**Before the**
**FEDERAL COMMUNICATIONS COMMISSION**
**Washington, DC 20554**

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| In the Matter of | ) | |
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| Applications of AT&T Inc. and | ) | |
| Deutsche Telekom AG | ) | WT Docket No. 11-65 |
| | ) | DA 11-799 |
| For Consent To Assign or Transfer Control | ) | |
| of Licenses and Authorizations | ) | |

# REPLY OF EARTHLINK, INC.


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June 20, 2011

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**Executive Summary**

Contrary to Applicants' claims, the record shows that the proposed merger would increase AT&T's ability and incentive to discriminate against its rivals by leveraging AT&T's power over wholesale inputs—including IP-IP interconnection, copper loops, and special access circuits—to disadvantage its rivals in the downstream converging markets for wired and wireless voice and broadband services. While AT&T discriminates against competitors today in the provision of wholesale inputs, the merged entity will have a greater incentive to discriminate. The addition of T-Mobile's 9.1 million Smartphone customers to AT&T's base of 31 million, together with the additional 55 million Americans to whom the merger will enable AT&T to deploy Long Term Evolution ("LTE") wireless broadband services, will result in a substantially larger footprint that will enable AT&T to reap more benefits from continued wholesale discrimination. This is a merger-specific effect that the Commission must address if, contrary to EarthLink's recommendation, it considers approving the merger prior to completing its wholesale competition reforms.

AT&T's past misconduct demonstrates that there are no competitive market forces sufficiently strong to prevent or limit the rate increases and anti-competitive wholesale conditions that it is highly likely to impose on its competitors should the Commission approve the proposed merger. To the contrary, even where competition exists on specific routes, to specific buildings, or for specific services, AT&T uses the combination of lock-up terms and a revenue make-whole policy to ensure that customers seeking lower prices or competitive alternatives are unable to achieve these goals without ensuring that AT&T realizes no loss in revenue. AT&T also unrealistically assumes that Commission regulation will be sufficient to constrain such discrimination. The failure of the Commission's special access pricing flexibility

regime, which resulted in AT&T imposing a 15% rate increase last year, has shown that pricing is not constrained by the theory of competition or projected competition. Moreover, the policy reforms required to address these issues must remain in effect permanently or until they are no longer needed and not rely on time bound merger conditions. As EarthLink and others have shown, those current conditions show that the proposed merger is not in the public interest and would harm competition and consumers. To restore and preserve competition and to protect consumers, the Commission must complete its wholesale competition reforms prior to considering the merger.

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**REPLY OF EARTHLINK, INC.**

Pursuant to the Public Notice issued by the Federal Communications Commission ("Commission" or "FCC") in the above-captioned proceeding on April 28, 2011,[1] EarthLink, Inc., on behalf of its operating subsidiaries,[2] ("EarthLink" or "Petitioner"), files this Reply to the Joint Opposition of AT&T Inc. ("AT&T"), Deutsche Telekom AG ("DT"), and T-Mobile USA, Inc. (T-Mobile," and together with AT&T and DT, "Applicants") to Petitions to Deny and Reply to Comments filed in the above-captioned proceeding on June 10, 2011 ("Opposition").

## I. COMPLETING WHOLESALE COMPETITION REFORM PRIOR TO MERGER APPROVAL AND/OR ADOPTING CONDITIONS THAT ADDRESS MERGER-SPECIFIC HARMS NOTWITHSTANDING PENDING RULEMAKINGS IS CONSISTENT WITH COMMISSION PRECEDENT

EarthLink proposed that the Commission complete its long-pending wholesale competition reforms *prior to* considering the proposed merger. Other parties also opposed the merger in part because sufficient pre-conditions, such as structural separation of AT&T's local

[1] FCC Public Notice, *AT&T Inc. and Deutsche Telekom AG Seek FCC Consent to the Transfer of Control of the Licensees and Authorizations Held by T-Mobile USA, Inc. and Its Subsidiaries to AT&T Inc.*, WT Docket No. 11-65, DA No. 11-799 (rel. Apr. 28, 2011) ("Public Notice"). This Petition is filed in reference to the following application File Numbers referenced in the Public Notice: 0004669383, 0004673673, 0004673727, 0004673730, 0004673732, 0004673735, 0004673737, 0004673739, 0004675960, 0004703157, 6013CWSL11, 6014CWSL11, 6015ALSL11, 6016CWSL11, 0004698766, ITC-T/C-20110421-00109, ITC-214-20020513-00251, ITC-T/C-20110421-00110, ITC-T/C-20110421-00111, ITC-214-20061004-00452 ITC-T/C-20110421-00112, and ITC-214-19960930-00473.

[2] EarthLink, Inc.'s operating subsidiaries include New Edge Networks, Inc., DeltaCom, Inc., Business Telecom, Inc., and the operating subsidiaries of One Communications Corp.

wireline networks, are not in place.[3] Applicants mistakenly characterize such positions by including EarthLink in a footnote that refers to what they call a "laundry list of other conditions" that the Commission should deny because they would "not address any merger-specific effect."[4] Contrary to Applicants' claims, EarthLink does not ask the Commission to use this merger to resolve industry-wide policy issues. Rather, EarthLink asks the Commission to resolve industry-wide policy issues *prior to considering the merger*.

AT&T states, without supporting analysis, that "the proposed [wholesale competition] conditions would not address any merger-specific effect and must therefore be rejected."[5] To the contrary, EarthLink showed that the merger would increase AT&T's incentive to discriminate against its competitors that offer wireline broadband services:

> As the importance of wireless broadband within AT&T's product set and customer base grows, its wireline incumbent LECs will have even greater incentives to increase their wireline competitors' costs (including special access) and decrease the availability of wholesale inputs to wireline broadband services (such as copper loops and DSL transmission). Indeed, the low latency of LTE makes it a viable option for offering voice-grade services. Thus there is a risk that AT&T will retire wireline loops in its incumbent territory and replace them with LTE loops, further diminishing the availability of wireline loops for inputs in competitive voice and broadband services.[6]

Similarly, other competitive providers of broadband services argued that:

> The increased broadband market share that the merged company will have will increase both AT&T's *incentive* and its *ability* to exclude competition from the broadband marketplace. Today, T-Mobile has the *ability* to offer its broadband

[3] *Applications of AT&T, Inc. and Deutsche TeleKom AG For Consent to Assign or Transfer Control of Licenses and Authorizations*, WT Docket No. 11-65, DA 11-99, Petition to Deny by the Computer & Communications Industry Association, at iii (May 31, 2011).

[4] Joint Opposition of AT&T, Inc., Deutsche Telekom, A.G, and T-Mobile USA, Inc. to Petitions to Deny and Reply to Comments, WT Docket No. 11-65, at 209-211 (June 9, 2011) ("Opposition").

[5] Opposition, at 211.

[6] *Applications of AT&T, Inc. and Deutsche TeleKom AG For Consent to Assign or Transfer Control of Licenses and Authorizations*, WT Docket No. 11-65, DA 11-99, EarthLink Petition to Deny, at 22 (May 31, 2011) ("EarthLink Petition").

> service on a wholesale basis to Joint Commenters and other CLECs in competition with AT&T. If, however, the merger is allowed and no conditions prevent it from doing so, T-Mobile will surely take the same approach as AT&T, enhancing AT&T's efforts to withhold broadband from wholesale customers. The merger also increases AT&T's *incentive* to withhold broadband from CLECs. This is because the broadband customer that the CLEC gains by wholesale purchase from AT&T may mean a lost broadband customer, not only for AT&T, but also for T-Mobile.[7]

While it is true that AT&T already has the ability and incentive to increase its rivals' costs and decrease the availability of wholesale inputs, the merger would increase those incentives because AT&T will need to gain market share with its Long Term Evolution ("LTE") product in order to recoup the costs of the merger and deploying LTE. As the Commission found with respect to a prior merger involving AT&T:

> the combined entity is likely to increase the level of discrimination that rivals must overcome to provide retail advanced services, interexchange services, and local exchange services. In the retail market for advanced services, incumbent LECs can engage in discriminatory conduct with respect to competitors' provision of services such as xDSL by refusing to cooperate with competitors' requests for the evolving type of interconnection and access arrangements necessary to provide new types of advanced services. The combined entity, controlling a larger area, will engage in more such discrimination against a competitor such as NorthPoint Communications that is seeking to enter on a national basis, as it will realize more of the benefits.[8]

Similarly, while AT&T already discriminates against EarthLink and others in the provision of wholesale inputs to wireline broadband services,[9] the merged entity will have a greater incentive to increase such discrimination because it will realize more of the benefits by incorporating T-Mobile's service areas and spectrum resources to make AT&T's footprint larger.

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[7] Comments of Access Point, Inc. and ACN Communications Services, Inc., WT Docket No. 11-65, at 5-6 (May 31, 2011) ("API/ACN").

[8] *Applications of Ameritech Corp., Transferor, and SBC Communications Inc., Transferee*, CC Docket No. 98-141, Memorandum Opinion and Order, 14 FCC Rcd 14712, ¶ 196 (1999) (footnotes omitted) ("*SBC/Ameritech Merger Order*").

[9] EarthLink Petition, at 22-24; API/ACN, at 4-5.

The merger will enable AT&T to increase its current 31 million Smartphone subscriber base[10] by adding T-Mobile's 9.1 million Smartphone subscribers[11] and increase by 55 million[12] the number of Americans to whom it will be able to offer LTE broadband services.[13] In short, the "merger's big footprint will create more incentives for the merged entity to discriminate against competitors."[14] This is a merger-specific effect that the Commission must address if, contrary to EarthLink's recommendation, it considers approving the merger prior to completing its wholesale competition reforms.

The lack of access to IP-IP interconnection is also a merger-specific effect that the Commission must address if it considers approving the merger. As the Commission has found, "evolving types of interconnection and access arrangements with incumbent LECs may be, or are likely to be, necessary for competitors to provide new, innovative services to consumers."[15] Indeed, the Commissions' Universal Service and Intercarrier Compensation NPRM seeks comment on means to encourage the move to IP-IP interconnection and numerous parties have provided record evidence in that docket that the Commission could take judicial notice of here to show that incumbents' refusal to offer IP-IP interconnection is slowing the deployment of

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[10] *See AT&T Inc. and Deutsche Telekom AG Seek FCC Consent to the Transfer of Control of the Licensees and Authorizations Held by T-Mobile USA, Inc. and Its Subsidiaries to AT&T Inc.*, WT Docket No. 11-65, Application Public Interest Statement, at 21 (filed Apr. 22, 2011) ("Public Interest Statement").

[11] T-Mobile USA Reports First Quarter 2011 Results, at 1, available at: http://s.tmocache.com/Cms/Files/Published/0000BDF20016F5DD010312E2BDE4AE9B/5657114502E70FF3012FD6A0635D5CAB/file/TMUS%20Q1%202011%20Press%20Release-Final.pdf.

[12] Public Interest Statement, at 56.

[13] Public Interest Statement, at 10.

[14] SBC/Ameritech Order, at ¶ 207.

[15] SBC/Ameritech Order, at ¶ 203.

advanced IP-based services.[16] By denying IP-IP interconnection to its competitors, AT&T would reap additional benefits post-merger by forcing its rivals to use legacy TDM interconnection that increases the costs of its rivals' competing voice and broadband services.

Finally, AT&T incorrectly implies that the Commission refuses to adopt merger conditions where it is considering reforms in an open, industry-wide proceeding.[17] For example, the Commission imposed special access price freezes on prior AT&T mergers notwithstanding its pending special access docket.[18] To the extent the Commission considers approving the merger, it should address the merger-specific harms notwithstanding the existence of open rulemaking proceedings.

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[16] *See, e.g., Developing a Unified Intercarrier Compensation Regime, Connect America Fund, A National Broadband Plan for our Future, High-Cost Universal Service Support et al.*, CC Dockets Nos. 01-92 et al., Comments of PAETEC Holding Corp., Mpower Communications Corp., U.S. TelePacific Corp., RCN Telecom Services, LLC, and TDS Metrocom LLC, at 3-4 (April 18, 2011) ("In order to achieve the FCC's objectives, stated in the Broadband Plan and the NPRM, of fostering the expansion of broadband services to all areas of the U.S. as rapidly as possible, requiring incumbent LECs to negotiate 251/252 interconnection arrangements for IP-to-IP interconnection should be one of the key outcomes of this NPRM."); *Developing a Unified Intercarrier Compensation Regime et al,* CC Dockets Nos. 01-92 et al., Comments of Comptel, at 5-9 (April 18, 2011) ("Relieving requesting carriers of the necessity of converting VoIP traffic to TDM before passing it on to legacy ILEC networks will allow consumers to begin to fully realize the benefits and economies of IP voice technology and its more efficient use of bandwidth."); *Developing a Unified Intercarrier Compensation Regime et al,* CC Dockets Nos. 01-92 et al., Comments of EarthLink, Inc. at 6-9 (April 18, 2011) ("the FCC should affirm that incumbents must offer facilities for both TDM and IP interconnection pursuant to section 252(d) cost-based rates. If it fails to do so, there is a risk that incumbents with market power will demand excessive prices for IP interconnection, thereby undermining the cost efficiencies that the industry and the FCC expect to realize by moving the public telecommunications network from TDM to IP.").

[17] Opposition, at 210.

[18] *See, e.g.*, AT&T/Bellsouth Order, at App. F, special access conditions 5 & 6 and ¶ 60; *SBC Communications, Inc. and AT&T Corp. Applications for Approval of Transfer of Control*, Memorandum Opinion and Order, WC Docket No. 05-65, ¶ 55 and App. F, Special Access Conditions 2 & 5 (rel. Nov. 17, 2005). *See also Verizon Communications Inc. and MCI, Inc. Applications for Approval of Transfer of Control*, Memorandum Opinion and Order, WC Docket No. 05-75, at ¶ 55 and App. G Special Access Conditions 2 & 5 (rel. Nov. 17, 2005).

## II. THE MERGED ENTITY WOULD HAVE THE ABILITY AND INCENTIVE TO DISCRIMINATE AGAINST COMPETITORS BY ABUSING AT&T'S CONTROL OF THE SPECIAL ACCESS AND LOOP MARKETS

### A. AT&T Retains the Ability to Sustain Anti-Competitive Prices for Wholesale Inputs (both TDM and Ethernet) to Disadvantage its Rivals in Retail Voice and Broadband Markets

The Applicants' premise that regulation and/or competition deprives AT&T of the ability to leverage its special access services to harm competition in downstream markets is false.[19] In its 22-state incumbent territory, AT&T maintains monopoly control over the copper loops and special access services that competitive broadband providers use as inputs to offer wireline broadband services, including Ethernet over copper ("EOC"). AT&T retains the ability and incentive to use its control over these bottleneck inputs to disadvantage competitive providers in retail markets, both wireline and wireless. As some have noted, "LTE technologies will provide pressure on Telcos and MSOs to deploy ever higher DSL, DOCSIS, and FTTH data rates in the markets served by these high bandwidth wireless data technologies" and "when it serves fixed subscribers, LTE competes with DSL, HFC DOCSIS, and FTTH."[20] EarthLink reiterates that AT&T, the market and regulators increasingly are relying on mobile broadband to deliver both voice and data services to consumers and businesses.[21] The combination of AT&T's 22-state monopoly in the wireline market, together with its proposed control of spectrum that would enable the merged entity to reach 97% of all Americans with wireline-quality wireless broadband technology, would give AT&T unparalleled dominance in retail markets by virtue of vertical

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[19] *See, e.g.*, Opposition, at 173.

[20] John Bartell, *Long Term Evolution (LTE) Overview*, FTTxtra (Sept. 8, 2009), *available at* http://www.fttxtra.com/wireless/long-term-evolution-lte-overview/.

[21] EarthLink Petition, at 20-22.

integration that gives it access to retail consumers and all necessary inputs (including loops and backhaul).

First, Applicants mistakenly limit analysis of the backhaul question to the wireless broadband market.[22] This ignores AT&T's ability and incentives to discriminate against its competitors in the wireless voice market. It also ignores AT&T's ability and incentives to discriminate against competitive broadband providers such as EarthLink that rely on special access as loop and backhaul inputs to their *wireline* broadband services. Because of the increasing convergence of communications, the Commission must evaluate AT&T's post-merger ability and incentive to discriminate against its rivals in downstream markets not only for wireless voice and broadband, but also wireline voice and broadband.[23] Indeed, as Ad Hoc argued:

> AT&T grossly mischaracterizes the state of the marketplace with respect to demand for TDM/DS1/DS3 services. What AT&T calls "dodos" are in fact the most common building blocks of corporate networks and will remain so for the foreseeable future. … [M]arket power in the special access market enables AT&T, Verizon, and Qwest to engage in anti-competitive price squeezes of their competitors in retail markets for which special access is an input, including Ethernet, wireless, and interexchange services. … [P]rice squeezes can be used to impede competition and exploit ratepayers before (and regardless of whether) competitors are completely forced from downstream markets…[24]

[22] *See, e.g.*, Opposition, at 162.

[23] EarthLink Petition, at 1-2, 22-24; *Applications of AT&T, inc. and Deutsche TeleKom AG For Consent to Assign or Transfer Control of Licenses and Authorizations*, WT Docket No. 11-65, DA 11-99, Petition to Deny of PAETEC Holding Corp., Mpower Communications Corp. and U.S. TelePacific Corp., at 11-18 (May 31, 2010) ("PAETEC Petition").

[24] Ad Hoc Telecommunications Users Committee, Ex Parte, WC Docket 05-25, at 5 (June 13, 2011).

Applicants ignore the downstream effects in all but the wireless broadband market and therefore have failed to rebut the showings that AT&T will have increased incentives to leverage special access (both loops and backhaul) to disadvantage its rivals in numerous downstream markets.[25]

Second, T-Mobile's comments in 2010, prior to announcement of the merger, establish that DS1 and DS3 special access services will continue to be a critical input for wireless providers for years. For example, T-Mobile has stated:

> Because Ethernet is a relatively new transmission technology for backhaul, many wireless providers will continue to rely on TDM technology for at least a few years to carry *voice* traffic. As such, even in markets where Ethernet is available, many mobile *broadband* providers will likely need a mix of DS1s, DS3s, and fiber to satisfy their backhaul connectivity needs for the near future.[26]

Further, T-Mobile acknowledged that it "relies on both TDM-based DS1s and DS3s and Ethernet-based services for both [wireless] backhaul."[27] Indeed, a careful reading of Mr. Mayo's declaration shows that he claims T-Mobile relies on Ethernet primarily for its *IP backhaul needs for mobile broadband*, not all of its backhaul needs.[28] In short, although AT&T attempts to give the impression that the entire wireless market is moving to Ethernet backhaul, a careful reading of the facts shows that the move to Ethernet is limited to only a segment of the wireless backhaul market. Thus AT&T retains the ability and incentive to use its control over TDM inputs, such as copper and special access loops and backhaul, to disadvantage its rivals in retail wireless markets.

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[25] *PAETEC Petition*, 11-18; EarthLink Petition, at 1-2, 22-24.

[26] Reply Comments of T-Mobile USA, Inc., WC Docket No. 05-25, at 2, 5 (Feb. 24, 2010) (emphasis added); *see*, Comments of the Ad Hoc Telecommunications Users Committee, WC Docket No. 05-28, at 4 (Feb. 24, 2010) ("We have about 20,000 T1 dodos and < 100 DS3 dodos. No immediate plans to abandon them to the wild.").

[27] Reply Comments of T-Mobile USA, Inc., WC Docket No. 05-25, at 6.

[28] Mayo Declaration, at ¶ 6.

Third, as the Commission has noted, the relevant market for special access services is route-by-route.[29] While AT&T repeatedly cites the addressable special access market as a whole, it does not rebut numerous claims, or EarthLink's experience,[30] that AT&T still enjoys a virtual monopoly on the provision of DS1 and DS3 special access services to specific buildings and on specific transport routes in its incumbent territory. Instead, AT&T relies on the existence of price cap and pricing flexibility regulation as sufficient to constrain its ability to price special access in an anti-competitive manner.[31] As EarthLink explained, such regulation was not sufficient to constrain AT&T's 2010 price increase that had a substantial financial impact on the price of inputs EarthLink uses to offer competitive broadband services.[32] On July 1, 2010, after the expiration of the Commission-imposed Bell South Merger Condition constraining special access price increases,[33] the AT&T-owned ILECs increased their Phase II interstate special access rates "by 15% or more"[34] --- far more than the 10% increase that AT&T reassures the Commission is "unlikely" should it approve the merger.[35] Remarkably, AT&T had so little fear of competition that it declared these massive price increases in 2007 (*e.g.*, some three years before their effective date in July 2010).[36] AT&T's boldness is evidence that the claimed

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[29] *AT&T Inc. and BellSouth Corporation Application for Transfer of Control*, Memorandum Opinion and Order, WC Docket No. 06-74, 22 FCC Rcd 5662, at ¶¶ 3, 27, 31, 36 and Appendix F (rel. Mar. 26., 2007) ("*AT&T/BellSouth Merger Order*").

[30] Brownworth Declaration, at ¶ 10.

[31] *See, e.g.*, Opposition at 172 (TDM-based special access services "are already subject to an extensive set of price cap rules that ensure just and reasonable rates.").

[32] Brownworth Declaration, at ¶ 11.

[33] *AT&T Inc. and BellSouth Corporation Application for Transfer of Control*, 22 FCC Rcd 5662 (2007).

[34] Sprint Ex Parte Comments, WC Docket No. 05-25, at n.1 (June 28, 2011); *see, e.g.*, Ameritech Tariff FCC No.2, Section 21.5.2. 7(B) and Section 21.5.2.7.1 (A). Similar tariff pages were filed by the other AT&T ILECs (SBC, Pacific Bell, Nevada Bell, SNET, and BellSouth).

[35] Carlton *et al.* Reply Declaration, at ¶ 125.

[36] Sprint Ex Parte Comments, at 2 (June 28, 2011).

competition in the special access market has little impact on AT&T's prices for special access services.

Fourth, to the extent AT&T's all-Ethernet claim was true, its secondary claim that it possesses no market power or advantages in the Ethernet backhaul market[37] is wrong. Although a nationwide measure of Business Ethernet Ports is meaningless where the Commission evaluates competition on a route-by-route basis, the index Applicants' cite nevertheless shows that AT&T "remain[s] at the top of the U.S. Ethernet Leaderboard" in shares of Business Ethernet Ports.[38] Applicants also use an index that appears to measure retail enterprise ports, not cell tower Ethernet backhaul,[39] and therefore does not support the proposition for which the Leaderboard is cited (lack of AT&T control over the Ethernet backhaul market). Finally, by measuring retail competition, the index ignores the fact that many of AT&T's retail competitors rely on AT&T-provided copper or special access loops to deploy competitive Ethernet Business Ports. Where providers of Ethernet Business Ports rely on the incumbents' copper loops, they are not full facilities-based competitors. As the Commission has recognized, in order to demonstrate "effective competition," an ILEC must "demonstrate that there are a sufficient number of significant, full facilities-based competitors providing the relevant retail services so as to make those markets effectively competitive."[40]

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[37] Opposition, at 163-64.

[38] *Mid-2010 U.S. Business Ethernet LEADERBOARD*, Vertical Systems Group, at 1 (August 16, 2010) available at http://www.verticalsystems.com/prarticles/stat-flash-0810-Mid2010_US-Leaderboard.html.

[39] *2010 U.S. Business Ethernet LEADERBOARD: Top Leaderboard tier solidifies*, Vertical Systems Group, at 1 (January 26, 2010) available at http://www.verticalsystems.com/prarticles/stat-flash-01-2011-Year-End2010_Leaderboard_prnews.html.

[40] *Petition of Qwest Corporation for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Phoenix, Arizona Metropolitan Statistical Area*, Memorandum Opinion and Order, WC Docket No. 09-135, FCC 10-113, ¶ 43 (rel. June 22, 2010).

As the Commission is aware, the Ethernet market is made up of at least two distinct markets for Ethernet loops and Ethernet backhaul. EOC as an alternative means of competitive entry is not available in the case of backhaul to cell towers, both because the copper loop UNE is not available[41] and wireless backhaul bandwidth needs require fiber-based Ethernet.[42] EarthLink's experience as a buyer of Ethernet services shows that there are a limited number of providers available to serve any specific address or route.[43] Applicants do not even attempt to show, on a route-by-route basis, that AT&T is subject to substantial competition in the market for Ethernet backhaul. Moreover, Applicants once again ignore AT&T's ability and incentive to discriminate against its rivals in retail markets by exercising control over Ethernet loops. As the No Choke Points Coalition argued:

> The inability of competitors to economically serve off-net locations with Ethernet service via TDM-special access inputs or obtain reasonably priced Ethernet special access services from incumbent LECs will lead inexorably to incumbent LEC dominance of the retail Ethernet market. Indeed, this is already beginning to occur.[44]

Finally, EarthLink's experience confirms that AT&T retains an advantage in the market for fiber-based Ethernet services. With respect to the limited number of buildings and/or cell towers where fiber is necessary, AT&T can build fiber more easily than competitive broadband providers such as EarthLink for a number of reasons. AT&T's market share enables AT&T to

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[41] *Unbundled Access to Network Elements, Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, Order On Remand, 20 FCC Rcd 2533 ¶ 34, n.99 (2005), *aff'd sub nom. Covad Comm'ns Co. v. FCC*, 450 F.3d 528 (D.C. Cir. 2006).

[42] Brownworth Reply Declaration, at ¶ 3 (wireless backhaul requires speeds of 10+ Mbps but EOC provides 10-20 Mbps and only within 3000 feet of a central office).

[43] Brownworth Declaration, at ¶ 10; PAETEC Petition, 12-13.

[44] Reply Comments of the NoChokePoints Coalition, WC Docket No. 05-25, at 15 (Feb. 24, 2010); Mike Robuck, *Cox top MSO for business Ethernet services; AT&T No. 1 overall*, CED Magazine.com ("'AT&T heads our leader board for the second year in a row by increasing its business Ethernet base more rapidly than the overall market.'").

obtain more revenue from its fiber builds to tower sites because such builds will pass by other AT&T customers.[45] One economist estimates that RBOC customer density exceeds competitors' customer density by 24-35 times.[46] As Applicants acknowledge, there is a very high fixed cost to deploying backhaul,[47] such that the ability to add additional subscribers on deployed fiber protects the builder from absorbing all such costs if the primary subscriber discontinues service.

As explained below, AT&T's revenue whole practices, in conjunction with its ability to tie competitive Ethernet services to the purchase of other services on non-competitive routes, also give it an advantage in winning market share in the Ethernet market, and thus the ability to increase its rivals' prices for inputs necessary to offer broadband services.

### B. AT&T Exercises Its Ability to Sustain Anti-Competitive Prices for TDM and Ethernet Loops and Backhaul Inputs through Lock-up Contracts and Revenue Whole Arrangements

Contrary to Applicants' claims, it is not true that AT&T lacks ability to impose a significant price increase in special access and will lose customers if it increases backhaul prices above competitive levels. Applicants first argue that it is "unlikely" that the consummation of the merger would "enable[] AT&T to raise its special access rates by 10%" and suggest that if it did it would lose backhaul customers to competitors.[48] Applicants' assertion is belied by AT&T's 2010 increase in Phase II interstate special access rates "by 15% or more."[49]

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[45] Brownworth Reply Declaration, at ¶ 2.

[46] *In the Matter of Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, Ex Parte Letter of PAETEC, Attached Declaration of Michael Starkey of QSI, at ¶ 10 (Oct. 17, 2008) ("Starkey Declaration") (RBOC customer density exceed competitors' customer density by 24-35 times).

[47] Opposition, at 176.

[48] Carlton, *et al.* Reply Declaration, at ¶ 125 (June 9, 2011); Opposition, at 171, 176 ("the combined company would lose substantial backhaul business").

[49] Sprint Ex Parte Comments, WC Docket No. 05-25, at n.1 (June 28, 2011); *see, e.g.*, Ameritech Tariff FCC No.2, Section 21.5.2. 7(B) and Section 21.5.2.7.1 (A). Similar tariff pages were filed by the other AT&T ILECs (SBC, Pacific Bell, Nevada Bell, SNET, and BellSouth).

Applicants next argue that even if AT&T could raise prices significantly, customers would "lower output or choose alternative backhaul suppliers."[50] In short, Applicants admit the opposite of the point they are trying to prove, namely that increased AT&T special access prices could lead to "lower output" of the competitive wired and wireless voice and broadband services that compete with AT&T's products. As explained above moreover, Applicants made no attempt to show, on a route-by-route basis, that customers could switch to competitive providers of special access services if AT&T raised its prices. Nor did Applicants rebut EarthLink's arguments that AT&T has the ability and incentive to raise prices on special access loops and other wholesale wireline inputs necessary to offer voice and broadband services that will compete with the merged entity's planned LTE offering.

Even if competitive alternatives were available on specific routes or to specific buildings, AT&T's contract tariff provisions make it unlikely that a customer could switch providers. As Mr. Brownworth explained, EarthLink purchases special access from AT&T under multi-year contracts with volume commitments to avoid high month-to-month rates.[51] To the extent AT&T increases its special access pricing above competitive rates, EarthLink cannot simply move its business to a competitive provider. To the contrary, conversion from an AT&T special access circuit to a competitor could actually increase the company's costs because of the impact it has on EarthLink's volume and term commitments and corresponding prices. Circuits must first move to a higher month-to-month rate to be disconnected without penalty or incur a shortfall charge that AT&T assesses a carrier that does not meet its revenue or volume commitments.[52] As Sprint put it, customers "cannot 'vote with their feet to object to the scheduled [or other] rate

[50] Opposition, at 176.

[51] Brownworth Declaration, at ¶ 10.

[52] Brownworth Reply Declaration, at ¶ 4.

increases, because in the overwhelming majority of cases, no competitive alternative exists," or "in those few instances in which there is an alternative, the ILEC customers are almost always prevented from selecting an alternative access provider because of the volume and term plan requirements and onerous termination liabilities AT&T imposes."[53]

EarthLink and Sprint are not the only carriers to face this dilemma. The record in WC Docket No. 05-25 demonstrates that AT&T has locked-up demand for special access services in its 22 state territory through contract and tariff provisions that require buyers to obtain a large majority of their special access services from AT&T in order to obtain steep discounts off of AT&T's excessive "rack rate" special access prices.[54] While economists have noted that volume and term discounts are not per se unreasonable, in the present situation where AT&T has overwhelming dominance in its 22 state territory and often imposes severe penalties for any shortfalls, price discrimination through such discounts can be used to deter competitive entry by increasing the minimum scale that a competitor must provide without setting prices below costs.[55] As Dr. Mitchell has explained, "the result is that the competitor must enter the market at a higher minimum scale, and often over a wider geographic area, than would be needed if the

[53] Sprint Ex Parte, WC Docket 05-25, at 1-2 (June 28, 2011).

[54] *See, e.g.*, *Special Access Rates for Price Cap Local Exchange Carriers*, Comments of Level 3 Communications, LLC, WC Docket No. 05-25, at 24-27 (Jan. 19, 2010) ("For example, several contract tariffs require that a certain percentage of the customer's purchase commitment each year or a certain amount of DS-1 and DS-3 services bought from the ILEC be converted from services previously provided by other carriers."); *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25, Comments of PAETEC Holding Corp., at 18-21 (May 28, 2010) ("PAETEC Comments") ("incumbent LECs' discount plans contain numerous unreasonable terms and conditions including onerous minimum annual revenue commitments ("MARC") or circuit commitments which "ratchet up" if the MARC or circuit commitment is exceeded (thereby locking-in excess demand), limitations on UNE purchases . . ."); PAETEC Holding Corp. *et al*., Petition to Deny, WT Docket No. 11-65, at 11-16 (May 31, 2011).

[55] Comments of Sprint Nextel Corporation, WC Docket No. 05-25, at 38-39 (Jan. 19, 2010) ("*Sprint Comments Jan. 2011*").

new entrant were able to compete on a circuit-by-circuit basis."[56] Discounts based upon a percentage of a customer's total demand when combined with excessive penalties for any shortfall in demand are particularly effective in deterring customers from shifting demand to other providers.[57] DeltaCom's experience as a seller of special access confirms this problem exists with respect to wireless backhaul. Wireless carriers have been unwilling to pay termination liabilities to move circuits to competitive providers and often use the competitor's quote as a means to get a lower price from incumbents such as AT&T.[58]

As PAETEC described the situation:

> [s]uch discount plans also harm competition because they tie the demand of the customer at locations where there is no competition to demand at the limited number of locations where there is competition. As a result, even though non-incumbent LEC wholesalers offer on-net service in certain locations at prices below those charged by the incumbent, the buyer would be worse off choosing the competitive wholesaler in many instances. This is because the penalties that the purchaser would need to pay or the discounts that the purchaser would lose due to missed volume commitments made to the incumbent might well exceed the cost savings associated with purchasing a small number of circuits from a non-incumbent LEC wholesaler.[59]

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[56] *Sprint Comments Jan. 2011*, at 39; Declaration of Bridger M. Mitchell, WC Docket No. 05-25, at ¶¶ 119-126 (Jan. 19, 2010) ("Mitchell Declaration") ("Minimum volume commitments can require the buyer to purchase all, or nearly all, of his special access services from the incumbent LEC and to incur substantial penalties for failing to maintain minimum volumes over the term of the contract. The effect of such conditions is to erect barriers to entry by competitive suppliers. In order to compete for a buyer's business the entrant must be prepared either to offer to supply the entire quantity required by the buyer or to offer a smaller quantity at a sufficiently lower price such that the savings to the buyer from switching a portion of its purchases to the competitor offsets the penalty under the incumbent LEC contract.").

[57] *Sprint Comments Jan. 2011*, at 39-42 ("Multiple-market terms and conditions tie the availability of discounts in areas without competition to the purchase of incumbent LEC services in areas where competition is present or feasible, thereby hampering the ability of alternative providers in the latter areas to compete effectively.").

[58] Brownworth Reply Declaration, at ¶ 5.

[59] PAETEC Comments, at 21, n.73. As economist Michael Pelcovits has explained, "[t]he key to successful exclusionary pricing is to condition the pricing of the monopoly portion of the customer's

Numerous others have encountered this anti-competitive dilemma. Sprint, for example, reports that it "typically has to commit to five-year contracts with its large rivals [AT&T and Verizon] to get the best rates, with the pricing structured to discourage looking at alternative suppliers."[60] In addition PAETEC, Sprint and others have catalogued and filed evidence of the onerous terms and conditions that AT&T and others use to lock up demand for special access services. Sprint, for example, has noted five general categories of such terms: (1) Revenue commitment levels set at up to 100 percent of current demand levels; (2) Shortfall penalties if actual demand falls below specified levels; (3) Overage penalties if actual demand exceeds specified levels; (3) Termination liabilities for exiting the plan prior to the scheduled expiration date; and (4) Onerous circuit migration charges and restrictions.[61]

AT&T's ability to stave off customer defections goes beyond its special access contract terms and conditions. Mr. Brownworth explained AT&T's current "revenue whole" policy in his declaration.[62] Under this policy, whether EarthLink is seeking a reduction in commitment under a contract that has not yet expired, or is seeking to renegotiate pricing at the end of a contract term, AT&T takes the position that it will only reduce commitments or negotiate lower prices if it is made revenue whole. In other words, for EarthLink to get a reduced commitment/lower price on one AT&T product (broadband facilities), it must agree to increase

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demand on the choices the customer makes for the competitively sensitive portion of demand. The customer then pays a higher price on the monopoly demand if he deals with a competitor on the competitively sensitive demand." Reply Comments of WorldCom, Attachment A: Declaration of Michael D. Pelcovits, RM-10593, at 7 (filed Jan. 23, 2003).

[60] Roger Cheng, *Leap Wireless Opposes T-Mobile Deal*, The Wall Street Journal (May 24, 2011).

[61] Mitchell Declaration, at ¶ 125; Sprint Comments, GN Docket No. 09-51, at 35-45 and Attachment 4 (Nov. 4, 2009). Sprint's Attachment 4 provides a table of AT&T provisions that serve to lock in demand for special access services.

[62] Brownworth Declaration, at ¶ 15.

commitment/purchase another AT&T product (metro Ethernet).[63] In short, AT&T uses its control over necessary inputs on non-competitive routes to restrict customers' ability to purchase from alternative providers those services that may be subject to competition.

AT&T's past misconduct establishes that there are no competitive market forces sufficiently strong to prevent or limit the rate increases that AT&T is highly likely to impose on its competitors should the Commission approve the proposed merger. AT&T also unrealistically assumes that Commission regulation is sufficient to constrain prices for TDM special access services. The failure of the Commission's pricing flexibility regime has shown that pricing is not constrained by the theory of competition or projected competition. To protect consumers, the Commission's policy decisions must address current circumstances and market conditions. Moreover, the policy reforms required to address these issues must remain in effect permanently or until they are no longer needed and not be time bound merger conditions. As EarthLink and others have shown, those current conditions show that the proposed merger is not in the public interest and would harm competition and consumers.

[63] *Id.*

## III. CONCLUSION

AT&T's acquisition of T-Mobile would increase its incentives to raise prices for, or restrict the availability of, wholesale inputs to competitive broadband services, thereby harming consumers. The Commission should not begin consideration of the Application until it completes reform of its wholesale competition policies.

Respectfully submitted,

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Dated: June 20, 2011

**SERVICE LIST**

I, M. Renee Britt, hereby certify that on this 20th day of June 2011, I have caused a copy of the foregoing Reply of EarthLink, Inc. to be served, as specified, upon the parties listed below:

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