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# TELECOMMUNICATIONS POLICY REVIEW: LESSONS LEARNED FROM THE TELECOMMUNICATIONS ACT OF 1996

## HEARING

BEFORE THE

## COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION UNITED STATES SENATE

ONE HUNDRED EIGHTH CONGRESS

SECOND SESSION

APRIL 27, 2004

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SENATE COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION

ONE HUNDRED EIGHTH CONGRESS

SECOND SESSION

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# TELECOMMUNICATIONS POLICY REVIEW: LESSONS LEARNED FROM THE TELECOMMUNICATIONS ACT OF 1996

**TUESDAY, APRIL 27, 2004**

U.S. SENATE,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
*Washington, DC.*

The Committee met, pursuant to notice, at 9:30 a.m. in room SR–253, Russell Senate Office Building, Hon. John McCain, Chairman of the Committee, presiding.

## OPENING STATEMENT OF HON. JOHN MCCAIN, U.S. SENATOR FROM ARIZONA

The CHAIRMAN. Good morning. At the Committee's hearing on Voice-Over-Internet Protocol, or VoIP held earlier this year, I announced that the Committee was undertaking a series of hearings this spring on telecommunications policy.

Today's uncertain telecommunications policy landscape, brought largely by rapidly developing technology, outdated statutory framework that's not keeping pace, and Federal regulations mired in litigation requires us to reexamine the assumptions under which the Telecommunications Act of 1996 was put into law. The VoIP hearing in February was the first hearing in this series, and gave Members an opportunity to look at the catalytic role of technology in our increasingly outmoded telecommunications policies.

Today, we look at the Act and the lessons we can learn from it. I look forward to hearing testimony from some of the telecom industry's finest leaders as they take a look back at the last 8 years since passage of the Act to identify its successes and failures.

Tomorrow, we'll take a look ahead and hear testimony from industry analysts and former Federal and state regulators about their suggested revisions of telecommunications law, including alternative regulatory frameworks that we might consider in any future reform of telecommunications policy. We'll also hold at least one more hearing in the coming weeks to give industry executives opportunities to comment on these proposals and provide their own suggestions for the future.

As I've said many times before and will continue to remind my colleagues as we proceed down the path of the reform, the Telecommunications Act was a piece of legislation to a large degree written by lobbyists that freezes telecommunications policy in a bygone era already rendered obsolete by technology advances.

I look forward to working with my colleagues on the issue of tremendous national importance so that our legal framework for the next decade is not in fundamental conflict with the goals upon which our telecom policy is originally based, as stated in the Act's preamble, "to promote competition and reduce regulation in order to secure lower prices and higher-quality services for American telecommunications consumers, and encourage the rapid deployment of new telecommunications technologies."

I just also want to emphasize, much of the technologies that have been developed have blurred many of the distinctions between different types of telecommunications services. I don't think anybody doubts that. The VoIP illustrates that as much as any other, but there have been numerous technological changes in the way that all of our telecommunications is conducted throughout this nation and the world. So I think it's appropriate for us to be looking at the legislation that was passed in 1996 and see what we need to do in the future to conform with the new realities of telecommunications in America today.

Senator Hollings?

**STATEMENT OF HON. ERNEST F. HOLLINGS,**
**U.S. SENATOR FROM SOUTH CAROLINA**

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

Let me, at the outset, hail the success, generally, in large measure, the competition that has ensued and the reduction in prices. And since we've got one of the distinguished witnesses with us still, Mr. Dick Notebaert, and I'm going to have to leave a little bit early, I ought to try to use this for a question and try to catch him off base.

[Laughter.]

Senator HOLLINGS. But instead of catching him off base, let me quote Mr. Notebaert, in February 1996, "Mr. Chairman, the real and open competition this bill promotes will bring customers more choices, competitive prices, better-quality services. In one day, this industry has gone from 1934 to the year 2000 and beyond. We believe this bill will rank as one of the most important and far reaching pieces of Federal legislation passed this decade. It offers a comprehensive communications policy solidly grounded on the principles of a competitive marketplace. It's truly a framework for the Information Age . . ." and on and on. It's magnificent.

Well, I agree with Mr. Notebaert. In fact, Mr. Clendennon said that same thing to me. The very evening that I told him we had gotten together a conference report, he said, "That's outstanding," and that he would be in long distance within a year. They're not yet, 8 years later, to any real extent.

Now, what happens is that they started in, Mr. Chairman—because I'm very familiar with this thing—instead of going in, and everything else of that kind, they immediately petitioned the FCC to get into long distance in their region. We allowed them into long distance anywhere they wanted to go except where they had a monopoly. Those monopolistic prices and procedures were all designed by us, and it worked. America had, at the time, and still has, the best communications in the world, so nobody's fussing about that.

But they wanted to get into their region; when they couldn't get into it, they immediately said that the Act was unconstitutional.

After they went all the way to the U.S. Supreme Court with that nonsense, they then said, "Oh, it didn't refer to data," they wanted to get into data. Well, we showed where it was 428 times mentioned in the records and in the bill itself, data. So we had considered data.

Then they wanted to say, "Ooh"—they had a bunch of rural fellows on the Commerce Committee, so if we could just extend it to the rural new Chairman of the Committee—Committee's subcommittee, Communications Subcommittee—and the whole time, they came up saying, "We're just trying to get into rural. Got to serve rural." They were selling off their rural entities and holdings at the very time that they were saying that they wanted to get into rural. They have tried every trick in the book, and, as a result, they have been fined, Mr. Chairman, for anti-competitive conduct, to the tune of $2.6 billion—$2.6 billion—in fines in the last 8 years. Now, that's been our problem.

They just absolutely—the Bell companies have just put their feet down and locked themselves in, and, in essence, they have gotten into long distance, forbidding anybody to get into the local. Now, they can get into long distance, in the long-distance market. If a Bell wishes to lease or purchase long-distance lines all they need to do, if AT&T's price—they can negotiate with a host of providers—if AT&T's price is too high, the Bells can call MCI, Sprint, Level 3, or any other long-distance provider. So they can get in, the Bell companies, into long distance. But if a long-distance provider wishes to bundle local services with customer offerings, there's only one party he can negotiate with, and that's the local Bell. And if the wholesale price is too high, that's too bad.

And what is the Chairman of the bloomin' FCC tell them? "Go ahead and negotiate and work it out." Instead of the public, in the open, setting rates, we've got a Chairman at the FCC, says, "Y'all get together on the rates." And 57 million Americans' rates are on the way up under that procedure, I can tell you that right now. That's our problem.

I'll ask, Mr. Chairman, that my complete statement be included in the record, and I thank you for holding the hearing.

[The prepared statement of Senator Hollings follows:]

PREPARED STATEMENT OF HON. ERNEST F. HOLLINGS,
U.S. SENATOR FROM SOUTH CAROLINA

Today, the Committee once again reviews the telecommunications marketplace and, more specifically, what effect the market-opening provisions of the 1996 Telecommunications Act has had on consumers. As one who helped to author this law, I believe that it has played an important role in lowering consumer phone bills and in spurring the development of innovative communications services.

For the better part of two decades now, our nation has struggled to promote competition in the telecommunications marketplace. With Judge Greene's assistance in 1984, we took an important first step by breaking up Ma Bell into AT&T and the 7 regional Bell companies. At that time, fearing that the Bell companies might use their significant market power in local markets to subsidize their entry into new markets, Judge Greene restricted the bells from entering the long distance and manufacturing markets.

Seen in its proper context then, the 1996 Act was merely the next logical step in our nation's effort to free telecommunications markets from the stranglehold of monopoly power. Specifically, the idea was to allow the Bell companies to compete

in long distance markets, but to prevent them from providing "in region" long distance until after they had opened their local markets to competition.

We all had high hopes, particularly given that all the major companies were at the table and signed onto the Act. If everyone played by the rules and kept their promises, the goal would be accomplished. But unfortunately, the ink on the 1996 Act was hardly dry before the Bells sought to renege on the very bargain that they had struck.

First, they challenged the constitutionality of the law they helped draft. Second, instead of competing, the seven Bells combined into four monopolists that today control the overwhelming share of local access lines. Third, they used every trick in the book to avoid meeting their obligations to competitors, and have been fined for their anti-competitive conduct to the tune of $2.6 billion over the past 8 years.

The effect of this foot-dragging is pronounced—particularly now, since the Bells have been cleared to provide long distance services in all states. Indeed, eight years after passage of the 1996 Act, CLECs have acquired less than 15 percent of last mile lines. In contrast, since December 1999, when the FCC granted its first approval for Bell provision of "in region" long distance services, the Bells have been able to capture over 30 percent market share in long distance services—with Verizon now ranking as the third largest long distance provider. This disparity does not happen by accident. It happens because of continuing Bell resistance to FCC rules designed to open their local markets to competition.

The FCC's current "laissez faire" attitude toward ensuring competitive access is only making a bad problem worse. Reliance on "marketplace" negotiations to ensure competitive access to local loops won't work in the absence of a "market" to begin with. Consider the difference. In the long distance market, if a Bell wishes to lease or purchase long-distance lines to enable its offering of a local/long distance service "bundle" to its customer, it can negotiate with a host of providers. If AT&T's price is too high, the Bell can call MCI, Sprint, Level 3, or any other long haul provider.

In contrast, if a long distance provider wishes to bundle local services with its customer offerings, there is only one party that it can "negotiate" with—the local Bell. If the wholesale price offered by the Bell is too high, too bad.

Ultimately, this disparity highlights the problem with the FCC's current stance toward local competition and its recent call for additional marketplace negotiations over the price of access to local networks. In the abstract, there is nothing wrong with more negotiations. Indeed, parties may value the certainty of a negotiated price over the uncertainty of one set by regulation. But in the absence of alternative providers, we, as policymakers, should not allow the Bell Companies to unilaterally dictate the terms of local competition.

To protect the public interest, the FCC must take a firmer hand to ensure that the negotiation process is open and above board, and that all interconnection agreements reached by the parties are filed with the appropriate state regulators as required by law.

Eight years ago, Congress emphatically stated that it believed in competition. We should not abandon that belief. I Thank the witnesses for joining us today and look forward to their testimony on this vital issue.

The CHAIRMAN. Thank you very much, Senator Hollings.

Mr. Notebaert, a quote from your press release reminds me of my beloved friend, Morris Udall's politician's prayer, "May the words I utter today be tender and sweet, because tomorrow I may have to eat them."

[Laughter.]

The CHAIRMAN. Senator Stevens?

## STATEMENT OF HON. TED STEVENS, U.S. SENATOR FROM ALASKA

Senator STEVENS. Mr. Chairman, I welcome this hearing, and Mr. Dorman, Mr. Notebaert, and Mr. Geiger. And I do think we have to look back at the 1996 Act, but we have to look forward to see where we're going. And I do hope we have series of hearings that deals with the subject. As a matter of fact, I'd like to have some consensus meetings where we sit around the table and try to get the Members to understand the technology we're trying to deal

with before we rush in to find new ways to, you know, legislate regarding it.

But, Mr. Chairman, this morning is the memorial service for my late good friend, Daniel Boorstin, who was the former Librarian of Congress. As the Joint Committee Chairman, I must leave, and I do thank you for holding the hearings and look forward to the other hearings.

Thank you very much.

The CHAIRMAN. Thank you, Senator Stevens. And please extend our sympathies to his family. Thank you.

Senator Wyden?

**STATEMENT OF HON. RON WYDEN,**
**U.S. SENATOR FROM OREGON**

Senator WYDEN. Thank you, Mr. Chairman. And I, too, appreciate your holding these hearings.

It is extraordinary when you think, for example, that the 1996 Act barely mentions the concept of the Internet. We had all of these staggering changes in the last 8 years. It took 60 years to do the first rewrite. And now, all of a sudden, the last 8 years, as a result of technology, we've got to look again. And these are three areas that I have a special interest in and I would hope we take a look at.

The first stems from our hearing on voice-over. It's pretty clear that under the current Act, the rules focus on a particular type of service, but in the IP world, in the Internet Protocol world, different services are all just indistinguishable bits of data traveling over the same network. So my sense is, as we look to the future, what we really ought to be doing is trying to frame policy around the concept of a network, and try to really be agnostic with respect to services. So I hope that we'll pursue that idea.

The second area that I'd like to see us look at, Mr. Chairman and colleagues, is on the issue of universal service. It doesn't seem to me to make sense to keep pouring 100 percent of the subsidies into old-fashioned phone-only networks. And if the future phone service is over broadband, I want to make sure that my constituents have access to those kinds of services. And I would hope that we would look at making broadband the focus of universal service in the future.

Finally, the current Act makes lots of distinctions between interstate services and intrastate services, or between local and long distance, but these distinctions are also breaking down. A lot of phone companies now offer buckets of minutes that don't distinguish between local and long distance, so I would hope that we would look at this issue, as well.

The title of this hearing, Mr. Chairman, "Lessons Learned from the 1996 Act," it's pretty clear that one lesson is that monopolies do not get toppled overnight. So there is work to be done here, and I look forward, as you do, to working, as we've done in the past, in a bipartisan way.

The CHAIRMAN. Thank you.

Senator Burns?

## STATEMENT OF HON. CONRAD BURNS, U.S. SENATOR FROM MONTANA

Senator BURNS. Thank you, Mr. Chairman, and thank you for starting these hearings of hearings.

We've looked at the 1996 Act, and I welcome our guests this morning. I'm struck by Mr. Wyden's words that the Internet wasn't mentioned, and how can we distinguish signals? My gosh, we talked nothing but digital then. We knew we had emerging technology that you're not going to distinguish whether it's voice or data or whatever it is because it is a movement of numbers, ones and zeros. And that's going to—and we talked about that a lot.

In fact, there was a section put in that Act for buildout and the promotion of broadband throughout. I mean, you don't have to sit there and say "that's the Internet," as such. But we talked a lot about broadband services and digital technology in order to move—and fiber optics and all of these technologies that were coming. And so I think maybe we didn't hear the message when we were doing it because there was a lot of things flying around here at that time.

We've got two guests today, Mr. Dorman and Mr. Notebaert, and they do a lot of business in my state of Montana, and I would imagine—Mr. Dorman has run an Internet startup group, a joint venture between British Telecom and AT&T, and now AT&T. Mr. Notebaert now heads a company that was formed when a long-distance provider created in the wake of the 1996 Act through U.S. West. I suspect both of them did not perceive where they would be today in 1996 because of the evolution of the Act and the actions of people in the industry.

And I would say there is tremendous change in the communications, and most of it has been—in fact, the greatest majority of it has been—the consumer has been pretty well treated in this. Because we can look at prices of services now compared to 1996.

So the ongoing challenges faced by our witnesses here today in their own careers, in a sense, is indicative of what industry has been through over the past 8 years, massive and ongoing changes.

But it is time we looked at the Act and take a look in the rearview mirror just a little bit. But we'd better not take our eyes off of the future, because there's going to be some more changes out here before this is all over, and it is an evolution that we welcome. I think it's good for the consumers, I think it's good for the investors, and the possibilities are still unlimited in the IT and telecommunications industry.

And I thank the Chairman.

The CHAIRMAN. Thank you, sir.

Senator Lautenberg?

## STATEMENT OF HON. FRANK R. LAUTENBERG, U.S. SENATOR FROM NEW JERSEY

Senator LAUTENBERG. Thanks, Mr. Chairman. It's certainly appropriate to have this review.

I think so much that was said in those days, regardless of the understanding of the then-current technology, had aims that, it seems to me, are still unmet. We've got to take a look and see whether the 1996 Act is promoting or, in some manner—competition between providers that are necessary to produce the lower

prices and better service to the public. And, again, I think that that answer is still being debated, challenges all over the place. And I hope that we can make sense, ultimately, for the public interest, and that is to give them the services at the lowest prices possible. The 1996 Act opened local telephone markets to competition, thereby, we thought, doing away with the historical monopoly in the telephone business.

Now, my home state of New Jersey, the most densely populated state in the country, consumers have benefited from competition in local phone service. They can choose between Verizon, AT&T, MCI, Sprint, and other smaller independent carriers. As a result of this competition, over 800,000 New Jersey consumers have chosen carriers other than the Baby Bell carrier which had operated in a regulated monopoly environment for so many years. And I think this is a positive change.

Since the breakup of the Bell system in 1984, there have been substantial reductions in long-distance telephone rates, with charges plunging from nearly $3 a minute to less than 10 cents a minute. Similarly, as a result of the 1996 Act, American consumers now can choose from a host of unlimited local and long-distance bundled offerings and features for a flat rate of roughly $50 or $60 a month, which is not a modest sum by any standard. For instance, consumers can buy a plan that provides unlimited local and domestic long-distance calls, unlimited calls to Canada, and a choice of features, including caller ID, call waiting, repeat dialing, call forwarding, three-way calling, et cetera.

However, even with some competition, local telephone rates are still too high. Local telephone rates for New Jersey, which are regulated by the State Board of Public Utilities, have been frozen since 1985, but the subscriber line charge, which is set by the Federal Communications Commission, has more than tripled, from $2 in the late 1980s to anywhere from $6 to 9.50 a month in some states.

And even though the Act has been mired in legal challenges since its enactment, I think there is a consensus that Congress did the right thing by opening both local and long-distance telephone markets to competition. The disagreement is whether or not the 1996 Act has been properly implemented. And I hope that today's witnesses, especially Mr. Dorman, the Chairman and CEO of AT&T—headquartered in New Jersey, I might add—will clarify for us some of the implementation issues that we should consider addressing when it comes to the 1996 Act and telecommunications generally.

I thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

Senator Smith?

**STATEMENT OF HON. GORDON H. SMITH,**
**U.S. SENATOR FROM OREGON**

Senator SMITH. Thank you, Mr. Chairman.

It's clear, from comments of all my colleagues, that we've learned much from the 1996 Act, and many revisions are appropriate. I believe one of those is to fix a very serious inequity in the current

funding mechanism for the Federal Universal Service Program. It's currently unsustainable.

Universal service is based on the percentage of long-distance charges. But as our witnesses can attest, long-distance rates have fallen to almost nothing, and the distinction between long distance and local is vanishing. If we do not act soon, universal-service funding will soon fall short of its needs, and we cannot allow this to happen.

To cite another serious program in the Universal Service Program, it is supposed to help ensure affordable telecom services to the majority of rural Americans. It is grossly unfair, and needs to be reformed. The USF program for rural areas, served by larger carriers, excludes 40 states from eligibility, including Oregon, Arizona, South Carolina, Texas, Maine, Kansas, Illinois, Nevada, Louisiana, North Dakota, California, Florida, Washington, and many others; in fact, most of the states represented in this Committee.

I've introduced legislation to fix this program, and my bill has been endorsed by a broad bipartisan coalition of more than 50 independent groups and leaders. I appreciate your support on this issue, Mr. Chairman, and I'm also committed to seeing this inequity fixed sooner rather than later.

In sum, we've got a lot of work before us, and I applaud you for getting started, and look forward to our witnesses today.

Thank you, sir.

The CHAIRMAN. Senator Sununu?

Senator SUNUNU. I have no opening statement.

The CHAIRMAN. Senator Brownback?

**STATEMENT OF HON. SAM BROWNBACK,**
**U.S. SENATOR FROM KANSAS**

Senator BROWNBACK. I'm going to have to leave, Mr. Chairman, for a hearing on the appointment of Ambassador Negroponte to Iraq, so I apologize to the witnesses and to the Chairman. I'm going to have to leave for that shortly. But I think this is an important set of hearings that we need to engage.

Thank you.

The CHAIRMAN. Thank you.

Senator Lott?

**STATEMENT OF HON. TRENT LOTT,**
**U.S. SENATOR FROM MISSISSIPPI**

Senator LOTT. Thank you, Mr. Chairman, I ask consent that my statement be made a part of the record.

The CHAIRMAN. Without objection.

Senator LOTT. I want to thank you for having these hearings. I think, certainly, we need to be taking a broad look at this 1996 Act and begin thinking now about what we need to do to upgrade and modernize that Act to reflect what's happened. So much has changed since 1996, it's breathtaking, and so we have a responsibility to think about where the future is going to take us.

Thank you, Mr. Chairman.

[The prepared statement of Senator Lott follows:]

PREPARED STATEMENT OF HON. TRENT LOTT, U.S. SENATOR FROM MISSISSIPPI

Mr. Chairman, thank you for holding these important hearings this week in order for the Committee to begin the process of reviewing our nation's telecommunications policy. A consensus is developing to begin a comprehensive reassessment of telecommunications policy in our country, and as we move into the 109th Congress, this review seems likely to be one of our top priorities in this committee and in the Congress.

It is important to examine both the positive aspects of the 1996 Telecom Act, and any of its provisions which may not have been as productive as we had hoped, as we look ahead to new telecommunications legislation in the future. As one of the principal Senators involved in the passage of the 1996 Telecom Act, I have followed the implementation of this legislation closely and plan to be involved in the intricacies of this comprehensive review.

While only eight years have passed since the passage of the 1996 Act, significant changes have taken place in the telecom sector. Some of these changes were encouraged by the text of the 1996 Act, such as the opening of local telecom markets to competition and the reciprocal entry of the incumbent carriers into the interstate long distance business. I am pleased that Section 271 approval has been granted in every state. This development indicates that the various state public service commissions and the FCC have found that the requirements of the fourteen point checklist, which I helped to craft, are being met. As a result of the completion of the Section 271 approval process, consumers in every state now have more competitive options for both local and long distance service. Congress will need to carefully continue to assess the status of telecom competition as future decisions are made regarding the rules under which future competition will proceed.

Other changes that have taken place in the telecom sector during the past eight years have been driven by technological developments. Since the passage of the 1996 Act, the Internet has become a pervasive and indispensable piece of our communications network, with the rapid evolution from early dial-up service to broadband access today. As a result, now "Voice over Internet Protocol" promises to revolutionize the way calls are made in this country and throughout the world.

State-of-the-art upgrades have been made to the traditional wireline infrastructure in the country, including the cable industry's push to upgrade their systems to enable digital transmission. Furthermore, the wireless communications industry has grown and matured dramatically. These technological developments have blurred the historical lines between different types of telecommunications services, and Congress will need to carefully review the way regulatory policies are applied when the same or similar services are being offered over the various different distribution platforms in the telecom marketplace.

Additionally, there are other challenges which we will need to face as we consider new comprehensive telecom policy legislation. It is critical that telecommunication services remain universally available to all Americans. My home state of Mississippi is a rural state, and meeting the unique challenges and expenses in the provision of telecommunications services in my state has been made feasible because of the Universal Service Fund. Congress will need to thoroughly study the Universal Service Fund to insure that it is funded through a fair and stable framework, and to make certain that disbursements are made according to carefully defined priorities.

Mr. Chairman, there are many other aspects of telecom policy—in addition to those I have touched on today—that we will need to examine as we move forward on legislative action in the coming Congress. We should learn as much as possible from the past and the present as we seek to establish the best guidelines for the future in this important area of our economy. I am glad that we are beginning this important review, and I will look forward to hearing the testimony of the witnesses.

The CHAIRMAN. Thank you.

I want to welcome our witnesses today, Mr. David Dorman, the Chairman and Chief Executive Office of the AT&T Corporation; Mr. Richard Notebaert, Chairman and Chief Executive Officer of Qwest Communications; and Mr. James Geiger, Chief Executive Officer, Cbeyond Communications.

I want to welcome the witnesses today. I thank you for taking the time from your schedules to be with us.

And we'll begin with you, Mr. Dorman, and thanks for coming back.

**STATEMENT OF DAVID DORMAN, CHAIRMAN AND CEO, AT&T CORPORATION**

Mr. DORMAN. My pleasure.

Mr. Chairman, Senator Hollings, and Members of the Committee, thank you very much for inviting me to speak with you today.

At AT&T, we do see a bright future for the telecom industry, as long as competition remains the guiding principle and pro-competition rules are enforced in a stable and predictable manner.

My message to you today is that, whatever one thinks about the 1996 Act, it has begun the very challenging process of opening the telephone exchange market to competition. Competition, thus far, has brought consumers billions of dollars in savings that would not otherwise have been possible.

The D.C. Circuit's recent decision invalidating the FCC's pro-competitive framework poses a mortal threat to this progress. Left in place, that decision could harm millions of consumers and businesses, eliminate thousands of jobs, and hamper investment in new technologies.

The goals of the 1996 Act have proven more difficult to attain than many of us had hoped; but they should be reinforced, not abandoned. Any changes to the Act must preserve the consumer benefits already realized today, and assure that competitors have sufficient customer base to allow investment in and widespread deployment of innovative new technologies, especially Voice-over-Internet Protocol, or Voice-over-IP.

Voice-over-IP holds great promise, but ensuring the appropriate regulatory framework for VoIP is critical. VoIP must be allowed to develop free of burdensome regulation. The intercarrier compensation and universal-service systems must be reformed to ensure that universal service is preserved and that all providers contribute on a fair, nondiscriminatory, and technologically neutral basis without requiring innovative competitors to contribute disproportionately or otherwise subsidize old technologies or incumbent carriers. Let me provide more detail on each of these points.

The Telecom Act of 1996 had the extraordinary and unprecedented goal of eliminating monopoly in the local exchange. Congress did not, however, predict and protect against factors that have complicated competitive entry. The Bells consolidated into four much larger companies, and resisted attempts to implement the pro-competitive provisions of the Act. Access to capital became seriously constrained after the burst of the dot-com bubble, and fraud crippled the industry.

We've done our best to surmount these barriers and become a viable player in the market for local telephone service. Today, AT&T provides local service to more than 4.3 million residential lines and 4.5 million business lines, including one million small-business lines. We do so through a combination of facilities-based entry and the lease of Bell network elements, which are two of the three competitive pathways established by the 1996 Act.

We've invested over $26 billion in our own local facilities since 1996, and we've invested tens of billions more in our long distance, network, cable, and wireless facilities. Facilities-based service, however, requires a significant customer base to be economic and to re-

duce the risk of network deployment. Until we can develop that local customer base, a strategy that relies solely on facilities-based competition is simply not feasible. UNE–P provides a stepping stone to facilities-based competition by enabling competitors to build scale needed to deploy facilities wherever possible.

Competition has meant more choices, better service, and lower prices for tens of millions of consumers. In response to competition, the Bells have had to lower their prices, often for the first time, and sometimes by as much as one third. Consumers and small businesses are savings billions of dollars annually because of competition. Competition has also resulted in bundled services. Bear Stearns recently estimated that over 52 million consumers in competitive markets have switched to one-stop shopping bundles of service, at a savings in the range of $7 billion per year.

Despite their rhetorical support of facilities-based competition, the Bells have repeatedly tried to eliminate UNE–P. As a result of a lawsuit initiated by the Bells, the Court of Appeals for the D.C. Circuit in March in validated the FCC's rules, ensuring that competitive carriers can lease unbundled network elements, when they otherwise would be unable to compete effectively in the local markets. The decision sets a nearly insurmountable presumption against competitors seeking to use these unbundled elements.

The Bells were also successful in their efforts to uphold the FCC rule eliminating competitors' access to broadband facilities, a ruling that will impair broadband competition and inhibit competitors' ability to invest in facilities for voice competition.

We do not like being dependent on a reluctant supplier for our critical service inputs. Until we're able to move to alternatives, however, we remain dependent on the Bells for leased use of their network. We have tried for years to negotiate access to these facilities commercially, and we continue that effort today, particularly given the FCC Commissioner's recent request that we engage in intensive efforts during a 45-day timeout in the legal proceedings. Given the Bells' persistent market power, these negotiations will be challenging, but AT&T is committed to pursuing the hope of preserving competition in the local market. We are negotiating in good faith to secure economically reasonable rates that allow us to continue providing competitive local service alternatives to customers.

While Mr. Notebaert and Qwest, commendably, have stepped forward to agree to the presence of an arbitrator, the remaining Bell companies have not, which could make a satisfactory outcome more difficult. Indeed, I'm afraid that there is a misconception among some about the purpose of these negotiations. These negotiations must not be about ending mass-market telephone competition, and AT&T will not accept wholesale rate increases that achieve that end. Rather, we believe that current negotiations are intended to find mutually acceptable commercial wholesaling arrangements that permit competition to continue, and facilitate a transition to facilities-based competition, wherever feasible. That is our focus in the negotiations, and that is what would best serve our nation.

It is critical that the government retain the option of Supreme Court stay and review of the D.C. Circuit decision. The decision is wrong as a matter of law, and it's bad policy for this Nation. The prospect of Supreme Court review of that decision is the most sig-

nificant reason for the Bell companies to negotiate right now. The stakes for consumers, small business, and my company, AT&T, are too high to risk a court vacatur of the FCC rules in hopes that the Bell companies, after 8 years of opposition, will negotiate commercially reasonable access arrangements. Given this Committee's long history of promoting competition, your support at this time to ensure that this decision can go to the Supreme Court if negotiations fail is absolutely critical.

Failing to reach a commercially reasonable agreement, and failing to appeal, would return consumers to the monopoly environment that existed before the 1996 Act, and would carry a heavy price. It would mean disconnecting millions of homes and businesses from their chosen carrier, taking away lower prices and more responsive services those customers gained from their choice, and the loss of a significant driver for our economy—competitive incentives to deploy and promote the use of broadband.

The importance of pro-competitive policies also go beyond today's greater choices and lower prices. Carrier's incentives to invest in new technology and services are substantially diminished by regulatory instability or market dominance by a given provider. Creating an environment in which companies feel confident to invest and deploy new service is particularly critical now, when existing new technologies, or exciting new technologies like Voice-over-IP, are emerging.

VoIP holds the promise of choices and capabilities far beyond today's offerings. It may very well be that a killer application could drive widespread broadband adoption for which we've all waited. And an important step to our nation's economic revival. A recent study concluded that Voice-over-IP could save the government alone three- to ten-billion dollars annually, up to 60 percent of their current phone bills.

I must add that we should not think of Voice-over-IP as simply cheaper phone service. It will deliver lower cost, but with a host of new user features and options that go well beyond the notion of "plain-old telephone service," or POTS.

If competitors cannot remain in the market today, they will not be able to maintain the scale to make this service a broad reality in the near future. And without the threat of losing customers to a VoIP rival, the Bells will have no incentive to invest in and deploy this new technology themselves.

AT&T fully intends to lead the Voice-over-IP revolution. We have invested heavily to make the necessary changes to our network, some three billion in 2003 alone. We already provide Voice-over-IP service to hundreds of businesses, and we have become commercial deployment to consumers. We have announced that we will provide VoIP service in the top 100 markets in the country this year. But without UNE–P, we cannot retain and grow our customer base; and without a stable customer base, Voice-over-IP deployment would become riskier and most costly.

AT&T welcomes the fact that Members of this Committee and Congress, such as Senator John Sununu and Congressman Chip Pickering, support a hands-off approach to VoIP. We recognize that providers of VoIP services must meet important social policies. Access for the disabled, enabling public safety, 911 response, and the

need for law enforcement to trap and trace calls when necessary are technical and operational issues that the industry can resolve, and AT&T is taking the lead in resolving them.

Let me also assure the Members of this Committee that nothing about VoIP threatens universal service. The problem with the Universal Service Fund is, it is supported by a shrinking base of interstate revenues, as Senator Smith suggested, for traditional telecom services. A growing fund with a shrinking base cannot be sustained. We think Voice-over-IP providers should contribute to universal service in a sustainable, fair, and nondiscriminatory manner.

There are no fewer than six access-charge methods in place for the use of the Bells' local networks. These differences create a range of unintended consequences, including favoring classes of technologies and competitors over others. The largest threat to VoIP is the application of 20th century access charge regulations to a 21st century technology. The access-charge scheme was developed decades ago, and just doesn't work today. The FCC has promised for years to overhaul its intercarrier compensation regime, but it continues to address these issues on a piecemeal and discriminatory basis.

The far-better course would be a comprehensive reform of intercarrier compensation and universal-service regimes to eliminate market distortions and opportunities for regulatory arbitrage while protecting and advancing this nation and my company's proud heritage of universal service.

In conclusion, Mr. Chairman, this Committee has a long commitment to promoting competition. You and your colleagues have provided the leadership necessary to move the telecommunications industry from the notion of natural monopoly to real competition. Today, we must call upon your leadership again. The competitive vision of the Telecom Act is being fulfilled, but it needs the continued support of lawmakers and regulators if all of its ambitious goals are to be met. If local markets remain open to competition, consumers, businesses, and the American economy can all win.

Thank you, again, for inviting me here today, and I look forward to your questions.

[The prepared statement of Mr. Dorman follows:]

PREPARED STATEMENT OF DAVID DORMAN, CHAIRMAN AND CEO, AT&T CORPORATION

Mr. Chairman, Senator Hollings, and Members of the Committee, thank you very much for inviting me to speak with you today regarding AT&T's view of the state of competition eight years after enactment of the 1996 Telecommunications Act. At AT&T, we see a bright future for the competitive telecommunications industry as long as competition remains our guiding principle and pro-competition rules are enforced in a stable and predictable manner.

I speak to you today from a unique perspective. When the Act was passed, I headed Pacific Bell, one of the incumbent Bell companies that today is part of SBC. In the post-1996 Act environment, I spent almost two years at PacBell and SBC, and have been with AT&T since December 2000. So I have seen how the Act's passage has affected the Bells, and how its implementation has affected the competitors.

My message to you today is that whatever one thinks of the 1996 Act, it has begun the very valuable process of opening the telephone exchange market to competition. It is indisputable that competition has brought residential and small business customers savings and choices that would not have been possible without the Act. Studies have shown that the competition produced by the Act has resulted in

savings to consumers and businesses of billions of dollars per year. The D.C. Circuit's recent decision invalidating the FCC's pro-competitive framework poses a mortal threat to this progress, however. Left in place, that decision could harm millions of consumers and businesses, eliminate thousands of jobs, and hamper investment in new technologies.

The goals of the 1996 Act have proven more difficult to attain than many of us—and many of you—may have hoped, but that means they should be reinforced, not abandoned. Any changes to the Act must maintain a strong, pro-competitive framework to preserve and extend the consumer benefits realized today, and to ensure that competitive national carriers have a sufficient and growing customer base to allow and justify our investment in and widespread deployment of innovative new technologies and services, especially Voice over Internet Protocol ("VoIP").

Firm resolve in enforcing the pro-competitive policies of the 1996 Act is a necessary first step on the path to VoIP, but ensuring the appropriate regulatory framework for VoIP itself is equally critical. VoIP must be allowed to develop free of burdensome regulation. In particular, the FCC should be encouraged to resist the insistence of the Bell companies—by far the largest telephone companies in the country—that they need subsidies in the form of inflated access charges from nascent VoIP providers. The intercarrier compensation and universal service systems must be reformed to ensure that universal service is preserved while at the same time not requiring new and innovative competitors to contribute disproportionately to universal service or otherwise subsidize incumbent carriers.

Let me provide more detail on each of these points.

**Attaining the Ambitious Goals of the 1996 Telecommunications Act Has Proven Difficult**

At its core, the Telecommunications Act of 1996 had an extraordinary goal. It sought to eliminate monopoly in the local telephone exchange, the last mile facilities that connect virtually every home and business to the public switched telephone network.

To achieve the goal of local competition, the Act offered the incumbent local telephone monopolies a remarkable trade. In exchange for opening their local monopolies to competition in accordance with a "competitive checklist," the Bell telephone operating companies would be permitted to enter into markets from which they had previously been excluded. It was widely believed that granting the Bells a clear path to provide wireline long distance services would give them the incentive to open their local markets to competition. The demonopolizing of local service and Bell entry into long distance was the mutual *quid pro quo.*

Creating a competitive local market, however, proved more difficult than first imagined. Building a local telephone network with no subscribers to fund that construction is incredibly risky and technically challenging. Entering a business in competition with an established provider whose network has ubiquitous capacity and was built with ratepayer funds at a guaranteed profit is even riskier. Indeed, even in 1996 many believed that local telephone service was a natural monopoly.

Recognizing the difficulty new entrants would face, Congress established several pathways for competitive entry. The Act allowed providers to interconnect their networks with those of the incumbents, to lease unbundled network elements ("UNEs") from the incumbents, and to resell the services of the incumbents.

Congress did not, however, predict and protect against factors that have complicated competitive entry. The Bells have resisted and challenged nearly every attempt to implement the pro-competitive provisions of the Act. They have spent years playing their two hole cards—price and process. And with them, they've largely managed to keep competitors out of their monopoly. Their strategy of resistance, delay, and litigation has enabled them to maintain their dominance of the local telephone market, while dozens of their competitors have been forced out of business.

Further, Congress could not have predicted that the Bells would become even more formidable opponents in the few years after the Act was passed. Rather than enter each other's territories to compete, as Congress anticipated, the seven Bell companies have consolidated into four, much larger companies wielding even more market power. Nevertheless, the FCC has granted the Bells the enormous competitive benefit of long distance entry in every state. To obtain that authority, the Bells relied upon the ability of competitors to use leased network elements—the very competition they now seek cynically to eliminate—as evidence of the competition that was a predicate of their first being allowed to enter the long distance market.

Other events, too, have made competitive entry more difficult. Access to capital has become seriously constrained. The enactment of the 1996 Act spurred investment in new telecommunications facilities and services far exceeding the historical norm. From 1980 to 1995, the industry average investment was $38.8 billion annu-

ally and there was an average annual investment growth rate of 2.8 percent. Investment after the Act passed soared—growth averaged 22.3 percent annually and the industry invested on average $95.3 billion per year. In the year 2000, competitive carriers' capital expenditures totaled nearly 64 percent of their revenues. The burst of the dotcom bubble essentially eliminated access to needed capital, however. Numerous competitors declared bankruptcy or shut down operations. For many of those that continued, stock prices plunged. While telecommunications companies captured an average of two billion dollars per month in initial public offerings in 1999 and 2000, they virtually ceased to be able to raise money in IPOs in 2001. As competitors scaled back their plans, consumers were left with fewer choices.

In addition, fraud has crippled the telecommunications industry. Competitors were significantly harmed at an already difficult time for the telecommunications industry by fraudulent practices that overstated both profitability and demand for long-haul telecommunications facilities and services. This led to crippling overcapacity, cost investors tens of billions of dollars, and imposed incalculable costs on the industry and the economy. At bottom, the confluence of events caused a severe misallocation of resources and investment throughout the telecommunications industry that has forever changed the complexion of the marketplace.

**AT&T's Experience**

At AT&T, we have done our best to surmount these barriers and become a viable player in the market for local telephone service. I am pleased to say that today we provide local service to more than 4.3 million residential lines and 4.5 million business lines, including 1 million small business lines. We have done so through a combination of facilities-based entry and the lease of Bell network elements, both means established by Congress in 1996 and rules crafted by the FCC as instructed by the Act.

First, we have invested billions of dollars in our own local facilities since 1996. In 1998, we purchased Teleport, a facilities-based competitive local service and access provider, for $11 billion to provide local and long distance service to enterprise customers. Since then, we have spent an additional $15 billion dollars on local facilities. As of September 30, 2003, we had invested in 158 local voice switches, 20,600 route miles of metropolitan fiber, and 8,400 fiber rings in 67 metropolitan statistical areas covering 91 cities in 49 states. All these investments have made AT&T the largest facilities-based competitive local exchange carrier in the country in terms of revenue. Further, all these sums are in addition to the tens of billions we invested in our long distance network, cable and wireless facilities.

In both the business and residential markets, however, facilities-based service requires a significant concentration of demand to be economic. To the extent multiple networks can ever economically compete, a significant customer base is needed to justify network deployment and reduce the risk of such deployment. Until we can develop that local customer base, a strategy that relies solely on facilities-based competition is simply not economically feasible. MCI and Sprint recognized this 25 years ago when they entered the long distance business by reselling AT&T's service. For the same reason, the Bell companies today are using the networks of AT&T and the other established interexchange carriers to offer long distance service rather than waiting to build their own long haul facilities.

There are other substantial challenges to facilities-based competition. Eight years after passage of the Act, the Bells still have substantial unique advantages over competitors in providing facilities-based service. For instance, only the Bells enjoy unfettered use of the public rights-of-way in most places, while a competitive carrier must negotiate—often over many months or even longer—a rights-of-way agreement with the municipality in which it seeks to provide service before it may even begin building its network. The Bells also have exclusive access to many multi-tenant buildings and have access to capital at much lower interest rates than new entrants. All these disparities between the incumbents and their competitors give the incumbents a substantial cost advantage over new entrants.

In the face of these economic challenges and the incumbents' legacy advantages, the only viable means of competitive local market entry in the mass market has proven to be the lease of capacity on the incumbent carriers' networks. Leasing unbundled network elements from the Bell companies and using them to create and assemble our own innovative service packages has allowed AT&T to remain in the market even as many others have failed.

The same has proven true for the rest of the competitive industry. The majority of competitors that have survived in the mass market are using UNE–P. UNE–P also provides the stepping stone to facilities-based competition by enabling competitors to build a customer base that justifies investment in facilities. Despite their rhetorical support for facilities-based competition, the Bells' repeated efforts to

eliminate UNE–P will eliminate this essential first step and with it the most meaningful prospect of facilities-based competition in the future.

As a result of a lawsuit initiated by the Bells, the Court of Appeals for the D.C. Circuit in March invalidated the FCC's rules ensuring that competitive local telephone companies can lease UNEs when they otherwise would be impaired in their ability to compete in local markets. In fact, the D.C. Circuit appears to have set a nearly insurmountable presumption against competitors seeking to use UNEs, driven by its view that—notwithstanding the mandate of Congress in the Telecommunications Act—local competition based on unbundled access rather than ownership of local facilities is "synthetic" and deters investment in telecommunications facilities. The D.C. Circuit decision is wrong. It blatantly contradicts two Supreme Court decisions that explicitly rejected arguments that the Act elevates facilities-based competition over other entry methods and that leased use of the network deters investment by competitors or the Bells as "fundamentally false." The Solicitor General and the Antitrust Division of the Department of Justice also have already rejected the D.C. Circuit's interpretation of the Act, arguing that it failed to "accord appropriate deference to the FCC's reasonable interpretation of a complex statute" and substituted a standard that creates an "unwarranted restriction on the FCC's implementation of the Act's network element provisions" that is "in tension with other provisions of the Act" and "not compelled by statutory text." The Solicitor General also has noted that the "job of judges" is "to ask whether the Commission made choices reasonably within the pale of statutory possibility in deciding what and how items must be leased," not to substitute its own policy views for those of Congress.

Likewise, the Bells were successful in their efforts to uphold the FCC rule eliminating competitors' access to broadband facilities—a ruling that will not only impair broadband competition but also significantly inhibit competitors' ability to invest in facilities for voice competition.

In fact, while the Bells claim that they welcome competition from facilities-based competitors, they regularly stifle attempts to construct such facilities. Just this month, Qwest engaged in a tremendous lobbying effort to halt Salt Lake City and other Utah municipalities from joining the Utah Telecommunication Open Infrastructure Agency ("UTOPIA"). UTOPIA is a government agency formed by 18 Utah cities to build a fiber-optic network that would provide Internet, telephone and TV access directly to households in member cities. AT&T and other competitors could lease space on the UTOPIA network rather than the Bell network, freeing Qwest of the need to allow AT&T access to its local facilities. Qwest, however, has done everything it can to secure opposition to the project, including promising to accelerate its DSL deployment in the area to 90 percent of homes. The Bells do not want facilities-based competition; they want to keep their monopoly.

Until we or others are able to build more of our own facilities, however, we remain dependent on the Bells for leased use of their network. For more than eight years, we have tried to obtain access to these facilities through commercially negotiated arrangements pursuant to sections 251 and 252 of the Act, and we continue that effort today, particularly given the recent request of the FCC Commissioners to engage in intensive negotiation efforts during a 45 day "time out" in legal proceedings. Given the Bells' persistent market power, these negotiations will be challenging. While the sale of wholesaling capacity is today a major revenue contributor to long distance and wireless companies where vibrant competitive markets exist, the Bells with retail market shares of 90 percent are most reluctant wholesale providers. Even as the largest customer of each of the Bells, we rarely see any effort by them to ensure that we are a loyal wholesale customer.

Nevertheless, AT&T is committed to pursuing any process that offers the hope of preserving competition in the local telecom market. I have designated our two most senior operating executives to handle the Bell negotiations, and I am reviewing their progress daily. Despite the challenges, we are negotiating in good faith to secure economically reasonable rates that allow us to continue providing competitive local service alternatives to customers.

AT&T has always preferred the business commitment of a fair commercial agreement over regulatory uncertainty. In fact, I called for such an approach in a speech before the American Enterprise Institute only last September. We're hopeful that the Bells will recognize, as we did in the long distance market, that a robust wholesale business is good for them. We hope that the FCC's call for genuine, good-faith negotiations will provide all parties with the proper incentives to create commercial arrangements that preserve competition and benefit consumers. At the same time, the government must retain the option of Supreme Court stay and review of the D.C. Circuit decision. The D.C. Circuit decision is wrong as a matter of law and bad policy for this nation. It is inconsistent with the Telecommunications Act and the Supreme Court's interpretation of the Act. Moreover, I believe that the prospect of

Supreme Court review of that decision is the most significant reason for the Bell companies to negotiate right now. The stakes—for consumers, small businesses, and AT&T—are simply much too high to risk a court vacatur of the FCC's rules in the hopes that the Bell companies, after eight years of opposition, will negotiate commercially reasonable access arrangements.

**Consumers Benefit From Competition**

While certainly not perfect, the 1996 Act represented an important shift in telecommunications policy that began the long process of opening the local monopoly to competitive entry. Competition has meant more choices, better service and lower prices for tens of millions of consumers. There are now more than 19 million UNE lines serving consumers and small businesses. Consumers and small businesses save close to $11 billion dollars annually. While the benefits to date have not met your expectations or ours, they would not have been realized without the Act. In response to competition, the Bells have had to lower their prices, often for the first time, and sometimes by as much as one-third.

Competition has also led providers to offer bundled services. In response to bundled offers from competitors, the Bells now offer bundled local and long distance service in all of their states, to about 85 percent of all American households. They offer bundled local and high-speed Internet (DSL) service to nearly three-quarters of all U.S. households. Bear Stearns recently estimated that the number of consumers in competitive markets that have switched to one-stop-shopping "bundles" of services is over 52 million.

Bundled services—both local and long distance—are often available for a flat "all you can eat" fee per month, rather than traditional per-minute charges. Estimates point to 30 percent savings where bundled offers are in the market, and suggest that consumers of bundles save in the range of $7 billion per year. So while the Act might not be perfect, there is no doubt it is delivering real and otherwise unachievable benefits to consumers and small businesses today.

**Encouraging Investment Will Bring Emerging Services to the Marketplace**

To preserve these benefits for consumers, it is imperative that Congress and the FCC renew their commitment to the pro-competitive policies that have given millions of residential and small business customers choice and billions of dollars in savings.

Staying the course on competition means resisting the incumbent providers' calls to repeal the market-opening reforms of the 1996 Act. It also means rolling back the FCC's decision to eliminate our ability to use UNEs to provide the broadband services that customers increasingly demand. Lack of access to broadband facilities will impede our ability to offer bundled voice and data services, putting us at a disadvantage vis-à-vis the incumbent Bell companies, at least in the short term during the incubation period of nascent technologies like Wi-Fi, WiMAX and broadband over power lines.

Clearly, there are those who would return consumers to the monopoly environment that existed before the 1996 Act. A move backwards—whether through regulation, legislation, or judicial order—would carry a heavy price. It would mean:

- disconnecting millions of homes and businesses from the carriers those customers chose to provide them with competitive phone services;
- taking away the lower prices and more responsive services those customers gained from their choice;
- taking away the benefits of lower prices and more responsive service from Bell customers once the threat of competition is removed;
- permitting the remonopolization of consumer and small business telecommunications (unless policymakers are willing to expel the Bells from the long distance market and restore an antitrust standard that keeps them out until they face market-disciplining facilities-based competition); and
- the loss of a significant driver for our economy—competitive incentives to deploy and promote the use of broadband—at a time when our Nation can least accommodate it.

The far better choice is to encourage existing competition. The importance of pro-competitive policies goes beyond today's greater choices and lower prices. The incentives of companies like AT&T—or even the Bells—to invest in new services and technology are substantially diminished by marketplace instability. Creating an environment in which U.S. companies feel confident to invest and deploy new services is particularly critical now, when exciting new technologies are emerging. Let me stress that we do not regard UNE–P as a panacea. We do not like being dependent

on a reluctant supplier for our critical service inputs, and we are highly motivated to escape our dependence on the Bells.

**VoIP Holds the Promise of New Choices and Capabilities**

While UNE–P and circuit-switched facilities are the "now" for competitors serving mass market consumers, VoIP is the future. VoIP holds the promise of choices and capabilities far beyond today's offerings. It will enable consumers to tailor their communications services to their needs and lifestyles at competitive prices and with important enhanced security benefits. It very well could be the "killer app" to drive widespread broadband adoption for which we have all waited. It could also be an important step to our Nation's economic revival. With VoIP, voice service is just another "hosted application," like e-mail, so customers can take their phone numbers wherever they go and access connections over any device, such as a standard home telephone, wireless phone, or computer. The Alexis de Tocqueville Institution recently concluded that government at all levels could save $3–10 billion annually—up to 60 percent of their current phone bills—by replacing circuit-switched service with VoIP.

VoIP has potential applications in all segments of the communications industry—in the enterprise market; on customers' premises, replacing old and costly PBX systems; in international service, where the FCC has recognized VoIP's value in bypassing high foreign settlement rates; and in private IP-and Internet-based networks, where AT&T and others are deploying VoIP technology. As the service develops, these deployments will continue to expand, enabling America's businesses and consumers to enjoy the benefits of voice, video and data services over one secure network. I must add that you should not think of VoIP as "cheap phone service." It promises to be lower-cost, yes, but with a host of new user features and options that go well beyond today's "POTS."

But if national carriers cannot remain in the market today, they will not be able to generate the revenues they need to make the investments necessary to make this service a reality in the near future. VoIP will be yet another technology controlled by the Bells—who held back DSL from consumers for some ten years so customers would have to take their other, higher priced services. It was only when cable operators deployed cable modem service that the Bells responded with a mass-market, high-speed Internet access service of their own. Similarly, without the threat of losing customers to a VoIP rival, the Bells will have no incentive to invest in and deploy this new technology, preferring to milk the legacy assets as long as possible. Competitors will spur investment by the Bells, not deter it.

AT&T fully intends to lead the VoIP revolution for businesses and our customers. We have invested heavily to make the necessary changes to our network—some $3 billion in 2003 alone. We are already providing VoIP service to hundreds of business customers, and we have begun commercial deployment of a broadband consumer VoIP offering. We have announced that we will be providing VoIP service in the top 100 markets in the country this year. But without UNE–P, we cannot retain and grow our customer base—and without a stable, mass market customer base, VoIP deployment would become riskier and more costly. Clearly, it will take much longer to reach wide penetration.

**VoIP Must Be Appropriately Regulated**

Ensuring the continued availability of UNE–P and facilities-based competition will promote the widespread availability of VoIP. Equally important are the decisions that Congress and the FCC make about the regulation of VoIP itself.

AT&T believes that VoIP should be allowed to develop in the marketplace. We welcome the fact that many Members of this Committee and Congress, such as Senator John Sununu and Congressman Chip Pickering, support a "hands off" approach to VoIP and have introduced legislation that would bring the benefits of competition and innovation to the telecommunications marketplace. Senator Sununu and Congressman Pickering's deregulatory approach to VoIP both acknowledges the need to reform the current subsidy system and allows this nascent service to flourish.

AT&T strongly supports this approach. Allowing emerging services to develop free of unwarranted, legacy regulation allows carriers to design the service to respond to customer needs and interests, and to remain flexible in their business plans as customer preferences emerge, rather than be bound by a government-dictated vision of what the service should include and what is a benefit to consumers.

We recognize, however, that providers of VoIP services must also meet important social policies. Access for the disabled, enabling public safety (911) response, and the needs of law enforcement to trap and trace calls when necessary are technical and operational issues that the industry can resolve, and AT&T is taking the lead to resolve them. And government has a legitimate role in ensuring this gets done. In-

deed, the enormous flexibility and power of VoIP promises to address these issues in ways superior to current circuit-switched technology.

Let me assure the members of this Committee that nothing about VoIP threatens universal service. The problem with the universal service fund (USF) is that it is still supported by a shrinking base of interstate revenues for traditional telecommunications services. A growing fund with a shrinking base cannot be sustained. It's long past time for the universal service systems in this country to be reformed, and we support VoIP being part of the broader reform of the USF system. We think VoIP providers should contribute to universal service—in a sustainable, fair, and nondiscriminatory manner. For example, basing contributions on telephone numbers or connections would broaden the base of contribution and assess it on voice communications regardless of underlying technology.

The largest threat to VoIP, however, comes from an effort to apply 20th century access charge regulations to 21st century technology. The access charge scheme was developed decades ago to ensure that whenever a long distance company used the local network, it would subsidize local service by paying grossly inflated rates to the local carrier. While there was much in this framework to which one could object, it remained workable as long as local carriers and long distance carriers operated in separate markets. Its infirmities became apparent and unsustainable when those carriers entered each others' markets, and even more so when the principle outside users were no longer long distance companies, but wireless companies and ISPs.

For that reason, eight years ago, Congress ordered that implicit subsidies, including those in access charges, must be eliminated. Unfortunately, they still remain in place eight years later. And while the FCC has promised for years to overhaul its intercarrier compensation regime—and FCC Chairman Powell has called the regulations "a mess"—it continues to address these issues on a piecemeal and discriminatory basis. The far better course would be comprehensive reform of the intercarrier compensation and universal service regimes in ways that eliminate market distortions and opportunities for regulatory arbitrage while also protecting and advancing this nation's proud heritage of Universal Service.

The Bells, realizing that VoIP could replace the switched long distance calls that bring them these inflated revenues, have seized on this inaction and are calling for VoIP providers to subsidize them as well, even though VoIP providers already pay the local companies directly for use of their networks. It is ridiculous to ask emerging providers of this nascent technology to subsidize monopolists many times their size operating in the same market. If we require the new grocer in town to subsidize the supermarket, we are not going to see many new grocers. Internet access flourished in this country in part because Internet service providers were not saddled with payment of access charges. The incredible growth of wireless services was helped substantially by the fact that wireless carriers pay far less in access charges than wireline competitors. The same approach will promote the widespread availability of VoIP.

AT&T agrees that affordable service needs to be maintained in high-cost areas of the country. Applying the legacy access charge regime to VoIP, however, is not the way to achieve this result and would prove counterproductive and market-distorting. It simply slows the deployment of new and desirable technologies while driving users away.

* * *

Mr. Chairman, this Committee has a long commitment to promoting competition and securing for consumers the benefits of choice and lower prices that competition can bring. You and your colleagues have provided the leadership necessary to liberate the telecommunications industry from the shackles of the monopoly era. Today we are at a crossroads where we must call upon your leadership again. The competitive vision of the Telecom Act is being fulfilled, but it needs the continued support of lawmakers and regulators if all its ambitious goals are to be met. If local markets remain open to competition, consumers, businesses and the American economy can all win.

Thank you again for inviting me here today, and I look forward to your questions.

The CHAIRMAN. Thank you very much.

Mr. Notebaert, welcome.

**STATEMENT OF RICHARD C. NOTEBAERT, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, QWEST COMMUNICATIONS**

Mr. NOTEBAERT. Thank you, Mr. Chairman and Members of the Committee. I appreciate this opportunity——

The CHAIRMAN. Would you like to respond to Senator Hollings' quotation from your press release before you——

[Laughter.]

Mr. NOTEBAERT. Senator, it didn't sound like a question.

[Laughter.]

Mr. NOTEBAERT. I appreciate this opportunity to offer a brief overview of the Telecommunications Act of 1996. I'll do that from the perspective of my experience at Ameritech, which I led when this legislation was passed; at Tellabs, a Chicago-based telecom equipment manufacturer; and now at Qwest, the incumbent local-exchange provider in 14 western states that also offer services, including long distance and enterprise systems, throughout the United States.

In 1996, we had high hopes for this legislation; not that the Act was everything we hoped, but that it would finally provide progressive, consistent national telecom policy, rather than the antiquated 1934 legislation then in place. We welcomed competition and the chance to enter new markets, and we were eager for reform. We thought this bill offered real promise, beginning with its very first line, and I quote, "The purpose of the Act is to promote competition and reduce regulation."

I'm here today to suggest some reasons why, in my view, of that opening line failed, but I'll do so very briefly, mindful of the words of the great philosopher, Tommy Lasorda, who said, and I quote, "I've found it's not good to talk about my problems. Eighty percent of the people who hear them don't care, and the other twenty percent are glad I'm having trouble."

[Laughter.]

Mr. NOTEBAERT. Mr. Chairman, if I boiled down where we think the Act went wrong, it would be in three areas. First, it was far too complicated. The bill, which was just over 100 pages, morphed into thousands of pages of decisions and rules. And those rules include complex and sometimes inconsistent procedures for achieving simple things. That creates significant ambiguity, and, thus, contributes to the dissension within the industry, just as you accurately envisioned, Mr. Chairman, when you predicted the legislation had, and I quote you, "the hallmarks of becoming a real regulatory nightmare."

Second, the regulatory process takes too long, especially in view of today's market realities. For instance, when Qwest responded to consumer demand and filed for permission to provide stand-alone DSL, that process cost us $130,000 and took 45 days. The cable company, which has twice as many broadband customers as we do, could have achieved the same thing in less than 24 hours.

And, third, it has created complete uncertainty. Three times since this Act was passed, the courts have rejected the rules that require us to sell network elements at below cost prices, but nothing has been resolved. And this ongoing limbo makes it difficult to raise capital, to build a business plan, or to justify infrastructure investment.

We agree with the final words of the recent court decision that reflects its exasperation due to, and I quote, "the Commission's failure after 8 years to develop a—lawful unbundling rules, and its apparent unwillingness to adhere to prior judicial rulings," end quote. Mr. Chairman, I am convinced there is a direct and dramatic connection between this uncertainty and the fact that nearly one million telecommunications employees have lost their jobs.

So what is the remedy? I believe it lies in the same vision that has been the foundation of Qwest's turnaround, looking at the market through the eyes of the customers. I would offer that any legislation or regulation you support should be based on two principles.

The first of those principles is, the customers view telecommunications, at least voice services, as a commodity. Multiple providers offer it via wireless or cable or landline or, increasingly, the Internet. We have accepted that at Qwest, and regulators should do the same by eliminating the regulation of a single provider when others offer the same capability regulation free.

The second principle is, the customers are embracing new technology now. If they decide wireless works better for them than wireline, they could care less that regulators say it's not a substitutable service. When their preference is for a technology that makes distance irrelevant, it doesn't matter that the government still considers distance important. If Voice-over-IP best suits their needs, it's irrelevant that the 1996 Telecom Act never considered the Internet as a real competitive factor.

The fact is that we will make real progress only when regulation becomes more in sync with the advances in technology, which is, by the way, advocated by Senator Sununu's approach to Voice-over-IP.

There are many initiatives, Mr. Chairman, that you and this distinguished Committee can take toward fulfilling the promise of legislation that had the stated purpose, and I quote again, "to promote competition and reduce regulation."

And I'll look forward to whatever questions you may wish to raise on our mutual journey toward that end.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Notebaert follows:]

PREPARED STATEMENT OF RICHARD C. NOTEBAERT, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, QWEST COMMUNICATIONS

Thank you, Mr. Chairman and Members of the Committee. I appreciate this opportunity to offer a brief overview of the Telecommunications Act of 1996. I'll do that from the perspective of my experience at Ameritech—which I led when this legislation passed; at Tellabs, a Chicago-based telecom equipment manufacturer; and now at Qwest, the incumbent local service provider in 14 western states that also offers services including long-distance and enterprise systems throughout America.

In 1996, we had high hopes for this legislation—not that the Act was everything we had hoped—but that it would *finally* provide a progressive, consistent national telecom policy rather than the antiquated 1934 legislation then in place. We welcomed competition and the chance to enter new markets, and we were eager for reform.

We thought this bill offered real promise, beginning with its very first line, and I quote, "The purpose of the Act is to promote competition and *reduce regulation.*"

I am here today to suggest some reasons why, in my view, that opening line failed. Mr. Chairman, if I boil down where we think the Act went wrong, it would be in three areas.

First, it was *far* too complicated. The bill, which was just over 100 pages, morphed into thousands of pages of decisions and rules. And those rules include complex—and sometimes inconsistent—procedures for achieving simple things. That creates significant ambiguity and thus contributes to nonproductive dissension throughout the industry. Just as you so accurately envisioned, Mr. Chairman, when you predicted the legislation had the "hallmarks of becoming a real regulatory nightmare."

Second, the regulatory process takes *too long*, especially in view of today's market realities. For instance, when Qwest responded to consumer demand and filed for permission to provide stand-alone DSL, that process cost us $130,000 and took 45 days. The cable company, which has twice as many broadband customers as we do, could have achieved the same thing in less than 24 hours.

And third, it has created *complete* uncertainty. Three times since the Act was passed, the courts have rejected the rules that require us to sell network elements at below-cost prices. But nothing has been resolved. And this ongoing limbo makes it impossible to raise capital, to build a business plan, or to justify infrastructure investment. We agree with the final words of the recent court decision that reflects its exasperation due to, and I quote, ". . . the Commission's failure, after eight years, to develop lawful unbundling rules, and its apparent unwillingness to adhere to prior judicial rulings."

In addition, Mr. Chairman, I am convinced there is a direct and dramatic connection between this uncertainty and the fact that nearly one million telecommunications employees have lost their jobs, and that the manufacturing side of this industry has lost some 90 percent of its market capitalization.

What is the remedy? I believe it lies in the same vision that has been at the foundation of Qwest's turn-around: looking at the market through the eyes of consumers. Because if we view this as consumers would, the path to success gets much, much clearer.

I would offer that any legislation or regulation you support should be based on two principles:

> The first of those principles is that *customers* view telecommunications—at least voice services—as a commodity. Multiple providers offer it via wireless or cable or landline or, increasingly, the Internet. We have accepted that, and regulators should do the same—by eliminating the *regulation* of a single provider when others offer the same capability regulation free. By the way, no provider in its right mind raises prices above those of its competitors in a commodity marketplace. At Qwest, in fact, we are responding to this new reality by lowering the amounts customers pay.
>
> The second principle is that customers are embracing new technology *now.* If they decide wireless works better for them than wireline, they could care less that regulators say it's not a substitutable service. When their preference is for a technology that makes distance irrelevant, it doesn't matter that the government still considers distance important. If VoIP best suits their needs, it's irrelevant that the 1996 Telecom Act *never even considered* the Internet as a competitive factor. The fact is that we will make progress only when regulation becomes more in sync with the advances in technology, which is, by the way, advocated by the Sununu approach to VoIP.

There are many initiatives, Mr. Chairman, that you and this distinguished committee can take toward fulfilling the promise of legislation that had the stated purpose "to promote competition and reduce regulation." And I'll look forward to whatever questions you may wish to raise on our mutual journey toward that end.

Thank you.

The CHAIRMAN. Thank you very much, Mr. Notebaert. That's a very succinct and, I think, courageous statement, in light of views of some of the Members of this Committee, and I thank you.

Mr. Geiger?

## STATEMENT OF JAMES GEIGER, CHAIRMAN, ASSOCIATION FOR LOCAL TELECOMMUNICATIONS SERVICES AND CEO, CBEYOND COMMUNICATIONS, LLC

Mr. GEIGER. Chairman McCain, Senator Hollings, and Members of the Committee, I'm Jim Geiger, Chairman of the Association for Local Telecommunications Services, usually referred to as ALTS. And I'm also the CEO of Cbeyond Communications. I thank the

Committee for its continuing oversight of the Telecommunications Act of 1996.

ALTS is the leading trade association for facilities-based local-exchange carriers, or CLECs. ALTS' mission is to open local telecommunications markets so that our members can provide more service options at lower prices to consumers.

ALTS' members provide service in nearly every state, both in metropolitan and outlying areas. We are facilities-based, meaning the companies own and invest in their own switches, fiber optic cables, wireless antennas, and other new infrastructure. ALTS' members do not focus on the so-called UNE–P platform.

Mr. Chairman, while the Act is not perfect, it is working. The 1996 Act was never intended to assure success for every competitor, nor to protect incumbents. But, at this point, 8 years after passage of the Act, a number of facilities-based CLECs are emerging as strong, healthy businesses that are bringing value to both investors and consumers.

To note, CLEC market share has increased each year since 1996, reaching 15 percent at the end of 2003. The CLEC industry has invested $75 billion since 1996. Facilities-based CLECs provide service to over 25 million phone and Internet users, including more than 10 million access lines. CLECs employ nearly 60,000 people in the U.S., mostly in high tech, skilled positions. And if you ranked all providers of local phone service by access lines, facilities-based CLECs would occupy nine of the top 25 slots.

This investment in the competitive sector has, in turn, stimulated investment by incumbents, creating downward pressure on prices, and contributing to making American workers the most productive in the world.

Now, allow me to briefly use Cbeyond as an example of the success of the Act. I could equally use other ALTS members.

Cbeyond uses a state-of-the-art IP network to provide an affordable bundle of voice communications, high-speed Internet access, voice mail, e-mail, web hosting, and other related services. Our exclusive focus is on businesses with between four and 100 employees. And typical customers include physicians' offices, real estate offices, attorneys, landscapers, and architects. Because of efficiencies involved in IP technology, Cbeyond is able to provide small-business customers affordable packages of services that the Bell Operating Companies, or BOCs, traditionally offered to big business at higher prices. Unlike the VoIP providers that have been getting a lot of press lately, Cbeyond is a full peer to the BOCs. We comply fully with all regulatory requirements, we pay access charges on our long distance voice traffic, and we make all requisite universal service contributions. We comply also with E911 and CALEA requirements.

Mr. Chairman and Members of the Committee, the promotion of intramodal competition through unbundling is at the very heart of the 1996 Act. Congress recognized that competition requires access to incumbent bottleneck facilities, such as the local loop or the last mile. Facilities-based CLECs build their own networks where it is economically feasible to do so, but require access to the facilities that we are just simply not able to duplicate. Without facilities-based CLECs, like us, providing intramodal competition, we would

most likely see a cozy duopoly develop between cable and the incumbent telephone companies.

Congress chose wisely, because intramodal competitors have been the source of key innovations over the last few decades. Digital subscriber lines, IP-based communications, and even the Internet, as we know it today, itself were initially developed by competitors.

Cbeyond jointly developed, with Cisco, over the past 4 years, an advanced local IP telecommunications network technology. It is the same technology that is currently being deployed by Cisco in China. These advanced IP applications in China are virtually leapfrogging legacy networks in that country. It would be a grim irony if regulation failed to preserve, in the United States, the rollout by intramodal competitors of advanced IP applications that were developed here, while China uses that technology to jump ahead of this country.

In my experience, incumbents, as rational businesses, will not introduce new, more efficient services that devalue their legacy investment and cannibalize existing higher-priced services.

ALTS members are working diligently to meet national broadband goals. Cbeyond exclusively uses high-capacity loops to deliver our service. Well over 90 percent of Cbeyond customers did not previously receive high-capacity DS–1 level broadband access, although the dormant capacity to do so existed. Likewise, upward of 90 percent of American homes have broadband access available to them, but the "take rate" is only 20 percent. Now, we believe that's because of the price and the lack of compelling applications.

Mr. Chairman and Members of the Committee, the problem I think we need to focus on is not broadband deployment; it is broadband acceptance and adoption. And that can only be achieved through continued CLEC innovation and continued competition to increase the utility of, and downward price pressure on, broadband access.

We are concerned that the FCC and Congress are moving toward scaling back key pro-competitive provisions of the Act. Intramodal competition must be preserved in any rewrite of the Act, or we risk losing the benefits that competition has produced so far. Unfortunately, based on its Triennial Review Order, the FCC is apparently headed down a path of fostering a closed, proprietary bottleneck immune from the disciplining impact of intramodal competition.

I would suggest that since BOC long-distance entry was premised on the provision of unbundled access, any elimination of that access would necessitate revisiting the quid pro quo embodied in the 1996 Act—that is, long-distance entry only after markets are opened to competition.

Finally, ALTS members share the goal of universal, affordable broadband access, and ALTS will work with Congress and the FCC to assure adequate funding mechanisms which ensure that broadband is available and affordable to all Americans.

That concludes my statement.

[The prepared statement of Mr. Geiger follows:]

PREPARED STATEMENT OF JAMES GEIGER, CHAIRMAN, ASSOCIATION FOR LOCAL TELECOMMUNICATIONS SERVICES AND CEO, CBEYOND COMMUNICATIONS, LLC

**Introduction**

Good Morning, Mr. Chairman and Members of the Committee. I am Jim Geiger, Chairman of the Association for Local Telecommunications Services, usually referred to as "ALTS," and CEO, of Cbeyond Communications, LLC. I thank the Committee for its continuing oversight of the Telecommunications Act of 1996 ("96 Act").

ALTS, now halfway into its second decade, is the leading trade association for facilities-based competitive local exchange carriers ("CLECs"). ALTS' mission is to open local telecommunications markets so that business and residential customers can obtain the benefits of competition including more service options and lower prices. As found by the Small Business Administration, ALTS' companies save its customers on average 30 percent per telephone line compared to the rates charged by the incumbent local exchange carriers ("ILECs").[1] Although ALTS members also serve residential and large business customers, we are the leaders in bringing local telecommunications value to the small and medium sized business market. Our members do not include major long distance companies or the BOCs. We are focused exclusively on promoting competitive local services. ALTS' thirty-three CLEC members provide service in nearly every state in both metropolitan and outlying areas. Our companies are facilities-based, meaning the company owns and is investing in switches, fiber optic cables, wireless antennas, and other broadband telecommunications networks. ALTS members are not focused on the unbundled network element platform, commonly known as UNE–P, because most ALTS companies install and use their own switching capability. Instead, ALTS companies purchase loops and transport from the ILECs, the transmission facilities that connect our customers to switching facilities. Because our companies deploy our own networks as much as possible, we are the leaders in deploying new communications technology, including IP and softswitching. ALTS supports the goal of universal affordable broadband access for all Americans. Our members are working zealously to meet that goal.

Although I am testifying this morning on behalf of ALTS, I would also like to briefly introduce Cbeyond. Cbeyond, headquartered in Atlanta, uses a state-of-the-art IP network to provide affordable voice telecommunications and Internet access service to small and medium-sized business customers in Atlanta, Denver, Dallas, and Houston. Cbeyond is a showcase for Cisco's innovative IP products. At Cisco's invitation, we are frequently visited by other companies because we are viewed as a model provider of IP communications. Because of the efficiencies involved in IP technology, Cbeyond is able to provide to small business customers affordable packages of services that BOCs traditionally offered to big business at higher prices. Well over ninety percent of Cbeyond's customers did not previously have DS–1 level access, which we use exclusively to deliver our services. Our company is fully funded and financially healthy. We fully comply with all regulatory requirements; we pay access charges on our voice traffic; we make all requisite universal service contributions; and reciprocal compensation is not part of our business plan. Cbeyond operates as a full peer to the BOCs offering E911 access, local number portability, and CALEA compliance.

**Competition Is Working**

As I will discuss below, the 96 Act is not perfect. Nonetheless it is a success story in very significant respects. The 96 Act was never intended to assure success for every competitor or every business plan. Nor was it intended to protect incumbents from the disciplinary impact of competition. But at this point, eight years after passage of the 96 Act, a number of facilities-based CLECs are emerging as strong, healthy businesses that are bringing value to both investors and consumers.

Congress got it right in choosing competition in local telecommunications markets as the best way to innovate and bring new services to consumers. The market-opening provisions of the 96 Act initiated, and made possible, substantial investment in new facilities and new technology that, in turn, has created a large competitive industry that is benefiting consumers.

- Facilities-based CLECs invested nearly $75 Billion from 1996 through 2003.

[1] *A Survey of Small Businesses' Telecommunications Use and Spending,* Stephen P. Pociask, SBA, March 2004, Tables 12, 13.

- The CLEC sector of the telecommunications industry represents $46 Billion in annual revenue, which is close to that of the cable industry.[2]
- CLECs employ nearly 60,000 persons in the U.S., mostly in high-tech, skilled positions.
- According to the FCC's 2003 Local Competition Report, facilities-based CLECs serve over 10 million access lines. (This is in addition to the 19 million lines served by the UNE–P carriers.)[3]
- Facilities-based CLECs comprise nine of the top 25 largest telephone companies in the U.S. measured by access lines.

Because of this enormous investment, CLECs have increased their market share every year since 1996. Of course, CLECs winning voice customers from incumbents through better service options and prices is not a public policy problem, but evidence of the success of the 1996 Act and the benefits it is intended to bring consumers. CLECs have experienced this growth because they compete and offer innovative new services and features typically to underserved markets. CLECs have created new markets and pioneered new ways of offering service, such as bundled offerings, and online customer care including online billing and online self-provisioning. Nevertheless, local telecom competition has grown more slowly than most of us thought when the 96 Act was passed. After eight years, the CLEC industry has won about 15 percent of the local market nationwide. Obtaining the cooperation of the Regional Bell Operating Companies (RBOCs), enforcing the 96 Act, convincing municipalities and building owners to allow competitors into their markets, have all been extremely difficult.

The slower-than-expected pace of competition can also be seen in the evidence of the RBOCs enormous profitability. Even as they complain to regulators about the local competition rules, the RBOCs' latest reports demonstrate that they are experiencing huge margins and profits. SBC, for example, recently reported for the 1st quarter of 2004 an EBITDA margin of 31 percent, and pretax income of $1.35 Billion.[4] SBC's DSL lines and long distance lines have increased 60 percent and 12 percent, respectively, in the last year.[5] BellSouth reported that its 1st quarter 2004 profit increased 30 percent to $1.6 Billion. BellSouth reports that growth in long distance and DSL offset access line declines.[6] For 2003, Verizon reported net income of $3.077 Billion.[7]

**Intramodal, Facilities-Based Competitors Are the Innovators**

Innovation and broadband deployment are the key success stories of the 96 Act. By requiring the RBOCs to open their networks to competitors, the 96 Act embraced intramodal competition. The Act's unbundling provisions and the explicit trade-off between BOC long distance entry and opening markets to local competition were designed to encourage CLECs to develop innovative and, in many cases, "intelligent" devices that can bring consumers more sophisticated broadband services using the relatively passive transmission pipes leased from the RBOCs. Intramodal competition is thus not simply reselling and re-branding the RBOC service; intra-modal competition has encouraged extensive deployment of new hardware and software that can turn the RBOCs' plain old copper loops into high-speed broadband transmission facilities.

Congress chose wisely because intramodal competitors have been the source of key telecommunications sector innovations over the last few decades. DSL, IP-based communications, even the Internet itself were initially developed by competitors.

To use an analogy, RBOC telecommunications facilities can be likened to train tracks, or the roads leading to every customer premises. If competitors are permitted to put their own trains and engines on these tracks, those same tracks formerly used to carry freight trains can be used to carry high-speed maglev trains, carrying infinitely more capacity, than when they were solely under the control of the monopolist. If, however, competitors must build tracks and roads to every customer, they will never be able to acquire the enormous amount of capital necessary to duplicate the existing telephone network.

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[2] New Paradigm Research Group.

[3] We estimate that 10 million access lines serve approximately 25 million end users because some reported access lines are trunks serving on average about 5 customers per trunk.

[4] Schwab Soundview Capital Markets, April 22, 2004. EBITDA is Earnings Before Interest, Taxes, Depreciation and Amortization.

[5] Communications Daily, April 22, 2004, p. 9.

[6] Communications Daily, September 23, 2004, p. 5.

[7] Verizon Communications, Inc.10–K 2003.

We believe that Congress should be quite disturbed, to put it mildly, to see how the RBOCs are seeking to dismantle the unbundling regime and eliminate the competitors' ability to obtain access to their networks, the train tracks. The RBOCs' principal argument is that they face competition from the cable companies, but this argument simply does not hold up under scrutiny. To give one reason, many ALTS members focus on the small and medium-sized business market, a market that is not served by the cable companies. Eliminating the ability of CLECs to serve the small and medium-sized business market would essentially leave these small and medium-sized business customers with a monopoly—their local RBOC. Even in those areas served by the cable companies, insufficient intramodal competition would leave a duopoly between cable and incumbent telephone companies. As a business person with over 20 years experience in a variety of companies, it is my opinion that a marketplace dominated by two providers would not stimulate innovation and competition. It is more likely that a cozy duopoly would develop, characterized by a division of the market perhaps along service lines. As a result, a return to the slower pace of innovation characteristic of the 70s and 80s would be likely.

**Incumbents Are not the Best Innovators**

VoIP is the latest example of the fact that BOCs are not the most efficient or innovative users of their own networks. Not because BOCs may not have some of the smartest business persons and technical experts and highly skilled craft persons. Rather, they delay innovation for very rational reasons. In part, BOCs are reluctant rapidly to embrace new technologies because they must move cautiously given the size and scope of their monopoly networks. Perhaps more importantly, however, they are reluctant to introduce new services that cannibalize their own higher-priced legacy services. VoIP providers, for example, offer voice service to consumers at considerable savings in comparison to traditional incumbent services and with more features, such as management of long distance calls from a website. BOCs are announcing plans to offer consumers these benefits that undercut their traditional voice offerings only because of competitive pressure. They would have no incentive to do so otherwise, and without competitors in the market, would only do so at much higher prices than those charged by new entrants.

Integrated IP-based services such as those offered by Cbeyond are another example. BOCs did not deploy this technology that undercuts their own more expensive DS–1 data services until competitive pressure from CLECs required them to do so. Similarly, CLECs were the first to offer DSL services. BOCs did not want to undercut their own inferior second line services used for dial-up Internet access. As stated in its 1999 Economic Report of the President's Council of Economic Advisors:

> "[t]he incumbents' decision finally to offer DSL service followed closely the emergence of competitive pressure from cable television networks delivering similar high-speed services, and the entry of new direct competitors attempting to use the local competition provisions of the Telecommunications Act of 1996 to provide DSL over the incumbents' facilities."

Similarly, in the 80s and before, incumbents were slow to introduce Telex, PBXs, and key systems, and only after the FCC took steps to assure a competitive market by competitive providers.

These examples show that BOCs will not innovate to rapidly bring consumers new services if this undercuts a legacy higher priced service. Instead, BOCs carefully evaluate competitive inroads and only when they have more to lose to competition by standing still will they move to introduce new services.

**Unbundling Promotes Broadband Investment**

A key initial success of the 96 Act is promotion of broadband investment by both CLECs and incumbents. The unbundling provisions of the 96 Act have provided a framework for robust investment in broadband. As noted, competitors have made very large investments in new telecommunications facilities, and this investment fueled the growth of the Internet. As recently as 2001, over half the Internet traffic in the country flowed over networks built by CLECs. The network investment by CLECs incented the RBOCs to increase their capital expenditures as well. For instance, the RBOCs have been engaged over the last decade or so in a gradual build-out of fiber networks. It began using fiber for all new feeder placements beginning in 1996. In 2000, when the unbundling rules applied to fiber as well as copper plant, BellSouth described itself as the "market leader" in deploying fiber to multi-premise

developments.[8] Already 50 percent of its loops can support 5 Mbps service.[9] BellSouth already has 1 million homes passed with fiber, and an additional 14 million with fiber to a nearby distribution point.[10] Similarly, in 1999, SBC announced its $6 Billion fiber-in-the-loop "Project Pronto." All the BOCs have invested heavily in DSL capability. These broadband investments by BOCs refute their argument that unbundling obligations inhibit investment.

In fact, incumbents are modernizing the loop because costs savings and efficiencies alone justify the investment. They do not need relief from unbundling to incent them to install fiber. As recently reported in an article in the Los Angeles Times concerning SBC's fiber project in Mission Bay, CA, quoting an SBC official:

> Fiber is expensive to deploy in existing communities because of the costs to install it. But after that, it's a cakewalk. Once I've got it in, my operational costs are much lower. There's less failure, fewer trucks rolling out and fewer workers needed to test and fix the system.[11]

**ALTS Shares the Goal of Advanced Affordable Broadband Networks**

ALTS believes that broadband access should be universal and affordable. ALTS members have helped expand the deployment of broadband services to almost all Americans. In 1996, fewer than 5 percent of Americans had access to broadband; today, almost 90 percent of American homes can purchase broadband services today from at least one provider of broadband services. This is an enormous accomplishment, and one for which Congress deserves a substantial amount of credit. However, that is not the end of the broadband story. Approximately 10 percent of American households can not yet purchase broadband services, and many of these households are in rural areas. ALTS supports efforts by Congress and the FCC to take steps to ensure that 100 percent of Americans have broadband available to them, and our companies are willing to pay our fair share to achieve this goal of universal broadband. Furthermore, it is also a concern that only 20 percent of American households actually subscribe to broadband services, even when it is available to them. Some Americans simply do not see the value of purchasing a broadband connection; other Americans would like to purchase broadband but simply cannot afford it. For many Americans, the price is simply still too high. Greater competition for broadband services would put downward pressure on rates and help to make broadband services more affordable. ALTS members are very willing to work with Congress to achieve the goal of universal and affordable broadband.

Let me give you an example of how the unbundling regime and intramodal competition has helped to promote broadband deployment. Without unbundling, the intramodal competition that served as the test bed and originator of broadband IP applications would not have been possible. Cbeyond jointly developed with Cisco advanced local IP telecommunications network technology and applications because the 96 Act gave Cbeyond the right to purchase high-capacity loops from the ILECs. These are the same technology and applications that are currently being deployed in China. These advanced IP applications in China are virtually leapfrogging legacy networks in that country. It would be a grim irony if regulation fails to preserve in the United States the roll-out by intramodal competitors of advanced IP applications that were developed here while China uses that technology to leapfrog ahead of this country.

We strongly disagree with the current views of the FCC as to how to achieve broadband goals. The FCC recently decided to exempt fiber-fed loops from the unbundling provisions of the 1996 Telecom Act. In other words, the FCC decided to grant the RBOCs a monopoly over customers served by fiber. Further, the FCC is considering whether to redefine incumbent bottlenecks as "Title I" networks so that incumbents would not even be required to provide nondiscriminatory access to competitive providers.

ALTS could not disagree more strongly with the FCC's cramped vision of closed, non-common carrier incumbent broadband networks. American consumers will be best served by an advanced broadband network that is open to competitive access on reasonable terms and conditions. As with DSL and VoIP, CLECs will rapidly introduce new broadband services at better prices than would ILECs. Insulating BOCs from the competition CLECs can provide will simply limit incentives for them to innovate. This will guarantee a slow roll-out of new and affordable broadband services.

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[8] *BellSouth Now Wiring New Homes for the Future,* BellSouth Press Release (June 15, 2000).
[9] *Id.*
[10] Vince Vittore, *Bill Smith, BellSouth,* Telephony (June 2, 2003).
[11] James S. Granelli, *Dialing in Competition,* L.A. Times, April 19, 2004.

The Committee should discourage requests by BOCs for further broadband unbundling relief. In particular, extending the FCC's fiber-to-the-home ("FTTH") policy to multiunit buildings and new housing development would permit BOCs to thwart provision of competitive services in these environments. Many building owners, shopping centers, real estate management companies, and apartment developers support the pro-competitive unbundling provisions of the Act because this promotes the availability of innovative services and lower prices.

As a businessman with considerable telecom experience, I believe that there is essentially no empirical evidence that eliminating unbundling would incent BOCs to deploy fiber. Quite the contrary, BOCs have been gradually installing fiber in the "last mile" notwithstanding unbundling obligations. The FCC in its *Triennial Review Order* took it on faith that BOCs would deploy more fiber if they are given a monopoly over these customers. I am concerned that BOCs have made similar promises and broken them before. For years, BOCs promised that they would build advanced "video dial tone" networks—essentially the same networks that they are now again promising to build—if they were permitted to provide video programming. Congress granted that permission in the open video provisions of the 96 Act, but BOCs never built those networks. Cbeyond and other ALTS members have been the first to offer new broadband services over the current network and if granted access to new fiber investment will do the same there. Of course, to the extent that BOCs are claiming that they have an insufficient return on fiber investment, this is better addressed through pricing of unbundled broadband access rather than denying such access altogether as the FCC has apparently chosen to do.

In this connection, however, it is noteworthy that the Supreme Court affirmed the FCC's TELRIC pricing methodology for UNEs and noted the substantial basis in past policy for rejecting BOCs' request that they be permitted to recover their historic costs. TELRIC pricing duplicates the prices that incumbents would be able to charge in a competitive market. TELRIC pricing includes a reasonable profit. BOC efforts to derail TELRIC are no more than an attempt to impose the costs of outmoded technology on customers. Regulators will best promote the introduction of new technology if they continue to require incumbents to base prices on competitive, not legacy, costs.

**Regulatory Uncertainty**

Unfortunately, however, I would have to count as a major deficiency of the 96 Act that it was not sufficiently clear in expressing Congress's view that broadband goals should be achieved by competition, not protecting incumbents from competition. Incumbents have been able to persuade regulators and the courts that they should be protected from competition that could be enabled by unbundled access to their bottleneck loops. If this approach stands, consumers will have at best a broadband duopoly of BOCs and cable companies with limited choices and ultimately rising prices. I would also count as a major deficiency of the 96 Act that it has invited such extensive litigation over the last eight years.

**If CLECs can no Longer Interconnect with the ILEC Network at Cost-based Rates, a New Section 271 Rebalancing Would Be Necessary**

If the RBOCs are successful in eliminating the unbundling rules and intramodal competition, Congress should establish a new trade-off between BOC long distance entry and opening markets to competition. Leading up to the 96 Act, BOCs strongly opposed a market share test for long distance entry, arguing that competitors could slow their entry into the market to delay the RBOC entry into long distance. In response to that concern, Congress chose instead to permit the RBOCs to provide long distance service after they opened and unbundled their networks to competitors, and the RBOCs agreed to this balance. The Department of Justice established the standard that the RBOCs should only be permitted to enter the long distance market after it was proved that the local market was "irreversibly opened" to competition. If unbundling is undermined, it will be clear that the market is not, in fact, irreversibly open. Indeed, since gaining long distance entry BOCs have worked diligently to eliminate the provision of unbundled network elements (UNEs) that formed the basis for long distance approval. If CLECs' access to the BOC networks is eliminated, either Congress or the FCC should revoke long distance authority and the FCC should immediately prohibit BOCs from taking on new customers.

**The Adverse Impact of *USTA II***

The substantial facilities-based CLEC industry built its business on the foundation of access to bottleneck loop and transport facilities. It is unfortunate, just as many of those CLECs have surmounted the difficult financial environment of the last few years, that the D.C. Circuit issued its recent decision which at least temporarily casts doubt on the legal basis for CLEC unbundled access to bottleneck facili-

ties on reasonable terms and conditions. The D.C. Circuit decision appears to be inconsistent in many respects with prior Supreme Court rulings on the 1996 Act. Furthermore, the Court erred in speculating that the availability of special access could eliminate the need for UNE transport. Special access has been available for many years, predating the 96 Act. If Congress believed that special access could substitute for UNEs, it would not have provided for unbundled access to transport and other network elements.

Nonetheless, the BOCs have already indicated that they intend to take advantage of this court case to impose huge rate increases on the CLECs. In particular, BOCs are already seeking to impose unacceptable price increases for high-cap loops and transport by transitioning them to their special access rates. For example, BellSouth's special access price for a Zone 1 DS–1 loop in Georgia is triple the UNE price. For Verizon in Pennsylvania the price would be double. SBC's price in Texas for Zone 1 DS–1 transport would increase by more than 50 percent. For Qwest in Colorado the price for such transport would more than double. DS–1 loop and transport prices are particularly important to CLECs because they are components of the loop-transport combinations that they use to serve customers. Any BOC assumption, such as BellSouth's view, that CLECs should simply pay higher special access prices is completely unacceptable from a business perspective and from a policy perspective as well since this fails to recognize the bottleneck character of loops and most transport. In this connection, most BOC special access services have been deregulated on the theory that they are competitive. But BOCs have not been reducing special access prices as would be expected in a competitive environment. BellSouth has been raising some special access prices.[12] Consequently, I am very concerned that BOCs' conduct in the wake of *USTA II* could lead to substantial service disruptions for tens of millions of telephone users. For these reasons, it will be important to obtain a stay and a new decision from the Supreme Court.

**Industry UNE Negotiations-What Happens on June 16, 2004?**

ALTS supports the FCC's recent call for negotiations between CLECs and incumbent telephone companies concerning access to unbundled network elements. While we strongly disagree with some aspects of the opinion of the D.C. Circuit in *USTA II,* ALTS supports good faith efforts to resolve key issues through negotiation rather than litigation. To that end, ALTS, on behalf of its members, on April 9, 2004 sent letters to each of the BOCs proposing negotiations on loop and transport issues. Individual ALTS members are pursuing separate company-to-company or group negotiations with BOCs, and one, Covad, has reached an agreement with Qwest concerning line sharing.

We hope that these negotiations result in long term agreements for access to incumbent bottleneck facilities that will permit facilities-based CLECs to provide competitive local services. We are disappointed that BOC negotiating efforts so far have apparently been almost exclusively focused on the so called UNE-Platform ("UNE–P"). We are also very disappointed that BellSouth has recently posted a notice on its website that unilaterally directs CLECs to transition from UNE to special access and much higher prices.

BellSouth has informed Cbeyond that after June 15 it will only provision new loops and transport as special access and that negotiations will be limited to the status of facilities that CLECs currently obtain as UNE. Qwest has also proposed special access pricing for apparently both existing and newly ordered facilities. As noted, price increases of the magnitude suggested by BOCs are completely unacceptable for DS-1 and other UNE that are the lifeblood of facilities-based CLECs. CLECs would not be able provide value propositions to their small and medium-sized business and other customers and competition would be stalled. Consequently, we do not view these BOC approaches to the post-*USTA II* environment as constructive or reflective of an intent to engage in good faith negotiations as requested by the FCC.

ALTS urges Members of the Committee to direct incumbents to negotiate in good faith with facilities based CLECs. We would be pleased to provide to the Committee any progress reports concerning negotiations that it would find useful.

Negotiations may not be successful. If that proves to be the case, ALTS and facilities-based CLECs will have no alternative but to appeal *USTA II* to the Supreme Court. We will encourage the government to do so as well. If we are unsuccessful in obtaining permission for appeal from the Supreme Court or a stay pending ap-

[12] In addition to appealing the D.C. Circuit decision, the FCC should initiate a comprehensive review and investigation of special access pricing. BOCs are also not subject to any performance metrics for provision of interstate special access. The FCC has failed to act in special access metrics rulemaking.

peal, facilities-based CLECs and the customers they serve could be harmed unless the FCC promptly clarifies among other things that *USTA II* did not vacate the FCC's loop rules.

**Need for Enforcement**

Since the 1996 Act, BOCs engaged in unprecedented violations of the Act. They have paid more than $2.1 Billion in fines including for failure to comply with UNE rules, Section 271 obligations, and merger conditions. While I am pleased that the FCC took the enforcement actions that it did, I question whether fines, and the delays in imposing them, are sufficient to deter incumbent incentives to deny access to bottleneck facilities. For example, Verizon is essentially declining to comply with the FCC's new rules concerning denial of access to loops based on "no facilities" and yet the FCC has done nothing. The FCC should be given additional resources and new tools, such as the ability to impose forfeitures as part of self enforcing performance measures, so that it may take a more pro-active and effective approach to enforcement. Furthermore, any penalties on the BOCs for failing to provision UNEs should be awarded directly to the CLEC in the form of liquidated damages, rather than as fines paid to the U.S. Government. Paying the penalty directly to its competitor should give the BOC even more incentive to comply with the law.

**Universal Service**

ALTS recognizes the potential challenge to universal service programs that could be occasioned by increasing demands on outflow to eligible telecommunications carriers and changes in underlying network technology that may make current contribution requirements insufficient to support current programs. ALTS looks forward to working with Congress and the FCC to assure adequate funding mechanisms as VoIP and broadband technologies become more widely deployed in carrier networks.

**Conclusion**

My experience under the 96 Act has shown that competitors such as my own company and other ALTS members are the first to innovate and introduce new technology. The 1996 Act as initially implemented has successfully provided a framework for the development of substantial facilities-based competition that is providing significant benefits to consumers. A shortcoming of the 96 Act is that it did not sufficiently make clear that broadband goals should be achieved through implementation of the unbundling obligations of the Act. ALTS and its member companies will endeavor to reach a negotiated solution to access to UNEs rather than litigation while preserving a right to further appeal of *USTA II* if necessary.

I want to thank the Committee for recognizing the importance of facilities-based competition and for consistently reiterating that support.

The CHAIRMAN. Thank you, Mr. Geiger.

Mr. Notebaert, how many jobs did you say have been lost since the passage of the 1996 Act?

Mr. NOTEBAERT. Close to a million, sir.

The CHAIRMAN. Close to a million. I was intrigued by your—in your statement, you said, "Qwest responded to consumer demand, and filed for permission to provide standalone DSL. The process cost $130,000, took 45 days. A cable company, which has twice as many broadband customers, could have achieved the same thing." Why is that? Why could the cable companies have achieved it in 24 hours—in less than 24 hours?

Mr. NOTEBAERT. The cable companies, which have about over half of the market share right in cable data modems, are not regulated at all. Another example would be where we have to post where we are going to deploy DSL 60 days in advance of making it available to customers; thereby, giving the competition—the cable company—an opportunity, Mr. Chairman to canvas, door to door, that very neighborhood that we're deploying in.

And one last comment. Where we support competition completely, they block us from even advertising on their systems—in other words, advertising a competitive service.

The CHAIRMAN. Well, that's pretty remarkable.

Mr. NOTEBAERT. Uh-huh.

The CHAIRMAN. And probably because when the Act was written—that it was not envisioned that the cable companies would have this kind of technological capability, right?

Mr. NOTEBAERT. No, Mr. Chairman. I believe that, at the time the Act was written, Senator Hollings and Senator Pressler, at the time, as well as the other side, the House, had talked to the cable companies about the deployment of cable telephony, and, in fact, talked to Time Warner at the time. So I believe that facilities-based competition was a strong part, and that the arbitrage that was created by the Act was only an interim process. And it's 8 years later; that's a long interim.

[Laughter.]

The CHAIRMAN. Let me just ask the witnesses a series of short questions, and I know they're tough questions, but I'd like to try to get them in, in the time that I have.

Michael Powell, the chairman of the FCC, has said the Telecommunications Act of 1996 is, quote, "walking dead." Do you agree? And if not, why?

Beginning with you, Mr. Dorman.

Mr. DORMAN. I don't agree, because I think it was a very complex undertaking. I think that the judicial challenges in litigation has slowed down progress, but I do believe now the benefit——

The CHAIRMAN. Nobody anticipated that, with a thousands pages of law, that there would be a lot of litigation, and——

Mr. Dorman: I did not mean—excuse me——

The CHAIRMAN.—many parts of this Act were written by lobbyists. Were you surprised, Mr. Dorman, that there was as much litigation as there was?

Mr. DORMAN. I think that the tone and tenor has been different than we would have expected. Challenges, yes. But the same issues being, you know, sort of, brought up over and over again——

The CHAIRMAN. I'm not gifted with clairvoyance, but I sure as hell predicted it.

Mr. Notebaert?

Mr. NOTEBAERT. I agree with Chairman Powell. And I wish, if we could go back and redo it, Senator, Packwood's suggestion that at 5 years the Act would terminate, would be—end. That would have been a good thing to do, because it has been a very expensive process.

The CHAIRMAN. Mr. Geiger?

Mr. GEIGER. Well, I approach these things by asking myself, "what problem are we trying to solve?" If, indeed, you believe the analytical reports that there is broadband within reach of 80 percent of homes from cable, 80 percent of homes and businesses from the Bell Operating Companies, I think that this piece of legislation——

The CHAIRMAN. How about the jobs lost?

Mr. GEIGER. I'm sorry, I can't speak to the jobs lost. We've lost a lot on our side of the industry, as well.

But it's also, I think, interesting to look at the financial health. Eight years of a regime that has supposedly been so terrible has produced a tremendous amount of investment by both sides, the

CLECs and the ILECs. And if you look at any relative measure of financial health, the ILECs, as a group, are roughly twice as profitable on a net-operating basis as the average S&P company; and on a free-cash-flow basis, they are also twice as profitable. So——

The CHAIRMAN. Thank you.

Is continued regulation of wireline competition necessary in light of the intermodal competition that both incumbents and competitive carriers increasingly face from wireless, cable, Voice-over-IP, and other providers of voice services?

Mr. Dorman?

Mr. DORMAN. I think that the real issue in regulation is the fact that you've got to de-monopolize before you deregulate. And the fact is that the Bell companies' market powers are still significant. Take the do-not-call legislation, the fact that in Qwest territory it does business with a significant percentage of customers—I would suspect in the high 80s—they had the ability to call those customers and ask them if they'd like to get long-distance service from them, for example. Wherein, AT&T, even at our size, does business with perhaps only 30 percent of the customers.

So until you can reduce the market power—like AT&T was regulated after 1984 under a basis that was established by the FCC called "dominant carrier status"—until AT&T's market share dropped below 55 percent, it was regulated as a dominant carrier. Well, I'm not proposing 55 percent. I certainly think that we've got to focus on de-monopolizing before we deregulate, in the case of the Bells.

The CHAIRMAN. Mr. Notebaert?

Mr. NOTEBAERT. It's unnecessary. If we look at the Act, and read the Act carefully, it says there will be no market-share tests. That was very specifically put in the Act.

Second, if you look at the intermodal competition that takes place between wireless, the cable companies, Voice-over-IP, and you look at the market share for voice communications for consumers, there is less than half that use the wireline, the traditional incumbent local-exchange carrier. There are more cell phones out there. Every one of us uses them. We're all used to it. And cable telephony is there to stay. If you take Omaha, Nebraska, we have about half the market share in Omaha.

The CHAIRMAN. Mr. Geiger?

Mr. GEIGER. I would say that there are a lot of promising new technologies—broadband over power, certainly cable—but if you look at market segments, we focus on small business, and there is less than a 5 percent overlap of any other network touching those businesses in this country, which would imply that if there were an abolishment of our access to that last mile, 95 percent of businesses would have no choice for their communications services.

The CHAIRMAN. I want to thank the witnesses.

Senator Hollings?

Senator HOLLINGS. Thank you, Mr. Chairman.

Let's don't run a touchdown in the wrong direction when we just, rat-a-tat-tat, a thousand pages and a million jobs.

The textile industry has lost a million jobs since 1996. Had nothing whatsoever to do with communications. The bill itself was a hundred pages, not a thousand pages. And it was written, not by

lobbyists, but by the chief executives and the best of lawyers of the communications companies.

Mr. Notebaert was head of Ameritech, and I've got the greatest respect for him. He's an outstanding individual, and I hailed when he took over Qwest, and he's running it right. I like it. Dorman, he was down with Bell South. Jim Cullen, of Bell Atlantic, just stood there as a referee. I know—Dick Notebaert starts smiling, because——

Look, it took me 4 years. I started writing this with a jaundiced eye there about deregulation. I had been on this Committee, I had gone along with the deregulation of natural gas, and the price had gone through the ceiling.

[Laughter.]

I had gone along with the deregulation of the airlines, and I still—costs a thousand dollars for a roundtrip to Washington. I've gone along with the deregulation of trucking, and we had 67 cross-country truckers, and they're down to 11 now. So I said wait a minute, let's make sure we do this one right.

And we had a problem, because we were trying to bring monopolies into competition. As of April 27, 2004, we still have monopolies not in the competition. They still have 85 percent of the last line, right, Mr. Geiger?

Mr. GEIGER. I think at least 85 percent.

Senator HOLLINGS. Yes, sure, they've got—so they've got a monopoly. And I'd love to run one of those Bell companies, because all you have to do is get some people to know a little bit about communications and go around and honey-up all the state legislators and the Congressmen and Senators, and give them dinners and parties, and play golf with everybody and be a nice fellow, because you cannot lose money. It's still a monopoly. They've got the cap—if it exceeds the cap, then, by gosh, they can make the profits—I mean, if it's less than the cap price setting at the local level, then they get that profit. If it exceeds it, the local commission takes care of them.

So they've got a monopoly, and the mistake—you list three; I list one—and that was, we trusted them. We trusted them. It was all enacted after 4 years. We had 2 years on this Committee. We lost out. George Mitchell was trying to bring the bill up, and we lost the Senate, the Democrats in the Senate. And then we turned around and—I'm sorry Senator Lott is gone, but he gave me his staffer.

Now Congressman Pickering, who's cosponsoring the bill that you attest for. And we—it was Chip Pickering representing the Republican side—and myself, and we worked with Tom Bliley over there, and we got this bill going, with Mr. Notebaert, Mr. Cullen, Mr. Clendennon—I can go right on down the list and call the roll—with the best of lawyers, communications lawyers. And, as a result, we had long-distance and Bell companies, both, all endorsed the bill. We passed it 95 to 5. Everybody agreed it was a good bill.

Now, there was the misplaced trust, Senator. What happened was, they used every gimmick in the book to frustrate it, which gives the thousand pages. When you say it doesn't have data, and it's got data mentioned 428 times—and, you know, communications lawyers down here, they'll bollix up everything, and particularly

when you've got a chairman who now says "the walking dead." He's made the regulatory commission a walking-dead commission, because the Bell companies have used that as a political instrumentality to frustrate and continue to take over the, by gosh, long distance. And now they're—the third-largest long-distance carrier is Verizon. I mean, they've gotten in there. But the long-distance companies can't get into that local; they've still got 85 percent.

So let's get right to the point. What has really happened, and what we should have done was, should have ordered the unbundling by a certain time, and everything else like that, and then we would have gotten open competition, and everything else like that, just like we wanted. And we thought—everybody said—I'd listen to them all during the 80s, with Judge Green's order and everything, "Oh, we're going to get—we've got to get into long distance." That's all they wanted to do. And they—by gosh, they're using every lawyer in town to resist doing it, and distorting the Federal Communications Commission in the entire process, and that's what's happened.

I mean, it isn't a complicated bill, Mr. Notebaert. You wrote it. He smiled. Let the cameras and the record show the gentleman is smiling.

[Laughter.]

Senator HOLLINGS. Thank you, Mr. Chairman.

The CHAIRMAN. Would any of the witnesses like to respond to that question?

[Laughter.]

Mr. NOTEBAERT. I guess I will.

Senator Hollings, when we worked on that bill, all of us, we felt that the bill, as it was written, had the opportunity to be a success. Those 1200 pages, or just over 1,000 pages, that were written by the FCC were written before any attempt was made to file for long distance. I know Ameritech was the first company. We filed in Michigan. And before those thousands pages, the ink was dry, we were already told that the Commission would ignore the market-share tests, which had been prohibited, with your good work, in the bill. And Henry Hyde worked on that, too.

So if I go back and think about what occurred, being as close to you as I was at the time, I don't think the bill was necessarily the issue. I think the interpretation of the bill—and when you have contradictory rules, we have a problem, no matter which side of regulation you come out on. So——

Senator HOLLINGS. We agree on that.

Mr. NOTEBAERT. Yes, sir.

The CHAIRMAN. Mr. Dorman or Mr. Geiger, would you like to make a comment?

Mr. GEIGER. No, thank you.

The CHAIRMAN. Senator Burns?

Senator BURNS. We keep coming back to this thing—thank you, Mr. Chairman—and coming back to this end of it, as Mr. Hollings has put it, and then the actions that were taken after the bill was passed.

There's another element in this that should be made part of the conversation, and I would ask all of you to respond to this, historically. Telecommunications regulation has been shared respon-

sibly—or a shared responsibility with both the FCC and the states. The states have always had a major role in the regulations and the enforcement of those regulations. As we think about the future of the industry and the possibility of revisiting this Act as of right now, what role should the states play? And should we go back into this idea? Because it was a big part of the conversation during the writing of the bill. What role do the states play? What role was—the FCC plays? Would you like to comment on that?

Mr. DORMAN. I think that the sharing of responsibility between the states and the FCC remains important. I think the FCC's ability to be familiar with every local market in the U.S. and the amount of communications business that gets done is difficult. And I think the recent FCC response to the last remand of the District Court suggested that taking into consideration local competitive requirements, local competitive conditions, was important. That's what the remand before this last remand asked for. And when the FCC majority put forth this set of rules in response to that, it suggested it needed the states' help in determining impairment of competition at the local level.

As technology evolves and we think about Voice-over-IP, the notion of locality and communications services is certainly blurred. The cell phone has done that, to a certain degree. So I would suggest that intrastate, interstate, interLATA, intraLATA, some of those mechanisms do not apply in the way they did in a wireline environment, and so we've got to update our thinking about it. But I do think there's still an important role for state authority.

Senator BURNS. Mr. Notebaert?

Mr. NOTEBAERT. Senator, I think if we're going to have a national communications policy, it needs to be a national policy. We see this problem in broadband today.

I brought along a chart, and I would just point out to you this was from April 5 in the *New York Times,* and it shows the policy that we have in various states as to taxing broadband access for the consumer. You'll look at this, and you'll note that there are three colors. In the yellow area, there is no tax on either DSL or on cable data modem. In the case of green, both are taxed. In the case of blue, only DSL is taxed; cable data modems are not taxed. How can we have a policy, a national policy, to get broadband in to every consumer—high-density markets or low-density markets—if we're going to have this type of difference between the regulations that states apply to a Federal issue?

So I believe that if we're going to have the policy, if we're going to catch up and move from number 11 in the world to where we should be as America, that we need a Federal approach to this.

Senator BURNS. Mr. Geiger?

Mr. GEIGER. The interaction of Federal oversight and state review of rate cases is a fairly mature process that I would say has worked well in the past. I think that states are very well suited to understanding their own constituents, and that many times there are very long and rich relationships between state commissions and the telecommunications companies in those states. So I think it should be preserved.

Senator BURNS. I've got to go get my glasses. I broke my glasses last night, and so I'll ask this question and then I'll leave.

If you were going to revisit the Act, and there's no doubt in my mind that somewhere along the line we're going to revisit this Act, give us one or two things that we should absolutely do, and give me a couple that we do not do.

The CHAIRMAN. That's a good question.

Senator BURNS. Mr. Dorman?

Mr. DORMAN. Well, I think in the case of how the Bell companies are regulated as a monopoly, we cannot lose sight of the aspect of what I said before in the Act, that de-monopolizing before deregulation—there should be a clear carrot for the Bell companies in that regard, that—you know, and sending someone to lose market share is a difficult thing to do, but I think anyone who looked at this at the time the Act was passed recognized that market-share loss would be inevitable, you know, going from monopoly to other things.

I would concur with Mr. Notebaert that in new markets, in markets where there is emerging capabilities, like cable modem and DSL, as long as the incumbent does not use this market power in the other area in any cross-subsidy mechanism, they should have deregulatory benefits in these new markets.

I think, on the other hand, new technologies, like Voice-over-IP, we need to have a policy of incenting them to be deployed. We need be moving faster than we are today, whether we're eleventh in broadband deployment or wherever we are. I would agree with Mr. Notebaert, we should be first.

The CHAIRMAN. How do you incentivize, Mr. Dorman?

Mr. DORMAN. I think in the case of new technologies, not applying legacy regulation, you know, things like the access-charge regime causing, you know, some groups of competitors to have to jump through hoops that others don't.

Take a look at what we did with the dial-up Internet service. In 1984, the ESP waiver was established, saying that information-service providers who use the local network don't have to pay access charges. What happened? The entire Internet early days was based on companies like AOL rapidly bringing service to customers, because they did not pay access charges the same way that the phone companies had historically paid them. Today, on Voice-over-IP, if we applied that same logic, not paying legacy access charges, the rate of adoption, I think, would near what we saw on dial-up Internet services. We created the entire Internet miracle largely because of the lack of regulation, or a different kind of a regulation, on those nascent services.

Senator BURNS. Mr. Notebaert?

Mr. NOTEBAERT. Senator, I go back to the 1996 Act and the opening line that I quoted in my earlier comments. I think we need to reduce regulation and recognize that technologies substitute for one another. And the whole regime was built on regulating copper wires, not applications. This is not about technology; this is about the customer. And the customer feels no difference in using a wireless device, whether it's for their computer, 802–11, or 802–16, which will be coming, or whether it's a copper wire or coaxial cable. I think we need to look at this from the eyes of the customer and recognize that the current regulatory format is sadly dated.

The second thing that I would do is, I would look very carefully at what universal service really means today compared to where we started. What is universal service, and what do we really want it to be?

Those are the two issues that I think need to be dealt with.

Senator BURNS. I would ask Mr. Geiger, but I'm going to stop right there—you know, we had two sessions—and I want to thank all of you at this table today—that were kind of closed-door stakeholders, and everybody was at the table for universal service. And we're almost to the point now where we're writing that bill. However, we're going to write it on the—probably the first end of it will deal with the revenues, and then I think it's very important that we should take a look at expenditures and how the money is spent and where it's spent. That will be more difficult, I think, than finding the revenue base to sustain the fund.

But we're almost there, and I just want to thank all of you. You were participants—Senator Dorgan—we hosted those closed meetings, and they were very good meetings. And so we can now move ahead on that.

Mr. Geiger, you want to respond? What's the first thing we should do and the first thing in your mind that we should not do?

Mr. GEIGER. Well, I think the first thing that we should do is preserve intramodal competitors' access into these pipes into the house. And in our business, we look at the pipe as a railroad track. It has capability that we can use differently. We can use the service equivalent, if you will, of putting a Mag Lev train on that railroad track. But without access to that last mile track in to the customer, we just simply don't have a business.

And it is irrelevant of what technology is involved. Technology has changed over time. Whether it's DSL, whether it's fiber, whether it's IP, we need access to those tracks to have a business and to compete with the incumbent. And I think any policy should preserve that right.

Senator BURNS. What shouldn't we do, then?

Mr. GEIGER. What we shouldn't do, in my opinion, is deny access on the basis of what technology is deployed.

The CHAIRMAN. Senator Wyden?

Senator WYDEN. Gentlemen, I know you've negotiated, and these negotiations are going on after the court decision with respect to new wholesale prices for competitors to access the incumbent's networks. Can you give us an update on what's going on? I mean, in some ways it's sort of hard to see, for example, how this is going to be of benefit to some of the incumbents, and I'm concerned about that. I'm also concerned that apparently some incumbents are taking the position that they don't need to disclose the deals they strike. So then you've got real problems for the little guy.

And so why don't the three of you just kind of give us a sense of where these negotiations are going, because I think that would be helpful.

Mr. GEIGER. Would you like me to start, sir?

Senator WYDEN. Go ahead.

Mr. GEIGER. Well, first of all, it's a little daunting to try and accomplish in 8 weeks what the FCC has not been able to accomplish

in 8 years. We are negotiating with a very, very powerful supplier that has many of the characteristics of a monopoly.

So it is difficult, and we don't have a lot of market power because there is truly no alternative for us to access upwards of 95 percent of our customers. Those railroad tracks, as I referred to, are only supplied by the local phone company, so we have very little leverage. And we have engaged in initial conversations, and really what we've gotten back is significant price increases, and price increases that would not allow us to sustain our business. And the assumption of the incumbent is that unbundling elements are gone.

Senator WYDEN. Mr. Notebaert?

Mr. NOTEBAERT. Senator, we view the negotiations as an opportunity to strike commercial contracts. These are distributors. I think it's a misnomer to call them Competitive Local Exchange Carriers, because, for us, it is a commodity, and we are a commodity business. We want every distribution channel we can get. So what we have done, we have struck an agreement already with Covad. We have, with MCI, gone out and hired—or, pardon me, retained—a mediator, Cheryl Perino, who is the head of the Wisconsin Commission. We have high hopes for that. We have a meeting tomorrow, in Colorado, where we've invited all of our distributors to come in, and we will try and reach an arrangement. And that is being worked by the mediator.

I think we can get there if people are willing to accept that the status quo has changed. And that'll be the difference.

Senator WYDEN. Sir?

Mr. DORMAN. I wish I could be as specific as I'd like to, but we are bound by nondisclosure in our negotiations specifically with the Bells. But I can say this, that there are different approaches being taken by the Bell companies. Mr. Notebaert's company has put a complete sunshine opportunity in place with a respected former commissioner, and I have high hopes for those discussions. They invited not only their direct negotiator, which is MCI, but all of the CLECs to be present in this hearing that will go on.

I think in the context of reality here, we have a reluctant supplier, who would prefer not to sell these items the way they are being sold today. That is reality. I would take this, and contrast it to AT&T's recent experience with the Cingular proposed acquisition of AT&T Wireless, our former wireless subsidiary. AT&T will get the use of the AT&T Wireless brand back, and we have announced our intention to reenter the wireless business. To do that, we will undoubtedly buy minutes from other wireless suppliers. And, as Mr. Notebaert knows, he himself has been able to go to the marketplace, to the six national wireless suppliers, and buy minutes and become a wireless distributor himself without owning his own networks facilities to do that. We' seeking to do the same thing.

I would simply contrast, in going to the six national wireless suppliers and saying, "Hey, I'd like to buy billions of minutes," the experience is very different than saying, "I'd like to spend nine-and-a-half-billion dollars with the Bell companies," as we do today as AT&T, and be treated like a customer.

Senator WYDEN. I appreciate that. And because the negotiations are ongoing, I understand there's limitation on what you can say, but I just hope we'll have as much transparency as we can, because

I think I'm particularly concerned about whether this can be a forum where essentially big guys can go after little guys and compound some of the problems. And I'm not accusing anybody of that, I'm just concerned that with lack of information it's certainly a possibility.

Let me ask you a policy question for the future with respect to the need to access to the last mile. And everybody constantly comes back to this issue. And I wonder if the three of you that last mile facilities are bottleneck. In some places they're a monopoly, maybe in other places they're a duopoly. But I'm curious whether you would say that mandatory access to the local loop now makes sense. And I'd just be interested in the three of you being on record on that.

Would you like to start, Dick?

Mr. NOTEBAERT. Yes. I think we would look at this, again—because people that buy this are our distributors—and I would rather get some return on an asset than no return on an asset. It's just good business.

I also believe, though, that there are multiple technologies. And, as I showed on the map that I held up, I continue to be amazed that we talk about copper wires, and we fail to talk about a cable company, again, that won't even let us advertise on their system. And we don't talk about wireless. And each day, we compete with wireless because customers have made a shift, in a lot of cases, and no longer have a wireline. So we seem to be hung up on one type of technology, versus regulating an application.

But let me go back and finish with—we would—I'm very comfortable with UNE now. I'm very comfortable selling those assets to our distributors.

Senator WYDEN. Mr. Dorman?

Mr. DORMAN. In 1984, AT&T had a high-90s-percent market share of the long distance business, and mandatory resale, in the form of selling WATS to Sprint and MCI, was a very key part of developing competition in long distance until some 20 years passed, and during the 1990s Sprint and MCI developed their own long-haul fiber networks, and their dependence on AT&T diminished. I was at Sprint for 14 years during that time, and I can say without access to AT&T's network we could not have built the ability to ubiquitously complete long-distance calls. That diminished over time.

I think in a case of access to the local exchange, we expect it to diminish over time as viable—economically viable technologies come to market that will allow us to accomplish for ourselves what we get from the Bells.

I've said this many times, and not to be funny about this, but it's certainly a perverse situation, where you're spending nine-and-a-half-billion dollars with four suppliers to have your eyes gouged out. And I wished all of them thought of us as distributors. So it does tend to make you highly motivated to develop your own facilities. But, being practical, for the 110 million American households and tens of millions of business locations, it will be a long time before there are viable means to reach all of them more economically than the use of the Bell network.

Mr. GEIGER. I would echo that. I think that the last mile is a bottleneck, especially if you try and segment the marketplace. Now, you could argue that there is another wire into a consumer, but wireless technologies are not available today that would displace broadband to businesses. And as they emerge, I think that the economics may become viable. They are not today.

Senator WYDEN. Thank you, Mr. Chairman.

The CHAIRMAN. Senator Sununu?

**STATEMENT OF HON. JOHN E. SUNUNU,**
**U.S. SENATOR FROM NEW HAMPSHIRE**

Senator SUNUNU. Thank you, Mr. Chairman.

As I listen to the supporters and the opponents of the 1996 Act talk about its shortcomings, I find it interesting that they all seem to be disappointed in the bill, whether they supported it or not, and their disappointment seems to flow from two particular areas, and I think they were mentioned in a number of the opening statements. One is a lack of clarity in the legislation itself, lack of clarity in the legislative language, and that's something that Congress obviously bears responsibility for.

In my discussions with interested parties and other legislators, it seems to me that that lack of clarity was created because we either attempted to predict where technology was headed, or we didn't foresee where technology was headed, and in the crafting of the language, therefore, we didn't deal with the kind of technical environment that we see today. But a lack of clarity is something that we should take away as being problematic, whether we're trying to write Voice-over-IP legislation or reopen the 1996 Act.

The second area are those circumstances where we delegated too much authority to regulators. A hundred pages of legislation, a thousand pages of regulation. I think that's just not quite the right ratio. I don't know what the right ratio is, but that's very, very problematic.

So, again, if you have a lack of clarity in the legislative language or you delegate too much to regulators, you get what we have, which is a lot of court cases and a lot of legal work, a lot of money being made by a lot of good lawyers, but we don't have an environment where people will step up to the plate and commit risk capital in the way they that would want to see to succeed in the deployment.

Those, for me, are the two important lessons as we either look at revising the 1996 Act or we begin to take up legislation like VoIP, which I appreciate.

I think at the last hearing the Chairman made a very polite gratuitous reference to my legislation, and I was very grateful for it. And now the witnesses have done it, and that's very flattering. But all that really is, is an attempt to make sure, going forward, we have as much clarity as possible in the legislative framework and that we're careful about what we delegate from a regulatory perspective. Some people have referred to it as a "lite regulatory touch." I don't mind that phrase. But the key is clarity.

As we talk about these issues—again, whether it's the broad context of the 1996 Act or Voice-over-IP legislation—I see two big potential areas where there might be, to use a technical term, a "food

fight." And that is on the issue of intercarrier compensation, one; and universal service, number two.

And what I would like to have each of the witnesses talk to is, In revising our intercarrier compensation system, what should be the principles for an equitable system? And what would be your principal concerns if we don't get an intercarrier compensation reform process right?

Mr. Dorman?

Mr. DORMAN. Well, I think that the discriminatory aspects of access today are what concerns us the most about intercarrier compensation. As I said before, ISPs pay one rate for the use of the local network, and they make heavy use of it, long call-holding times associated with sessions on AOL or whatever service provider you might use. Cellphone providers pay a different rate. CLECs pay a different rate. One class of Voice-over-IP call, based on last week's ruling by the FCC, pay interstate rates or intrastate rates, depending on the origination of the call, which in an Internet environment is difficult, if not impossible, of determining. And then, finally, intrastate access rates and interstate rates are vastly different. You know, a half a cent, roughly, for interstate rates, and state rates that range up to several cents—and in independent territories, as much as nine to ten cents.

We need to create a situation where technology deployment follows its own economics, not the access-charge regime's steering of it. And we remove from the system, encouraging arbitrage, at the nicest end of the spectrum, to outright deceit on the other end, by masking what a certain call may be to get a lower rate.

Senator SUNUNU. I'm sorry, you're talking about routing calls to specific regions in order to——

Mr. DORMAN. One form.

Senator SUNUNU.—avoid——

Mr. DORMAN. One form. You know, changing the jurisdiction of a call to interstate, for example, from intrastate, would allow someone to pay a much lower rate.

So we think that having completely technology and supplier-neutral access charges for the use of the local network is absolutely essential. We don't find it offensive to pay for use of the local network; we simply want all players to pay the same amount.

In doing so, the pool for universal service could be much more significant, and I think that we could find a compromise in this with the local exchange carriers, certainly the large ones.

Senator SUNUNU. Mr. Notebaert, do you agree with Mr. Dorman?

Mr. NOTEBAERT. I would start out by asking—and we support universal service, obviously, and would comply with whatever the policy that is established—but we should decide first what we're going to do, and then decide how to fund it.

Access charges, I think, can be put away, and we can do bill-and-keep. The question is, How do you want to subsidize? How do you want to tax? But to decide that, you have to decide what you want to do with it. And, as I said earlier, I think we need to determine what USF is in the future, and then we can go back and say, "How do we tax? How do we fund?"—versus creating huge funds, and then finding an issue for them.

Senator SUNUNU. So instead of deciding how much we want to spend, then decide what we want to spend it on, set some goals first——

Mr. NOTEBAERT. That's the thought, Senator.

Senator SUNUNU.—for accomplishment.

Mr. Geiger, do you agree with what's been said?

Mr. GEIGER. I agree with Mr. Dorman. I think that a call is a call. The use of the public switched network should be compensated, and an interLATA versus an interstate versus an international terminating call should not create an opportunity for arbitrage. And Cbeyond is, if not the only CLEC in the country, one of a few that is a bill-and-keep carrier for exchange of local traffic. We do not arbitrage on access charges.

Senator SUNUNU. And does that go for the larger organization, ALTS' support for a bill-and-keep system?

Mr. GEIGER. I'm sorry, I was speaking for Cbeyond.

[Laughter.]

Mr. GEIGER. I think you would find the flexibility with the ALTS organization in a transition mode from the current regime to a regime of a sort of "all users pay comparable charges."

Senator SUNUNU. But speaking as a forward-looking provider for Cbeyond, you would support a nondiscriminatory uniform system.

Mr. GEIGER. We would. Cbeyond would, right.

Senator SUNUNU. Thank you.

Thank you very much, Mr. Chairman.

The CHAIRMAN. Senator Lautenberg, I know you have a pressing appointment.

Senator LAUTENBERG. Yes.

The CHAIRMAN. I apologize.

Senator LAUTENBERG. There are not many of us here, but there's a World War II Memorial being dedicated out there, and half of this Committee on that case left—Senator Hollings, and I don't want to miss any words that Senator Hollings gives, I'll tell you.

I'd ask you this. Mr. Notebaert, you had—you're experts in local service, and technically you could go beyond your region if you wanted to get into the business—more of the local business and more of the opportunity that's presented. Why haven't you, for instance, among others of the old Bell systems, gone beyond the territories that were originally consigned to them, to try to compete in those areas?

Mr. NOTEBAERT. Senator, we do. We do billions of dollars outside of the 14 states where we are an incumbent local exchange carrier. We do business in Philadelphia, Atlanta, New York, San Francisco, Los Angeles——

Senator LAUTENBERG. Local——

Mr. NOTEBAERT. Yes, we do. Yes, we do. We compete head to head with the larger companies, the—what used to be called IXCs—and we've been very successful. In fact, the Yankee Group just put out a report talking about the fact that we had taken share from the top three providers, and we've been doing this for a number of years.

Senator LAUTENBERG. Do you offer, in those areas, the full range of services that Qwest might be offering in their local areas?

Mr. NOTEBAERT. Yes, we have. We have pulled back in two areas. We were offering DSL. We disposed of that business to Covad. We were doing pay phones outside of where we were the local incumbent exchange carrier, and we have disposed of that group of assets. But, other than that, we do consumer long distance, we do package switching, ATM frame, all the different types of services to everyone from the government to Crate and Barrel to Delta Airlines and others.

Senator LAUTENBERG. Mr. Dorman, are you able to move a facility into these markets? I assume Mr. Notebaert's company is not compelled by access charges that prevent them from moving ahead rapidly in these marketplaces that they go to. Do you have the same access?

Mr. DORMAN. We have—AT&T today provides local service in 46 states. That's a fairly recent occurrence. In fact, we did not provide service in any of the 14 Qwest states a year ago. We went into Arizona, as our first state in the 14 Qwest state regions, principally because of the prices that were charged for the unbundled elements in those states. The prices determine how broadly we can compete, or not. And I think in the case of AT&T, at least, we've found ways to enter some of the markets recently, because we have a bigger base now, we're amortizing our fixed investment over a larger number of customers. But I would say that we are dependent upon access to the Bell networks as certainly our entry strategy until we can build sufficient customer base to deploy our own facilities.

And just as a matter of clarification, Qwest is a combination of the old Qwest and the old U.S. West, so, in Mr. Notebaert's case, he actually has—well, you know, U.S. West was acquired by Qwest, and Qwest was operating nationally as an IXC, so it's the one example of a Bell company that is a hybrid, versus the other three, who are largely as they were before, local exchange companies.

Senator LAUTENBERG. What would happen with AT&T if access rates were increased to 50 percent, as has been petitioned, in that many instances?

Mr. DORMAN. Well, I can give you a specific example. Recently, the Indiana Commission raised prices that we paid SBC for access, and we've stopped marketing two of our most popular plans that consumers had selected because they are no longer economical for us to offer. While we've stopped short of completely exiting the market, we've made it clear if some of the requested rate increases were approved—in New Jersey recently, Verizon requested a 50 percent rate increase. The state commission granted a 14 percent increase. We weren't happy about that, but we can still continue to compete, albeit at what I'd consider to be a razor-thin margin.

If prices went up as proposed from some of the public statements the Bells have made about, sort of, their public offers during the negotiation period, it undoubtedly would lead to us having to exit, almost completely, the local market.

Senator LAUTENBERG. Interesting. Well, then part of your advertising campaign, which is fairly robust, is, you ought to say, "Well, we would charge a lot less even than we do—even than the low price that we do if your local company would permit us to come in and offer you these services." And there's no charge for that advice, I promise.

[Laughter.]

Senator LAUTENBERG. In New Jersey, Mr. Chairman, what happened is, the BPU granted Verizon a 14 percent increase, and they got so angry that they threatened to call off a $240 million investment in capital equipment to let New Jersey know how they responded to that. Not satisfied with a 14 percent increase. And this is not a company that's starving for earnings or revenues.

Thanks, Mr. Chairman, appreciate it.

Thank you very much.

The CHAIRMAN. Thank you.

I'm not sure if Senator Cantwell or Senator Dorgan is next. Senator Dorgan, do you——

**STATEMENT OF HON. BYRON L. DORGAN,**
**U.S. SENATOR FROM NORTH DAKOTA**

Senator DORGAN. Mr. Chairman, thank you.

First of all, let me thank the witnesses for the testimony today. I think that this hearing, which is the first of a couple of hearings, is important and kind of sets the stage for a broader discussion about some of these issues.

Let me also point out that I think—while we're talking about different devices by which people communicate, I think the interests of the 1996 Act was about a set of principles, not devices. Doesn't matter to me much whether somebody is talking over a telephone that's connected to a wire that goes to a wall someplace, someone is speaking on a cell phone, or someone else is on VoIP using a computer. The issue is the set of principles. And one of the principles was to promote competition.

Now, even when we wrote the 1996 Act, we understand there was robust aggressive competition with respect to long distance. We knew that, because all of us got calls at home every day, relentlessly, asking whether we would be willing to change our long distance carrier. There were some 500 competitors, and at least when we wrote the 1996 Act the cost of long distance had diminished substantially as a result of that robust competition. The same was not true with respect to local service and local exchange.

So the design of the Act was an attempt to promote competition in the local exchanges, number one. Number two, the Act did talk about reducing regulation. And, number three, about preserving the principle of universality. And the reason that that's important is, we, long ago, decided that communications ought to be universally available at an affordable price. So we did anticipate—although we didn't know exactly what advanced services would be, we did anticipate advanced services, because we wrote the provision in law talking about advanced services, and we provided in law also that the Universal Service fund, which shall be continued under the 1996 Act, would promote comparable service at comparable prices.

Now, why is that important? Because in some parts of the country it had traditionally been much more expensive to provide these communications services than in other parts of the country. And so the Universal Service Fund was to drive down those high-cost areas so that Donald Trump could call a telephone in Grenora,

North Dakota if he wanted to. Not that he would. But the fact is, everyone would have access to a telephone at an affordable price.

So those were the principles in the Act. And, frankly, while I think a lot has changed since 1996, those principles haven't changed, and the need to pursue those principles have not changed, in my judgment.

I think that, Mr. Chairman, a number of bad decisions have been made by, first of all, an FCC that's made wrong decisions, and, second, an FCC that has been content to observe. So you've got two different problems over a period of about 8 years; one, making bad judgments, and then, in other circumstances, deciding to make no judgments and simply be an observer, despite the fact that we pay them are regulators.

So, you know, we come to this point, in the year 2004, and we have what I think is an interesting discussion, because I think perhaps these three witnesses represent a pretty healthy slice of most of the competitive circumstances, in terms of what changes are necessary and how we proceed.

I understand that if I were in Mr. Notebaert's chair or Mr. Dorman's chair or Mr. Geiger's chair, my responsibility is to my business, the stockholders, and advancing the interests of that business, period, end of story. That's the responsibility. And so if I have Mr. Notebaert's customers, I don't want anybody coming to get them. If I have a dominant position in the local exchange, I don't want anybody coming to get them. To the extent that I can prevent that and protect my base, that's what I'm going to do. If I'm in Mr. Dorman's position, I want to—what I want to do is maximize my capability of going to get the customer somebody else has, and then trying to anticipate with what technology we're going to compete in the future, and how do I best accomplish that. These are difficult, vexing decisions that we have to make, both in the private sector and in the public sector.

Let me make just one or two other points.

Mr. Notebaert, first of all, I think you're a breath of fresh air for Qwest. When I say "fresh air," I don't mean that you're a kid and you haven't been there very long; I mean that——

Mr. NOTEBAERT. I can take that, that's OK.

Senator DORGAN.—I mean that Qwest was a company that's very important to my state and was being run in a way that was devastating, in my judgment. And I regret that those who ran it that way did that, but that's change. I respect the work you're doing, I'm glad you're there and that you've changed the orientation of that important company.

And, Mr. Dorman, you and I have talked before, I have no idea how you make decisions in this environment in a business of the type that you're in.

But these are very interesting, difficult, in some ways, very challenging times. And let me just ask one question, if I might, because I think there are many other questions. And what I would perhaps like to do is send you some questions, because we're going to have some other hearings, and I do want to get some of this on the record.

It deals with this issue of competition. Facilities-based competition is not something that happens like that, and we understood

that in 1996. You're not going to stand up—and we didn't in long distance—you're not going to stand up a separate industry that says, "All right, today we've got facilities, we're going to compete." So the result is, we kind of develop an approach, like UNE–P and requiring unbundling and so on, or bundling, and try to create this competition.

Mr. Notebaert, you indicated that you're in Philadelphia, I believe, for local exchange service. Is that facilities-based competition or—how do you compete in——

Mr. NOTEBAERT. We have facilities throughout the United States. We also purchase——

Senator DORGAN. For local——

Mr. NOTEBAERT.—local loops or private lines from companies. We do not use UNE–P.

Senator DORGAN. All right.

Let me just say that I hope in this period, post-action by the courts, that when we have these negotiations that are going on for the 45-day period—I hope that to the extent that we can make them available to the public and let some sunshine in, as I think you have done, Mr. Notebaert, in your area, I hope that occurs.

And let me just ask the question, What happens if we don't succeed in making any progress in the 45-day period and things collapse and we don't have the capability under UNE–P any longer to access other facilities? I assume that the answer to that is, it dramatically, dramatically diminishes the opportunity to promote local competition in the local exchanges. Is that correct?

Mr. DORMAN. Well, based on our reading of the decision and what it asks the FCC to do, it would be our belief that, without further appeal to the Supreme Court, that UNE–P as a mechanism disappears because the Bells don't want to provide it at the current price levels that are regulated. And my view is that all 50 states didn't get it wrong with respect to setting cost-based prices. I think it's been pretty clear from the price-increase request across the Bell companies, that we are seeing price increases, you know, that would average nine to ten dollars per loop, which would translate into 50 to 100 percent price increases in some cases. That would take our already very thin margins as the largest UNE–P reseller, down to the point where we could not continue. So AT&T, from its part, would have to exit those local markets, because we wouldn't choose to keep doing something we lose money at.

Mr. GEIGER. While it wasn't our interpretation, we've been informed by a couple of the phone companies, the incumbent phone companies, that it is their interpretation that access to unbundled network-element loops—not the platforms, not the switching—we don't buy that—but the loops themselves were vacated. And we have been told that, as of June 16th, we would not be able to order them anymore and that the price increases—they would revert to the interstate special-access tariffs, which are between three- and four-hundred percent increases over our UNE-loop pricing.

So my quick answer is that it would be Armageddon in the industry, nationally I can speak for all of our members on that.

Senator DORGAN. Mr. Notebaert?

Mr. NOTEBAERT. Yes, I think that commercial negotiations are always better. And from our point of view, since we face severe

competition from wireless and cable television—maybe more than others, I don't know; I mentioned the Omaha statistics—it's very important for us to find common ground so that our distributors are pushing our product. I think UNE–L and access to the loop is a good thing. Where I have a problem is with UNE–P, because the whole concept is total—totally economically foreign. I mean, arbitrage is a bad thing, not sustainable, especially the arbitrage built upon taking a cost structure of a future incremental cost, and not the actual cost of the asset that you put in. And so I have a lot of problems with that.

We've put forth a plan at the FCC. We made it public. We've also entered into mediation. I think—maybe I'm optimistic—I think reasonable people negotiate all the time. And we've done it with satellite providers so that we have competition. Those negotiations aren't simple, but one has to be willing to compromise. And when one's not willing to compromise, one shouldn't have a guarantee of their business success. There's risk in everything we do.

Senator DORGAN. Mr. Notebaert, just one final point. The question the Chairman asked in response to your testimony about the 24 hours for the cable, is—the approval—is that not because the cable was defined as an information service?

Mr. NOTEBAERT. No. It's because we don't regulate—we chose, in the Telecom Act, to regulate copper wires and not regulate the application or telephony. We don't regulate telephony. We regulate copper wires. And as the court said, you know, we probably shouldn't treat these companies as pinatas. There's more to this than that. And if we're going to regulate, we should regulate applications. And our only plea, as I showed in the chart from the *New York Times,* is that it be consistent, that it be balanced, and that there is a chance for success for those of us who invest billions of dollars every year.

Senator DORGAN. And my final point is that whatever the application is by which someone communicates, the principles, in my judgment, that persuaded us to proceed with an act in 1996 remain the same principles today.

The CHAIRMAN. Senator Cantwell?

**STATEMENT OF HON. MARIA CANTWELL,**
**U.S. SENATOR FROM WASHINGTON**

Senator CANTWELL. Thank you, Mr. Chairman.

And, gentlemen, I've heard most of your testimonies and read parts of it, and we've had this discussion now for the last hour or so. But I want to ask you a question. And if you could, I'm requesting—if you could, just answer in a yes-or-no fashion to this first question. And the reason I'm asking it is because I think it really does boil down to how we view Voice-over-IP in the next year or two, and whether we should regulate it or not. Because I hear various things coming out of the panel. So just a yes-or-no answer from each of you on whether you think Voice-over-IP, just, say, for the next 2 years, should be regulated.

Mr. DORMAN. No.

Mr. NOTEBAERT. No. I want to add one thing. Yesterday, we announced that we wouldn't charge access fees on VoIP.

Mr. GEIGER. Yes.

Senator CANTWELL. Thank you. Thank you for that brevity. I'll give you a chance to explain in a second.

My second question, Isn't this dilemma really—now that we know that technology is evolving and that we all want to be in the Voice-over-IP business, and we all want to have is a level playing field—isn't the real issue that the definition under the Telecom Act of "information service" is not really sustaining us, not really allowing the FCC to make decisions that will create a level playing field, and actually creating a lot of havoc and legal fees and an unpredictable environment, instead of predictability?

Mr. DORMAN. Well, I think the notion of information service—again, going back 20 years, to nascent suppliers at the time that we were hoping to promote their evolution—is a far cry from where we are today. Yahoo, as an information service provider, uses the Internet network, doesn't pay access charges to use the Internet network, but provides a range of services—you know, not necessarily voice today, but perhaps voice tomorrow—and their market capitalization is over twice what AT&T's market capitalization is, not that that—I'm just making the point that when you think about——

Senator CANTWELL. So you think, yes, information services is limiting? Because I have a question that I do want you to spend a lot of——

Mr. DORMAN. Yes.

Senator CANTWELL.—time on.

Mr. DORMAN. Information services needs to—be reformed.

Mr. NOTEBAERT. I don't think that's the issue. We didn't regulate wireless the same way we did wireline, and look at how it's blossomed, and look how well it's done. We didn't regulate many different features that we have out there, and they blossom, and technology and investment is made. We could blame it on the definition of "information service," but it's really a question of, do you want to regulate an application or a technology?

Senator CANTWELL. So you think the definition suits us well and we should keep it?

Mr. NOTEBAERT. I'm fine with it.

Senator CANTWELL. Interesting. Thank you.

Mr. Geiger?

Mr. GEIGER. I don't have anything to add to that comment, but did you want me to explain my——

Senator CANTWELL. Let me ask one more question——

Mr. GEIGER. Sure.

Senator CANTWELL.—and then anybody can explain anything that they want.

Mr. GEIGER. OK.

Senator CANTWELL. My question is—there is a lot of dialogue floating around there by MCI and others. I have a feeling that Vince Cerf, as I—as most people think of him, the Father of the Internet—probably had a hand in promulgating this notion. And this notion is that our current infrastructure on telecom is this siloed approach, if you will, having the various titles of voice and wireless and audio broadcasts and radio and everything else. And shouldn't we move more to a physical layer, with the applications on top of it?

And I—this is very interesting, because Mr. Notebaert is actually advocating that we do something to regulate the application, but I would propose—I think I agree with this proposal. I think it's the other way around. I think you should look at the transport layer, and then have net neutrality on top of that, and have everybody—because you're all going to be in the same business in 10 years, I guarantee it—or the ones that can navigate their way through this. We'll all be in the same business. Everybody's going to offer video, everybody's going to offer Voice-over-IP, all of that. So why not look at the transport layer, regulating the transport layer, and then having the applications on top of that be the things that we leave alone? So that's what I'd like your comments on.

Mr. DORMAN. I think the way I see it is that we tend to debate the voice application a lot, and the fact is, it's the one application—if you look across all the services that can flow through an IP network—streaming video and audio, you know, finding out what the weather is in Seattle tomorrow, moving your photos to oPhoto, you know, meeting someone over the Internet, whatever the application may be—voice is consistently singled out for different treatment.

Our notion is, Services-over-IP, or SoIP, as we call for it, is very similar to your view, which is, once you have a broadband network in place of sufficient speed and the software tools of quality of service that exists in the IP network realm today, the notion that you're going to take one application and treat it differently from everything else that we know about today or ultimately will see developed just doesn't make good sense.

Senator CANTWELL. They're all bits.

Mr. DORMAN. It's all bits at some level. So our notion is that we certainly see voice requiring special things because of the interactivity of the human conversation. You know, latency in a network matters, so you've got to be able to have the bits leave one person's mouth and arrive at the other person's ear in a coherent fashion. So there will be voice application service providers. That's what AT&T seeks to be. Some of them will own networks and deploy them because it fits their requirements, and some won't.

Senator CANTWELL. Mr. Notebaert, if I could—I hope Qwest—being in the West, I hope Qwest is the broadband video service delivery. I would get my video on demand from Qwest in the future.

Mr. NOTEBAERT. I'd be happy to take your order today.

[Laughter.]

Mr. NOTEBAERT. Right after—I'll get the information.

I would be OK with net neutrality, except we don't have it. Take a look at your bill for your telephone service, look at the fees that the government applies. Take a look at your wireless bill, look at the fees that are applied. Take a look at your cable bill and look at the fees that are applied. If you mean by "net neutrality" that we're going to regulate them all the same, I'm with you. But we have been incapable of seeing the world through the eyes of the customer. We haven't done this.

Senator CANTWELL. So, in the future, if everybody was pushing bits, and all the bits were basically the same—I mean, obviously, there are more bits in streaming video than there is in IP telephony—but you believe if you were in that business and Mr. Dorman was in that business, all the bits would be net neutral, that every-

body would be pushing everybody's bits at the same speed, and that you wouldn't tax somebody or regulate some—one of those applications—I'm concerned about your comments about regulating the applications.

Mr. NOTEBAERT. I'm just trying to get us to move from the status quo of regulating a pair of copper wires to move toward regulating cable telephony, or cable, the same way, or regulating wireless the same way, so that we do have neutrality. The only way I know to get people there is to use the discussion of the application that's run over the networks, and that starts to bring people back to what's really important, and that's customers. We spend a lot of time talking about things, but most of the time the discussions don't come down to what's important, and that's the customer, who's the center of our universe.

Senator CANTWELL. And I think that is the concept of the transport layer, is that everybody coaxial—everybody would be——

Mr. NOTEBAERT. Then I would be very supportive.

Mr. GEIGER. This is very rich discussion. I think it speaks to the Senator Dorgan's notion about principles. And a principle I think that we need to keep in sight is intramodal. And if you were here for my analogy about a train track—it might not be very articulate, but we don't have a business without access to that train track, which I would call the transport layer. Today, we happen to use a technology that is a next-generation technology—allows us to deliver a richer—more rich cargo within our train cars than our competitors do. And so we get customers because of that. And, you know, that's an opportunity to induce others to buy and deploy new broadband technologies, new service technologies.

So I would agree with you in your analogy that the transport layer, broadband, and the access to those train tracks and the last mile, are essential for competition, and we think that competition is best served by intramodal.

And I would tell you that my opinion on VoIP—first of all, voice bits fetch more money than other bits, and that's why there's this much discussion around it.

Senator CANTWELL. Today.

Mr. GEIGER. Today.

Senator CANTWELL. Today, they do.

Mr. GEIGER. That's right. Today. But I think VoIP needs to be held accountable for other public service issues, like E911, like CALEA. And I don't think VoIP should get a hall pass on access charges.

Senator CANTWELL. Well, Mr. Chairman, I know my time is expired, but, under the transport layer of the future, you would change your opinion and then say VoIP——

Mr. GEIGER. That's correct.

Senator CANTWELL. You would not change your—OK.

Thank you, Mr. Chairman. And if I could just add—I know the Chairman entered into the record a statement for the Consumers Union and the Consumer Federation of America, but I would just request, if—I know we're going to have more hearings—but if they could testify sometime in the future, I think that this set of hearings are important hearings, and I know it seems like many of them get down to the battlefield of current business, when I think

we need to keep in mind the ultimate effect we're trying to strive for, as the 1996 Act tried to, is, How do we protect consumers in the future to more economical—in this case, delivery of bits?

Thank you.

The CHAIRMAN. I'll certainly do that. And I—as you know, they have testified before this Committee on many occasions on a variety of issues, and their opinions are highly valued.

I thank the witnesses for their time today. We've been more than 2 hours. We thank you for being here, and you've contributed a great deal to our efforts that I think are necessary to get underway. And whether we do anything this year or not, or next year, it's certainly important, I think, to review the Act and to see what areas we need to change and improve on. And I thank the witnesses.

And this hearing is adjourned.

[Whereupon, at 11:30 a.m., the hearing was adjourned.]

# A P P E N D I X

PREPARED STATEMENT OF HON. DANIEL K. INOUYE, U.S. SENATOR FROM HAWAII

Thank you. Mr. Chairman. Today's hearing is an opportunity for the Committee to revisit progress made since passage of the Telecommunications Act of 1996, in promoting greater competition in the communications marketplace. Lest we forget, we should remember that our efforts to rewrite the 1996 Act were taken only after many hearings and much debate. I trust that our consideration of potential future changes in telecommunications policy will be taken with similar care.

In my view, the 1996 Act was an important piece of legislation designed, first and foremost, to bring the benefits of competition to local markets. Since that time, competitors have provided millions of Americans with a choice of local telephone service and lower phone rates. The benefits of this competition also extend to customers of the incumbent phone companies, as competitive pressures have forced them to become more efficient and to respond with competitive bundles of telecommunications services.

Yet, despite measurable benefits, the growth of competition in local markets it is still only in its early stages. In most areas of the country, the Bell operating companies and other incumbent providers still retain the lion's share of local telephone lines. Indeed, according to recent FCC data, incumbent phone companies today—eight years after the 1996 Act—still retain over 85 percent of all local access lines across the nation.

Mr. Chairman, it is abundantly clear to anyone regularly reading the business section of their daily newspaper that the telecommunications industry in the midst of some fundamental technological changes. In many cases, these advancements have the potential to provide consumers with new features and services that may enhance productivity and promote economic growth. But, in addition, these new technologies raise some important policy questions that need to be carefully examined and answered. For example, should providers of similar services be subject to similar regulation, or are their legitimate reasons for different regulatory obligations? How will new communications technologies affect our commitment to universal service in rural and insular areas? And, what action may be necessary, if any, to ensure that network providers do not discriminate against competitive service offerings? These are only a few of the many questions that we will have to wrestle with in the coming months.

As such, I appreciate the Committee's efforts to begin this discussion and look forward to the testimony from today's witnesses.