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February 11, 2013

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VIA COURIER AND ECFS

FEB 11 2013

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, SW, Room TW-A325
Washington, DC 20554

Federal Communications Commission
Office of the Secretary

**Re: *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***

Dear Ms. Dortch:

On behalf of BT Americas Inc., Cbeyond Communications, LLC, EarthLink, Inc., Integra Telecom, Inc., Level 3 Communications, LLC and tw telecom inc. (collectively, the “Joint Commenters”), please find enclosed two copies of the redacted version of the Joint Commenters’ comments on Sections IV.A and C of the Further Notice of Proposed Rulemaking released on December 18, 2012 in the above-referenced proceeding¹ (the “Comments”). The Comments contain information that the Wireline Bureau has deemed highly confidential under the *Second Protective Order*² in this proceeding, including both highly confidential information that was previously submitted into the record by other parties and highly confidential information that is being submitted for the first time in the Comments.

¹ *Special Access 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*, Report and Order and Further Notice of Proposed Rulemaking, 27 FCC Rcd. 16318 (2012).

² *In the Matter of Special Access for Price Cap Local Exchange Carriers*, Second Protective Order, 25 FCC Rcd. 17725 (2010) (“*Second Protective Order*”); see also *Special Access for Price Cap Local Exchange Carriers*, Letter from Sharon E. Gillett, Chief, Wireline Competition Bureau to Paul Margie, Wiltshire & Grannis LLP, 26 FCC Rcd. 6571 (2011) (supplementing the *Second Protective Order*); *Special Access for Price Cap Local Exchange Carriers*, Letter from Sharon E. Gillett, Chief, Wireline Competition Bureau to Donna Epps, Vice President, Federal Regulatory Affairs, Verizon, 27 FCC Rcd. 1545 (2012) (further supplementing the *Second Protective Order*).

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Pursuant to the procedures outlined in the *Modified Protective Order*³ and *Second Protective Order*,⁴ as modified by the instructions in the second data request in this proceeding,⁵ one copy of the highly confidential version of the Comments has been served upon each party other than the Joint Commenters who submitted highly confidential information that appears in the Comments, the original highly confidential version of the Comments is being filed with the Secretary's Office under separate cover, two copies of the highly confidential version of the Comments will be delivered to Andrew Multz of the Pricing Policy Division of the Wireline Competition Bureau, and one machine-readable copy of the redacted version of the Comments will be filed electronically via ECFS. In addition, pursuant to a request from members of the Wireline Competition Bureau staff, one copy of the highly confidential version of the Comments will be delivered to Derian Jones of the Pricing Policy Division of the Wireline Competition Bureau.

Please do not hesitate to contact me at (202) 303-1111 if you have any questions regarding this submission.

Respectfully submitted,

/s/ Thomas Jones

*Counsel for BT Americas, Cbeyond, EarthLink,
Integra, Level 3 and tw telecom*

Enclosure

³ See *In the Matter of Special Access for Price Cap Local Exchange Carriers*, Modified Protective Order, 25 FCC Rcd. 15168, ¶¶ 5, 14 (2010).

⁴ See *Second Protective Order* ¶ 15.

⁵ See *Competition Data Requested in Special Access NPRM*, Public Notice, WC Docket No. 05-25, RM-10593, at 21 (rel. Sept. 19, 2011) (“[P]lease provide those copies of confidential and highly confidential filings that are to be delivered to staff of the Pricing Policy Division to Andrew Multz instead of Marvin Sacks.”)

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

**COMMENTS OF
BT AMERICAS, CBeyond, EarthLink, INTEGRA, LEVEL 3 AND TW TELECOM**

WILLKIE FARR & GALLAGHER LLP
1875 K Street, NW
Washington, DC 20006
(202) 303-1000

*Counsel for BT Americas, Cbeyond, EarthLink,
Integra, Level 3 and tw telecom*

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TABLE OF CONTENTS

	<u>Page</u>
I. INTRODUCTION AND SUMMARY	1
II. THE COMMISSION SHOULD ADOPT RULES NOW TO DIMINISH THE HARMFUL EFFECTS OF INCUMBENT LEC EXCLUSIONARY PURCHASE ARRANGEMENTS.....	11
A. Incumbent LECs Possess Overwhelming Market Shares, and Competitors Face High Barriers to Entry, in the Provision of DS1 and DS3 Special Access Services.....	14
B. Incumbent LEC Exclusionary Purchase Arrangements Prevent Competition from Developing Without Yielding Any Identifiable Efficiencies or Other Benefits.....	20
1. Incumbent LEC Exclusionary Purchase Arrangements Effectively Require Competitors to Purchase a Large Proportion of Their Special Access Demand from Incumbent LECs.....	20
2. Incumbent LEC Exclusionary Purchase Arrangements Tie the Sale of Services That Are or Might Be Subject to Competitive Supply to the Sale of Services That Are Not Subject to Competitive Supply.....	30
3. Incumbent LEC Exclusionary Purchase Arrangements Harm Competition and Consumer Welfare.....	33
4. Incumbent LEC Exclusionary Purchase Arrangements Do Not Have Countervailing Efficiency Justifications.....	34
5. Antitrust Precedent Supports the Conclusion that Incumbent LEC Exclusionary Purchase Arrangements Are Anticompetitive and Harm Consumer Welfare.....	36
C. Incumbent LEC Exclusionary Purchase Arrangements Undermine the Policy Goals of Section 706.....	40
D. The Commission Should Take Several Steps Now to Address the Harm Caused by Incumbent LEC Exclusionary Purchase Arrangements.....	42

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III.	THE COMMISSION SHOULD UTILIZE A RELIABLE AND ADMINISTRABLE MEANS OF ASSESSING THE LEVEL OF ACTUAL AND POTENTIAL COMPETITION IN RELEVANT SPECIAL ACCESS MARKETS.....	47
A.	The Commission Should Adhere to its Established Market Power Framework and, Where Appropriate, Panel Regression Analysis, in Assessing the Level of Actual Competition in the Provision of Special Access Services.....	48
1.	Defining Relevant Product Markets.....	49
2.	Defining Relevant Geographic Markets	59
3.	Identifying Market Participants	62
4.	Applying the Established Market Power Framework to Measure Actual Competition in Relevant Special Access Markets	64
5.	Applying Panel Regressions to Relevant Special Access Markets.....	72
B.	There is No Reliable Basis for the Commission to Predict That Significant Competitive Entry Will Occur in Any Relevant Special Access Market.	74
1.	Applying the Market Power Framework to Measure Potential Competition in Relevant Special Access Markets	75
2.	Applying Panel Regression Analysis to Measure Potential Competition in Relevant Special Access Markets	79
IV.	CONCLUSION.....	82

REDACTED – FOR PUBLIC INSPECTION

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)	

**COMMENTS OF
BT AMERICAS, CBeyond, EARTHLINK, INTEGRA, LEVEL 3 AND TW TELECOM**

BT Americas Inc. (“BT”), Cbeyond Communications, LLC (“Cbeyond”), EarthLink, Inc. (“EarthLink”), Integra Telecom, Inc. (“Integra”), Level 3 Communications, LLC (“Level 3”), and tw telecom inc. (“tw telecom”) (collectively, the “Joint Commenters”), through their undersigned counsel, hereby submit these comments in response to Sections IV.A and C of the Further Notice of Proposed Rulemaking released on December 18, 2012 in the above-referenced proceeding.¹

I. INTRODUCTION AND SUMMARY

The Joint Commenters applaud the Commission for adopting the *Data Request Order* and *Further NRPM*. This combined item is another step toward completion of the Commission’s review of the regulatory regime governing incumbent LEC special access services. It is no secret that this step is long overdue, however, since the Commission has now been reviewing its special

¹ *Special Access 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*, Report and Order and Further Notice of Proposed Rulemaking, 27 FCC Rcd. 16318 (2012). In these comments, the Report and Order is referred to as the “*Data Request Order*.” The Further Notice of Proposed Rulemaking is referred to as the “*Further NPRM*.”

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access rules for a decade. The Commission must therefore move forward as quickly as possible to complete the final steps in this proceeding. Those steps include working closely with the Office of Management and Budget (“OMB”) to complete the review of the data request pursuant to the Paperwork Reduction Act, collecting and analyzing the requested data, and reaching final conclusions as to the appropriate regulatory regime for incumbent LEC special access services. It is well within the Commission’s power to complete this process and issue final rules in this proceeding by the summer of 2014. It must do everything in its power to do so.

By now it should be beyond dispute that the regulatory treatment of special access has broad implications for American businesses and the U.S. economy. Special access service is a “general purpose technology” used as a platform for innovation, investment, and competition in virtually every sector of the economy. High prices and suppressed competition in this market and in downstream business broadband service markets are costing U.S. businesses and consumers hundreds of thousands of jobs and billions of dollars in consumer welfare.² These costs mount every month that passes without the adoption of appropriate constraints on incumbent LECs’ abuse of their market power.

While the incumbent LECs will undoubtedly argue that there is no need to address this problem, they take an entirely different view when operating in countries where they lack the enormous advantages of incumbency. For example, in a 2011 filing with Ofcom, the

² See Susan M. Gately *et al.*, Economics and Technology, Inc., *Regulation, Investment and Jobs: How Regulation of Wholesale Markets Can Stimulate Private Sector Broadband Investment and Create Jobs*, at 1-3, 6-11 (dated Feb. 2010) (attached to Letter from Harold J. Feld, Legal Director, Public Knowledge; William Weber, Chief Administrative Office, Cbeyond; Anthony Hansel, Assistant General Counsel, Covad; Russell Merbeth, Assistant General Counsel, Integra; William A. Haas, Vice President Public Policy & Regulatory, PAETEC; Don Shephard, Vice President, Federal Regulatory Affairs, tw telecom, to Marlene H. Dortch, Secretary, FCC, GN Docket No. 09-51; WC Docket Nos. 05-25, 06-172, 07-97, 09-135, 09-222 (filed Feb. 12, 2010)).

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telecommunications regulator in the United Kingdom, Verizon explained that “Verizon holds the view that continued regulatory controls must remain in place to safeguard access to the necessary wholesale inputs and thereby support competition to the benefit of customers.”³ Verizon went on to explain that Ofcom should adopt regulations—including rate regulations—necessary to ensure that competitors have access to incumbent LEC local transmission facilities on reasonable terms and conditions:

As a general principle, Verizon considers that the prices of core access products should be as low as possible in order to facilitate a genuinely competitive marketplace and drive down prices for customers. It is clear that the most effective way to achieve this is to ensure that operators who have [significant market power] in the relevant markets adhere to [price] controls.⁴

The benefits of these policies need not and should not be limited to businesses and consumers located in *other* countries. The Commission should follow Verizon’s advice to ensure that “necessary wholesale inputs,” such as DS1 and DS3 as well as Ethernet and other packet-mode special access services, are available in *this* country on reasonable rates, terms and conditions.

Addressing Incumbent LEC Exclusionary Conduct. The Commission should begin by addressing the exclusionary effects of incumbent LEC special access purchase arrangements (hereinafter referred to as “exclusionary purchase arrangements”). These arrangements take many forms, including generic tariff offerings, contract tariffs and commercial agreements, but they all contain loyalty and tying provisions that are unreasonable and that violate the prohibition against unreasonable conduct by common carriers in Section 201(b) of the Communications

³ See Verizon Business Response to Ofcom – BCMR Call for Inputs, at 1 (June 2011), *available at* <http://stakeholders.ofcom.org.uk/binaries/consultations/bcmr-inputs/responses/Verizon.pdf>.

⁴ *Id.* at 2-3.

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Act.⁵ As explained below, the Commission has held that it may enforce that provision against any carrier, regardless of whether it has market power.

As Dr. Stanley Besen and Dr. Bridger Mitchell—two leading experts in competition and pricing in the telecommunications industry—explain in a paper filed as Appendix A to these comments, exclusionary purchase arrangements are especially harmful to competition when imposed by a firm with a high market share in a market characterized by high entry barriers.⁶ The markets for DS1 and DS3 special access services—the services encompassed by the incumbent LEC exclusionary purchase arrangements—clearly meet these criteria. The Commission, the Department of Justice (“DOJ”), and the Government Accountability Office (“GAO”) have all concluded that incumbent LECs have extremely high market shares in the provision of DS1 and DS3 special access services. In the *Data Request Order*, the Commission repeated this conclusion, observing that non-incumbent LEC competitors (hereinafter referred to as simply “competitors”) serve only “a relatively small proportion of all locations that have special access.”⁷ In addition, data recently filed in this proceeding further support these conclusions. Moreover, the Commission has long held that the provision of DS1 and DS3 services is characterized by extremely high entry barriers.

As Drs. Besen and Mitchell explain, the incumbent LECs’ exclusionary purchase arrangements perpetuate and exploit the incumbent LECs’ position in the markets for DS1 and

⁵ 47 U.S.C. § 201(b). The Communications Act of 1934, 47 U.S.C. §§ 151 *et seq.* (“Communications Act” or “Act”), was amended by the Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (“1996 Act”).

⁶ *See generally* Stanley M. Besen and Bridger M. Mitchell, “Anticompetitive Provisions of ILEC Special Access Arrangements” (dated Feb. 11, 2013) (attached hereto as “Appendix A”) (“*Besen and Mitchell Paper*”).

⁷ *Data Request Order* ¶ 25.

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DS3 special access services by (1) forcing competitors to purchase a large proportion of their special access demand from incumbent LECs and (2) tying the sale of special access services (and sometimes other services) that are or might be subject to competitive supply to the sale of special access services that are not subject to competitive supply. These arrangements harm competition and result in higher prices for special access services by: (1) causing demand for incumbent LEC DS1 and DS3 special access services to become less elastic, thereby giving the incumbent LECs the incentive and ability to increase rates for these services without the threat of losing sales to alternative providers of special access services; (2) depriving competitors of the ability to expand their operations to achieve economies of scale, thereby requiring those competitors to increase their prices; and (3) diminishing competitors' investment in research and development. At the same time, there is no efficiency justification for these arrangements. Moreover, by stifling competitive deployment of local fiber transmission facilities and suppressing demand for Ethernet and other packet-mode special access services, the incumbent LECs' exclusionary purchase arrangements undermine the goal of increased deployment and adoption of advanced services set forth in Section 706 of the 1996 Act.

In light of the incumbent LECs' high market share and the existing high barriers to entry into the provision of DS1 and DS3 services, the Commission need not and should not await the completion of the upcoming data gathering and review process before adopting regulations that address the effects of the incumbent LEC exclusionary purchase arrangements. As Drs. Besen and Mitchell recommend, the Commission should, among other things, promptly adopt regulations that: (1) limit the size of the volume commitment that an incumbent LEC may require as a condition of providing a discount or other benefit; (2) prevent incumbent LECs from using unjustified termination penalties as a means of engaging in anticompetitive conduct; and

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(3) require that each incumbent LEC offers, throughout its territory and across its DS1 and DS3 service offerings, any purchase arrangement that it offers for any DS1 or DS3 special access service in any part of its service area. Taken together, these basic protections would increase alternative wholesale providers' opportunity to compete for the provision of special access services. The resulting benefits in the form of investment, innovation, job creation and lower prices will contribute to economic growth.

Analyzing Incumbent LEC Market Power. While the Commission must address the incumbent LECs' exclusionary practices as soon as possible, it must also of course address the incumbent LECs' high monthly recurring prices for DS1 and DS3 special access services as well as the high prices that many incumbent LECs charge for Ethernet and other packet-mode special access services. While the record already supports firm conclusions regarding incumbent LEC market share and entry barriers in the provision of DS1 and DS3 services, the Joint Commenters nevertheless support the Commission's decision to proceed with an extensive mandatory data request as a means of developing an even more comprehensive factual record regarding competitors' deployment of facilities and the prices charged for special access services by both incumbent LECs and competitors.

Actual Competition. The Commission states in the *Further NPRM* that it intends to assess the level of both actual and potential competition in relevant markets by utilizing a combination of the established market power framework and panel regressions. Given the extent to which these analytical frameworks overlap, the Joint Commenters suggest that the Commission choose either the market power framework or panel regressions rather than apply both frameworks. It would be simpler for the Commission to apply the market power framework, although it may be possible for the Commission to utilize panel regressions *in lieu* of

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the market power framework. In order for the Commission to utilize panel regressions, it would need to overcome significant methodological challenges, as discussed below.

In any event, both of these methodologies require that the Commission define relevant product and geographic markets. In so doing, the Commission should adhere to certain bedrock principles. For example, in defining product markets, the Commission should, among other things, (1) exclude “best efforts” services, such as cable modem services, from any relevant product market for dedicated special access services; (2) consider utilizing the capacity of services as a simplified means of defining markets; (3) treat channel termination and transport services as separate product markets where, as with DS1 and DS3 services, those two services are offered separately at different prices but not treat these components as separate product markets where, as with Ethernet, channel termination and transport are offered on an integrated basis and at a single price; and (4) treat services sold to wholesale and retail purchasers as belonging to different product markets.

In defining geographic markets, the Commission should determine the geographic area in which a service provider’s network must be located in order to offer a competitive service in a relevant product market at a particular location. Given the barriers to extending the reach of fiber networks to new locations, it is likely that the Commission will need to define the relevant geographic markets for DS1, DS3 as well as mid- and low-capacity Ethernet and other packet-mode services as the commercial building or particular transport route where the service is demanded. The Commission will also need to aggregate these relevant geographic markets into larger areas (*e.g.*, wire centers) subject to similar levels of competition.

The Commission must also identify market participants. In so doing, it should only consider firms that utilize their own transmission facilities. Firms that rely on leased incumbent

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LEC facilities should not qualify as market participants. Moreover, the Commission should only count as market participants those firms with facilities that are capable of providing services in the relevant product market.

The Commission would need to account for different issues when applying the market power test as opposed to regression analysis to assess the level of actual competition among market participants in relevant markets. When utilizing the market power test, the Commission would need to assess market shares. While it is already clear, as explained, that incumbent LECs have very high market shares in the provision of DS1 and DS3 services across their territories, it may be useful for the Commission to identify variations in market shares in different locations. The Commission should measure market shares by counting facilities that can be used to provide the service in the relevant market, even if the facilities are not yet used for this purpose. In all relevant markets, the Commission should presume that the presence of a single competitor is insufficient to discipline incumbent LEC conduct.

The Commission must also analyze demand and supply elasticity and the effect of incumbent LECs' structural advantages that yield lower costs when providing special access services. In assessing elasticities of demand and supply, it is especially important that the Commission account for the harmful effects of incumbent LEC exclusionary purchase arrangements as well as the high barriers to extending the reach of local transmission facilities. These factors combine to dramatically limit both elasticities of demand and supply in special access markets.

Once the Commission has identified relevant markets in which incumbent LECs have market power, it will need to compare incumbent LEC prices in those markets with suitable benchmarks for reasonable prices. In the case of DS1 and DS3 services, the Commission could

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use prices for unbundled network elements (“UNEs”) as benchmarks. In the case of Ethernet and packet-mode services, the Commission could compare incumbent LEC wholesale prices with the wholesale prices charged by other incumbent LECs and by competitors, and with the retail prices charged by incumbent LECs and competitors for these services. These comparisons will enable the Commission to determine the extent to which incumbent LECs are charging supra-competitive prices for special access services.

Reliance on panel regressions to assess the level of actual competition in relevant special access markets implicates a different set of considerations. It is theoretically possible for the Commission to use panel regressions to identify the market conditions in which incumbent LECs are able to maintain supra-competitive prices in a relevant market. To do so, however, the Commission would need to account for a wide range of variables. For example, it would need to somehow exclude competition from firms that provide services via leased incumbent LEC facilities. It would also need to account for the fact that, as discussed, incumbent LEC exclusionary purchase arrangements artificially inflate prices even beyond their already high levels. It may also find that incumbent LEC prices generally do not vary from one location to another and that, where they do vary, the differences are not caused by competitive conditions as much as the specific non-price benefits incumbents receive from a discount arrangement negotiated with a particular customer. The Commission will need to account for these and other factors.

Potential Competition. Finally, assessing the level of potential competition would again require that the Commission account for the differences between the market power framework and panel regressions. But the result of any such analysis should already be clear: there is simply no reliable basis for predicting that there will be significant entry into any relevant special access

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market in which incumbent LECs possess market power. Under the market power framework, the Commission only considers future entry relevant if it would be timely, likely and of sufficient scale to counteract incumbent LECs' exercise of market power. The reality is that the barriers to entry into special access markets continue to be extremely high and that incumbent LEC exclusionary purchase arrangements essentially lock up demand and restrict the opportunities for entry. These facts alone should limit the Commission's confidence that entry is likely to occur in a particular circumstance. In addition, the Commission has a long history of predicting future competition in the special access market, but every one of those predictions has been proven to be wrong. There is therefore no basis for predicting that future entry into a special access market in which the incumbent LECs have market power will be timely, likely and of sufficient scale to counteract incumbent LECs' exercise of market power.

Nor would it be possible for the Commission to rely on panel regressions to predict circumstances in which entry will occur in the future. Utilizing panel regressions in this manner is significantly more difficult than would be the case for analyzing actual competition because the factors affecting future entry are more numerous and complex. Most importantly, the Commission would need to account for the effects of incumbent LEC exclusionary purchase arrangements. These effects largely determine the circumstances in which entry occurs, and they govern a large percentage of the special access services purchased in this country. It is not at all clear that the Commission could control for these effects. The Commission would also need to account for a wide range of variables across geographic areas that affect entry, including differences in the terms and conditions for obtaining access to commercial buildings, to public rights of way, and to utility-owned poles, ducts and conduits. It would also need to account for

differences in labor costs, building density and other factors that affect the cost of deploying fiber.

In the end, the far more sensible approach to potential competition would be for the Commission to conclude—in light of the significant barriers to entry and the Commission’s long history of incorrect predictions of future entry—that there is no basis for predicting timely entry into relevant special access markets in which incumbent LECs are dominant. Instead, the Commission should promptly adopt protections against the harmful effects of incumbent LEC exclusionary purchase arrangements discussed above and, of course, other regulations needed to constrain incumbent LEC abuse of market power. After those protections have been in place for a period of time, the Commission can reassess the level of actual as well as potential competition in the market.

II. THE COMMISSION SHOULD ADOPT RULES NOW TO DIMINISH THE HARMFUL EFFECTS OF INCUMBENT LEC EXCLUSIONARY PURCHASE ARRANGEMENTS.

In the *Further NPRM*, the Commission states that it plans to gather further information regarding the terms and conditions of incumbent LEC special access purchase arrangements and to engage in further analysis of the effect of these terms and conditions on competition in relevant special access markets.⁸ As explained in Section III *infra*, the Joint Commenters support a data-intensive review of the relevant special access product markets. Nevertheless, the Commission need not and should not wait until it has concluded its market analysis to begin to curb incumbent LECs’ harmful exclusionary practices in the market for special access services.

The Commission has the authority to adopt rules now to address these harms. The existing record demonstrates that incumbent LECs have induced a large percentage of wholesale

⁸ *Id.* ¶¶ 91-93.

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purchasers of special access services to enter into tariffed discount plans, contract tariffs, and non-tariffed commercial agreements that contain anticompetitive terms and conditions (*i.e.*, exclusionary purchase arrangements). Many of these terms and conditions are patently unreasonable in violation of Section 201(b) of the Act.

Under the U.S. Communications Act, the Commission may adopt regulations designed to limit the harmful effects of these exclusionary purchase arrangements even without proof that the incumbents have market power in the provision of DS1 and DS3 special access services. Indeed, “the Commission has never previously refrained from enforcing sections 201 and 202 against common carriers, even when competition exists in a market.”⁹ Rather, “where the Commission has reclassified carriers as ‘non-dominant’ because they lack market power, . . . the Commission has continued to require compliance with sections 201 and 202.”¹⁰

In any event, as explained below, there is ample evidence to support the conclusion that incumbent LECs *are* dominant in the provision of DS1 and DS3 special access services.

Specifically, incumbent LECs possess overwhelming market shares in the facilities-based provision of DS1 and DS3 special access services, and these market shares are extremely durable

⁹ *In the Matter of Personal Communications Industry Association’s Broadband Personal Communications Services Alliance’s Petition for Forbearance for Broadband Personal Communications Services et al.*, Memorandum Opinion and Order and Notice of Proposed Rulemaking, 13 FCC Rcd. 16857, ¶ 17 (1998) (“*PCIA Forbearance Order*”). The Commission has often acted to prohibit anticompetitive conduct absent a market power finding. *See, e.g., In the Matter of Exclusive Service Contracts for Provision of Video Services in Multiple Dwelling Units and Other Real Estate Developments*, Report and Order and Further Notice of Proposed Rulemaking, 22 FCC Rcd. 20235, ¶ 38 (2007) (prohibiting exclusive contracts between all MVPDs and MDU owners regardless of whether a given MVPD possesses market power); *In the Matter of Promotion of Competitive Networks in Local Telecommunications Markets*, Report and Order, 23 FCC Rcd. 5385 (2008) (extending MDU exclusivity prohibition to telecommunications carriers regardless of whether a given telecommunications carrier possesses market power).

¹⁰ *PCIA Forbearance Order* ¶ 17.

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because of the high entry barriers faced by competitors. As Drs. Besen and Mitchell explain, substantial and enduring market share combined with high entry barriers gives a firm the ability to stifle future competition by imposing exclusionary loyalty and tying arrangements on their customers.¹¹ This is exactly what the incumbent LECs have done.

The Commission should act as soon as possible to adopt rules designed to diminish the harmful effects of the incumbent LECs' exclusionary terms and conditions. The Commission should not wait to gather further data and analyze that data. The process of finalizing and obtaining OMB approval for the data request, collecting information submitted in response thereto, conducting an extensive market analysis based on this information, and adopting comprehensive final rules will take more than a year.¹² Meanwhile, each month that passes is another month in which American businesses must make do without the benefits of a truly competitive business broadband marketplace.¹³ There is simply no reason for the Commission to stand by and do nothing while this harm continues. Prompt action will establish the preconditions for what will hopefully be increased competition in the future, potentially yielding very large benefits to consumer welfare.

¹¹ See *Besen and Mitchell Paper* ¶ 13.

¹² See, e.g., Comments of Cbeyond, Integra, EarthLink, Level 3 and tw telecom, GN Docket No. 12-353, at 2, 6-13 (filed Jan. 28, 2013) (setting forth a timeline under which the Commission would adopt its final rules in spring 2014).

¹³ See Comments of the Office of Advocacy, U.S. Small Business Administration, WT Docket No. 12-69; WC Docket Nos. 10-188, 05-25; GN Docket No. 09-51, RM-11358, at 5 (filed May 24, 2012) (“Broadband remains an indispensable input for growing businesses. . . . [P]reserving and promoting competition in the business broadband market is essential in order to provide small businesses with affordable access and choice regarding the services they need to grow and create new jobs.”); *id.* (“[T]he FCC’s special access docket requires particularly urgent attention.”).

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A. Incumbent LECs Possess Overwhelming Market Shares, and Competitors Face High Barriers to Entry, in the Provision of DS1 and DS3 Special Access Services.

The fundamental characteristics of the markets for facilities-based DS1 and DS3 special access services have long been understood. Incumbent LECs possess ubiquitous networks, allowing them to provide such services to every commercial building in the country. Any company seeking to compete with an incumbent LEC by constructing its own facilities to a given location faces exceptionally high barriers that often preclude entry.¹⁴ Thus, incumbent LECs have managed to retain overwhelming market shares in the provision of relatively low capacity services (such as DS1s and DS3s) that show no signs of falling. Year after year, the Commission, the DOJ, and numerous independent researchers have reaffirmed these conclusions.

In its 2005 review of the proposed SBC-AT&T and Verizon-MCI transactions, for example, the DOJ found that “[f]or the vast majority of commercial buildings in its respective territory, either SBC or Verizon is the only carrier that owns a last-mile connection to the

¹⁴ As the Commission explained in the *Triennial Review Remand Order*, there are “substantial fixed and sunk costs” involved in deploying competitive transport and loop facilities. *In the Matter of Unbundled Access to Network Elements; Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, Order on Remand, 20 FCC Rcd. 2533, ¶¶ 72-77, 150-154 (2005) (“*Triennial Review Remand Order*” or “*TRRO*”). These costs include, among other things, “the costs of obtaining rights-of-way and other necessary legal permissions, the costs of the actual fiber-optic facilities, and the costs of physical deployment itself.” *Id.* ¶ 150, n.149. In addition, competitors also face “substantial operational barriers” to deploying their own facilities, such as “problems in securing rights-of-ways from local authorities” and “construction moratoriums which prevent the grant of a franchise agreement to construct new facilities in the public rights-of-way.” *Id.* ¶ 151. tw telecom’s experience is particularly informative. For years, tw telecom has invested billions of dollars of capital—often amounting to between 23 and 25 percent of its annual revenues—in order to construct fiber facilities to commercial buildings. Yet, even at this aggressive and sustained level of investment, tw telecom has only been able to construct last-mile facilities to approximately 17,000 commercial buildings nationwide.

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building.”¹⁵ The DOJ explained that competitive entry is “difficult, time-consuming, and expensive,” and that “firms typically only build a connection after they have secured a customer contract of sufficient size to justify the anticipated construction costs.”¹⁶ The FCC similarly found that there was “little potential for competitive entry” because of the high entry barriers faced by competitors.¹⁷

Soon thereafter, a report by the GAO reached similar conclusions.¹⁸ The GAO studied 16 urban markets and found that competitors had deployed loop facilities to, on average, less than 6 percent of the buildings with demand of a DS1 or greater in those markets.¹⁹ The GAO found that nearly all of the loops that competitors had deployed were to buildings with demand far

¹⁵ Opinion, *United States v. SBC Communications, Inc. & AT&T Corp.*; *United States v. Verizon Communications, Inc. & MCI, Inc.*, Civil Action No. 05-2102, at 7 (D.D.C. Mar. 29, 2007) (citing Complaint, *United States v. SBC Communications, Inc. & AT&T Corp.*, Civil Action No. 05-2012, ¶ 15 (D.D.C. filed Oct. 27, 2005) (“*DOJ SBC-AT&T Complaint*”); Complaint, *United States v. Verizon Communications, Inc. & MCI, Inc.*, Civil Action No. 05-2012, ¶ 15 (D.D.C. filed Oct. 27, 2005) (“*DOJ Verizon-MCI Complaint*”)).

¹⁶ *Id.* at 10 (citing *DOJ SBC-AT&T Complaint* ¶ 27). The DOJ identified five factors that affect whether a competitive LEC can build a new last-mile facility to a particular location: “(1) the proximity of the building to the CLEC’s existing network interconnection points; (2) the capacity required at the customer’s location (and thus the revenue opportunity); (3) the availability of capital; (4) the existence of physical barriers, such as rivers and railbeds, between the CLEC’s network and the customer’s location; and (5) the ease or difficulty of securing the necessary consent from building owners and municipal officials.” *Id.*

¹⁷ *In the Matter of SBC Communications Inc. and AT&T Corp. Applications for Approval of Transfer of Control*, Memorandum Opinion and Order, 20 FCC Rcd. 18290 ¶ 39 (2005) (“*SBC-AT&T Merger Order*”), *In the Matter of Verizon Communications Inc. and MCI, Inc. Applications for Approval of Transfer of Control*, Memorandum Opinion and Order, 20 FCC Rcd. 18433 ¶ 39 (2005) (“*Verizon-MCI Merger Order*”).

¹⁸ See GAO, *FCC Needs to Improve Its Ability to Monitor and Determine the Extent of Competition in Dedicated Access Services*, GAO 07-80 (rel. Nov. 2006) (“*GAO Report*”).

¹⁹ *Id.* at 19-20.

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greater than a single DS1, and that competitive entry at low circuit capacities was unlikely.²⁰ Because of “long-standing entry barriers” that “are not likely to be alleviated,” the GAO concluded that “wireline facilities-based competition itself may not be a realistic goal for some segments of the market for dedicated access”²¹ Similarly, another independent research group, the National Regulatory Research Institute (“NRRRI”), found that in 2007, the median percentage of special access sales attributable to the incumbent LEC in a given market was 99 percent for DS1 channel terminations, 98 percent for DS1 transport, 91 percent for DS3 channel terminations, and 67 percent for DS3 transport.²² Based on this data and the entry barriers faced by competitors, NRRRI concluded that incumbent LECs “still have strong market power in most geographic areas, particularly for channel terminations and DS-1 services.”²³

All available evidence indicates that this situation has not materially changed. In 2007 and 2008, the Commission reviewed the extent of competitive fiber deployment in 10 urban areas selected as the basis of petitions for forbearance filed by Verizon and Qwest.²⁴ Verizon and Qwest presumably chose these areas because they are subject to more competition than any other geographic areas in their incumbent LEC territories. After studying these areas, the

²⁰ *Id.*

²¹ *Id.* at 42.

²² P. Blum, National Regulatory Research Institute, *Competitive Issues in Special Access Markets*, Revised Edition, at 42 (first issued Jan. 21, 2009) (“NRRRI Study”).

²³ *Id.* at 79.

²⁴ See *In the Matter of Petitions of the Verizon Telephone Companies for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Boston, New York, Philadelphia, Pittsburgh, Providence and Virginia Beach MSAs*, Memorandum Opinion and Order, 22 FCC Rcd. 21293 (2007) (“6-MSA Order”); *In the Matter of Petitions of Qwest Corp. for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Denver, Minneapolis, St. Paul, Phoenix and Seattle MSAs*, Memorandum Opinion and Order, 23 FCC Rcd. 11729 (2008) (“4-MSA Order”).

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Commission found that competitors served only 0.25 percent of commercial buildings with their own fiber facilities in the six markets selected by Verizon, and served only between 0.17 percent and 0.26 percent of commercial buildings in the four markets selected by Qwest.²⁵ Competitors in these markets were effectively required to rely on the incumbent LEC’s facilities because they lacked “any significant alternative sources of wholesale inputs.”²⁶ Similarly, in 2010, the Commission determined that Qwest faced insufficient competition in the market for wholesale loops and in the market for retail enterprise services to justify forbearance in the Phoenix Metropolitan Statistical Area (“MSA”), the urban area that Qwest presumably selected as the *most* competitive in its incumbent LEC territory.²⁷ The record in that proceeding further indicated that “the existence of significant barriers to entry, both in general and specifically in the Phoenix MSA, indicate[d] that potential competition poses no significant competitive constraint.”²⁸

Even more recently, the Commission found in the August 2012 *Pricing Flexibility Suspension Order* that the evidence in the record raises serious questions as to whether competitors have deployed transmission facilities to provide special access services in areas

²⁵ 6-MSA Order ¶ 41; 4-MSA Order ¶ 40.

²⁶ 6-MSA Order ¶ 38 (emphasis added); see also 4-MSA Order ¶ 37.

²⁷ See *In the Matter of Petition of Qwest Corporation for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Phoenix, Arizona MSA*, Memorandum Opinion & Order, 25 FCC Rcd. 8622, ¶ 71 (2010) (“*Phoenix Order*”) (“[T]he record indicates that, other than Qwest, there are no significant suppliers of relevant wholesale loops with coverage throughout the Phoenix MSA, either individually or in the aggregate.”); *id.* ¶ 87 (“Qwest has not demonstrated that there exists significant actual or potential competition for enterprise services by competitors that rely on their own last-mile connections to serve customers”).

²⁸ *Id.* ¶ 72.

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subject to pricing flexibility.²⁹ Soon thereafter, the Commission concluded in the *Data Request Order* that competitors still serve only “a relatively small proportion of all locations that have special access.”³⁰

New information submitted into the record in this proceeding further supports these findings. An analysis of the data submitted in response to the Commission’s first data request yielded the conclusion that non-incumbent LEC service providers own connections to less than [BEGIN HIGHLY CONFIDENTIAL] ■ [END HIGHLY CONFIDENTIAL] percent of the locations in 17 out of the 18 LSAs for which data was available, and to less than [BEGIN HIGHLY CONFIDENTIAL] ■ [END HIGHLY CONFIDENTIAL] percent of the locations in 14 out of the 18 LSAs for which data was available.³¹ In addition, by aggregating available lists of commercial buildings to which alternative providers own last-mile facilities, tw telecom recently analyzed the extent of competitive deployment in the Phoenix MSA.³² Even in this

²⁹ *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*, Report and Order, 27 FCC Rcd. 10557, ¶¶ 68-69 (2012) (“*Pricing Flexibility Suspension Order*”).

³⁰ *Data Request Order* ¶ 25. The Commission also acknowledged that “competition in the provision of special access appears to occur at a very granular level – perhaps as low as building/tower or a floor of a building,” *id.* ¶ 38, reaffirming the notion that even when an alternative provider has deployed facilities to particularly high-volume locations in a given geographic area, it cannot be assumed that it has deployed facilities to other locations in the same area.

³¹ See Declaration of Susan Gately, ¶ 4 (dated July 10, 2012) (attached as Attachment 2 to Petition of Ad Hoc Telecommunications Users Committee, BT Americas, Cbeyond, Computer & Communications Industry Association, EarthLink, MegaPath, Sprint Nextel, and tw telecom to Reverse Forbearance from Dominant Carrier Regulation of Incumbent LECs’ Non-TDM-Based Special Access Services, WC Docket No. 05-25, at 30-60 (filed Nov. 2, 2012) (“*Ad Hoc et al. Petition to Reverse Forbearance*”)).

³² See tw telecom Estimate of Non-Incumbent LEC Deployment in Phoenix MSA (attached hereto as “Appendix B”).

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market, tw telecom found that the incumbent LEC owns the only last-mile facility to more than [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] percent of commercial buildings.³³

The Joint Commenters' own purchase data paints a similar picture. As large purchasers of wholesale special access services, tw telecom and Level 3 have every incentive to purchase services from alternative wholesale providers in order to stimulate a more competitive market. However, tw telecom still purchases more than [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] percent of its DS1 channel terminations from incumbent LECs,³⁴ and Level 3 still purchases approximately [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] percent of its DS1 channel terminations and transport circuits from incumbent LECs.³⁵ This information simply confirms what is already abundantly clear—that incumbent LECs are dominant in the provision of DS1 and DS3 special access services.

³³ *See id.*

³⁴ In June 2012, approximately [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] percent of tw telecom's expenditures on all channel terminations—including both DS_n-based services and Ethernet services—were for purchases from incumbent LECs. For DS1 channel terminations, which accounted for more than [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] percent of the amount that tw telecom spent on channel terminations, more than [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] percent of its purchases were from incumbent LECs. Even for channel termination services that were provided using Ethernet technology, which accounted for less than [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] percent of the total amount that tw telecom spent on channel terminations, more than [BEGIN HIGHLY CONFIDENTIAL] [REDACTED] [END HIGHLY CONFIDENTIAL] percent of tw telecom's purchases were from incumbent LECs.

³⁵ *See* Level 3, Evidence that the Special Access Market is Not Competitive, and A Way to Remedy It, at 4 (dated June 27, 2012) (attached to Letter from Erin Boone, Senior Corporate Counsel, Federal Regulatory Affairs, Level 3, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25 *et al.* (filed June 28, 2012)).

B. Incumbent LEC Exclusionary Purchase Arrangements Prevent Competition from Developing Without Yielding Any Identifiable Efficiencies or Other Benefits.

Incumbent LECs exploit and perpetuate their dominance in the markets for facilities-based DS1 and DS3 special access services by inducing competitors to purchase services pursuant to purchase arrangements that contain anticompetitive terms and conditions. These exclusionary purchase arrangements (1) effectively require competitors to purchase a large proportion of their special access demand from incumbent LECs; and (2) tie the sale of services that are subject to competitive supply to the sale of services that are not subject to competitive supply. These so-called “loyalty” and “tying” practices further raise the barriers to competitive entry and solidify the incumbent LECs’ dominance in these markets.

1. Incumbent LEC Exclusionary Purchase Arrangements Effectively Require Competitors to Purchase a Large Proportion of Their Special Access Demand from Incumbent LECs.

In order to illustrate how incumbent LEC exclusionary purchase arrangements effectively require competitors to purchase a large proportion of their special access demand from incumbent LECs, this section outlines the structure of such arrangements and the context within which they are offered. Although incumbent LEC purchase arrangements are diverse in their details, many share the attributes described herein. For the purposes of illustration, we focus predominantly on two tariffed discount plans: (1) the Term Payment Plan (including its optional “portability commitment”), which AT&T offers in legacy Southwestern Bell and Pacific Bell territories³⁶; and (2) the Commitment Discount Plan, which Verizon offers in legacy Bell

³⁶ See Southwestern Bell Tariff F.C.C. No. 73 § 7.2.22; Pacific Bell Telephone Company Tariff F.C.C. No. 1 § 7.4.18.