

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

In the Matter of

Combined Application for Consent to the Transfer of Control of Telecomunicaciones de Puerto Rico, Inc., Holder of Domestic and International Section 214 Authorizations, from Verizon Communications Inc. to América Móvil, S.A. de C.V.

DA 06-1245

WT Docket No. 06-113

**Centennial Communications Corp. Reply to Opposition to Petition to Deny**

**1. Introduction and Summary.**

Centennial Communications Corp. (“Centennial”) respectfully replies to the opposition to Centennial’s petition to deny filed by Verizon Communications, Inc. (“Verizon”) and América Móvil, S.A. de C.V. (“América Móvil”).<sup>1</sup>

Cutting through the rhetoric, Applicants’ basic position is this: “Maybe there aren’t many public interest benefits to this deal, but there isn’t any harm, either – so go ahead and approve it.”<sup>2</sup> The difficulty with this position is twofold.

First, what the record actually establishes is that there are *no* public interest benefits to this transaction. The Puerto Rico Telephone Company (“PRTC”), now a subsidiary of multi-billion-dollar Verizon Communications, is to become a subsidiary of multi-billion-dollar América Móvil. On the *benefits* side, it is quite fair to greet this prospect with a shrug. Applicants assert that América Móvil’s experience selling landline service in El Salvador, Nicaragua and Guatemala will somehow give it a leg up on increasing landline penetration in Puerto Rico, but they never explain how or why this should be so – and there is no reason to think that it is. Verizon has five times the

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<sup>1</sup> See América Móvil’s and Verizon’s Opposition to Petitions to Deny (July 24, 2006) (“Opposition”). See also Centennial Communications Corp.’s Petition to Deny (July 14, 2006) (“Petition to Deny”). Verizon and América Móvil are referred to herein as the “Applicants.”

<sup>2</sup> See, e.g., Opposition at 5-6.

resources of América Móvil and has not been able to do much about landline penetration. There is no rational basis to conclude that América Móvil will fare any better.

Second, the record also establishes that there are reasons for concern about this transaction. Centennial identified two: the radical change in corporate culture that will necessarily follow from it, and national security concerns.

Centennial explained that PRTC's culture will inevitably change as it goes from being one of many Verizon-owned domestic incumbent local exchange carriers ("ILECs"), to being América Móvil's *only* U.S. ILEC. Moreover, PRTC's 1.1 million landline customers will join 2 million Salvadoran, Nicaraguan, and Guatemalan landline customers as part of the tiny landline fraction of América Móvil's wireless-focused business. So PRTC's landline ILEC operation – interconnection with which is critical to competition in Puerto Rico – will go from being part of the parent company's core business to being twice-relegated to the fringes: not just a landline business, but a landline business subject to unique and counter-intuitive regulatory obligations. Centennial plainly has legitimate reason to be concerned that its interconnection and competitive relationships with PRTC will go downhill once this deal goes through.

Applicants make no effort to address the problem of changing corporate culture and how it will affect PRTC's performance of its pro-competitive, ILEC-specific duties. They mention corporate culture only once (Opposition at 15), only in passing, and combined and confused with other parties' concerns. Centennial's showing on this point stands essentially un rebutted.

To deal with this problem, Centennial proposed two modest conditions. First, PRTC should fund an entity to monitor and report on its compliance with its 1996 Act obligations, for a period of three years. This will heighten the new PRTC's awareness of its duties and provide a sensible counterweight to the natural desire of its new owners to harm, rather than assist, its competitors. Second, PRTC should be barred from raising residential landline rates for a period of two years. This will prevent PRTC's new owners

from milking the landline business as a cash cow to fund investments and marketing efforts focused on wireless services.

These proposed conditions are a measured and appropriate response to the competitive problem that Centennial has identified. Applicants say nothing about the proposed monitoring condition. As for the ban on residential rate increases, they say that the Commission's cost allocation and ARMIS reporting rules should suffice. Opposition at 11-12. As the Supreme Court has observed, however, the advantage in any cost-based regulatory approach always lies with the entity that controls – and can manipulate – the underlying cost information. *Verizon Communications v. FCC*, 535 U.S. 467, 486, 512 (2002). What actually works to prevent cross-subsidies is eliminating the opportunity to recover costs from captive ratepayers – like PRTC's landline residential customers. Centennial's proposed condition is entirely reasonable and should be adopted.

Applicants do not dispute that there are national security concerns associated with foreign ownership of PRTC. Opposition at 4 (“The only legitimate concern here involves national security...”). However, they argue that the Commission should ignore Centennial's proposal for dealing with these concerns – allowing government agencies to opt out of contracts with PRTC without financial penalty or need for explanation – because affected Executive Branch agencies will fully address security matters. This is disingenuous. Certainly the Commission will consult with appropriate agencies in assessing whether this transaction should go forward and on what terms. But over time this Commission has been becoming more, not less, involved in national security and related matters, for example through its continued and expanding implementation of CALEA. It is therefore reasonable and appropriate for Centennial to propose – and for the Commission to consider – conditions to address these issues.

Assessing the public interest implications of any transaction necessarily involves the exercise of the Commission's predictive judgment. Centennial submits that it has provided a reasonable basis for concern about the proposed transaction and has proposed reasonable, measured conditions to alleviate those concerns. The Commission should accept Centennial's proposed conditions before allowing this transaction to proceed.

**2. There Are No Public Interest Benefits To This Transaction.**

Applicants have identified nothing good that will come out of this transaction. Their claims to the contrary are vague, non-specific, and not particularly credible. The Commission should conduct its review accordingly.

Applicants claim that the deal will bring to Puerto Rico “the benefits of América Móvil’s operating experience and business approach that it developed in offering service throughout the Americas.” Opposition at 3. But as Applicants note, PRTC is only part of Verizon’s Latin American assets, all of which are being sold. *See id.* at 7. Verizon, therefore, already has “operating experience and [a] business approach” relevant to the Americas. Indeed, Verizon’s experience also includes extensive operations in the United States of America – which is, of course, particularly relevant to Puerto Rico. So this claimed “benefit” boils down to a shift in parent company from a large firm with Latin American experience *and* United States experience, to a large firm with Latin American experience alone. That’s a loss, not a gain.

América Móvil also claims that its experience in El Salvador, Guatemala and Nicaragua in selling products “specifically for rural and low-income populations” will assist in Puerto Rico. Opposition at 3. Those countries, however, all have income and landline teledensity levels well below those of Puerto Rico:

COUNTRY	2004 PER CAPITA GDP <sup>3</sup>	2004 LANDLINE TELEDENSITY <sup>4</sup>
El Salvador	\$4,700	13.0%
Guatemala	\$4,700	9.2%
Nicaragua	\$2,900	3.9%
Puerto Rico	\$12,659	27.6%

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<sup>3</sup> Figures for El Salvador, Guatemala and Nicaragua taken from country-specific sections of: <https://www.cia.gov/cia/publications/factbook/index.html> (“Factbook”). Figure for Puerto Rico taken from [www.budde.com.au/Reports/Contents/Puerto-Rico-Telecoms-Market-Overview-Statistics-1887.html](http://www.budde.com.au/Reports/Contents/Puerto-Rico-Telecoms-Market-Overview-Statistics-1887.html) (“Budde Report”). As noted earlier, *see* Petition to Deny at 10 n.23, Applicants themselves rely on this report. *See* Public Interest Statement at 9 & n.20.

<sup>4</sup> Teledensity figures for all but Puerto Rico calculated from Factbook population and telephone figures. Teledensity figure for Puerto Rico taken from the Budde Report, *supra*.

It is not at all obvious why experience in El Salvador, Guatemala, and Nicaragua – obviously demographically quite different from Puerto Rico – will be particularly transferable to, or useful in, Puerto Rico.

Applicants also claim that the deal will “bring consumers the benefits of América Móvil’s economies of scale and scope.” Opposition at 3. But as Centennial noted, this is not a benefit, because América Móvil is five times *smaller* than Verizon.<sup>5</sup> PRTC’s parent company will enjoy *lesser* “economies of scale and scope” after the deal than before. This cannot remotely be treated as a “benefit” of this deal. If anything, it is a *cost*.

Logic requires that, just as any harms must be “transaction-specific,” *i.e.*, must arise from the transaction itself,<sup>6</sup> so too must any purported benefits arise from the transaction sought to be approved. Anything else results in an “apples to oranges” comparison, and the Commission should reject such arguments. *See e.g.*, Opposition at 6-7. For example, Applicants claim that since Verizon has decided to sell off its Caribbean and Latin American operations, the relevant comparison is not Verizon versus América Móvil, but rather América Móvil versus a purely hypothetical stand-alone PRTC. *Id.* But this assumes that Verizon could withdraw from the Puerto Rico market without Commission approval – *i.e.*, that the loss of Verizon as PRTC’s parent entity is a *fait accompli*. Verizon, however, cannot exit the market without Commission approval.<sup>7</sup> Applicants’ argument here is simply sleight-of-hand to obscure the fact that looking specifically at the effects of the transaction that they are asking the Commission to

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<sup>5</sup> See Petition to Deny at 14 n.30.

<sup>6</sup> See *Verizon Communications, Inc. and MCI, Inc. Applications for Approval of Transfer of Control*, Memorandum Opinion and Order, 20 FCC Rcd 18433 (2005) at ¶ 19 (“*Verizon-MCI Order*”).

<sup>7</sup> Cf. *Arbros Communications, Inc. Apparent Liability for Forfeiture*, Notice of Apparent Liability for Forfeiture, 18 FCC Rcd 3251 (2003).

approve, PRTC's access to parent-company economies of scale and scope will get worse, not better.<sup>8</sup>

Finally, Applicants claim that the transaction will bring to Puerto Rico América Móvil's "experience in providing service in areas with difficult-to-serve terrain and dramatic urban/rural differences." Opposition at 4. But Verizon plainly has plenty of that kind of experience as well. In addition to Verizon's Latin American businesses, noted above, Verizon has provided landline service in, for example, Maine, Hawaii, and West Virginia. There is no reason to think that América Móvil truly brings anything of value to the table on this point, as compared with Verizon's experience and capabilities.

In sum, the Applicants have not shown that anything good will come out of this transaction. The reality is simply this: Verizon for its own strategic business reasons has chosen to sell its Latin American and Caribbean businesses. *See* Opposition at 7. América Móvil, for *its* own strategic reasons, wants to buy them. As regards Puerto Rico, there is no reason to think that PRTC and its landline operations will be any better off with América Móvil as the owner. There are, however, some good reasons to think that there are downsides to the transaction that the Commission should not ignore.

### **3. Applicants Ignore The Inevitable Change In PRTC's Corporate Culture.**

Centennial pointed out that the change in the nature and business focus of PRTC's parent company will inevitably result in a change in PRTC's corporate culture, and provided numerous citations – including citations to decisions of this Commission – showing that it is reasonable to take changes in corporate culture into account when assessing likely corporate behavior. Applicants completely ignore this point. Their sole

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<sup>8</sup> Applicants point out that the Commission has previously approved transactions where the acquiring firm would have less extensive economies of scale/scope than the selling firm. *See* Opposition at 8 & n.13. That is true, but beside the point. It is certainly possible that a transaction in which access to economies of scale and scope will decline would still, on balance, be in the public interest. But that does not mean that a loss of economies of scale and scope – such as will occur here – should somehow be counted as a public interest *benefit*.

reference to corporate culture is a single sentence in which it is muddled with other parties' unrelated claims. *See* Opposition at 15; *cf. id.* at 23.

Given that Applicants appear to have nothing substantive to say on this point, Centennial will not belabor it. We do, however, note the following contradiction: When the Applicants are trying to convince the Commission that PRTC's new owners will do good things for Puerto Rico, they urge the Commission believe that América Móvil's experience and business knowledge derived in Latin America will allow it to change PRTC's ways of doing business in Puerto Rico, for the better. *See* Opposition at 3-4. But when Centennial observes that América Móvil's business focus and experience will lead it to behave in ways that would not fully align either with PRTC's obligations as a U.S. ILEC or with the interests of PRTC's landline residential ratepayers, Applicants dismiss these observations as "cynical claims" and "vague assertions." Opposition at 15.

Centennial's concerns about changes in PRTC's corporate culture are neither cynical nor vague. Common business experience teaches that the attitudes and objectives of the larger corporate organization of which an entity is a part affects how the subsidiary entity behaves. In this regard, as then-Commissioner Powell stated (commenting on the environment created by the 1996 Act): "In the time that I have been at the Commission, I have observed how corporate and even regulatory culture *can dramatically affect the objectives and performance of different firms.*"<sup>9</sup> While it is impossible to say with absolute precision how a change in corporate culture will affect specific behaviors, that simply means that in making this assessment the Commission must reasonably rely on its ability and authority to make predictive judgments based on its expertise.

Note that this is not in any way an argument based on claims that PRTC's past performance of its duties has "somehow been inadequate." Opposition at 19. Centennial is far from happy with PRTC's past performance, but the point here is that the impending change in PRTC's corporate culture is likely to cause that performance to degrade.

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<sup>9</sup> Text of speech, December 2, 1998, 1988 FCC LEXIS 6165 (emphasis added).

Specifically, Centennial pointed out that a 6-year-old Mexican firm with an overwhelming focus on Latin American competitive wireless services – and no experience with the market-opening obligations of the 1996 Act – will create a vastly different corporate culture for PRTC than existed under the auspices of Verizon, a successor to two century-old United States firms with enormous experience operating under that Act since it was passed. This seems so obvious that it is difficult to dispute it – which may be, in fact, why Applicants have not actually done so.

Applicants’ entire argument on this point boils down to the claim that since the transaction will not affect market concentration in the landline business, it will necessarily also not affect PRTC’s behavior with regard to that business. *See, e.g.*, Opposition at 2, 9, 17. The flaw in this claim is the assumption that the only thing that affects a firm’s behavior is its market share. In fact – to use Chairman Powell’s words – corporate culture “can dramatically affect the objectives and performance” of a firm. The Commission should not turn a blind eye to this fact in the context of this unique transaction – again, the first time a non-U.S. firm has sought to acquire a major ILEC.<sup>10</sup>

The impending change in PRTC’s corporate culture is a real, identifiable, transaction-specific problem. We urge the Commission to take it into account in assessing this transaction.

#### **4. Centennial’s Proposed Conditions Are Focused And Reasonable.**

Centennial proposed two modest conditions to offset the effects of the impending change in PRTC’s corporate culture. First, PRTC should fund an outside entity to monitor and provide semi-annual reports on its compliance with the 1996 Act, for three years. Applicants do not address this proposed condition in any detail. Centennial

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<sup>10</sup> Applicants point out that a high market share does not necessarily translate into the ability to engage in anticompetitive conduct. Opposition at 11. Fair enough – market share is not always destiny. But Applicants fail to acknowledge that for this very reason, the fact that PRTC’s market share will remain constant does not mean that *other factors* – here, a radical change in corporate culture – cannot or will not affect PRTC’s behavior following the transaction.

submits that it responds directly to the problem of changing corporate culture by demanding that PRTC's new owners pay adequate attention to, and rapidly develop sensitivity to, their 1996 Act obligations. As we noted earlier, from an outsider's perspective, those obligations are counter-intuitive, in that they call on the ILEC to cooperate with and even assist its most bitter rivals. Petition to Deny at 5-7. The fact that a monitor exists and will be filing reports – not to mention the fact that the requirement will have been imposed as a condition of the transaction itself – will force PRTC's new owners to take these obligations more seriously.

Centennial's second proposed condition is that PRTC be barred from raising residence rates for two years. PRTC's new owners will be sorely tempted to use PRTC's landline residential service as a cash cow to fund wireless and other growing, competitive businesses. Applicant's response, quoting materials more than a decade old, is that the Commission's cost allocation and ARMIS rules are adequate to prevent cross-subsidy. Opposition at 11-12. But this is clearly wrong. The benefit of price caps is that they make it unnecessary for regulators or competitors to pore over arcane accounting records after the fact, looking for evidence of cost misallocations – evidence that, logically, PRTC will have done everything in its power to manipulate and obscure. Instead, price cap regulation *prevents* cross-subsidy by making it unprofitable from the start.

The United States Supreme Court recently explained why accounting-based, cost-based regulation is inevitably stacked in favor of the regulated company, and why price-cap regulation is better:

[T]he prudent-investment rule, in practice [was often] ... no match for *the capacity of utilities having all the relevant information to manipulate the rate base and renegotiate the rate of return every time a rate was set*. The regulatory response in some markets was adoption of a rate-based method commonly called "price caps," ...

There are, of course, objections other than inefficiency to any method of rate making *that relies on embedded costs as allegedly reflected in incumbents' book-cost data, with the possibilities for manipulation this presents*. Even if incumbents have built and are operating leased elements at economically efficient costs, *the temptation would remain to overstate*

*book costs to rate making commissions and so perpetuate the intractable problems that led to the price-cap innovation.*

*Verizon Communications v. FCC*, 535 U.S. 467, 486, 512 (2002) (emphasis added).

In this regard, Centennial’s proposed ban on residential rate increases is, in practical effect, a form of temporary “price cap” imposed on the rates most likely to be the source of cross-subsidy. It is a focused and simple way to prevent PRTC’s new owners – with their new corporate culture – from taking advantage of the system of cost-based regulation to which PRTC is now nominally subject.

Centennial’s final proposed condition relates to national security concerns. Specifically, Centennial suggested that government agencies currently buying communications services from PRTC be permitted to terminate their contracts without financial penalty, irrespective of any term or volume commitments that might exist in such contracts. The benefits of this proposal are obvious: any agency that for whatever reason is uncomfortable with its critical communications being supplied by a firm controlled by PRTC’s new owners should not have to jump through any economic, financial, or business hoops to avoid any problems such an agency might perceive. Particularly, such agencies should not be put in a position where they face financial or contractual pressures to explain *why* they are concerned, or what the nature of their concerns might be. This seems to Centennial to be a fair and reasonable way to address these types of concerns, should they actually exist.<sup>11</sup>

Applicants agree that national security is a legitimate basis for concern about this transaction. Opposition at 4. They assert, however, that the Commission should deny Centennial’s proposed condition because the entire problem of national security should be dealt with by the most directly affected executive branch agencies. Opposition at 26-27. Centennial fully expects those agencies to consult with the Commission on these matters, and fully expects the Commission to accommodate their concerns. The fact

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<sup>11</sup> Of course, any agency receiving service from PRTC that is not concerned about the new regime would simply allow its existing contracts to remain in force.

remains, however, that the standard under which this transaction is to be assessed is the “public interest,” which obviously includes considerations of national security.<sup>12</sup>

Centennial does not expect the Commission to adopt its proposed condition in the absence of consultation with affected executive branch agencies. But the fact that such agencies will be consulted is no reason not to consider Centennial’s proposed condition in the first place, as Applicants apparently believe. To the contrary, over time this Commission has been becoming more, not less, involved in national security and related matters, for example through its continued implementation of CALEA.<sup>13</sup> It is therefore reasonable and appropriate for Centennial to propose – and for the Commission to consider – conditions to address these issues.

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<sup>12</sup> See *Promoting Efficient Use of Spectrum Through Elimination of Barriers to the Development of Secondary Markets*, Report And Order And Further Notice Of Proposed Rulemaking, 18 FCC Rcd 20604 (2003) at ¶ 4 (noting that policies relating to “homeland security” are included among “public interest concerns”); *Communications Assistance for Law Enforcement Act and Broadband Access and Services*, First Report And Order And Further Notice Of Proposed Rulemaking, 20 FCC Rcd 14989 (2005) at ¶ 14 (footnote omitted) (public interest includes consideration of whether a regulatory action would “protect public safety and national security”).

<sup>13</sup> For example, the Commission recently held that it will treat deficiencies in CALEA compliance as violations of the Commission’s own rules, not merely matters for law enforcement agencies to sort out with carriers in federal court. See *Communications Assistance for Law Enforcement Act and Broadband Access and Services*, Second Report and Order and Memorandum Opinion and Order, 2006 FCC LEXIS 2862; 38 Comm. Reg. (P & F) 645 (2006) at ¶¶ 63-68. Of course, CALEA is an “other applicable statute” that the Commission is required to consider in assessing the public interest associated with a proposed transaction. See *Verizon-MCI Order* at ¶ 16.

**5. Conclusion.**

For the reasons stated here and in Centennial's Petition to Deny, the Commission should not approve the proposed sale of PRTC to América Móvil unless the conditions proposed by Centennial are imposed on the transaction.

Respectfully submitted,

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## CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing “Centennial Communications Corp. Reply to Opposition to Petition to Deny” was delivered by electronic mail, or First Class, postage prepaid, U.S. Mail on this 28<sup>th</sup> day of July 2006 to the following:

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