

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 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)	
Regulation of Incumbent Local Exchange Carrier)	RM-10593
Rates for Interstate Special Access Services)	

COMMENTS OF TELEPACIFIC COMMUNICATIONS

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Mpower Communications Corp. and U.S. TelePacific Corp. (both of whom d/b/a TelePacific Communications) (“TelePacific”) respectfully submit these comments in response to the *NPRM* issued by the Commission in the above-referenced dockets.¹

I. INTRODUCTION AND SUMMARY

TelePacific is a facilities-based CLEC serving more than 1,200,000 business customer lines in California, Nevada, and Texas. It is the largest competitor to the Bell Operating Companies (“BOCs”) in California and Nevada and the second largest local provider of business services in California. It has 15 TDM switches and 9 soft switches, nearly 300 collocations, which it uses to obtain last mile access from ILECs, and over 50,000 fiber route miles of network. TelePacific can provide service to nearly 20% of all small and medium businesses nationwide. It has been named to Inc. Magazine’s list of fastest growing private companies in America in each of the last six years.

TelePacific supports the Commission’s proposed one-time, multi-faceted market analysis, and believes that it will constitute a sound approach to analyzing the market data. TelePacific

¹ *In the Matter of Special Access for Price Cap Local Exchange Carriers; AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, WC Docket No. 05-25, RM-10593, Report and Order and Further Notice of Proposed Rulemaking, FCC 12-153 (rel. Dec. 18, 2012) (“*NPRM*”).

expects the Commission's proposed market analysis will be far more accurate than the pricing flexibility's competitive showing requirement, which incorrectly predicted price-constraining competitive entry.

In examining the 2010 and 2012 data, the analysis need not separately consider potential competition because the data, such as pricing data, will itself account for the effects of both actual and potential competition. In addition, TelePacific believes that potential competition based on the deployment of laterals has any little, if any, effect on constraining special access prices of ILECs because laterals rarely can be constructed in an economical and timely manner, so as to constrain ILECs' market power. Thus, ILECs continue to control last mile access to the vast majority of customers.

TelePacific also believes that the proposed market analysis will facilitate a useful examination of both potential barriers to broadband deployment and investment and an examination of substitutable services, whether the services constrain ILEC special access rates, and whether ILECs have market power. The Commission's analysis should evaluate three separate relevant product submarkets: loops, transport and entrance facilities, as these facilities are not substitutes for one another. It should also examine submarkets for different capacity levels, such as DS1, DS3, Ethernet and OCn. For each of these product submarkets, the Commission should analyze the data in representative sample of national geographic markets subject to price caps and/or pricing flexibility. TelePacific expects that the Commission's analysis will show that (a) an ILEC's price flexibility rates are higher, if not much higher, than the ILEC's rates subject to price caps, the NECA rates, the CLECs' rates, and rates for best efforts broadband services; and (b) the rate of return of ILECs subject to price caps or pricing flexibility are recouping supracompetitive profits.

TelePacific believes that the record shows that the Commission's price cap and pricing-flexibility rules have not prevented the BOCs from imposing anticompetitive and unreasonable terms and conditions on the purchase of special access services. In particular, the price cap LECs establish exceedingly high rack rates in areas where they have been given price flexibility, then

condition discounts off those inflated prices on a customer committing all or almost all of its past purchase level to the price cap LEC. The record already establishes this pervasive nature of this practice, and the Commission should take immediate action to stop it, rather than waiting to conduct and complete the exhaustive market analysis that it has proposed.

II. THE COMMISSION’S PROPOSED ONE-TIME, MULTI-FACETED MARKET ANALYSIS SHOULD BE PERFORMED BASED ON A REPRESENTATIVE SAMPLE OF NATIONWIDE MARKETS SUBJECT TO PRICE CAP AND/OR PRICING FLEXIBILITY

A. The Commission’s proposed market analysis will likely be far more accurate than the current competitive showing requirement for pricing flexibility that failed to predict price constraints on competitive entry

TelePacific supports the Commission’s proposed one-time, multi-faceted market analysis (“market analysis”)² because the FCC has stated that this analysis will incorporate both a structural market analysis and an analysis with “econometrically sound panel regressions to determine how the intensity of competition (or lack thereof), whether actual or potential, affects prices, controlling for all other factors that affect prices.”³ TelePacific believes that the Commission’s proposed market analysis is a sound approach to analyzing the market data. The Commission should perform a thorough market analysis as it did in the *Qwest Phoenix Forbearance Order*⁴ and not truncate or otherwise engage in a less rigorous structural analysis.

In prior comments, TelePacific has emphasized that the Commission’s pricing flexibility triggers, which are based on collocation of competitive carriers in ILEC wire centers, are not an accurate proxy for the kind of sunk investment by competitors sufficient to constrain ILEC special access prices for channel terminations and dedicated transport facilities.⁵ TelePacific

² *NPRM*, ¶ 72.

³ *NPRM*, ¶ 71.

⁴ *Petition of Qwest Corporation for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Phoenix, Arizona Metropolitan Statistical Area*, WC Docket No. 09-135, Memorandum Opinion and Order, 25 FCC Rcd 8622 (2010) (“*Qwest Phoenix Forbearance Order*”), *aff’d*, *Qwest Corp. v. FCC*, 689 F.3d 1214 (10th Cir. 2012).

⁵ *See* Comments of PAETEC Holdings Inc. *et al.*, WC Docket No. 05-25, RM-10593, at ii & 10 (filed Jan. 19, 2010) (“TelePacific Jan. 19, 2010 Comments”); Reply Comments of

expects the Commission's proposed market analysis will be far more accurate than the pricing flexibility's competitive showing requirement, which incorrectly predicted price-constraining competitive entry.

B. The proposed analysis of the marketplace in 2010 and 2012 need not separately consider potential competition

The Commission asks in the *NPRM* if there are “significant competitors who would not be easily accounted for under the proposed analysis, such as firms who self-supply their own special access?”⁶ The Commission further asks “[i]s such an approach likely to show whether a specific provider is a probable source of competition in a given geographic area, *i.e.*, that its presence could reasonably be found to constrain special access prices?”⁷

The Commission need not distract itself with such purely theoretical issues. The 2010 and 2012 data accounts for the effect of the actual and potential competitive conditions that existed during these years. The Commission's analysis should show whether actual and/or potential competition in fact constrained special access prices of ILECs during these years and should facilitate a comprehensive forward-looking evaluation of competitive conditions.⁸

Moreover, TelePacific does not believe that the existence of potential competition based on the deployment of laterals to buildings will have an effect on the Commission's proposed market analysis. The entry into a market by a competitive carrier is far more difficult than for the incumbent. For a competitive carrier to deploy a building lateral is “extremely difficult, time consuming and costly” even when adding buildings that are located in close proximity to a

PAETEC Holdings Inc. *et al.*, WC Docket No. 05-25, RM-10593, at iii & 20 (filed Feb. 24, 2010) (“TelePacific Feb. 24, 2010 Comments”).

⁶ *NPRM*, ¶ 72.

⁷ *Id.*

⁸ *NPRM*, ¶ 73.

network ring.⁹ Moreover, there are “other barriers to entry, including the delays in or impossibility of securing municipal franchise agreements, rights-of-way agreements, building access agreements, and building and zoning permits” that competitive carriers must address.¹⁰

For these reasons, TelePacific believes that potential competition based on the deployment of laterals has any little, if any, effect on constraining special access prices of ILECs. Therefore, this type of speculative potential competitive data should be given little, if any, weight in the analysis. To “balance the need for an analysis that is forward-looking with the importance of relying on non-speculative data,”¹¹ the Commission should only look at competition where facilities have been deployed and either are already in service or can quickly be put into service by a competitor (within a month). Only such facilities potentially serve to constrain special access prices of ILECs. For instance, if a dark fiber wholesale provider offers strands of fiber or a retail provider offers service on a wholesale basis on a particular route or location, there is potential retail competition on the route or location (assuming the potential competitor can put such facilities into service within a month).

C. The Commission’s proposed market analysis does not undermine its non-dominance analysis

Contrary to the claims of certain ILECs,¹² TelePacific believes the Commission’s proposed market analysis is appropriate in the special access context. While certain ILECs argue

⁹ Comments of Covad *et al.*, WC Docket No. 05-25, RM-10593, at Govil Decl. para. 16 (filed Aug. 8, 2007). *See also Special Access for Price Cap Local Exchange Carriers; AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, WC Docket No. 05-25, RM-10593, Report and Order, 27 FCC Rcd 10557, ¶ 54 (2012) (“*Special Access Aug. 22, 2012 Report and Order*”); TelePacific Jan. 19, 2010 Comments, at 46;

¹⁰ *See Special Access Aug. 22, 2012 Report and Order*, ¶ 54.

¹¹ *NPRM*, ¶ 73.

¹² *NPRM*, ¶ 74 & n.166.

that “a dominance/non-dominance analysis is inappropriate in the special access context because ‘[t]he pricing flexibility rules are merely an incremental measure within the context of dominant carrier regulation,’”¹³ a more rigorous analysis is required because the pricing flexibility rules are flawed.

The Commission acknowledged previously that the results of its findings based on this rigorous analysis could prompt a finding that an ILEC is non-dominant for a particular service in a particular area. Specifically, in its *Special Access Aug. 22, 2012 Report and Order*, the Commission stated that,

once we have performed a broader evaluation of competitive conditions, our analysis may show that a carrier classified as dominant does not possess market power as defined in the *Competitive Carrier* proceeding for a particular special access service in a geographic area. In that case, the Commission may ultimately conclude that it is appropriate to grant regulatory relief in the form of non-dominance treatment for the particular service and geographic area. We will determine at a future date what criteria the Commission will consider to assess whether a finding of non-dominance for special access service is warranted in a given area.¹⁴

Nevertheless, the Commission should not refrain from undertaking an analysis that includes a rigorous market structure analysis with panel regressions in the special access context.

D. The Commission’s proposed market analysis should facilitate a useful examination of potential barriers to broadband deployment and investment

There is no question that the Commission’s proposed market analysis will reveal potential barriers to broadband deployment and investment,¹⁵ because a significant use of special access services is to provide broadband services. Contrary to AT&T’s claims,¹⁶ however, the Commission’s special access rules have not hindered carriers’ transition to IP-based services, nor

¹³ *NPRM*, ¶ 75 & n.167 (quoting AT&T 2009 PN Comments at 25-26 (italics removed)).

¹⁴ *Special Access Aug. 22, 2012 Report and Order*, ¶ 104.

¹⁵ *See NPRM*, ¶ 75.

¹⁶ *See id.* & n.169.

have they encouraged reliance on legacy services.

Competitive carriers utilize special access network facilities along with other facilities to provision IP-based services. TelePacific agrees that the industry should move from non-IP-based services to IP-based services; however, the transition to IP-based services has nothing to do with the actual network facilities needed and used to provision IP-based services to end user customers. Further, the ongoing evolution to IP-based networks does not alter the fact that ILECs have the only last mile connections to most businesses.¹⁷

As explained, economic barriers to self-provisioning include significant sunk costs, substantial economies of scale and scope, and access to rights of way and buildings. Consequently, the deployment of competitive last mile access facilities is “costly and difficult.”¹⁸ A study recently performed by TelePacific showed that only 12.5 percent of its customer locations in 30 wire centers were served by alternative last mile facilities.¹⁹ Clearly, ILECs continue to control the vast majority of last mile access to business customers.

E. The Commission’s proposed market analysis should facilitate a useful examination of substitutable services, whether the services constrain ILEC special access rates, and whether ILECs have market power

The Commission asks “how can we structure our analysis to account for all services that enterprise customers view as substitutable, including services used by small and medium-sized businesses.”²⁰ TelePacific believes that the Commission could determine all services that such enterprise customers view as substitutable by not limiting the analysis to TDM-based services.

¹⁷ See Comments of TelePacific, GN Docket No. 12-353, at 6-9 (filed Jan. 28, 2013). See also Letter from Eric J. Branfman *et al.*, counsel for TelePacific *et al.*, to Marlene H. Dortch, Secretary, FCC, WC Docket Nos. 10-188, 12-353; GN Docket Nos. 09-51, 13-5; RM-11358, at 6 (filed Jan. 25, 2013)(“TelePacific *et al.* 1/25/13 Letter”).

¹⁸ *Qwest Phoenix Forbearance Order*, 25 FCC Rcd at 8661, ¶ 73.

¹⁹ TelePacific *et al.* 1/25/13 Letter at 6.

²⁰ *NPRM*, ¶ 75.

The analysis should include an analysis of “best efforts” services, whether they are substitutes for special access services, and whether such services constrain ILEC special access prices. This evaluation should inform the Commission’s analysis of whether the ILECs’ special access rates are just and reasonable and whether ILECs have market power, based on whether they constrain ILEC special access prices.

F. The Commission’s market analysis should evaluate the three relevant markets: loops, transport and entrance facilities

Consistent with Commission precedent, the three relevant special access markets the Commission should analyze include: (1) the last mile connection or local loop (also known as a channel termination); (2) local transport (also known as channel mileage); and (3) entrance facilities.²¹ The Commission should evaluate competition in these markets separately from one another.

There is no question that these discrete products are not interchangeable. A loop connecting a customer to an ILEC central office is not a substitute for transport between two ILEC central offices or vice-versa. Further, the Commission recognized the need to evaluate these products separately in recent BOC mergers, finding that “services provided over different segments of special access (e.g., channel terminations and local transport) constitute separate relevant product markets, which may be subject to varying levels of competition.”²² In the 2009 NARUC study of special access competition, NRRI also evaluated competition in the loop and transport markets separately.²³

²¹ TelePacific Jan. 19, 2010 Comments at 29-30.

²² *SBC Communications Inc. and AT&T Corp. Applications for Approval of Transfer of Control*, WC Doc. No. 05-65, Memorandum Opinion and Order, 20 FCC Rcd 18290, ¶ 27 (rel. Nov. 17, 2005).

²³ Nat’l Regulatory Research Inst., “Competitive Issues in Special Access Markets, Revised Edition,” No. 09- 02, at 38-48, Jan. 21, 2009,

Similarly, the Commission must separately evaluate each product market by capacity level.²⁴ A DS1 loop, for example, is not a substitute for a DS3 loop, which has far more capacity.²⁵ A capacity level analysis should be applied in the transport market as well.²⁶ TelePacific proposes that the Commission eliminate the forbearance prematurely granted the BOCs for Ethernet and OCn level special access services.²⁷ Consequently, the Commission's market-power analysis should separately analyze competition for OCn level services (at least OC3, OC12 and OC48) and Ethernet services.²⁸ The Ethernet market should also distinguish between mid-band Ethernet and high capacity Ethernet.²⁹

For loops, the Commission should adopt a building as the appropriate geographic market for analyzing competition.³⁰ The Commission should analyze competition in the transport market on a route-by-route basis.³¹ Further, it makes little sense to evaluate whether competition exists on a point-to-point route by examining only one end point.³² MSAs are an inappropriate geographic market for the special access analysis because they are overbroad.³³

http://nrri.org/pubs/telecommunications/NRRI_spcl_access_mkts_jan09-02.pdf.

²⁴ TelePacific Jan. 19, 2010 Comments at 30.

²⁵ *Id.*

²⁶ *Id.* at 31.

²⁷ TelePacific Jan. 19, 2010 Comments at 36-42.

²⁸ *Id.* at 31.

²⁹ *Id.*

³⁰ *Id.* at 32-33.

³¹ TelePacific Jan. 19, 2010 Comments at 36.

³² *Id.*

³³ *Id.*

G. The Commission’s market analysis should be based on a representative sample of national geographic markets and whether proxies can be derived from those findings that can be used to determine ILEC market power in other regions

To best balance the need for “analytic rigor” with the need to be “administratively feasible,”³⁴ the analysis should be based on a representative sample of national geographic markets and whether certain proxies can be derived from those findings that can be used to determine the ILEC market power in other regions. Instead of a nuanced *nationwide* analysis for the 2010 and 2012 years, the Commission should analyze the data in representative sample of national geographic markets subject to price caps and/or pricing flexibility.

With these findings, the Commission can draw preliminary conclusions and determine proxies that could be used to test the conclusions and proxies in a *sample* of additional markets. The Commission may be able to identify simple indicators or market characteristics reflective of competitive or noncompetitive markets that could be used in making preliminary assessments of other geographic areas.

The preliminary assessment could be established as a presumption that a stakeholder would need to overcome. To the extent a stakeholder disputes a preliminary finding that a market is competitive, it could request that a detailed analysis be performed in which it can try to overcome the presumptions established.

GAO only looked at 16 markets in drawing the conclusions for the report it issued back in November of 2006.³⁵ The Commission need not evaluate every market in a nuanced fashion to establish proxies for identifying where competition does or does not exist.

³⁴ *NPRM*, ¶ 77.

³⁵ U.S. GENERAL ACCOUNTABILITY OFFICE, REPORT TO THE TO THE CHAIRMAN., COMMITTEE ON GOVERNMENT REFORM, HOUSE OF REPRESENTATIVES - TELECOMMUNICATIONS, “FCC NEEDS TO IMPROVE ITS ABILITY TO MONITOR AND DETERMINE THE EXTENT OF COMPETITION IN

Other administratively feasible analyses could (1) compare the rack rates in pricing flexibility areas with non-pricing flexibility areas, NECA rates, CLEC rates and best efforts broadband services; and (2) compare rate of return of ILECs subject to price caps or pricing flexibility for TDM and non-TDM services with rate of return of NECA carriers.³⁶ In determining whether the ILEC's special access rates are unjust and unreasonable and therefore, unlawful, the Commission could base decisions on such things as rate comparisons, benchmarks, and non-cost factors.³⁷

DEDICATED ACCESS SERVICES, GAO-07-80, at 10 (Nov. 2006).

³⁶ The Commission has the authority to require the BOCs to provide special access cost and revenue accounting data that they committed to maintain and produce upon request. *See* TelePacific Feb. 24, 2010 Comments at 10-11.

³⁷ “[T]he Commission has frequently used rate comparisons, benchmarks, and non-cost factors to evaluate the justness and reasonableness of rates and to prescribe just and reasonable rates for regulated entities.” *AT&T Corp. v. Business Telecom, Inc.*, Memorandum Opinion and Order, 16 FCC Rcd 12312, ¶ 23 (2001) (“*BTI Order*”); *id.* at n.73 (citing and explaining “[s]ee, e.g., *Access Charge Reform Order*, 12 FCC Rcd at 16141-42, ¶ 364; *Expanded Interconnection Order*, 12 FCC Rcd at 18790-93; *Annual 1990 Access Tariff Filings*, Memorandum Opinion and Order, 5 FCC Rcd 7487 (1990) (rejecting rates 8 times higher than benchmark rate); *Beehive Telephone Co.*, Memorandum Opinion and Order, 13 FCC Rcd 12275 (1998) (rejecting rate above “industry averages” for comparable companies); *Operator Communications, Inc. d.b.a. Oncor Communications, Inc.*, Memorandum Opinion and Order and Order to Show Cause, DA-95-02, 1995 WL 248343 (Com. Car. Bur. Apr. 27, 1995) (“*Oncor Communications*”) (finding that rates that “substantially exceed” rates charged by other service providers for comparable services in the same market to be unjust and unreasonable); *Capital Network System, Inc.*, Memorandum Opinion and Order and Order to Show Cause, 10 FCC Rcd 13732 (1995) (same as *Oncor Communications*); *International Settlement Rates*, Report and Order, 12 FCC Rcd 19806, 19943 at ¶ 295 (1997), *aff’d*, *Cable & Wireless PLC v. Federal Communications Commission*, 166 F.3d 1224 (D.C. Cir. 1999) (establishing benchmark governing international settlement rates based, in part, upon non-cost factors). Cases decided under the Interstate Commerce Act, from which the Communications Act derived, also determine the reasonableness of a carrier's rates by comparing them to the rates of other carriers and other rates of the same carrier. *See, e.g., Railroad Comm'rs of Fla. v. Seaboard Air Line Ry.*, 16 ICC 1, 5 (1909) (examining charges by carrier's competitor for similar services to determine the reasonable rate); *Freight Bureau v. Cincinnati, N.O. & Tx. Pac. Ry. Co.*, 4 ICC 92 (1894) (“where the reasonableness of rates is in question, comparison may be made, not only with rates on another line of the same carrier, but also with those on the lines of other and distinct carriers”).

The Commission has “broad discretion in selecting methods to evaluate the reasonableness of rates³⁸ and “courts are ‘particularly deferential’” to the Commission’s evaluation.³⁹ Such comparisons would likely reveal that (a) an ILEC’s price flexibility rates are higher, if not much higher, than the ILEC’s rates subject to price caps, the NECA rates, the CLECs’ rates, and rates for best efforts broadband services; and (b) the rate of return of ILECs subject to price caps or pricing flexibility are recouping supracompetitive profits.

This sampling approach could allow the Commission to “identify reliable new proxies for special access competition, which could be employed” to make preliminary and streamlined findings regarding whether other geographic markets are competitive.⁴⁰ The Commission could determine if these proxies are sound based on the in depth market analysis performed.

III. THINGS HAVE NOT CHANGED - THE TERMS AND CONDITIONS OF THE BOCS’ SPECIAL ACCESS CONTRACTS CONTINUE TO BE UNJUST AND UNREASONABLE

A. The BOCs’ terms and conditions are unjust and unreasonable

The record fully demonstrates that the Commission’s price cap and pricing-flexibility rules have not prevented the BOCs from imposing anticompetitive and unreasonable terms and conditions on the purchase of special access services.⁴¹ TelePacific recognizes that volume and

³⁸ *BTI Order*, 16 FCC Rcd 12312, ¶ 23 & n.80 (citing *Southwestern Bell v. FCC*, 168 F.3d at 1352; *MCI Telecommunications Corp. v. FCC*, 675 F.2d 408, 413 (D.C. Cir. 1982); *Aeronautical Radio, Inc. v. FCC*, 642 F.2d 1221, 1228 (D.C. Cir. 1980), *cert. denied*, 451 U.S. 920 (1981).

³⁹ *BTI Order*, ¶ 25 (footnote and citations omitted).

⁴⁰ *NPRM*, ¶ 78.

⁴¹ *See, e.g.*, TelePacific Jan. 19, 2010 Comments at 80-84; TelePacific Feb. 24, 2010 Comments at 71-73; Reply Comments of Level 3 Communications (“Level 3”), WC Docket No. 05-25, RM-10593, at 9-16 (filed Feb. 24, 2010); Letter from William P. Hunt, Vice President, Public Policy, Level 3, to Marlene H. Dortch, Secretary, FCC, WC Docket 05-25, RM-10593 (filed July 21, 2010); Letter from John M. Ryan, Assistant Chief Legal Officer, Level 3, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25, RM-10593 (filed Aug. 20, 2010);

term commitments may in the abstract represent a typical way of doing business in any industry - buy in bulk or buy for longer, and thereby buy cheaper. But there is a real anticompetitive impact of such arrangements when the firm offering them faces little, if any, competition.⁴² BOCs have twisted the application of volume and term commitments to turn them into “lock-ups” in many cases, and they have also loaded onto their special access purchase arrangements a number of other anticompetitive terms and conditions. While there are numerous types of terms and conditions that are unjust and unreasonable, the provisions most problematic to TelePacific, which Level 3 and others have thoroughly discussed, work through the combined effect of some or all of the following practices:

Letter from Andrew D. Lipman, counsel to Level 3, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25 (filed Oct. 25, 2010); Letter from Erin Boone, Senior Corporate Counsel, Federal Regulatory Affairs, Level 3, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25, RM-10593, at 1-2 (filed June 23, 2011); Letter from Michael J. Mooney, General Counsel, Regulatory Policy, Level 3, to Marlene H. Dortch, Secretary, FCC, WC Docket 05-25, RM-10593 (filed Feb. 22, 2012) (“Level 3 Feb. 22, 2012 Letter”); Letter from Erin Boone, Senior Corporate Counsel, Federal Regulatory Affairs, Level 3, to Marlene H. Dortch, Secretary, FCC, WC Docket 05-25, RM-10593 (filed March 1, 2012); Letter from Michael J. Mooney, General Counsel, Regulatory Policy, Level 3, to Marlene H. Dortch, Secretary, FCC, WC Docket 05-25, RM-10593 (filed June 8, 2012); Letter from Michael J. Mooney, General Counsel, Regulatory Policy, Level 3, to Marlene H. Dortch, Secretary, FCC, WC Docket 05-25, RM-10593 (filed June 27, 2012); Letter from Erin Boone, Senior Corporate Counsel, Federal Regulatory Affairs, Level 3, to Marlene H. Dortch, Secretary, FCC, WC Docket 05-25, RM-10593 (filed June 28, 2012); Letter from Eric J. Branfman, counsel to Level 3, to Marlene H. Dortch, Secretary, FCC, WC Docket 05-25, RM 10593 (filed June 28, 2012); Letter from Erin Boone, Senior Corporate Counsel, Federal Regulatory Affairs, Level 3, to Marlene H. Dortch, Secretary, FCC, WC Docket 05-25, RM-10593, at 2-7 (filed Aug. 23, 2012); Letter from Michael J. Mooney, General Counsel, Regulatory Policy, Level 3, to Marlene H. Dortch, Secretary, FCC, WC Docket 05-25, RM-10593 (filed Sep. 28, 2012); Letter from Michael J. Mooney, General Counsel, Regulatory Policy, Level 3, to Marlene H. Dortch, Secretary, FCC, WC Docket 05-25, RM-10593 (filed Oct. 31, 2012) (“Level 3 Oct. 31, 2012 Letter”).

⁴² See Letter from Thomas Jones, Counsel to tw telecom inc., to Marlene H. Dortch, Secretary FCC, WC Docket No. 05-25, at 22 (filed July 9, 2009) (citing Decl. of Michael D. Pelcovitz, at n.6, attached to Reply Comments of WorldCom, RM-10593 (filed Jan. 23, 2003) (stating that volume and term commitments “do not have exclusionary effects in a competitive environment, because each seller is able to supply a customer’s entire needs. Exclusionary or anticompetitive possibilities only arise when one firm, the incumbent monopolist, can supply each customer’s entire demand.”)).

- Very high rack rates, *i.e.*, list prices, which customers rarely pay;
- Large “loyalty”⁴³ discounts from these rack rates conditioned on the customer committing 85% to 100% of their prior years’ purchases to the BOC (because the discounts are applied to such a large percentage of the service, the discounted rates effectively become the “normal” price);
- Heavy shortfall penalties if purchases fall below required levels; . . .
- Onerous circuit migration charges and restrictions which impede (a) switching to competitors, and (b) self-provisioning services over newly-constructed facilities;
- Conditioning discounts on wide geographic lock-ups that competitors cannot match and/or tying of purchases in non-competitive and potentially competitive locations; [and]
- Providing additional discounts for shifting away from rivals, or imposing penalties for using the competition.⁴⁴

These ILEC lock-up terms are highly anticompetitive because they effectively prevent facilities-based competitors from competing against BOCs fully and meaningfully in the multi-billion dollar special access market. Businesses (and investors) refuse to commit the capital needed to build extensive facilities because most customers are locked into contracts with BOCs. In fact, despite the presence of well-capitalized and aggressive rivals, the price-cap LECs have not only maintained a market share in excess of 90% for special access lines within their regions, but also have been able to price such service at levels that earn supra-competitive returns.⁴⁵

In a competitive market, such lock-up provisions would not be present because suppliers would compete against one another with better pricing without the need for further concessions.

⁴³ These discounts are “loyalty” discounts that prevent a customer from filling more than a small fraction of its needs from a competitor of the ILEC, not “volume” discounts. The discounts are not based on the size of the customer’s purchases, but by the size of the customer’s purchases *relative to the customer’s past demand for special access circuits*. See Level 3 Feb. 22, 2012 Letter, at 9-11.

⁴⁴ Level 3 Feb. 22, 2010 Letter at 5.

⁴⁵ *Id.* at 5.

But in a market where “the only game in town” to serve the bulk of a customer’s needs is the ILEC, the customer is forced to accept the lockup provisions if it wants to buy at any rate better than the bloated “rack” rates for special access services.

B. The BOCs abuse their market power in a given area such that the unjust and unreasonable terms and conditions extend to all of a BOC’s markets, even the ones where competition presumably exists

BOCs leverage their market power in one market to achieve a competitive advantage in another market through anticompetitive or exclusionary means,⁴⁶ such as tying.⁴⁷ Such improper leveraging not only forces customers to purchase products that they might not otherwise need or want (just to obtain better rates on the monopoly products), but it also can be used to exclude competitors who cannot offer as wide a range of products.⁴⁸ Such exclusionary deals are contrary to established antitrust principles that prohibit anticompetitive bundling or tying.⁴⁹

The tying in which the BOCs engage comes in two primary forms. First there is tying of purchases in non-competitive and potentially competitive locations. Second, there is tying of purchases of non-competitive and potentially competitive products.

As to the first form of tying, BOC discounts are generally not offered on a location-specific basis to large, multiple location customers that are known to purchase and have the largest share of the relevant services. Rather, BOC discounts are offered only on a regional or nationwide basis. As a result, commitments and penalties are established on this basis.⁵⁰ Because

⁴⁶ See, e.g., *Verizon Comms., Inc. v. Trinko*, 540 U.S. 398, 415 (2004).

⁴⁷ *NPRM*, ¶ 93.

⁴⁸ See, e.g., *Lepage’s Inc. v. 3M*, 324 F.3d 141, 155 (3rd Cir. 2003)

⁴⁹ The Commission has long considered the impact of such principles on bundling or tying of communications services and other services and products. See, e.g., *In the Matter of Amendment of Section 64.702 of the Commission’s Rules and Regulations (Second Computer Inquiry)*, Docket No. 20828, Final Decision, 77 FCC2d 384, ¶¶ 149-61 (1980).

⁵⁰ When location-specific discounts are offered, they either lack portability or (in Verizon’s

CLECs cannot match the geographic coverage of a BOC, CLECs are generally only able to offer competitively-priced services in a small section of the BOC's territory, such as 25%. While a customer with multiple-locations may wish to use CLECs in that 25%, the BOC conditions a discount from inflated rack rates in the other 75% on purchases throughout its territory. As a result, CLECs rarely offer a price low enough in the 25% of locations to offset the lost discounts (or risk thereof) and potential penalties in the other 75%.

Take the following hypothetical, a customer needs one circuit where there is no competition (Circuit A), and one circuit where competition exists (Circuit B). In this hypothetical, the BOC's rack rate is \$1000 per circuit and if the customer purchases both circuits from the BOC, the customer obtains a 30% discount on both circuits.⁵¹ Thus, the cost of buying Circuit A from the price-cap LEC is \$1000 and the cost of buying Circuits A and B from the LEC is \$1400 (\$1,000 x 70%). As a result, the customer's marginal cost of buying Circuit B from the BOC is \$400 and therefore, if a competitor wants to win the customer's business at the location for Circuit B, the competitor would need to offer a price for Circuit B that is less than the customer's \$400 marginal cost. If only a limited number of circuits were at issue, competitors might be able to compete and capture the incremental business by reducing prices.

In reality, this is not the case because, given the number of circuits that are typically at issue, the BOCs' demand lock-up provisions create a significant barrier to entry for the competitive provider. To put this into perspective, assuming the same pricing and the presence of competition in 25% of locations, if a customer needs 100 circuits, the rate analysis is as follows:

case) include conditions on portability that impede use of portability. Level 3 Feb. 22, 2010 Letter at 9-11.

⁵¹ While round numbers are used in this hypothetical, they are representative of real world numbers.

Scenario One

- Rack Rate Pricing from the BOC (with no commitment to a demand lockup):75 Circuits x \$1000 per circuit=\$75,000 monthly recurring charge; and 25 Circuits from CLECs **for FREE** (\$0 monthly recurring charge).
- Total \$75,000 monthly recurring charge for all 100 circuits

Scenario Two

- Discounted Pricing from the BOC (Commitment to Demand Lock-up):100 Circuits x \$700 per circuit \$70,000 monthly recurring charge
- Total \$70,000 monthly recurring charge for all 100 circuits

Under these scenarios, even if the CLECs provisioned their circuits for **free** in the locations where they could compete, the customer is still better off purchasing all of its circuits from the BOC.

The tying is not only geographically based. In addition, the BOCs engage in classic monopoly leveraging by conditioning discounts on channel terminations (where the BOCs have the most market power) on interoffice transport purchases (where the BOCs have less market power). Consequently, a competitor offering only interoffice transport must match the discounts that are offered by the BOC on both interoffice transport and channel terminations. As one economist put it: “These conditions leverage the carrier’s dominance in the provision of channel terminations into greater control of the interoffice transport business, where competition is marginally more feasible.”⁵²

At bottom, the lock-up terms and conditions that tie up significant portions of special access demand have no place in a competitive marketplace when employed by entities with

⁵² Comments of Sprint Nextel Corp., WC Docket 05-25, RM-10593, at Attachment A - Declaration of Bridger M. Mitchell, p. 31, ¶ 127 (filed Jan. 19, 2010).

dominant shares of the market. TelePacific believes these practices are pervasive, and should be restricted.

C. The Commission should implement the remedies proposed by Level 3

Pursuant to Section 201(b) of the 1996 Act, the prices, terms and conditions of the BOCs' special access services must be "just and reasonable."⁵³ The lock-up commitments discussed above violate Section 201(b) and therefore, the Commission should address these anticompetitive practices and take the necessary actions. TelePacific urges the Commission to adopt the remedies proposed by Level 3 in its October 31, 2012 *ex parte*, which the Commission has authority to do and can quickly implement.⁵⁴

IV. CONCLUSION

For the foregoing reasons, the Commission should adopt the recommendations proposed and relief requested herein.

Respectfully submitted,

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⁵³ 47 U.S.C. § 201(b).

⁵⁴ Level 3 Oct. 31, 2012 Letter at 2-3.