

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

In the Matter of)	
)	
)	
Special Access Rates for Price Cap)	WC Docket No. 05-25
Local Exchange Carriers)	
)	
AT&T Corp. Petition for Rulemaking to Reform)	RM-10593
Regulation of Incumbent Local Exchange Carrier)	
Rates for Interstate Special Access Services)	

**COMMENTS OF
THE UNITED STATES TELECOM ASSOCIATION**

Its Attorneys:	Jonathan Banks
	Robert H. Mayer
	Indra Sehdev Chalk

607 14th Street, NW, Suite 400
Washington, DC 20005
(202) 326-7300

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TABLE OF CONTENTS

	<u>Page</u>
SUMMARY	i
I. THE SPECIAL ACCESS SERVICES MARKET IS HIGHLY COMPETITIVE	1
A. Overview of Special Access Regulation	3
B. Standard for Regulating Special Access Services	8
II. ECONOMIC ANALYSIS AND MARKET FACTS SHOW THAT THERE IS NO BASIS FOR BELIEVING THAT TURNING BACK THE REGULATORY CLOCK WILL BENEFIT CONSUMERS OR COMPETITION.	12
A. Prices Are Lower Since the Adoption of Pricing Flexibility	13
B. Special Access Competition is Robust	14
C. New Services Are Being Introduced	19
III. USE OF ARMIS DATA IS MISLEADING	21
A. ARMIS data is not reliable for measuring service-specific profits, and, therefore, ARMIS data is not useful for setting just and reasonable rates	22
B. There is no credible evidence that current rates are not just and reasonable	23
IV. THE COMMISSION DOES NOT HAVE THE INFORMATION IT NEEDS TO IMPOSE STRICTER PRICING REGULATIONS.	24
V. THE COMMISSION SHOULD UPDATE PRICING FLEXIBILITY RULES.	25
VI. CONCLUSION	25

SUMMARY

Over 15 years ago, following the successful introduction of competition in the interexchange services and consumer premises equipment (CPE) markets, the Federal Communications Commission (Commission) recognized that the special access services market was likewise conducive to competition. As special access competition developed, the Commission adopted pricing flexibility rules to encourage competition to replace regulation as the primary means of setting special access prices. Although companies looking for below-market rates have called for re-regulating special access services, the United States Telecom Association (UStelecom) urges the Commission not to do so because pricing flexibility is working: Prices are down, investment is up, and competition is robust. Re-imposing price regulation on special access services would lack any economic support and would be bad regulatory policy.

The Commission should not regulate special access services unless the benefits of doing so exceed the costs. The benefits of a price regulation scheme are likely to exceed the costs only in monopoly or near-monopoly conditions, and there are no monopoly or near-monopoly conditions in the special access market today. As a recent GAO study confirms, special access prices have declined in the years since the Commission adopted pricing flexibility. Competitive local exchange carriers (LECs) themselves confirm that competition for special access is fierce and that they continue to experience downward pricing pressure. Those arguing for increased regulation do not offer meaningful evidence to refute the fact that special access prices are declining because of pricing flexibility and competition. They simply appear to want the Commission to guarantee them cheaper prices than today's competitive market supports.

Special access competition is robust and has indisputably increased since 1999 when the Commission adopted pricing flexibility. Incumbent LECs face widespread and growing competition from competing LECs, cable operators, and providers of wireless broadband services. Incumbent LECs also face increasing competitive pressure from carriers using new technologies. This robust and increasing competition in the special access market is the result of the Commission's pro-market policies. The Commission must not turn its back on those policies by re-regulating special access.

Some of the same competing LECs that publicly characterize the market as fiercely competitive are calling for the re-regulation of special access based on misleading use of ARMIS data. This accounting data was never intended to be used to measure the rates of return on individual services, and, therefore, the Commission should not rely on it when examining competition in the special access market.

Before the Commission could act on any recommendation to re-impose pricing regulation, it would need a complete record of what competitors charge to provide special access services and what they are actually paying, not just to incumbent LECs but also to competitive providers with whom they have negotiated private contracts to buy special access services. The Commission also needs information about where competing LECs are deploying facilities and serving customers.

Given the eight years since the *Pricing Flexibility Order* and the competitive state of the market, the Commission should update its pricing flexibility rules by extending Phase I pricing flexibility to all carriers so they have the freedom to reduce prices and aggressively compete and by updating Phase II criteria to reflect competition from cable and fixed wireless providers.

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I. THE SPECIAL ACCESS SERVICES MARKET IS HIGHLY COMPETITIVE.

Based on every conceivable measure, the special access services market is extremely competitive. This is true whether one considers actual prices or revenue trends, as the record in this proceeding makes clear. Investment and competitiveness are further underscored by the recent major network expansions of facilities-based competing LECs and widespread entry by intermodal cable and wireless providers.

Today's robust competition in the special access market is due in no small part to the Commission's decision in 1999 to adopt pricing flexibility rules to advance its central policy objective—to help competition “replace[] regulation as the primary means of setting prices.”¹ The Commission's pricing flexibility regime, under which special access services offered by incumbent LECs qualify for decreased price regulation if

¹*Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers*, Fifth Report and Order and Further Notice of Proposed Rulemaking, 14 FCC Rcd 14221, 14224 ¶ 2 (1999) (“*Pricing Flexibility Order*”).

certain competitive thresholds are satisfied, makes economic sense, has been affirmed by the D.C. Circuit, and has benefited carriers and customers alike. USTelecom² reiterates its support for this regime.

Although some special access customers looking for cheaper prices have called for greater regulation of special access rates, USTelecom urges the Commission to refrain from doing so. The Commission's pricing flexibility regime has led to lower prices, increased investment, and robust competition. It is working. Reimposing onerous pricing rules that the Commission began phasing out in the 1990s—before competition had matured to today's levels and before there was any intermodal and wireless special access competition at all—would make no economic or regulatory sense. Doing so also would be inconsistent with congressional policy and Commission precedent to allow competition rather than regulation to secure lower prices, higher quality services, and the rapid deployment of new technologies.³

² USTelecom is the premier trade association representing service providers and suppliers for the telecommunications industry. USTelecom members provide a full array of services, including broadband, voice, data, and video over wireline and wireless networks.

³ See, e.g., 47 U.S.C. § 160(c) (requiring the Commission in connection with deciding whether to forbear from applying regulation to consider the extent to which forbearance “will promote competitive market conditions ...”); 47 U.S.C. § 161 (requiring the Commission to repeal or modify any regulation that it determines “is no longer necessary in the public interest as the result of meaningful economic competition between providers of such service”); *Pricing Flexibility Order*, 14 FCC Rcd at 14224 ¶ 2 (noting the Commission's central objective to help competition “replace[] regulation as the primary means of setting prices”).

A. Overview of Special Access Regulation

The Commission first began planting the seeds of special access competition in 1985 when it fostered “bypass” service by competitive access providers (CAPs).⁴ In doing so, the Commission noted its desire to promote “competition in the provision of interstate common carrier services” and encourage interstate carriers “to use alternative facilities and technologies in their systems,” which, according to the Commission, would “stimulate innovation, lower rates, increase diversity and encourage the efficient use of facilities.”⁵ As a result of these efforts, companies such as Teleport, Metropolitan Fiber Systems, and other CAPs began building their own fiber facilities to compete with incumbent LECs.

Beginning in 1992, the Commission continued its efforts to promote special access competition by giving CAPs not only the right to bypass, but also a right to interconnect with, any incumbent LEC by collocating on the LEC’s own premises.⁶ The Commission used competition in the interexchange and CPE markets as its model, noting that competition in these markets benefited consumers through “increased service

⁴ See *Cox Cable Communications, Inc.*, Memorandum Opinion, 102 F.C.C. 2d 110 (1985), *vacated as moot*, 61 Rad. Reg. (Pike & Fisher) 967 (1986).

⁵ *Id.* at 127.

⁶ See, e.g., *Expanded Interconnection with Local Telephone Company Facilities; Amendment of the Part 69 Allocation of General Support Facility Costs*, Report and Order and Notice of Proposed Rulemaking, 7 FCC Rcd 7369 (1992) (granting expanded interconnection for special access services) (“*First Expanded Interconnection Order*”), *vacated on other grounds and remanded*, *Bell Atlantic Tel. Cos. v. FCC*, 24 F.3d 1441 (D.C. Cir. 1994); *Expanded Interconnection with Local Telephone Company Facilities*, Second Report and Order and Third Notice of Proposed Rulemaking, 8 FCC Rcd 7374 (1993) (extending expanded interconnection to switched transport services). Although the D.C. Circuit eventually rejected the Commission’s physical collocation requirement in *Bell Atlantic v. FCC*, it was reinstated by the Telecommunications Act of 1996.

options, reduced rates, and faster implementation of new technologies”; according to the Commission, similar benefits were likely to result from competition in the special access market as well.⁷

The Commission’s efforts to introduce competition in the special access services market were successful. Even before passage of the Telecommunications Act of 1996 (1996 Act),⁸ 29 CAPs had deployed fiber networks consisting of more than 21,000 fiber route miles in approximately 100 cities.⁹ Just four years after the passage of the 1996 Act, the Commission observed that “facilities-based competitive access providers” represented a “mature source of competition in telecommunications markets.”¹⁰

With the advent of special access competition, the Commission began the process of allowing the competitive market rather than regulation to determine prices. In 1990, the Commission adopted price cap regulation in order to sever the relationship between rates and costs and replicate the efficiency incentives of a competitive market.¹¹ In so doing, the Commission broadly embraced “a policy judgment that incentive-based

⁷ See, e.g., *First Expanded Interconnection Order*, 7 FCC Rcd at 7378-80 ¶¶ 13-14.

⁸ 47 U.S.C. § 251(c)(6).

⁹ See UNE Fact Report 2002, CC Docket Nos. 01-338, 96-98, 98-147, at III-7 (prepared for and submitted by BellSouth, SBC, Qwest, and Verizon Apr. 2002).

¹⁰ *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, Supplemental Order Clarification, 15 FCC Rcd 9587, 9597 ¶ 18 (2000), *aff’d*, *Competitive Telecomms. Ass’n v. FCC*, 309 F.3d 8 (D.C. Cir. 2002).

¹¹ *Policy and Rules Concerning Rates for Dominant Carriers*, Second Report and Order, 5 FCC Rcd 6786 (1990) (“*LEC Price Cap Order*”).

regulation is superior to rate of return for the regulation of certain dominant carriers, including local exchange carriers.”¹²

Similarly, at the same time the Commission first imposed expanded interconnection obligations on incumbent LECs in 1992, the Commission recognized that incumbent LECs should be given additional flexibility in setting special access prices due to the “significantly increased potential for competition” in the special access market.¹³ Specifically, the Commission permitted incumbent LECs “to implement a system of traffic density-related rate zones to bring special access rates more in line with costs” and to offer reasonable volume and term discounts, which, according to the Commission “can be a useful and legitimate means of pricing special access services to recognize the efficiencies associated with larger volumes of traffic and the certainty of longer term deals.”¹⁴

In 1995, when special access competition was far less expansive than it is today, the Commission reaffirmed its judgment that competition in the special access market was preferable to regulation.¹⁵ The Commission further found that, unlike rate-of-return regulation, price cap regulation can and should “act as a transitional system as LEC regulated services,” such as special access, become “subject to greater competition.”¹⁶

¹² *LEC Price Cap Order*, 5 FCC Rcd at 6789 ¶ 21 (citing *Policy and Rules Concerning Rates for Dominant Carriers*, Report and Order and Second Further Notice of Proposed Rulemaking, 4 FCC Rcd 2873, 2931-33 ¶ 113 (1989)).

¹³ See, e.g., *First Expanded Interconnection Order*, 7 FCC Rcd at 7453 ¶ 177.

¹⁴ *Id.* at 7454 ¶ 178; see also *id.* at 7463 ¶ 199.

¹⁵ *Price Cap Performance Review for Local Exchange Carriers*, First Report and Order, 10 FCC Rcd 8961, 8989 ¶ 64 (1995) (“*LEC Price Cap Review Order*”).

¹⁶ *Id.*

In 1999, a Democratic-led Commission continued this transition by adopting pricing flexibility rules in order to help competition “replace[] regulation as the primary means of setting prices.”¹⁷ The Commission reasoned that incumbent LECs should enjoy “progressively greater pricing flexibility [for special access services] as they face increasing competition.”¹⁸ The establishment of pricing flexibility was consistent with the Commission’s belief that “competition can be expected to carry out the purposes of the Communications Act more assuredly than regulation” ever could, and that regulation is therefore appropriate “only where and to the extent that competition remain[s] absent in the marketplace.”¹⁹

In its *Pricing Flexibility Order*, the Commission established two phases of pricing flexibility for special access services, Phase I and Phase II. Under Phase I, incumbent LECs are permitted to enter into contract tariffs.²⁰ Phase II pricing flexibility removes the incumbent LEC’s special access services from price cap regulation,²¹ though, as the Commission has made clear, they remain subject to regulation under sections 201 and 202 of the Communications Act of 1934, as amended (the Communications Act): “Sections 201 and 202 of the [Communications Act] require that rates, terms and conditions for telecommunications services be just and reasonable, and prohibit unjust or unreasonable discrimination. Part 69 implements these sections of the Act by

¹⁷ *Pricing Flexibility Order*, 14 FCC Rcd at 14224 ¶ 2.

¹⁸ *Id.* at 14257, ¶ 67.

¹⁹ *LEC Price Cap Review Order* at 8989 ¶ 64.

²⁰ 47 C.F.R. § 69.727(a).

²¹ 47 C.F.R. § 69.727(b)(2).

establishing rules that . . . establish the degree of pricing flexibility available to price-cap LECs.”²²

The United States Court of Appeals for the District of Columbia (D.C. Circuit) affirmed the Commission’s *Pricing Flexibility Order* in *WorldCom, Inc. v. FCC*, 238 F.3d 449 (D.C. Cir. 2001). The Court of Appeals rejected arguments that the Commission’s pricing flexibility regime was arbitrary and capricious by failing to condition relief upon a finding of sufficient actual competition. According to the D.C. Circuit, there is “no statutory requirement that the FCC be confident to a metaphysical certainty of its predictions about the future of competition in a given market before it may modify its regulatory scheme.”²³ Furthermore, the D.C. Circuit upheld the Commission’s decision to make ease of administration and enforceability a consideration in setting its standard for regulatory relief and made clear that, while the Commission must provide a rational basis when setting a competitive threshold, it is not held to a standard of perfection. As such, the D.C. Circuit found that the Commission’s approach in the *Pricing Flexibility Order* was “precisely the sort of ‘rational legislative-type judgment’ the FCC is empowered to exercise and we are required to respect.”²⁴

Since adoption of the *Pricing Flexibility Order*, the Commission has granted numerous flexibility petitions, finding that competition has increased to a level where incumbent LECs have met the qualifications for Phase I and Phase II relief in

²² See *Wireline Competition Bureau Biennial Regulatory Review 2004*, Staff Report, 20 FCC Rcd 263, 339 (2005)(footnotes omitted).

²³ *WorldCom, Inc. v. FCC*, 238 F.3d 449, 459 (D.C. Cir. 2001) (citations omitted).

²⁴ *Id.* at 461-462 (citations omitted).

Metropolitan Statistical Areas (MSAs) throughout the United States. The first petition for pricing flexibility for an incumbent LEC was approved in December 2000 when BellSouth received Phase I and II pricing flexibility in several MSAs.²⁵ Similar relief was granted for MSAs in the Verizon²⁶ and SBC²⁷ operating areas. The Commission has continued to grant Phase I and II pricing flexibility as competition has increased in even more MSAs.

B. Standard for Regulating Special Access Services

The Commission should not regulate special access services unless the benefits of doing so exceed the costs. The Commission consistently has embraced this principle, decreasing regulation where competition is taking hold.²⁸ Competitors have been investing in special access facilities for more than two decades, and the Commission's

²⁵ *BellSouth Petition for Pricing Flexibility for Special Access and Dedicated Transport Services*, Memorandum Opinion and Order, 15 FCC Rcd 24588 (Com. Car. Bur. 2000) *aff'd* 16 FCC Rcd 18174 (2001).

²⁶ *Verizon Petitions for Pricing Flexibility for Special Access and Dedicated Transport Services*, Memorandum Opinion and Order, 16 FCC Rcd 5876, 5881 ¶ 12 (Com. Car. Bur. 2001).

²⁷ *Petition of Ameritech Illinois, Ameritech Indiana, Ameritech Michigan, Ameritech Ohio, and Ameritech Wisconsin for Pricing Flexibility; Petition of Pacific Bell Telephone Company for Pricing Flexibility; Petition of Southwestern Bell Telephone Company for Pricing Flexibility*, Memorandum Opinion and Order, 16 FCC Rcd 5889 (Com. Car. Bur. 2001).

²⁸ *See Policies and Rules Concerning Rates for Competitive Carrier Services and Facilities Authorization Therefor*, Further Notice of Proposed Rulemaking, 84 FCC2d 445,448-55 ¶¶ 11-14,20 n.14 (1981); *Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorization Therefor*, Second Report and Order, 91 FCC2d 59,60-62 ¶¶ 1, 12 (1982). Likewise, Congress has recognized that competition is superior to regulation, requiring the Commission to loosen or eliminate regulation in response to growing competition. *See, e.g.*, 47 U.S.C. § 161 (requiring the Commission biennially to review all regulations issued under the Communications Act to determine if they no longer are necessary due to competition).

special access rules have evolved in light of such competition so as not to “unduly interfere with the operation of interstate access markets as competition developed in those markets.”²⁹ The pricing flexibility rules are intended “to facilitate the *removal* of services from price cap regulation as competition develops in the marketplace,”³⁰ which reflects the Commission’s longstanding recognition that “competition can be expected to carry out the purposes of the Communications Act more assuredly than regulation” ever could and that regulation is therefore appropriate “only where and to the extent that competition remain[s] absent in the marketplace.”³¹ Indeed, as the market continues its more than 20-year trend of becoming increasingly more competitive, “[pricing] constraints become counter-productive.”³²

In a declaration recently submitted by Verizon, Professor Howard Shelanski confirms that “[g]overnment imposed price limits may diminish the incentives for the incumbents or potential challengers to innovate, reduce profit opportunities that attract new entrants, and ultimately entrench both a particular provider and a particular technology in the market, to the detriment of consumers.”³³ Moreover, imprecision in

²⁹ *Special Access Rates for Price Cap Local Exchange Carriers; AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, Order and Notice of Proposed Rulemaking, 20 FCC Rcd 1994, 2001 ¶ 16 (2005) (NPRM).

³⁰ *Ameritech Operating Companies Petition for Pricing Flexibility for Dedicated Transport and Special Access Services*, Order, WBC/Pricing File No. 05-14, DA 05-1525 ¶ 3 (rel. May 25, 2005) (emphasis added).

³¹ *LEC Price Cap Review Order*, 10 FCC Rcd at 8989 ¶ 64.

³² *Pricing Flexibility Order*, 14 FCC Rcd at 14233 ¶ 19.

³³ Declaration of Howard Shelanski at ¶ 4 (attached to Letter from Joseph Jackson, Associate Director, Federal Regulatory to Marlene H. Dortch, Secretary, FCC, WC Dkt. No. 02-112 (Mar. 29, 2007)).

price regulation can have negative effects. Professor Shelanski notes that “[i]n a market moving toward competition... regulated prices that are too high can act as focal points around which market prices cluster,” and “accomplish nothing, except possibly to raise consumer prices, in a market that would otherwise be naturally moving toward competition.”³⁴ As the Commission found in 1992 when it initially provided for CAP interconnection with incumbent LEC facilities, “[e]xcessive constraints on LEC pricing and rate structure flexibility will deprive customers of the benefits of competition and give the new entrants false economic signals.”³⁵

Given the extensive competition in the special access market today, no legal basis exists for the Commission to reverse course by re-imposing archaic regulations that it abandoned years ago. While the Commission has the “theoretical right to modify, or even overrule, long-standing precedents, . . . abrupt shifts in policy do constitute ‘danger signals’ that the Commission may be acting inconsistently with its statutory mandate.”³⁶

Furthermore, re-imposing price regulation on special access services would lack any economic support and would constitute bad regulatory policy. The benefits of a price-regulation scheme are likely to exceed the costs only in the very narrow

³⁴ *Id.*, ¶ 5.

³⁵ *First Expanded Interconnection Order*, 7 FCC Rcd at 7451 ¶ 172.

³⁶ *Office of Communication of the United Church of Christ v. FCC*, 707 F.2d 1413, 1425 (D.C. Cir. 1983) (citing *Joseph v. FCC*, 404 F.2d 207, 212 (D.C. Cir. 1968)); see also *Small Refiner Lead Phase-Down Task Force v. EPA*, 705 F.2d 506, 526 (D.C. Cir. 1983); *Meriden Community Action Agency v. Shalala*, 880 F. Supp. 882, 886 (D.D.C. 1995) (“There is a presumption ‘against changes in current policy that are not justified by the rulemaking record.’”) (quoting *Motor Vehicle Mfrs. Ass’n, Inc. v. State Farm Mutual Auto Ins. Co.*, 463 U.S. 29, 42 (1983)).

circumstance of monopoly or near monopoly conditions.³⁷ The Commission has recognized as much in other contexts. For example, in declining to regulate the broadband market, the Commission noted that it “is still an emerging and changing market, where, as the Commission previously has concluded, the preconditions for monopoly are not present.”³⁸

In the special access services market, there are no monopoly or near-monopoly conditions. As long ago as 1992, the Commission recognized that the structure of the market lent itself to competition, and for over 20 years competitors have been investing in competitive facilities. Competitive choices abound. For example, just one week ago, Level 3 announced that it had deployed nationwide network services, including intercity private line services, to Leap Wireless, a leading provider of wireless communications services.³⁹ The record is replete with other evidence of robust competition in the special access market, as described in greater detail below.

In addition to there being no economic basis to subject the special access market to price regulation, price regulation is likely to cause consumer harm.⁴⁰ One of the

³⁷ See Declaration of Dr. Harold Furchtgott-Roth and Professor Jerry Hausman, at 5-6, WC Docket No. 05-25, RM-10593, Attachment 7 to the Comments of BellSouth Corporation (filed June 13, 2005) (“*Furchtgott-Roth and Hausman Declaration*”); see also Declaration of Howard Shelanski, ¶ 4 WC Docket No. 02-112, submitted on behalf of Verizon (filed March 29, 2007) (noting that “dominant carrier regulation makes sense only in a market where competitive forces ... are unlikely to discipline the ‘dominant’ carrier’s pricing and other practices because the carrier has monopoly power”).

³⁸ *Petitions for Forbearance Pursuant to 47 U.S.C. § 160(c)*, Memorandum Opinion and Order, 19 FCC Rcd 21496, 21505-07 ¶ 22 (2004).

³⁹ Press Release, “Level 3 Provides Nationwide Services to Leap Wireless (July 31, 2007).

⁴⁰ *Furchtgott-Roth and Hausman Declaration* at 9.

primary difficulties with price regulation is determining precisely the correct price, which is all but impossible to do for special access services. If prices are set too high, the result is excess supply and distorted investments. If prices are set too low, the result is shortages and distorted investments.⁴¹ In the long run, no one, including special access customers, benefits from either outcome.

Given “the many unsuccessful examples of price regulation in the 20th century, the use of price regulation in many regulated industries has been in steady decline in the United States—and, in fact, throughout the world, for decades.”⁴² As noted by Dr. Furchtgott-Roth and Professor Hausman, “[a]lthough the FCC appears to have retained much of the same legal authority it once had to regulate strictly interstate and international rates, it has progressively lessened price regulation, including price regulation for special access services. Indeed, it is difficult to find counter-examples where the Commission in the past 30 years has decided to introduce or expand price regulation to a telecommunications service.”⁴³

II. ECONOMIC ANALYSIS AND MARKET FACTS SHOW THAT THERE IS NO BASIS FOR BELIEVING THAT TURNING BACK THE REGULATORY CLOCK WILL BENEFIT CONSUMERS OR COMPETITION.

Various economic indicators and marketplace factors prove that imposing price controls or other market distorting regulatory requirements on special access would harm competition and consumer welfare. Specifically, the evidence shows that special access prices are lower today than they were in 2001, competition for special access services is

⁴¹ *Id.*

⁴² *Id.*

⁴³ *Id.* at 9-10.

robust, and innovation is occurring as new services have been introduced and will be introduced in the near term that compete directly with special access providers.

A. Prices Are Lower Since the Adoption of Pricing Flexibility.

Contrary to the claims of some parties, special access prices have declined in the years since the Commission adopted pricing flexibility. The GAO confirmed this fact in a recent study, noting that “[a]vailable data suggest that incumbents list prices and average revenues for dedicated access services have decreased since 2001” in areas with more traditional and more flexible regulation.⁴⁴ This conclusion is supported by incumbent LEC data. In response to the Commission’s 2005 NPRM in this docket, Verizon noted that “average revenues per special access line, both overall and separately for individual high-capacity special access services, have fallen significantly since the introduction of pricing flexibility.”⁴⁵ SBC has demonstrated that “the average true price to the customer of SBC’s special access services has dropped, not risen as some have alleged, and even base tariff rates in Phase II MSAs are generally no higher today, in nominal terms, than they were in 2001.”⁴⁶

Those arguing for increased regulation do not offer meaningful evidence to refute that special access prices are declining because of flexibility and competition. Indeed, these parties appear simply to want the Commission to guarantee them lower prices than they can obtain in today’s competitive markets. In an effort to support their positions,

⁴⁴ FCC Needs to Improve Its Ability to Monitor and Determine the Extent of Competition in Dedicated Access Services, Government Accountability Office, GAO 07-80, 1 (Nov. 2006) (GAO Report).

⁴⁵ Comments of Verizon, WC Dkt. No. 05-25, 6 (June 13, 2005).

⁴⁶ Comments of SBC, WC Dkt. No. 05-25, 21 (June 13, 2005).

these parties misconstrue pricing information, most notably by pointing to allegedly high “sticker prices” for certain special access services and claiming that these are indicative of rising or unreasonable prices for customers. As these parties surely know, however, base tariff rates are rarely equivalent to what customers actually pay for special access services. In fact, in today’s competitive market, the majority of incumbent LEC special access customers purchase their services under contractual discounts of 40 to 70 percent off the base tariff rate—significant discounts by any measure. Moreover, if any parties truly believe that special access rates are unjust or unreasonable, they can challenge those rates before the Commission under Section 208 of the Communications Act.⁴⁷

B. Special Access Competition is Robust.

By any measure, special access competition is robust and has indisputably and substantially increased since 1999, when the Commission adopted pricing flexibility. Time Warner Telecom provides a good example. At the beginning of 1999, Time Warner Telecom claimed that it had fewer than 7,000 route miles of (local and long-haul) fiber and about 4,300 “lit” buildings in 19 metropolitan areas.⁴⁸ Today, Time Warner Telecom has more than 7,600 lit buildings, a number that grew 24 percent since first quarter 2006,⁴⁹ and it has over 18,000 miles of local fiber in more than 70 markets.⁵⁰ In some

⁴⁷ 47 U.S.C. § 208 (2006).

⁴⁸ Time Warner Telecom LLC, Form 10-K, For The Fiscal Year Ended Dec. 31, 1998, at 4.

⁴⁹ See Press Release, *Time Warner Telecom Reports Solid First Quarter 2007 Results*, May 2, 2007, available at <http://www.twtelecom.com/Documents/Announcements/News/2007/TWTCQ107PressRelease.pdf>.

areas, Time Warner Telecom has apparently amassed more lit buildings than any other competitive provider.⁵¹ Time Warner Telecom bills itself as “*the leading provider of metro area broadband optical networks and services to businesses ... deliver[ing] ‘last-mile’ broadband data, voice, Dedicated Internet Access, and Dedicated Web Hosting in 44 major U.S. markets,*”⁵² including Atlanta where Time Warner has announced plans to expand its metro fiber network, enabling it to offer “communications solutions to more than 6,000 additional businesses located in the Atlanta area,”⁵³ and Silicon Valley, where it recently completed a 480-mile fiber ring.⁵⁴

Other competing LECs have been similarly expanding their local networks in recent years. For example, Level 3 has continued to invest in the acquisition of several network operators including Progress, ICG, TelCove, Looking Glass Communications, and Broadwing. Today, Level 3 has approximately 6,700 lit buildings and 25,000 metro

⁵⁰ See *id.* at 13; Time Warner Telecom, *2006 Annual Report*, at 10, available at http://www.twtelecom.com/Documents/Announcements/Financial_Docs/2005/TWTC_04AR.pdf.

⁵¹ Reply Comments of BellSouth, *In re Special Access Rates For Price Cap Local Exchange Carriers*, WC Docket No. 05-25, Declaration of Stephanie Boyles at 5 (July 29, 2005).

⁵² See <http://www.twtelecom.com/Documents/Announcements/News/2006/Overture.pdf> and <http://www.twtelecom.com/Documents/Resources/PDF/MarketingCollateral/2701NativeLan.pdf> (emphasis added).

⁵³ Press Release, *Time Warner Telecom Extends Atlanta Fiber Network*, Jan. 20, 2006, available at http://www.twtelecom.com/Documents/Announcements/News/2006/Atlanta_Extension_Final_1_06.pdf.

⁵⁴ Press Release, *Time Warner Telecom Completes its 480-Mile Fiber Network Ring for Businesses in Silicon Valley*, Sept. 12, 2006, available at http://www.twtelecom.com/Documents/Announcements/News/2006/Bay_Area_Expansion.pdf.

fiber miles in North America.⁵⁵ Most significantly, Level 3 promotes its intent to continue to expand its metro network and building connections.⁵⁶ “By constructing our network and over 650 laterals, Level 3 *is an undisputed expert in off-net lateral construction*. Last year, Level 3 delivered 200 customer construction projects with an on-time delivery rate of greater than 95 percent.”⁵⁷ Level 3 advertises that “[i]f we don’t already have your requested buildings On-Net, our large footprint is likely to put you close for a lateral.”⁵⁸ Sophisticated companies such as Time Warner Telecom and Level 3 do not make such substantial network investments unless they firmly believe they can be successful and obtain a significant return. Such actions are further evidence of the continuing success of competing LEC fiber operations and the increasing competitiveness of the special access market.

In addition to competition from competing LECs, incumbent LECs face widespread and growing intermodal competition for special access services. Unlike in 1999, all of the major cable operators now serve business customers using their ubiquitous networks. For example, Cox Communications offers its “Transparent LAN Service” at speeds from 1.0 Mbps up to 1.0 Gbps over its fiber and hybrid fiber coaxial

⁵⁵ Network Metrics, Level 2, *at* http://www.level3.com/about_us/aboutlevel3network/network_metrics.html.

⁵⁶ Level 3 Communications, SEC 10-K Filing, at 5 (Mar. 1, 2007).

⁵⁷ See <http://www.level3.com/2700.html> (emphasis added).

⁵⁸ See http://www.level3.com/userimages/DotCom/pdf/offnlateral_useng_global_letter_forscreen.pdf (emphasis added).

network.⁵⁹ Cox has added at least 40,000 business customers since 2003 and a total of 140,000 customers in 2005.⁶⁰ While it has traditionally focused on small and mid-sized business customers, Cox is increasingly targeting larger customers.⁶¹

Unlike in 1999, Time Warner Cable now actively competes for large business customers as well, highlighting its expertise in establishing Metro Ethernet networks within the states in which it has a presence. Time Warner Cable's broadband network offerings feature point-to-point connectivity, point-to-multipoint connectivity, teleworker aggregation, or Internet access to business customers.⁶² Time Warner Cable has aggressively targeted enterprise customers, especially through a variety of Ethernet business services, such as private line, private LAN, and broadband Internet connections. Time Warner Cable's products take advantage of its extensive metropolitan fiber networks, which are independent of existing telecom providers.⁶³ Some of its products, such as new storage solutions, cater to the specific disaster recovery needs of the financial sector.⁶⁴ Time Warner Cable provides service to approximately 500 enterprise

⁵⁹ Information Sheet, Cox Transparent LAN, available at <http://www.coxbusiness.com/products/data/transparentlan.html>.

⁶⁰ See Not Just TV: Cable Competes for the Office Domain, N.Y. Times, Sept. 27, 2005, reprinted at <http://www.coxbusiness.com/pressroom/recentmedia/09-27-05-nytimes.html>.

⁶¹ See Press Release, Cox Business, Cox Enterprise Presents Even "Bigger" Opportunity for Cox Business Services in 2004 (Mar. 29, 2004), available at <http://www.coxbusiness.com/pressroom/pressreleases/2004-0329.html>.

⁶² Time Warner Cable: Products and Solutions: Enterprise Technology, available at <http://www.twcbroadband.com/solutions/enterprise.cfm>.

⁶³ International Telecommunications, Intelligence Telecommunications, ESPICOM Business Intelligence Ltd. (Feb. 8, 2005.) ("Time Warner Cable of New York and New Jersey offers Optical Ethernet and Storage Services using Nortel Solutions.").

⁶⁴ *Id.*

customers, and the company claims a total of over 211,000 business customers as of the fourth quarter 2005.⁶⁵ Time Warner Cable and other cable operators are increasingly seen by industry analysts as viable competitors for business customers.⁶⁶

In addition to intermodal competition, other carriers increasingly are using broadband wireless to compete for special access services. First Avenue Networks is one such company offering “[h]igh capacity services (TDM, ATM, or Ethernet) up to 600 Mbps and beyond.”⁶⁷ The company specifically markets itself to enterprise service providers, enabling them to access “the ‘un-served’ ... enterprises that can’t get high capacity services because their buildings lack fiber.”⁶⁸

Recent statements by competing LECs confirm that competition for special access services remains fierce. For example, XO recognizes that the “telecommunications services market is *highly competitive* and continues to experience *downward pricing pressure*.”⁶⁹ Cbeyond Communications confirms this analysis, stating, “we anticipate

⁶⁵ Press Release, Time Warner Cable, Road Runner Business Class Further Penetrating Growing Business Market With Customized Offerings (July 8, 2004), *available at* <http://www.timewarnercable.com/InvestorRelations/PressReleases/TWCPressReleaseDetail.aspx?PRID=139&MarketID=0>; Press Release, Strong Continued Customer Growth for Time Warner Cable Business Services (Feb. 8, 2006), *available at* <http://www.rrbiz.com/RoadRunner/docs/2000/1955.pdf>.

⁶⁶ *See, e.g.*, Brian Santo, “The Commercial Services Market,” *CED Magazine* (Oct. 2006) (noting that cable operators’ share of the business market is projected to grow from \$1.1 billion in 2004 to \$10.7 billion in 2009), *available at* <http://www.cedmagazine.com/article/CA6366119.html>.

⁶⁷ Information Sheet, Enterprise Services, Wireless Acc4ess, *available at* <http://www.firstavenet.com/interior.php?sections=EnterpriseServices&subsection=WirelessAccess1>.

⁶⁸ *Id.*

⁶⁹ XO Holdings, Inc., Form 10-K at 4 (Mar. 16, 2006) (emphasis added).

that *aggressive price competition will continue.*⁷⁰ Time Warner Telecom has observed that incumbent LECs have originated much of this increased competition for enterprise business: “We believe that the ILECs have become more *aggressive in pricing competition* With several facilities-based carriers providing the same service in a given market, price competition is likely to continue.”⁷¹

C. New Services Are Being Introduced.

In addition to intermodal competition, incumbent LECs face increasing competitive pressure from carriers using new technologies, including wireless solutions, to compete for special access services. FiberTower Corporation, formerly First Avenue Networks, is one such company offering “backhaul and access services to government and enterprise markets.”⁷² The company specifically markets itself as an alternative to incumbent LEC services, noting that it can “solve[] the access bottleneck by delivering high capacity services to enterprises located in both on-net and off-net buildings”⁷³ and that its fiber and wireless network “delivers the coverage, capacity and service quality that carriers, enterprises and government agencies demand to upgrade their business

⁷⁰ Cbeyond Communications, Inc., Form 10-K at 29 (Mar. 31, 2006) (emphasis added).

⁷¹ Time Warner Telecommunications, Inc., Form 10-K at 13 (Mar. 16, 2006) (emphasis added).

⁷² Press Release, *FiberTower Reports First Quarter 2007 Results* (May 8, 2007), available at http://www.firstavenet.com/corp/downloads/press_releases/FT_Q107_Earnings_Release.pdf.

⁷³ FiberTower Corporation, Access at <http://www.firstavenet.com/corp/solutions-access.shtml> (last visited Aug. 3, 2007).

operations.”⁷⁴ XO Communications also recently announced that it “has deployed fixed broadband wireless in nine metropolitan markets – Atlanta, Chicago, Dallas, Houston, Los Angeles, Miami, San Diego, Tampa, and Washington, D.C.,” and that “[i]n addition to expanding our [XO’s] network ... [increased facilities] also gives us a more cost-effective and scalable replacement to leased network elements that connect local switches to our own fiber network.”⁷⁵ XO explains that its broadband wireless services will enhance its ability “to deliver business-class broadband solutions directly to businesses and help reduce local network costs.” It specifically mentions that it will target businesses that “lack direct access to fiber,”⁷⁶ and it can serve any building that is within five miles line-of-sight of its wireless hubs that are broadly deployed across these metropolitan areas.⁷⁷ Moreover, even more competition for special access services is on the horizon. Recently, Sprint Nextel and Clearwire announced a partnership to accelerate the

⁷⁴ FiberTower Corporation, Setting New Standards in Backhaul and Access Services, at <http://www.firststavenet.com/corp/solutions.shtml> (last visited Aug. 3, 2007).

⁷⁵ See, Press Release, *XO Communications Deploys Fixed Broadband Wireless in Nine Cities to Expand Metro Coverage and Reduce Network Access Costs* (August 28, 2006), available at <http://www.xo.com/news/316.html>.

⁷⁶ *Id.*

⁷⁷ These market developments confirm the Commission’s prior findings that broadband wireless increasingly represents a meaningful competitive alternative to special access. See, e.g., *Applications of Nextel Communications, Inc. and Sprint Corporation For Consent to Transfer Control of Licenses and Authorizations*, Memorandum Opinion and Order, 20 FCC Rcd 13967 (2005) (“we expect that this spectrum may be used to provide fixed or portable wireless broadband services (e.g., Wi-Max type services) that will provide alternative service platforms for last mile services to residence and businesses”); *Availability of Advanced Telecommunications Capability in the United States*, Fourth Report to Congress, 19 FCC Rcd 20540, 20561 (2004) (“[t]he major upperband carriers, such as Teligent and XO Communications, have begun to focus on providing backhaul transport and private line telecommunications services to other carriers and large businesses”).

deployment of a nationwide mobile WiMAX network operating at speeds at least “five times faster than today’s third generation wireless networks at lower cost.”⁷⁸

The facts demonstrate that competition in the special access market from competing LECs, cable, and wireless is robust and increasing. Such competition is the result of the Commission’s market-oriented policies and is the reason that the Commission must not turn its back on those policies by re-regulating special access.

III. USE OF ARMIS DATA IS MISLEADING.

Competing LECs are basing their calls for lower prices on Automated Reporting Management Information System (ARMIS) data. These are some of the same carriers that have recognized the market as characterized by aggressive price competition. The Commission should not rely on accounting data that was never intended to be used to measure rates of return on individual services. ARMIS was created to provide the Commission with a generalized overview of the industry before price cap regulation—not to measure service-specific rates of return under price cap regulation. Indeed, the Commission has rejected use of ARMIS data for this purpose, and it would be a mistake for the Commission to assess competition in the special access market based on such unreliable measures.

⁷⁸ Press Release, Sprint Nextel and Clearwire to Partner to Accelerate and Expand the Deployment of the First Nationwide Mobile Broadband Network Using WiMAX Technology, Press Release, *available at* http://www2.sprint.com/mr/news_dtl.do?id=17520 (July 19, 2007).

A. ARMIS data is not reliable for measuring service-specific profits, and, therefore, ARMIS data is not useful for setting just and reasonable rates.

As the Commission itself has recognized, it is questionable to rely on accounting rate of return data to draw conclusions about market power.⁷⁹ ARMIS was not designed to accurately measure service-specific rates of return under price cap regulation. In fact, the basket for special access services in ARMIS sweeps in a number of services, including voice grade, WATS, metallic, and telegraph special access services, audio and video services, high-capacity special access services, and wideband data and analog services.⁸⁰ The Commission recognizes, “High or increasing rates of return calculated using regulatory cost assignments for special access services do not in themselves indicate the exercise of monopoly power.”⁸¹ ARMIS should not, therefore, be used as evidence of supposedly excessive returns in order to reduce special access rates.

The Commission has recognized that the existing separations rules do not produce meaningful and reliable allocation results for measuring rates of return. The cost allocation process involves multiple stages of activity that require companies to make numerous determinations about proper cost allocations. These determinations include allocations between regulated and unregulated accounts, between interstate and intrastate jurisdictions, and for interstate regulated costs, further apportioning occurs among interexchange services and rate elements. Moreover, this allocation methodology produces numerous and significant “downstream” impacts as allocations are applied to

⁷⁹ NPRM ¶ 129.

⁸⁰ *Id.* ¶ 48, n. 144.

⁸¹ *Id.* ¶ 129.

other cost categories such as allocations of general support facilities and general support expenses. In the end, the amounts allocated to interstate special access represent the sum of all imprecise allocations, and therefore should not be used for any rate setting purposes.

The separations freeze that the Commission put in place in 2001 further distorts the reporting of special access earnings. The Commission acknowledges that its “cost allocation rules and factors...may undermine the usefulness of examining rates of return derived from ARMIS data.”⁸² By freezing allocation factors so they do not account for changes in the way costs are incurred, a material mismatch between costs and revenues is produced. In the case of special access this is particularly pronounced as the number of special access lines have grown significantly along with company revenues. The costs, however, have not been adjusted in the past eight years to reflect the growth in special access services and the declines in switched access. As a consequence, the reported returns associated with special access are neither reliable nor meaningful.

B. There is no credible evidence that current rates are not just and reasonable.

To date, no participant in this proceeding has provided evidence that even remotely suggests that the rates actually being paid for special access services are unjust or unreasonable. This is not surprising, since incumbent LECs could hardly extract monopoly rents for special access services when competitors are determined to win customers and build market share. In such a market, prices are carefully calibrated to ensure that customers are retained so that contribution to high fixed-cost related

⁸² *Id.* ¶ 61.

investments are not diminished. Furthermore, gouging customers when competitors have been building facilities for over 20 years and at a time when new entrants utilizing new access technologies are emerging on the scene would not constitute a particularly productive market strategy.

IV. THE COMMISSION DOES NOT HAVE THE INFORMATION IT NEEDS TO IMPOSE STRICTER PRICING REGULATIONS.

The special access services market is competitive—with prices going down and investment going up. Before the Commission could even consider acting on the recommendations of competitors in this proceeding to re-impose stricter pricing regulations, it would need a complete record of prices charged by competing LECs and others for their special access services. Commercial mobile radio service providers, interexchange carriers, competing LECs, cable operators, and other providers that offer special access services as a key part of many of their respective service offerings, but they are not required to report price data to the Commission. Furthermore, although many of them contract to provide wholesale special access services to other carriers and readily reveal their network and building locations in commercial contexts, they enforce non-disclosure agreements that prevent this data from coming to light in regulatory proceedings. And they are not forthcoming with the information when asked. The GAO has asked competitive companies how much they charge for their special access services, but has been unable to collect price data: “We asked competitive firms to supply prices, however, they did not.”⁸³ Competitors would provide only anecdotal information about their prices. The GAO concluded that competing providers could not provide it with the

⁸³ GAO Report at 59.

information it needed to properly assess the market for its study. Until there is data for a complete picture of the special access market, the Commission cannot possibly re-impose stricter pricing regulations.

V. THE COMMISSION SHOULD UPDATE PRICING FLEXIBILITY RULES.

Given the eight years since the *Pricing Flexibility Order* and the competitive state of the market, the Commission should update its pricing flexibility rules by extending Phase I pricing flexibility to all carriers so they have the freedom to reduce prices and aggressively compete. There is no downside to this. Phase I simply allows incumbent LECs to negotiate contract tariffs that invariably result in lower prices, as no provider contracts to pay higher prices. Moreover, under Phase I, price cap rates remain as a backdrop. As Cbeyond Communications and others have recognized, aggressive price competition will continue. If pricing flexibility is not granted to all carriers, the result will be artificial prices and consumer harm. In addition, the Commission should update Phase II criteria to reflect competition from cable and fixed wireless providers that do not typically co-locate the way fiber-based competitors typically do and to allow carriers to prevent evidence of extensive fiber facilities that may not be collocated in incumbent LECs' central offices.

VI. CONCLUSION

Competition in the special access services market robust. Competing LECs themselves confirm that competition for special access is fierce and that they continue to experience downward pricing pressure. Incumbent LECs face widespread and growing intermodal competition from competitive LECs, cable operators, and providers of

broadband wireless services and increasing competitive pressure from carriers using wireless solutions and other new technologies. Such competition is the result of the Commission's pro-market policies. In the face of competition and market-driven outcomes, the Commission should continue its pro-competitive policy of pricing flexibility.

Respectfully submitted,

UNITED STATES TELECOM ASSOCIATION



By: _____

Jonathan Banks
Robert H. Mayer
Indra Sehdev Chalk

Its Attorneys

607 14th Street, NW, Suite 400
Washington, DC 20005
(202) 326-7300

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