**BEFORE THE PUBLIC SERVICE COMMISSION**
**OF THE STATE OF MISSOURI**

| | | |
|---|---|---|
| In the Matter of the Determination of Prices, Terms, and Conditions of Line-Splitting and Line-Sharing. | ) ) ) | Case No. TO-2001-440 |

**SOUTHWESTERN BELL TELEPHONE COMPANY'S**
**RESPONSE TO ORDER DIRECTING FILING**

COMES NOW Southwestern Bell Telephone, L.P. d/b/a Southwestern Bell Telephone Company ("Southwestern Bell") and for its Response to Order Directing Filing, respectfully states to the Missouri Public Service Commission ("Commission ") as follows:

1. On May 24, 2002, the United States Court of Appeals for the District of Columbia Circuit granted petitions for review in companion cases challenging the legality of the Federal Communications Commission's ("FCC") UNE Remand Order[1] and its Line Sharing Order.[2] See United States Telecomms. Ass'n v. FCC, 290 F.3d 415 (D.C. Cir. 2002). A copy of that decision is attached hereto as Exhibit 1. The D. C. Circuit expressly vacated the Line Sharing Order and remanded both decisions to the FCC for further consideration consistent with the principles outlined by the court. In its June 10, 2002 Order Directing Filing, the Commission requested the parties to submit briefs assessing the impact of the D.C. Circuit's USTA decision on these proceedings.

2. In the short run, the USTA decision is likely to have only a modest impact on these proceedings. Under the Federal Rules of Appellate Procedure, the court's mandate does

[1] Third Report and Order and Fourth Further Notice of Proposed Rulemaking, Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, 15 FCC Rcd 3696 (1999) ("UNE Remand Order"), petitions for review granted, United States Telecomms. Ass'n v. FCC, 290 F.3d 415 (D.C. Cir 2000) ("USTA").

[2] Third Report and Order in CC Docket No. 98-147 and Fourth Report and Order in CC Docket No. 96-98, Deployment of Wireline Services Offering Advanced Telecommunications Capability, 14 FCC Rcd 20912 (1999) ("Line Sharing Order"), vacated and remanded, United States Telecomms Ass'n v. FCC, 290 F.3d 415 (D.C. Cir 2000) ("USTA").

not issue until seven days after either the time for filing a petition for rehearing has passed (*i.e.*, 45 days) or the court denies a timely petition for rehearing. See Fed. R. App. P. 41(b). Because the D.C. Circuit issued the USTA decision on May 24, 2002, the court's mandate will not issue until at least July 15, 2002. Should a party file a petition for rehearing, the mandate will not issue until the rehearing request is addressed. Until the mandate issues, the FCC's line sharing rules, as well as the general unbundling rules articulated in the UNE Remand Order, remain in effect.

3. Even after the mandate issues, Southwestern Bell will continue to comply with existing interconnection agreements, where Southwestern Bell's unbundling obligations are set forth. Those contracts will continue in effect notwithstanding the D.C. Circuit's decision to vacate the Line Sharing Order. Southwestern Bell's interconnection agreements, however, contain change-of-law provisions, which set forth a detailed process of negotiations and, if necessary, a dispute resolution process to modify the agreement to reflect the intervening change in law. With regard to this particular proceeding, the Optional Line Sharing Amendment Appendix to Attachment 25: xDSL of the Missouri 271 Agreement ("M2A") specifically anticipates what is to happen in the event that the Line Sharing Order is struck down on appeal. Section 11.2 of the Optional Line Sharing Amendment provides that, if the FCC's line sharing rules are vacated:

> The parties shall negotiate in good faith to arrive at an agreement on conforming modifications to this Appendix. If negotiations fail, disputes between the parties concerning the interpretation of the actions required or the provisions affected shall be handled under the dispute resolution procedures set forth in the underlying interconnection agreement.

Section 9 of the M2A's General Terms and Conditions provides for dispute resolution procedures, including the presentation of disputed issues to the Commission.

4. In the longer term, though, the USTA decision is likely to have a significant impact on these proceedings. Because the D.C. Circuit has expressly vacated the Line Sharing Order, the FCC's line sharing rules will be eliminated once the mandate issues later this summer.[3] Given the USTA decision, it is unlikely that the FCC will be able to promulgate similar line sharing rules on remand. Under the principles that the court directed the FCC to consider when conducting its unbundling analysis – and given specifically the requirement that the FCC strike an appropriate balance between avoiding wasteful duplication of facilities, on one hand, and imposing costs such as "disincentives to research and development by both ILECs and CLECs and the tangled management inherent in shared use of a common resource," USTA, 290 F.3d at 429, on the other hand — it is difficult to conceive how the FCC legally could readopt a line sharing obligation.

5. The USTA court made clear that in considering which particular network elements to unbundle under section 251(c)(3) of the Telecommunications Act of 1996 ("1996 Act"), the FCC must balance any potential benefits associated with unbundling a specific network element against the costs that necessarily accompany the obligation to unbundle. The court flatly rejected the "[FCC's] expression of its belief that in this area more unbundling is better" because "Congress did not authorize so open-ended a judgment." USTA, 290 F.3d at 425. As the Supreme Court had recognized in AT&T Corp. v. Iowa Utilities Bd., 525 U.S. 366 (1999), "unbundling is not an unqualified good." USTA, 290 F.3d at 429. Rather, "[e]ach unbundling of an element imposes costs of its own, spreading the disincentive to invest in innovation and creating complex issues of managing shared facilities." USTA, 290 F.3d at 427.

[3] Under the SBC-Ameritech Merger Conditions, SWBT will continue to provide other CLECs access to the same network functions as are provided to its structurally separate affiliate SBC Advanced Solutions, Inc. ("ASI"). SBC will, of course, continue to honor its obligations under the SBC-Ameritech Merger Conditions, which expire in October 2003.

6. Under a proper unbundling analysis, the FCC cannot require an incumbent LEC to unbundle advanced services or advanced-services equipment, including the high frequency portion of the loop. As the D.C. Circuit explained, the FCC's line sharing rules were rooted in "[t]he Commission's naked disregard of the competitive context" for broadband, id. at 429, "detached from any specific markets or market categories." Id. at 426. Yet there is significant competition from other facilities-based providers in the market for broadband services (so-called "intermodal" competition), and the incumbent LEC's digital subscriber line ("DSL") technology is a decidedly minority player in that market. "The Commission's own findings (in a series of reports under § 706 of the 1996 Act) repeatedly confirm both the robust competition, and the dominance of cable, in the broadband market." Id. at 428. Under these circumstances, where the cable companies have roughly twice as many broadband customers as DSL and provide a clear alternative to the incumbent, it is impossible to conclude that the absence of an unbundling requirement for DSL facilities "will genuinely impair competition" in the market for broadband services. Id. at 425. Indeed, the court anticipated as much, declining to address the incumbent's challenge to the FCC's pricing rule for line sharing because "we think the possible mootness . . . warrant[s] deferring the issue to another day." Id. at 430

7. Although not legally obligated to do so, Southwestern Bell has committed to continue to provide line sharing pursuant to the terms and conditions in its interim and final line sharing agreements and appendices that were in effect as of May 24, 2002 (the date of the USTA decision), and through February 15, 2003, by which time the FCC should have issued its new unbundling rules as a part of its ongoing Triennial Review. Southwestern Bell's commitment is set forth in a letter from William M Daley, President of SBC Communications, Inc. to Michael Powell, Chairman of the FCC, dated June 18, 2002, a copy of which is attached hereto as Exhibit

2. This commitment ensures that CLECs will be able to continue to operate pursuant to the provisions of the Optional Line Sharing Amendment to the M2A even though the legal basis for line sharing has been eliminated by the D.C. Circuit's USTA decision. Southwestern Bell's voluntary commitment should alleviate any CLEC concerns that they may experience interruptions in the availability of line sharing under the terms and conditions of the Optional Amendment to the M2A. Southwestern Bell's wholesale operations are an important part of its business, and this commitment provides for certainty during this time of transition. Southwestern Bell's commitment to continue to provide the HFPL under the Optional Amendment does not, however, extend to the imposition of new terms and conditions beyond those in effect as of the date of the USTA decision. See: Exhibit 2, p.2. Accordingly, the Commission may not impose new terms and conditions beyond those specifically set forth in the Optional Amendment as it existed on May 24, 2002.

8. Accordingly, Southwestern Bell believes that the Commission cannot adopt any of the proposals in this proceeding to expand its scope or to change the terms and conditions that were in effect as of May 24, 2002. Since the Commission initiated this docket, various parties have attempted to expand the scope of these proceedings (1) to make the Commission's determinations available to any CLEC, regardless of whether it has signed the M2A or otherwise complied with the negotiation/arbitration requirements of sections 251 and 252 of the 1996 Act and (2) to include a review of Southwestern Bell's Project Pronto architecture and establish terms and conditions under which that architecture must be made available to CLECs, regardless (again) of whether such CLECs have complied with the negotiation/arbitration provisions of the Act. So far, the Commission has wisely refused to expand the scope of this proceeding, and it has specifically determined that issues relating to Project Pronto are to be considered in a

separate proceeding. The Commission specifically noted that "[t]he issues surrounding the proposed deployment of Project Proto architecture are broad and complex, and are beyond the scope originally envisioned for this case. Inclusion of these complex issues would substantially delay the conclusion of this case."[4] The D.C. Circuit's USTA decision confirms the wisdom of this determination, and the Commission should reject any proposals to examine the Project Pronto architecture as part of this proceeding. Southwestern Bell notes that its Broadband Service offering, under which Southwestern Bell has voluntarily permitted CLECs to utilize the Project Pronto network for the provision of competing services, remains available to CLECs pursuant to the terms of the SBC-Ameritech merger conditions.

9. The USTA decision makes clear that the FCC cannot legally require any unbundling of the advanced-services equipment the is part of the Project Pronto architecture. See supra ¶ 6. And the FCC had already indicated that it has begun to move in the same direction. For example, in its Triennial Review NPRM,[5] the FCC explained that "[t]he task set out by the statute – to implement a competition policy that provides incentives for the 'deployment' of advanced telecommunications capability without regard to transmission technology – requires a special focus on questions of intermodal and intramodal competition as they relate to broadband technology." Triennial Review NPRM ¶ 27. Unbundling, however, destroys those very incentives. See USTA, 290 F.3d at 424. ("If parties who have not shared the risks are able to come in as equal partners on the successes, and avoid payment for the losers, the incentive to invest plainly declines.") As individual FCC Commissioners have separately explained, "new entrants have little incentive to build their own facilities, since they can use the

[4] Order Regarding Request for Supplemental Testimony and Request for Additional Cost Studies, Case No. TO-2001-440, at 4 (Oct. 9, 2001).

[5] Notice of Proposed Rulemaking, Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers, 16 FCC Rcd 22781 (2001) ("Triennial Review NPRM").

incumbents' cheaper and more quickly. And incumbents have some disincentive to build new facilities, since they must share them with all their competitors." Kevin J. Martin, Commissioner, FCC, Framework for Broadband Deployment, Remarks at the National Summit on Broadband Deployment, Washington, D.C. (Oct. 26, 2001).[6] When these costs are considered against the backdrop of the competitive market for broadband services, the balancing analysis required by the 1996 Act, the Supreme Court's Iowa Utilities Bd. decision, and the D.C. Circuit's USTA decision are all clearly pointing in the same direction – i.e., the rules that require the incumbent to offer line sharing cannot stand.

10. The 1996 Act expressly assigns to the FCC the task of "determining what network elements should be made available for purposes of" satisfying the requirement that an incumbent local exchange carrier provide to competitive local exchange carriers nondiscriminatory access to network elements on an unbundled basis. See 47 U.S.C. § 251(d)(2). The Commission is not, therefore, at liberty to disregard the balance that the FCC eventually strikes. Once the FCC has balanced the costs against the prospective benefits of unbundling, and conducted an "analysis of the competing values at stake in the implementation of the Act," USTA, 290 F.3d at 428, the states are not free to disregard the FCC's determination.

11. Under the Supremacy Clause of the United States Constitution, a state legal requirement is preempted if "'under the circumstances of th[e] particular case . . . [such a

[6] See also Kathleen Q. Abernathy, Commissioner, FCC, Remarks at the USTA Annual Convention (Oct. 7, 2001) ("Unless properly circumscribed, forced unbundling can impose costs and distort investment incentives. Unbundling requirements that are too broad destroy an incumbent's incentive to invest in facilities. This is because incumbents will avoid risking capital on new infrastructure if rivals can piggy-back on their facilities risk-free. By the same token, new entrants will have diminished incentives to invest in their own facilities if the incumbent's network is readily available at below cost rates.").

requirement] stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress'" – whether that 'obstacle' goes by the name of 'conflicting; contrary to; . . . repugnance; difference; irreconcilability; inconsistency; violation; curtailment; . . . interference,' or the like." Geier v. American Honda Motor Co., 529 U.S. 861, 873 (2000) (quoting Hines v. Davidowitz, 312 U.S. 52, 67 (1941)); English v. General Elec. Co., 496 U.S. 72, 78-79 (1990); Fidelity Federal Sav. & Loan Ass'n v. De la Cuesta, 458 U.S. 141, 152-53 (1982).

12. The Commission has no authority to promulgate or enforce a regulation that is inconsistent with the 1996 Act or with FCC regulations implementing the Act. A state's authority to impose any requirement in areas covered by the local competition provisions of the federal Communications Act is expressly limited to instances in which there is no conflict between the state and federal requirements. Such a conflict would arise not only when a state regulation expressly requires a telecommunications carrier to do something that is forbidden under federal law, but also when a state regulation prevents or frustrates the accomplishment of a federal objective. Geier, 529 U.S. at 873.

13. The Commission may not, therefore, strike a different balance than that which the FCC ultimately strikes as it considers the issues on remand from the USTA court. It makes no sense, therefore, for the Commission to expand these proceedings by considering additional line sharing obligations, for such obligations will either be preempted if inconsistent with the rules that the FCC ultimately promulgates, or be redundant if duplicative of those same FCC rules. For all of these reasons, therefore, Southwestern Bell respectfully requests that the Commission abate these proceedings pending the FCC's determination on remand of the incumbents' line

sharing obligations. But, under no circumstances, should the Commission expand these proceedings or initiate any new proceedings to consider additional unbundling obligations.

WHEREFORE, for all the foregoing reasons, Southwestern Bell respectfully requests the Commission not to impose any obligations on it regarding line sharing which are inconsistent with the D.C. Circuit Court of Appeals USTA decision or which seek to expand on Southwestern Bell's voluntary commitment to continue the availability of the existing Optional Amendment during the transition period as the FCC reacts to the USTA decision.

Respectfully submitted,

SOUTHWESTERN BELL TELEPHONE, L.P.

BY Paul G. Lane /TM


PAUL G. LANE #27011
LEO J. BUB #34326
ANTHONY K. CONROY #35199
MIMI B. MACDONALD #37606
Attorneys for Southwestern Bell Telephone L.P.
One SBC Center, Room 3520
St. Louis, Missouri 63101
314-235-4300 (Telephone)
314-247-0014 (Facsimile)
paul.lane@sbc.com

## CERTIFICATE OF SERVICE

I hereby certify that copies of the foregoing document were served to all parties on the Service List by first-class, postage prepaid, U.S. Mail, e-mail or via hand-delivery on June 20, 2002.

Paul G. Lane /TM

Paul G. Lane

DAN JOYCE
MISSOURI PUBLIC SERVICE COMMISSION
PO BOX 360
JEFFERSON CITY, MO 65102

MICHAEL F. DANDINO
OFFICE OF THE PUBLIC COUNSEL
PO BOX 7800
JEFFERSON CITY, MO 65102

LISA CREIGHTON HENDRICKS
SPRINT COMMUNICATIONS COMPANY L.P.
6450 SPRINT PARKWAY, BLDG. 14
MAIL STOP KSOPHN0212-2A253
OVERLAND PARK, KS 66251

REBECCA B. DECOOK
AT&T COMMUNICATIONS OF THE SOUTHWEST, INC.,
1875 LAWRENCE ST., STE. 1575
DENVER, CO 80202

MARK W. COMLEY
CATHLEEN A. MARTIN
NEWMAN COMLEY & RUTH
P.O. BOX 537
JEFFERSON CITY, MO 65102

MICHELLE BOURIANOFF
AT&T COMMUNICATIONS OF THE SOUTHWEST, INC
919 CONGRESS, SUITE 1500
AUSTIN, TX 78701

MARY ANN (GARR) YOUNG
WILLIAM D. STEINMEIER, P.C.
P.O. BOX 104595
JEFFERSON CITY, MO 65110

DAVID J. STUEVEN
IP COMMUNICATIONS CORPORATION
1512 POPLAR AVENUE
KANSAS CITY, MO 64127

STEPHEN F. MORRIS
MCI TELECOMMUNICATIONS CORP.
701 BRAZOS, SUITE 600
AUSTIN, TX 78701

CARL J. LUMLEY
LELAND B. CURTIS
CURTIS OETTING HEINZ GARRETT & SOULE, P.C.
130 S. BEMISTON, SUITE 200
ST. LOUIS, MO 63105

CAROL KEITH
NUVOX COMMUNICATIONS
16090 SWINGLEY RIDGE ROAD, SUITE 500
CHESTERFIELD, MO 63006

PAUL GARDNER
GOLLER, GARDNER & FEATHER
131 EAST HIGH STREET
JEFFERSON CITY, MO 65101

J. STEVE WEBER
ATTORNEY FOR AT&T COMMUNICATIONS OF THE SOUTHWEST, INC.

101 W. MCCARTY, SUITE 216
JEFFERSON CITY, MO 65101

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

Argued March 7, 2002 Decided May 24, 2002

No. 00-1012

United States Telecom Association, et al.,
Petitioners

v.

Federal Communications Commission and
United States of America,
Respondents

Bell Atlantic Telephone Companies, et al.,
Intervenors

Consolidated with
01-1075, 01-1102, 01-1103

---------

No. 00-1015

United States Telecom Association, et al.,
Petitioners

v.

Federal Communications Commission and
United States of America,
Respondents

AT&T Corporation, et al.,
Intervenors

Consolidated with
00-1025

On Petitions for Review of Orders of the
Federal Communications Commission

Michael K. Kellogg argued the cause for petitioners and supporting intervenors in 00-1012 & 00-1015. With him on the briefs in 00-1012 were Mark L. Evans, Sean A. Lev, James D. Ellis, Paul K. Mancini, Roger K. Toppins, Gary L. Phillips, Lawrence E. Sarjeant, Linda L. Kent, Keith Townsend, John W. Hunter, Julie E. Rones, William P. Barr, Michael E. Glover, Edward H. Shakin, John P. Frantz, Richard M. Sbaratta, and James G. Harralson. With him on the briefs in 00-1015 were Mark L. Evans, Sean A. Lev, David L. Schwarz, Lawrence E. Sarjeant, Linda L. Kent, Keith Townsend, John W. Hunter, Julie E. Rones, Sharon J. Devine, Robert B. McKenna, William T. Lake, John H. Harwood II, Jonathan J. Frankel, James D. Ellis, Paul K.

Mancini, Roger K. Toppins, Gary L. Phillips, Michael E. Glover, Edward H. Shakin, William P. Barr, John P. Frantz, Jonathan B. Banks, Richard M. Sbaratta, and James G. Harralson. Donna M. Epps entered an appearance in 00-1012. Daniel L. Poole and William R. Richardson, Jr. entered appearances in 00-1015.

Laurence N. Bourne, Counsel, Federal Communications Commission, argued the cause for respondents in 00-1012. With him on the brief in 00-1012 were Charles A. James, Assistant Attorney General, Daniel M. Armstrong, Associate General Counsel, John E. Ingle, Deputy Associate General Counsel, James M. Carr, Counsel, Catherine G. O'Sullivan and Nancy C. Garrison, Attorneys, U.S. Department of Justice. Lisa S. Gelb, Counsel, Federal Communications Commission entered an appearance in 00-1012.

Richard K. Welch, Counsel, Federal Communications Commission, argued the cause for respondents in 00-1015. With him on the briefs in 00-1015 were Charles A. James, Assistant Attorney General, Daniel M. Armstrong, Associate General Counsel, John E. Ingle, Deputy Associate General Counsel, Laurence N. Bourne and James M. Carr, Counsel, Catherine G. O'Sullivan and Nancy C. Garrison, Attorneys, U.S. Department of Justice. Lisa S. Gelb, Counsel, Federal Communications Commission, entered an appearance in 00-1015.

Jonathan Jacob Nadler argued the cause for intervenors AT&T Corp., et al. in 00-1012. With him on the brief in 00-1012 were David W. Carpenter, Peter D. Keisler, James P. Young, Mark C. Rosenblum, Lawrence J. Lafaro, Richard H. Rubin, Donald B. Verrilli, Jr., Maureen F. Del Duca, Michael B. DeSanctis, Thomas F. O'Neil III, William Single, IV, Theresa K. Gaugler, Charles C. Hunter, Catherine M. Hannan, Albert H. Kramer, Robert McDowell, Jay C. Keithley and H. Richard Juhnke. John J. Heitmann, Jonathan E. Canis and Roy E. Hoffinger entered appearances in 00-1012.

David W. Carpenter argued the cause for intervenors AT&T, Corp., et al. in 00-1015. With him on the brief in 00-1015 were Peter D. Keisler, James P. Young, C. Frederick Beckner III, Mark C. Rosenblum, Lawrence J. Lafaro, Richard H. Rubin, Donald B. Verrilli, Jr., Maureen F. Del Duca, Michael B. DeSanctis, Thomas F. O'Neil III, William Single, IV, Rodney Joyce, Christy C. Kunin, Russell I. Zuckerman, Francis D.R. Coleman, Richard E. Heatter, Marilyn H. Ash, Douglas G. Bonner, Albert H. Kramer, Charles C. Hunter and Catherine M. Hannan. Roy E. Hoffinger, Lawrence G. Acker, John J. Heitmann and Jonathan E. Canis entered appearances.

Before: Edwards and Randolph, Circuit Judges, and Williams, Senior Circuit Judge.

Opinion for the Court filed by Senior Circuit Judge Williams.

Williams, Senior Circuit Judge: Petitioners in these two cases--certain incumbent local exchange carriers ("ILECs") and the U.S. Telecom Association, representing approximately 1200 such carriers--seek review of two rulemaking orders of the Federal Communications Commission. One order requires ILECs to lease a variety of "unbundled network elements" ("UNEs") to competitive local exchange carriers ("CLECs"), and the other unbundles a portion of the spectrum of local copper loops so that CLECs can offer competitive Digital Subscriber Line ("DSL") internet access. We grant both petitions, and remand both rules to the Commission.

I. Background

Congress passed the Telecommunications Act of 1996, Pub. L. 104-104, 110 Stat. 56, codified at 47 U.S.C. s 151 et seq. (the "1996 Act" or the "Act"), to "promote competition and reduce regulation in order to secure lower prices and higher quality services for American telecommunications consumers and encourage the rapid deployment of new telecommunications technologies." 1996 Act, preamble. In pursuit of that goal, s 251 of the Act requires that ILECs "unbundle" their

network elements--that is, provide them on an individual basis to competitive providers on terms prescribed by the Commission. 47 U.S.C. s 251(c)(3). To guide the Commission in deciding which network elements are to be unbundled, the Act goes on to specify:

> (2) Access standards
>
> In determining what network elements should be made available for purposes of subsection (c)(3) of this section, the Commission shall consider, at a minimum, whether--
>
> (A) access to such network elements as are proprietary in nature is necessary; and
>
> (B) the failure to provide access to such network elements would impair the ability of the telecommunications carrier seeking access to provide the services that it seeks to offer.

47 U.S.C. s 251(d)(2) (emphasis added).

In its first effort at implementation, Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, CC Docket No. 96-98, 11 FCC Rcd 15499 (1996) ("First Local Competition Order"), the Commission gave this section the following reading:

> The term "impair" means "to make or cause to become worse; diminish in value." We believe, generally, that an entrant's ability to offer a telecommunications service is "diminished in value" if the quality of the service the entrant can offer, absent access to the requested element, declines and/or the cost of providing the service rises. We believe we must consider this standard by evaluating whether a carrier could offer a service using other unbundled elements within an incumbent LEC's network.

Id. at 15643, p 285 (emphasis added). In AT&T Corp. v. Iowa Utilities Board, 525 U.S. 366 (1999), the Supreme Court found the Commission's view far too broad, saying that under such a standard it was "hard to imagine when the incumbent's failure to give access to the element would not constitute an 'impairment.' " Id. at 389. It specifically criticized the Commission's having "blind[ed] itself to the availability of elements outside the incumbent's network," including self-provisioning and leasing from other providers. Id. It criticized the Commission's view that "any increase" in the competitor's cost (resulting from lack of access to an incumbent's element) would be an "impairment." Id. at 389-90 (emphasis in original). Summarizing the overall picture, it said that if "Congress had wanted to give blanket access to incumbents' networks," it "would simply have said (as the Commission in effect has) that whatever requested element can be provided must be provided." Id. at 390.

In Iowa Utilities Board, the Supreme Court also addressed the Act's provisions on rates for UNEs, reversing the Eighth Circuit's holding that the Commission had no authority to set such rates. Id. at 377-86. It accordingly returned the remaining rate issues to the Eighth Circuit, which on remand invalidated the Commission's rate-setting principle, known by the acronym TELRIC (for "total element long-run incremental cost"). See Iowa Utilities Board v. FCC, 219 F.3d 744 (8th Cir. 2000). The Supreme Court reversed, upholding the TELRIC principle. Verizon Communications, Inc. v. FCC, No. 00-511, 2002 WL 970643 (May 13, 2002).

Following the Supreme Court's remand on the "impairment" standard, the Commission again tackled that issue in the rulemakings now on review. In what we will call the "Local Competition Order," Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, Third Report and Order and Fourth Further Notice of Proposed Rulemaking, 15 FCC Rcd 3696 (1999), it revised its definition of "impair" so as to require unbundling if, "taking into consideration the availability of alternative elements outside the incumbent's network, including self-provisioning by a requesting carrier or acquiring an alternative from a third-party supplier, lack of access to that element materially diminishes a requesting carrier's ability to provide the ser-

vices it seeks to offer." Local Competition Order, 15 FCC Rcd at 3725, p 51 (emphasis added); 47 C.F.R. s 51.317(b)(1). In weighing the availability of alternative network elements, the Commission noted that it would examine five factors--cost, effect on timeliness of entry, quality, ubiquity, and impact on network operations. Local Competition Order, 15 FCC Rcd at 3731, p 65, 3734-45, p p 71-100; 47 C.F.R. s 51.317(b)(2). Finally, it said that beyond looking simply to "impairment," it would consider five factors that it believed would further the Act's goals, namely whether unbundling would lead to "rapid introduction of competition in all markets," promote "facilities-based competition, investment, and innovation," reduce regulatory obligations, promote certainty in the market, and be administratively practical. 15 FCC Rcd at 3745-50, p p 101-16; 47 C.F.R. s 51.317(b)(3).

Of particular importance to this case, the Commission decided to make its unbundling requirements (except for two elements) applicable uniformly to all elements in every geographic or customer market. We return in detail to this issue after a survey of the elements unbundled by the Local Competition Order:

- Local loops, defined as "all features, functions and capabilities of the transmission facilities, including dark fiber and attached electronics (except those used for the provision of advanced services, such as DSLAMs [DSL Access Multiplexers]) owned by the incumbent LEC, between an incumbent LEC's central office and the loop demarcation point at the customer premises." 15 FCC Rcd at 3772, p 167; 47 C.F.R. s 51.319(a)(1). The Commission also required that incumbent LECs "condition" loops so as to allow CLECs to offer advanced services. 15 FCC Rcd at 3775, p 172; 47 C.F.R. s 51.319(a)(3). Conditioning, for these purposes, means removing devices such as bridge taps, low-pass filters, range extenders, etc., that improve voice transmission but may decrease a loop's advanced services capabilities. Id.

Subloops, i.e., those "portions of the loop that can be accessed at terminals in the incumbent's outside plant." 15 FCC Rcd at 3789, p 206; 47 C.F.R. s 51.319(a)(2). Points of access might include the pole near the customer's premises, the network interface device ("NID"), and the feeder distribution interface (where the trunk line from the central office interfaces with the distribution line to the subscribers). 15 FCC Rcd at 3789-90, p 206.

Network Interface Devices, which include all "features, functions, and capabilities of the facilities used to connect the loop distribution plant to the customer premises wiring, regardless of the particular design of the NID mechanism." Id. at 3801, p 233; 47 C.F.R. s 51.319(b). This broad definition is intended to make the unbundling requirement "flexible and technology-neutral," so as to apply to any new NID technologies that may develop. 15 FCC Rcd at 3801, p 234.

Circuit switching, defined as the "basic function of connecting lines and trunks," including "all the features, functions and capabilities of the switch." Id. at 3805, p 244; 47 C.F.R. s 51.319(c). The Commission made one narrow exception to circuit switch unbundling, which we discuss below.

Packet switching under some circumstances. Packet switches perform "the function of routing individual data units based on address or other routing information contained in the units." 15 FCC Rcd at 3833, p 302; 47 C.F.R. s 51.319(c)(4). The Commission for the most part denied unbundling for packet switching, requiring it only where the ILEC has used digital loop carrier systems, placing a DSLAM at a remote terminal and refusing to allow the competitor to collocate its own DSLAM at that remote terminal. 15 FCC Rcd at 3838, p 313. That is, if the loop is such that a remote DSLAM is necessary to provide DSL service at all, and the ILEC has denied the CLEC the right to collocate a DSLAM remotely, then unbundling the packet switching (i.e., the ILEC's own DSLAM) would be the only way to allow the CLEC to provide DSL service.

Dedicated transport, defined as "facilities dedicated to a particular customer or carrier that provide telecommunications between wire centers owned by incumbent LECs or requesting telecommunications carriers, or between switches owned by incumbent LECs or requesting telecommunications carriers." Id. at 3842, p 322; 47 C.F.R. s 51.319(d)(1)(i). The Commission expanded this traditional definition so as to include all high-capacity transmission facilities of specified types and "such higher capacities as evolve over time," 15 FCC Rcd at 3843, p 323, as well as dark fiber, id. at 3843-46, p p 325-30; 47 C.F.R. s 51.319(d)(1)(ii).

- Shared transport, defined as "transmission facilities shared by more than one carrier, including the incumbent LEC, between end office switches, between end office switches and tandem switches, and between tandem switches in the incumbent LEC's network." 15 FCC Rcd at 3862, p 370; 47 C.F.R. s 51.319(d)(1)(iii).

- Signaling networks and call-related databases. Signaling networks include signaling transfer points, to which each local switch must be connected. 15 FCC Rcd at 3868, p 384; 47 C.F.R. s 51.319(e). Call-related databases are "used in signaling networks for billing and collection or the transmission, routing, or other provision of telecommunications service." 15 FCC Rcd at 3875, p 403. The databases specifically unbundled include the calling name database, the 911 database, the toll free calling database, and several others. Id.

- Operations support systems. These are the "functions supported by an incumbent LEC's databases and information," including "pre-ordering, ordering, provisioning, repair and maintenance, and billing." 15 FCC Rcd at 3884, p 425; 47 C.F.R. s 51.319(g).

So far as we understand, this list is narrower than that which the Court reversed in Iowa Utilities Board only in its exclusion of some circuit switches, as well as of operator services and directory assistance. See 15 FCC Rcd at 3822-31, p p 276-98, 3890-92, p p 438-42. In other areas, the Commission's list has actually been expanded, now including high-capacity loops, id. at 3777, p 176, 3780, p 184, dark fiber, id. at 3785, p 196, 3843-46, p p 325-30, subloops, id. at 3788-89, p p 202-05, and packet switches in a few circumstances, id. at 3832-35, p p 300-06.

In what we call the "Line Sharing Order," In the Matters of Deployment of Wireline Services Offering Advanced Telecommunications Capability and Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, Third Report and Order in CC Docket No. 98-147 and Fourth Report and Order in CC Docket No. 96-98, 14 FCC Rcd 20912 (1999), the Commission refined unbundling further. Copper loops have a range of spectrum in which the transmission of information is possible. Analog telephone service uses only the lower frequencies of that spectrum (typically 300 to 3400 hz), leaving higher frequencies unused. Recent technological development allows the provision of DSL high-speed internet access over the high-frequency (i.e., 20,000+ hz) spectrum.1 By fitting the loop with splitters (which split apart voice and digital signals) and DSLAMs (Digital Subscriber Line Access Multiplexers) (which send voice traffic to the circuit-switched telephone network and data traffic to the packet-switched data network), local carriers can provide both

1 There are numerous types of DSL technology: ADSL (asymmetric DSL, in which upstream transmissions are much slower than downstream), HDSL (high-speed DSL), UDSL (universal DSL), VDSL (very-high-speed DSL), and RADSL (rate-adaptive DSL). See Line Sharing Order, 14 FCC Rcd at 20915 n.5. The Commission here and elsewhere refers to these technologies collectively as "xDSL," the "x" serving as a generic identifier. In the interests of judicial economy, we shall simply use "DSL" as the generic term.

plain old telephone service and DSL internet access at the same time.

In the "Line Sharing Order" the Commission decided that the high frequency portion of copper loop spectrum should be unbundled as to those loops on which ILECs are currently providing telephone service. The Commission defined the "high frequency" portion as simply any frequency "above the voiceband on a copper loop facility used to carry analog circuit-switched voiceband transmissions." Line Sharing Order, 14 FCC Rcd at 20926, p 26; 47 C.F.R. s 51.319(h)(1).

Such unbundling means, of course, that CLECs and ILECs would share the same copper loop to provide two different services at once. See, e.g., 14 FCC Rcd at 20923, p 17. The Commission clarified that the unbundling obligation extends to only one competitor per line. Id. at 20948, p 47.

The Commission also required ILECs to condition loops, that is, to remove loading coils, bridge taps, and other voiceband transmission enhancing equipment that tends to interfere with DSL service. Id. at 20917; 20952-54, p p 81-87; 47 C.F.R. s 51.319(h)(5). An ILEC can escape this obligation by demonstrating that conditioning would significantly degrade analog voice service. The Commission explicitly recognized that such a showing would be practically impossible for loops under 18,000 feet. 14 FCC Rcd at 20954, p 86.

## II. The Local Competition Order

We note at the outset the extraordinary complexity of the Commission's task. Congress sought to foster competition in the telephone industry, and plainly believed that merely removing affirmative legal obstructions would not do the job. It thus charged the Commission with identifying those network elements whose lack would "impair" would-be competitors' ability to enter the market, yet gave no detail as to either the kind or degree of impairment that would qualify. We review the two orders with this in mind.

### A. Unvarying Scope

As to almost every element, the Commission chose to adopt a uniform national rule, mandating the element's unbundling

in every geographic market and customer class, without regard to the state of competitive impairment in any particular market. As a result, UNEs will be available to CLECs in many markets where there is no reasonable basis for thinking that competition is suffering from any impairment of a sort that might have the object of Congress's concern.

One reason for such market-specific variations in competitive impairment is the cross-subsidization often ordered by state regulatory commissions, typically in the name of universal service. This usually brings about undercharges for some subscribers (usually rural and/or residential) and overcharges for the others (usually urban and/or business). Petitioners' opening brief in the Local Competition Order case cites testimony of a former FCC Chairman for the proposition that 40% of telephone service is charged below cost, Petitioners' Br. at 35 & n.16, and the Commission and its supporting intervenors do not demur. See also, e.g., Robert W. Crandall & Thomas W. Hazlett, Telecommunications Policy Reform in the United States and Canada, at 18, Working Paper 00-9, AEI-Brookings Joint Center for Regulatory Studies (Dec. 2000) (chart showing that in many American cities, businesses are charged substantially more than residences for single lines); see also generally Robert W. Crandall & Leonard Waverman, Who Pays for Universal Service? When Subsidies Become Transparent (2000).

Competitors will presumably not be drawn to markets where customers are already charged below cost, unless either (1) the availability of UNEs priced well below the ILECs' historic cost makes such a strategy promising, or (2) provision of service may, by virtue of economies of scale and scope, enable a CLEC to sell complementary services (such as long distance or enhanced services) at prices high enough to cover incomplete recovery of costs in basic service. The Commission never explicitly addresses by what criteria want of unbundling can be said to impair competition in such markets, where, given the ILECs' regulatory hobbling, any competition will be wholly artificial. And, although it offers an explanation as to why it is desirable as a general matter that CLECs should have "ubiquitous" unimpaired access to

network elements, see Local Competition Order, 15 FCC Rcd at 3744, p p 97-98, it never explains why the record supports a finding of material impairment where the element in question--though not literally ubiquitous--is significantly deployed on a competitive basis in those markets where there is no reason to suppose that rates are artificially low, compare id. at 3847, p 335 (finding that 47 of the top 50 areas have 3 or more competitors providing interoffice transport), with id. at 3849, p 340 (finding absence of requisite ubiquity for such transport).

But it is in the other segments of the markets, where presumably ILECs must charge above cost (at least above average costs allocated in conventional regulatory fashion) in order to offset their losses in the subsidized markets, that the gap in the Commission's reasoning is greatest. In finding that the CLECs' lack of access to each of the many elements "materially diminish[ed]" their ability to provide service, the Commission nowhere appears to have considered the advantage CLECs enjoy in being free of any duty to provide underpriced service to rural and/or residential customers and thus of any need to make up the difference elsewhere. As a matter of pure language, perhaps, one might regard as an "impairment" any cost disadvantage that the CLECs suffer in markets where ILECs are hampered by regulatory redistribution, even if the disadvantage is fully offset by the exigencies faced by ILECs. But the Commission has never explained why such a view makes sense. Indeed, pointing to evidence of considerable investment by CLECs in facilities for service in what are evidently the relatively overcharged markets, see, e.g., Petitioners' Br. at 16 (noting that as of 1999, CLECs had deployed transport facilities in all of the top 50 markets), the petitioners argue that there has been little or no real net impairment. The Commission responds with an expression of doubt whether these "data accurately reflects [sic] the extent to which alternatives are actually available to competitors." Local Competition Order, 15 FCC Rcd at 3849, p 341. But because the Commission has loftily abstracted away all specific markets, and because its concept of impairing cost-

differentials is so broad (an issue discussed below), we have no way of assessing the real meaning of that conclusion.

We now turn to the reasons offered by the Commission for adopting an undifferentiated national rule for each element (with narrow exceptions). Having found legal authority to adopt such a rule, it said that it would help achieve the goals of the Act, to wit: (1) rapid introduction of competition, (2) promotion of facilities-based competition, investment and innovation, (3) certainty in the marketplace, (4) administrative practicality and (5) reduced regulation. See Local Competition Order, 15 FCC Rcd at 3754-62, p p 124-143; see also 47 C.F.R. s 51.317(b)(3) (identifying same five factors as guiding Commission decision whether to unbundle a network element).

We first address the third and fourth justifications, both of which seemingly turn on how clear any non-universal rule can be. The Commission appears simply to assume that any such rule would be unpredictable and hard to apply. Yet the Commission itself, in regard to circuit switches, chose a partial rule, denying unbundling for local circuit switches serving customers with four or more lines in the highest-density zone in any of the top 50 Metropolitan Statistical Areas ("MSAs"). See Local Competition Order, 15 FCC Rcd at 3823-31, p p 278-99. The Commission's order has no explanation of why comparable differentiation was not available for other elements.

As to reduced regulation, the Commission says that a national list "will result immediately in reduced regulation." Id. at 3762, p 143. It does not elaborate on this counterintuitive proposition. It goes on to say that a national list is consistent with "the deregulatory goals of the Act":

> Reduced regulation will occur as we remove elements from the list as requesting carriers are no longer impaired without access to those elements, and it otherwise does not further the goals of the Act to continue requiring incumbent LECs to unbundle them.

Id. We understand that elimination of an entire universal mandate at one whack will achieve more deregulation than removal of a partial mandate. But imposition of a national mandate does not itself entail national elimination, and in any event we cannot see how imposition and then retraction of a national mandate is more deregulatory, overall, than imposition and retraction of a partial one.

This leaves the more substantive justifications--the ideas that universal rules would promote the goals of the Act by leading to rapid introduction of competition, Local Competition Order, 15 FCC Rcd at 3754-57, p p 125-33, and to promotion of facilities-based competition, investment, and innovation, id. at 3757-60, p p 134-39. Using certain definitions, the first point--more rapid introduction of competition--indeed follows automatically. If competition performed with ubiquitously provided ILEC facilities counts, the more unbundling there is, the more competition. The Commission, here in unison with the ILEC petitioners, evidently assumes that the Commission-imposed prices are highly attractive to CLECs: on that assumption, universal rules encompassing as many elements as possible would indeed generate a rapid spread of "competition."

But the Commission never makes the argument in quite so stark a form, unwilling to embrace the idea that such completely synthetic competition would fulfill Congress's purposes. Thus it turns to the argument that universal rules promote investment and facilities-based competition.

The Commission says that "adoption of a national list" will "facilitate the deployment" of competitive facilities. Id. at 3757, p 134. There are plainly two sides to the effects on investment of ubiquitously available UNEs at Commission-mandated prices. On one side, the more widespread the availability of elements that can be more efficiently provided by the incumbent (presumably because of economies of scale and scope--an issue to which we'll return), the quicker competitors will set about providing the other elements and offering of complete competitive service, including long distance service. Compare Iowa Utilities Board, 525 U.S. at

416-17 (Breyer, J., concurring in part and dissenting in part), cited at Respondent's Br. 32-33. Further, access to UNEs may enable a CLEC to enter the market gradually, building a customer base up to the level where its own investment would be profitable.

On the other side, the petitioners argued before the Commission that mandatory unbundling at Commission-mandated prices reduces the incentives for innovation and investment in facilities. Their reasoning, of course, is that a regulated price below true cost will reduce or eliminate the incentive for an ILEC to invest in innovation (because it will have to share the rewards with CLECs), and also for a CLEC to innovate (because it can get the element cheaper as a UNE). Indeed, many prices that seem to equate to cost have this effect. Some innovations pan out, others do not. If parties who have not shared the risks are able to come in as equal partners on the successes, and avoid payment for the losers, the incentive to invest plainly declines.2 See Iowa Utilities Board, 525

2 The Commission's standard for deciding that a network element should be unbundled--whether lack of access to it "materially diminishes" the requesting carrier's "ability" to provide the services in question--implicitly builds in a relation to the prices at which CLECs get access to UNEs. (The Commission is rarely clear on precisely what costs are being compared, but in saying that lack of access to unbundled elements would cause a material increase in cost it often uses terms implying that the comparison is to the Commission-mandated price of unbundled elements, i.e. that

present TELRIC. See, e.g., 15 FCC Rcd at 3815, p 263; id. at 3864, p 375.) Lack of access would not diminish the requester's ability at all if it could secure the function more cheaply on its own. Thus, the closer the Commission's pricing principle is to the low end of what it may lawfully set, the greater the probability that lack of access would cause "material diminution." As a result low UNE prices would not only have the direct effect mentioned in the text, but would inherently tend to expand the sphere of these effects. As the "price squeeze" jurisprudence shows, even prices that are set within the band of what is lawfully permissible may have perverse effects, and the Commission may be obligated to consider them. Cf. FPC v. Conway Corp., 426 U.S. 271, 278-79 (1976); Sprint

OU.S. at 428-29 (Breyer, J., concurring in part and dissenting in part); cf. FPC v. Hope Natural Gas Co., 320 U.S. 591, 647-53 (1944) (Jackson, J., dissenting) (discussing supply implications of cost-based regulation of natural gas production). In any event, the Commission's own assumption that universal access to virtually all network elements would prove attractive (leading to rapid introduction of "competition") suggests that such a disincentive effect cannot be discounted a priori.

The Commission's only response is to point to evidence that both CLECs and ILECs have built facilities since passage of the 1996 Act (the same evidence invoked by the ILECs to show the existence of many markets where unbundling is unneeded), despite the Act's obviously having created a prospect of unbundling. Local Competition Order, 15 FCC Rcd at 3758-59, p p 135-38. But the existence of investment of a specified level tells us little or nothing about incentive effects. The question is how such investment compares with what would have occurred in the absence of the prospect of unbundling, compare Sugar Cane Growers Cooperative of Florida v. Veneman, No. 01-5335, 2002 Westlaw ----, slip op. at 7 (D.C. Cir. May 10, 2002); Competitive Enterprise Institute v. NHTSA, 956 F.2d 321, 325 (D.C. Cir. 1992), an issue on which the record appears silent. Although we can't expect the Commission to offer a precise assessment of disincentive effects (a lack of multiple regression analyses is not ipso facto arbitrary and capricious), we can expect at least some confrontation of the issue and some effort to make reasonable trade-offs.

In the end, then, the entire argument about expanding competition and investment boils down to the Commission's expression of its belief that in this area more unbundling is better. But Congress did not authorize so open-ended a judgment. It made "impairment" the touchstone. The Commission argues that s 251(d)(2), directing it to consider necessity and impairment "at a minimum," clearly allows it to consider other elements. We assume in favor of the Commission that that is so. But to the extent that the Commission orders access to UNEs in circumstances where there is little or no reason to think that its absence will genuinely impair

---

Communications Co. L.P. v. FCC, 274 F.3d 549, 555 (D.C. Cir. 2001).

competition that might otherwise occur, we believe it must point to something a bit more concrete than its belief in the beneficence of the widest unbundling possible.

Besides the analysis described above, the Commission addressed the question whether Iowa Utilities Board precluded its adoption of universal rules for each network element. It concluded that nothing in that opinion would require it "to determine, on a localized state-by-state or market-by-market basis which unbundled elements are to be made available." Local Competition Order, 15 FCC Rcd at 3753, p 122. We certainly agree that the Court's brief passage reversing the Commission on the impairment issue contained little detail as to the "right" way for the Commission to go about its work. But the Court's point that if "Congress had wanted to give blanket access to incumbents' networks," it "would simply have said (as the Commission in effect has) that whatever requested element can be provided must be provided." Iowa Utilities Board, 525 U.S. at 390, suggests that the Court read the statute as requiring a more nuanced concept of impairment than is reflected in findings such as the Commission's--detached from any specific markets or market categories.

B. Kinds of Cost Disparities

Petitioners complain that the Commission myopically focused on "cost differences," thereby skewing its inquiry to produce the maximum unbundling.

Of course any cognizable competitive "impairment" would necessarily be traceable to some kind of disparity in cost. Indeed, the ILECs argued before the Commission and the Supreme Court that Congress intended that the impairment standard embody the criteria of the "essential facilities" doctrine, see Iowa Utilities Board, 525 U.S. at 388, which itself turns on concepts of cost. The doctrine's basic idea is that where one firm controls some facility (such as a bridge) that is essential for competition in a broader market, and it would make no economic sense for competitors to duplicate the facility, and certain other criteria are satisfied, see generally Phillip E. Areeda & Herbert Hovenkamp, 3A Antitrust Law p p 771-73 (1996), the owner may be compelled to share the facility with its competitors. The classic case where competitor duplication would make no economic sense is where average costs are declining throughout the range of the relevant market. See Areeda & Hovenkamp, supra, at p 771c; see also 2 Alfred E. Kahn, The Economics of Regulation: Principles and Institutions 119 (1989). In such a case, duplication, even by the most efficient competitors imaginable, would only lead to higher unit costs for all firms, and thus for customers. See Areeda & Hovenkamp, supra, at p 771c; 2 Kahn, supra, at 122; see also generally Iowa Utilities Board, 525 U.S. at 416-17, 427-31 (Breyer, J., concurring in part and dissenting in part).3 Thus the Supreme Court in Verizon observed that "entrants may need to share some facilities that are very expensive to duplicate (say, loop elements) in order to be able to compete in other, more sensibly duplicable elements (say, digital switches or signal-multiplexing technology)." Verizon, slip op. at 38 n.27 (emphasis added). See also id. at 39 n.27 (characterizing the elements with respect to which new entrants and incumbents are not required to compete (i.e., the elements to be unbundled) as those " 'the duplication of [which] would prove unnecessarily expensive' ") (quoting Justice Breyer, post, at 8, dissenting).

Petitioners' position here is fundamentally that the Commission relied on cost disparities that, far from being any indication that competitive supply would be wasteful, are simply disparities faced by virtually any new entrant in any sector of the economy, no matter how competitive the sector. See Petitioners' Br. at 28. Indeed, the Commission's order does reflect an open-ended notion of what kinds of cost disparity are relevant.

For example, in the discussion of local switching, the Commission notes that there are economies of scale in switches, Local Competition Order, 15 FCC Rcd at 3812-13, p 259, and that it is cheaper to buy a 20,000-line switch than four increments of 5000 lines each, id. at 3813, p 260. The Commission refers explicitly to a CLEC's probable inability to enjoy scale economies comparable to ILECs' "particularly in the early stages of entry." Id. at 3814, p 261 (emphasis added). But average unit costs are necessarily higher at the outset for any new entrant into virtually any business. The Commission has in no way focused on the presence of economies of scale "over the entire extent of the market." 2 Kahn, supra, at 119 (emphasis added). Without a link to this sort of cost disparity, there is no particular reason to think that the element is one for which multiple, competitive supply is unsuitable. See generally id. at 119-26.

The Commission of course has recognized that marketplace changes and increases in competition may justify later reductions in unbundling mandates. See, e.g., Local Competition Order, 15 FCC Rcd at 3704, p 15. But this acknowledgement doesn't respond to the analytical problem. To rely on cost disparities that are universal as between new entrants and incumbents in any industry is to invoke a concept too broad, even in support of an initial mandate, to be reasonably linked to the purpose of the Act's unbundling provisions.

Each unbundling of an element imposes costs of its own, spreading the disincentive to invest in innovation and creating complex issues of managing shared facilities. See Iowa Utilities Board, 525 U.S. at 428-29 (Breyer, J., concurring in part and dissenting in part). At the same time--the plus that the Commission focuses on single-mindedly--a broad mandate can facilitate competition by eliminating the need for separate construction of facilities where such construction would be wasteful. Id. at 416-17. Justice Breyer concluded that fulfillment of the Act's purposes therefore called for "balance" between these competing concerns. Id. at 429-30. A cost disparity approach that links "impairment" to universal characteristics, rather than ones linked (in some degree) to natural monopoly, can hardly be said to strike such a balance. The Local Competition Order reflects little Commission effort to pin "impairment" to cost differentials based on characteristics that would make genuinely competitive provision of an element's function wasteful.

Petitioners here do not explicitly attack the Commission for its refusal to incorporate the essential facilities doctrine, and we do not intend to suggest that the Act requires use of that doctrine's criteria.4 But what we do say is that cost compari-

---

3 Compare William J. Baumol, On the Proper Cost Tests for Natural Monopoly in a Multiproduct Industry, 67 Amer. Econ. Rev. 809 (1977) (proposing concept of "subadditivity" for ascertainment of natural monopoly), and William W. Sharkey, The Theory of Natural Monopoly (1982) (further development of subadditivity).

4 We note that scholars have raised very serious questions about the wisdom of the essential facilities doctrine as a justification

sons of the sort made by the Commission, largely devoid of any interest in whether the cost characteristics of an "element" render it at all unsuitable for competitive supply, seem unlikely either to achieve the balance called for explicitly by Justice Breyer or implicitly by the Court as a whole in its disparagement of the Commission's readiness to find "any" cost disparity reason enough to order unbundling. The Commission's addition of a materiality notion, see Local Competition Order, 15 FCC Rcd at 3725, p 51 (finding impairment in any case where lack of access to an element "materially" diminishes ability to provide services), submits to the Court's ruling in a nominally quantitative sense (though the reality of such acquiescence cannot be measured and may be belied by the virtual identity of the old and new orders). More important, adding the adjective "material" contributes nothing of any analytical or qualitative character that would fulfill the Court's demand for a standard "rationally related to the goals of the Act." Iowa Utilities Board, 525 U.S. at 388.

Because the Commission's concept of "impairing" cost disparities is so broad and unrooted in any analysis of the competing values at stake in implementation of the Act, we cannot uphold even the two non-universal mandates adopted by the Commission (for circuit switches and packet switches).

Petitioners also attack the rules on specific elements. Some of these attacks parallel the universality and cost-disparity issues already discussed. Petitioners' critique as to advanced services equipment coalesces with the issues they raise about the Line Sharing Order (see below). This leaves two issues, neither of which we need address here. First, petitioners attack the Commission's requirements of certain information disclosure and "loop conditioning." After remand, these issues may well be moot, and if they recur will do

for judicial mandates of competitor access, and accompanying judicial price setting. See, e.g., Areeda & Hovenkamp, supra, at p 771c. But a doctrine that is inadequate for that purpose may nonetheless offer useful concepts for agency guidance when Congress has directed an agency to provide competitor access in a specific industry.

Oso in a different context. Second, petitioners argue that the "enhanced extended link" condition to the exception to the switch unbundling mandate is in reality a mandate to combine otherwise uncombined network elements, and is therefore invalid. The Supreme Court appears to have definitely removed the basis of this claim, holding that the Commission has authority to require such combinations, affirmatively--that is, not merely as a condition to an unbundling exception. See Verizon, slip op. at 58-68. If any comparable claim somehow survives, it too can be raised in the remand proceedings.

III. The Line Sharing Order

Petitioners primarily attack the Line Sharing Order on the ground that the Commission, in ordering unbundling of the high frequency spectrum of copper loop so as to enable

CLECs to provide DSL services, completely failed to consider the relevance of competition in broadband services coming from cable (and to a lesser extent satellite). We agree.

The Commission's own findings (in a series of reports under s 706 of the 1996 Act) repeatedly confirm both the robust competition, and the dominance of cable, in the broadband market. The first s 706 report found that "[n]umerous companies in virtually all segments of the communications industry are starting to deploy, or plan to deploy in the near future, broadband to the consumer market," including "cable television companies, incumbent LECs, some utilities, and 'wireless cable' companies." In the Matter of Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996, 14 FCC Rcd 2398, 2404 p 12 (1999). The Commission also noted that the "most popular offering of broadband to residential consumers is via 'cable modems'...." id. at 2426, p 54, that "no competitor has a large embedded base of paying residential consumers," id. at 2423, p 48, and that the "record does not indicate that the consumer market is inherently a natural monopoly," id. The most recent s 706 Report

(not in the record of this case) is consistent: As of the end of June 2001, cable companies had 54% of extant high-speed lines, almost double the 28% share of asymmetric DSL. Third Report Pursuant to s 706, 2002 FCC LEXIS 655, at p p 44, 48 (Feb. 6, 2002). Even in the Local Competition Order on review in this case, the Commission said, "Competitive LECs and cable companies appear to be leading the incumbent LECs in their deployment of advanced services." 15 FCC Rcd at 3835, p 307.

Relying on the Commission's repeated findings, petitioners argue that it is "antithetical to the 1996 Act's language and deregulatory objectives" to mandate unbundling in a market that "already has intense facilities-based competition." DSL Petitioners' Br. at 3. They note the Supreme Court's observation that a proper "impairment" standard should be limited by the "goals of the Act." Id. at 23 (quoting Iowa Utilities Board, 525 U.S. at 388).

The Commission's response to this argument is to say that it was "merely adhering" to the letter of the statute: Thus it quotes the instruction of s 251(d)(2)(B) that it consider whether "failure to provide access to such network elements would impair the ability of the telecommunications carrier seeking access to provide the services that it seeks to offer." DSL Respondent's Br. at 20, quoting 47 U.S.C. s 251(d)(2)(B) (emphasis added by Respondent). On this theory the Commission believes it was justified in focusing solely on DSL because that is what "CLECs seek to offer when they request line sharing." Id. at 21. The Commission thus appears to acknowledge that it adopted the Line Sharing Order with indifference to petitioners' contentions about the state of competition in the market.

The Commission's inference from s 251(d)(2)(B)'s allusion to the services the requester "seeks to offer" strikes us as quite unreasonable. See Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837, 842-43 (1984). As Justice Breyer's separate opinion carefully explained, mandatory unbundling comes at a cost, including disincentives to research and development by both ILECs and

CLECs and the tangled management inherent in shared use of a common resource. Iowa Utilities Board, 525 U.S. at 428-29. And, as we said before, the Court's opinion in Iowa Utilities Board, though less explicit than Justice Breyer on the need for balance, plainly recognized that unbundling is not an unqualified good--thus its observation that the Commission must "apply some limiting standard, rationally related to the goals of the Act," id. at 388, and its point that the Commission "cannot, consistent with the statute, blind itself to the availability of elements outside the incumbent's network," id. at 389. In sum, nothing in the Act appears a license to the Commission to inflict on the economy the sort of costs noted by Justice Breyer under conditions where it had no reason to think doing so would bring on a significant enhancement of competition. The Commission's naked disregard of the competitive context risks exactly that result.

Accordingly, the Line Sharing Order must be vacated and remanded. Obviously any order unbundling the high frequency portion of the loop should also not be tainted by the sort of error identified in our discussion of the Local Competition Order and identified by petitioners here as well.

Petitioners also claim that the Commission without explanation reversed a prior decision that a portion of the spectrum of a loop cannot qualify as a "network element." The Commission urges that any language suggesting such a view is explicable as simply reflecting a judgment on technical feasibility, which it here reversed on the basis of a reexamination of the facts. Line Sharing Order, 14 FCC Rcd at 20942-43, p 63. We think the Commission's view is convincing.

Finally, petitioners attack the Commission's pricing rule, which limited an ILEC's charges for access to the high frequency portion of the loop to the value the ILEC "allocated to [asymmetric] DSL services when it established its interstate retail rates for those services," even where this rule would reduce the charges below the level derived from the Commission's general UNE pricing principles. Line Sharing Order, 14 FCC Rcd at 20975-76, p 139. As in the case of the element-specific claims raised in the Local Competition Order

case, we think the possible mootness, and certainty that any recurrence will be in a different context, warrant deferring the issue to another day.

* * *

We grant the petitions for review, and remand both the Line Sharing Order and the Local Competition Order to the Commission for further consideration in accordance with the principles outlined above.

So ordered.

SBC

William M. Daley
President

SBC Communications Inc.
175 E. Houston Street
Suite 1308
San Antonio, TX 78205

210.351.3700 Phone
210.351.3711 Fax

Exhibit 2

June 18, 2002

The Honorable Michael K. Powell
Chairman
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Dear Chairman Powell,

Questions have been raised about the potential short-term effects of the D.C. Court of Appeals' recent line sharing decision. SBC's wholesale operations are an important part of our business, SBC wants to improve its relationships with its wholesale customers and SBC understands the need for some certainty in light of the very fluid state of the law at this time. Accordingly, SBC welcomes the opportunity to clarify its position on line sharing and provide much needed certainty to its wholesale customers regarding this issue.

In view of the fact that the FCC has reiterated its plans to complete its *Triennial Review* proceeding by the end of the year, in which case the order should be published and effective by mid-February, SBC's local exchange companies (SBC) will continue to provide the high frequency portion of the loop (HFPL) UNEs, loop conditioning and splitters on a line at a time basis at least until February 15, 2003 pursuant to current agreements. After February 15th, there should be certainty from the FCC regarding applicable line sharing rules. Until February 15, 2003, SBC will comply with and will not unilaterally change the terms, conditions or rates in interim and final line sharing orders, agreements and appendixes (including "opt-in most favored" provisions) that were in effect as of May 24, 2002 (the date the D.C. Circuit issued the line sharing opinion). Hence, SBC will not unilaterally disconnect the HFPL UNEs, disconnect splitters, or cease providing loop conditioning or unilaterally change the prices of these network elements and services provided under current agreements with its wholesale customers as a result of the recent D.C. Circuit line sharing opinion. SBC is making this commitment in order to provide additional certainty to its wholesale customers and to regulators while the FCC considers the appropriate regulatory treatment of line sharing. During the transition period, SBC is also willing to work with CLECs to develop mutually acceptable line-sharing related market-based solutions and prices that could be implemented before or after February 15th.

The commitment described above should maintain the regulatory status quo and fully address and alleviate the concerns that have been raised by some CLECs. SBC makes this commitment in a good faith spirit of cooperation. In making this commitment, SBC (and CLECs), of course, are not waiving any of their legal rights or contractual change of law provisions and SBC reserves all of its rights under relevant FCC Orders and the D.C.

Circuit and Supreme Court orders. During the transition period through February 15, 2003, SBC and CLECs will be free to oppose, challenge, appeal and preserve their legal rights regarding line sharing and Project Pronto related interconnection agreements and contracts and related terms, conditions and rates that have been imposed or will be imposed during the transition period by state regulatory agencies that SBC or CLECs believe are inconsistent with or unlawful under the 1996 Telecommunications Act, FCC Orders or the DC Circuit opinion. If it is necessary for SBC to send change of law notices regarding line sharing related interconnection agreements or contracts that preserve its rights under the D.C. Circuit opinion, and to negotiate and arbitrate terms that comport with the D.C. Circuit order and applicable FCC rules, SBC will institute the dispute resolution process during the transition period, but will not implement the requisite conforming changes to those agreements or contracts until after February 15, 2003, as long as the CLEC agrees in writing that this voluntary commitment will not constitute a waiver or impairment of any of SBC's rights.

We believe the actions taken by SBC today will go a long way to alleviate the concerns that were raised by some competitors and to provide the Commission with the time it needs to address line sharing issues in a balanced and pro-competitive manner.

Sincerely,