

**TRO REMAND ORDER PUTS BALL BACK IN COURT; IMPAIRMENT THRESHOLD
HIGHER THAN EXPECTED**

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The FCC's much-anticipated "triennial review" order (TRO) on remand returns the issue of incumbent local exchange carriers' network unbundling obligations to the U.S. Court of Appeals in Washington.

The courts and the agency have been volleying network unbundling rules back and forth since the passage of the 1996 Telecommunications Act, and the three-Commissioner majority that adopted the latest version said they had judicial sustainability as a primary goal during the final crafting of the order. The appeals court has a pending "mandamus" proceeding that should ensure a speedy review of the remand order to determine whether it complies with the court's ruling that overturned the agency's TRO earlier this year.

In October the court issued an order holding in abeyance until Jan. 4 a petition for a writ of mandamus submitted by the U.S. Telecom Association, Verizon Communications, Inc., and Qwest Communications International, Inc. Wireline Competition Bureau Chief Jeffrey Carlisle told reporters the Commission would submit a brief to the court by that date explaining its decision and why it believes the order comports with the court's earlier ruling.

The FCC's 3-2 decision as expected eliminated unbundled access to mass market circuit switching and the availability of the unbundled network element platform (UNE-P) - albeit with a somewhat longer phaseout transition than was earlier contemplated - while retaining unbundled access to high-capacity loops and transport in more situations than would have been mandated by the TRO remand order first drafted by FCC staff. The decision also rejected incumbents' arguments for relief from unbundling requirements when special access is available as an alternative service offering.

The amalgamation of incumbent and competitor victories embodied in the decision - at least in comparison to the TRO and reports on the earlier draft version of the remand order - are the

result of what both Republican and Democratic commissioners described as intense negotiations, particularly during the final week before the Dec. 15 vote. Efforts to reach a compromise ultimately failed, however, apparently foundering over differences in how far the Commission could go in guaranteeing access to competitors while maintaining a judicially sustainable order.

'Reasonably Efficient' CLEC Assumed

Although the text of the order was not immediately available, the FCC offered fairly specific details on the decision. The order clarifies that impairment evaluations assume a reasonably efficient competitor and prohibits the use of UNEs for the provision of mobile wireless and interexchange telecom services. The 1996 Telecommunications Act requires the FCC to evaluate whether a competitor's ability to offer service would be impaired without access to a given network element when determining whether an ILEC must unbundle that element.

The FCC said that in applying the impairment test, "we draw reasonable inferences regarding the prospects for competition in one geographic market based on the state of competition in other, similar markets." It considered the appropriate role of tariffed local exchange carrier services in the unbundling framework and determined that "in the context of the local exchange markets, a general rule prohibiting access to UNEs whenever a requesting carrier is able to compete using an incumbent LEC's tariffed offering would be inappropriate."

With respect to impairment tests for high-capacity loops and transport, the order finds that competitors are impaired without access to DS1 transport except on routes connecting a pair of wire centers that both contain at least four fiber-based collocators or at least 38,000 business access lines.

The impairment threshold for DS3 and dark fiber transport between wire centers is at least three fiber-based collocators or at least 24,000 business access lines. The lack of access to entrance facilities connecting an incumbent's network with a competitor's network is deemed never to impair a competitor. The order sets a 12-month transition for competitors losing access to unbundled DS1 and DS3 dedicated transport and an 18-month transition for those losing access to dark fiber transport.

Competitors will be deemed impaired without access to DS3 loops except in wire centers containing 38,000 or more business lines and four or more fiber-based collocators. They will be deemed impaired without access to DS1 loops except in wire centers containing 60,000 or more business lines and four or more fiber-based collocators. The

order finds lack of unbundled access to dark fiber loops never constitutes impairment.

The order sets a 12-month transition for competitors losing access to unbundled DS1 and DS3 loops and an 18-month transition for those losing access to dark fiber loops.

There will be a 12-month transition for competitors losing access to mass market local switching.

Rates for loop and transport UNEs will be the higher of (1) 115% of the rate the requesting carrier paid for the UNE on June 15, 2004, or (2) 115% of a state commission rate established between June 16, 2004, and the effective date of the order. A similar rate provision applies to mass market local switching, except that the referenced rate will be increased by a dollar a month.

Transition plans apply only to the embedded customer base and do not allow new customers to be added. The transition periods will begin with the effective date of the order.

Powell: Sustainability at Issue

Speaking to reporters after the Commission's vote adopting the order, FCC Chairman Michael K. Powell said, "Most of our disagreements were just simply on the fault line of what people believed was sustainable and other people believed was not. I think that that's what it came down to. And it does not surprise me that you have a range of opinion from one end of the spectrum to the other for different purposes. That makes me feel like we probably drove it in the middle where it belonged."

Asked why the three-Commissioner Republican majority issued an order with provisions that were widely considered to be concessions made to Democratic Commissioners in the hopes of producing a unanimous decision, Mr. Powell said, "We happen to believe in facilities-based competition, too. ... We did significantly move in a direction to try to gain their support. You know, regrettably - and I respect their position - it wasn't enough for them.

"But my own belief was that I couldn't go any further without being almost certain that we were going to lose [in court]. I wasn't willing to have kind of a Pyrrhic decision that felt good but that wasn't going to be sustained. ...

"In credit to our own commitment to these items, we didn't take them out in retribution either. We proposed them, they didn't accept them, but we left them in the order anyway because we believed we could defend them. [Compared to media reports on the draft order a

few weeks before the vote], there's been a number of very significant improvements both towards the competitors and consumers. Transitions have been significantly lengthened, thresholds have been raised, tests have been set at levels that are very significant," Mr. Powell said.

Chairman Powell suggested that the elimination of UNE-P access ultimately would not have a great effect on consumers. "There are many, many opportunities for competition and choice heading for consumers, and I think for people to turn a blind eye to them is just simply willful ignorance of the kind of developments the technology is producing. I think, for example, voice-over-IP [and] cable telephony next year will likely provide more ... actual consuming Americans choices in those services than UNE-P has provided over an eight-year period."

In his statement during the meeting, Chairman Powell said he expected both competitors and incumbents to be unhappy with the decision. "One will undoubtedly hear the tortured hand-wringing by incumbents that they are wrongly being forced to subsidize their competitors. They have a legal duty to provide access under limited conditions and they do protest too much in arguing for the end of vast portions of their unbundling requirements. Conversely, one can expect to hear dire predictions of competition's demise from those who wanted more from this item," he said.

Early reactions from industry generally proved his prognostications true (see below).

Commissioner Kathleen Q. Abernathy, who supported the decision, said, "Determining which elements in which markets [should be unbundled] has been difficult," resulting in two reversals at the District of Columbia Circuit and one at the Supreme Court. "The only responsible decision is to adopt rules that faithfully adhere" to those court rulings, she added.

Commissioner Kevin J. Martin also voted for the order but expressed concerns about its legality. He said the decision gave "insufficient recognition to special access" in light of the appeals court's statements regarding the FCC's failure to take into account the availability of tariffed special access services when conducting the impairment analysis. He also expressed concern that the order fails to include a building-by-building analysis of impairment, relying instead on a wire-center level of analysis.

Commissioner Michael J. Copps, who was at home recovering from back surgery and participated in the FCC's meeting via teleconference, dissented from the decision, which he said "effectively dismantles facilities-based competition." He predicted

more competitive carriers would abandon residential markets, stranding investment, eliminating jobs, and leaving consumers with fewer choices. "Protestations of the need for judicially sustainable rules comes from the same people who refused to seek [Supreme] Court review" of the D.C. Circuit's decision, he added.

Commissioner Jonathan S. Adelstein, who also dissented, said the order "pulls the plug on competitors who tried to fulfill the promise" of the 1996 Telecommunications Act. "By not appealing the D.C. Circuit decision [vacating the TRO] to the Supreme Court, the majority placed itself in a box, in effect a coffin for telecom competition. Now the majority buried telecom competition six feet under. The only choice I was given was where to pound the nails," he said.

Commissioner Adelstein predicted the decision would disrupt service for thousands of businesses and likely would diminish innovation. He did say he appreciated the majority's willingness to extend the transition period.

ILECs, CLECs Both Voice Discontent

Both the incumbent and competitive local exchange industries took immediate issue with various aspects of the FCC order.

Walter B. McCormick Jr., president and chief executive officer of the U.S. Telecom Association, said the FCC was "moving in the right direction, although not fast enough, on phasing out the unlawful UNE platform." He added, "Instead of fully acknowledging the competitive choices across numerous platforms that exist today, key aspects of this order appear to defy the direction of the D.C. Circuit."

James C. Smith, senior vice president-FCC for SBC Communications, Inc., praised the FCC for eliminating "the harmful and unlawful UNE-P subsidy program on a going-forward basis," but criticized the agency for perpetuating "the harmful unbundling regime for high-capacity business lines. ... This irrational decision does not bode well for job creation, network investment, and consumer benefit."

He called the impairment test for DS1 loops a sham, saying that it would result in SBC having to unbundle loops in Houston, the eighth largest metropolitan statistical area, where "10 different carriers operate their own fiber networks and serve hundreds of separate buildings in Houston with those networks."

Steve Davis, Qwest Communications International, Inc.'s SVP-public policy, praised the FCC's decision on switching but saw many other flaws in the order. "For the fourth time, this Commission has defied

the courts by ignoring competition and opting instead for an approach to this industry that relies on intrusive government regulation," he said.

"Contrary to the court's directive that the Commission account for the tremendous growth of facilities-based competition across this country, its decision continues to require that incumbents provide more than 99% of their broadband facilities to competitors at below-cost prices. ... As previously announced, Qwest has entered commercial agreements to provide switching services to MCI [Inc.] and about a dozen other companies. It is our belief that this decision will not affect these arrangements and will cause other firms to follow the course we have established," Mr. Davis added.

BellSouth Corp. and Verizon Communications, Inc., issued similar statements praising the switching decision and criticizing the impairment analyses for loop and transport UNEs.

H. Russell Frisby Jr., CEO of CompTel/ASCENT, said, "While this decision is not unexpected, CompTel/ASCENT is disappointed that the FCC could not reach an acceptable compromise in this critical proceeding." He added that the FCC's decision could hinder investment and economic development: "Our hope is that, in the long term, this decision does not ultimately hamper the evolution of alternative IP [Internet protocol] networks and the deployment of competitive VoIP offerings."

Jonathan Lee, CompTel/ASCENT's SVP-regulatory affairs, elaborated on the association's problems with the order, in which the FCC appears to abandon its commitment to facilities-based competition, he said. "I don't really buy the fig leaf of judicial sustainability," he said, citing the Commission's decision to shorten the transition time for eliminating UNE-P although that particular provision of the TRO was not appealed and "wasn't in contention," he said.

References by FCC Commissioners and staff to the relatively small number of high-capacity loops affected by the TRO remand order struck Mr. Lee as "disingenuous" or evidence of "a striking ignorance to the reality of the market."

Facilities-based competition is capital intensive, leading competitors to concentrate their operations in particular markets, he said. So "it's not 7% of [DS1 lines in] Dubuque" that are affected, "it's 25% of New York and 0% of Dubuque," he said.

Furthermore, the provisions of the FCC's impairment tests for high-capacity loops that exempt incumbents from unbundling in wire centers where a threshold number of fiber collocators is present

don't necessarily mean competitors will have alternative wholesale suppliers of loops, he said. "To my mind [fiber collocator] just means someone who has fiber to the collo cage, but they're probably buying loops from the Bell. Why else would they be collocating?" he added.

Jason Oxman, general counsel of the Association for Local Telecommunications Services, said the FCC's decision "only partially delivers on its promise to develop network unbundling rules that ensure consumers and small businesses continue to benefit from the innovative broadband services facilities-based competitors have brought to the market."

AT&T Corp. issued a statement criticizing the FCC's decisions regarding mass-market switching and the high-cap UNE impairment tests.

Jim Kirkland, SVP and general counsel for Covad Communications, Inc., however, took a more optimistic view of the order. Noting that the text of the order was not yet available, he said, "Based on the discussion at the FCC's meeting, ... the new rules maintain access to high-cap loops (UNE DS1s) as unbundled network elements in the vast majority of cases, supporting Covad's provision of cutting-edge services such as voice over IP over its state-of-the-art broadband network."

The Consumer Federation of America also criticized the FCC's decision as "the final nail in the coffin of local competition for residential consumers." CFA Research Director Mark Cooper said, "The Bells will soon be able to leverage their new market power over new services, such as broadband and voice over Internet protocol, stymieing competition in those new territories as well."

He added, "The Commission failed to heed the court order and conduct analysis of local markets. A national finding of nonimpairment for switching is contradicted by the facts of this proceeding. Over half the offices in Texas, for example, have no competitive switching and no economic possibility of having any for the foreseeable future.

Michael D. Gallagher, administrator of the National Telecommunications and Information Administration, told TR through a spokesman, "We appreciate the FCC's adoption of new competition rules. In June, we called for an end to litigation and for adoption of legally sustainable rules that preserve appropriate competition. The FCC has now acted. The focus of all stakeholders should now be on meeting President Bush's call for universal, affordable access to broadband by 2007 - through investment, innovation, and competition."

Michigan Public Service Commissioner Robert Nelson, chair of the National Association of Regulatory Utility Commissioners' Telecommunications Committee, indicated disappointment in the FCC's decision in terms of the 12-month time frame allotted by the FCC for competitors to transition away from the use of unbundled mass market local switching.

"We were hoping for at least 18 months," he told TR, noting that for large competitive carriers - for example, Talk America with 350,000 customers in Michigan - 12 months may not be long enough to install their own equipment and go through the batch "hot-cut" process to transition customers to their own networks.

Meanwhile, NARUC President and Washington Utilities and Transportation Commission Chairwoman Marilyn Showalter lauded the FCC's impairment finding for DS1 facilities. However, she said NARUC remained "concerned about small-business customers in areas that are not covered by the FCC's impairment finding, as well as other important issues, including line sharing, that still require the FCC's immediate attention."

Commissioner Nelson also said he was disappointed that the FCC's rules didn't address line sharing.

Economist Criticizes Remand Order

The TRO order as described by the FCC includes a number of assumptions that are difficult to justify from an economic standpoint, according to a Washington think tank economist.

Among the problems in the order are the agency's decision to base its impairment analyses on a "reasonably efficient competitor," Phoenix Center Chief Economist George Ford said Dec. 17 at a Washington telecom symposium sponsored by his organization. He added that an inefficient competitor should get access to any network element it needs, and the FCC should "let the market kill it" for its inefficiency.

The FCC's decision to prohibit the use of UNEs to deliver purely interexchange services and commercial mobile radio services "is blatantly anticonsumer," Mr. Ford said.

Regarding the tests for determining impairment with respect to high-capacity interoffice transport, Mr. Ford noted the FCC had not said whether the required fiber collocators in the two offices on a given route had to be the same. Only if they are the same is it reasonable to assume that nonincumbent transport will be available, he said. With regard to high-capacity loops, "it is just silly" to

assume that trunk-side fiber collocation has anything to do with competitive alternatives for loop provisioning, he added.

The decision not to allow competitors to obtain switching UNEs for new customers during the one-year transition period will severely compromise the viability of their operations, given the 5% monthly customer churn they experience, Mr. Ford said. If a competitor starts the transition period with 100 customers and it takes it a year to get a switch up and running, attrition through churn and the inability to provision new customers will leave it with only 54 customers at the end of the year, he said.