

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

In the Matter of)
)
Petition of Verizon for Forbearance Under)
47 U.S.C. § 160 from Enforcement of)
Certain of the Commission's)
Recordkeeping and Reporting)
Requirements)
_____)

WC Docket No. 07-273

Reply Comments of BT Americas Inc. on Behalf of Itself and Other BT Entities

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Pursuant to the Commission’s Public Notice,¹ BT Americas Inc., a wholly owned indirect subsidiary of BT Group plc (“BT plc”), submits these Reply Comments on behalf of itself and other BT operating entities in the US (collectively referred to herein as “BT”)² opposing Verizon’s petition for forbearance from the reporting and recordkeeping requirements:³ (1) of the Automated Reporting and Management Information System (“ARMIS”) and “rate of reporting” rules;⁴ (2) the Commission’s affiliate transaction rules;⁵ and (3) the Property record

¹ DA 07-5034 (December 18, 2007).

² BT holds section 214 licenses and employs approximately 4000 people in the United States. BT, through the Global Services group, serves the global information and communications technology needs of large business (“enterprise”) customers worldwide.

³ Verizon also seeks to have the Commission preempt state recording keeping and reporting requirements, Verizon Petition at 5. See generally, Joint Comments and Opposition of the New Jersey Division of Rate Counsel and the National Association of State Utility Consumer Advocates (Feb. 1, 2008) (“State Advocates’ Comments”).

⁴ 47 C.F.R. §§ 1.795, 65.600, 69.301-10 and 69.401-15. Verizon Petition at 11-12 and 29-30. This includes ARMIS Report 43-01 (Annual Summary); ARMIS Report 43-02 (Uniform System of Accounts); ARMIS Report 43-03 (Joint Cost Report); ARMIS Report 43-04 (Separations and Access Report); ARMIS 43-05 (Service Quality Report); 43-06 (Customer Satisfaction report); ARMIS Report 43-07 (Infrastructure Report); ARMIS 43-08 (Operating Data Report); ARMIS Report 495A (Forecast of Investment Usage); ARMIS Report 495B (Actual Usage of Investment); and 492A Report (Rate-of-Return Monitoring Report). As noted in Sprint Nextel Corporation’s Comments in Opposition to Verizon’s Petition for Forbearance From Enforcement of Certain of the Commission’s Recordkeeping and Reporting Safeguards (Feb. 1, 2008) (“Sprint/Nextel’s Comments”) at 2, what Verizon denotes as the “rate of return reporting rules” is “more accurately categorized as part of the Commission’s cost assignment rules for apportioning investment and expenses to access elements, including common line, traffic sensitive and special access.”

rules.⁶ These rules and reporting requirements are essential for the Commission to make informed decisions about the extent to which it can deregulate critical telecommunications services.

INTRODUCTION AND SUMMARY

The rules and reporting requirements as to which Verizon seeks forbearance are critical in those segments of the marketplace, such as special access, where the record shows the incumbents have profound market power. Verizon fails to distinguish between the consumer and business markets when claiming that local markets are competitive. The special access market, essential to enterprise business customers and wholesale purchasers who seek to serve those customers, is not competitive.

The data generated as a result of compliance with these rules and reporting requirements are critical for meaningful oversight of the special access market by the Commission. The U.S. Government Accountability Office noted in its recent report on Special Access that the ARMIS reports on “general rates of return as well as specific revenue figures and line counts for the last mile connections per incumbent” (which are some of the reports as to which Verizon seeks forbearance) are the only “publicly available” “major source of data that FCC uses to gauge competition in the markets for dedicated access services.”⁷ Indeed, retail and wholesale purchasers of special access in the U.S., who have been the victims of excessively high prices, refusals to provide inputs for new access services such as Ethernet, and “lock-in” “discount”

⁵ 47 C.F.R. §§ 32.27 and 32.23, 64.902-64.904, 43.21 (d-k) and 47 U.S.C. §254k (Universal Service).

⁶ *Id.*, §§ 32.2000 (e)-(f) and 32.11.

⁷ U.S. Government Accountability Office, Report to Chairman, House Committee on Government Reform, *FCC Needs to Improve its Ability to Monitor and Determine the Extent of Competition in Dedicated Access Services*, GAO 07-80 (November 2006) at 38 <http://www.gao.gov/new.items/d0780.pdf> (“GAO Report on Special Access”).

plans,⁸ have relied heavily on ARMIS data to develop the record in the various iterations of the still unresolved *Special Access Proceedings*⁹ showing that the Bell Operating Companies (“BOCs”), including Verizon, have overwhelming market power in the special access market.¹⁰ And one Commissioner has suggested that there will be yet another refresh of the record in that proceeding.¹¹ And it is clear that Verizon in this proceeding would like to eliminate this “major source of data” to frustrate any effort to demonstrate that BOC rates of return, already calculated on the basis of ARMIS data as ranging from 52% to 132% in 2006¹² have increased even more.¹³

It is clearly in the public interest to require Verizon and the other incumbent Local Exchange Carriers (“ILECs”) to report this data. The most recent European Competitive

⁸ As to Verizon’s plans, *see, e.g.* Comments of CompTel/ALTS, Global Crossing North America, Inc., and NuVox Communications WC Dkt. No. 05-25 (June 13, 2005) at 19-20; *Ex parte* letter from A. Richard Metzger, Jr, Lawler, Metzger & Milkman, LLC on behalf of MCI to Marlene H. Dortch, Secretary, Federal Communications Commission, RM 10593 (June 30, 2004) at 9-10.

⁹ The original petition was filed in 2002, AT&T Corp, Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services, RM No 10593 (Oct. 15, 2002). In the face of a petition for mandamus, AT&T Corp et al, Petition for a Writ of Mandamus, DC Circuit Case No 03-1397, the Commission issues a Notice to refresh the record in 2005, In the Matter of Special Access Rates for Price Cap Local Exchange Carriers, Order and Notice of Proposed Rulemaking (31 January 2005) WC Docket No 05-25 (“2005 Refresh of the Special Access Proceeding”). The Commission again took no action until pressured by Congress, and again issued a Notice to refresh the record in 2007, In the Matter of 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, WC Docket No 05-25, RM-10593 (released 9 July 2007) but once again took no action.

¹⁰ *See* note 23 *infra*.

¹¹ Petition of AT&T Inc. for Forbearance Under 47 U.S.C. § 160(c) from Title II and Computer Inquiry Rules with Respect to Its Broadband Services; Petition of BellSouth Corporation for Forbearance Under Section 47 U.S.C. § 160(c) from Title II and Computer Inquiry Rules with Respect to Its Broadband Services, Memorandum Opinion and Order, FCC 07-180 (rel. October 12, 2007) (“*AT&T Broadband Forbearance Order*”) Statement of Commissioner McDowell (“many parties allege that competition in the special access market is uneven and is limited to certain urban areas, thus creating supply bottlenecks that favor incumbent local exchange carriers in the business broadband and wireless markets. Despite requests for better data to help us resolve disputes of these material facts, the Commission still has inadequate information to determine whether allegations that competition is scarce in certain segments of the special access market have merit. I will continue to work to ensure that these questions are explored further in the Special Access proceeding after a more granular record has been established through detailed mapping of business broadband facilities”).

¹² Comments of AdHoc Telecommunications User Committee (“AdHoc’s Opposition”) CC Docket no. 05-25, (Aug. 8, 2007) at 5-6.

¹³ In each refresh of the record in the special access proceeding, the rates of return have increased. For example, the rates of return in 2001 ranged from 21.72%, to 54.6%. Declaration of M. Joseph Stith submitted with AT&T’s Petition in *AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM No. 10593 (“*Special Access Proceeding*”) (Oct. 15, 2002).

Telecommunications Association (ECTA) annual benchmark of 19 European countries showed that the countries with the “lowest prices and highest investment” were those where cost accounting, comparative quality data, and more general data on infrastructure were made available to regulators and the public. New Zealand similarly found itself “slipping behind its OECD peers in broadband services” until it imposed such rules and reporting requirements.

ARGUMENT

Section 10 of the Act provides that the Commission “shall forbear from applying any regulation or provision” if it determines that:

- (1) enforcement of such regulation or provision is not necessary to ensure that the charges, practices, classifications, or regulations by, for, or in connection with that telecommunications carrier or telecommunications service are just and reasonable, and are not unjustly or unreasonably discriminatory;
- (2) enforcement of such regulation or provision is not necessary for the protection of consumers; and
- (3) forbearance from applying such provision or regulation is consistent with the public interest.¹⁴

In evaluating the public interest, the Commission must ask whether forbearance “will promote competitive market conditions.”¹⁵ However, “... the Commission may not forbear from applying the requirements of section 251(c) or 271 ... until it determines that those requirements have been fully implemented.”¹⁶

As shown below, the reporting requirements and regulations as to which Verizon seeks forbearance are essential to monitoring whether Verizon’s special access rates are unjust and unreasonable and whether Verizon is engaging in improper cost-shifting. Granting Verizon’s forbearance requests will harm consumers and not be in the public interest, because it denies the

¹⁴ 47 U.S.C. § 160(a).

¹⁵ *Id.*, § 160(b).

¹⁶ *Id.*, § 160(d).

Commission and the public¹⁷ data they need to evaluate market performance. Experience outside the United States demonstrates that the availability of such data in comparable markets promotes competitive pricing and innovative investment.

I. VERIZON’S FORBEARANCE PETITION SEEKS TO WITHHOLD CRITICAL INFORMATION AND REGULATORY PROTECTIONS NECESSARY TO PROTECT THE PUBLIC

A. The Data and Regulations Are Critical Because There is Demonstrated Market Failure in the Special Access Market

1. There is A Need to Evaluate Competition in the Business Market Separately from the Residential Market

The Commission needs to distinguish between mass market (residential/small business) customers on the one hand and large (enterprise) business customers on the other. While there may be more competition, and hence more choices available, for some segments of the mass market, that does not mean that there is effective competition in the enterprise business market.

The Commission has recognized that the enterprise market, at least on the retail level, is a discrete market segment.¹⁸ Application of traditional market definition principles¹⁹

¹⁷ Verizon’s assertion that “while consumers are theoretically able to monitor trends based on the information contained in the ARMIS reports, such data are technical in nature *and not understood by consumers*” Verizon Petition at 15 (emphasis added) is wrong. First, the Notice of Proposed Rulemaking, *In the Matter of the 2000 Biennial Regulatory Review – Telecommunications Service Quality Reporting Requirements*, 15 FCC Rcd. 22113 ¶ 14 (2000) from which Verizon paraphrases this quote actually says “may not be easily translated by consumers.” “Consumers” include residential consumers and business consumers. The filings in the *Special Access Proceedings* by e.g. American Petroleum Institute in CC WC Docket No. 05-25 & RM No. 10593 on June 14, 2005 (Comments in the 2005 Refresh Proceeding) and on August 2, 2005 (Reply Comments) and AdHoc’s August 8, 2007 Comments in the 2007 refresh proceeding, n. 12 *supra* demonstrate that large enterprise business customers certainly understand this data. So can other consumers, *see e.g.*, the ex parte filed by the Consumers Union in WC Docket No. 05-25 & RM No. 10593 (Oct. 4, 2007).

¹⁸ *See, e.g., In re Application of SBC Commc’ns Inc. & AT&T Corp.*, Memorandum Opinion and Order, WC Dkt. No. WC Dkt. No. 05-65, FCC 05-183 (Nov. 17, 2005) (“*SBC/AT&T Merger Order*”) ¶ 58.

¹⁹ Applying such a rigorous analysis, supported by evidence, is essential for a reasoned decision compliant with due process and the Administrative Procedure Act, 5 USC §556(d) (agency action must be supported by “reliable, probative, and substantial evidence”) and consistent with the Commission’s obligation under *Section 1.1* of the WTO Reference Paper, GATS/SC/90/Suppl.2, 11 April 1997, which provides that “appropriate measures shall be maintained for the purpose of preventing suppliers who, alone or together, are a major supplier from engaging in or continuing anti-competitive practices.” Yet such an analysis may not have been used by the Commission in its *AT&T Broadband Forbearance Order*, Memorandum Opinion and Order, FCC 07-180 ¶¶ 20 (“it is appropriate for us to look more broadly at competitive trends without regard to specific geographic markets”) and 23 (“We

demonstrates that there is a discrete market for access to be supplied to enterprise customers, separate and apart from the mass market.

The nature of the two markets is fundamentally different. Mass market customers need access connectivity to a single location. Large multi-site enterprise business customers need “universal connectivity” to all their sites, including not only sites in Central Business Districts, but more often, due to lower labor and land costs as well as for tax reasons, in suburban, exurban and even rural areas. And this “multi-site requirement” includes access for remote workers. A supplier must be able to provide connectivity at the right speeds and at the right level of security to *all* of the enterprise customer’s sites if the supplier is to successfully compete for its business.

The conditions of competition for supply of businesses in the U.S. are different from the supply of mass market services. Last mile access to business customers outside of central business districts, *i.e.* to the vast bulk of sites, is usually only possible from one incumbent supplier. The BOCs dominate the business access market.²⁰ Thus, the United States Government Accountability Office recently found that competitors provide access service to only 6% of business customer sites for services at 2 Mbps and 15 to 25% of sites for services at 45 Mbps and above.²¹

recognize that the record in this proceeding does not include detailed market share information for particular enterprise broadband services ... we do not find it essential to have such detailed information”).

²⁰ Despite what the Commission wrote in the *AT&T Broadband Forbearance Order* ¶24, enterprise customers do not have effective “countervailing buyer power” for at least three reasons. First, even strong buyers may be relatively small purchasers in particular (geographic and/or product) markets. Second, the cost of the product or service may be a relatively insignificant part of the overall cost of the end product, and the strong buyer, for strategic reasons, may not have the incentive to exercise any countervailing market power that it may have. Finally, dominant undertakings have strategies to minimize buyer power, including the conditional rebate strategy. Such rebates could be used to lock in sufficient demand so that remaining providers could not realize minimum economies of scale and scope. Thus strong buyers could not exercise any countervailing power by threatening to take their business elsewhere or to self-provision.

²¹ GAO 07-80 Telecommunications. FCC needs to improve its ability to monitor and determine the extent of competition in dedicated access services, p.20 (November, 2006).

2. There is No Meaningful Competition in the Business Market

Contrary to Verizon's assertions, the special access market, essential to enterprise business customers and to wholesale providers seeking to serve those customers, is not competitive.²² To the contrary, prices are excessive.²³ ARMIS data submitted in the *Special Access Proceeding* showed that Verizon's rate of return, which was 23.2% when the record was first developed in 2003,²⁴ had jumped to 52% in 2006 when the record was last refreshed.²⁵

As BT and others demonstrated in the *Special Access Proceedings*, there is no meaningful intramodal competition,²⁶ and indeed Verizon does not argue that such competition exists. Verizon instead argues that there is inter-modal competition for "consumers" from "cable companies, wireless carriers and Voice over Internet Protocol ("VoIP") providers" without distinguishing between residential and business services.²⁷ In fact, there is no meaningful cable competition for access services in the *enterprise* market because cable operators are focused on

²² Verizon's Petition at 2 ("vibrantly competitive"), 4 ("vigorously competitive" "robust choice of service from a variety of competing providers") and 13 ("robust competition").

²³ Contrary to Verizon's assertions in its petition at 4, 14 and 24, price caps do not protect consumers from excessive pricing or price squeezes. *See generally*, AdHoc's Opposition at 6-9.

²⁴ Declaration of Susan Gately on behalf of AdHoc Telecommunications Users Committee, WC Docket No 05-25, RM-10593 ¶ 9 (August 8, 2007) (or two times the FCC authorized rate of return of 11.25%).

²⁵ *Id.* ¶ 9

²⁶ *E.g.* BT's Reply Comments in the most recent Special Access Refresh Proceeding, WC Docket No 05-25, RM-10593 (filed on August 15, 2007) at 4-5 (showing that there is no meaningful competition from the CLECs or the BOCs. The CLECs with the greatest potential for succeeding, AT&T and MCI, were acquired by the BOCs. The other national or regional competitive carriers were, or are, being driven out of the market, unable to achieve minimum scale as a result of the BOCs "lock-in" long term "discount" bundled plans and other onerous conditions. There is also no meaningful intra-modal competition from the better financed BOCs. AT&T's filings in the BellSouth merger in 2006 demonstrated that eight years after SBC had adopted an "aggressive" strategy to enter 30 out-of-region markets as a facilities-based competitor, *Application of SBC Communs. & Ameritech Corp. for Transfer of Control to SBC Communications*, CC No. 98-141 (July 24, 1998) at 17, and even after it had acquired AT&T Corp's national "fiber rich, POP rich" facilities, it was still a meaningless special access competitor outside its region. As to Verizon, *see Applications of GTE Corp., Transferor, and Bell Atlantic Corp., Transferee, For Consent to Transfer Control of Domestic and International Sections 214 and 310 Authorizations and Application to Transfer Control of a Submarine Cable Landing License*, CC Docket No. 98-184 (Dec. 30, 1998) (Bell Atlantic's similar announcement of its intent to enter as a facilities-based carrier out-of-region).

²⁷ Verizon's Petition at 3 and 5-8.

shoring up their residential services against emerging competition with the incumbent BOCs and they do not have sufficient additional capacity to serve the business market as well.²⁸

Verizon's claims as to the viability of wireless, WiFi and WiMax to compete with special access, in light of those wireless technologies bandwidth, service quality and reliability constraints are also wildly overstated. Wireless broadband has not emerged as a meaningful competitive alternative and in any event the incumbent wireline broadband access providers control the U.S wireless market.²⁹ Wi-Fi and WiMax don't have the bandwidth, service quality or reliability required for enterprise network services.³⁰ Verizon's positioning of VoIP (which is in any event not an access technology) as an independent source of competition is particularly ironic in light of the recent judicial developments in *Verizon Services Corp. v. Vonage Holdings Corp.*, where a jury found that Vonage infringed three Verizon patents relating to VoIP.³¹ If

²⁸ See the report by Heavy Reading (Sterling Perrin), *Cable vs. Telcos: The Battle for the Enterprise Market* ("Cox Communications Inc. ... regarded as the most aggressive MSO in the space yet makes only 6 percent of its revenue there" and that includes all business customers, including small and medium businesses). http://www.lightreading.com/document.asp?doc_id=89210. See, http://goliath.ecnext.com/coms2/gi_0199-5228147/Cable-Operators-May-Miss-a.html (Feb. 15, 2006). The Executive Summary and Table of Contents of this Report can be found at, <http://translate.google.com/translate?hl=en&sl=ja&u=http://www.dri.co.jp/auto/report/hr/hrcvst06.htm&sa=X&oi=translate&resnum=7&ct=result&prev=/search%3Fq%3DHeavy%2BReading%2B%252B%2B%25E2%2580%259CCable%2Bvs.%2BTelcos%2BThe%2BBattle%2Bfor%2Bthe%2BEnterprise%2BMarket%25E2%2580%259D%2B%26hl%3Den%26rls%3DSUNA,SUNA:2006-29,SUNA:en> (Feb. 17, 2006).

²⁹ The total U.S. Market was 230.8 million subscribers, and the four largest carriers were: Cingular Wireless with almost 61 million subscribers (26.5%); Verizon Wireless with over 59 million (25.6%); Sprint Nextel with 48 million (21%); and T-Mobile with 25 million (11%). Market Share: Mobile Connections, North America, 4Q06, Gartner Dataquest. See more generally BT's Reply Comments in *In the Matter of Skype Communications, S.A.R.L. Petition to Confirm a Consumer's Right to Use Internet Communications Software and Attach Devices to Wireless Networks*, RM No. 11361 (filed May 15, 2007) and BT's Reply Comments in *Implementation of Section 6002(b) Of the Omnibus Budget Reconciliation Act of 1993 Annual Report and Analysis of Competitive Market Conditions with Respect to Commercial Mobile Services*, WT Docket No. 07-71 (filed May 22, 2007) which are incorporated herein by reference.

³⁰ WiMax services (using non-certified CPE) offer consumers between 512 Kbps and 1,536 Kbps — a far cry from the WiMAX Forum's 70 Mbps boast – Forrester Research, "Let's Get Real About WiMax," July 2005. WiFi is a more highly contended and less secure service. See also, *AT&T scales back plan for citywide Wi-Fi in St. Louis*, Orlando Sentinel (28 October 2007) ("AT&T engineers couldn't find a cheap way to power the network's transmitters, which carry the network signal and send it to people's computers. One estimate required 50 transmitters per square mile.").

³¹ See, <http://news.moneycentral.msn.com/provider/providerarticle.aspx?feed=OBR&Date=20070308&ID=6589920>; see

competition exists at all, it is with respect to residential service where issues of reliability and security are not nearly as critical as they are for business purposes.³²

B. The Data Verizon Seeks to No Longer Report Is Critical For the Commission and the Public

Data from ARMIS Reports 43-01 (Annual Summary), 43-04 (Separations and Access Report) and 43-08 (Operating Data Report) were heavily relied upon by the parties in the special access proceeding (and the recent BOC merger proceedings) to establish RBOC overcharges in interstate special access services and to demonstrate that they earned excessive realized rates of return.³³ The data in these same reports and 43-02 (Uniform System of Accounts) are also essential in calculating the X-factor for price capped services (representing the extent to which the overall LEC productivity growth is expected to exceed the productivity growth of the economy as a whole), including the X-factor being considered in the special access proceeding.³⁴

These Reports, and ARMIS Report 43-03 (Joint Cost Report) are also essential to monitor Verizon's and the other BOCs' compliance with the Commission's *Section 272 Sunset*

also, Slip Copy, 2007 WL 528749 (E.D. Va., Feb. 12, 2007) (setting forth the patent claims). *Cf. United States v. Microsoft Corp.*, 253 F.3d 34 (D.C. Cir.), *cert. denied*, 534 U.S. 952 (2001) (regarding the positioning of Java applications).

³² See Comments of the AdHoc Telecommunications Users Committee, WC Docket No. 05-25 & RM No. 10593 (August 8, 2007) ("AdHoc's Comments") at 7 (discussing "the severe security and reliability concerns raised by cable-based services and technologies"). The level of reliability and security demanded by residential customers for transmission of a "YouTube" program is far less than the demanding levels of reliability and security demanded by financial institutions for the transmission of data related to financial transactions, or defense firms transmitting critical plans relating to national security applications.

³³ See *e.g.*, Declaration of Stephen Friedlander and the Declaration of M. Joseph Stith submitted with AT&T's Special Access Petition, RM No 10593 (Oct. 15, 2002) (¶¶ 2-7 and Exhibits 1 and 2; rates were calculated from ARMIS 43-01, Table 1, Cost and Revenue Table, Column S, Rows 1910 and 1915); Comments of AdHoc Telecommunications User Committee, CC Docket no. 05-25, (August 8, 2007) at 20, n. 25 (ARMIS 43-08) and Appendix thereto, Selwyn, Gately, Golding and Weir, *Special Access Overpricing and the US Economy; How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness*, Tables A1, A4 and A5 (ARMIS 43-01 and 43-04); and Appendix 2, Susan Gately's Declaration on Behalf of AdHoc Telecommunications User Committee at 11, ¶16 (same); Reply Declaration of Lee L. Selwyn on behalf of Comptel/ALTS, *In the Matter of AT&T and SBC Communications Inc. Application Pursuant to Section 214 of the Communications Act of 1934 and Section 63.04 of the Commission's Rules for Consent to the Transfer of Control of AT&T Corp. to SBC Communications Inc.*, WC Dkt. No. 05-65 (filed May 10, 2005) ¶¶ 10, 48-49, Figure 2 and Table 2 (based on the ARMIS 43-04 Report).

³⁴ See Sprint/Nextel's Comments at 16; AdHoc's Opposition at 8-9.

*Order*³⁵ where the Commission found that the BOCs possessed “[e]xclusionary market power within its respective regions by reason of its control over these bottleneck access facilities.”³⁶

The Commission nevertheless eliminated the separate subsidiary requirement for in-region long distance service relying on non-structural safeguards such as the ARMIS data reporting requirements.³⁷

The other ARMIS Reports as to which Verizon seek forbearance are also critical. ARMIS Report 43-05 captures data on the quality of service an ILEC provides to its retail and wholesale customers. ARMIS Report 43-06 is an annual report on customer satisfaction and reports the percentage of customers who are dissatisfied with various features of the reporting carrier’s services.

The affiliate transaction rules address the transfer of assets between regulated and non-regulated affiliates.³⁸ These rules are necessary to prevent cost misallocation and cross-subsidization between regulated and unregulated affiliates. The continued existence of the affiliate transaction rules was the basis for the Commission’s decision to grant the BOCs request to be relieved of the “operate independently” rules prohibiting a BOC’s Section 272 affiliate

³⁵ Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements, 22 FCC Rcd 16440 (2007).

³⁶ *Id.*, ¶ 64.

³⁷ *Id.*, ¶ 84-85 and 90. *See* Sprint/Nextel’s Comments at 11-12 (discussing the “targeted imputation requirement for any access services that the BOCs’ incumbent LEC affiliates provide to their in-region, long distance operations” and the Commission’s reliance on the BOCs’ ARMIS filing obligations); Comments of Time Warner Telecom, CBeyond and One Communications (“TWTC’s Comments”) (Feb. 1, 2008) at 4-5 (BOC compliance with ARMIS requirements and affiliate transaction rules both essential).

³⁸ *See*, Sprint/Nextel’s Comments at 5-6 (the affiliate transaction rules “set forth the requirements for recording assets and services transferred or provided between the regulated entity and its non-regulated affiliates ... serve as a safeguard to protect consumers of regulated services from bearing the risk and the costs associated with non-regulated activities through improper cost shifting and cross subsidization”); *see also*, Huber, Kellogg and Thorne, Federal Communications Law, “[s]uch transactions must be recorded on the carrier’s books at market or tariff price if such a price can be determined. If not, transactions must be recorded at the higher of net book cost or fair market value (for the transfers from the regulated to the unregulated side) or at the lower of the two (for transfers the other way.” *Id.* at 107, http://books.google.com/books?id=etWdR9D78tAC&pg=PA107&lpg=PA107&dq=fcc+affiliate+transaction+rules&source=web&ots=ncQtC1R0TB&sig=MCzDbiqd_vCiteDVBcq_0A64c84.

from sharing operating, installation and maintenance (OI&M) functions with the BOC or another BOC affiliate.³⁹

C. Verizon's Claim That the Critical Data Is Otherwise Available is Specious

Verizon asserts that the ARMIS reports and the affiliate transaction and property records rules are not necessary because of Verizon's "expanded and reporting obligations in its capacity as a publicly traded company, including those imposed by the Securities and Exchange Commission ('SEC') and Generally Accepted Accounting Principles ('GAAP'), the Foreign Corrupt Practices Act, and the Sarbanes-Oxley Act."⁴⁰ Verizon has been bound by the reporting obligations of the *Securities Exchange Act of 1934*⁴¹ and the *Foreign Corrupt Practices Act of 1977*⁴² for decades; clearly the Commission, when the ARMIS reporting system was developed (beginning in 1987),⁴³ was of the view that the additional ARMIS reporting requirements were necessary despite those other reporting requirements. Moreover, Verizon makes no effort to show how the data reported in the ARMIS reports can be found in these filings⁴⁴ or are rendered unnecessary by a carrier's compliance with GAAP. To the contrary, both ARMIS and the

³⁹ Report and Order and Memorandum Opinion and Order (FCC 04-54), Docket Nos. WC 03-228, CC 96-149, 98-141, 01-337 (March 11, 2004). *See also, In the Matter of Implementation of the Telecommunications Act of 1996: Accounting Safeguards Under the Telecommunications Act of 1996*, CC Docket No. 96-150, Comments of AT&T Corp on Verizon's Section 272 Compliance Biennial Audit Report, 2 and 31-35 (April 8, 2002) and Notice of Apparent Liability for Forfeiture, *In the Matter of Verizon Telephone Companies, Inc.* File No EB-03-IH-0245 (8 September 2003); *In the Matter of Section 272 Biennial Audit of Verizon Communications Inc.*, Comments of AT&T Corp. on Verizon's Second Section 272 Compliance Biennial Audit Report, 26-28 (Feb. 10, 2004) and Consent Decree, *In the Matter of Verizon Telephone Companies, Inc.* No EB-03-IH-0245 (27 July 2004).

⁴⁰ Verizon's Petition at 4, 9 and 25-27.

⁴¹ 15 U.S.C. § 78m(b).

⁴² *Id.* §§ 78dd-1, et seq.

⁴³ *Automated Reporting Requirements for Certain Class A and Tier 1 Telephone Companies (Parts 31, 43, 67, and 69 of the FCC's Rules)*, Report and Order, 2 FCC Rcd 5770 (1987).

⁴⁴ To the contrary; the discussion in its Petition about the additional efforts needed to collect the ARMIS data above and beyond what is needed to collect the other public filings, Verizon Petition at 17-18 strongly suggests no overlap in the data.

publicly required filings are essential to monitor cost-shifting by the BOCs.⁴⁵ For example, in the *Special Access Proceeding*, “an analysis of Verizon’s ARMIS and 10-K reporting together with its various public disclosures indicates that, over the period of 2004-2006, Verizon has spend some \$9- to \$10-billion on FIOS and appears to have charged virtually [sic] of this to TPIS [Telecommunications Plant in Service] in its regulatory accounting.”⁴⁶

Verizon further argues that:

information about Verizon’s network is reported on Form 477, which collects data about Verizon’s broadband connections, and about Verizon’s local telephone service in individual states. The information provided by Verizon on Form 477 is specifically geared toward describing broadband infrastructure and competition for local telephone service. *All carriers are required to complete Form 477, making this a far more useful comparative tool for the Commission and consumers than the Commission’s other reporting requirements.*⁴⁷

Yet in the *Special Access Proceeding* Verizon argued that the Commission did *not* have, except as to the BOCs (who filed ARMIS reports), “any data about the true extent of networks, facilities, service offerings, and market successes.”⁴⁸ Implicit in Verizon’s argument is that the relevant infrastructure data could *not* be found by the Commission in the Form 477s that its competitors also have to file. Either the Form 477s provide all the necessary data on infrastructure and competition or they do not; Verizon cannot have it both ways.

⁴⁵ As noted in the Opposition of AdHoc Telecommunications Users Committee (Feb 1, 2008) (“AdHoc’s Opposition”), “[t]he accounting requirements specified by GAAP, Sarbanes-Oxley, the Securities and Exchange Commission, and the Foreign Corrupt Practices Act would not allocate costs and revenues between service categories and would otherwise not produce the data that the Commission needs to meet its statutory obligations” *id.* at ii, and at 12-15 (noting the different function and purpose of the reporting requirements); *see also* State Advocates’ Comments at 27.

⁴⁶ Selwyn, Gately, Golding and Weir, *Special Access Overpricing and the US Economy; How Unchecked RBOC Market Power is Costing US Jobs and Impairing US Competitiveness*, Appendix 1 to Comments of AdHoc Telecommunications User Committee, CC Docket no. 05-25, (August 8, 2007) at A-7 (emphasis added). *See also*, AdHoc’s Opposition at 6 (“[w]ithout cost assignment and allocation rules, carriers subject to price cap regulation could misallocate costs to repress earnings levels and thus ... cross subsidize unregulated services such as FIOS.” *Id.* at 6.

⁴⁷ Verizon Petition at 9-10.

⁴⁸ Verizon’s Comments, WC Docket No. 05-25, RM-10593 (August 8, 2007) at 14 and 38.

II. THE EUROPEAN EXPERIENCE DEMONSTRATES THAT GRANTING FORBEARANCE IS NOT IN THE PUBLIC INTEREST

Verizon's claim that the rules from which it seeks forbearance "*potentially* constrain development and launch of new products and services that consumers want"⁴⁹ is utterly unsubstantiated and speculative. Verizon's claims as to the cost of complying with these regulatory requirements are selectively anecdotal.⁵⁰ Verizon makes no claim that the costs it cites in those particular instances are typical. Verizon fails to disclose the actual costs of compliance, or in any other way substantiate its claim, although it has done so in other proceedings.⁵¹ And the experience from other countries shows that in the context of enduring local access bottlenecks such as special access, the maintenance of such regulatory oversight and the public reporting of this data are *essential* for the development and launch of new products and services that consumers want.

A. The ECTA Regulatory Scorecard and the UK Experience Provide Benchmarks Demonstrating that Such Reports and Regulations Are in the Public Interest

The European Competitive Telecommunications Association (ECTA) does an annual benchmark of 19 European countries. The most recent (2007) ECTA Regulatory Scorecard found that the "[t]he United Kingdom remains the highest scoring country overall for effective regulation of the telecoms sector. The Netherlands has improved its position from 4th place in

⁴⁹ Verizon Petition at 19, emphasis added.

⁵⁰ *Id.* at 21-24; *see also* at 28-29.

⁵¹ *E.g., In the Matter of Section 272(b)(1)'s 'Operate Independently' Requirement for Section 272 Affiliates*, WC Docket No 03-228; *see* Verizon's filings in that proceeding on May 12, 2003 (detailing the costs of compliance); June 4, 2003, especially Attachments 3 and 4 (proving the going forward savings and projected cost data) and June 24, 2003 (detailed analysis of elements). And in other proceedings Verizon has minimized the significance of similar "administrative costs." *See e.g., Opposition of Verizon, In the Matter of InterCall, Inc. Appeal of Decision of the Universal Service Administrative Company and Request for Waiver; InterCall, Inc's Petition for Stay of the Decision of the Universal Service Administrative Company Universal Service*, CC Dkt. No. 96-45 (Feb. 25, 2008) at 9-12 ("arguing that the fact that InterCall will be required to "file the required FCC revenue reporting and other forms related to such contributions, make systems changes to identify which of its revenues are subject to contribution, and train personnel to execute on all of these requirements" "did not give rise to a cognizable claim of irreparable harm" *id* at 10).

2006 to 2nd place this year just four points behind the UK.”⁵² The authors further concluded, based on their 19 country survey, that “the lowest prices and highest investment occurs where regulators have strong tools to enforce EU pro-competition rules.”⁵³ And it is clear from that study that one of those “key tools” for realizing lower prices and higher investment is the public availability of audited accounting separations data, which includes data on volumes, cost and prices of key services, and data on the quality of the services provided.

Specifically, the 2007 Regulatory Scorecard found that: “accounting separation, a vital measure to ensure consistent pricing to promote competition and investment – has been mandated in all countries but has yet to be fully implemented except in the UK, Netherlands and Ireland.”⁵⁴ The Scorecard’s recommendation to the regulators in the other countries was that they “[e]nsure that separated accounts are published in a timely manner following best practice identified by ERG and Commission.”⁵⁵ For business services, ECTA further recommended that National Regulatory Authorities “[a]pply and publish KPIs [Key Performance Indicators] that allow industry to compare whether services provided by dominant operators to competitors match expressed demand and the standard of services supplied internally.”⁵⁶

As reported in the Regulatory Scorecard, BT in the UK is required to prepare cost accounting and/or accounting separation statements on 18 wholesale and 7 retail markets. BT’s

⁵² European Competitive Telecommunications Association, Regulatory Scorecard, November 2007, p.3 (“Regulatory Scorecard”). Available from <http://www.ectaportal.com/en/>

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http://www.ectaportal.com/en/upload/File/Regulatory%20Scorecards/2007/2007_Regulatory_Scorecard_press_release_final.pdf

⁵⁴ Regulatory Scorecard at 9.

⁵⁵ *Id* at 8. ERG is the European Regulators Group set up by the Commission and composed of the heads of each relevant national regulatory authority in each Member State or their representative. Commission decision, 2002/627/EC of 29 July 2002. The “best practice” can be found in *ERG Common Position: Guidelines for implementing the Commission Recommendation C (2005) 3480 on Accounting Separation & Cost Accounting Systems under the Regulatory Framework for Electronic Communications*, at http://www.erg.eu.int/doc/publications/consult_accounting_sep/erg_05_29_erg_cp_rec_as_and_cas_final.pdf

⁵⁶ Regulatory Scorecard at 9.

regulated Financial Statements⁵⁷ include statements specifically designed to show sales of products from wholesale Significant Market Power (“SMP”) markets and into relevant retail SMP markets. The published regulatory accounts of BT detail cost components and show how these are allocated consistently to regulated services. BT also has an obligation to publish some KPIs on quality of service. For example on Partial Private Circuits (“PPCs”) (what is called special access in the U.S.) BT is required to publish KPIs on a quarterly basis.⁵⁸

An example of the extent of financial disclosure comparing charges to affiliated (internal) and non-affiliated (“external”) charges can be found in BT’s 2007 Report.⁵⁹ Extensive data is provided on costs of special access (PPC) services and Ethernet access.⁶⁰ Both BT’s Wholesale group and Openreach publish KPIs.⁶¹

As to the Netherlands, the ECTA Regulatory Scorecard describes the accounting separation imposed on KPN in the new (2005) regulatory framework. The description of the cost system and costing methodologies is published annually as part of the accounting separation report. The accounting separation report must (a) cover the wholesale and retail cost system as

⁵⁷ BT’s 2007 regulatory Financial Statements can be found at <http://www.btplc.com/Thegroup/Regulatoryinformation/Financialstatements/index.htm>.

⁵⁸ Available from BT Wholesale website. http://www.btwholesale.com/application?pageid=editorial_one_column&nodeId=navigation/node/data/Pricing_and_Contracts/Reference_Offers/Partial_Private_Circuits_PPC_Reference_Offer/PPC_Quality_of_Service_Performance/navNode_PPC_Quality_of_Service_Performance.

⁵⁹ The “Current Cost Financial Statements for 2007 including Openreach Undertakings” report can be found at <http://www.btplc.com/Thegroup/Regulatoryinformation/Financialstatements/2007/CurrentCostFinancialStatements.pdf>.

⁶⁰ See Section 3 of the Report (“Review of Access Markets”) pp. 22-43, especially Sections 3.8 and 3.9 (PPCs) and 3.10 (Ethernet).

⁶¹ For BT Wholesale, *see* http://www.btwholesale.com/application?origin=child_link_index.jsp&event=bea.portal.framework.internal.refresh&pageid=editorial_two_column&nodeId=navigation/node/data/Footer/About_BTW/Key_Performance_Indicators/navNode_Key_Performance_Indicators. For Openreach *see e.g.*, for LLUs (Local Loop Unbundling) <http://www.openreach.co.uk/orpg/products/llu/kpi/kpi.do>.

approved by the National Regulatory Authority, OPTA, (b) be audited and (c) be published.⁶²

With respect to wholesale markets, the internal and external wholesale revenues have to be specified. With respect to the retail markets, the transfer charges of internal wholesale purchases must be specified. The fixed incumbent has to use one single, consistent cost system for all different services and markets. This is also explicitly stated in the obligation and subject of the audit of the separated accounts. Costs of assets which are used by different services and markets are allocated to these services and markets on the basis of a single, consistent, methodology and allocation mechanism. The report includes an audit statement.

B. The New Zealand Experience Similarly Confirm the Importance of Such Reports and Regulations in Promoting Competition and Innovation

The ECTA analysis is confirmed by the experience in New Zealand. New Zealand initially adopted a deregulatory process similar to that being implemented in the United States only to find that it began slipping behind its OECD peers in broadband services.⁶³ In response, the Government, in December 2005, commenced a “stocktake” of the telecommunications sector.⁶⁴ That analysis showed that the governing Telecommunications Act 2001 “at present does not provide the Commission with specific powers to [] provide for public information disclosure of relevant undue discrimination performance measures including applicable accounting information.”⁶⁵ It concluded that “[a] transparency requirement that enables the regulator to specify the precise information to be made available can render undue discrimination

⁶² The KPN reports for 2005 and 2006 can be found on KPN’s wholesale website www.kpn-wholesale.com, search for “accounting separation”. For 2007, the public version of the accounting separation report was published on OPTA’s website on 17 October 2007.

⁶³ See the Statement of Communications and Information Technology Minister, Hon David Cunliffe, (March 5, 2006) (“Cunliffe Statement”) at <http://www.beehive.govt.nz/ViewDocument.aspx?DocumentID=25636>.

⁶⁴ *Id.*

⁶⁵ Regulatory Measures to Address Wholesale Supply Discrimination Issues and Information Needs (Published 28 April 2006) at 12. This report can be found at http://www.med.govt.nz/templates/MultipageDocumentTOC___20558.aspx.

actions less likely to succeed by making the behaviour observable and enabling initiation of enforcement action.”⁶⁶ It was accordingly recommended that New Zealand require the incumbent provider to make available the following “publicly available” information:

- “information including in respect of similar services the access provider supplies to itself, including technical specifications, network characteristics, service order provision characteristics,”
- “accounting records ... pricing and revenue related data, cost related data, including in relation to equivalent services and related services supplied by the access provider to its own affiliates,”
- “business unit accounting information that is required in respect of the resolution of terms and conditions of a regulated service or the monitoring or enforcement of a determination,”
- “from access providers, which is required by the parties to efficiently monitor compliance with the relevant access principles.”⁶⁷

One of the key elements in the resulting legislation was a provision requiring the incumbent telecommunications provider to publicly provide a set of regulatory accounts (accounting separation) based around its wholesale businesses.⁶⁸

C. The Public Interest in Innovative Investment Requires the Denial of Verizon’s Forbearance Petition So Long as there is Market Failure in the U.S. Special Access Market

Because of persistent market failure in the U.S. special access market, the U.S. lags in broadband penetration.⁶⁹ A good example is Ethernet, a protocol which is particularly efficient for the transfer of Internet Protocol (IP) packets and is used in place of the traditional synchronous digital hierarchy (SDH) protocol. Ethernet provides higher bandwidth at lower prices than traditional special access. This is good for businesses, consumers and the economy at

⁶⁶ *Id* at 13.

⁶⁷ *Id* at 14-15.

⁶⁸ *See* Cunliffe Statement *supra*.

⁶⁹ Free Press, Consumers Union, Consumer Federation of America, *Broadband Reality Check II, The Truth Behind America’s Digital Decline*, (Aug. 2006) (“*Broadband Reality Check II*”) (study, relying on OECD data, found that the U.S. remains sixteenth in the world in broadband deployment and Americans pay more per megabit than consumers in other countries). The most recent OECD statistics (June 2007) show that the U.S. ranked 15th in net growth in broadband penetration.
http://www.oecd.org/document/54/0,3343,en_2649_33703_38690102_1_1_1_1,00.html.

large. Ethernet is more widely deployed in Europe than in U.S., even though enterprise customers want it wherever they do business.⁷⁰ The reason for the lag in U.S. Ethernet deployment: the incumbent providers, who control the access bottleneck, refuse to provide the facilities needed to provide an Ethernet solution, in order to retain the revenue and high margins of their legacy services.

CONCLUSION

For the foregoing reasons, Verizon's Petition for Forbearance should be denied in its entirety.

Respectfully submitted,

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⁷⁰ Boyd Chastant, *International Ethernet Services: An Overview*, IDC (Apr 2007) ("In Europe ... Ethernet access is more widely available [than in the U.S.] and typically lower priced ... Ethernet services ... offer less ability for carriers to work their way up the value chain alongside customers and ... requires carriers to invest in new service for which they then need to charge less, cannibalizing or preventing growth of customer bases of superior-quality services for which they charge more (e.g., private line, VPN) ... AT&T does not currently offer end-to-end international Ethernet services. It claims ongoing VPLS trials toward offering such service internationally by sometime in 2008. It ... appears — like many other carriers — to be waiting to see how much pressure the market will exert over the next couple of years in the direction of pushing Ethernet services internationally."); *See also*, Phil Sayer, *Making Sense of European Ethernet Services*, Forrester, (May 1, 2007).