Exhibit G

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

In the Matter of	)	
	)	
Petition of ACS of Anchorage, Inc. Pursuant to	)	
Section 10 of the Communications Act of 1934, as	)	WC Docket No. 05-281
amended, for Forbearance from Sections 251(c)(3)	)	
and 252(d)(1) in the Anchorage LEC Study Area	)	
	)	

REPLY STATEMENT OF HOWARD A. SHELANSKI IN SUPPORT OF PETITION OF ACS OF ANCHORAGE, INC. FOR FORBEARANCE FROM SECTIONS 251(C)(3) AND 252(D)(1)

Summary

1. The purpose of this reply statement is to respond to the declarations submitted on behalf of General Communication, Inc. ("GCI") by Dr. David Sappington[1] and Mr. William Zarakas.[2] As a preliminary matter, Dr. Sappington and I agree on certain basic economic principles at issue. We agree on the proper tests for market power and market definition and on the illogic of forbearing in cases where competition depends on the very UNEs that forbearance would make less available. I disagree, however, with Dr. Sappington and Mr. Zarakas over the

[1] Declaration of David E. M. Sappington, *Opposition of General Communication, Inc. to the Petition for Forbearance from Sections 251(c)(3) and 252(d)(1) of the Communications Act Filed by ACS of Anchorage*, WC Docket No. 05-281, attached thereto as Exhibit D ("Sappington Decl.").

[2] Declaration of William P. Zarakas, *Opposition of General Communication, Inc. to the Petition for Forbearance from Sections 251(c)(3) and 252(d)(1) of the Communications Act Filed by ACS of Anchorage*, WC Docket No. 05-281, attached thereto as Exhibit C ("Zarakas Decl.").

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relevant facts of this case and over their application of relevant economic principles to those facts. Both Dr. Sappington and Mr. Zarakas argue that the existing level of local competition in Anchorage depends on access to ACS of Anchorage, Inc. ("ACS") facilities and that, absent such access, ACS could dominate telecommunications facilities in Anchorage and have market power in Anchorage telecommunications markets. These claims are incorrect and are indeed refuted by the very data and economic feasibility analysis that Mr. Zarakas has submitted on GCI's behalf.

2. The first part of this declaration discusses why the markets proposed by GCI are improperly narrow. The second section explains why Dr. Sappington's characterization of ACS as a "dominant supplier" of essential competitive inputs is based on an exaggerated measure of competitive dependence on ACS facilities. The third part discusses why, in light of a more accurate measure of GCI's feasible facilities-based entry, ACS could not exercise market power over consumers in the relevant market. The fourth section refutes GCI's claims that forbearance would disrupt the undeniably vibrant and enduring competition in the Anchorage market.

<u>The relevant markets are not as narrow as GCI contends.</u>

3. Dr. Sappington and GCI argue for very narrow definitions of geographic and product markets to support their argument that ACS would be able to exercise market power upon forbearance. In this section I argue that the market definitions GCI and Dr. Sappington propose are incorrect. Given the available economic evidence and in the light of relevant precedent and economic principles, the geographic market should be defined as the entire Anchorage LEC study area, not as the splintered set of atomistic markets GCI proposes. Regarding relevant products, I agree that services to mass-market (residential and small-

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business) customers and services to enterprise (medium- and large-business) customers should constitute distinct product markets.[3] I disagree, however, with Dr. Sappington's treatment of "small business" customers[4] and residential MDU customers as distinct markets,[5] and his further subdivision of enterprise customers according to their service needs.[6]

<u>Geographic Market</u>

4. Dr. Sappington fails to propose a clear geographic market definition to rebut ACS's use of the Anchorage study area. He argues that competitive conditions[7] and costs of implementing facilities[8] differ across Anchorage but never states what the relevant geographic market boundaries should be. At one point he cites wire-center data[9] suggesting that he thinks wire centers are the relevant markets, despite GCI's statement to the contrary.[10] Dr. Sappington then speaks more generally of geographic "regions" without proposing any specific markets the Commission should consider in this case.[11]

5. Dr. Sappington's discussion of geographic markets is based on a backward-looking analysis of competitive conditions across Anchorage and therefore provides an

[3] Sappington Decl. at ¶ 28.

[4] *Id*. at ¶ 231.

[5] *Id.* at ¶ 29.

[6] *Id.* at ¶ 30.

[7] *Id.* at ¶ 108.

[8] *Id.* at ¶ 109.

[9] *Id.* at ¶ 108.

[10] GCI Opposition at 15 n.42.

[11] *See, e.g.*, Sappington Decl. at ¶¶ 110, 111.

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inaccurate picture of geographic market power.[12] He cites O'Malley and Rabbit Creek as areas in which GCI is almost entirely dependent on UNEs from ACS to compete. GCI has indeed chosen to serve customers in those locations through TELRIC-priced UNEs, but that does not mean, as Dr. Sappington implies, that there would be a lack of competition in those areas upon forbearance. Indeed, Mr. Zarakas finds that **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]** of GCI's residential lines in O'Malley and **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]** of GCI's residential lines in Rabbit Creek are near cable plant;[13] the comparable figures for switched business lines in those areas are respectively **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]** and **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]**.[14] Dr. Sappington ignores Mr. Zarakas's findings both as to these specific wire centers, as well as his overall findings that it would be economically feasible for GCI to expand its facilities dramatically. Dr. Sappington does not offer any basis for the Commission to conclude that ACS could profitably raise its retail rates in any submarket or region within the Anchorage study area. GCI's own findings as to its facilities-based expansion, on the other hand, suggest that ACS would have no such monopoly power and, accordingly, that the Anchorage Study Area is the correct geographic market for purposes of this case.

6. GCI itself agrees with ACS that wire centers do not delineate appropriate markets,[15] but GCI seeks even more granular markets defined according to "each residential

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[12] *Id.* at ¶ 108.

[13] Zarakas Decl. at Exhibit V.

[14] *Id.* at Exhibit VI.

[15] GCI Opposition at 15 n.42.

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customer's location."[16] GCI's proposed definition ignores the Commission's finding that a geographic market should include "those consumers with similar choices regarding a particular good or service in the same geographical area."[17] According to the Commission, a relevant geographic market is one in which "all customers in that area have the same competitive alternatives for a product."[18] GCI's proposal of miniscule markets consisting of individual customers or individual buildings takes no account of such common sources of competitive supply and are thus inconsistent with the Commission's geographic market determinations in forbearance proceedings.

7. Moreover, neither GCI nor its experts provide any evidence that such minute geographic markets could satisfy the accepted "hypothetical monopolist test" which Dr. Sappington agrees should guide market definition.[19] This test asks whether a hypothetical, profit-maximizing monopolist could impose a small but significant and non-transitory increase in price in a particular group of products or geographic region. The fact that ACS is the sole provider of telephone service to a given customer (or customer location) at a given time does not mean that ACS can impose a profitable and non-transitory price increase on that customer. As long as a competitor like GCI can step in and provide service within a reasonable time, supply is elastic, and the hypothetical monopolist test fails. GCI's proposed market definition based on "customer location" assumes that this elasticity of supply is unlikely. Yet GCI's own expert's

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[16] *Id.* at 13.

[17] *Qwest Order* at ¶ 18.

[18] *Id.*

[19] Sappington Decl. at ¶ 33.

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report (discussed *infra* at paragraphs 11-21) demonstrates exactly the opposite: such supply elasticity is economically feasible on a broadly distributed basis throughout the Anchorage study area.

8. In addition, GCI's geographic market definition would render meaningless the Commission's finding in its *Qwest Order* that a CLEC need not have complete market coverage in order to be deemed non-impaired.[20] In this decision, the Commission stated that the Communication Act's competition provisions can be considered "fully implemented" in a relevant market even if a CLEC cannot reach some customer locations. If each customer location were itself a relevant market, the Act could not be fully implemented until the CLEC could serve every customer.

Product market

9. GCI's proposed product market definitions are similarly too narrow. GCI incorrectly divides enterprise customers according to variations in the kinds of services they require.[21] Yet those varying needs do not necessarily imply distinct product markets. Dr. Sappington overlooks the facts that a provider with a given set of facilities can provide multiple services to a customer and that competitors can step in if a customer's existing carrier raises the price of a particular service. It appears that GCI's market definitions incorrectly place into

[20] *In the Matter of Petition of Qwest Corporation for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Omaha Metropolitan Statistical Area*, WC Docket No. 04-223, Memorandum Opinion and Order, FCC 05-170, at ¶ 69 (rel. Dec. 2, 2005) ("*Qwest Order*").

[21] Sappington Decl. at ¶ 30.

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distinct markets services customers would view as substitutes.[22] The correct product market definition must include all services a firm would have to dominate in order to raise prices successfully.

10. In the residential market, GCI argues that service to buildings housing multiple dwelling units (MDUs) should constitute a separate market.[23] However, GCI does not provide evidence that service to customers in MDUs should be considered a separate geographic or product market. More fundamentally, GCI provides no basis for its conclusion that competitive supply to the small number of MDUs in Anchorage differs from that of the residential market as a whole. As ACS explains in its reply comments, ACS faces the same costs and considerations that GCI faces in serving MDUs.[24] GCI does not explain why, if ACS were to try to raise prices to MDU customers, GCI would not be able to come in with a competitive offering. To the extent GCI is arguing that it has not been successful in receiving permission from MDU owners to enter the buildings, that is a separate issue of competitive success, not an issue of comparative economic impairment.

<u>Competition in Anchorage does not depend on ACS's facilities.</u>

11. The foundation of GCI's competitive impairment arguments is that ACS is a dominant supplier of essential inputs because "more than 80% of the switched service lines in

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[22] GCI Opposition at 17-18.

[23] *Id.* at 65.

[24] Statement of Randall W. Poor, *Reply Comments of ACS of Anchorage, Inc. in Support of its Petition for Forbearance from Sections 251(c)(3) and 252(d)(1)*, WC Docket No. 05-281, attached hereto as <u>Exhibit B</u>.

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service in Anchorage employ loops supplied by ACS."[25] GCI's experts repeatedly imply that competitors are dependent on access to ACS facilities to reach the great majority of customers in the Anchorage study area.[26] Yet GCI's 80% figure provides an overstated and misleading measure for competitive dependency on ACS' facilities, for two reasons.

12. First, GCI's claim of 80% includes ACS's market share. It is of course the case that ACS serves its own customers over its own facilities. The more important figure is therefore how many of ACS's current customers GCI *could* serve over its own facilities if it were able to attract those subscribers away from ACS. Only if that figure were 0—a most improbable result given the scope of GCI's cable, copper, and fiber networks—does it make sense to include all of ACS's customers in a measure of dependency on ACS facilities. Similarly, the fact that ACS serves its own customers over its own facilities does not justify the assumption that GCI would need ACS's network to serve all of those same customers. Yet that assumption is exactly what GCI's 80% dependency suggestion implies. GCI can only create such a high number by failing to count its facilities that could serve current ACS customers.

13. Second, the 80% figure is backward-looking: it includes only the facilities GCI has chosen to use given its option of regulated UNEs. As the FCC has made clear and GCI does not dispute, forward-looking economic feasibility of facilities-based competition is the applicable test for impairment. Thus, the relevant number for conducting forbearance analysis must include the facilities GCI could deploy on an economically feasible basis.

[25] Sappington Decl. at ¶ 76.

[26] Sappington Decl. at ¶ 91; Zarakas Decl. at ¶ 4, Exhibit I.

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14. GCI's own analysis of economic feasibility, prepared by Mr. Zarakas, soundly refutes any notion that GCI is dependent on ACS to reach a majority of consumers. While GCI never states how many of ACS's current customers it could feasibly serve over its own cable or fiber facilities, Mr. Zarakas concludes that it would be economically feasible for GCI to serve all but **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]** of its own customers over its own facilities and without any recourse to UNEs or wholesale services from ACS.[27]

15. It is regrettable that Mr. Zarakas did not extend his economic feasibility study to GCI's provision of facilities-based service to customers currently subscribing to ACS. GCI knows where those customers are and GCI alone knows the details of what facilities it has to serve those customers. Mr. Zarakas again simply places all ACS customers in the category of lines currently served over ACS facilities, excludes them from consideration in his economic feasibility study, and suggests that ACS controls access to **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]** of Anchorage customers even after economically feasible expansion of GCI's facilities.[28] Yet that **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]** figure is meaningless without the feasibility analysis GCI has omitted. Looking at the last line of Mr. Zarakas's Exhibit 1, the more informative and relevant figure for competitive dependency on ACS is **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]**, not **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]**.

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[27] Zarakas Decl. at Exhibit I.

[28] *Id.*

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16. Available information suggests that had GCI done a more complete economic feasibility analysis, it would have found that overall dependence on ACS facilities is low. Indeed, when all relevant factors are considered, it is likely even lower than the **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]** dependence that Mr. Zarakas finds would exist after economically feasible build-out to GCI's current customers.

17. First, GCI is not the only actual or potential entrant into the Anchorage market. Even where GCI does not have facilities, ACS' network is not necessarily the only network in place that could provide local exchange services. As GCI points out, another cable company, Eyecom, serves customers in Girdwood.[29] There are also wireless facilities capable of fixed service owned by Clearwire and AT&T Alascom covering a large part of Anchorage.[30]

18 Second, GCI may have understated its own facilities in its economic feasibility study. For example, Mr. Zarakas counts only **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]** lines served over GCI's network in a group of wire centers ("other wire centers")[31] that includes Elmendorf, an area in which GCI is the exclusive provider to some subdivisions via its own copper network and in which GCI's other expert witness, Dr. Sappington, says GCI serves **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]**

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[29] Sappington Decl. at ¶ 36.

[30] Statement of Kenneth L. Sprain, *Reply Comments of ACS of Anchorage, Inc. in Support of its Petition for Forbearance from Sections 251(c)(3) and 252(d)(1)*, WC Docket No. 05-281, attached hereto as Exhibit A; Statement of David E. Eisenberg, *Reply Comments of ACS of Anchorage, Inc. in Support of its Petition for Forbearance from Sections 251(c)(3) and 252(d)(1)*, WC Docket No. 05-281, attached hereto as Exhibit C; Statement of Charles L. Jackson, *Reply Comments of ACS of Anchorage, Inc. in Support of its Petition for Forbearance from Sections 251(c)(3) and 252(d)(1)*, WC Docket No. 05-281, attached hereto as Exhibit E.

[31] Zarakas Decl. at Exhibits V, VI.

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customers on-net.[32] Because ACS does not have access to the underlying data, it is impossible to verify the accuracy of the other figures underlying Mr. Zarakas's calculations.

19. Third, Mr. Zarakas improperly excludes from economic feasibility a substantial number of customers—nearly **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]** of them[33]—that GCI can economically reach with its facilities but has not been able to persuade to allow GCI onto their premises. He counts as "uneconomic" cases where the only barrier to GCI's deployment of facilities is the customer's refusal to allow GCI onto its premises to complete necessary upgrades. It is incorrect to consider GCI competitively impaired in serving such customers. First, there is a difference between being competitively impaired and being competitively unsuccessful. The fact that GCI cannot persuade a particular customer to let it perform an upgrade says more about that customer's view of GCI's services than about GCI's economic impairment. Second, such a customer could change its mind, an outcome that is increasingly likely should ACS try to raise its prices. The correct, forward-looking question is whether GCI could economically serve that customer if ACS tried to exercise market power and the customer sought GCI as an alternative supplier. If the answer is yes, that customer should be included in the percentage of the Anchorage market that GCI can economically serve "on-net." Such customers should not be excluded from the economically feasible set, as Mr. Zarakas has done with **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]** of residential customers and **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]** of small business customers—roughly

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[32] Sappington Decl. at ¶ 95.

[33] Zarakas Decl. at ¶¶ 32, 36.

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[BEGIN CONFIDENTIAL] [END CONFIDENTIAL] customers from the figures contained in Mr. Zarakas's declaration.[34]

20. Moreover, although this case does not depend on it, there is more significant intermodal competition than GCI acknowledges. Recent FCC data and findings show wireless substitution to be of growing importance in today's market. The FCC has found that 62% of all Americans, and over 90% of those between 20 and 49 years old, own cell phones.[35] Those subscribers have been using their wireless phones for an increasing number of minutes per month—an average of 580 monthly minutes per user at last count.[36] This increase has been accompanied by a marked decline in the amount of landline calling consumers have been doing. In 1996 American consumers made an average of 143 minutes of long-distance calls per month; by 2003 that figure had fallen to 71 minutes.[37] In 1996 Americans placed 504 billion conventional local telephone calls; in 2003 the number had dropped to 425 billion.[38] The inference of growing wireless substitution for wireline service is strong, and is corroborated by other data. The FCC has reported that 5.5% of Americans live in wireless-only households, a

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[34] Zarakas Decl. at ¶¶ 32, 36.

[35] FCC, *Trends in Telephone Service*, at ¶ 195 (rel. June 21, 2005), *available at* http://www.fcc.gov/Bureaus/Common_Carrier/Reports/FCC-State_Link/IAD/trend605.pdf ("Trends in Telephone Service").

[36] FCC, *Annual Report and Analysis of Competitive Market Conditions with Respect to Commercial Mobile Radio Services, Tenth Report*, at ¶ 5 (Sept. 30, 2005), *available at* http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-05-173A1.pdf.

[37] Trends in Telephone Service at Table 14.2.

[38] *Id.* at Table 10.2.

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figure that rises to 14% for 18- to 24-year olds.[39] Yet such figures understate the true degree of substitution. As the Commission has found, "[e]ven when not 'cutting the cord' completely, consumers appear increasingly to choose wireless service over traditional wireline service, particularly for certain uses."[40] The Commission went on to cite data that one-third of all households receive more than half of their calls wirelessly and 9% of households receive almost all their phone calls on their wireless phones.[41] To be sure, wireless substitution varies by market, but its potential force in disciplining ILEC market power should not be disregarded.

21. The above discussion shows critical flaws and omissions in GCI's (and its experts') portrayal of competitive conditions in Anchorage. My discussion of GCI's impairment analysis has been constrained by the need to take Mr. Zarakas's calculations at face value. As Mr. Blessing discusses in more detail in his reply statement, there is no way for ACS or the Commission to assess key aspects of GCI's feasibility calculations because key inputs and assumptions are absent from Mr. Zarakas's declaration. It is unclear how exactly the calculation worked or how the analysis distinguished customers to whom it would be economic for GCI to build out from those to whom it would not. The analysis is, in crucial respects, a black box, the output of which is hard to examine. Yet even with such constraints it is evident from GCI's analysis that there is no merit to GCI's contention that ACS is a "dominant" provider of essential inputs or has any meaningful control over access to customers in the Anchorage market.

ACS will not be able to exercise market power if forbearance is granted.

[39] *Id.* at ¶ 196.

[40] *Id.* at ¶ 197.

[41] *Id.*

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22. Dr. Sappington argues that if the FCC grants forbearance, ACS will be able to exercise market power to the detriment of consumers. As a threshold matter, Dr. Sappington and I agree that preservation of consumer welfare is the reason to be concerned about market power. We also agree about the basic principles and methods for determining whether a firm possesses market power. I disagree, however, with how Dr. Sappington has applied this test to the Anchorage market.

23. Dr. Sappington overstates ACS's ability to raise prices and understates the elasticity of facilities-based competitive supply. He simply asserts that "[u]nder forbearance, ACS could make it difficult or impossible for GCI" to serve customers seeking to escape a hypothetical ACS price increase.[42] The only basis for Dr. Sappington's claim, however, is his erroneous argument that ACS is a "dominant supplier" of essential inputs;[43] a claim he bases on his mistaken contention that ACS is the "exclusive facilities-based operator" for 81% of the Anchorage market.[44] Were that number true, I would agree with Dr. Sappington about ACS's market power. But as previously discussed, Dr. Sappington's 81% figure is plainly wrong: it does not include facilities GCI could economically provide to its own customers and it does not include either the facilities GCI already has, or could economically deploy, to serve ACS customers that GCI might win over. Dr. Sappington's figures ignore other competitors' facilities altogether.

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[42] Sappington Decl. at ¶ 89.

[43] *Id.*

[44] *Id.* at ¶ 95.

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24. A more accurate calculation of facilities-based competition in Anchorage—one that includes the facilities GCI can economically deploy both to its own and to ACS's current customers—leads to a dramatically diminished picture of ACS' control over central inputs: not over 80%, but well under **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]**. This fact undermines the two key premises of Dr. Sappington's conclusion that ACS possesses market power in Anchorage: that ACS is currently a "dominant" input supplier and that competitive supply of facilities-based service is not sufficiently elastic to make prices increases unprofitable.

25. Supply elasticity is of particular importance to competitive analysis. The ability of competitive firms to supply customers that wish to switch from the incumbent protects consumer welfare and demonstrates lack of competitive impairment. The degree of supply elasticity is an important factor in refining the inferences that one can draw from market share data. It is because GCI can expand its facilities-based output of service that Dr. Sappington's 81% number is an incorrect measure of competitive dependence on ACS facilities. Dr. Sappington elsewhere acknowledges the error in such analysis when he emphasizes that retail market share is not a reliable measure of market power.[45] He fails to carry that basic insight into his own analysis of ACS's market power.

26. Supply elasticity also explains why one cannot simply dismiss the competitive significance of GCI's expanding market share.[46] Dr. Sappington argues that GCI has used UNEs to expand market share and, in particular, to serve customers seeking to escape an ACS price

[45] *Id.* at ¶ 94.

[46] *Id.* at ¶ 88.

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increase. Dr. Sappington therefore labels as "(at best) misleading" the argument that GCI's competitive response demonstrates lack of market power on ACS's part.[47] There are two problems with Dr. Sappington's critique. First, my argument in my statement in support of ACS's Petition was that GCI's expansion of market share was significant precisely because it occurred at the same time GCI was *reducing* its reliance on UNEs. The sentence that came before the one Dr. Sappington chose to quote makes that clear. Second, the fact that GCI chose to expand output partly through UNEs does not mean GCI could not have used its own facilities to accomplish much of the same expansion. Mr. Zarakas's declaration suggests quite strongly that significant supply elasticity is feasible in the absence of UNEs. If GCI can economically expand its self provisioning from roughly **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]** lines to about **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]** lines for customers it currently serves,[48] there is good reason to believe it can also economically expand its facilities to accommodate customers GCI might win from ACS.

27. Moreover, neither successful disciplining of ACS's market power nor GCI's competitive success depends on GCI's having immediate, complete coverage of the Anchorage market. Dr. Sappington claims GCI will need to gain immediate facilities-based coverage to every Anchorage customer if the FCC forebears.[49] Elsewhere GCI's experts argue that the lack

[47] *Id.*

[48] Zarakas Decl. at Exhibit I.

[49] Sappington Decl. at ¶¶ 7, 8, 47, 55, 84, 87 (arguing repeatedly that forbearance should not be granted unless GCI can provide service wholly through its own facilities rather than depending on unregulated UNE rates).

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of complete coverage by GCI's facilities should be a barrier to forbearance.[50] This is the wrong approach as a matter of both law and economics. First, some lag against the incumbent is a normal incident of competitive entry and, as such, should not be considered a disadvantage that rises to the level of "impairment" under the Act.[51] The FCC itself has recently made clear that forbearance does not require that a competitor be able to serve all customers in the market over its own facilities, and that the required level of competitive coverage need not be immediate but could occur "within a commercially reasonable time."[52]

28. Second, competitive discipline of ACS does not depend on immediate, facilities-based access by GCI to every ACS customer. ACS will not be able profitably to raise prices even if a portion of its current customers can quickly switch to GCI. Even partial, or partially available, substitutes can be very powerful drivers of competitive behavior for ILECs because fixed costs are high compared to the variable costs of service. When an ILEC loses a customer, it loses the revenue that customer would provide; but it does not save much from not serving that customer. The result is that a lost customer is particularly harmful to a network operator because the operator loses not just the profit it would earn from the customer, but that customer's

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[50] Declaration of Gina Borland, *Opposition of General Communication, Inc. to the Petition for Forbearance from Sections 251(c)(3) and 252(d)(1) of the Communications Act Filed by ACS of Anchorage*, at ¶ 28, attached thereto as Exhibit A (stating that UNE termination is inappropriate because "the cable plant footprint does not cover the entirety of the ACS Anchorage study area"); Declaration of Gina Borland, *Opposition of General Communication, Inc. to the Petition for Forbearance from Sections 251(c)(3) and 252(d)(1) of the Communications Act Filed by ACS of Anchorage*, at ¶¶ 3-21, attached thereto as Exhibit H (discussing the obstacles preventing GCI from immediately providing service over its own facilities).

[51] *United States Telecom Ass'n v. FCC*, 290 F.3d 415, 427 (D.C. Cir. 2002).

[52] *Qwest Order* at ¶¶ 60 n.159, 69.

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contribution to fixed costs the operator must continue to bear. The lack of a downward adjustment in cost to offset revenue loss is particularly acute in telecommunications businesses because the fixed costs of building and maintaining a network are very high while the marginal costs of serving any customer are very low. The important consequence is that a competing network's coverage need not be complete for the ILEC to face acute competitive pressure to retain customers. There is certainly no reason to doubt the force of a competitor, particularly GCI, that can reach the clear majority of customers in Anchorage.

Forbearance will not lead to harmful results.

29. Once the accurate picture of ACS's market power is brought into focus, many of the bad consequences Dr. Sappington predicts from forbearance disappear. The "full fury of unconstrained ILEC wholesale market power"[53] that GCI tries to invoke turns out to be neither furious nor unconstrained. Perhaps realizing that GCI's case for impairment is made improbable by GCI's great competitive success to date and its ability economically to build out its facilities to serve the majority of customers, Dr. Sappington offers several additional arguments against forbearance. First, Dr. Sappington argues that the Commission should disregard GCI's own competitive success and capabilities and instead examine the competitive prospects of a hypothetical, reasonably efficient CLEC. Next, he presents a list of negative effects that he argues would result from forbearance. None of these arguments succeeds.

30. As a preliminary matter, there is no legal or economic reason for the Commission to consider the competitive effects of a hypothetical, "reasonably efficient" firm instead of GCI

[53] Sappington Decl. at ¶ 8.

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itself. Even if the Commission had adopted the hypothetical competitor standard for the analysis of impairment, there is no basis for importing that standard into a forbearance analysis, which by its terms looks at actual competition in a specific market.[54] More fundamentally, Dr. Sappington has the logic of the "reasonably efficient" carrier standard backward. The Commission did not say that data from a real-world competitor should be trumped by models of what a hypothetical, reasonably efficient competitor could accomplish. Instead, the Commission stated in its Triennial Review Remand Order that "to the extent competitors have deployed facilities sufficient to demonstrate that entry is economic in one geographic market, we presume that those facilities are reasonably efficient and that that carrier, or other carriers, could enter other similar geographic markets on an economic basis using similar (or even more efficient) technologies."[55] If anything, what is "reasonably efficient" is to be presumed from, not presented in contrast to, the progress of real-world competitors. GCI itself appears to recognize this as, in its comments, it neither references Dr. Sappington's argument regarding such a standard nor suggests that the "reasonably efficient competitor standard" is applicable in this case.

31. Looking to the actual market conditions in Anchorage, there is no basis for the harmful consequences Dr. Sappington speculates will arise after forbearance. First, Dr. Sappington argues that after forbearance, CLECs in Anchorage will be left to pay for UNEs at

[54] *See, e.g., Qwest Order* at ¶ 67 n.177 ("In today's Order, rather than making national impairment findings, we are applying the statutory standards of section 10 in a specific geographic market.").

[55] *In the Matter of Unbundled Access to Network Elements; Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, CC Docket No. 01-338, FCC 04-290, at ¶ 28 (2005) ("TRRO").

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rates that reflect embedded costs.[56] This is a red herring. As Mr. Zarakas's own analysis shows, the main effect will be that GCI will use its own facilities, not that it will buy more expensive UNEs.

32. Dr. Sappington also raises the specter of a deterrent effect on CLECs if forbearance is granted. He states that "[f]orbearance in Anchorage at the present time would send the chilling message to CLECs everywhere that the moment they demonstrate an emerging ability to serve some customers using only their own facilities . . . they will either be compelled to serve all customers in the manner immediately or be exposed"[57] to ILEC market power. Suffice it to say that there is nothing "emerging" about GCI's competitive ability and nothing "moment[ary]" about its progress. GCI's own expert says it can economically serve over 80% of its customers on-net. GCI has steadily marched to a market share that is greater than ACS's over the past several years. ACS did not seek forbearance at the moment GCI entered the market or even when it first started to transition customers to its own facilities. ACS seeks forbearance now, at a time when GCI is the largest service provider in Anchorage and after GCI has made clear it can supply most customers on its own network.

33. Dr. Sappington also argues that forbearance would force CLEC costs to escalate rapidly because CLECs would have to transition quickly to their own facilities to make up for the lack of UNEs. Given that Mr. Zarakas has found that GCI can make the transition economically to most customers, Dr. Sappington's conjecture is unsupported on the particular facts of this

[56] Sappington Decl. at ¶ 48.

[57] *Id.* at ¶ 8.

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case. It is indeed possible that accelerated deployment could raise costs, but Mr. Zarakas finds that GCI's build-out would be economic even if costs were to rise as much as **[BEGIN CONFIDENTIAL] [END CONFIDENTIAL]**.[58] Moreover, since GCI is deploying facilities in a number of different markets, including rural markets in Alaska,[59] there is no evidence that increased speed or scope of facilities deployment would be a barrier to GCI. Most importantly, however, there is no evidence that forbearance would require GCI to build or upgrade facilities any faster than it has already said is economically feasible.

34. Finally, Dr. Sappington suggests that if ACS remains under retail rate regulation after forbearance, it "will be reluctant to reduce its price aggressively in one portion of Anchorage if doing so will require it to reduce its price throughout Anchorage."[60] This statement might apply to a carrier that faced only limited pockets of competition but remained mostly dominant. However, if ACS failed to cut prices it would stand to lose most of its customers, not a small segment of them, as the supply elasticity evidence makes clear. For ACS, the consequence of keeping prices high would not be the preservation of revenues from most of its customers, but the loss of most customers to GCI and other competitors. There is nothing conjectural about that outcome: GCI's actual competitive success to date and GCI's own analysis

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[58] Zarakas Decl. at ¶ 33.

[59] *In the Matter of the Petition for Suspension and Modification of Certain Section 251(c) Obligations to Section 251(f)(2) of the Telecommunications Act of 1996 filed by Matanuska Telephone Association Inc*., Order Granting in Part, Petition for Suspension and Modification and Affirming Electronic Rulings ("MTA Order"), U-05-46, at 47 (Dec. 20, 2005).

[60] Sappington Decl. at ¶ 114.

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of economically feasible expansion of its facilities-based service make clear that ACS is in no position to exercise market power over consumers or competitors in Anchorage.

Respectfully Submitted,

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