September 7, 2005

Ex Parte

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, DC 20554

Re: ***Applications for Consent to Transfer Control of Filed by Verizon Communications, Inc. and MCI, Inc.*****, WC Docket No. 05-75**

Dear Ms. Dortch:

We are writing to respond to an ex parte presentation made on August 9, 2005, and again on August 22, 2005, by Mr. Rindler and Mr. Donovan of Swidler Berlin LLP on behalf of a variety of carriers ("Opponents").[1/] The Opponents largely repeat the same assertions that we have already addressed and refuted. Because the transaction will not result in any of the harms that the Opponents posit, the remedies they propose are unsupported and address issues that are not merger-specific. Accordingly, their proposed conditions should be rejected.

Special Access. The Opponents again assert (at 2, 3, 7, 12) that the transaction will harm competition by eliminating MCI as an independent provider of alternative fiber facilities. Yet they nowhere rebut Verizon/MCI's detailed evidentiary showing that there is competing fiber in the limited areas where Verizon and MCI have overlapping facilities. In the 39 areas where overlap does exist, there are a total of 92 fiber providers other than Verizon and MCI, there is at least one competing fiber provider in all but one of those areas (and that one area consists of a single wire center), there are competing providers in 89 percent of the individual wire centers where MCI has fiber, and there are an average of nearly 6 competing fiber providers in those wire centers. *See* Public Interest Statement at 31-34; Powell/Owens Decl. ¶¶ 6-9, 16-18; Lew/Lataille Decl. ¶¶ 18-24. Looked at from the building level, approximately 96 percent of the buildings that MCI serves "on-net" using its local fiber are located in specific wire centers where at least one other competitor has deployed fiber; 81 percent of those buildings are in wire centers where four or more other competitors have deployed fiber. *See* Lew/Lataille Decl. ¶ 24. The result is that in virtually all of the locations where MCI has deployed fiber there are other competitive fiber suppliers that are either already serving those exact locations, or that have nearby fiber facilities that could readily be extended to such locations.

[1/] *See* Letter from Patrick J. Donovan, Counsel for ACN Communications Services, Inc. et al. to Marlene Dortch, Secretary, FCC, WC Docket No. 05-75 (Aug. 10, 2005); Letter from Patrick J. Donovan, Counsel for ATX Communications, Inc. et al. to Marlene Dortch, Secretary, FCC, WC Docket No. 05-75 (Aug. 23, 2005).

For those limited set of buildings where there arguably is not already a fiber competitor in place, competitors could easily add the required network extensions, which need only be limited in scope. Approximately two-thirds of the MCI buildings are either already served by competing fiber or are within one-tenth of a mile of an existing CLEC fiber ring; and 86 percent of those buildings are within a half mile of an existing ring. *See* Letter from Dee May, Verizon and Curtis Groves, MCI to Marlene Dortch, Secretary, FCC, WC Docket No. 05-75, Attachment at 36-37 (Aug 25, 2005). The cost of deploying fiber laterals in these circumstances is not a significant barrier to entry: as the range of estimates from CLECs themselves demonstrates, the costs typically range from roughly $110,000 to $210,000 per mile. *See id.* at 38-41.

The demand at the MCI buildings would support the limited cost of such fiber extensions. At least 80 percent of MCI's lit buildings meet the "triggers" the Commission established for de-listing high-capacity DS3 loops, or have sufficient demand to justify the use of OCn circuits. *See* Powell et al. Reply Decl. ¶ 31. Moreover, in the vast majority of the MCI-lit buildings – at least 74 percent – MCI has customer demand for a single DS3 or more, which in MCI's experience generates enough revenues sufficient to recover the costs of constructing a fiber lateral. *See* Powell et al. Reply Decl. ¶ 28. And in at least 62 percent of MCI's lit buildings, MCI has customer demand at the OCn or near-OCn level, *see id.*, which the Commission has said generates sufficient revenues at that location to support new fiber deployment by a reasonably efficient CLEC. *See Triennial Review Remand Order* ¶¶ 21, 28, 87. And all of these figures significantly understate the extent to which competing carriers can deploy fiber to these locations because they represent only MCI's demand at the location, not total demand, which is undoubtedly higher in most or all cases. Thus, Verizon's acquisition of MCI's local fiber networks will not substantially lessen competition for special access services.

The Opponents also reiterate (at 2, 12) the contention that MCI is a significant independent provider of access services because it passes on unique volume discounts it receives on special access purchased from Verizon. But, as we have explained, MCI resells ILEC special access to only a minimal extent today, and it does not resell circuits obtained entirely from Verizon as special access. *See* Letter from Dee May, Verizon and Curtis Groves, MCI to Marlene Dortch, Secretary, FCC, WC Docket No. 05-75, at 2 (July 18, 2005) ("*Applicants' Response to Level 3*"). Nor are any "unique" discounts available to MCI. The overwhelming majority of Verizon's discount plans — including the plans from which MCI purchases the channel terminations that it resells — are term and not volume based, so that the same significant discounts are available to all carriers regardless of the size of the order. *See* Reply at 37-39; Powell et al. Reply Decl. ¶ 11.

The Opponents' vertical concerns (at 9-11) fare no better. Verizon/MCI already have rebutted assertions that the transaction will permit them to engage in a price squeeze or other forms of discrimination in the pricing or provisioning of special access. *See* Reply at 40-47. As an initial matter, issues concerning the pricing of special access services are not merger-specific but are the subject of ongoing rulemaking proceedings. Indeed, the merger itself does not change any theoretical incentive or ability Verizon might have to discriminate since it is already vertically integrated.

In any case, various regulatory safeguards protect against the types of discrimination the Opponents posit. The Opponents do not even mention these regulatory safeguards, let alone explain why they would not prevent the types of conduct they hypothesize. For example, Section 272(e) requires Verizon to provide special access to unaffiliated providers on terms and conditions that are no less favorable than those made available to affiliated providers. Furthermore, a BOC must impute to itself special access rates that are the same as those charged to unaffiliated providers. Commission regulations prevent Verizon from offering a new contract tariff for special access service to one of its long-distance affiliates until Verizon "certifies to the [FCC] that it provides service pursuant to that contract tariff to an unaffiliated customer." 47 C.F.R. § 69.727(a)(2)(iii). In addition, of course, special access is subject to price cap regulation, modified by pricing flexibility only in those MSAs where competitive fiber-based carriers are already in place. Moreover, as Verizon has shown, through pricing flexibility and other discounts, Verizon's average revenue per special access line has fallen, and at a faster rate than would have otherwise been required by price cap regulation. *See* Letter from Dee May, Verizon and Curtis Groves, MCI to Marlene Dortch, Secretary, FCC, WC Docket No. 05-75, at 4-5 (July 1, 2005).

The Opponents' claim (at 11) that the combined company will engage in undetectable non-price discrimination in terms of functions such as ordering and provisioning similarly provides no basis to place conditions on the merger. As an initial matter, special access performance metrics are already the subject of an ongoing industrywide rulemaking and do not raise merger-specific concerns. *See* Reply at 41. In any case, as noted above, section 272(e) already protects against these forms of discrimination, and both MCI and Verizon have proposed metrics to compare special access performance. *See id.* at 46-47. The Opponents' two purported examples of "discrimination" (at 11) do not support their point. With respect to commingling and Verizon's facilities policy, the issue was a good faith dispute concerning what services Verizon was required to provide. Verizon made no effort to hide its position, and the CLECs brought the issue to the Commission's attention: it hardly qualifies as an example of "undetectable" discrimination. The Opponents' reference to an alleged "finding" of discrimination by the New York PSC four years ago also provides no support for their claim: the fact that the PSC made such an initial "finding" (which Verizon subsequently contested[2/]) demonstrates that Regulators can and do review Verizon's performance.

Given that the transaction will not give rise to any of the competitive harms the Opponents conjecture, none of the self-serving remedies they seek are justified or appropriate. Regardless, their suggestion that MCI be required to divest all customers and/or local exchange and exchange access facilities would be disruptive and impractical.. Any divestiture of MCI's customers in Verizon's region would be inappropriate for a number of reasons, the most significant of which is that customers would rightly object to being "'involuntarily' conveyed" to another carrier. The enterprise customers that have chosen MCI, from among the possible suppliers, as the carrier for their mission-critical high-capacity services did so for a reason, and the Commission should not attempt to override that choice with a regulatory fiat that forces them

[2/] *See* Verizon New York Inc.'s Petition for Rehearing, Case 00-C-2051, at 5-8 (NY PSC filed July 16, 2001).

to have those services disruptively transferred to another carrier. Indeed, even other merger opponents such as Level 3 and Global Crossing have acknowledged the difficulties associated with divestiture of customers.[3/] Facilities divestitures likewise would result in substantial challenges from a practical standpoint. As Global Crossing has conceded, facilities divestures are "extremely complex," as "[f]acilities are not easily segregated" and complicated issues of coordination arise with respect to "[m]aintenance of facilities and equipment." June 2, 2005 Global Crossing Ex Parte at 23. The Opponents do not begin to discuss how such implementation issues would be addressed.

The Opponents' remaining proposals are solutions in search of a problem. Their proposal to regulate Verizon's special access pricing in various ways (at 17, 21) is not a merger-specific issue and should be decided in the industrywide rulemaking already underway. As noted above, however, under Commission rules, Verizon obtains special access pricing freedom only upon a showing that an MSA has significant competition. The Opponents offer no support for their proposal (at 18) that the Commission reimpose section 272 requirements that have already sunset or explain why such a reversal is necessary. In any case, section 272(e) (discussed above) continues beyond the sunset of other section 272 separation obligations. 47 U.S.C. § 272(f). And their suggestion (at 17) that the combined company be required to make available the lowest rate in any contract or tariff to all comers regardless of any volume or term requirement is self-serving and appears to be an effort to undermine the economics of offering those discounts, which would force Verizon to raise rates and become less competitive. That is a result that may be in the interests of these few competitors, but it is surely not in the public interest.

Mass Market. As we have demonstrated, the transaction will not harm competition in the mass market. The Opponents' bare assertion that competition will be diminished due to MCI's exit (at 3) ignores the substantial and unequivocal evidence that MCI's mass market business is in a continuing and irreversible decline and that it will not be one of a small number of significant competitors for mass-market customers going forward. *See, e.g.*, Public Interest Statement at 46-51; Reply at 60-62. Whether measured in terms of lines, revenues, or minutes, MCI's business has lost customers and traffic for long distance, local, and all-distance services. *See* Huyard Decl. ¶¶ 2-3; Huyard Reply Decl. ¶ 3. That decline has been accompanies by a significant cut back in marketing and advertising and the number of mass market employees. Huyard Decl. ¶¶ 16-17.

Moreover, facilities-based intermodal alternatives such as cable, wireless, and VoIP provide extensive and increasing competition for mass-market customers, and this transaction will not affect that competition. *See, e.g.*, Public Interest Statement at 39-45; Reply at 49-60. Because consumers increasingly view wireless, cable telephony, and VoIP as viable alternatives

[3/] *See* Level 3 June 17 Ex Parte Attach. at 2-3. Ex Parte Letter from Teresa D. Baer, Latham & Watkins LLP, to Marlene H. Dortch, FCC, WC Docket Nos. 05-65 & 05-75, at 23 (FCC filed June 2, 2005) (Global Crossing acknowledging that "[d]ivestiture of customers presents . . . challenges," chief among them being "[c]ustomer opposition.").

to wireline service, wireline access lines are now falling at a 5.2% annualized run-rate.[4/] Some major cable operators, including Time Warner Cable and Cablevision, already offer telephony services in all of their footprint; Comcast plans to expand its VoIP deployment to 15 million homes passed by the end of 2005, and to all the 40 million homes it passes by the end of 2006, while Cox already offers circuit-switched voice telephone service and VoIP to 6.8 million of the 10.7 million homes it passes nationally and plans to add five more markets by year-end.[5/] The surging availability of cable telephony service has been accompanied by rapid growth in the number of cable telephony subscribers. For example, Time Warner added over 240,000 net new customers in the second quarter of 2005, about sixty percent more than the number it added in the first quarter.[6/] Cablevision added more than 100,000 voice telephony customers in the second quarter of 2005 and now has approximately 478,000 customers.[7/] Industry experts forecast that cable and VoIP will have almost 7 million subscribers by year end and that in five years 45% of U.S. households will either be wireless only or subscribe to VoIP rather than wireline service.[8/] In addition to the loss of lines, intermodal competition is increasingly displacing revenue-producing traffic. For example, analysts estimate that wireless made up nearly 30 percent of voice minutes in 2004. *See* Public Interest Statement at 41-44.

The Opponents' assertion (at 14) that the transaction might cause independent facilities-based long distance carriers to die off is belied by the market facts. As we have shown, the wholesale long distance business is intensely competitive and includes numerous carriers other than MCI, including Sprint, Qwest, Level 3, Global Crossing, WilTel, and others. *See, e.g.*,

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4/ *See* Qaisar Hasan and May Tang, Buckingham Research Group, *The Last Mile – Monitoring Quarterly Trends in Telecommunications, Video and Data* at 1 (Aug. 18, 2005).

5/ *See* Craig Moffett, *et al.*, Bernstein Research Call, *Cable and Telecom: VoIP Deployment and Share Gains Accelerating; Will Re-Shape Competitive Landscape in 2005*, December 7, 2004; Thomson StreetEvents, *TWX—Q4 2004 Time Warner Inc. Earnings Conference Call*, Conference Call Transcript, February 4, 2005 (statement of Time Warner Inc. CFO Wayne Pace); Cablevision News Release, "Cablevision Systems Corporation Reports First Quarter 2005 Results" (May 5, 2005); Comcast, presentation at the Bear Stearns 18th Annual Media, Entertainment & Information Conference at 10-11 (Mar. 2, 2005); Cox Communications Inc. Summary of Operating Statistics, *attached to* Cox News Release, *Cox Communications Announces Second Quarter and Year-to-Date Financial Results for 2005* (Aug. 9, 2005); Cox News Release, *Cox Names New 2005 Telephone Markets* (Aug. 1, 2005).

6/ Time Warner Inc., Presentation of Wayne Pace, CFO, *Time Warner Inc.: Second Quarter 2005 Results* (Aug. 3, 2005).

7/ Cablevision Press Release, *Cablevision Systems Corp. Reports Second Quarter 2005 Results* (Aug. 9, 2005).

8/ *See* John Hodulik and Aryeh Bourkoff, UBS Investment Research, *Broadband Hit by Seasonality as VoIP Ramps* at 15 (Aug. 16, 2005); Frank G. Louthan, IV, Raymond James & Associates, Inc., *Reassessing the Impact of Access on Wireline Carriers* at 2 (July 11, 2005).

Reply at 65-66. Because Verizon does not have a national long-haul network of its own and generally does not provide wholesale long distance, the transaction will not reduce competition in this business. The claim that these other competitors will not survive because Verizon will move its long distance traffic to the combined company's network makes no sense: as the evidence demonstrates, the amount of wholesale long distance that Verizon purchases is a tiny fraction of the total amount of U.S. voice long distance wholesale revenues, let alone the total for all wholesale traffic that traverses these competitors' long-haul networks. *See id.* at 67.

Because the transaction will not harm mass market competition, the Opponents' proposed remedies are unnecessary and unjustified. As discussed above, proposals to divest facilities and customers (at 19) – aside from being needless here – are disruptive and impractical. The Opponents' suggestions (at 21) to freeze UNE prices for five years and to reduce "GTE" UNE rates to "Bell Atlantic/NYNEX" rates makes no sense. UNE rates are supposed to reflect costs. To the extent states find that those costs have changed or determine more accurate measures of those costs, UNE rates should reflect that rather than being arbitrarily frozen for five years. Further, costs, and therefore UNE rates, are state-specific, and there accordingly is no basis to reduce rates in one group of states to reflects rates in another group of states. Finally, the Opponents' offer no rationale for their proposal (at 22) that the Commission impose additional performance metrics or that penalties be paid to competitors. Verizon already is subject to a variety of performance metrics and penalty regimes, and there is no basis to conclude those existing rules are inadequate.

Internet. The Opponents offer no new analysis of any Internet-related issue but instead repeat the tired refrain that the transaction will substantially increase concentration in the Internet backbone business (at 15). However, as we have shown, the addition of Verizon's relatively small backbone to MCI's existing backbone will have do little to alter the status quo: the combined company will carry less than 10% of North American Internet traffic and remain fourth in traffic share among seven larger or comparable providers, and operators other than those seven would carry approximately 35 percent of Internet traffic. *See* Reply at 70-80; Kende Reply Decl. ¶ 8. The Opponents offer no response to these facts other than to speculate (at 6, 15) that *other* BOCs might someday acquire other Internet backbones. But obviously this transaction must be evaluated on its own merits, not based on hypothetical conjecture about some other transactions that may or may not occur sometime in the future. Because this transaction will not give the combined company "control" of the Internet backbone business, it will not have the ability or incentive to successfully engage in discrimination or strategic de-peering. *See* Reply at 69-86; Letter from Dee May, Verizon and Curtis Groves, MCI to Marlene Dortch, Secretary, FCC, WC Docket No. 05-75, at 3-11 (Aug. 8, 2005) ("*Applicants' Response to Earthlink*").

Given the absence of the anticompetitive effects that the Opponents posit, their proposed remedies (at 20) are unwarranted and unjustified. There is no need for the Commission to start regulating the pricing of interconnection and transit service because the Internet backbone business will remain highly competitive, and customers will have the choice of a variety of backbone operators from which to obtain interconnection and transit at market prices. *See, e.g.*, Reply at 75-76. The Opponents' call for "net neutrality requirements" is not a merger-specific issue, and, in any event, as we have previously explained, market forces – and in particular, the significant and growing competition from other broadband access providers – make nondiscrimination a matter of economic self-interest because providers will otherwise lose customers. *See, e.g.*, *Applicants' Response to Earthlink* at 11-12. Anticipatory regulation is both unnecessary and inappropriate in a competitive market and would only spawn a new regulatory regime that would hamper rather than promote development and deployment of new broadband services.

In sum, the Opponents offer no new arguments and fail to refute Verizon/MCI's detailed evidentiary showing. Accordingly, there is no basis for imposing their list of conditions.

Sincerely,

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cc: Julie Veach
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