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THE TELECOM ACT FIVE YEARS LATER: IS IT PROMOTING COMPETITION?

HEARING

BEFORE THE

SUBCOMMITTEE ON ANTITRUST,
BUSINESS RIGHTS, AND COMPETITION

OF THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

ONE HUNDRED SEVENTH CONGRESS

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THE TELECOM ACT FIVE YEARS LATER: IS IT PROMOTING COMPETITION?

WEDNESDAY, MAY 2, 2001

U.S. SENATE,
SUBCOMMITTEE ON ANTITRUST, BUSINESS RIGHTS AND COMPETITION,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The Subcommittee met, pursuant to notice, at 2 p.m., in room SD–226, Dirksen Senate Office Building, Hon. Mike DeWine (Chairman of the Subcommittee) presiding.

Present: Senators DeWine and Kohl.

OPENING STATEMENT OF HON. MIKE DEWINE, A U.S. SENATOR FROM THE STATE OF OHIO

Chairman DEWINE. Good afternoon. Let me welcome all of you to the Antitrust Subcommittee hearing on the state of local telephone competition 5 years after the implementation of the 1996 Telecommunications Act.

Our Subcommittee has examined the competitive status of this industry on numerous occasions since 1996. Over that time, we have seen some improvement in the competitive environment as a result of the Act. However, we still have a long way to go.

Candidly, after 5 years, growth in competition among local carriers has been disappointing. Though no one expected immediate miracles upon the Act's implementation, competition is far from where it could and should be.

On the positive side, the most recent FCC data available shows that between the end of 1999 and June, 2000, the competitive local exchange carriers increased their market share from 4.4 percent of local telephone lines to 6.7 percent. This competition is particularly strong in the local business sector, where the competitive local exchange carriers have gained 17.5 percent of the market.

We also have seen some progress under section 271 of the Telecom Act. The Bell companies now have satisfied FCC and Justice Department conditions for opening their local markets in five States, including three since the beginning of this year.

Another positive trend is the movement among some cable companies to begin providing residential phone service over their cable systems. As many of you know, one of the guiding principles behind the Telecom Act was that cable would serve as a so-called "second wire" into the home, providing facilities-based competition to the local phone companies. It is encouraging to see promising developments in this area.

At the same time, however, there are many reasons for concern. Incumbent telephone providers still have over 93 percent of the overall local market, and the competitive picture in the local residential market is even worse. The competitive local exchange carriers have only 3.2 percent of the residential market. With competitive providers serving just over 3 percent of these residential customers, it seems fair to say that most residential phone customers continue to have really only one choice, one choice, for local service.

Now, we must be careful, however, not to consider market share as the exclusive indicator of whether or not competition actually exists. The Act does not set market-share benchmarks because it recognizes that sometimes even markets that are open will be dominated by one company. Nevertheless, after 5 years, it is hard to argue that a 3-percent market share by competitive carriers in local residential markets is an acceptable result.

Even worse, many of the companies that have tried to provide competitive service have suffered financial setbacks. We already have seen some go out of business as the capital markets begin to reevaluate the financial prospects of the market for competitive telecommunications services. If this trend continues, competition and consumers will suffer.

Some within the industry argue that the struggles competitive providers have suffered recently are part of a natural market evolution. Others argue that many of the problems have resulted because the 1996 Telecom Act has not been properly enforced. These are issues we need to discuss with our witnesses today.

Further, while we see many competitive providers struggling, there are some that believe the Act should be reopened to allow the Bell companies to begin immediately providing long distance data services. It is not my intention to focus on this specific legislative proposal during our hearing today.

However, that specific issue is related to the broader question of whether we need to revisit the Telecom Act to provide a different balance between the incumbent and competitive providers of local telephone service. For example, some have suggested we should consider additional legislation to improve the access of local providers to residential buildings. This is one of the important policy issues that we will discuss here today.

Let me say I look forward to our examination of these very complicated issues, and I remain committed to ensuring a competitive environment in this very important industry.

Before I turn to Ranking Member Herb Kohl, I would like to note for the record that, as a rule, the Antitrust Subcommittee usually receives testimony from industry witnesses who are responsible for the business operations of their respective companies. We have found that those who are responsible for the day-to-day operations and the big picture strategic thinking have been able to give us the most insight into the competitive issues we focus on in this subcommittee.

In this instance, however, Mr. Ed Whitacre, the CEO of SBC Communications, was unable to be here today because of scheduling conflicts, so Mr. Jim Ellis, the General Counsel of SBC, is here in his place. We appreciate Mr. Ellis being here today and we anticipate that his testimony will focus on the business environment

and challenges facing SBC, rather than on any legal battles that may be ongoing. We anticipate that our other witnesses on the second panel will have a similar focus.

One final note before I do turn to Senator Kohl. As some of you may be aware, Senator Kohl's basketball team, the Milwaukee Bucks, successfully advanced to the second round of the NBA playoffs just last night. We all want to congratulate Senator Kohl and, in his honor, we are all using Milwaukee Bucks pens. I'm sure that if any of you want to see the Senator afterwards and want a pen, I'm sure that Senator Kohl has a few more.

Senator Kohl. Congratulations.

STATEMENT OF HON. HERBERT KOHL, A U.S. SENATOR FROM THE STATE OF WISCONSIN

Senator KOHL. Thank you very much, Senator DeWine. We appreciate your holding this hearing here today.

More than 5 years have passed since the Telecommunications Act of 1996 became law, so this is a good time to see what progress has been made to bring true competition to telecommunications. The main goal of the Act was to bring real competition to all aspects of communications services, particular to local telephone service. But with the regional bells still controlling abut 93 percent of the local phone market, and rates remaining steady over the last 10 years, no one can claim that the Act has been a roaring success. We have been waiting for local phone competition for 5 years, and we are still being kept on hold.

As we look back on 5 years of the Act, it is time to try to learn some lessons. With AT&T about to be broken into four companies, and most of the potential competitors to the regional Bells in serious financial trouble, the biggest lesson seems to be this: Congress cannot mandate competition, and if competition doesn't make business sense, then laws like the Telecom Act will not really work.

Now, that doesn't mean that we shouldn't consider "fine tuning" the Act so that it is a more effective tool to promote competition. For example, one major stumbling block to competition has been building access. If the owner of a big apartment or office building has a sweetheart deal with a phone company, then building residents are often prohibited from shopping around for a different phone company. As a result, the telecom competitors are denied access to a large, important pool of potential customers, and people are locked into expensive service because the building owner has a special deal. This is a recurring problem that we have observed in our recent cable hearing as well.

But, despite the need for fine tuning, most Americans would probably look at the telecommunications field today and stand in awe of the innovation explosion over the last 5 years. From cell phones to the Internet, from e-mail to DSL lines, consumers can communicate with each other quicker, faster, and more efficiently than ever before.

Competition for long distance telephone service is vigorous, with rival providers engaged in fierce competitive battles and inexpensive rates of five cents a minute and lower being common. Cellular telephone use continues to grow, with more than 80 million users nationwide. With prices dropping, cell phones are changing from a

luxury item to a true mass means of communications used for everyday needs.

That's the good news. But local residential service is still the bread and butter of the telecommunications field, and competition to provide that service is still the "Holy Grail". We have not gotten there yet.

Maybe we need more time, but with the first round of competitors dropping out of the field, maybe we need to tinker with the Act. We need to ask whether the Act needs more enforcement authority—through antitrust laws or by the FCC—and we also should ask whether we need to give the regional Bells more of an incentive to open up their networks.

Finally, we need to keep a vigilant eye on another potential round of mergers, where antitrust laws and principles will play a very important role.

We look forward to hearing from today's distinguished panel of witnesses, and we thank you all for your willingness to testify.

Thank you, Mr. Chairman.

Chairman DEWINE. Thank you, Senator Kohl.

Let me turn to our first panel. Pat Wood is the Chairman of the Public Utilities Commission of Texas, a three-member panel which regulates the State's telecommunications and electric power industries. He has served on the Commission since 1995. He also has been nominated by President Bush to be a Commissioner on the Federal Energy Regulatory Commission. We congratulate him on his nomination and are certainly glad to have him with us today. Thank you, Mr. Wood, for joining us.

Reed Hundt served, of course, as Chairman of the Federal Communications Commission from 1993 to 1997, where he presided over the implementation of the Telecom Act of 1996. Prior to his work on the Commission, Mr. Hundt was a partner in the Washington, D.C. Office of LathaM & Watkins. He is a senior advisor on information industries, currently to McKinsey and Company. Mr. Hundt has testified before our Subcommittee many times in the past, and we welcome him back.

Mr. Wood, we will start with you. We have both your written statements, which will, without objection, be made a part of the record. We would ask you to proceed for about 5 minutes or so and then we will have more of an opportunity to ask questions.

Mr. Wood.

STATEMENT OF PATRICK HENRY WOOD, III, CHAIRMAN, PUBLIC UTILITY COMMISSION OF TEXAS

Mr. WOOD. Thank you, Senator DeWine, Senator Kohl. It's a pleasure to be here.

I view that the States are the front line for implementing the Act that you all passed in 1995, and working with our colleagues at the Federal Communications Commission, I think I would like to provide some, I guess, real world checks on the perceptions perhaps that the Act is not working.

I think in States like ours, where we have taken the challenge from the Congress and the mandate from our State legislatures and Governors to get the competition, the tools that were given were quite sufficient. They may not be in years to come, but cer-

tainly the tool of 271, which I mention at some length in my testimony—and I should add that the end stages of that 271 were negotiated with Mr. Ellis and some of his colleagues, so his strategic business acumen I will attest to from personal experience.

But the key takeaway from us, I hope, is that the Act can work. It's not necessarily predestined to work, 271 being one aspect. Certainly it is the one that is most fresh in my mind because it was in 1998, 1999 and early 2000 timeframe that we worked with the industry, with the company, with the competitors, with customers, with our own staff, to try to craft a 271 approval process that, in fact, got us from a relatively highly regulated world for Southwestern Bell Telephone to a wide open world, that was inviting to competitors, that had sufficient bristling enforcement tools available, to incentivize good business practices—because, quite frankly, you're turning a business relationship that was adversarial between competitors into one of being a wholesale supplier and a wholesale customer.

I don't know what the analogy to divorce would be, but I think it's similar to putting together a marriage that's been irrevocably broken into one that now has a parent-child relationship. Incest and all those wonderful things come to mind, but it's a difficult relationship to monitor. Just trust me. As the front line, it has been difficult.

But we do try to use some tools of our own making, working with the Federal Commission. Some tools, quite frankly, a lot of this has been make it up as you go. Regulators at the State level have historically kind of looked at things, run them through a typical procedural timeframe that's way too long for competitive markets, and try to come up with outcomes.

Today, we do a "rope 'em/throw 'em" docket that is rough. It can be from a 72 hour decision to a 14-day decision, or a slow decision is viewed to be a 60-day decision. That requires kind of a different mindset. It has been as difficult for us as it has for the affected companies to adjust to this new world, but it is one that we're slowly getting comfortable with.

I can speak for my sister States when I say that certainly the 271 carrot, which was "if you open your local markets, then you get to get into that guy's long distance markets and data markets" is a great incentive. In the States that have used it—and I think a number of us are using it still—even after it's over, it still works. I get data every week from the company as to how well they're performing under a series of some 100 performance metrics on every aspect of their business relationship with their wholesale customers.

That allows me and my colleagues and our staff and the industry to track Southwestern Bell's performance, and I will say that everyone had feared that once they get into long distance, they'll say great, they'll never take it away from us, let's just do it, and we need to do it anyway. They have done a better job. It has not been backsliding. In fact, it has gotten better in the Texas market, and I would venture to say in the other markets as well.

So you can have a company come to the table, decide that the old world is something they want to leave behind as well, and move forward into the new world.

I would like to point out briefly before I close two things that are in my testimony, that I would like to call to your attention based on your comments. On building access, in 1995 Texas passed a building access law that Governor Bush signed, and it has been on the books kind of quietly, quite frankly, for the past 5 years. We put in some implementing rules to make sure, if there was ever a process, the Commission could handle it. But I would like to call to your attention that, at least in our State, we have had a rule that allowed the last foot to be not just the last mile but the last few inches of it to be open at a customer's request in these multi-tenant buildings.

Finally, one thing I mentioned recently is a good aspect of our Texas law. We standardized how municipalities, how local governments interface with telephone companies. That has been, quite frankly, something that facilities-based competitors tell me is the best thing Texas could have ever done for its local markets, is to standardize the way that you deal with, in Texas, 1,200 municipalities. It's one thing to win a decision at the PUC, but it's another to have to go slug it out at the different cities of Texas. So that's something that doesn't call for a Federal solution but is of interest.

Finally, residential rates. Residential rates are low. I believe in your States they are as well. They may even be lower than cost. I mentioned in my testimony some numbers there. It will be difficult for competitors to ever come into the Texas market, just as it will be difficult to get into the California electricity market, if you can't sell for the proper price or compete with the proper price which you just bought for ten dollars more. That's a reality that I think we're going to have to face.

Again, it's probably a State issue, but as Federal decisionmakers that are lamenting, as I think is fair, the lack of residential competition, it is important to know that residential rates were purposely subsidized for 80 years, and business rates and long distance rates were kept high to make up for that.

Those are attractive markets for competitors. There is a great market entry. The Texas statistics that I provided you show there is plenty of entry into the business market. There is some entry into the residential market as well, but to the broad market, it's going to be a long time until there is comprehensive competition due to the fact that the residential rate has been largely subsidized to a below-cost offering over the last 80 years.

I'm not urging that something be done for that. I think it is difficult politically and on a policy basis to go there, but please understand that that is one issue that is really our fault. But it impacts the statistics that you all look at.

[The prepared statement of Mr. Wood follows:]

STATEMENT OF PAT WOOD, III, CHAIRMAN, PUBLIC UTILITY COMMISSION OF TEXAS

I am pleased to give you a "Report from the Front Line" of the telecommunications revolution. I like to think of Texas as a good example of how the Federal Telecommunications Act of 1996 (FTA96) is working. Thanks to the FTA96, and to Texas legislation in 1995 and 1999, Texas has seen marked progress toward a more competitive local market. We are already experiencing the benefits of more competition in the long-distance and data markets.

Competition sets the stage for eventual deregulation, and that is a goal worth working hard for. On our best days as regulators, we cannot begin to compare with

a well functioning market in delivering better prices, more responsive service and unleashed technological innovation to customers.

The FTA96 removed legal barriers to entry of companies into various telecommunications lines of business, and that was a significant step. But that alone has not made competition happen. Undoing the effects of a century of pervasive regulation has taken time, more time than most thought would be needed. These effects are primarily operational in nature and stem from the understandable reluctance of incumbents in all markets to assist in implementing a regime that necessarily erodes their historical market shares.

The FTA96 focused on opening the voice markets to competition, and its primary focus was on opening the non-competitive local markets. The FTA96 also pointed the way for greater competition in long-distance markets. Data services were a small part of the text of the FTA96, but, as technology has speedily evolved, some of the provisions of the Act have been applied to these services as well.

Congress gave the state commissions a significant front line role in implementing the various aspects of the FTA96:

- arbitration of unresolved issues in incumbent-competitor interconnection agreements under §§ 251 and 252,
- a mandate to reform decades-old universal service subsidy structures under § 254, and
- the responsibility of steering the largest local providers, the Regional Bell Operating Companies, through § 271 long-distance authority checklist.

Working with the federal commission, we have plowed through myriad operational, technical and financial details to implement these provisions. Implementing the Act has been the most resource intensive project that we at the state level have undertaken in recent decades, requiring us to become experts on every aspect of the telephone network, from the Network Interface Device at a customer's home to ultra-high bandwidth optical transport, and everything in between. We have developed expertise on modern network design, pricing and operational support systems. We have often interpreted the law in real-time, often faced with deciding issues before the FCC or other states did. We have been faced with numerous twists and turns as various federal courts have issued their pronouncements.

State commissioners and our professional staffs have done these things while keeping our focus on the retail customer. There has never been such an opportunity to pull together so many key issues in this industry for comprehensive resolution, and I can fairly speak for my state commission colleagues when I thank Congress for giving us this §§ 251, 254 and 271 gift, which has allowed us to move swiftly away from the old world of monopoly style regulation to a new world of marketplace competition. We aren't all the way there yet, but I believe that in Texas, at least, we have shown that the FTA96 can and does work.

§ 252 ARBITRATIONS.

The fundamental business contract model of the Act (interconnection agreements) was different from the tariff-based model familiar to us at the Texas Commission. The FTA96 model is based on the premise that the incumbents and competitors will negotiate many aspects of their business relationship. In fact, in mid-1996, due to the relative imbalance of bargaining position, we were called upon, under FTA96 § 252, to arbitrate a comprehensive set of rates, terms and conditions for Southwestern Bell Telephone Company (SWBT) and a host of competitors (AT&T, MCI, Sprint, ACSI and Teleport). My two fellow Commissioners and I presided over this "Mega-arbitration," directly, employing the considerable legal, technical, financial and process-management talents of our staff. After a three week hearing, we issued our Arbitration Award in December 1996, thereby establishing Texas' policies for interconnection, provisioning and pricing. The resulting interconnection agreement was later affirmed in substantial part by the local Federal District Court and the U.S. Court of Appeals for the Fifth Circuit, and numerous other competitors have adopted the agreement for their own.

Following the approval of these initial agreements, the Texas Commission has been involved in numerous follow-up contract interpretation disputes. We adopted the famous "rope 'em and throw 'em" expedited dispute resolution process to facilitate competitive market entry. Often, these complaints related to money. Other issues have related to the technical feasibility of certain network interconnection arrangements and required the opposing parties to provide our staff arbitrators with rapid primer courses in the latest telecommunications technology. Our goal has been for the incumbent to provide the requested service immediately unless it can show direct network incompatibility, and the Commission will swiftly determine the ap-

propriate pricing. This prevents the incumbent from using the dispute process to stall a competitor's entry.

Because most of 1996–1997 agreements had three-year terms, the Texas Commission was called upon in 1999 and 2000 to arbitrate successor agreements. The list of decision points for arbitration was dramatically shorter, perhaps indicating that the initial 1996 decisions were generally acceptable to the parties. Interestingly, these second-round arbitrations focused on new technology issues, such as access to and pricing of xDSL technology, which reflected an increased focus on the data services markets. As before, the Texas Commission has had to make many determinations in real time, without much precedent from other jurisdictions. Where other jurisdictions, such as New York, have plowed similar ground, we have borrowed heavily from their fine work to maximize our resources. NARUC, the state commission national association, has aggressively and successfully facilitated this exchange of information among the states.

At the Texas Commission, we have gotten relatively comfortable with our role as wholesale market referee among industry players. The balance between the FCC, as policy clearinghouse, and the states, as front line arbitrators and watchdogs, seems to be working well.

UNIVERSAL SERVICE AND OTHER SUBSIDIES.

Over the years, state and federal regulators used various regulatory subsidy mechanisms to maintain low retail prices for residential service, particularly in rural areas. The arrival of competition into telecom markets has forced us to revisit the way these subsidies are handled. In the FTA96, Congress made clear it wanted the rural universal service support to be maintained. This is challenging, but it can be done. So long as the subsidy is competitor-neutral and technology-neutral, it can be sustained in a competitive market.

In times of industry change, it was important for us to establish early what the ground rules were so that sufficient investment would come to Texas, particularly to rural areas. So, in 1997, the Texas Commission began a two-year process to restructure our rural subsidy support system. For years we had kept intrastate access charges much higher than needed to subsidize the higher cost of providing dial tone to low-density rural Texas. Using some rather complex cost modeling, we quantified the excess cost faced by rural providers (above the revenues obtained from the typical customer). We then removed those amounts from the rates of all providers' access charges, and collected these amounts on a 3.6 percent of retail revenue basis from all telecom customers, including long-distance, local and wireless customers. This explicit surcharge on customers' bills yields $600 million annually for the Texas Universal Service Fund (USF). Although over 90 percent of the fund is for rural support, the Texas USF also supports low income subsidy programs and funds hard-of-hearing customer programs. A separate 1.25 percent surcharge provides support to schools, libraries and rural health institutions to offset costs of advanced technology connections. This ten-year Fund, which began in 1995, is administered by the Texas Infrastructure Fund Board.

I have been a member of the State-Federal Joint Board on Universal Service for the past few years. In the national discourse over the federal USF, I have expressed the view that all states should attempt to address their own rural subsidy issue themselves to the maximum extent possible, relying on the federal USF only as a last resort. This would mean that current recipient states from the federal USF, like Texas, should directly fund more subsidy from state USFs instead, leaving federal support for those states which have few lower-cost urban customers to support a sufficient state fund. With the many present claims on the federal USF and a court determination restricting the assessment base for the federal USF, the current federal USF surcharge level is high and should not be stressed further.

SOUTHWESTERN BELL LONG DISTANCE ENTRY.

Southwestern Bell Telephone Company (SWBT) serves over three-fourths of the local access lines in Texas. As a Regional Bell Operating Company, it was subject to satisfying the fourteen-point checklist of FTA96 § 271 before it could offer long distance to customers in Texas. This "carrot" has been the most effective tool Congress could have given states that desired to open their local markets. But it has not been an easy process.

In March 1998, SWBT asked the Texas Commission to review and approve the steps it has taken to open its local market under the checklist. After a 90-day review process, which included three weeks of hearings before my fellow Commissioners and me, we concluded that SWBT had not met the checklist; we detailed 129 specific issues requiring resolution. We then set up a collaborative process

which would include SWBT, its wholesale customers (CLECs) and the Commission staff to work through the list. This ran from July through November, 1998 and resulted in closing out many but not all of the 129 items. Patterning off of New York PSC Chairman O'Mara's closure process earlier that year in his state, and complying with our state's strict Open Meetings law, my fellow Commissioners deputized me to negotiate the remaining items directly with SWBT, which I did (with the assistance of highly capable staff) in the Spring of 1999. Shuttling between a room of SWBT executives and a room of CLEC experts to resolve issues, I was able to recommend to my colleagues in April 1999, a Memorandum of Understanding between SWBT and the Commission closing out all of the issues identified the year before. With some amendments, the full Commission approved the Memorandum.

The Memorandum formed the basis for a comprehensive thousand-page interconnection agreement which we determined fully satisfied the entire fourteen-point checklist. Over the following five months, specific details of the Texas 271 Agreement (T2A) were worked out among the parties, requiring some direct rulings by the Commission on specific language. On October 13, 1999, the Texas Commission formally approved the Agreement, permitting any interested CLEC to adopt the agreement. Over 150 have done so to date, and many others have adopted substantial parts of the T2A into their own customized agreements. I am pleased that our sister state commissions in Oklahoma, Missouri and Kansas have modeled their 271-compliant interconnection agreements on the T2A.

One of the most significant aspects of the T2A was the adoption of over 100 specific performance measures and a Performance Remedy Plan placing up-front financial penalties on SWBT if it delivered sub-par performance to its wholesale customers (CLECs). This set of performance standards continues to serve as the weekly and monthly report card for SWBT's wholesale performance, much the same as the Texas Commission has monitored SWBT's retail performance. It has generated several million dollars in penalties for the State and for individual competitors since October 1999, but, more importantly has provided a very strong incentive for SWBT to swiftly remedy any processes which have failed to meet the performance standard. The measures themselves have undergone two six-month reviews (removal of some measures, amendments to others, creation of new ones) and are being spot audited by the Commission for accuracy. We have combined this review process with our sister SWBT states to ensure uniformity as much as possible.

While the T2A was being prepared, the Commission was closing out its twelve-month review of SWBT's extensive Operation Support Systems (OSSs) by an independent third-party advisor, Telcordia. All aspects of SWBT's pre-ordering, ordering, maintenance/repair and billing systems (both mechanized and manual) were reviewed. A number of items were found lacking and required rework. The process was a military style test, in that it ran and re-ran until it was passed. The total bill for the testing process exceeded $14 million and was funded by SWBT.

The final step needed for the Texas Commission to conclude that the SWBT local market was irreversibly open to competition was a review of SWBT's actual performance. By reviewing the results of the monthly performance data with the Commission and CLECs and by diagnosing various shortcomings, SWBT made a number of further business process improvements.

In December 1999, the Texas Commission was fully satisfied with the evidence on SWBT's performance, and we finally voted our unqualified support of SWBT's application to the FCC for long distance authority. Throughout SWBT's initial Texas 271 FCC filing in January 2000, and its updated application in April 2000, the Texas Commission worked with the Department of Justice and the FCC to explain and detail SWBT's application. In July 2000, after receiving the Department of Justice's first endorsement of a § 271 application, the FCC granted the request, making Texas the second state to fulfill the § 271 requirements.

The SWBT OSS is a regional system. The work of the company and CLECs to meet our requirements in Texas assisted our sister states of Kansas and Oklahoma in their successful § 271 grants earlier this year. The Missouri application is now pending before the FCC. Without question, a regional approach on common matters is the most effective way to move forward with the § 271 checklist. I note with interest that the fourteen US West/Qwest states are also engaged in a regional collaborative on δ271 matters.

Aggressive use of the § 271 carrot has greatly accelerated Texas' goal of opening its local markets to competitors. Attachment A to this testimony is a staff compilation of data demonstrating that substantial entry has already taken place in Texas. As of March 2001, approximately 2,636,000 access lines are now being served by some 300 CLECs in SWBT's Texas region. This compares to SWBT's total access line count of approximately 10,210,000 access lines. (September 1999).

Of course, the *quid pro quo* of this proceeding was SWBT's entry into long distance in Texas. Public reports indicate that SWBT has been successful in attracting about two million customers to its long distance service. The presence of this significant new competitor has dropped average retail long distance rates below 10 cents per minute for the first time in Texas history.

About 22 percent of the access lines in Texas are not being served by SWBT, and market entry by competitors in these mostly non-urban areas is much lower. (Data from non-SWBT areas is not included in Attachment A). I must fairly point to the lack of the § 271 carrot as the principal reason for this disparity. CLECs have discovered that, even in competition-friendly Texas, market opening is not for the poor or the weak-hearted. It requires money, smart people, and patience. By consolidating all issues in a common proceeding, § 271 allowed CLECs, SWBT and the Texas Commission to pool efforts to achieve what I believe is the most significant competitive breakthrough in our Commission's history.

OTHER TEXAS POINTS OF NOTE.

Winning approval of a wholesale contract before the Texas Commission is one thing; implementing it in 1200 Texas municipalities is quite another. In 1999, the Legislature passed and Governor Bush signed a law which standardized the municipal rights-of-way process for incumbents and competitors. The law stabilized the municipal franchise fee at the 1999 level and simplified its collection into three fee-per-access-line categories (residential, commercial and point-to-point). Payment of this fee to the end-user's municipality allowed unquestioned access to the necessary municipal rights-of-way by any certified telecommunications provider in any municipality. Many companies in Texas have told me that this is the single best thing Texas could have done to welcome facilities-based carriers to our state.

In 1995, Texas also adopted a building access statute which required multi-tenant building owners to provide equal access to certified telecommunications providers. In 2000, the Texas Commission adopted specific procedural guidelines that should be observed and set out a Commission process to be used if negotiations between building owners and providers failed. To date, the Commission has not been asked to formally adjudicate such a dispute.

More information about the Texas Commission can be found on our Web Page at www.puc.state.tx.us.

CURRENT ISSUES.

In the five years since the FTA96 was passed, the Internet has transformed our culture. In 1996, "www" was more often the result of a lazy finger sitting on the keyboard than a pervasive form of corporate and personal identification. It is amazing that, despite this dramatic transformation of this industry, some of the fundamental aspects of pricing under the 1996 Act are pending before the U.S. Supreme Court, which may be completed by the sixth anniversary of the Act. The time required for judicial review of every aspect of FTA96 implementation has been, and remains a destabilizing aspect of this transition.

Another issue relates to capital investment. Unlike the transitioning electric power industry nationwide, the telecommunications industry has been relatively successful in attracting capital. We have witnessed a slowdown in capital investment in the past eight months, but I believe this is more a rest stop for the market than an exit. Some business plans are passing sober investor review; others, particularly narrow ones, are not. Nevertheless, one of our bigger challenges is to continue to provide investor certainty with a clear long-range vision and stable rules of the road. Predictable, balanced outcomes and consistent enforcement of obligations are- needed to maintain investor confidence in the sector.

One final concern worth pointing out, although it is unquestionably a state jurisdictional issue, is the nature of local phone service pricing. During the years of monopoly phone regulation, most states have priced business service higher than residential service in order to achieve social and political goals. One truth of functioning competitive markets is that prices are driven to cost. Where the retail price of residential service is below the wholesale cost of providing it, the market fails to work.

In Texas, the "all-in" monthly retail price for SWBT basic residential service (with no add-ons such as call waiting or caller ID), is about $17. The corresponding business price is $32. Under the extensive cost-study reviews conducted in the Texas Commission's "Mega-Arbitration" and continued in the SWBT Texas 271 Agreement, the monthly wholesale price for a standard access line is about $21. These numbers go a long way toward explaining why residential competition falls far behind business competition today. While customers who use multiple services will always be attractive, broader residential competition will likely come from other technology

platforms (cable, wireless, satellite) rather than resale of incumbent networks. The solution of raising residential rates to enable residential competition is unpalatable. Again, this is an issue for state Legislatures and regulators to wrestle with, but federal decision-makers should understand that it is a core issue.

On behalf of my state commission colleagues across the nation, we appreciate the confidence Congress had in us five years ago when it designated us the "Front Line" for implementing competition in the nation's critical telecommunications industry. I trust we have kept faith with your intent.

Competition in SWBT Serving Area in Texas
Attachment A

SUMMARY SHEET
Competitive Entry
In SWBT Serving Area

	Dec '99		Mar '01	
Interconnection Trunks	349,400 trunks	698,800 lines *	595,589 trunks	1,191,178 lines *
UNE Platforms	145,198		1,102,029	
Resale	350,667		343,424	
TOTAL *	1,194,665		2,636,631	

* = one trunk represents 2.5 customer access lines, 80% utilization rate

Competition in SWBT Serving Area in Texas
Attachment A
CLEC Line Count for 2001

Total Service Resale Providers

The growth in number of access lines served by total service resale providers as of March 2001 is fairly flat since December 1999.

	Dec'99	Jan'01	Feb'01	Mar'01
Total Service Resale				
Residential	171059	172,571	164,817	160,768
Business	179608	188,359	188,332	182,656
Total	**350,667**	**360,930**	**353,149**	**343,424**

UNE-Platform Providers

UNE-Platform CLECs have gained significantly large number of lines (approximately 659%) as of March 2001, in comparison to December 1999. However, during the first quarter of 2001, the growth appears to be fairly flat.

	Dec'99	Jan'01	Feb'01	Mar'01
UNE - P	145,198	981,383	1,043,595	1,102,029

Competition in SWBT Serving Area in Texas
Attachment A

Switch-Based Providers (CLECs)

Number of UNE Loops

Some of the access line growth for switch-based CLECs can be estimated by counting the number of unbundled loops, to the extent the CLECs are using the UNE loops.

Deployment data show a 287% growth in the number of UNE loops from December 1999 to March 2001. However, the average monthly growth rate during the first quarter of 2001 is about 2.9%.

UNE – Loop				
	Dec'99	Jan'01	Feb'01	Mar'01
8 dB Loop	18301	72,498	74,400	76,797
5 dB Loop	2881	5,029	5,171	5,267
Total	**21,182**	**77,527**	**79,571**	**82,064**

Number of Interconnection Trunks and Calculated Access Lines

Also, the growth in the number of interconnection trunks indicates increased traffic from SWBT network to CLEC network. With the assumption that the CLEC trunks carry 2.5 lines per trunk with a utilization level of 80%, the number of access lines served by CLECs can be estimated. Deployment data shows a 70.5% growth in interconnection trunk and calculated access line count for switch-based CLECs in SWBT serving area as of March 2001 in comparison to December 1999 data. However, during the first quarter of 2001, the average monthly growth rate is at 4% approximately.

	Dec'99	Jan'01	Feb'01	Mar'01
# of Interconnection Trunks	349,400	556,999	588,079	595,589
Calculated # of Lines	698,800	1,113,998	1,176,158	1,191,178

Number of NXXs

To a certain extent, the increase in the total number of NXXs loaded on to SWBT switches can also be attributed to the increase in competition. Please see table below for the number NXXs that are active as of March 2001.

	Jan'01	Feb'01	Mar'01
# of NXXs loaded	7,933	8,015	8,122

Competition in SWBT Serving Area in Texas
Attachment A

Number of Digital Lines

The number of unbundled digital Lines served by CLECs as of the end of January, February, and March 2001 is shown in table below. The effects of recent Data CLEC slowdown are visible in this data.

	Jan'01	Feb'01	Mar'01
ISDN BRI Loop	9,097	9,305	9392
ISDN PRI	2,662	2,514	2657
DS-1 Loop	5,071	5,435	6014
DSL - Stand Alone	24,389	25,481	25,337
DSL - Line Shared	3,693	3,799	3,799
DS-3	655	674	686
Dark Fiber	903	941	797

Number of Physical and Virtual Collocation Arrangements

The number of CLEC collocation arrangements in ILEC central offices or in other ILEC facilities is a significant indicator of the penetration of facilities-based competitors. From January 2000 to January 2001 the number of completed arrangements more than doubled.

	Jan'00	Jan '01
Physical Collocations	1,012	2,333
Virtual Collocations	89	76
Total	1,101	2,409

CLEC Firm Orders Confirmed

The monthly ordering activity for residential and simple business lines increased by 165% in March 2001 compared to December 1999. However, during the first quarter of 2001, the number of orders per month ranged from 179,000 to 188,000. The mechanized ordering activity (EDI, LEX) has increased significantly while the manual ordering activity decreased.

	Dec'99	Jan'01	Feb'01	Mar'01
Res. and Simple Bus				
LEX	6,834	43,459	47,446	44,504
EDI	19,458	118,238	114,031	143,038
Manual	44,634	17,513	17,761	939
Total	70,926	179,210	179,238	188,481

Chairman DEWINE. Good. Thank you, Mr. Wood.
Mr. Hundt.

STATEMENT OF REED E. HUNDT, SENIOR ADVISOR, MCKINSEY AND COMPANY, INC., AND FORMER CHAIRMAN, FEDERAL COMMUNICATIONS COMMISSION

Mr. HUNDT. Thank you very much, Mr. Chairman, Senator Kohl. Thank you very much for inviting me back.

I would like to, if I might, compliment this committee, and these two Senators, for your continuing stewardship and monitoring of the information sector and the development of competition in the sector. I think that the world should know that your attention to developments in this sector is of particular significance because there is now no doubt that this is the most important sector of the American economy. It's not the biggest sector of the American economy, but it is clearly the most important sector of the economy, as the events of the last 5 years have demonstrated.

In the last 5 years, this sector, while accounting for less than an eighth of the total economy, is responsible for one-third of all the economic growth in the economy. It is responsible for more than ten million new jobs in the economy. And most important of all, this sector, and no other sector, is responsible for the record productivity gains that all parts of our economy have enjoyed.

There has probably never been a law passed by not only this Congress but any Congress, or any legislature in any country, that has been so complex as the Telecommunications Act of 1996. I doubt that there's ever been a law that has had such aspirations. There are few, if any, laws that have represented such a radical departure from precedent.

The precedent, as you certainly know, Senators, was to have regulated monopoly in the information sector, and in all dimensions of that sector, whether it was the media or telephony or any part, at the very most to allow carefully controlled oligopoly, and in most cases, a regulated monopoly.

The 1996 Telecom Act is the first law passed by any significantly large country in the world that repealed that entire idea and said, instead, that it was the law of the land that we would promote

competition and investment and innovation. There is so much in this law that any single piece of it can justly be criticized and litigated and debated, but I think it's wise to take a step back and, if you'll permit me, as a former seventh grade school teacher, to attach a grade, if you will.

I think that Congress should give itself an "A" on this law, and here's why. There is no question whatsoever that, in the aggregate, consumers have benefited. Consumers now spend about twice as much as they used to spend of disposable income on communications services, not because they're paying twice as much for the same things but because prices have gone down in so many areas, and there's been such a flourishing of choice and alternative in so many areas, that they're just spending more because that demand was previously constrained by a regulated environment.

No. 2, there has been a fantastic investment boom. The entire business world in the United States purchased in 1995 about $250 billion of communications stuff—equipment, software, services, et cetera. That number doubled in just 4 years, from $250 billion to $500 billion between 1995 and 1999. That is an astounding increase. In fact, all manufacturing output growth in 5 years, all manufacturing output growth in those 5 years, two-thirds was driven by the information sector alone.

The productivity gains that have come out of this sector have doubled all of the caps that economists said were absolutely in concrete and limited expansion possibilities for the American economy. Dr. Greenspan has, in a variety of different ways, somewhat obliquely, repeatedly pressed the same point over and over. None of these productivity gains are going away. They are structural, they are locked into our economy, and we will benefit forever from these productivity gains.

Now, an awful lot of people in this sector are wringing their hands, and an awful lot of people have lost a lot of paper value—and now that I'm in this sector, I could even talk to you about that myself—in the last six to 9 months of stock market downturn. But let me make sure that, in the face of all that negativism, I at least speak out in favor of long-term confidence. Because these assets that have been installed are not disappearing, and as long as we stick with the policies of the 1996 Act—promoting competition and innovation and investment—we will get through this stock market downturn and we will get through the inventory reduction, and we will go on to even greater heights in terms of economic growth and productivity gains. We did the right thing in 1996. We have to stick with it.

Thank you very much.

[The prepared statement of Mr. Hundt follows:]

STATEMENT OF REED E. HUNDT, SENIOR ADVISOR, MCKINSEY & COMPANY, AND FORMER CHAIRMAN, FEDERAL COMMUNICATIONS COMMISSION

Mr. Chairman and Members of the Subcommittee:

Thank you for inviting me to testify today on the state of competition in the telecommunications industry five years after enactment of the Telecommunications Act of 1996 (1996 Act). It is a pleasure to appear before you to address this topic. I want to commend you for holding this hearing to examine our progress toward the goal of the 1996 Act—the goal of a fully competitive, deregulated telecommunications sector. The focus of today's hearing underscores the vital importance of the tele-

communications sector and of competition policy to the overall growth and health of our nation's economy.

My testimony today reflects my personal views and not necessarily the views of any of the companies with which I am affiliated. I currently serve as a member of the boards of directors of Allegiance Telecom, Inc., a facilities-based provider of telecommunications services; Novell, Inc., a manufacturer of computer software; Brience, Inc., a provider of platform software for extending e-business applications to wireless devices; and Gemini Networks, Inc., a new facilities-based provider of highspeed, broadband services to residential customers. I also serve as Chairman of the Board of Sigma Networks, Inc., a broadband telecommunications provider. In addition, I am a Senior Advisor at McKinsey & Company, Inc., an international management consulting firm, and also serve as a consultant to venture capital firms.

I am pleased and honored to appear on this panel with my distinguished colleague, Pat Wood, Chairman of the Public Utility Commission of Texas. When I was Chairman of the Federal Communications Commission I enjoyed and greatly benefited from many discussions of telecommunications policy issues with Chairman Wood. He has been a steadfast advocate of pro-competition policies in the State of Texas. As you know, last year Texas became the second state in which the FCC concluded that the incumbent Bell Operating Company had opened its local markets to competition, in accordance with Section 271 of the Communications Act of 1934, as amended (1934 Act). That decision is testament to Pat's relentless efforts to carry out the mandates of the 1996 Act.

Five years ago, in a dramatic ceremony held at the Library of Congress, President Clinton signed into law the first major overhaul of the nation's communications statute since passage of the 1934 Act. The 1996 Act reflected a sea change in telecommunications policy. Where monopolies were once presumed and protected, the 1996 Act required the FCC, in partnership with the state commissions, to foster the development of competition for all telecommunications services.

THE 1996 ACT: BRINGING COMPETITION TO LOCAL TELECOMMUNICATIONS MARKETS

The dominant themes of the 1996 Act can be described in two words: competition and deregulation. Congress set forth in this landmark legislation an extremely innovative plan for achieving these goals. It gave new competitors in the telecommunications industry the tools they need to enter the market quickly and establish their presence. In addition to eliminating regulatory barriers to such entry, the 1996 Act required the incumbent telephone companies to interconnect their networks with the networks of new entrants. It also required incumbents to provide access to their networks for lease by new entrants.

Congress gave the FCC and the state public utility commissions the critical job of implementing these market-opening provisions of the 1996 Act. The FCC is charged with establishing policies to facilitate new competition as well as deregulating as soon as competition rendered regulation unnecessary.

While I was Chairman of the FCC, I worked with Chairman Wood and many others in state commissions to fulfill the pro-competitive mandate of the 1996 Act. We put in place what I believe were strong and fair policies that, consistent with the FCC's statutory mandate, sought to promote competition in all segments of the telecommunications industry and deregulate as soon as competition permitted.

EXPLOSIVE ECONOMIC GROWTH IN THE LATE 1990S

By embracing competition instead of monopoly, the 1996 Act unleashed unprecedented expansion in the information and telecommunications sectors. In our great nation of innovators and entrepreneurs, a multitude of brilliant technologists and creative businesspersons seized the opportunities created by the new statute. They launched new businesses that brought competition to markets previously dominated by a single firm. With the 1996 Act, we changed our legislative and regulatory policies in an attempt to throw open the doors to competition.

Congress opened markets to new entrepreneurs and innovators. The 1996 Act provided the catalyst that resulted in hundreds of new companies entering the telecommunications industry and the net creation of hundreds of thousands of new jobs. New and existing firms invested tens of billions of dollars in facilities, services, and research and development. These investments in turn resulted in enormous productivity gains for American businesses, increased capacity on our telecommunications networks, the deployment of new technology, and the rollout of advanced communications services. As a result, the United States is the world's clear leader in the Information Economy.

According to a report issued by the Department of Commerce last year, the productivity gains, investment rates, and real wage growth the U.S. experienced in the five years ending in 2000 were all higher than they have been in decades; unemployment and inflation were lower than thought possible; and the expansion set an all-time U.S. endurance record.

Information technologies and the Internet are the driving forces behind this record growth. Consider the following:

- Although Information Technologies ("IT ") industries account for a relatively small share of the economy's total output—about 8 percent—they contributed nearly a third of real U.S. economic growth between 1995 and 1999.
- The prices for IT goods and services have declined at an accelerated rate—from about 1 percent in 1994, to nearly 5 percent in 1995, and an average of 8 percent for the years 1996 to 1998. Declining IT prices have in turn reduced the overall rate of inflation for the years 1994 to 1998, by an average of 0.5 percent a year, or from 2.3 percent to 1.8 percent.
- Between 1994 and 1999, U.S. R&D investment increased at an average annual (inflation adjusted) rate of about 6 percent—up from roughly 0.3 percent during the previous five-year period. The lion's share of this growth—37 percent between 1995 and 1998—occurred in IT industries. In 1998, IT industries invested $44.8 billion in R&D, or nearly one-third of all company-funded R&D.

U.S. Dep't of Commerce, Economics and Statistics Administration, Digital Economy 2000, page vi (June 2000).

The dynamic growth created by the Information Technology industries prompted the Department of Commerce to conclude that the U.S. economy "may well have crossed into a new era of greater economic prosperity and possibility, much as it did after the development and spread of the electric dynamo and the internal combustion engine."

Just as the Information Economy has played such a large part in driving the growth of the broader economy, so have new entrants driven the success of the Information Economy. Fueled by an entrepreneurial spirit and robust capital markets, new entrants invested over $30 billion dollars in new telecommunications infrastructure. This prompted incumbent telecommunications carriers to renew their own infrastructure investment. Investment by incumbent local telephone companies, while flat in the early 1990s, grew by 19 percent between 1995 and 1998.

THE SLOWING ECONOMY AND REDUCED COMPETITION

The economic benefits conferred by the 1996 Act were immediate and substantial. Competition in the telecommunications industry produced extraordinary economic growth. New technologies were developed and deployed, offering a tremendous array of new services to business and residential consumers. The Internet Economy boomed, and many consumers enjoyed more choice, better quality and better prices.

The burst of economic growth has slowed significantly in the past year, however, particularly in the telecommunications sector. The slowing economy, falling stock prices, and credit squeeze have made it difficult for businesses to raise money. The debt markets are providing little capital, and venture capital financing is down. U.S. telecommunications companies that were able to raise an average of $2 billion a month in initial public offerings over the past two years raised only $76 million in IPOs this past March.

This is having a domino effect on the rest of the economy, as demonstrated by one example described in a recent news article:

- Last year, Sycamore Networks Inc. was white-hot, with a soaring stock price and booming sales as telecom players scooped up its cutting-edge communications equipment. But on Apr. 5, CEO Daniel Smith told Wall Street analysts that his largest customer, Williams Communications Group Inc., and other telephone companies were slashing their spending. Smith said the company's sales for the current quarter would be only $50 million to $60 million, about $100 million less than analysts expect. . . . The next day, the company's stock plummeted 20%, to $7.25—a far cry from its 52-week high of $172.50. Worse, Sycamore's troubles will trickle throughout its hometown of Chelmsford, Mass., about 25 miles northwest of Boston. The company will lay off 140 of its 1,100 employees, cut back its spending, and delay construction on a new corporate campus in nearby Tyngsboro. Sycamore is just one example of how the meltdown in the telecom industry is rippling through the economy.

Peter Elstrom, "Telecom Meltdown," Business Week, April 23, 2001.

REINVIGORATE THE TELECOMMUNICATIONS SECTOR BY PROMOTING COMPETITION

Until the recent downturn, the telecommunications sector resembled a runner with boundless energy. It now looks more like a sprinter who has paused to catch his breath. As the economy catches its breath, it is important that we adhere to policies that will fuel competition, innovation and growth in the local telecommunication industry. Much of the credit for the extraordinary economic growth in the telecommunications industry belongs to the scores of innovators and entrepreneurs who took the risks to seize opportunities in the marketplace. But we should also recognize that many of these opportunities would not have been possible nor would they have been apparent to investors without the firm commitment to competition articulated by Congress in the 1996 Act.

At least part of this economic downturn can be traced to the barriers new entrants continue to face in trying to compete in local telephone markets, and the need to have policymakers underscore their belief in pro-competitive principles. Incumbent local telephone companies have little, if any, economic incentive to open their networks to competition. It will take steadfast implementation and enforcement of the 1996 Act's market-opening provisions to overcome the incumbents' economic incentive to resist new entry. If the new entrants lose the foothold that they established during the past several years, we risk losing the competitive dynamic that prompted the extraordinary economic growth and innovation the industry experienced in the late 1990s. Incumbent carriers will face no competitive threat, and we will return to monopoly telecommunications markets, undermining our ability to remain the world leader in broadband communications.

As a recent *New York Times* article observed, the "local phone companies have networks that cannot be duplicated. That is why . . . unfettered deregulation will not lead to more competition. If competition and lower prices are the goal, pro-competition oversight is required to ensure that the companies with essential assets do not use them to stifle others." Seth Schiesel, "Sitting Pretty: How Baby Bells May Conquer the World," *The New York Times*, April 22, 2001.

The most important aspect of these essential assets is the "local loop"—the copper wire that connects the consumer to the local telephone network. New entrants must be able to gain access to this local loop, which is typically owned by the incumbent telephone company. The 1996 Act requires incumbents to give competitors access to the local loop and it will be essential that policymakers enforce that obligation. The FCC must be guided by the 1996 Act's objective of opening up the local telephone market to new entrants. Only in this way can we transform the local telecommunications marketplace from a regime of heavily regulated monopolies to one characterized by competition.

Competition policy will also be a large factor in determining who will benefit from broadband technology. Data networks are revolutionizing the way large businesses operate and we should be proud that our nation has led this "revolution". These networks offer not only the prospect of delivering innovative telecommunications and information services, but also a realistic potential for creating facilities-based alternatives for traditional voice services. But we should not be satisfied if only large enterprises reap the benefits of broadband deployment. Pro-competition policies will encourage all sectors of the industry, incumbents and new entrants, wireless and wireline, to develop and deploy broadband networks to medium and small businesses and residential consumers.

CONCLUSION

If we are to reinvigorate the telecommunications sector and to encourage investment in broadband technology, we need to have a clear commitment to procompetitive policies. Competition policy has had, and will have, an enormous influence on economic growth and innovation. A Princeton University study has found, for example, that countries such as the U.S. and Finland that have government policies fostering free competition in telecommunications have a significantly higher Internet penetration than countries that continue to have monopoly telecommunications services.

E. Hargittai, "Weaving the Western Web: Explaining Differences in Internet Connectivity Among OECD Countries," 23 Telecommunications Policy 701 (1999).

This is why Congress's enactment of the 1996 Act, and the steadfast implementation of the Act's procompetition goals, are so important. Reviving competition is essential to reinvigorating investment and economic expansion in the telecommunications industry. Vibrant competition will advance the promise of the 1996 Act: innovation and deregulation in a telecommunications industry shaped by competitive market forces. With firm pro-competitive policies, the promise of the 1996 Act, the

exceptional economic growth and consumer benefits it has nurtured, and America's leadership in broadband can be sustained.

Alan Greenspan has said "[t]here is . . . little of a truly old economy left. Virtually every part of our economic structure is . . . affected by the newer innovations." Alan Greenspan, Remarks at the 18th Annual Monetary Conference: Monetary Policy in the New Economy (Oct. 19, 2000). The New Economy, as we know, has suffered a downturn in recent months. We need a strong commitment to competition to return it to robust health. An essential element of ensuring strong economic and job growth, technological innovation, and America's leadership in a broadband world will be policies that promote new entry and competitive markets in the telecommunications industry.

Chairman DEWINE. We appreciate, Mr. Wood and Mr. Hundt, your testimony. Let me start off with a question for you, Mr. Hundt.

We often hear that competition in the local telephone market is moving forward and that we simply need to stay the course. At the same time, we hear for calls to step up enforcement of the 1996 Act.

What specific enforcement measures do you believe need to be implemented or adjusted that would improve the competitive environment, if any?

Mr. HUNDT. Well, I'm not prepared to be a critic of any enforcement efforts, you know, that may exist at the present time.

I would just say this. Probably the single most important feature in the communications sector, or the telephony sector, of the Act was the provision that required that the incumbent telephone companies, for the most part, Bells, unbundle the local loop, and do so at forward pricing.

Now, these provisions, the various words around them, have been among the most intensely litigated provisions of any statutes ever passed. The Supreme Court has already granted cert. Here's the litany: two cases out of section 251, one 254, one 252, and one 224. The point is that all these core sections which are about unbundling have repeatedly been the subject of litigation.

In the face of all of that, the most important thing is that all the enforcement powers at the FCC and at the State level stick with one, basic philosophy: enforce it and talk about it all the time, which is that the local loop will be unbundled and will be made available to rivals at forward-looking prices.

There are many debates about methodology. I am certainly eager to stay away from the arcane details of them. But forward pricing is critical to the competitive model, and it is critical that these loops be made available. It is the way that the promise of the Act will be delivered in years to come.

Chairman DEWINE. Mr. Wood, any comment on that?

Mr. WOOD. Enforcement from, again, the front line, we have traditionally taken the promise of 251, which requires, among other things, what Mr. Hundt just mentioned, and a number of other obligations that the companies have to their competitors, incorporating those in a business contract, and then served as the body that people could come to to resolve matters in that business contract if performance was not sufficient under that contract.

So, rather than going into a District court and going on those timetables, people could come to the Commission, again up to that 72 hour and 60 day timeframe, depending if it was customer affecting or not.

Our general philosophy has been to provide the service now, so that competition won't be delayed by a litigation tactic, and we will work on the price as fast as we can, so that customers are not affected.

In a real way, enforcement is—a lot of these issues are about money, how much money are you going to charge. That's no surprise to you all. And it is a fair request of the company to get compensated for what they do. I think as Mr. Hundt pointed out, there is a philosophy, which the State of Texas has also adopted, to use forward-looking costs on pricing these very important parts of the network.

As long as that has a forum, I would venture that probably closer to the problem is better, not necessary because of a State's right argument, which I would probably be glad to make, but just for the convenience of the parties, rather than having to come up here and litigate that before a Commission that has plenty of work to do—not that we don't—come before the State who knows the parties, make the cut, get on with it and go on to the next problem.

So enforcement might need some other aspects that I'm not as familiar with, from what I don't deal with, but when you do an interconnection agreement, those tend to have an enforceability to them that we can handle pretty well.

Chairman DEWINE. A question for Mr. Wood, and also possibly Mr. Hundt.

Consumers have benefited from increased competition in the long distance market and have received lower rates as a result. However, the rate of return in the market has declined at the same time. Some, therefore, have argued that this makes the long distance market less attractive to the Bell companies and, therefore, provides less incentive for them to open their local markets to competition.

Do you agree with that or not?

Mr. WOOD. Well, I can just say that I'm glad we were the second State in line. If I were the 20th or 25th, it may not be as attractive a place. When rates go from 12 cents on the average a minute, as they were in Texas, down to eight cents a minute, competition is—

Chairman DEWINE. What did they go from? What was that again?

Mr. WOOD. From 12ish, on average, down to eight. When Bell entered into long distance, some had single digit long distance rates. That starts to make the gravy a little thinner than it was when you put it on the potatoes, but they still taste good.

[Laughter.]

So, I'm assuming, with other aspects of long distance entry that are availing—data, for example, and others—it is still a pretty tasty plate. But it has changed its flavor.

Chairman DEWINE. A lot of food on the table here, Mr. Hundt. Do you have any comment?

Mr. HUNDT. Well, I'm going to pass up the food metaphors and not get into competition with my colleague on that particular topic.

The return on investment capital has gone down for every player in every sector of the information sector for five straight years. It has gone down in long distance; it has gone down everywhere. That is because of two things: it is because there has been so much more

invested capital put in, and the revenue has not kept pace with that, and No. 2, there is so much competition.

From a policy perspective, actually, it is a good thing to put the pressure on industry and to not have guaranteed returns on investment capital which correlate to regulated monopoly as your paradigm.

Now, what do you expect the people in industry to do under those circumstances? The answer is they need to move into new business models and they will seek consolidation. So I think what we're going to see for sure over the next couple of years is the incumbent local telephone companies confront the necessity of making a strategic decision about vertical integration, about moving into the long haul network.

That is not a bad thing. That is part of the working out of the Act. In Texas, that is the way that Pat approached the issue, and he laid the groundwork for that move. I'm not talking about when. I'm talking about the inevitability of this particular trend.

We now have in the country at least 15 different long haul networks. It was not that way just a few years ago. There is room to have integration here between local and long distance. And it should happen. It should not be the case that government abandon scrutiny and runs away from the issues, but we should expect these issues to be presented.

Chairman DEWINE. Senator Kohl.

Senator KOHL. Thank you very much, Mr. Chairman.

There may be some redundancy in my questions, but I would still like to address them a little bit more fully.

Mr. Hundt, in the past 5 years, since the passage of the Telecom Act of 1996, the purpose of which was to jump-start competition in the telecom industry, we have seen an explosion of communication technologies, from cell phones to Internet, satellite, television, just to name a few. Yet, at the same time, most consumers have seen little, if any, competition in the most basic of all telecommunications services, which is local telephone service.

Last year, the FCC reported that competitive telephone companies had a market share of less than 7 percent of local telephone lines, and while we have all seen sharp declines in long distance and cell phone rates, the average local phone rate has not declined in a decade, since 1990.

So why have consumers not seen more competition for their local telephone service in the 5 years since the Telecom Act? Is there a flaw in the Act that needs to be fixed, or is there anything that we, as policymakers, can do to encourage and see that, in fact, more competition exists in local telephone service?

Mr. HUNDT. Well, if I might, let me first mention some things that consumers definitely need to chalk up as benefits. There is much more competition at last in video coming down from satellites. It is because Congress passed the Satellite Home Viewers Act which has changed the structure of this particular industry in a very positive way.

There is infinitely more competition in wireless. Prices have dropped. There is service available in many more places and the prices per minute are going down.

There is, in fact, tremendous competition in all kinds of equipment that attach to the network, and there is an awful lot of competition in terms of Internet access. We do have some emerging big players. We still have several thousand Internet access providers in the country.

In terms of residential voice telephone service, as Pat knows from Texas in detail, roughly speaking, on a nationwide basis, about 40 percent of all consumers are paying less than the cost of providing the service. Maybe Mr. Ellis at SBC has a different number for his region, and I wouldn't want to debate the specifics. But it is a big number. There is no way that someone else is building an overlapping network to repeat the experience of offering a below-cost service.

What will happen—and I am so confident of this, if we just stick with our competition policies—what will happen in about four to 5 years, actually, very soon in terms of how long it takes to do these massive investments, we will see the cable networks and the telephone networks delivering broadband to more than half the homes in America. And at around that time period, somewhere around 2005, maybe a little later, we will see that routinely, when someone is buying broadband or high-speed access to the Internet, they are getting along with it a voice service that substitutes for today's voice service.

What I'm saying is that that will be the experience of about 40 million homes in the United States by 2005. By the end of the decade, if we stick with your competition policies, it will be the experience of 75 to 80 percent of all homes.

That environment, the broadband competition between cable and telephony networks, that is the environment in which we will see the kind of competition for the residential consumer in what today is called "voice" and then will be a bundled service with data. That's the way that's going to work, I believe.

Senator KOHL. So you're saying, in terms of the local telephone service, it is a huge money-losing business, and that's why there's no competition?

Mr. HUNDT. I'm saying it is for 40 percent, maybe 50 percent of homes. It isn't for the other percentage. But the only real way to have competition, just on the residential side, is to have it be that you have two competing delivery mechanisms or infrastructures—and we have them; one is cable and one is telephony—that are going to be competing with high-speed access to the Internet, and along with that will come voice.

I know that we all are impatient for it. Everyone can tell a story of how they tried to order it. But the reality is that this is happening. Cable has already built, I believe, into more than 70 percent of its homes the capability to do what I'm talking about.

We're talking here about tens of billions of dollars that needed to be invested, and people who were doing it out of their own pocket in the face of good and bad markets, but it really is happening and we really should stick with our policies because they actually are working out.

Senator KOHL. Mr. Wood, do you have a comment?

Mr. WOOD. The only thing is just to give a number reference, Senator Kohl. In Texas, the price for just a residential line—no

Call Waiting, no Caller ID, which a lot of people actually in Texas have those—but if you don't, it's about 17 bucks, taxes included.

For those that want to compete against Southwestern Bell, if they want to buy that underlying line from Southwestern Bell, or even build it themselves, we have calculated—and I think the rates on our end are pretty low, actually -the calculated rate to buy that $17 line is $21. So you can't sell at a four dollar loss and make a lot of money.

I think that's where the rub is. If you get customers who want Caller ID, want the Call Waiting, add some long distance minutes on the network, add a broadband product—DSL, for example, which you would buy from one of the Bell companies or AmeriTech—then you get about that $21 pretty fast. The company can make a return from coverage costs and make future investments.

Quite frankly, we're stuck with our rate design errors of the past. As I admitted to you all, that is really a State problem. But it does explain, I think, why the figures for residential are relatively dismal, and I think they will stay so until the bundled platforms of cable-type products, or I would even add wireless type products to those that Reed mentioned, as well as what the phone company can offer, will be kind of a salvation.

But there are always going to be what we call the "grandmas", who just want to get the basic dial tone and make maybe two long distance calls a month, and that's all they want. They're never going to be profitable people. It has been a public policy in our State, and I believe in yours as well, to keep the rate for those folks low and affordable. We will face that music 1 day, but we're not there yet.

Senator KOHL. OK. Thank you, Mr. Chairman.

Chairman DEWINE. Well, we appreciate your testimony. Mr. Hundt, it's always good to have you. Mr. Wood, we appreciate your testimony very much. You have both been very helpful. Thank you.

Mr. HUNDT. Thank you.

Mr. WOOD. Thank you, Mr. Chairman.

Chairman DEWINE. Let me invite our second panel to come up. I will introduce you as you are coming up.

David Dorman is President of AT&T. His responsibilities include the consumer business and network services groups, international ventures, and AT&T labs. Prior to becoming President of AT&T, he served as chief executive officer of Concert, and President of Spring Business. He was also the chief executive officer of Pacific Bell.

James Robbins is the President and Chief Executive Officer of Cox Communications. Mr. Robbins joined Cox as Vice President of the company's New York operations in 1983. He also has served as the Chairman of the board of the National Cable Television Association. He has testified before our Subcommittee in the past and we welcome him back.

Larissa Herda is the President and Chief Executive Officer of Time Warner. She rose to that position 3 years ago after serving as the company's senior vice president of sales and marketing for a year-and-a-half. She serves on the executive Committee of the Association of Local Telecommunications Services.

James Ellis has been the Senior Executive Vice President and General Counsel of SBC Communications since 1989. His Bell System career extends back some 29 years and has included the position of Southwester Bell's vice president and general counsel and secretary. We look forward to his testimony as well.

Thank you all very much for joining us. I guess we got the nameplates sorted out here and we're rolling.

Again, the same rules apply as to the last panel. We appreciate your testimony. We have written testimony, which we will, without objection, make a part of the record. We would welcome you all here.

Mr. Dorman, please proceed.

STATEMENT OF DAVID DORMAN, PRESIDENT, AMERICAN TELEPHONE & TELEGRAPH

Mr. DORMAN. Thank you, Mr. Chairman, and Senator Kohl, for inviting me here today to share AT&T's views on the state of competition in the telecom industry.

Since 1996, AT&T has been the leader in developing competitive alternatives to the local incumbent monopolies. I know that our time here today is short, so I will just try to make a couple of points.

First, the market opening provisions of the 1996 Act can work. It is now clear that, despite the incumbents' arguments to the contrary, there are no technical impediments to local competitors seeking to deliver service over the incumbent's high-speed facilities. In response to passage of the Act, AT&T and dozens of companies invested tens of billions of dollars in new telecom facilities and services.

AT&T itself has spent $11 billion to purchase Teleport in 1998, and since that time invested another $8 billion in that business to expand it. We spent nearly $90 billion in 1999 and 2000 to buy the cable companies TCI and MediaOne, and earlier this year, we committed more than $130 million to acquire the assets of the now-defunct NorthPoint Communications. We spend billions more each year to upgrade these networks, laying new fiber and interconnecting to local customers. These investments have paid off. Today we serve over two million local customers, and we have local business customers in 71 markets around the country.

Secondly, although the 1996 Act established a sound framework for opening up local telecommunications to competition, the continued viability of local competition is in trouble. The incumbent local exchange carriers have resisted and challenged nearly every attempt to implement the pro-competitive provisions of the Act. Their strategy of resistance, delay, and litigation, and their control over the prices and processes upon which competition depends, has enabled them to maintain their dominance of the local phone market.

Incumbent local exchange carriers have refused to comply with the Act's unbundling obligations, have made interconnection as difficult as possible, and they charge wholesale rates that are in many cases, as has been noted earlier, higher than their own retail rates.

The anticompetitive behavior of the incumbent local telephone companies, magnified by the recent market downturn, has caused the competitive local exchange industry, or CLECs, to virtually col-

lapse. Numerous competitors, including Winstar, NorthPoint, Actel, e-spire and others, have declared bankruptcy or shut down operations altogether.

Each of these decisions has been accompanied by hundreds of eliminated jobs. The CLECs, as a group, dismissed over 6,500 employees last year, attempting to remain in business and viable. For those that continue to struggle in operation, stock prices have plunged and the capital market for emerging competitors has dried up, making it difficult for competitors like AT&T.

The repercussions of these events on consumers is significant. CLECs reinvested most all of their revenues in 2000 in local network facilities. The CLECs declaring bankruptcy in 2000 had planned to spend over $600 million on capital expenditures this year. Those competitive networks will not be available to customers. Further, as CLECs leave the market, incumbents raise their prices and lose incentive to rapidly deploy advanced services.

Third, even though the Bell companies are on the verge of re-monopolizing the telecom industry, they are now calling on Congress for further deregulation. Current legislation in the House would create broad exemptions for the incumbents' unbundling and resale obligations for high-speed data facilities and services. It would deprive competitors of the ability to purchase access to crucial aspects of the incumbents' network in order to gain a foothold in the market and provide advanced services. Indeed, the House bill confers an unbundling exemption so broad that competitors would probably not even be able to lease the facilities that they need to provide basic voice services in competition with the incumbents. Further, it permits incumbents into long distance markets, even though local competition is not emerged.

The incumbents claim that these changes will spur investment and increase rural deployment, but history belies that claim. After having DSL available for years as a technology, the incumbents deployed it only after competitive offerings sprung forth from the cable companies and CLECs. And their arguments that new legislation will give them an incentive to bring high-speed access to rural areas ring hollow when you consider the fact that the Bells have already divested 10 million rural access lines.

Finally, Congress must reaffirm its commitment to the market opening provisions it created in the 1996 Act if the local competition created by AT&T and others is to survive. Congress must resist efforts by the Bell companies to weaken the commitment through unwarranted legislation that would relieve the incumbents of the very obligations in which local competition depends.

Congress must demonstrate its renewed commitment to the principles of the Act by sending a clear signal that the goals of the Act can only be realized through vigorous enforcement of the provisions designed to end this century of monopoly control over the local telecom market.

Five years ago, this Subcommittee and Congress concluded that more, not less, competition would best protect consumers and spur broadband deployment. We ask that you today reaffirm that commitment by considering ways to make the Act more, not less, effective.

We remain optimistic, that with the assurance of strict adherence to the requirements of the Act, that the promise of the Act will become a reality.

Thank you, again, for the chance to represent AT&T's views.

[The prepared statement of Mr. Dorman follows:]

STATEMENT OF DAVID DORMAN, PRESIDENT, AMERICAN TELEPHONE & TELEGRAPH

Thank you, Mr. Chairman and members of the Subcommittee, for inviting me here today to share AT&T's views on the state of competition in the telecommunications industry. Since 1996, AT&T has been a leader in developing competitive alternatives to the incumbent telephone monopolies. We have invested tens of billions of dollars in local telecommunications and cable networks and now serve over 2 million local customers. Unfortunately, our efforts and the efforts of other local competitors have been resisted at every turn by the incumbents. And now the incumbents seek changes in the law that would repeal the rules that are essential to local competition and remove the incentives put in the statute to encourage them to open their local markets. If enacted, such changes would exacerbate the current financial crunch and extinguish the prospects for competition that seemed so bright only five years ago.

My message today is straightforward: Congress must reaffirm its commitment to the market-opening provisions it created in the 1996 Act if the local competition created by AT&T and others is to survive. Congress must resist efforts by the Bell companies to weaken that commitment through unwarranted legislation that would relieve the incumbents of the very obligations on which local competition depends. And Congress must demonstrate its renewed commitment to the principles of the Act by sending a clear signal that the goals of the Act can only be realized through vigorous enforcement of the provisions designed to end almost a century of monopoly control over the local telecommunications market.

The Telecom Act promised to spread the benefits of competition across all segments of the communications industry. To keep that promise, Congress made a simple deal with the Bell companies: Open your monopolies to competition - real competition - and then you'll be allowed into long distance. The incumbents were not given a choice. Congress said in no uncertain terms that monopolies must be opened. And that regulators should make sure that it happened, and that it happened quickly.

The 1996 Act provided three pathways to local competition: A competitive local exchange carrier ("CLEC ") could purchase local telephone services at wholesale rates from the incumbent and resell them to local customers; a CLEC could lease specific pieces of the incumbent's network on an unbundled basis, using what the industry calls unbundled network elements ("UNEs "); or a CLEC could build its own facilities and interconnect them with the incumbent's network. In return for opening their markets to competition, the Bell companies would be allowed into the long distance market. This Subcommittee played an instrumental role in crafting the procedure by which the Department of Justice, the State commissions, and the FCC review a Bell company's application for long distance entry.

Just the promise of competition spurred billions of dollars of investment in new telecommunications networks. Competitive local companies sprang up to compete with the Bells. Long-distance companies began making plans to offer local service in every state. AT&T and many others eagerly commenced efforts to offer local telecommunications services.

We are discouraged to report, however, that the 1996 Act has not functioned as Congress intended. The flaws are not in the Act; they are in the implementation of the Act. For five years, the Telecom Act has bounced from legislation to regulation to litigation. Although subscribers have responded positively to the competitive service offerings of AT&T and others, and although it is now clear that there are no technical impediments to local competitors seeking to deliver service over the incumbents' facilities, the Bell companies are on the verge of remonopolizing the telecommunications industry. Due primarily to the anticompetitive behavior of the incumbent telephone companies themselves—and magnified by the recent market downturn—the CLEC industry has virtually collapsed. To finish off the job, the incumbents are now calling on Congress for massive deregulation that would exempt most of their network facilities from the market-opening requirements of the 1996 Act and permit them into the long distance market even though local competition has not yet emerged.

The incumbents' requests for government-sanctioned remonopolization would be a defeat for the procompetitive impulse that led to the enactment of the 1996 Act.

Five years ago, this Subcommittee and Congress concluded that more, not less, competition would best protect consumers and spur broadband deployment. We ask you today to reaffirm that commitment by considering ways to make the 1996 Act more, not less, effective.

I will address each of these concerns in turn.

AT&T is Committed to Local Competition

Soon after the enactment of the 1996 Act, AT&T realized that it could not rely solely on the incumbents for the network facilities it needed to offer local service. After all, we are the competition and the incumbents have little reason to cooperate in giving us access to their networks in a timely and reasonable fashion. We realized we could not be solely dependent on our rivals for essential facilities. As a result, we began to acquire our own local networks. In 1998 we purchased Teleport for $11 billion to serve business customers. Then, in 1999 and 2000, we spent nearly $90 billion to buy the cable companies TO and MediaOne so that we would have a line into the homes of residential customers. We spend billions more each year to upgrade those networks, lay fiber, and create data centers. These investments have paid off: we've gone from about 50,000 cable-telephone customers a year ago to nearly 600,000 today, and AT&T has local business customers in 71 major markets around the country.

But our own local networks do not reach everywhere. Until recently, for instance, FCC rules limited us to serving only about one-third of all cable subscribers. The incumbents are under no such restriction, as the reduction in the number of Bell companies from 7 to 4 in the last few years dramatically illustrates. To bring competitive choices to more Americans, we must rely on the market-opening requirements of the 1996 Act to lease facilities from the incumbents and resell their services. Even in the fact of grudging and spotty compliance with these requirements, the results have been dramatic: nearly 2 million local residential customers in 18 states have chosen AT&T as their service provider.

Earlier this year, AT&T committed more than $130 million to acquire the assets of the now-defunct NorthPoint Communications. The assets include collocations in 1920 locations, 3000 DSLAMs and other DSL networking equipment, 153 ATM switches, and the associated systems (hardware and software) that support provisioning, engineering, testing and maintenance functions. However, without access to the incumbents' facilities, as contemplated by the 1996 Act, AT&T's ability to put these assets to use for consumers will be substantially diminished. As I explain below, the incumbents' unceasing efforts to undermine the Act have impeded the availability of competitive alternatives for American consumers.

Anticompetitive Behavior By the Incumbents Has Hindered the Development of Local Competition

Back in 1996 the Bell companies pledged to support the Telecom Act. Then they went to court to stop it. They challenged Congress' authority to pass it, the FCC's authority to implement it, and just about every meaningful interpretation of it by the states. The 1996 Act established a sound framework for opening up the local telecommunications marketplace to competition, but the incumbent local exchange carriers have resisted and challenged nearly every attempt to implement the pro-competitive provisions of the Act. Their strategy of resistance, delay, and litigation, and their control over the prices and processes upon which competition depends, has enabled them to maintain their dominance of the local telephone market, while dozens of their competitors are forced to scale back service plans, and many others go out of business entirely.

Incumbents Eliminate Competitors By Refusing to Comply with Unbundling Obligations.

Competitive local exchange carriers seeking to lease elements of the incumbents' networks to provide competitive service have been frustrated by the incumbents' insistence that their obligation to provide UNEs is limited to the most basic services. They will supply competitors with the elements necessary to provide voice services (at inflated prices designed to eliminate competitors), but will not supply the elements used to provide the advanced data services that are the economic heart of today's telecommunications industry. Competitors also find that incumbents mishandle or delay their service requests. Last year, Verizon admitted to mishandling *more than a quarter of a million* competitive requests. And an FCC report for Penn-

sylvania shows that while Verizon always fills orders for its own customers in under five days, 80% of competitive customers must wait longer than five days.

Where regulators adopt policies to promote competition, the incumbents respond by withdrawing new services rather than complying. That happened recently in Illinois, where SBC announced it would halt its digital subscriber line deployment program rather than comply with an Illinois Commerce Commission order allowing competitors access to its fiber optic technology at costbased rates. There is no better indication of SBC's monopoly power than a unilateral decision to cease providing service. As Illinois Commerce Commissioner Terry Harvill aptly observed in a letter to Speaker Hastert, "if the market were competitive, SBC/Ameritech would not be able to unilaterally halt the deployment of DSL infrastructure and deny these [Illinois] customers advanced telephony services."

AT&T agrees with Commissioner Harvill that "[w]ithout competitive guidelines like those [SBC] objects to, it is unlikely that millions of customers in Illinois will ever see the intended benefits of the Act in the form of lower prices, many choices for broadband services, and better customer service." And if this happened in Illinois, it could happen in Ohio, Wisconsin, or any other state served by SBC.

INCUMBENTS THWART COMPETITION BY MAKING INTERCONNECTION DIFFICULT.

Although CLECs are entitled to obtain dedicated space in an incumbent's central office or at other of their locations (such as remote terminals) and to place equipment there to interconnect with the incumbent's network, the incumbents have taken every possible step to deny CLECs this right, including challenging the FCC's rules implementing these requirements in court. In the meantime, the incumbents have attempted to restrict the type of equipment and facilities that CLECs may collocate at their central offices, and they are refusing to permit CLECs collocated in the same central office to connect to one another.

INCUMBENTS' WHOLESALE RATES WOULD ELIMINATE COMPETITION.

Although competitors seeking to enter the market by reselling the incumbent's service are entitled to buy that service at the wholesale rate, incumbents have virtually eliminated resale as an option for new competitors by offering wholesale rates for local network capacity that are too high for competitors to make a profit on the resold service. In some cases, the wholesale rates offered to potential competitors exceed retail rates. In New Jersey, for example, the average retail rate is $8.19 per month, while the wholesale rate offered to competitors is $25 per month. After paying the "wholesale" rate, there is no margin between the cost of service and what competitors can charge for its services, including retail local exchange and exchange access services.

As a result of litigation brought by the incumbent monopolists, the FCC lost its wholesale pricing authority for local telephone services. Although the Supreme Court eventually restored this authority in 1999, the FCC now appears unwilling to override state commissions that have permitted the incumbents to charge anticompetitive rates.

In the face of these types of behavior, many competitors have been forced to stop offering local telephone service. AT&T has warned that because it is losing money on local telephone customers, it may have to stop offering service in New York and Texas. Sprint has left both those markets, and the Georgia and California markets as well. And where competitors leave the market, price increases follow. In Texas, SBC has announced a ten to thirty percent price increase for long distance service.

The same is true for advanced services, where the incumbent carriers now control approximately 90 percent of all residential DSL lines. Analysts at Legg Mason have noted that "with numerous DSL providers exiting the playing field . . . DSL pricing appears to be on the rise." SBC, for example, raised its residential DSL rates in February by about 25 percent and Earthlink followed suit.

FACING RESISTANCE BY INCUMBENTS, LOCAL COMPETITORS WILL NOT SURVIVE THE DOWNTURN IN THE FINANCIAL MARKET

The recent downturn in the financial markets has further punished competitors who faced incumbent-imposed technical, legal and procedural hurdles to getting the access to services and facilities mandated by the 1996 Act. Numerous competitors, including Winstar, Actel, e.spire, Picus, Jato, OpTel and many others, have declared bankruptcy or shut down operations. Even NorthPoint, which was widely considered the type of major competitive player created by the Act, is now defunct.

For those that continue to struggle in operation, stock prices have plunged, and the capital market has virtually dried up. While telecommunications companies cap-

tured an average of two billion dollars per month in initial public offerings over the last two years, they raised only $76 million in IPOs in March, leading numerous companies to withdraw their IPO plans.[1]

The difficulty in entering local markets has also caused nearly all competitors to scale back their plans to offer service. Covad, originally another success story, is closing down over 250 central offices, and will suspend applications for 500 more facilities. Rhythms has cancelled plans to expand nationwide. Net2000 has put its plans for expansion on hold. Numerous other competitors, such as DSL.net, have resolved to focus on a few core markets. Each of these decisions has been accompanied by hundreds of eliminated jobs. CLECs dismissed over 6500 employees in the last year, attempting to remain in business.

The repercussions of these events on consumers is significant. CLECs reinvested most of their 2000 revenues in local network facilities. CLECs declaring bankruptcy in 2000 had planned to spend over $600 million on capital expenditures in 2001. Those competitive networks will not be available to consumers. Further, as CLECs leave the market, the incumbents raise their prices, and lose incentive to deploy advanced services. Indeed, we could well return to the environment that existed before the 1996 Act, when the Bells kept DSL technology on the shelf, feeling no pressure to deploy it in the marketplace.

REGULATORY RELIEF FOR THE INCUMBENT MONOPOLISTS IS UNWARRANTED

In 1996, there were eight major providers of local phone service. Those eight have become four today, thanks to a series of mega-billion dollar mergers. All four are still monopolies. The only difference is that today they are much bigger monopolies. And they aren't eager to compete against each other. Verizon made a loud media splash last year when they said they would compete against other Bells for local service in nine states. They were a lot quieter just before the New Year when they said they were pulling out of all nine of those states.

Despite the remonopolization of the industry, incumbent telephone companies are now seeking changes in the law that would weaken regulatory oversight and make it even harder for new entrants to compete. Current legislation in the House would create broad exemptions from the incumbents' unbundling and resale obligations for high speed data facilities and services. It would deprive competitors of the ability to purchase access to crucial aspects of the incumbents' networks in order to gain a foothold in the market and provide advanced services. Indeed, the House bill confers an unbundling exemption so broad that competitors would probably not even be able to lease the facilities they need to provide basic voice service in competition with the incumbents. It would effectively close off one of the three competitive pathways forged by Congress in 1996.

The Bell companies also seek the ability to provide high speed data services across LATA boundaries without meeting the pro-competitive requirements of the 1996 Act. As this Subcommittee is well aware, in order to foster local competition, the 1996 Act permits a Bell company to gain in-region interLATA authority only after it has opened its local market to competition. This incentive-based approach takes full advantage of the long distance restriction to provide the Bell companies with a reason to open their local markets for the benefit of all consumers. And the ability to provide high speed data services across LATA boundaries is a powerful incentive: currently, the majority of traffic traveling over long haul networks is data traffic, not voice, and analysts predict that data traffic will make up 90 percent of all traffic within four years. The pending proposal is a fundamental abandonment of the incentive-based approach embodied in the 1996 Act.

The incumbents claim that these changes will spur investment and increase rural deployment, but history belies this claim. After sitting on DSL technology for years, the incumbents finally deployed it only in response to competitive offerings of CLECs and cable companies (specifically, AT&T). Under this competitive spur, they have made substantial investments in broadband. Verizon, for instance, will spend $18 billion this year on capital investment.[2] SBC is spending more than $6 billion on its heavily-promoted "Project Pronto,"[3] and Qwest will spend $9.5 billion this year to build out its facilities.[4] BellSouth "invested over $33 billion . . . during the 1990's," and expects "total DSL revenue of approximately $225 million this year and

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[1] Telecom Meltdown, Business Week (April 23, 2001).

[2] *Id.*

[3] SBC Investor Briefing, *SBC Announces Sweeping Broadband Initiative*, at 2 (Oct. 18, 1999).

[4] "Running on Empty; Industry Trend or Event," *Communications Week International* (Mar. 5, 2001).

$500 million in 2002."[5] Tellingly, the BellSouth chief executive acknowledges that the regulatory challenges BellSouth is facing "are unlikely to slow down the momentum of the marketplace."[6] What is clear is that this investment will slow dramatically without the competitive spur that the 1996 Act makes possible.

Further, these investments are producing significant revenue for the incumbents. SBC has boasted to investors that "[t]he network efficiency improvements alone pay for this [Project Pronto] initiative, leaving SBC with a data network that will be second to none."[7] Beyond those savings, of course, SBC and the other incumbents will earn substantial revenues from the new services made possible by the deployment of advanced facilities. And when SBC makes advanced facilities available to competitors as unbundled network elements, they earn yet another revenue stream from competitors who must pay the costs of these elements plus a profit.

There also is no assurance that the incumbents would use regulatory relief to deploy broadband facilities any faster or to historically underserved areas like rural communities or inner cities. Their arguments that new legislation will give them the incentive to bring highspeed access to rural areas ring hollow when you consider the fact that the Bells have already divested 10 million rural lines, and there is little evidence that the incumbent monopolists have used the last five years to extend broadband to unserved communities.

To accede to the incumbents' requests for relaxed regulation would be a retreat from the competitive goals of the 1996 Act. Although they argue that such an approach would stimulate a renewed commitment on their part to deploy advanced services, this approach already has been tried and failed. There is no justification for allowing the incumbents to evade their unbundling responsibilities, or creating a loophole in section 271's balance of incentives designed with this Subcommittee's participation to protect the public interest.

The CLEC industry is at a critical juncture. If we don't succeed now, it will be a long time before others are willing to invest the billions of dollars needed to try again. If local competition is to succeed, Congress should send a clear signal of its renewed commitment, both by rejecting the incumbents' self-serving requests for deregulation, and by encouraging vigorous enforcement of the pro-competitive provisions of the Act.

Senators Hollings, Inouye, Stevens and Burns recently emphasized in a letter to FCC Chairman Michael Powell that there is a tremendous need for "strict adherence and strong enforcement of [the 1996 Act's] market opening requirements," and that "[m]eaningful exercise of [section 271] authority is needed in light of the current precarious state of the competitive carriers, which is due largely to their inability to obtain affordable, timely, and consistent access to the Bell networks." AT&T agrees with the Senators that what is needed today is not a rewrite or even abandonment of the principles embodied in the 1996 Act, but rather a rededication to those principles in the form of vigorous oversight and enforcement. We remain optimistic that with the assurance of "strict adherence" to its requirements, the promise of the 1996 Act can become reality.

Thank you again for the chance to present our views.

Chairman DEWINE. Mr. Dorman, thank you very much.

Mr. Robbins.

STATEMENT OF JAMES ROBBINS, PRESIDENT AND CHIEF EXECUTIVE OFFICER, COX COMMUNICATIONS

Mr. ROBBINS. Mr. Chairman and Senator Kohl, thank you for the pen, incidentally, and congratulations on your ball team last night.

Senator KOHL. Thank you.

Mr. ROBBINS. I'm here to tell a straightforward story and make one simple promise. Cox is committed absolutely to the provision of competition in the local telephone exchange marketplace. This has been and will continue to be a highly capital-intensive and extremely complex undertaking.

Going up against the entrenched incumbent local exchange carriers is decided not for the faint of heart. But Cox is succeeding and

[5] Duane Ackerman, *Talk Notes*, Salomon Smith Barney Conference (Jan. 9, 2001) at 7, 15.
[6] *Id.* at 11
[7] *Id.* at 2.

Cox is in it to stay. In the process, Cox will have spent about $10 billion on such necessities as network improvements, incremental equipment, infrastructure hardening, call centers and billing and collection systems. This year alone, we will spend about $2 billion. In addition, we have had to employ and train the people to operate this network with the reliability and quality of service that is the best in the business.

How are we doing? I will let our performance to date speak for itself. By the end of this year, Cox will be able to provide residential telephone service to 75 percent of our customers in eight initially targeted market clusters. These markets comprise nearly half of our 6.2 million customers. As of the end of March, we had 300,000 residential customers and 410,000 residential access lines. We handle about 1.2 million telephone calls each day. Cox Telephone is growing at an annual rate of 118 percent, and is adding 4,000 new residential customers per week. We already have deployed 20,000 route miles of bundled fiber, ten telephone network switches, and back-up power supplies.

The service that Cox is providing is a lifeline telephone service. We are making payments to the Universal Service Fund on all of our telephone revenues. In California, for example, we have been certified as a carrier of last resort. By 2004, almost 70 percent of our customer base will have access to Cox local telephone service.

On the business side, we now have 1,250,000 voice grade equivalent lines in service. Of our three new digital services, video, high-speed data, and telephony, our new telephone offering is by far the most challenging and time-consuming to deploy, market and operate. But we are inexorably moving forward.

Mr. Chairman, the next question then becomes, what do Cox customers think about our telephone service. They love everything about it. First and foremost, they love the price, 10 percent less than the incumbent local exchange carrier service for the first line, and about 50 percent off for the second line in most markets. Enhanced services are up to 30 percent less expensive.

Moreover, Cox customers like our state-of-the-art technology, our quality customer service, and the reliability of our network. In fact, 7 percent of our telephone customers take only telephone service from us, but the vast majority of our telephone customers also take data and/or our video product.

I should take a moment to comment about the future promise of Internet protocol cable telephone, or IP telephone. Next year, we will begin to test this new technology. There are questions to settle about scalability empowering of IP networks, but Cox is confident that IP telephony will add great value for our customers, particularly in smaller systems where circuit switch systems are not as economic to deploy. We envision circuit-switched and IP services will coexist in all of our networks.

The final question then, Mr. Chairman, is what should be the government's role in fostering the speedier deployment and development of local exchange competition. I have five suggestions:

No. 1, encourage regulatory certainty in the marketplace by allowing the 1996 Act to work.

No. 2, shift the FCC's focus away from CLEC resale and UNE-P models, which are failing in the marketplace, toward facilities-based competition which is succeeding.

Three, dramatically increase penalties for repeated ILEC litigiousness, which is setting an all-time record.

Four, provide facilities-based competitors with special fast-track enforcement and much more aggressive economic sanctions against entrenched ILEC anticompetitive behavior.

Finally, No. 5, prohibit abuses of pole attachment, rights-of-way and franchise requirements and local tax gouging.

Mr. Chairman, the prospect for local telephone exchange competition is in its infancy. Entrenched incumbents, as you have heard, still control 97 percent of the residential marketplace. But if Cox is any example, the cable industry is poised to ensure that robust facilities-based competition will become a reality. Consumer choice will usher in a new era of better service, lower prices, and technological innovation.

[The prepared statement of Mr. Robbins follows:]

STATEMENT OF JAMES O. ROBBINS, CEO, COX COMMUNICATIONS, INC.

Cox Communications, Inc. ("Cox") is the country's fifth largest cable MSO, providing basic cable services to roughly 6.2 million regionally-concentrated and highlyclustered customers.[1] Since the passage of the Telecommunications Act of 1996 ("1996 Act"), Cox has transformed itself from a distributor of traditional, one-way video programming services to a provider of multiple, two-way advanced digital offerings. This metamorphosis has been costly, difficult and time-consuming. It also has been embraced fully by Cox's cable customers, who signaled their approval by purchasing more than 1.2 million new services from Cox last year.[2]

In the past two years, Cox spent $10 billion acquiring more cable systems to ensure that it has sufficient scale and scope to enter the broadband marketplace. Through these acquisitions, Cox increased its customer base from approximately 4 to 6.2 million. Cox also is spending an additional $10 billion to upgrade its cable networks to support new broadband services.[3] This massive capital investment is already well underway. At the end of last year, roughly 73 percent of Cox's cable plant in its 15 largest cluster markets had two-way capability and 70 percent had 750 MHz (or greater) capacity. By the end of this year, Cox will have completed similar upgrades for more than 80 percent of all of its cable systems nationwide.

Over the past several years, Cox has deployed three new broadband services over its upgraded cable platform. The first of these is a digital television service, branded Cox Digital TV, that enables Cox to compete more effectively against the high-channel, highquality video programming services offered by DBS providers DirecTV and Echostar and, in some cases, the incumbent telephone company. The second offering is highspeed Internet access, offered by Cox under the brand names *Cox@Home*, Cox Road Runner and Cox Express. These services provide customers high-speed access to the Internet via cable modems and a network designed to maximize cable technology. They also offer customers their own unique national and local broadband content, as well as access to broadband content offered by third parties.

The third new service is local telephony, branded Cox Digital Telephone, that already has proven to be a formidable competitor to services offered by incumbent local exchange carriers ("ILECs"). Indeed, as of March 31, 2001, Cox was providing local telephone services to 300,000 residential customers using 410,000 residential access lines. By Cox's rough estimate, these customer figures put Cox on par with the 12th largest telephone company in the country. And, Cox is continuing to roll out new telephone services to its customers. Its residential telephone service is growing at a rate of 118 percent annually, and it is now adding 4,000 new residential telephony customers each week. By the end of this year, Cox will be able to pro-

[1] More than 70 percent of Cox's customers are located in 15 markets that serve an average of 285,000 customers apiece. Cox's three largest markets are Phoenix (serving 610,000 customers), San Diego (serving 509,000 customers) and New England (serving 430,000 customers).

[2] Cox expects to add about 1 million new service customers in 2001.

[3] This $20-plus billion investment in broadband is a substantial commitment for a company with annual revenues of $3 billion.

vide residential phone service to 75 percent of its customers in eight markets - markets that serve nearly half of its 6.2 million customers. By 2004, Cox estimates that perhaps as much as 70 percent of its customer base will have access to competitive residential telephone service.

The capital expenditures required to deploy digital telephone service over Cox's upgraded cable systems are significant. Cox has installed 10 telephone switches in its largest markets that are routing 1.2 million phone calls each day. Assuming a telephony penetration rate of 25 percent of homes passed and an average take-rate of 1.5 lines per customer, the switching cost per customer is $105 alone. Cox must then spend an additional $505/customer for the Network Interface Unit (NIU), the drop, the tap and the Headend Interface Terminal (HIT). This combined variable cost of $610/customer for the provision of local telephony is in addition to the $220/home passed that Cox must invest to upgrade its cable plant to 750 MHz capacity and introduce two-way interactivity. It also does not include the $100/customer that Cox is investing to power its cable networks to ensure that telephone service continues in the event of a power failure. By deploying back-up power throughout the network and utilizing a unique "ring-inring" architecture, Cox is able to offer its customers a highly-reliable, lifeline telephone service. Indeed, the reliability of Cox's cable systems exceeds the Bellcore standards adopted for local telephone networks. Cox also has been designated a carrier of last resort in the state of California, and receives universal service subsidies for its provision of telephone service to high-cost and low-income customers.

Cox first rolled out local telephone service to residential customers in its Orange County, California system in 1997, nearly four years ago. Customer response to Cox's local phone service since that time has exceeded expectations. Overall, roughly 10 percent of Cox customers able to purchase Cox Digital Telephone have done so. In some neighborhoods, penetration rates exceed 30 percent. A key aspect of Cox's value proposition for its residential telephone service is price. Cox Digital Telephone is roughly 10 percent cheaper than the ILEC's offering for the first telephone line and 50 percent cheaper for the second. (Not surprisingly, about one third of Cox's telephone customers purchase a second line.) Enhanced features such as call forwarding and call waiting are up to 30 percent less expensive than the prices charged by the incumbent. Cox also resells long distance service, branded Cox Long Distance, which is purchased by roughly 75 percent of its local phone customers.

Cox does not require its telephone customers to buy other Cox services (such as cable service or high-speed Internet access), and approximately 7 percent choose to purchase Cox telephone service alone. Many more phone customers, however, do buy cable and/or Internet access from Cox, and enjoy additional savings in the form of bundling discounts. Cox also is testing a flexible bill program, which will give customers the option of receiving a single bill or multiple bills for the Cox services they purchase. Market research suggests that while some consumers want the convenience of receiving a single bill, others prefer to receive one, two or three separate bills. Cox's new billing options will be responsive to all of its customers' desires.

Cox's provision of local telephone service over its cable networks has had an unforeseen benefit beyond simply providing the company with another revenue stream. Customers with the most favorable impression of Cox are those that purchase phone service as well as cable service. By considerable margins over cable-only customers, Cox cable/phone customers believe that Cox "uses state-of-the-art technology," "provides reliable service with few interruptions," and "provides quality customer service." The purchase of Cox Digital Telephone also improves customer retention. Indeed, Cox's research shows that customers who purchase two or more Cox services are noticeably more likely to remain Cox customers than those who buy only a single Cox service.

While Cox is rapidly expanding its telephone service to residential customers, it also has made a substantial investment in facilities designed to serve business customers ranging in size from small retail shops to large corporations. Cox has served business customers from the time it began to offer telecommunications services and it expects that the business sector will continue to be an important source of its growth in the future. Its business services are now providing more than 1.2 million voice grade equivalent circuits nationwide.

Cox's local telephone services are provided entirely over Cox's upgraded cable networks; with rare exception, Cox does not purchase unbundled network elements (UN-Es) from the incumbent telephone company or otherwise resell ILEC services. In addition to being fully facilities-based, Cox also is offering circuit-switched, not Internet Protocol (IP), telephony. Cox intends to begin testing IP technology next year, and is aware that there are significant questions of scalability and powering that will need to be resolved before IP telephony can be marketed on a mass scale. Nonetheless, Cox is confident that IP telephony will add great value for its cus-

tomers, particularly those served by its smaller systems for which it can be economically difficult to deploy a switch. Cox believes that, ultimately, circuit-switched and IP telephone services will coexist in all of its cable networks.

Although Cox has enjoyed considerable success rolling out local telephone services over its cable infrastructure, its telephony deployment has been fraught with challenges. In addition to mastering a new technology and overcoming significant operational hurdles, Cox has had to navigate treacherous waters roiled by ILEC misbehavior and regulatory miscues. For example, as a facilities-based competitor, one would expect that Cox would be able to reach interconnection agreements with the ILECs without much controversy since the principle issue to be negotiated is how the parties will interconnect to exchange traffic. Yet Cox has had to submit virtually all of its interconnection agreements to state public service commissions for arbitration due to ILEC intransigence. In addition, Cox has been forced to deal with a variety of anticompetitive tactics undertaken by its ILEC competitors. Cut-over schedules have not been met. Timely provisioning of trunks has been a problem, resulting in busy signals for Cox customers. Ported numbers have not been properly loaded by ILECs into their switches, making it impossible for Cox customers to receive incoming telephone calls. Some ILECs have declined to pay reciprocal compensation (and not simply for ISPbound traffic) or have challenged Cox's exchange access rates. Cox has had great difficulty getting ILECs to comply with state regulations that guarantee its access to multiple dwelling units (MDUs). These are but a few of the systematic roadblocks thrown up by entrenched ILECs to thwart Cox's competitive entry into the local phone market.

Cox also has faced problems on the regulatory front. In particular, Cox has had difficulty persuading regulators of the importance of promoting facilities-based competition over the less viable resale and UNE competitive entry strategies envisioned by the 1996 Act. The stark reality is that it is difficult to implement a business model that relies heavily on purchasing essential inputs from your fiercest competitor, who also happens to be a long-standing monopolist. A far more reliable approach is to make capital investments in your own infrastructure and decrease reliance on the ILECs as much as possible.

Moreover, as the Federal Communications Commission has recognized, facilitiesbased competition creates more consumer benefits than any other form of competition. Facilities-based providers can compete more effectively with incumbents, provide more reliable service and, because they control the entire transmission path, can offer more innovative and advanced services than non-facilities-based providers. Unfortunately, regulatory initiatives aimed at encouraging the deployment of new telecommunications infrastructure often take a back seat to activities aimed at promoting resale and the lease of UNEs - despite the fact that it is far less timeconsuming to promote facilities-based competition than it is to sort through the myriad complexities of implementing OSS and UNE-P.

A perfect example of regulators working at cross-purposes with the development of facilitiesbased competition is the challenges Cox faces when seeking to place back-up power supply cabinets in local rights-of-way. As mentioned previously, Cox must install remote power supplies (known as "Network Reliability Units" or "NRUs") throughout its upgraded cable systems in order to ensure the network reliability that its advanced services customers demand. In particular, consumers will not switch their residential telephone service from the ILEC to Cox unless they are assured that their telephone service will work in the event of a power outage. Unlike the ILECs' copper plant, electricity cannot be sent over fiber, which has been extended deep into Cox's hybrid fiber-coax cable networks. Cox accordingly has been installing state-of-the-art remote NRUs as part of its network upgrades to ensure the reliability of its advanced services. These units contain batteries, and are often coupled with gas generators that can provide immediate and unlimited back-up capacity should the supply of commercial power be interrupted.

As an authorized rights-of-way user, Cox works closely with its local franchising authorities before installing NRUs in public streets. Often, communities have initial questions about the safety, noise and aesthetics of the NRUs to be installed by Cox. In most cases, Cox is able to satisfactorily address these concerns in a reasonable timeframe through the normal permitting process. In some communities, however, Cox has encountered considerable resistance to the placement of its critical powering equipment in public rights-of-way. A few communities, for example, have enacted discriminatory cable-only ordinances that effectively preclude Cox from installing units—even though these same communities continue to promptly process permits for similar cabinets submitted by other rights-of-way users (such as ILECs). Other communities have set up community "review" procedures that are so onerous that Cox has been unable to install a single cabinet in over three years. Still others have adopted arbitrary size limitations, raised unsubstantiated safety "problems" or

simply refused to act on pending permit requests. In each of these situations, Cox has been forced to delay—sometimes by a number of years—its provision of local telephone service to community residents.

Cox has experienced similar difficulties securing local permission to deploy residential telephone service over its upgraded cable systems. Although Cox already has permission through its cable franchises to use public rights-of-way, and although the provision of local phone services over its cable networks generally does not impose any additional burden on public streets, a number of local governments have asked Cox to secure a separate "telecommunications franchise," and to pay a separate telecommunications "franchise fee," before rolling out local telephone service. All too often, the onerous requirements included in such telecommunications franchises, and the significant fees that accompany them, are imposed only on CLECs, and not on ILECs. These obstacles increase Cox's cost of doing business and, again, serve only to delay its provision of competitive local telephone service.

Cox believes that there are five constructive steps that policymakers could take to help speed the deployment of local telephone service by facilities-based CLECs such as Cox and other cable telephony service providers:

1. *Encourage regulatory certainty in the marketplace by allowing the 1996 Act to work*. Constructing telecommunications networks and deploying competitive local telephone service is a daunting undertaking, even for a company as well-positioned as Cox. New networks and services simply will not be deployed if the regulatory regime is destabilized. Facilities based CLECs depend on the capital markets to survive. They cannot do so if regulators inject uncertainty into an already precarious environment. The Congress accordingly should resist urgings to re-visit the delicate balance achieved in the 1996 Act. While not perfect, the Act is working to introduce competitive local exchange service into the marketplace.

2. *Shift the FCC's focus away from CLEC resale and UNE models and toward facilities-based competition*. It would be impossible to count the endless hours devoted by the FCC to implementing the CLEC resale and UNE models contemplated by the 1996 Act. While much of this activity obviously must continue, the FCC must not let facilities-based competitors get lost in the shuffle. Initiatives to promote the deployment of new facilities, such as the Commission's competitive networks proceeding, should be given top priority, not left indefinitely on the back burner.

3. *Dramatically increase penalties for repeated ILEC litigiousness*. CLECs like Cox often face the prospect of "death by a thousand cuts." The ILECs are renowned for their willingness to litigate every issue rather than negotiate reasonable business arrangements. ILECs with a proven track record of aggressively litigating disputes against CLECs should face dramatically increased penalties in regulatory proceedings in which the CLECs prevail.

4. *Provide facilities-based competitors with special fast-track enforcement and implement much more aggressive economic sanctions against entrenched anti-competitive behavior*. Like all other CLECs, Cox has had to repeatedly enlist the aid of regulators and the courts to compel the ILECs to comply with their obligations under the 1996 Act and related state and federal rules. If regulators are serious about promoting the deployment of new telecommunications facilities, they should establish enforcement procedures which give priority to resolving the complaints of facilities-based competitors. They also should adopt economic sanctions that penalize the ILECs' anti-competitive behavior far more severely than the current regime allows. Small fines and slow enforcement only encourage the ILECs to continue their pervasive efforts to stymie local exchange competition.

5. *Prohibit abusive pole attachment, rights-of-way and franchise requirements and local tax gouging of CLECs*. Although local governments have a vital role to play in ensuring the integrity and safety of public rights-of-way, they should not be permitted to abuse their oversight and impose burdensome requirements, taxes and fees on facilities-based CLECs. Similarly, the owners of essential infrastructure such as utility poles should be prevented from charging unreasonable rates when facilities-based providers deploy new services over their existing networks.

Chairman DEWINE. Mr. Robbins, thank you very much.
Miss Herda.

STATEMENT OF LARISSA HERDA, PRESIDENT AND CHIEF EXECUTIVE OFFICER, TIME WARNER TELECOM INC.

Ms. HERDA. Thank you, Chairman DeWine, and Senator Kohl, for the opportunity to speak to you today.

Before I tell you who we are, I would like to tell you who we are not. We are not Time Warner, Inc.; we are not Time Warner Cable. We have nothing to do with movies, entertainment, "Bugs Bunny" or "Roadrunner". AOL Time Warner is a large shareholder of ours. However, they do not provide funding for our business and they do not run our business. We are a separately managed, separately traded public company.

We have built large fiber optic networks in 39 markets across the U.S., and we will have 44 active markets operational by the end of this year in 21 States. We have also built a national IP backbone network.

Our local networks are large. They average 400 route miles per city. We take that fiber all the way to the customers' buildings, providing them with a completely diverse and separate network from the RBOC. As a result, we have been able to put 80 percent of our revenue stream 100 percent on our fiber networks.

We have spent over $2 billion to crease these networks. We generate positive operating cash-flow, and we are fully funded. We provide Internet, voice and data tele-communication services to over 5,000 diverse customers, consisting of small, medium and large businesses, as well as public schools, government agencies and hospitals in both of your districts. In fact, the service touches all the Members of Congress, since our network serves the Defense megacenter in Columbus which does the payroll for Congress and the White House.

When I started with Time Warner Telecom 4 years ago, we had around 500 employees. Today, we have 2,500. So we have grown significantly.

My response to the question "is the Telecom Act promoting competition" is a qualified Yes. We are precisely what the Telecom Act envisioned. To put it in terms that I am familiar with, however, the Telecom Act is a good business plan, but the execution of the plan needs improvement. And where improvement is needed is in enforcement.

In each State that the RBOCs obtain 271 or long distance relief, it is critical that the RBOC have performance standards and meaningful financial penalties for noncompliance with those standards. The RBOCs have no financial incentive to cooperate with us. When they cooperate, they lose customers. So it is in their best interest not to cooperate. But in order to transition from a monopoly environment to a competitive environment, this cooperation is critical.

The only way to ensure this cooperation is to give the RBOCs a financial incentive to cooperate. The financial incentive is provided by clearly outlining the standards the RBOCs must meet as a wholesale provider and interconnecting carrier, and then imposing meaningful financial penalties for noncompliance with those standards.

The best example I can give you from our perspective is interconnection trunking. Interconnection trunks are the facilities that connect our switches to the RBOC switches. They are the facilities that allow our customers to make calls to the RBOC's customers and vice versa.

When Southwestern Bell filed for its 271 application in Texas, Time Warner Telecom was experiencing major problems to get

interconnection trunks installed in a timely manner. Not only does an insignificant amount of trunking impair the service quality to existing customers, but it also prevents us from adding new customers to the network.

The solution that the Texas PUC devised, and the approach that's being adopted by many other States, was to create specific performance measures relating to how fast Southwestern Bell had to respond to our request to add additional trunking facilities, and required financial penalties for failure to meet those measures. By clearly outlining the responsibilities of both parties, and providing for penalties for noncompliance of those responsibilities, the Texas PUC and the FCC created a mechanism that works.

If Southwestern Bell cannot fill orders for a forecasted need, they know that they will be forced to pay. If Time Warner Telecom does not forecast properly, the fines won't be imposed and we won't be able to get the inter-connection trunks we need to provide quality service to our customers and grow our business.

I am pleased to report that this is working in Texas for interconnection trunking. However, there are other services, like special access, which still need a lot of attention. Interconnection trunking is only one component of the 14-point checklist, but the theory I have described applies to the entire list.

Another measure of whether the Act is promoting competition is by considering what I would like to call barriers to construction. In order to recognize the goal, true facilities-based competition companies must physically construct the network. Two obstacles to Time Warner Telecom's ability to construct networks are, one, which was mentioned by Senator Kohl, the failure of building owners to open up their buildings to competitors, and No. 2, the failure of municipalities to approve quick entry on a competitively neutral basis.

Chairman Pat Wood of the Texas Public Utility Commission coined one of my favorite phrases: "access to the first foot"—excuse me, "access to the last foot." First, last, it doesn't matter. It's all the same.

[Laughter.]

In order to serve customers with our own facilities, we must obtain access to the buildings where they can talk to business, because we take our fiber directly into the customer's buildings. The incumbents were given access, in most cases, without having to contract with the building owners for the rate, terms and conditions

Last October, the FCC adopted an order that prohibits exclusive contracts between carriers and building owners. This order sent an extremely important message to building owners. However, the order falls short because the FCC didn't take the next step of imposing penalties on building owners that deny or delay access to their buildings.

With regard to access to rights-of-way, I simply say our competitors who purchased unbundled network elements from incumbents talk a lot about the last mile. Time Warner Telecom also needs access to the last mile, but rather than leasing it from the incumbents, we prefer to build it to the customer. We are willing to pay for this access and to comply with reasonable rules for access to the

right-of-way, but too often municipalities attempt to charge unreasonable rates and put unreasonable terms and conditions on us.

In closing, I would like to leave you with some thoughts to give you some perspective.

Last year, Time Warner Telecom had $487 million of total revenue. It took Verizon 2.8 days to bring in the same revenue. It took Bell South 6.9 days. It took SBC 3.5 days to bring in the total revenues that we brought in in 2000. And keep in mind, we're one of the larger CLECs out there. Honestly, I can't quite understand why they keep looking to Congress for more help.

Now, if you ever question whether or not the RBOCs would use this market power, remember, time and money are on their side. Their weapon is delay. They can call it process delays. I call it strategic incompetence. Either way, it really doesn't matter because it still serves them well to hurt our business.

This has already contributed to the near downfall of an entire sector. RBOC provisioning delays and regulatory agency delays in responding precisely, in my humble opinion, are one of the leading factors that have hurt the DSL industry. The RBOCs were able to delay provisioning and dramatically decrease pricing to their end users, which resulted in higher costs, lower revenues, and margins that were choked for the DSL companies. They really didn't have a chance. Now that the competition has been stifled, the RBOCs are raising their rates. Time and money are on their side, but not on ours.

So, once again, I would like to stress the importance of compliance with the 14-point checklist of the Telecom Act, objective performance measures, and punitive penalties for failure to meet those performance measures. The entire competitive sector's ability to meet the goals of our business plans are dependent upon vigorous enforcement of the Telecom Act.

Thank you.

[The prepared statement of Ms. Herda follows:]

STATEMENT OF LARISSA HERDA, PRESIDENT AND CEO, TIME WARNER TELECOM INC.

Mr. Chairman and Members of the Subcommittee:

On behalf of Time Warner Telecom Inc. I would like to thank the committee for the opportunity to talk to you today about the status of local phone competition. My name is Larissa Herda and I am the President and CEO of Time Warner Telecom ("TWTC "), which has grown to be one of the largest new competitive entities in the telecommunications industry. We exist today because of the pro-competitive policies adopted in the Telecommunications Act of 1996. We are unique in a number of respects.

TWTC builds its own local and regional fiber optic networks and delivers "last-mile" broadband data, dedicated Internet access, and voice services to small, medium and large businesses. We provide service to a diverse customer base across the country. The Company currently serves business customers in 39 U.S. metropolitan areas. We plan to begin offering service in five other metropolitan areas in 2001. (See attached map) Since the passage of the 96 Act, we have invested approximately $2.0 billion in building a network infrastructure and have created nearly 2,500 high-tech jobs nationwide.

My response to the question "Is the Telecom Act promoting competition?" is a qualified yes. To put it in terms that I am familiar with, it's a good business plan, but the execution of the plan needs improvement. And where improvement is needed is in enforcement.

I. Time Warner Telecom Inc. is Providing Facilites-Based Competition Just as Congress Envisioned

COMPANY HISTORY

Time Warner Telecom began in 1993 as part of the Time Warner Entertainment Limited Partnership. The focus of the Company was to provide cable/phone services to residential and business customers using hybrid fiber coax (HFC) technology. After an extensive pilot program to test residential service, Time Warner Communications evolved into a company that offers business phone services over fiber-optic networks.

In 1997, the Company added voice circuit switches and began operating as a business CLEC. In 1998, Time Warner Communications became a separate entity from Time Warner Entertainment and began to operate as Time Warner Telecom Inc. During 1999, TWTC became EBITDA positive, acquired an ISP, built a national IP backbone and went public, offering 18,000,000 shares on the NASDAQ exchange. We trade under the symbol: TWTC. In August 2000, TWTC successfully bid, during an open auction bankruptcy proceeding, for most of the assets of GST Telecommunications. This allowed us to double the size of the company and extend our operating footprint throughout the Western United States. By end of 2001, TWTC plans to offer telecommunications services over its own fiber optic networks in 44 markets in 21 different states.

OWNERSHIP STRUCTURE

We are very proud to carry the Time Warner name. As I described earlier, TWTC was initially created as division of Time Warner Entertainment. While Time Warner Inc, now AOL Time Warner, owns 44% of Time Warner Telecom Inc. stock, Time Warner Telecom Inc. is an independently owned and operated company. The most important point, from both your perspective and mine, is that we have no financial backing from AOL Time Warner. We obtain the capital we need to do business the same way the rest of the independent CLECs obtain theirs, through debt and equity offerings in the financial markets and from operating cash flow.

COMPANY GROWTH

During a time when the news is full of stories on bankruptcies and employee layoffs we are expanding our network and hiring new people. In 1996 TWTC had 500 employees, the majority of them located in the corporate headquarters in Littleton, Colorado. Today we have approximately 2500 employees and by the end of 2001 will be providing service and employing people in 21 states. Time Warner Telecom's growth plans focus on geographic expansion, extension into new market segments and development of new data and Internet-based products and services. Our success to date is the result of building and deploying our extensive local and regional fiber optic networks all the way to the end user's building and providing a diverse physical alternative to the incumbent LEC. Our expertise is in selling complex network services that customers want and need over these networks. We execute and deliver on a sound business plan. We provide high quality broadband service to a diverse segment of the small, medium and large businesses in the country. In 1996 we had already constructed 5000 route miles. Today that has almost doubled to approximately 9800 route miles. TWTC has constructed more route miles than any other local competitive carrier in the U.S. The fiber optic infrastructure we have built is important because—it allows us to continue to layer more products and services on our network. One of the distinguishing characteristics of our network is that we have been laying this fiber in metropolitan areas; and the networks are large, averaging 400 route miles per city. We're building fiber where it is needed most, the last-mile. However, it is important that Congress recognize that the largest competitor in all of our markets, the local ILEC, has the ability to stymie our growth. Vigorous enforcement of the Act is the only elixir to the poison pill of anti-competitive behavior and abuse of market power.

SERVICE PROVIDED

This is how we do business. In every city that Time Warner Telecom lays fiber, the sales staff is required to prove in advance that there is business to be had. We don't build a network just to show growth, we build a network to provide a service that is desired. This serves our customers and our shareholders well because it ensures our continued viability in the marketplace. And I can assure you that there is demand for the service we provide. In many cases we supplement the services that the incumbent carrier provides. Often, companies will come to us for their new

business or for a specific portion of their telecom needs. As we prove our ability to provide this service, they give us more and more of their business.

The fiber optic networks we have built allow us to offer our customers any technology, product or service solution. With virtually unlimited bandwidth, we can meet the rapidly changing demands of our customers. Our networks allow us to provide voice and data telecommunications services to a diverse customer base including public schools, private schools, universities, health care facilities, banks, the high-tech community, government agencies and military installations, law firms, public utilities, many small businesses, Internet Service Providers, insurance companies and most interestingly many of the telecommunications companies operating in the U.S.

MARKETS SERVED

ARIZONA: Phoenix, Tucson
COLORADO: Denver (2001)
CALIFORNIA: San Diego, Los Angeles/Orange County, Santa Barbara, San Luis Obispo,
Bakersfield, Fresno, San Francisco, Oakland, Sacramento
FLORIDA: Orlando, Tampa
HAWAII: Honolulu
GEORGIA: Atlanta (2001)
ILLINOIS: Chicago (2001)
INDIANA: Indianapolis
MINNESOTA: Minneapolis (2001)
NEw JERSEY: Northern Jersey City
NEw MEXICO: Albuquerque
NEw YORK: Albany, Binghamton, New York City, Rochester
NORTH CAROLINA: Charlotte, Greensboro, Raleigh, Fayetteville
OHIO: Cincinnati, Columbus, Dayton
OREGON: Portland
SOUTH CAROLINA: Columbia (2001)
TENNESSEE: Memphis
TEXAS: Austin, Dallas, Houston, San Antonio
WASHINGTON: Seattle, Spokane, Vancouver
WISCONSIN: Milwaukee

III. The Key to Successful Implementation of the Telecom Act is Enforcement

TWTC has not just spent the last five years building networks. We have also been engaged in legal and regulatory battles across the nation for the right to do so. We are making progress in breaking the monopoly stranglehold, but it has not been quick and it has not been easy. The 96 Telecom Act provided one method for transitioning the local telephone market from a monopoly to a competitive marketplace: The "carrot" of in-region long distance entry for the incumbents if and when they open their local networks to competition. The simple fact is, no company wants to lose business. This creates strong incentives for the monopoly provider to act in anti-competitive ways. But, in order to have a competitive market, the monopoly must lose customers to new entrants. Company policies are driven by financial decisions. It is not in the incumbent's financial interest to cooperate and assist their competitors in taking their customers. But, without this very activity, competition will not exist. That is the brilliance in the 96 Act. By requiring the incumbents to meet the 14-point checklist prior to entering the long distance market, Congress has given the RBOCs a financial incentive to cooperate.

INTERCONNECTION WITH THE RBOCS NETWORK

I would like to provide an example of how this has worked for TWTC. When Southwestern Bell Telephone first applied for 271 relief in Texas, TWTC was experiencing an unacceptable amount of call blocking because TWTC and SWBT did not have the right quantity of interconnection trunks connecting the two networks. Through months of negotiations with SWBT under the supervision of the Texas PUC, a set of performance standards was created. These standards clearly outlined the responsibilities of both companies. TWTC had the responsibility of providing accurate forecasts for the amount of interconnection trunking it would require over the year. SWBT was required to plan for that amount of trunking and if TWTC ordered trunks within its forecasted amount, SWBT was required to cooperate in the installation of those trunks in designated intervals. If SWBT fails to meet its end

of the obligation, fines are assessed. If TWTC fails to meet its end of the obligation, SWBT is not required pay fines if it does not meet the installation intervals and TWTC takes risks of not having the capacity to add new customers to its network.

As long as the CLEC and ILEC companies have the right amount of trunks in place, customers on both networks can make calls without experiencing call blocking. However, it is clearly in SWBT's best interest not to install trunks in a timely manner. If they fail to do this the quality of TWTC's service is severely diminished because customers cannot make calls and TWTC's overall business suffers because we cannot grow the business. The 271 process, through performance measures and penalties, provided SWBT with the financial incentive it needed to get the job done. We needAs our business grows and we add more and more customers to our network, SWBT will have more of a natural or "market-based" financial incentive to ensure that adequate trunking exists between it and its competitors. If it fails to do so, a larger percentage of its customers will suffer from poor quality of service. Because of the nature of the marketplace and the fact that until 1996 SWBT had all of the local phone customers, trunking problems today impact a very small percentage of their customer base but a large percentage of ours.

Government intervention and regulation are necessary until a competitive marketplace exists to replace that regulation. In the long run, it is in everyone's best interest to see this occur. Until it exists, government must stand ready to supply the incentives that the market cannot.

BARRIERS TO CONSTRUCTION

In order for facilities based competition to exist, companies like Time Warner Telecom must be able to negotiate with municipalities and building owners to gain access to the rights of ways and buildings in order to lay fiber and bring that fiber to our customers. Our main competitors, the incumbent LECs already have agreements or have been allowed in without agreements. One of the more unfortunate results of the 96 Act is that cities and building owners are attempting to control the pace of competition by extracting unreasonable rates, terms and conditions for access to a critical pathway to the customer. We are willing to pay for access and meet specific terms of entry; we just want them to be fair and reasonable.

BUILDING ACCESS

Chairman Pat Wood of the Texas Public Utility Commission coined one of my favorite phrases, "access to the last foot." In order to serve customers with our own facilities, we must obtain access to the buildings where they conduct business. The incumbents were given access in most cases without having to contract with the building owners for rates, terms and conditions. It is our belief that the FCC has the authority today to require fair and non-discriminatory access to buildings so that providers can bring the benefits of competition to businesses in multi-tenant buildings. Last October, the FCC adopted an order that prohibits exclusive contracts between carriers and building owners. This order sent an extremely important message to building owners. However, the order falls short because the FCC did not take the next step of imposing penalties on building owners that deny or delay access to their buildings.

ACCESS TO RIGHTS-OF-WAY

Because of our relationship to Time Warner, our initial ability to access rights-of-ways in municipalities may not have been as difficult and time consuming as for some other CLECs. But as we have been expanding into areas where Time Warner Cable is not in business we face many of the same obstacles that our competitors have been complaining about. Competitors purchasing unbundled network elements from the incumbents talk a lot about access the lastmile. TWTC also needs access to the last mile, but rather than leasing it from the incumbents we prefer to build to the customer. We are willing to pay for this access and to comply with reasonable rules for access to the rights-of-way. But too often municipalities attempt to charge unreasonable rates and put unreasonable terms and conditions on us.

To ensure that competitors are able to gain access to the necessary rights-of way to provide service, Congress should consider amending the Act to give the FCC the ability to ensure fair and consistent public policy by establishing non-discriminatory access on a competitively neutral basis.

IV. Description of Differences in Local and Long Distance Markets Importance of Growth in Local "Last Mile" Markets

I believe the Act as written, if vigorously enforced, provides the tools necessary to ensure a successful transition from a monopoly environment to a competitive environment. TWTC is a new entrant in both the local and the long distance market. Our experience entering the local market has been very different from our experience entering the long distance market. To use Ohio as an example, it took TWTC more than $1 million and 2 years to obtain the certification and interconnection agreements necessary to enter the local market. This time and expense does not take into account the huge capital investment required to construct facilities. In sharp contrast, it took $2000.00 and 30 days to obtain approval to offer long distance service in Ohio.

We have spent considerable time and money entering the local markets in states across the nation. It took on average an entire year (often longer) to obtain the required certificates and negotiate the interconnection agreements and obtain the access to rights-of-way that must be in place prior to our ability to provide service. In sharp contrast, getting into the long distance market was a breeze. We didn't have a network in place so we contracted with a provider to resell theirs. There were five different companies bidding for our business. Once we decided on an underlying carrier, we filed tariffs and filled out simple application forms and we were quickly in the long distance business. It was a completely different experience from the difficult and protracted negotiations required to obtain an interconnection agreement with the local monopoly.

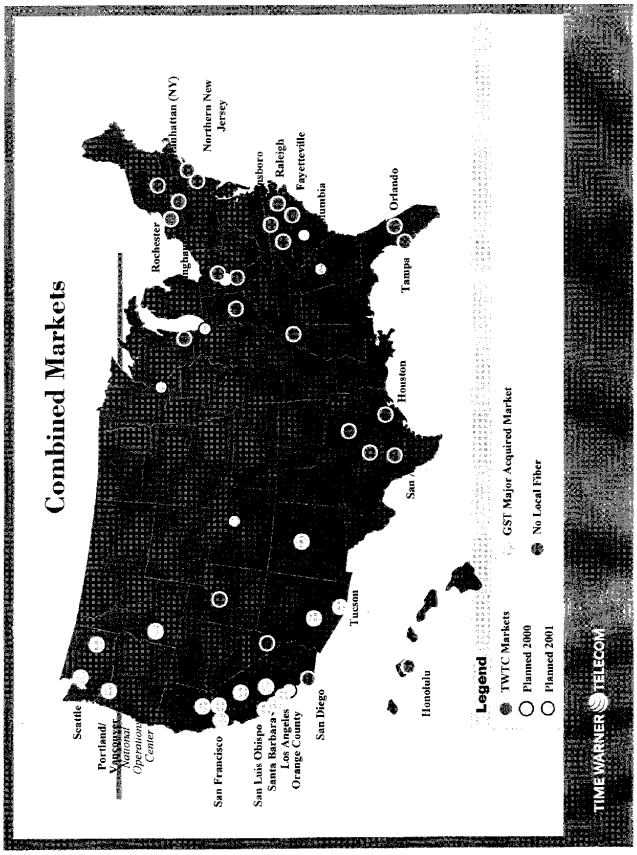
I would like to put this in perspective, focusing onthe goals of Time Warner Telecom's business plan and the goal of the 96 Telecom Act. TWTC wants to provide the highest quality broadband telecommunications service to its customers by building its own network. By providing broadband local telephone service, TWTC is providing the 'last mile' of the broadband network. For well over a decade companies have been building broadband long haul or long distance networks. While I appreciate the RBOCs desire to be able to offer along distance product, that product is available to customers and carriers today on a competitive basis. In order for consumers to truly enjoy the benefits of a broadband network and truly competitive pricing, we must have competition at the local level. The only true way to incent the RBOCs to provide their customers with broadband telecommunications service is by ensuring that if they don't, there is another carrier in the marketplace that will. Our ability to meet the goals of our business plan is contingent upon vigorous enforcement of the Telecom Act

V. Conclusion

I agree that today we clearly have a "Digital Divide." But the divide exists between the long distance broadband fiber optics networks and the local narrowband copper networks. The only bridge that will connect this divide is competition. Time Warner Telecom is committed to building broadband networks in the local markets. Faced with this direct competition, the incumbents will have no choice but to meet us in the marketplace by deploying new facilities or finding more ways to expand the ability of their copper wires to provide broadband services.

Congress drafted the right business plan in 1996. Now the FCC and state PUCs need to vigorously enforce that business plan. I wholeheartedly support the statements FCC Chairman Powell recently made before the House Commerce Committee: The enforcement measures that state PUCs and the FCCs employ must be meaningful. They must be something more than just the "price for doing business." It is naive to expect the incumbent phone companies to develop policies and procedures that will allow their competitors to steal their customers. But without competitors taking customers away from the local monopoly, you will not have competition.

Again, I very much appreciate to opportunity to appear before you today, and I welcome the opportunity to answer any questions that you may have. Thank you.



Chairman DEWINE. Miss Herda, thank you very much.
Mr. Ellis.

STATEMENT OF JAMES D. ELLIS, SENIOR EXECUTIVE VICE PRESIDENT AND GENERAL COUNSEL, SBC COMMUNICATIONS, INC.

Mr. ELLIS. Mr. Chairman, Senator Kohl, thank you for the opportunity to appear and testify.

There are many subjects of the Telecom Act that would certainly be worthy of discussion today, but I'm going to focus on what I think, from my perspective, is one of the most important—that is, whether my company has met its obligations to open the local network to assist our competitors getting into business and, ultimately, taking part of our business. That is exactly what SBC has done.

You have heard today suggestions that we have interfered and our market is not open. Some of the testimony is to that effect. Numbers have been quoted as to the extent of competition. But, I think if we look at the basic facts—and I speak only for SBC's territory—it would demonstrate that we have opened our markets. We

spent billions of dollars to comply. We continue to spend millions of dollars to comply.

We started with a wholesale organization that had six people in 1996. We now have 6,000 employees, and their sole purpose in being is to serve the growing needs of our competitors in the wholesale business.

We have almost 2,000 contracts with competitors. Those contracts let them lease parts of our network, they let them resell our services, exchange traffic with us. We have another 500 contracts in the process of being negotiated. We have 10,000 co-location facilities arrangements in which our competitors come into our central offices, put there facilities in, and compete with us. We have eight million OSS orders of our competitors that were processed last year, eight million. We have exchanged 200 billion minutes of traffic. We have provided almost three million trunks to our competitors for them to provide their services. We have seen the so-called UNE-P in some markets grow by 500 percent last year alone. We have hundreds of competitors, large and small, operating in virtually every one of our markets.

I think perhaps most telling, we started with an industry that had zero exchange lines in 1996. Today, in our territory, they have obtained ten million lines. Ten million. By any stretch of the imagination, you can't say our markets are not open. If competitors want to come in and compete, they can, where they choose and when they choose.

Which brings me to the second point. We have heard a lot about residential competition, or the lack thereof. And that's correct. About 80 percent of those ten million lines are business. But to any observer of our industry—and you've heard it discussed here today—that's not surprising.

Mr. Dorman goes where the money is. For 100 years, the name of the game in telecom in this country was to subsidize and keep affordable the local rate. The Telecom Act didn't change that. The day before the basic rate in Texas, for example, was about ten dollars, before taxes and the universal service charges, about ten dollars. And it is still ten dollars after 100 years. It hasn't changed. The competitors go where the money is. They go after the more lucrative markets, and I don't blame them.

But the Act anticipated that. It recognized that problem, that the old system of implicit subsidies was not sustainable. The Act recognized it and directed the FCC to address that and make those subsidies explicit. They gave them 15 months. Now, you can say whether it was to complete the whole thing in 15 months, or get it started. But we're over 5 years from the passage of the Act and nothing significant has happened in that regard. We still have the same system of implicit subsidies. As long as we do, as long as we do, they will be disincented to go after the residential customer.

The one exception, the one exception is where we have entered the long distance market. When that happens, they come in. The statistics are in my testimony and in Chairman Wood's. They enter the market to go after that bundle and to hold that long distance customer.

The other thing I would tell you, the exact systems that are used, the facilities, the wholesale group, the processes, are equally avail-

able for whether you want to use them for business or residence. But they follow the money, and that will continue, until the subsidy.

So if somebody says there isn't sufficient residential competition, urge them to call the FCC. Ask them to move and make those subsidies explicit. Level that playing field.

One other thing I would like to mention is on advanced services. In the last few days, I have seen nothing but television ads on both sides on that. It's an important subject. In advanced services, I'm not talking about the legacy network of the telephone company. We're talking about four ways to get to the high-speed Internet. That's what I mean. That's what it's all about, fast access to the Internet.

There are four ways to get there: cable modem, DSL, wireless, and satellite, four technologies offering the same service. That's the reality of the world today. Each of those technologies requires spending new money. It's not about the old. It's new money investing, competing for who is going to win that customer.

You wouldn't know it from the ads, and you wouldn't know it from Mr. Dorman's testimony, but today, AT&T and its cable modem compadres provide 75 percent of that high-speed access, 75 percent. The other three technologies, DSL, wireless and satellite, are 25 percent.

Every analyst will tell you there is one market. It's high-speed access. They are the dominant provider. It is the future, I agree with them on that. But what they want is to have a system of asymmetric regulation where the only provider that is subject to regulation is DSL. They have absolutely no service regulation on cable modem, none whatsoever. They want to extend the legacy network regulation on to DSL.

I'm here to tell you, whether it be as a lawyer or businessman, no incumbent is going to invest in DSL and enter a market where they have the burdens of regulation and our direct competitor is totally free of regulation. It doesn't have to be that way. We have a model that's been alluded to, and that's the wireless model. We have four or five competitors who spend their own money, invest their facilities, operate independently, not dependent on anybody's network, and they compete head to head, with minimal or no regulatory intervention. We have the most competitive wireless market in the world. I hope that the Commission will follow that model, and if they don't, I hope the Congress will grant that relief.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Ellis follows:]

STATEMENT OF JAMES D. ELLIS, SENIOR EXECUTIVE VICE PRESIDENT AND GENERAL COUNSEL, SBC COMMUNICATIONS INC.

I. INTRODUCTION

Good Morning. My name is James D. Ellis. I am of Senior Executive Vice President and General Counsel of SBC Communications Inc. I am pleased to be here this morning to discuss the Telecommunications Act of 1996 and the impact it has had on competition in the local exchange markets throughout SBC's thirteen state region. Although the fundamental goal of the 1996 Act—to open all telecommunications markets to competition and to do so in a deregulatory, marketbased, competitive manner—is still to be achieved, there is simply no question that the impact of the 1996 Act on local competition has been enormous.

II. SBC Has Opened Its Local Markets

Empirical evidence demonstrates conclusively that SBC has opened its local markets to competition. Simply put, SBC has done an outstanding job fulfilling its obligations under the 1996 Act to open local markets to competition. The FCC has already granted SBC long-distance authority in Texas, Kansas, and Oklahoma. By approving SBC's applications for these states—the most for any Bell company the FCC found that SBC has taken the statutorily required steps to open its local exchange markets to competition. SBC has instituted the same market-opening systems and processes throughout its region.

SBC has spent more than three billion dollars in developing systems and processes to make it possible for competitive local exchange carriers ("CLECs") to enter and compete in the market for local telecommunications services. It has devoted enormous staff and technical resources in order to satisfy each of the 14point checklist obligations that Congress identified in section 271 as a prerequisite for granting long-distance relief. The facts demonstrate that SBC has made each of the 14 point checklist items available to CLECs and that CLECs have taken advantage of all of those checklist items.

For example, as of the end of March 2001, the SBC operating companies have signed more than 1,860 interconnection agreements with CLECs and those CLECs have captured more than 10 million lines throughout the SBC region. As of April 2, 2001, SBC has provided more than 2.9 million interconnection trunks to CLECs for the transmission and routing of telephone exchange service and exchange access. SBC has provided CLECs with 10,496 physical collocation arrangements (and over 600 virtual collocation arrangements), and there are CLECs collocated in 1,346 of its wire centers. Since the beginning of 1998, SBC has processed more than 18.9 million CLEC orders for unbundled network elements. And while SBC has provisioned more than 1.2 million stand-alone loops and more than 7,780 stand-alone switch ports, it has provided more than 1.3 million UNE-Platform loop/port combinations.

As of the end of March 2001, there were more than 3.45 million business listings in SBC's E91 1 database and more than 886,000 residential listings.[1] The total number of CLEC end-user white pages listings now totals over 4.2 million entries. Over 3.6 million telephone numbers have been converted (i.e., ported) from SBC to facilities-based CLECs. And CLECs are reselling over 1.69 million SBC access lines. Since January 1997, excluding ISP traffic, SBC and CLECs have exchanged over 210 billion local minutes of use.[2]

Figures provided by AT&T to the FCC also demonstrate that CLECs are aggressively competing in the telecommunications market. According to its own estimates, AT&T paid approximately $106 million to CLECs in access charges between January and December 2000.[3] The FCC has determined that AT&T paid a weighted average of 4.33 cents per access minute,[4] meaning that CLECs originated and terminated last year over 2.4 billion long-distance minutes for AT&T alone.

Because the FCC and state regulators have made it far more profitable for CLECs to serve business customers than residential customers, CLECs in SBC's region have concentrated their efforts by competing in the higher profit business market. Historically, of course, residential rates have been kept artificially low in order to guarantee universal service. By contrast, business rates have been kept higher in

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[1] This number substantially understates the actual number of facilities-based lines served by CLECs in SBC's region. For example, E91 1 listings only represent those customer lines from which outbound calls can be made. As a result, business customers such as call centers, reservationists, telemarketing centers, and Internet providers will have few of their access lines represented in the E91 1 database. In addition, when a number is ported from SBC to the new serving CLEC, the number would continue to appear as SBC's line in the E911 database. Finally, CLECs themselves may make errors in entering E911 listings, and SBC does not 'police' those entries to ensure that they are accurate and complete. For all these reasons, the listings in the E91 1 database provide a very conservative estimate for the number of business and residential listings served by facilities-based CLECs. The true number of CLEC facilities-based access lines throughout SBC's region can only be estimated, but it probably falls between 4.2 million and 9.3 million lines.

[2] Three years ago, an analyst recognized that competitive local exchange carriers ("CLECs") had signed up more new customers in that quarter than the incumbent local exchange carriers had—something that took MCI and Sprint more than ten years to accomplish in the long distance market. See J. Grubman, et al., Salomon Smith Barney, CLECs Surpass Bells in Net Business Line Additions for First Time, May 6, 1998.

[3] Seventh Report and Order and Further Notice of Proposed Rulemaking, *Access Charge Reform; Reform of Access Charges Imposed by Competitive Local Exchange Carriers, CC* Docket No. 96–262, § 22 (FCC Apr. 27, 2001).

[4] *Id*. § 48, Table 1.

order to subsidize the lower residential rates. That CLECs have chosen to concentrate on serving business customers—where the potential profit is much greater—is entirely rational, and nearly 80% of the CLEC access lines in SBC's region are in the business market.

III. Local Competition and the Granting of Long-Distance Authority

There is simply no question that local competition is directly related to longdistance relief—the closer that SBC has come to providing a bundled package of local and long-distance services, the more intense has been the commitment of traditional long-distance providers to enter the local market. SBC can now provide customers in Texas, Kansas, and Oklahoma with a single source for local and longdistance service, and this has put significant pressure on the competition to provide lower prices, enhanced services, and greater quality.[5]

SBC filed its Texas 271 Application with the FCC in January 2000. Approval was granted at the end of June, and SBC began offering long distance service to subscribers in Texas on July 10, 2000. As Table 1 illustrates, the growth in local competition in Texas since SBC filed its application has been phenomenal:

Table 1
Growth in Competitive Indicators for Texas 271 Application
January 2000 to March 2001

Competition Indicators	Texas
Lines Captured by Facilities Based CLECs	1,243,000 / 2,732,000 (% growth = 119%)
Total Lines Captured (Including Resale)	1,590,000 / 3,063,300 (% growth = 92%)
Interconnection Trunks	398,000 / 591,800 (% growth = 48%)
Operational Physical Collocations	1,012 / 2,373 (% growth = 134%)
Unbundled Stand-Alone Loops	49,000 / 117,650 (% growth = 140%)
Orders Processed Per Month (Both Electronic and Manual)	171,000/584,421 (% growth = 242%)
UNE Platform Loop/Port Combinations	148,000 / 983,400 (% growth = 564%)
E911 Listings	368,327 / 508,600 (% growth = 38%)

AT&T offers its Local One Rate® promotional service only to customers in Texas and New York, the only states where the incumbent Bell Operating Company is in a position to compete seriously for long-distance market share. The Local One Rate® plan bundles local and long distance into one package offering, and AT&T promoted it through direct mail and telemarketing in Austin, Dallas, Houston, San Antonio

[5] "We need only review the state of competition in New York and Texas to know the Act is working." William E. Kennard, Chairman. FCC. *Statement Before the Committee on the Judiciary United States House of Representatives on H.R. 1686—the "Internet Freedom Act" and H.R. 1685—the "Internet Growth and Development Act"* (July 18, 2000),—*at* http://www,house.gov/judiclary/k-ennO7l8.htm ("Kennard Testimony').

and South Texas, offering 60 minutes of free long distance to consumers as an incentive to choose AT&T Local One Rate® for local and long distance service. Most importantly, the AT&T Consumer Sales & Services Contacts for AT&T Local Service list only two geographical options for this service: New York—AT&T Local One Rate; and Texas—AT&T Local One Rate. No other states are apparently given these promotional alternatives.[6]

In July 2000, coincident with SBC's entry into the Texas long distance market, AT&T also reduced its long distance rates in Texas (offered through the Texas One Rate Plan) by greater than 50%—from 15-cent a minute to 7-cent a minute. In addition, a Wall Street Journal article on November 30, 2000[7] described AT&T's plan to launch a separate promotion involving local cable telephony:

AT&T TO OFFER FREE CABLE TELEPHONY IN CAMPAIGN TO HIT SUBSCRIBER GOALS

AT&T Corp., scrambling to meet a year-end promise to Wall Street to sign up thousands of new cable-telephony customers, plans to offer as many as five months of free local and longdistance service to people who subscribe.

The new marketing campaign, which is expected to begin in a number of big cities on Friday, is aimed at boosting the number of AT&T consumers for "cable telephony," industry parlance for phone service over cable-TV lines. The campaign offers free installation and as man as five months of free local and long-distance hone service.[9]

Recently, the cable company Cox Communications, Inc. announced that, in the first quarter of 2001, it had "experienced vigorous growth in residential telephone service, adding about 4,000 customers per week by the end of March, achieving 11 % penetration of telephone ready homes."[8] In SBC's region, Cox offers telephony service in San Diego and Orange County, California; Oklahoma City, Oklahoma; in West Texas; and in various towns in Connecticut.

On March 5, 2001, two days before Southwestern Bell's scheduled launch of longdistance service in Kansas and Oklahoma, AT&T announced a special deal exclusively for its longdistance customers in Kansas and Oklahoma. AT&T customers in these two states automatically received a special AT&T customer service greeting while placing a call and thirty free minutes of long-distance calling. The promotion in Oklahoma and Kansas by AT&T "is part of the first broader application of this innovative technology."[9] And last week, Birch Telecom Inc. announced plans to reenter the residential markets in both Kansas and Oklahoma, offering a bundled package of local and long-distance services.[10]

Not to be outdone, WorldCom responded to SWBT's Texas 271 approval with the introduction of three new rate plans: MCI WorldCom 7-cent Anytime; 9-cent Anytime and WorldCom Weekends. Effective September 7, 2000 WorldCom also began offering Texas consumers different options (the One Company Advantage 200 and One Company Advantage 7 plans) for bundling local, local toll and long distance calling, as well as discounts on calling features.

The benefits of granting long-distance relief to the BOCs are clearly not limited to enhanced long-distance competition. Indeed, the granting of section 271 relief has led all competitors to increase substantially their commitment to local competition. SBC and Verizon, together with their local competitors, have begun to invest even greater sums in advanced services and in upgrading the local infrastructure in those states where section 271 authorization has been granted. Verizon has invested approximately $1.5 billion in Western New York during the past year, including 150,000 miles of fiber optic cable, more than 90 switching centers, and more than

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[6] Three webpages may be consulted for this information: AT&T, *For Home:Customer Service Numbers, AT&T Residential Service,* http://www.att.com/help/callusihome/; AT&T,—*As Advertised: AT&T Local One Rates*sm' New York, http://www.att.com/local—service/ny/; and AT&T, *As Advertised: AT&T Local Service in Texas*, http://www.att.com/local-service/tx/. Interestingly, the AT&T Local One Rate promotion began in New York shortly before the FCC granted Bell Atlantic permission to offer long distance in New York. As of February 5, 2001, this promotional offering was not available in any other state.

[7] D. Solomon, *AT&T to Offer Free Cable Telephony in Campaign to Hit Subscriber Goals*, Wall Street Journal at A3 (Aug. 30, 2000).

[8] Press Release, *Cox Communications Announces First Quarter Financial Results for 2001: Solid Growth in New Services Fuels Healthy Financial Results* (Apr. 26, 2001), at http://biz.yahoo.com/bw/010426/2084.htm1.

[9] *See* AT&T Press Release, *AT&T Long Distance Customers in Kansas Get the Message: Thanks for Your Loyalty*, Mar. 5, 2001, at http://www.att.com/press/item/ 0,1354,3701,OO.html; *AT&T Press Release, AT&T Long Distance Customers in Oklahoma Get the Message: Thanks for Your Loyalty*, Mar. 5, 2001 at http://www.att.com/press/item/ 0,1354,3702,OO.html.

[10] *See Birch to Enter Residential Market Again*, Kansas City Star, Apr. 24, 2001; *Birch Telecom Offers LongDistance Service*, Tulsa World, Apr. 24, 2001.

800,000 access lines.[11] Last year in Texas, SBC invested more than $1 billion to upgrade its central offices, expand Advanced Intelligent Network capacity, and install 2,600 miles of fiberoptic cable.[12] In addition, through SBC's $6 billion broadband initiative—Project Pronto—SBC's DSL service was made available to an additional 900,000 Texas residences and businesses, bringing broadband service at the start of 2001 to a total of 46 cities in Texas.[13] To upgrade its networks and central offices, and lay new fiber-optic cable, SBC last year invested over $230 million and $135 million in Kansas and Oklahoma, respectively—this includes 300 miles of new fiber optics in each state.[14]

Along with discounts on local/long-distance bundles and reduced intrastate rates, the incumbent interexchange carriers are also leveraging advanced technologies. According to former FCC Chairman Kennard, "We have witnessed a dynamic market for broadband services develop as a result of the opening of local markets in Texas and New York."[15] AT&T recently announced major improvements to its networks serving several Texas cities, including upgrading its fiber network to OC–192 (ten gigabits per second).[16] And AT&T is using Texas as one of its test grounds for cable telephone service.[17] All three of the major interexchange carriers are implementing fixed wireless networks to provide broadband access and residential telephone services. In parts of Texas, AT&T uses a fixed wireless system to offer customers a local/long-distance package.[18] In Dallas, MCI WorldCom offers a new alternative to wireline voice and Internet service with Multichannel Multipoint Distribution Service technology.[19] And Sprint has developed a wireless Internet service, using line-of-sight technology, that debuted this past summer and is already available in Houston.[20]

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[11] *Verizon Fiber Network Wires Buffalo Market*, American City Bus. J., Jan. 15, 2001, at 11 ("Competition is driving this investment with more and more companies vying for service.").

[12] *See* SWBT Press Release, *Southwestern Bell Invests $1 Billion in Network Enhancements, High Tech Product Offerings to Ensure State-of-the-Art Communications for Texans in 2001*, Feb. 8, 2001, at http://www.swbell.com/About/NewsCenter/ShowRelease/ 0,1018,20010208–01,00.htm1?NID=.

[13] *See id.*

[14] *See* SWBT Press Release, *Southwestern Bell Invests Millions in Network Enhancements, High Tech Product Offerings to Ensure State-of-the-Art Communications for Kansans in 2001*, Mar. 2, 2001,—*at* http://www.swbel1.com/About/NewsCenter/ShowRelease/ 0,1018,20010302–01,OO.html?NID=; SWBT Press Release, *Southwestern Bell Invests Millions in Network Enhancements, High Tech Product Offerings to Ensure State-of-the-Art Communications for Oklahomans in 2001, Feb. 20, 2001*,—*at* http://www.swbell.com/About/ NewsCenter/ShowRelease/ 0,1018,20010220–O1,00.html?NID=.

[15] Kennard Testimony, *supra* n.5.

[16] *See* AT&T Press Release, *AT&T Offers Austin Business Customers Local Service Choice*, Dec. 5, 2000 ("In a move to enhance the suite of local voice and data services it offers business customers, AT&T has completed a $10 million enhancement of its high-speed local network serving the Austin area."),—at http://www.att.com/press/item/0,1354,3527,00.html; AT&T Press Release, *AT&T Offers San Antonio Business Customers Local Service Choice*, Dec. 5, 2000 ("AT&T has completed an $1 1 million enhancement of its high-speed local network serving the San Antonio area. The company is aggressively targeting the lucrative $110 billion-plus local services marketplace nationwide with promotional offers."), at http://www.att.com/press/item/0, 1354,3526,OO.html; AT&T Press Release, *AT&T Offers Houston Business Customers Local Service Choice*, Nov. 29, 2000 ("AT&T has completed a $100 million enhancement of its high-speed local network serving the Houston area"),—at http://www.att.com/press/item/ 0,1354,3501,00.html; AT&T Press Release, *AT&T Offers Dallas/Fort Worth Business Customers Local Service Choice*, Oct. 19, 2000 ("AT&T is completing a $28 million enhancement of its high-speed local network serving the Dallas and Fort Worth metroplex"), *at* http://www.att.com/press/ item/0,1354,3408,00.html.

[17] AT&T Broadband spokeswoman Sarah Duisik commented on how AT&T has spent nearly $200 million in Dallas to upgrade cable networks to offer two-way transmission. See Jim Landers, *Faster, Faster: Americans Clamor for HighSpeed Net; FCC to Release Data on Spread of Broadband Services*, Dallas Morning News, Aug. 3, 2000, at 22A.

[18] *Technology Briefs*, Dallas Morning News, Feb. 28, 2001, at 2D ("AT&T Corp. changed the name Tuesday of its fixed wireless service in North Texas to AT&T Wireless Digital Broadband. The service will cost 529.35 a month for unlimited local and long-distance calls within Texas.").

[19] *See* MCI WorldCom Press Release, *MCI WorldCom Adds Dallas to "Fixed Wireless" Service Trials*, Apr. 5, 2000 ("MCI WorldCom today announced Dallas as the fifth market for test cutting-edge wireless technology which soon will offer customers a new, competitivealternative for high-speed, broadband service. The Dallas trial is the latest step in MCI WorldCom's overall strategic efforts to offer high-speed, broadband services using radio spectrum designated for an advanced technology known as Multichannel Multipoint Distribution Service (MMDS)") *at* http:/ /www.worldcom.com/about—the—company/press—releases/ display.phtml?cr/20000405.

[20] *See* Tom Fowler, *Sprint Has Wireless Net Access*, Houston Chronicle, Oct. 3, 2000; *Sprint Press Release, Sprint Introduces New Broadband Wireless Service to Fresno's Residential and Small Business Customers*, Jan. 23, 2001, *at* http://144.226.116.29/PR/CDA/PR CDA—Press Releases Detail/1,1579,2198,OO.html.

IV. CONCLUSION

Local competition has taken hold in the states within SBC's region, and SBC is committed to ensuring that it continues to flourish. As the evidence from Texas, Kansas and Oklahoma makes clear, however, the key to greater local competition is in permitting all carriers to compete equally in all markets, giving everyone the incentives necessary to invest in telecommunications facilities and to compete for all customers.

Chairman DEWINE. Mr. Ellis, thank you very much.

Mr. Dorman, do you want to respond?

Mr. DORMAN. To the point about DSL?

Chairman DEWINE. Yes.

Mr. DORMAN. I think it is a fact that the cable modem has more of the high-speed data marketplace. That is owing largely to the fact that it started sooner. The cable companies began providing cable modem service I think in advance of DSL deployment in a big way in the local telephone companies.

It doesn't change the fact, however, that, in the case of AT&T, we serve 16 million homes with our cable plant. We need the opportunity to provide high-speed services to other customers outside of our cable footprint. So we are pursuing the provision of DSL service.

What concerns us is not having the ability to access DSL services, either on the deployment ourselves—in other words, being able to get to the local loop to provide the DSL equipment ourselves—or having some disadvantage, inherent disadvantage, by changing the Act's requirements for unbundling for essential facilities.

Chairman DEWINE. Let me ask a question of the whole panel.

A recent New York Times article dealt with the future of the telecommunications industry. The article speculated that many of the current long distance and competitive local phone companies could potentially either fail or be acquired by the Bell companies. That version of the future had the Bell companies in control of the telecommunications industry in just a few years. Obviously, the 1996 Act did not contemplate a competitive landscape such as that described in this New York Times article.

Any comments? Let's start with you, Mr. Dorman. Get your crystal ball out here.

Mr. DORMAN. Sure. Well, if you go back to the separation in 1983 that basically spun the Bell companies off from AT&T in settlement of the antitrust suit, I think we have to recognize that the long distance industry, as it's been referred to, is really a product. Long distance is a product of a more complete telecommunications bundle. I think the fact it takes, as we've talked here today, much longer to make progress in the local entry than it does long distance, does create asymmetry.

I would agree with Mr. Ellis. There is asymmetry. The cost and the time necessary—I think Verizon was granted authority to be in the Massachusetts long distance market within the last week or so. They were in the market the next day offering it across the State to any of their customers.

When AT&T announced it was going to upgrade the TCI MediaOne cable plants, we had been hard at it for 3 years. We have spent $20 billion, and we still don't have it all done yet. That's to 16 million homes.

I think the final point is, as former Chairman Hundt said, vertical integration is an economic reality in situations where you have these kinds of asymmetries. You know, there has been a lot of speculation about that already in the industry, where people want to accelerate their entry into different markets, or do it in a more capital efficient way. So I don't think that the article was suggesting something that hasn't already been considered by some, or is completely out of the realm of the possible.

Mr. ROBBINS. Mr. Chairman, let me make a couple of points about the article that I think sort of outline the incumbent local exchange carriers' behavior.

Yes, according to Mr. Ellis, 75 percent of broadband access users are using the cable modem, and the reason for that is, as Mr. Dorman just pointed out, cable did get out there in front and provide this service, while the phone companies warehoused the DSL technology. It wasn't until cable rolled out the modems that the phone company said, "Hey, we had better get with it or we're going to lose this market opportunity." They were selling second lines, they were selling ISTN, they were selling T–1's.

I would give you another example of the power of incumbency here. While there's been all sorts of talk about local rates being subsidized, some of the ILECs have asked for pricing flexibility so that they could decrease their local rates and drive competitors like ourselves out of the business. So take what Mr. Ellis says with a little bit of salt, please.

Chairman DEWINE. Miss Herda.

Ms. HERDA. Mr. Chairman, I didn't see the article, but I think I understand the point.

If you had asked me 2 years ago, two or 3 years ago, who would end up the stronger, the long distance companies or the local companies, I don't think I would have predicted what has occurred today. But I think what has occurred today is that you have very significant competition in long distance services and a lot of market share that a lot of the parties are going after.

Regardless of what Mr. Ellis says about all of the competition that's going on in his marketplace, there truly isn't open competition going on. They still have the vast majority of the marketplace and, without enforcement, it's going to stay that way.

Yes, that article could be true if that, indeed is what occurs. I do believe, though, that if there is enforcement, if the Congress and the FCC is vigilant, that article does not have to be reality.

Chairman DEWINE. Mr. Ellis.

Mr. ELLIS. Senator, there is a lot I want to respond to. I would just start out by saying, with respect to the advanced services market, I don't think there's a single analyst who has a different view but that cable modem will be the dominant provider of advanced Internet services for as far out into the future as they predict it. The question is whether there's going to be an alternative to it. They're the dominant provider.

The allegation that were slow getting into it is kind of ironic. We know what we've been through in the last 5 years. We have been spending billions and devoting thousands of employees to comply with the Act. And for somebody to come in and fault us because

we're not embarking on DSL technology as fast as perhaps we would have liked to, that's just wrong.

With respect to the issue that Miss Herda has raised about enforcement, to my knowledge, we don't have any problems with Time Warner. She referred to an incident that took place in 1999 and it was worked out. Our trunk performance, for example, over the last year, there's been no problems. So if we have difficulties with Time Warner or with any carrier, there are processes in place to work them out.

Your question about the merger—I think that's where we started, about potential mergers—all I can say is this industry is increasingly competitive. There is an increasing globalization of the market. It would not surprise me, across telecom, that you will see people and businesses doing exactly in our industry what they do in others. They look for scale and efficiencies.

Chairman DEWINE. Mr. Ellis, as part of SBC's takeover of AmeriTech, it promised to enter the markets of other established phone companies. The Cleveland Plain Dealer reported in March of this year that SBC had decided to delay these plans.

First of all, is that true, and if it is, what is the company's plans for the future?

Mr. ELLIS. Under the merger conditions, we were required to be in 15 cities, I believe on March 9th, and we're in 20 cities. We are five cities out of the 30 ahead.

What we did, we put together what is called the national local plan before the AmeriTech merger, more than 3 years ago. It depended directly on our ability to go to customers, major business, small business, medium-size business, and offer a complete package, particularly data.

No one, I submit, would have predicted that almost three-and-a-half years from when those plans were put together we would be in only three States. It became clear to us that we could not—that it did not make sense to fulfill our very ambitious plans until we had that capability.

We are meeting our requirements. We are in a holding pattern in terms of those cities. We're not going to spend the money that we had originally intended until we got data and primarily long distance relief. It's as simple as that. Nobody would have anticipated—Just like no one would have anticipated that here we are, 5 years plus after the Act, and there are five States that have passed the 271 test. Nobody would have predicted. And we didn't predict it would be three-and-a-half years and there would only be three of our States.

Chairman DEWINE. Senator Kohl.

Senator KOHL. Thank you, Mr. Chairman. Senator Leahy is not able to attend, but he asked that his statement be placed into the record.

Chairman DEWINE. We will place that in the record.

Senator KOHL. I thank you.

Mr. Dorman, your company, AT&T, has plenty of experience with antitrust law. I mention that because the regional local phone companies created after the breakup of AT&T are now engaged in several mergers of their own so that there are now only four left, as you know. These companies maintain their monopoly status for

local telephone service and they control over 90 percent of the service to local phone lines.

So, Mr. Dorman, what role should the antitrust laws again play in ending the near monopoly of the incumbent local phone companies, just as these laws were used to end the AT&T monopoly?

Alternatively, many say that what we really need is to give the FCC real enforcement power so that they can take action to implement the Telecom Act. Is that a better route than the one I mentioned first?

Mr. DORMAN. I think you have a situation where we have laws, and having more policemen on the street is probably a good idea. What I mean by that is that both the FCC and the State commissions have important roles in enforcement, and the swiftness of that enforcement is critical. As Miss Herda said, time and money is one the side of the incumbent.

So if we are in a situation where the only course of action is antitrust, having recalled how long it took for the Bell System and AT&T to be separated and settle that antitrust action, I think that would create a situation where competition would suffer and competitors would suffer.

But I do believe we cannot ignore the fact that there are antitrust laws and we have to be vigilant in following those. If there are abuses, then they should be pursued. I think, as a business person, your first reaction in facing situations where someone is, in your view, violating an antitrust law, is to try to work it out, to point it out.

I think in the case of the Telecom Act we have a vehicle that was established to identify the behavior, disincent it, and, in fact, actually reward behavior opposite of that, with the "carrot" of long distance entry. So I think a lot of that was thought of in the building of the Act. But I don't think we can walk away from the fact that there has to be a test in the antitrust context that can be ignored.

Senator KOHL. Mr. Ellis, do you have an opinion?

Mr. ELLIS. Senator, I have obviously not done a very good job of trying to make the point, that our markets are open. In some markets, Houston, Dallas, we have lost 30, 40 percent of business lines. The very same systems that the competitors used to take the business lines from us and provide that market are available for residents.

I can't change the fact that people focus on the business markets, but it is not because of a failure on my company's part. They're there. We have lost those very lucrative customers. They follow the money. That market is open for competitors to come in. We have hundreds. I'll send you the list of them. Look in a phone book. People have choices.

Now, I grant you, they are not focused on residents, and we have talked about why. But the business market is flourishing in every major city. There are multiple switches by Time Warner and others. Facility-based, resale, UNE-P, the customer has choices. It is wrong to characterize our market as a monopoly, just as it's wrong in SBC's territory to say we have 93 or 96 percent of the market. We do not. And we certainly don't have the most attractive customers in terms of returns. The competitors are going right after them, for the reasons we talked.

Senator KOHL. Miss Herda, Time Warner Telecom has not had the problems that many other competitors have had. Why have you achieved your successes while many of the other companies in your industry have failed, and is there a lesson from your successes that can be applied to other CLECs?

Ms. HERDA. That sounds like a question I would get from the investment community.

Well, first of all, we have been very focused on being a true facilities-based provider. We build fiber optic networks and our strategy is to leverage those networks with additional products and services and continue to get a good return on our investment.

I think that a lot of our competitors, quite frankly, their biggest competitor is also their biggest vendor. When you have a situation where your biggest competitor is your biggest vendor, in an environment where there is no enforcement, you run into problems.

As I said in my testimony, that's what happened to the DSL providers. It happens to us today, because even though we are very independent from the local exchange carriers with our own networks, we must interconnect with them.

I am happy to agree with what Mr. Ellis said earlier, that the trunking problems in Southwestern Bell territory were taken care of. But that's just the point. The 271 process worked there, and we need that type of enforcement all across the country.

I just recently lost a $100,000 a month customer in Verizon territory because of trunking problems. They were slow to respond and, by the time we got all the trunks in, the customer had already chosen another provider. Now I have to take the trunks down because, if I don't use them in 90 days, then they're no longer valid trunks. But I lost the customer, so we spent a lot of money for nothing.

I think the fundamental reason why we have also succeeded is because we have also focused on getting a return on our investment, and our business plan works. It's very facilities-based and we are not as dependent upon the local exchange carriers as others are.

Senator KOHL. As you know, your company does not currently directly serve residential customers, but you instead serve business companies. Why is this, Miss Herda?

Ms. HERDA. Actually, prior to me joining the company in 1996, we were very deeply involved in a residential pilot in Rochester, NY, which was very successful in terms of customer acquisition. The only problem was we couldn't figure out a way to make money. So the company decided to leave the residential. That was over the hybrid fiber coax cable with Time Warner Cable at the time we were integrated within that same company.

When I came on board, I separated the company from Time Warner Cable and refocused it on business services, where I knew we could make money. There is limited capital out there for businesses, and that's where we thought we could get a better return on our investment.

I think a lot of people have testified today that there was no money in residential service then. I really can't say if there's money in it today. We haven't been pursuing it.

Senator KOHL. OK, Miss Herda.

Mr. Dorman, many competitive local phone companies face difficulties gaining access to multi-tenant buildings, and many argue that this is one important reason why their companies have had such a difficult time competing with the incumbent phone companies.

Would you favor building access legislation that would enable phone companies to gain access to multi-tenant buildings on the same terms as incumbent companies? Wouldn't this promote competition by removing a major competitive bottleneck?

Mr. DORMAN. I think, as Chairman Wood said earlier, the last foot or first foot, whatever the case may be, is very important. If a customer wants to be served by our company and they cannot be because of the control of that last foot or the connection into the building, then obviously that's a difficult thing for us to overcome.

The benefit of having national legislation is obviously not having to work through a crazy quilt of 50 individual States considering that issue and coming to some conclusion which may perhaps be very different State by State. So I think, whether it goes all the way to legislation or FCC action, having an ability to do that on a national basis would be attractive for national competitors.

Senator KOHL. Any other opinions on that?

Mr. ELLIS. I would just say, Senator Kohl, this issue is not unique to the CLECs. This is between the landlords. We have the same problem. The landlord and a competitor enter into a contract and we have to live with it. So this is not an issue that we have a position that's any different from any of the other competitors.

Senator KOHL. OK.

Ms. HERDA. Although I think that the advantage that the RBOCs have is that they are in quite the vast majority of the buildings that are out there. Without a doubt, there are a few landlords—I mean, quite frankly, the landlords have been trying to get a piece of telecom revenue for as long as I've been selling competitive telecom, which is about 13 years. We have always had to spar with them.

We eventually do get into buildings where we have the tenants in the buildings, but when you sell to a lot of small customers in the building, the tenants, those types of customers don't have the pull with the landlords, and those are the customers that don't get the competitive telecom services. It's usually the larger ones that do.

The landlord community absolutely needs to be compelled to provide nondiscriminatory access, and there should be penalties for any delays that they create. We have lost millions of dollars of business because they've delayed or refused to let us into buildings.

Senator KOHL. I thank you, Mr. Chairman.

Chairman DEWINE. Miss Herda, do you want to tell me a little bit about what you all are doing in Ohio, what your plans are?

Ms. HERDA. We actually have quite a presence in Ohio. I was just looking through some of my customer lists here.

We are in Dayton, we're in Columbus, we're in Cincinnati. We have large networks in those cities. We are serving customers like Wright-Patterson Air Force Base in Dayton. We serve a lot of school districts actually in Cincinnati, the Kings local school dis-

trict, Roger Bacon High School, Covington Catholic High School. We serve large customers, too, and hospitals, like Mercy Hospital.

We are connecting up our cities, also. We have a strategy of building regional connections between our cities, and those particular cities have a lot of community of interest between them, so that we can truly provide a completely diverse network to the customers in the Ohio area.

Chairman DEWINE. Good. Thank you very much.

Ms. HERDA. You're welcome.

Chairman DEWINE. Let me thank our panel very much. It has been very informative, both panels.

I think this has been an informative and important discussion about competitive progress in the local telephone market 5 years after the 1996 Telecom Act took effect. The testimony we heard today has demonstrated that, to some extent, the Act is working and competition is moving forward.

It is the pace at which it is moving that concerns us. Competitive providers have less than 7 percent of the national market and, clearly, much remains to be done. We will continue to watch the competitive developments closely to ensure that we have vigorous competition in the tele-communications industry. We look forward to working with those in the industry to promote competition and to protect consumers.

We thank you all for your patience, and again, we thank our witnesses very much.

Ms. HERDA. Thank you very much.

[Whereupon, at 3:30 p.m., the Subcommittee was adjourned.]

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