDENTIAL]).

**V. DIVESTITURE OF MCI'S LOCAL FIBER NETWORKS IS UNNECESSARY AND WILL RESULT IN SIGNIFICANT INEFFICIENCIES AND COSTS TO CUSTOMERS**

Based on purported concerns about competitive effects of combining the local fiber networks of MCI and Verizon, some competitors have suggested imposing conditions on the transaction that would include company-specific pricing rules for Verizon's special access

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