

## **INTRODUCTION AND EXECUTIVE SUMMARY**

Verizon Massachusetts' application should be denied because its unbundled network element pricing is not cost-based and does not support effective competition. That one critical failure infects multiple aspects of this application. Most of all, Verizon has failed to meet checklist item two, 47 U.S.C. § 271(c)(2)(B)(ii), which imposes on Verizon the burden of proving that it has made available unbundled network elements at just, reasonable and non-discriminatory prices based on the costs of the elements. Verizon's eleventh-hour decision to abandon its prices rather than defend them shows that even Verizon understands that the rates upon which it must rely are indefensible. In addition, the absence of competition due to uneconomic UNE pricing contributes to Verizon's failure to meet its burden of proving working OSS, access to DSL-compatible elements, and adequate performance standards and penalties. Finally, because defective pricing erects an impassable barrier to entry into the local residential market, the Commission should conclude that a grant of this application is contrary to the public interest, as well as a violation of the checklist.

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At its most basic level, local residential competition requires that competitors have the technical ability to interconnect with and share the multi-billion dollar local telephone infrastructure, and that they be able to do so at a price that allows them profitably to offer consumers competitive services. The 1996 Act is designed to accomplish these twin goals: its central provisions open the incumbents' networks and mandate that the FCC oversee a federal wholesale price structure that is reasonable and includes non-discriminatory and cost-based pricing. In section 271 Congress also created an incentive: if the BOCs open their networks

with cost-based competitive prices and satisfy the other elements of the checklist, they can participate in their in-region long-distance markets.

In early section 271 applications, several BOCs attempted to win entry into their long-distance markets before they had truly opened their local markets. In part because the FCC's pricing authority was subject to legal challenge, the decisive issues facing the FCC and state commissions in these early applications usually concerned whether the BOC networks were open as a technical matter. In landmark decisions by the Michigan Public Service Commission and the FCC in 1997, bolstered by subsequent FCC decisions in South Carolina and Louisiana, regulators made clear that paper promises to comply with the Act's market-opening provisions would not be enough, and that the BOCs had to prove, with solid empirical data, that they actually provide the same network access to competing carriers that they provide to themselves.

The results of these decisions are now plain to see. The Bell Companies who want access to their long-distance markets are increasingly willing to undertake the necessary technical work to open their local networks to get that access. After the Ameritech and BellSouth decisions, the Bell Companies literally went back to the drawing board, participating with experts like KPMG to create and test operations support systems that actually do support the activities necessary to share network facilities. The applications since these seminal early section 271 decisions have seen the development of important particulars of working OSS. And while the BOCs have not yet completed the necessary work to implement commercially ready OSS, all parties now understand and accept that true working OSS is an achievable goal and a baseline prerequisite for section 271 approval.

The lesson of this recent history should not be forgotten. Without regulators mandating that competitors have fair and workable access to BOC networks, there would be little prospect

of local residential competition today. Without federal support, state regulators that wanted to open their markets would have been on their own, the bar would have been set so low that applicants would have had only to go through the motions of checklist compliance to prevail, and the failure of local competition would have been chalked up to unrealistic Congressional expectations and renewed assertions of a “natural monopoly” in local telephony.

But even perfect OSS is useless if the network’s lines and switches cost too much to lease. So today the Commission stands at another crossroads, and the issue is pricing. Just as in 1997, the BOCs hope that the Commission lacks the will to insist that the Act really means what it says, that “reasonable” wholesale prices must be “based on cost.” And just as in 1997, the stakes for local residential competition are enormous. If wholesale prices that are indefensible (and, indeed, are undefended) are found to be “good enough,” the Bell companies will redouble their efforts to resist cost-based pricing, and the effort to open the local markets will be set back immeasurably.

The Commission has fought hard to vindicate its authority to insist on local wholesale pricing that works because it is cost-based. Now is the time for the Commission to stand by its judgment that pricing must be right – not perfect, but within a range that fairly derives from the Commission’s cost-based pricing principles – before section 271 authority is granted. Verizon’s last-minute stunt of substituting one set of unacceptable rates for another as a way to preempt any rational analysis of its pricing should not be tolerated. As we show in what follows, based on the facts Verizon presents on this record, its application must be denied. And while no detailed analysis of its tariff filing of October 13<sup>th</sup> is either possible or relevant to this proceeding, it is worth noting that its “new” rates are not supported by any cost studies on the record, and appear to lead to the same competitive dead-end that has left most Massachusetts households without a choice of local telephone providers.

Our Comments are organized in the following manner:

First, WorldCom sets forth the relevant legal standard, which requires the Commission alone to find compliance with the competitive checklist, including the requirement that prices for network elements be “just, reasonable” and “based on . . . cost.” 47 U.S.C. § 251(c)(2); id. § 252(d)(1). It is equally clear that the burden of proof is on Verizon to develop a record that proves checklist compliance. While the standard is not perfection, the prices must be good enough so that the Commission is comfortable that the prices fairly derive from the forward-looking costs of the elements taking into account the particular conditions present in each state.

WorldCom then shows that Verizon has failed to carry its burden of proving that its network element prices are cost-based and reasonable. WorldCom focuses particularly on the price of unbundled local switching, though it also describes Verizon’s failure of proof on other element prices, including transport and loops.

As to switching, WorldCom shows first that there is a complete failure of proof on Verizon’s part. Verizon does not even address most criticisms that have been leveled at its rates. And its cost study, which it submitted but does not defend, is equally unrevealing. Critical figures relating to the switching costs are explained only on the ground that they have been spit out of a proprietary model that is not made part of the record. Of course, if Verizon intends to rely on its Friday the 13<sup>th</sup> switching prices, despite its gross violation of the Commission’s “complete when filed” rule, there is no record at all for the Commission to evaluate.

Next, we show that to the extent figures can be evaluated at all, many are grossly inflated. Thus, while switches are purchased at large discounts from switch vendors, Verizon set the switching rates as if it never received these discounts. And while it may cost as much as 10% of the cost of the switch to have the switch installed, Verizon makes the ludicrous assumption that it

pays well over half as much to install a switch as to purchase it in the first place. And to further jack up its switch price, Verizon makes the indefensible assumption that every single building it owns is built solely to house switches, so that literally its entire building plant's costs are larded into its switch price. These and other errors have a compounding effect: the rates generated by Verizon's compliance cost study (which was adopted virtually in its entirety by the Massachusetts Department of Transportation and Energy ("DTE") from Verizon's initial study), bears no relation whatsoever to Verizon's real costs in purchasing switches, never mind to the forward-looking cost of reproducing its switch plant.

Nor is there room to doubt that the results here are deeply flawed. Verizon's cost model values the switch plant as worth between \$2 and \$3 billion. But the FCC's own TELRIC model values that same switch plant at only \$500 million, and Verizon reports its embedded switching costs as having a book value of only \$600 million. Thus, on the generous assumption that Verizon's embedded costs are themselves not grossly inflated, Verizon's switching rates ought to be reduced by some 77%. The same point is made by comparing Massachusetts' switching rates to those of other states. Such a comparison similarly shows that Massachusetts' rates are three to four times higher than rates in other states. These are not cost-based rates. They are at least four times cost-based rates.

While Verizon's switching rates are the most egregious example of non-cost-based rates, WorldCom also explains how transport and loop rates are not cost-based and need to be recalculated.

Next WorldCom shows that it and others have repeatedly called on the Massachusetts DTE to correct these rates, and that the DTE has consistently declined to do so. Given the magnitude of the errors and the DTE's track record, this is not a case in which the market is open

now and the FCC can rely on the DTE promptly to make the necessary corrections to the rates after this application is granted.

Nor is Massachusetts the least bit like New York, where the state commission has aggressively challenged Verizon's cost proposals and insisted that rates based on cost models with serious defects be promptly corrected. As this Commission frequently has stressed, such differences are critical, for checklist compliance is a contextual inquiry, and the FCC must "look at each application on a case-by-case basis and consider the totality of the circumstances" to see if the checklist is satisfied. TX Order ¶ 46. To state the obvious, rates that satisfy TELRIC and the checklist in New York for any number of reasons may well be inadequate in Massachusetts. As the D.C. Circuit Court of Appeals warned in approving the FCC's judgment that New York's switching rates satisfied TELRIC under the circumstances present in New York, "application of TELRIC principles may result in different rates in different states." AT&T Corp. v. FCC, 220 F.3d 607, 615 (D.C. Cir. 2000).

It should come as no surprise that rates this flawed have devastating competitive consequences. WorldCom shows that reliance on Verizon's rates creates a competition-killing price squeeze. For the average consumer, Verizon's UNE-P wholesale rates are actually higher than its retail rates. A competitor offering retail service for the same price as Verizon, relying on a combination of elements leased from Verizon at its extortionate rates, would find itself almost \$11 in the hole for each customer each month, even before it started to pay its own internal costs of providing service, never mind thinking about a profit. Nor is the picture any different if a CLEC were to take advantage of somewhat lower switching usage rates negotiated by Z-Tel. Application of that rate only reduces the price squeeze to a \$4 per customer loss each month, without considering CLEC costs.

In this regard, Verizon's cynical tariff filing this Friday the 13<sup>th</sup> is too little and too late. Too late because it is not and cannot become part of the record of this case, and therefore cannot properly play any role in the Commission's consideration of this application. Too little because a preliminary analysis suggests that these newest rates still substantially exceed Verizon's costs and still do not allow for competitive entry using UNE-P. While no definitive analysis is possible on such short notice, the new rates appear to be useless, as are the rates they replace.

Next, WorldCom demonstrates that there are a host of potential problems with OSS, performance measurements and Verizon's DSL offering whose full competitive impact cannot be fairly assessed on this record. In these ways as well, Verizon has failed to carry its burden of proving that it has fully implemented the competitive checklist.

WorldCom finally shows that when leased elements are priced out of reach, it is not in the public interest to allow Verizon into the long-distance market. To do so would be to remove Verizon's only incentive to lower its wholesale rates, and so would be to consign the majority of residential customers in Massachusetts to Verizon's monopoly local service. Whatever the marginal benefit to consumers of having another competitor join the already competitive long-distance market is far outweighed by the loss of any prospect of competition in the local markets for the majority of residents of the state, as well as the hard to long-distance competition posed by Verizon's continuing local monopoly.

For all of these reasons, this application should be denied.

**FEDERAL COMMUNICATIONS COMMISSION  
WASHINGTON, D.C. 20554**

In the Matter of	)	
	)	
Application by Verizon New England Inc.	)	
Bell Atlantic Communications, Inc.	)	
(d/b/a Verizon Long Distance), NYNEX	)	CC Docket No. 00-176
Long Distance Company (d/b/a Verizon	)	
Enterprise Solutions), and Verizon Global	)	
Networks Inc., for Authorization to Provide	)	
In-Region, InterLATA Services in Massachusetts	)	
_____	)	

**COMMENTS OF WORLDCOM, INC. ON THE  
APPLICATION BY VERIZON FOR AUTHORIZATION TO PROVIDE  
IN-REGION, INTERLATA SERVICES IN MASSACHUSETTS**

Verizon seeks permission to enter the in-region long-distance market in Massachusetts when it has erected an impassible barrier to entry in its local market. It has priced unbundled network elements at non-cost-based rates so high that competitors cannot as a practical matter use unbundled network elements (“UNEs”), and in particular the unbundled network element platform (“UNE-P”), to provide broad-based service to residential customers in the state. Because of this barrier to entry, Verizon cannot point to solid commercial evidence that its OSS works. To make matters worse, it also has declined to report performance measurements that would capture critical aspects of this evidence for the few residential orders it does handle. Nor does Verizon provide nondiscriminatory access to the elements of its network necessary to provide advanced services. For these reasons, it has failed to carry its burden of showing that it has met the requirements of the competitive checklist, or that long-distance entry would be in the public interest.



**I. VERIZON HAS NOT MET ITS BURDEN OF PROVING THAT IT HAS  
SATISFIED THE CHECKLIST'S PRICING REQUIREMENTS.**

**A. Legal Framework**

Verizon's burden here is to prove that it has "fully implemented" the requirement of the second checklist item that it provide access to unbundled network elements "in accordance with the requirements of sections 251(c)(3) and 252(d)(1)."<sup>1/</sup> Section 251(c)(3) in turn specifies that network element rates be "just, reasonable and nondiscriminatory" and in compliance with section 252's requirement that rates be cost-based and non-discriminatory.

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<sup>1/</sup> Section 271(c)(2)(B)(ii) of the 1996 Act. See NY Order ¶ 44; MI Order ¶ 105; LA II Order ¶ 50 (noncompliance with a single checklist item sufficient to deny application). A table of citation abbreviations and corresponding full citations is provided above, following the Table of Contents.

The FCC has “emphasize[d] that it is [its] role to determine whether the factual record supports a conclusion that particular requirements of section 271 have been met.” MI Order ¶ 30. While the Commission must consult with the state commissions to verify compliance with all checklist items (section 271(d)(2)(B)), it is not required by statute to give the state’s evaluation any particular weight. Thus it has made clear that it “has discretion in each section 271 proceeding to determine what deference the Commission should accord to the state commission’s verification in light of the nature and extent of state proceedings to develop a complete record.” MI Order ¶ 30.<sup>1/</sup> The D.C. Circuit, charged with reviewing the FCC’s section 271 judgments, reached the same conclusion, holding that “the statute does not require the FCC to give the State commissions’ views any particular weight. . . . Congress has clearly charged the FCC, and not the State commissions, with deciding the merits of the BOCs’ requests for interLATA authorization.” SBC Communications, Inc. v. FCC, 138 F.3d 410, 416-17 (D.C. Cir. 1998).

In considering what weight to give to state commission evaluations, the FCC has pointed out that it is willing to give credence to state commission resolution of factual disputes where the state has “conducted an exhaustive and rigorous investigation into the BOC’s compliance with the checklist.” NY Order ¶ 51. The FCC also has indicated it is more willing to accept state benchmarks “if the state commission has made these determinations in [a] rigorous collaborative proceeding,” though it retains the right to “reach a different conclusion where justified.” Id. ¶ 56. Specifically addressing challenges to state-set UNE rates, the Commission has found it relevant that the state “engaged in extensive fact-finding in its rate case” and did not simply rubber-stamp

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2/ See, e.g., TX Order ¶ 11 (“the Commission has discretion in each section 271 proceeding to determine the amount of weight to accord the state commission’s verification”). This is in direct contrast to the Commission’s responsibility to give the Attorney General’s evaluation “substantial weight.” 47 U.S.C. § 271(d)(2)(A).

ILEC-proposed rates. Id. ¶ 246 (accepting PUC-set rates in part because state scrutinized and then rejected BOC rates and adopted prices close to those proposed by CLECs).

A state's evaluation of pricing is not entitled to any different weight than its evaluation of any other checklist element. To the contrary, consistent with its statutory mandate, the Commission has made it clear that it alone must decide whether the BOC has satisfied the pricing requirements of the checklist. It specifically rejected the contrary view urged by the BOCs that it "confine its pricing role under section 271(d)(3)(A) to determining whether applicant BOCs have complied with the pricing methodology and rules adopted by the state commissions," and the FCC's view was definitively upheld by the United States Supreme Court.<sup>3/</sup>

The Commission thus concluded that the "Act vests in the Commission the exclusive responsibility for determining whether a BOC has in fact complied with the competitive checklist. In so doing, we must assess whether a BOC has priced interconnection, unbundled network elements, transport and termination and resale in accordance with the pricing requirements set forth in section 252(d), and, therefore, whether the BOC has fully implemented the competitive checklist." MI Order ¶ 282. See also, e.g., SC Order ¶ 210 (expressing "concern" with the South Carolina Commission's approval of rates alleged not to be cost-based). Of course to meet its burden of proving such compliance, the BOC must put on the record the particulars of the rate case that support the rates upon which it relies. NY Order ¶ 241.

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<sup>3/</sup> See Iowa Utils. Bd. v. FCC, 135 F.3d 535, 543 (8th Cir. 1998) (rejecting the FCC's view of its authority), rev'd, 525 U.S. 1133 (1999).

Moreover, in deciding what weight to place on the state's view that pricing is cost-based, the Commission also has taken pains to caution that the label the state attached to its pricing methodology is irrelevant. For states that merely pay lip service to TELRIC principles, prices do not avoid scrutiny by being labeling "TELRIC":

We emphasize, however, that it is not the label that is critical in making our assessment of checklist compliance, but rather what is important is that the prices reflect TELRIC principles and result in fact in reasonable, procompetitive prices. . . . [Of course] TELRIC principles will not generate the same price in every state; indeed it will not even generate the same formula for pricing in every state. But such principles are fair and procompetitive and should create even opportunities for entry in every state, while permitting, indeed obliging, each state commission to determine prices on its own. In order for us to conduct our review, we expect a BOC to include in its application detailed information concerning how unbundled network element prices were derived.

MI Order ¶¶ 290-291.

That is not to say that the FCC is required to undertake its own cost study in the 90 days it has to review an application, or that any small error identified in the BOC study means that the prices are not cost-based. Rather, the Commission has made clear that it will reject an application "if basic TELRIC principles are violated or the state commission makes clear errors in factual findings on matter so substantial that the end result falls outside the range that the reasonable application of TELRIC principles would produce." NY Order ¶¶ 244, 246.

The legal requirement of independent decisionmaking by the FCC on pricing issues is well grounded in sound public policy. "Because the purpose of the checklist is to provide a gauge for whether the local markets are open to competition, we cannot conclude that the checklist has been met if the prices for interconnection and unbundled elements do not permit efficient entry. Moreover, allowing a BOC into the in-region interLATA market in one of its states when that BOC is charging noncompetitive prices for interconnection or unbundled network elements in that state could give that BOC an unfair advantage in the provision of long distance or bundled

services.” MI Order ¶ 287 (emphasis added). For that reason the Commission also made clear that competitive pricing is “a relevant concern in [its] public interest inquiry under section 271(d)(3)(C).” Id. See Point III, infra.

**B. Verizon’s Unbundled Network Element Pricing Is Neither Reasonable Nor Cost-Based, And Therefore Fails To Meet The Checklist Requirements.**

Remarkably, Verizon has almost nothing to say about its network element pricing. Its application does not argue that the rates satisfy the checklist, and its brief “public interest” discussion of pricing is notable mostly for what it does not discuss. Verizon’s only declarant to address the issue is content briefly to recite the chronology of the state’s cost proceeding and the state’s justifications for refusing to consider mounting evidence that its rates were not cost-based. See Mudge Decl.

As previously indicated, the Commission has specifically required each applicant “to include in its application detailed information concerning how unbundled network element prices were derived.” MI Order ¶ 291. This is especially critical when pricing was a central disputed issue before the state: “[A] BOC must address in its initial application all facts that the BOC can reasonably anticipate will be at issue. Through state proceedings, BOCs should be able reasonably to identify and anticipate certain arguments and allegations that parties will make in their filings before the Commission.” TX Order ¶ 37.

Pricing, and in particular the pricing of unbundled local switching, was perhaps the central focus of the recently concluded section 271 proceedings in Massachusetts. WorldCom and AT&T offered concrete evidence that the switching rates were not cost-based, pointing out flaws in, among other things, the switching discount, the cost of capital, the installation factor, the

utilization rates, and miscalculation of the off-peak factor.<sup>4/</sup> But, apart from a passing reference to the fact that the DTE rejected CLEC arguments about the switching discount, Verizon makes no mention of a single one of these critical issues anywhere in its application.

In an extraordinary act of contempt for the Commission and its rules, rather than attempt to defend the rates on which it based its application, Verizon instead has decided to change them altogether the business day before interested parties must submit comments, assuring that no one has the opportunity to respond adequately to the new rates at this time. The Commission's response to this distraction must be to decide the case on the record presented to it when the application was filed. Indeed, it has no other choice.

To begin, such a response is compelled by the Commission's "complete when filed" rule that governs this application, which forbids an applicant "at any time during the pendency of its application, [to] supplement its application by submitting new factual evidence that is not directly responsive to arguments raised by parties commenting on its application." TX Order ¶ 35. The very point of the rule is "to prevent applicants from presenting part of their initial prima facie showing for the first time in reply comments." Id. Of course, that is exactly what Verizon intends to do by changing its rates now. Thus, Verizon apparently intends to rely on the prima facie showing it made in its New York section 271 application to defend its rates here. As we show in what follows, such reliance is unjustified, but for present purposes it is enough to note that

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<sup>4/</sup> See Joint Declaration of Dr. August Ankum and Vijetha Huffman On Behalf of WorldCom, Inc., DTE 99-271 (DTE filed July 18, 2000) (VZ-MA App. B, Tab 455).

Verizon would deny commenters sufficient opportunity to rebut that case, the very situation the “complete when filed” rule is designed to prevent.

If Verizon wants new rates to be considered as satisfying its checklist obligation, its only choice is to withdraw and refile its application, and to produce the record evidence upon which it seeks to rely in showing that the new rates are TELRIC-compliant. Any other process would be sheer lawlessness.

Moreover, even if Verizon sought to amend the record to include these new rates, and even if the Commission were for some reason inclined to consider the new rates, the record would be grossly inadequate to prove Verizon’s prima facie case that these rates are cost-based. The rates, we are told, are “the same” as New York rates. But none of “the extensive records of the New York Commission’s network element rate case” that the Commission ruled were needed to carry Bell Atlantic’s burden of proof in New York are on this record. See NY Order ¶ 241.

Nor is this some mere technical quibble. The missing record evidence is critical to resolving the question whether the record that supported a prima facie case in New York is adequate to support a prima facie case in Massachusetts. There is good reason to believe that it is not. The New York Commission considered what it acknowledged to be a defective switching rate that it ordered to be reconsidered, but reviewing a whole range of New York-specific factors “asserted that it ‘appropriately exercised its power to take account of conditions in New York’ when it determined switching costs pursuant to TELRIC.” Id. ¶ 245 (quoting New York Commission Reply at 46).

Such a modulated and state-specific judgment cannot be imported wholesale into another state. Specifically, there is no record pursuant to which the FCC could “take account” of differences in “conditions” in New York and Massachusetts that might lead the FCC to reach a

reasoned conclusion about application of New York rates in Massachusetts. Among other things, there is no way on this record for the FCC to conclude that in Massachusetts, as in New York, “the switching prices at issue here . . . provid[e] ample margin to competitors even at their present level,”<sup>5/</sup> one of the many factors that led the New York Commission to leave flawed rates in place temporarily in New York, and one of the many factors the FCC considered when it approved those rates in the context of Bell Atlantic New York’s section 271 application.

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<sup>5/</sup> In re Joint Complaint of AT&T Communications of New York Inc. et al., Order Denying Motion to Reopen Phase 1 and Instituting New Proceeding, Case 95-C-0657 et al. at 12 (NYPSC Sept. 30, 1998) (“Order Instituting New Proceeding”) (VZ-MA App. B, Tab 455, Exh. F).



Because checklist compliance is by its nature such a contextual inquiry, the Commission has made clear that “each state commission” is “indeed obligat[ed]” to “determine prices on its own.” MI Order ¶ 291. Importing one component of a New York rate package into a suite of Massachusetts rates without saying a word about why this substitution satisfies TELRIC principles in Massachusetts obviously will not do. That these New York rates may not satisfy Verizon’s checklist pricing obligations in Massachusetts is suggested by a cluster of factors, including serious uncorrected problems in the rates for a variety of UNEs in Massachusetts, the DTE’s lack of commitment to correct these problems on an urgent basis, and the failure of Verizon’s newest UNE rates to provide an adequate margin for competition.<sup>1/</sup> And, to repeat, even if, arguendo, the New York prima facie case could be imported wholesale into Massachusetts, still competitors here have had no opportunity to rebut that case, and there is as yet no record to be rebutted.

In sum, whatever Verizon’s strategy, this application should be denied because Verizon fails to offer adequate proof on what it knows to be one of the central issues in the case.

**1. Verizon’s Switching Rates Are Not Cost-Based or Reasonable.**

The failure of Verizon’s current switching rates – those operative today and in place when Verizon filed this application – to meet the cost-based standard set by Congress is demonstrable from every relevant vantage point. First, from the vantage point of Verizon’s Massachusetts cost studies, the assumptions and inputs Verizon used are unjustified and unjustifiable – and

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<sup>6/</sup> We share below our preliminary assessment that these new rates are in fact not adequate for widespread competition. See infra p. 33 n.45. Not even a preliminary assessment is possible on the host of other issues relevant to TELRIC analysis. As our analysis of the DTE rates set out below makes clear, the question of whether the various inputs that support a rate are set within a reasonable range is complex and calls for detailed analysis that cannot be accomplished overnight.

inconsistent with assumptions and inputs the Commission, other ILECs, and even Verizon have used in estimating the cost of providing local switching in other states and proceedings.

Second, from a wider vantage point, Verizon bases its UNE rates on an estimated cost of the switch plant needed to serve Massachusetts that is more than four times the estimate calculated by this Commission. Indeed, Verizon's UNE rates are based on an overall estimate that is more than four times its own historic, embedded costs – as reported by Verizon itself to this Commission.

Verizon's switching and port rates are not just a little too high, they are quadruple what they would be if legitimately based on cost, as Congress directed. Verizon attempted to side-step this failure to comply with the preconditions for section 271 authorization by entering into a negotiated interconnection agreement with Z-Tel and then offering the same "promotional" rates to others. But this is a wholly inadequate attempt to cure for a number of reasons. As a matter of law, the so-called Z-Tel rates cannot satisfy the cost-based standard because they are not based on any cost estimates or calculations, and Verizon does not pretend otherwise. The Z-Tel rates are made up of numbers arbitrarily plucked from the air.

In any event, the Z-Tel switching rates remain far higher than cost-based rates. First, the Z-Tel agreement does not even offer a "promotional" rate for analog switch ports. Thus, the only rates available for analog ports are the dramatically inflated rates proposed by Verizon and adopted by the DTE.<sup>1/</sup> Second, as we show in what follows, even those per minute switching rates that are covered in the Z-Tel agreement are not reduced to cost-based levels. Verizon has offered urban rates reduced by 30% and suburban rates reduced by 35%, whereas reducing the

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<sup>1/</sup> The Z-Tel agreement also offers no alternative to the per minute switching rate in the most dense "Metro" region of the state.

rates to a genuinely cost-based level would require cutting the lower Z-Tel rates by at least two-thirds.

The FCC need not undertake to set the appropriate rates in this proceeding. The statute requires only that the Commission assess whether Verizon has proved that its rates are within a range that would result from reasonable application of the standard Congress and the FCC established. By all the evidence – from any vantage point – it is clear Verizon has not provided such proof..

- a. Verizon's switching rates are based on unexplained and unjustifiable inputs and assumptions rejected by the FCC and other states.**

Many of the inputs and assumptions underlying Verizon's switching usage and port rates cannot be reviewed at all. Notably missing in Verizon's comments, declarations, and volumes of CD-ROMs is any coherent description of the way in which its unbundled switching rates are derived from the forward-looking cost – indeed any cost – of providing the switching. Verizon's defense of its switching rate is that it derives from Telcordia's (formerly Bellcore's) Switching Cost Information System ("SCIS") – a proprietary engineering cost model upon which Verizon relied in developing its rates. To the question – "why is this input set at this number?" Verizon's answer is "that is how it came out of the SCIS."<sup>8/</sup> The SCIS model is not in the record, the algorithms and many of the inputs are thus unknown to regulators and potential competitors, and Verizon made no effort to defend any of the SCIS outputs. Bryant Decl. ¶ 16. Because Verizon relies on figures that cannot be analyzed, and does not even attempt to provide any other defense of its rates, it has failed to meet its burden of proving that its pricing is based on the cost of providing switching. The Commission has previously rejected switching models that rely on SCIS because "the defaults used to generate the results . . . have not been placed on the record in this proceeding." In re Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Fifth Report & Order, 13 F.C.C.R. 21323, ¶ 78 (1998). It should do the same here, for as to many issues, there is simply no way to know which inputs and assumptions could be found questionable, if they were available to be questioned.

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8/ See NYNEX's Revised Version of Anglin's Test. at 15 (VZ-MA App. H, Tab 97).

Nonetheless, even within the limits imposed by Verizon's choice to rely on a secret cost model, WorldCom has been able to identify seven unreasonable inputs and assumptions that significantly inflate Verizon's Massachusetts switch-related rates. These involve calculations performed by Verizon on the numbers that emerge from the SCIS model. Because these calculations can be rerun using numbers and assumptions that are consistent with the findings of this Commission, other ILECs, and Verizon in other states, it is possible to determine the impact of replacing these unreasonable values with reasonable ones. Bryant Decl. ¶¶ 17-18.

As we demonstrate in what follows, correcting these seven errors alone would reduce the Verizon Massachusetts rate for analog ports by more than 77% and the rate for switching usage by 63% to 67%, depending on geographic zone. Bryant Decl. ¶ 18 (tables). In other words, taking into account only these seven errors, Verizon's port rates are more than four times higher than cost-based rates, and its switching usage rates are about three times higher than cost-based rates.<sup>1/</sup> As noted, correcting these seven errors alone reduces the switching usage rates to approximately half the "promotional" Z-Tel rates.<sup>1/</sup>

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<sup>9/</sup> This critique hardly exhausts the list of errors in the studies. For example, Verizon relied

i. Vendor discounts

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on then-current minutes-of-use assumptions rather than a projected future minutes-of-use factor. The latter assumption failed to capture even the annual growth typical at the time Verizon undertook its cost studies, much less the growth that has occurred as a result of the phenomenal growth in the Internet over the last five years. Bryant Decl. ¶ 36 n.25.

10/ There is no Z-Tel rate for analog port charges.

In calculating the cost of switches, Verizon failed to apply the large discounts that vendors routinely provide to switch purchasers. Instead, it applied only the much smaller discount offered by vendors for expanding existing switches.<sup>11/</sup> No one suggests that these smaller discounts apply to initial switch purchases.<sup>12/</sup> To the contrary, Verizon itself now acknowledges that switch vendors routinely provide the much larger discounts when carriers purchase switches not accounted for in its cost studies.<sup>13/</sup>

But when switch prices were first set, Verizon (then NYNEX) made very different claims. Verizon declined to open its vendor contracts to scrutiny in both New York and Massachusetts, and when MCI and AT&T first challenged its failure properly to account for switch discounts, Verizon falsely claimed in New York that the most recent switch discounts it had received – when it converted from analog to digital switches – should not be expected in the future and therefore

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<sup>11/</sup> Phase 4 Order, D.P.U. 96-73/74, 96-75, 96-80/81, 96-83, 96-94, at 36-37 (DTE Dec. 4, 1996) (“Phase 4 Order”) (VZ-MA App. H, Tab 162) (citing Verizon’s testimony that it had used the discounts currently obtained for purchases of incremental additions to existing switches).

<sup>12/</sup> Bryant Decl. ¶ 20. This SCIS model is based on list prices and therefore does not reflect any of the discounts vendors offer. Id.

<sup>13/</sup> Declaration of Nancy Sayer, In re NYNEX Corp. And Bell Atlantic Corp., Application for Consent to Transfer Control, Tracking No. 960205, 960221, ¶ 10 (FCC filed Oct. 22, 1996)



should not be reflected in a forward-looking model.<sup>14/</sup> In Massachusetts Verizon also argued that the cost model should not rely on the actual prices it paid for switches because “if we wanted to carry this TELRIC thought experiment to its ultimate and we assumed that all people in the industry were doing this all at the same time, I would suggest we would pay much higher prices than we are today, because there would be a worldwide shortage of digital switches.” Transcript of 11/6/96 Hearing, at 356 (VZ-MA App. H, Tab 119).

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(“Sayer Decl.”) (Bryant Decl., Att. 3).

<sup>14/</sup> See Hearing Transcript, NYPSC, Case 95-C-0657 et al. at 3004-06 (Testimony of C.R. Curbelo On Behalf of Bell Atlantic) (VZ-MA App. B, Tab 455, Exh. D).

Yet in October 1996, at the same time it was telling Massachusetts regulators that reliance on its past discounts was inappropriate and unduly “speculative,” in the course of the Bell Atlantic-NYNEX merger proceedings, Bell Atlantic was telling the FCC to the contrary that it should rely on the fact that it always obtains large discounts on switch purchases. In that context it testified that the Commission should assume for purposes of future planning that switches cost much less than the retail price, because “[t]he pricing structures imposed by switch vendors, including Lucent Technologies, favors the purchase of new switches, rather than switch upgrades. Vendors offer substantial discounts on new switches, but do not offer comparable discounts on switch upgrades.”<sup>15/</sup> Its statements to the contrary in New York and Massachusetts had been misrepresentations.

Verizon denies none of this, but argues instead that since the FCC passed on its misrepresentations in New York, so it should pass on them here.<sup>16/</sup> It is therefore instructive to review how the two state commission’s addressed Verizon’s misstatements.

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<sup>15/</sup> Sayer Decl., ¶ 10 (emphasis added) (Bryant Decl., Att. 3).

<sup>16/</sup> See VZ-MA Br. at 69.

In New York, the Commission as an initial matter rejected NYNEX's proposed switching rates based on the inadequate discount because they were so out of line with the rates proposed by AT&T and MCI. Instead, "'appropriately exercis[ing] its power to take account of conditions in New York,'"<sup>17</sup> the New York Commission selected rates closer to those proposed by AT&T, though it did not directly apply the larger discounts in adopting its compromise switching rate. Thereafter, when the New York Commission learned that it had been misled by Bell Atlantic, even though it had not adopted Bell Atlantic's rate in the first place, it directly confronted Bell Atlantic's false testimony, and rejected Bell Atlantic's attempt to minimize it as an "inadvertent misstatement." The New York Commission reminded Bell Atlantic on the record that its statements were "unequivocal and were made not only in discovery response and brief but also on cross examination" and were for that reason "distressing" and "disruptive of the process."<sup>18</sup> It then rejected the same Bell Atlantic argument that the Massachusetts DTE later accepted – that the relevant discount is that provided for the incremental purchases of switch ports – since that argument "forgets that a Total Element Long-Run Incremental Cost (TELRIC) analysis of the sort used in these proceedings contemplates the construction of a new system."<sup>19</sup>

While the New York Commission acknowledged that the existing switching rates were defective, reviewing the New York record, it concluded that piecemeal correction of the rates was not possible given the extent to which it had already modified the rate to account for Bell

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<sup>17</sup>/ NY Order ¶ 245 (quoting New York Commission).

<sup>18</sup>/ Order Instituting New Proceeding, at 9 (VZ-MA App. B, Tab 455, Exh. F).

<sup>19</sup>/ Id.

Atlantic's "seriously flawed" studies.<sup>1/</sup> It therefore agreed to review all rates promptly, but found no need to make immediate changes to correct the error, because "the switching prices at issue here are much lower than New York Telephone's retail prices, providing ample margin to competitors even at their present level."<sup>1/</sup>

Reviewing this process, the FCC acknowledged the many factors that went into the New York Public Service Commission judgment, and "stress[ed] that we place great weight on the New York Commission's active review and modification of Bell Atlantic's proposed unbundled network element prices, its commitment to TELRIC-based rates, and its detailed supporting comments concerning its extensive, multi-phased network elements rate case." NY Order ¶ 239. See also id. ¶¶ 245-246.

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<sup>20/</sup> Id. at 3.

<sup>21/</sup> Id. at 12.

In Massachusetts, in contrast, the DTE began by accepting virtually without any modification NYNEX's switching rate proposal based on the erroneous small discount. Addressing claims that the switching discount was inadequate, the DTE accepted without question NYNEX's argument that if all the BOCs had to purchase all of their switches at the same time, there would be a shortage of switches, and so the TELRIC price of switches might well be higher than the discounted prices the CLECs alleged NYNEX received.<sup>4/</sup> The DTE thus concluded that any cost-based calculation of switching rates would be too "speculative," since it

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<sup>22/</sup> Phase 4 Order at 36-37 (VZ-MA App. H, Tab 162). Leaving aside that this is obviously not the kind of analysis contemplated by TELRIC, it also is entirely unfounded as an historical matter. The analog to digital switch conversions for which NYNEX received large discounts did involve all of the ILECs, and did not lead to scarcity of supply or higher prices. Moreover, the FCC also has consistently concluded that cost-based pricing must give competitors the advantages of scale economies enjoyed by incumbents. In re Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98, First Report and Order, 11 F.C.C.R. 15499, ¶ 11(1996) ("First Report and Order").

required the DTE “to assume what manufacturers’ discounts would be if a TELRIC network were being constructed today.” It then accepted without any explanation NYNEX’s decision to apply only the small discount which applied only to switch add-ons to all switching costs.<sup>1/</sup>

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<sup>23/</sup> Phase 4 Order, at 37 (VZ-MA App. H, Tab 162).

Worse yet, in stark contrast to the New York PSC, DTE's response to Bell Atlantic's admission of a material misstatement regarding switch discounts was to refuse to reconsider the switching rate.<sup>1/</sup> Indeed, rather than reconsider the rates, it decided to make them permanent, and declared that it would refuse to consider them again until December 2001.<sup>1/</sup> Then, as the residential competitive situation continued to stagnate, earlier this year it once again declined to reconsider the switching rate, and created ambiguity that the review would begin even in 2001.<sup>1/</sup>

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<sup>24/</sup> See Consolidated Petitions of New England Telephone and Telegraph Co., Phase 4-A Order, D.P.U. 96-73/74, 96-75, 96-80/81, 96-83, 96-94, at 8-9 (DTE Feb. 5, 1997) ("Phase 4-A Order") (not included in record attached to Verizon's application) (Bryant Decl., Att. 2). DTE's July 27, 2000 Letter Denying AT&T's Petition Requesting the Review and Reduction of UNE Recurring Charges ("DTE 7/27/00 Letter") (VZ-MA App. B, Tab 481).

<sup>25/</sup> DTE's Order Granting BA-MA's Motion to Adopt Permanent UNE Rates, DTE 98-15 (Phase II, III), at 15-16 (DTE March 19, 1999) (VZ-MA App. F, Tab 157).

<sup>26/</sup> DTE 7/27/00 Letter at 3-4 (VZ-MA App. B, Tab 481).

The DTE's decision to apply only the small discounts available for switch upgrades is inconsistent with the New York PSC's decision to reject NYNEX's switching rates when they were first proposed, inconsistent with the New York PSC's subsequent decision to review rates when it learned the truth about vendor contracts, inconsistent with the FCC's chosen approach to estimating switch costs,<sup>1/</sup> inconsistent with TELRIC and court decisions interpreting TELRIC,<sup>1/</sup> and inconsistent with even an embedded cost calculation, which would have to account for the price of both new switches and switch upgrades. The resultant rate is grossly inflated and not cost-based.

The precise discounts available to Verizon in Massachusetts from applicable vendors is not known because Verizon, which bears the burden of proof, stubbornly continues to refuse to put its contracts on the record – even under a protective order. However, Verizon has submitted testimony in other proceedings from which it is possible to estimate the impact of applying new purchase discounts rather than upgrade discounts on Massachusetts rates. See Sayer Decl. ¶ 11 (Bryant Decl., Att. 3) (explaining that the total cost of the hardware and software for a new switch can be \$55 - \$60 per line, but the cost of hardware alone for adding an additional capacity would be \$125 per line).

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<sup>27/</sup> This Commission, in its Universal Service proceeding, determined that a forward-looking cost estimate for switches must be based entirely on the cost of new switches, at the steep discounts vendors offer for such purchases, and not on the cost of switch upgrades at all. In re Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Tenth Report and Order, 14 F.C.C.R. 20516, ¶¶ 315-317 (1999) (“USF Tenth Report and Order”); Bryant Decl. ¶ 22.

<sup>28/</sup> See Bell Atlantic - Delaware, Inc. v. McMahon, 80 F. Supp. 2d 218, 238-39 (D. Del. 2000) (“In the long run . . . an efficient and rational competitor would replace all of its existing switches with the most current technology and receive the bulk-rate discounts. . . . Bell's proposed switch costs, which it premised upon the smaller add-on discounts . . . [is] deficient in that it does not reflect a long-run approach.”).



Based on the differential in discounts testified to by Verizon's own witness, WorldCom has recalculated the Verizon rates. Bryant Decl. ¶ 24. Recalculation using the discounts applicable to purchases of new switches – and changing no other input – reduces analog port rates by 55% and switching usage rates by 38% to 41%. Id. In other words, Verizon essentially doubled its rates by making an indefensible assumption, by misrepresenting facts, and by withholding the underlying contracts that would have exposed the extent of its misrepresentation.

ii. Installation factor

Verizon also wildly inflated its estimate of its cost to install switches. As is usual, Verizon calculated its estimate of its installation costs as a factor of the cost of the switch itself. But its rates are based on the implausible assumption that it must spend another 65.4% of the cost of the switch to install it. In other words, if a switch cost \$1 million, Verizon would have to spend an additional \$654,000 to install it in a wire center. Bryant Decl. ¶ 26. Verizon's inflation of the installation factor is particularly invidious because it builds on every overestimation in the basic switch costs in the first place for a magnifying effect on the rates Verizon imposes on its potential competitors. Id. For example, if Verizon claims that a switch costs \$1.5 million, but it really costs \$1 million, the installation factor adds not only an inflated \$654,000 based on the appropriate \$1 million switch cost, but also another \$327,000 based on the spurious half a million dollars Verizon wrongly added to switch costs.

Every other available source – including Verizon itself in another context – makes clear that the installation cost Verizon Massachusetts “estimated” for purposes of imposing costs on its potential competitors are at least six times higher than any reasonable estimate for such costs. For example, a number of ILECs, including Bell Atlantic, submitted cost estimates as part of the FCC's Open Network Architecture proceedings. Bell Atlantic's estimates included switch

installation factors ranging from 6% to 10%. HAI Consulting, Inc., HAI Model Release 5.0a, Inputs Portfolio, § 4.1.8, Jan. 27, 1998 (citing Bell Atlantic's ONA filing (FCC Docket 92-91) on Feb. 13, 1992) (Bryant Decl., Att. 4).<sup>1/</sup>

If Verizon's rates are recalculated, changing only the installation cost estimate to a more reasonable 10% of switch costs, correction of that error alone would reduce analog port rates by 33% and switching usage rates by 23% to 25%. Bryant Decl. ¶ 29.<sup>1/</sup>

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<sup>29/</sup> Southwestern Bell submitted cost estimates of 8% to 12% in the same proceeding, Id. (Citing SBC's ONA filing (FCC Docket 92-91) on May 18, 1992) (Bryant Decl., Att 4). More recently, BellSouth submitted installation cost factors ranging from 5.9% to 15% in the FCC's Universal Service proceeding. Reply Comments of BellSouth Corp., In re Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Attachment 1, Ex. 2-13 (FCC filed June 12, 1998) (Bryant Decl., Att. 5). The Bell model uses a nationwide default installation factor of 5.77%. Ex Parte Letter from Pete Sywenki to Magalie Roman Salas in CC Docket Nos. 96-45 and 97-160 (Aug. 20, 1998) (attaching Bell Switch Model Inputs, page 17, April 30, 1998 edition) (Bryant Decl., Att. 6).

<sup>30/</sup> Any claim by Verizon that its installation factor should be higher because it performs more of the installation work itself rather than relying largely on the vendor, as do other ILECs, is

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either implausible or irrelevant. It is implausible because if Verizon were undertaking tasks worth more than 50% of the cost of a switch, rather than requiring those tasks to be performed by the vendor, the price of the switch to Verizon should reflect an additional, substantial discount to account for that. But Verizon has not discounted the switch cost output from the SCIS model to reflect different installation terms, and its overall switch investment figures are higher, not lower, than in other states. See Bryant Decl. ¶ 27 n.18. In any event, it is not reasonable for Verizon to assume self-installation of switches if self-installation really costs six times more than vendor installations.

iii. Busy hour conversion factor/Weekend and holiday usage.

Verizon's switching usage rates are based both on calculations of the overall traffic-sensitive costs of the switch plant needed to serve Massachusetts and calculations of how many minutes switches will be in use, in order to determine what rates need to be paid per minute to provide full recovery of switch costs. Bryant Decl. ¶ 31. Therefore, the estimation of the number of minutes of use is critical. If the estimate is too low, the rate per minute will be too high – because the same switch costs will be need to be recovered from fewer minutes. Id. ¶ 32. In that situation, Verizon will recover more than its actual switch costs, because it will have recovered its full costs after the smaller number of minutes is reached, and all usage over that would be an unjustified cost imposed on its competitors, and pure gravy for Verizon.

Verizon's calculation deliberately and inexcusably underestimates the number of minutes switches will be in use, to achieve just this result. Verizon allegedly based its estimation on an undisclosed traffic sample for the month of March 1996. Id. ¶ 35. However, in calculating usage, Verizon counted only business days, of which there were 21 that month. It did not count any of the ten weekend days or holidays that month, as if no one ever used their telephones or computers on weekends or holidays. Id. ¶ 36. Verizon, nonetheless, charges its competitors for the switching their UNE customers use on weekends and holidays.

If Verizon's rates are recalculated, replacing only that assumption with the conservative estimate that switch usage on weekends and holidays is half of what it is on business days, correction of that error alone would reduce switching usage rates by 19.2%. Id. ¶ 37.

iv. Utilization factor

Verizon also underestimates the percentage of switch facilities that are “spare” – installed but beyond what is currently needed in determining its port rates. Some operational “headroom”

is expected, to permit unexpected increases in demand or failures in equipment. But Verizon adds to the utilization factor included in SCIS, which appears to be 95%, an additional utilization factor of 85.26%. Id. ¶ 39. Thus, Verizon assumes that only 81% of switch capacity will actually be in use.

Objective evaluation results in the conclusion that significantly less “headroom” is needed. For example, this Commission has determined that 94% of the line ports on switches are available for use, and only 6% headroom is required. Id. ¶ 40

By underestimating the utilization factor, and therefore the amount of the port capacity that is deemed to be in use, Verizon increases its overall estimate of switch costs, because more port capacity is assumed to be needed to provide the same level of service. Inflating the overall estimate of switch costs increases the rates Verizon imposes on its potential competitors. For example, if Verizon had assumed a port utilization rate of 94%, as did the FCC, it would have increased its switch costs to accommodate this headroom by only 6.3%. Id. ¶ 41. By assuming that a significantly larger amount of headroom was needed, Verizon increased the assumed switching costs on which it based the rates it charges competitors by 23%. Id. ¶ 39. If Verizon’s rates are recalculated, replacing its underestimated rate of 81% with the more appropriate assumption, correction of that error alone would reduce analog port rates by 13.7%. Id. ¶ 41.

v. Cost of capital

Verizon’s overestimation of the cost of capital also inflated switch rates by inflating its annual switch carrying charge factor. Cost of capital is determined by calculating the cost of equity (the return on the shareholders’ investment in the switches), the cost of debt to finance the purchase of the switches, and the weighting of the financing obtained from each. Id. ¶ 42.

Verizon inflated the cost of capital in two ways. First, the DTE set a cost of equity factor of

13.5%. Second, Verizon assumed that 76.49% of switches were paid for by shareholders' investments and only 23.51% were paid for by borrowing. Id. ¶ 43. As is true for Verizon's installation factor, its inflation of its cost of capital factor also builds on every overestimation in the basic switch costs for a magnifying effect on its switch rates. Id. ¶ 43 n.29.

The cost of equity factor used by Verizon – 13.5% – is not cost-based. The arbitrator, and the DTE initially, made a determination as to the proper method for calculating the cost of equity. Phase 4-A Order at 5 (Bryant Decl. Att. 2). When Verizon used that method, it reached a cost of equity of 11.38%, which it then challenged as too low in a motion for reconsideration to the DTE. The DTE then arbitrarily chose a new cost of equity factor – not by application of any method of calculation, or resulting from any cost study – of 13.5%. Id.

In addition, Verizon inflated the cost of capital figure by assuming that an inordinate proportion of its switching investment was paid for by shareholders as opposed to by borrowing. These are not interchangeable categories. Equity is more expensive than debt financing and also incurs income tax costs. Bryant Decl. ¶ 45. Verizon's assumption that 76.49% of its switch plant would have to be paid for by investors and that only 23.51% could be financed by borrowing bears no relationship to its actual situation or to any forward-looking model of capital financing. It simply serves to inflate the rates it charges competitors. The FCC has found that 44.2% of local network costs are financed through debt and only 55.8% from shareholder investment. See In re Represcribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers, CC Docket No. 89-624, Order, 5 F.C.C.R. 7507, ¶ 231 (1990) (“Represcription Order”).<sup>1/</sup>

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<sup>31/</sup> The Commission found that the capital structure of other types of companies did not accurately depict the capital structure of RBOCs and therefore based its equity to debt ratio on

Verizon's overall cost of capital calculation – based on these improper assumptions – is 12.16%. Bryant Decl. ¶ 44. That figure is significantly higher than the 11.25% figure this Commission has used in parallel proceedings to determine both cost estimates for universal service and costs of supplying local access to long distance carriers in its interstate ratemaking proceedings. Id. (citing USF Tenth Report and Order, ¶¶ 432-435; Represcription Order, ¶ 231). This is virtually the same cost of capital initially required by the DTE when it applied a forward-looking methodology, but later amended when NYNEX asked for a higher number to be substituted. See Phase 4-A Order at 5 (Bryant Decl., Att. 2).

If Verizon's rates are recalculated, replacing only its cost of capital assumption with the cost of capital the FCC uses, correction of that error alone would reduce both switching usage and analog port rates by 7.6%. Bryant Decl. ¶ 46.

vi. Building factor

Verizon also added a factor to its estimation of overall switch costs to cover the cost of buildings associated with switches. In calculating the building factor, however, Verizon did not merely allocate those building costs that are actually associated with switches; instead it allocated all of its building costs to its estimation of switch costs, as if the company did not use any part of any building for sales representatives, engineers, collocation space for which it is already being compensated, office workers, storage, etc. Id. ¶ 48. There is no legitimate reason to do so.

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the actual capital structure used by RBOCs. Represcription Order, ¶¶ 57-60 (rejecting the roughly 75% equity/25% debt structure typical of other types of companies).

Verizon of course uses buildings for many purposes, not just to house switches, and a forward-looking network obviously would contain buildings that house things other than switches.

Further, as is true for Verizon's installation and cost of capital factors, its inflation of the building factor escalates every overestimation in the basic switch costs to magnify the effect on switch rates. Id. ¶ 48 n.35.

Verizon's obviously improper allocation yielded a building factor of 18.35%. Id. ¶ 47. Performing the same calculation, and using Verizon's reported historic, embedded costs as listed in ARMIS, but replacing Verizon's allocation of all building costs with a generous allocation of all of its building costs that are associated with wire centers, yields a building factor of 14.61%. Id. ¶ 49.<sup>1/</sup> If Verizon's rates are recalculated, by substituting the 14.61% building factor based on Verizon's historic building costs, correction of this error alone would reduce switching usage and analog port rates by approximately 3.4%. Id. ¶ 50.

vii. Power factor

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<sup>32/</sup> An estimate for building costs associated with switching that is consistent with TELRIC would, of course, be based on a from-the-ground-up approach rather than Verizon's historic, embedded costs. Calculating these costs based on TELRIC principles yields a building factor of 14.09%. Bryant Decl. ¶ 49 n.37 (computed from the results reported for Verizon/Massachusetts by the FCC on its website).



Verizon's calculation of the cost of generators, batteries, and other equipment supplying power to switches is more than double any reasonable estimate of these costs. Verizon claims that power supplies added an additional 10.72% to switch cost. *Id.* ¶ 52. But in a recent filing submitted to the New York PSC, Verizon claimed that power added only an additional 5% to switch cost.<sup>1/</sup> Moreover, in describing this 5% power factor proposal in New York, Verizon explained that it was developed "on a region[al] basis." *Id.* at 53. There is no cost-based reason for a higher factor in Massachusetts. The figure Verizon used to set its rates in Massachusetts is simply unjustifiably inflated. As is true for Verizon's installation, cost of capital and building factors, inflation of the power factor builds on every overestimation in the basic switch costs for a magnifying effect on switch rates. Bryant Decl. ¶ 52 n.41.

If Verizon's rates are recalculated, replacing only the power factor Verizon used in Massachusetts with the one proposed by Verizon itself in New York, analog port rates are reduced by 5.1% and switching usage rates are reduced by over 3.5%. *Id.* ¶ 53.

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<sup>33/</sup> Panel Testimony of Bell Atlantic-New York on Revised Costs and Rates for Unbundled Network Elements and Related Wholesale Services, Proceeding on Motion of the Commission to Examine New York Telephone Company's Rates for Unbundled Network Elements, Case 98-C-1357, at Workpaper, Part H, Section 1, at 5 and Exhibit Part H Section 1, at 1 (NYPSC filed Feb. 7, 2000) (Bryant Decl., Att. 7).

viii. Summary

As indicated above, correcting these seven errors alone would reduce the Verizon Massachusetts rate for analog ports by more than 77% and the rate for switching usage by approximately 65%.<sup>1/</sup> Such gross disparity is inconsistent with cost-based rate-setting under any definition of cost-based. The rates are infected with “clear errors in factual findings on matters so substantial that the end result falls outside the range that the reasonable application of TELRIC principles would produce.” NY Order ¶ 244. Indeed, these rates not only fail to reflect forward-looking costs, they do not even reflect historic embedded costs, or any real measure of cost whatsoever.<sup>1/</sup>

**b. Verizon’s rates allow it to recover four times Verizon’s actual switching investment in Massachusetts and four times the FCC’s estimate of the switching investment needed to serve Verizon’s territory in Massachusetts.**

WorldCom’s conclusion that a cost-based switching model would result in rates a small fraction of the rates derived from Verizon’s model is powerfully corroborated by comparing the total cost of providing switching in Massachusetts generated by Verizon’s model with two other measures of that same cost, and by comparing Verizon’s switching rates to those of other BOCs across the country. These “macro” approaches leave no doubt that Verizon’s estimate of the costs it needs to recover from the rates it imposes on potential competitors is not simply inflated, it is hyper-inflated – by a multiple of approximately four.

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<sup>34/</sup> Bryant Decl. ¶ 18 (tables). Nor is this gross deficiency corrected by applying the Z-Tel usage rates, which would have to be cut in half to produce a rate that resembled a cost-based rate. Id.

<sup>35/</sup> Thus, whatever the ultimate outcome of the currently stayed Eighth Circuit decision on pricing, Verizon’s Massachusetts rates preclude approval of its section 271 application.

First, Verizon's cost study concludes that the total switching investment required to serve its territory in Massachusetts is \$2.641 billion, including Verizon's estimate of switch costs, installation costs, power equipment, and right-to-use fees. Bryant Decl. ¶ 55 (citing Verizon's compliance filing with the DTE). Yet Verizon's own reported booked investment in its switching plant at the time it undertook the cost studies on which its rates are based was only \$603 million. Id. ¶ 56. The comparison makes clear that Verizon's rates are calculated to recover more than four times the then-current value of Verizon's historic, embedded investment in switching in Massachusetts – a claim irreconcilable with any definition of cost-based rates.

Second, a recent estimate from the FCC provides another measure which demonstrates exactly the same disconnect between a legitimate estimation of total costs and the estimate on which Verizon bases its rates. Verizon's estimated total switching investment required to serve its territory in Massachusetts, not including investment related to ISDN lines, is \$2.125 billion. Id. ¶ 57.<sup>1/</sup> The total for the switching investment needed to serve Verizon's territory in Massachusetts, as determined by the FCC's model based on actual LEC switching contracts, is \$491 million.<sup>1/</sup> This measure further corroborates our demonstration that Verizon's rates are calculated to

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<sup>36/</sup> To be fair to Verizon, in order to compare Verizon's estimate with the FCC's, it is necessary to subtract investment related to ISDN lines from its cost study. Id. ¶ 57.

<sup>37/</sup> Id. ¶ 58.

recover more than four times the cost of providing local switching in Verizon's territory in Massachusetts – rather than complying with any cost-based standard. Id. ¶ 54.

Finally, a simple comparison with the rates in other states provides powerful evidence that something is badly wrong with Massachusetts' switching rates. WorldCom has calculated the effective switching and transport costs in approximately half the states in the nation.<sup>1/</sup> What that comparison shows is that most states' rates fall within a range between \$0.002 - \$0.004/minute/line. Leaving Massachusetts aside, only one state, New Jersey, is above four-tenths of a cent/minute, and it is just barely above four-tenths, and, more to the point, the court reviewing that rate concluded it is not cost-based.<sup>1/</sup> Massachusetts is starkly alone at over \$0.008/minute/line.<sup>1/</sup> Nor is it the case that exorbitant per-minute charges are offset by low fixed charges on the switch port. To the contrary Massachusetts has one of the highest flat-rated port charges as well, easily double that of most states. Id. In total, unbundled local switching rates in Massachusetts are three to five times higher than comparable rates elsewhere in the country. There is no explanation provided for this gross discrepancy. Verizon cannot possibly be paying over four times more for its switches in Massachusetts than it is in Pennsylvania.

In sum, whether the Commission looks at the particulars of Verizon's cost study to the extent they have been put on the record, at its embedded book costs, at the Commission's own

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38/ See Proferes Decl. ¶¶ 27-29 & attach. 2. WorldCom chose to review the largest states for its own business purposes, not because it had any sense of what their switching rates were. There is no reason to believe that analysis of the other half of the states would yield a different result. Id. ¶ 27.

39/ AT&T Communications of New Jersey, Inc. v. Bell Atlantic-New Jersey, Inc., No. 97-5762 (KSH), Civ. No. 98-109 (KSH), (D. N.J. June 6, 2000).

40/ Once again, the Z-Tel rates are nearly \$0.006/minute, which still leaves Massachusetts' rates as outliers, the highest in the country.

pricing model, or at comparable switching rates across the country, the result is the same. The rates are infected with “clear errors in factual findings on matters so substantial that the end result falls outside the range that the reasonable application of TELRIC principles would produce.” NY Order ¶ 224.

## **2. Verizon Massachusetts’ Transport and Loop Rates Are Not Cost-Based or Reasonable.**

The gross deficiencies in the unbundled local switching rates should not mask the fact that other unbundled network element rates are also not cost-based and therefore greatly contribute to the competitive problems facing CLECs in Massachusetts. Most of the same errors that wildly inflate Verizon’s analog port and per minute switching rates were made also with respect to its trunk port costs and led to per minute trunk port rates almost five times higher than cost-based rates. As with its switching rates, many of the assumptions and inputs are hidden inside the proprietary SCIS model Verizon relied on but did not submit to the DTE or permit potential competitors to assess. Nonetheless, in calculating its trunk port rates, Verizon made various adjustments to the SCIS outputs and, in doing so, inserted the same kinds of unjustifiable assumptions and inputs in calculating trunk port rates as it inserted in calculating other switch rates. The result is trunk rates imposed on its competitors that are not just somewhat higher than cost-based rates, but almost five times higher.

Correcting Verizon’s failure to apply the appropriate switch discounts alone would reduce the trunk port rates by 55.56%. Bryant Decl. ¶ 71. Correcting Verizon’s indefensibly high installation factor alone would reduce the trunk port rates 33.5%. Id. ¶ 70. Correcting Verizon’s calculation of how many minutes of use would be available for recovery of costs, which was based on the assumption that no one makes any local calls on weekends, would reduce the trunk

port rates 19.23%. Id. ¶ 72. Correcting Verizon's improperly calculated cost of capital, building factor, and power factor would reduce the rates, respectively, 7.64%, 3.42%, and 5.17%. Id. ¶¶ 73-75. Correcting all six errors would reduce Verizon's Massachusetts' trunk port rates 79.76%, i.e., by almost four-fifths. Id. ¶ 69.

In addition, the per-minute charges for unbundled local common transport are every bit as out-of-line as the switching rates, for many of the same reasons. Verizon used the same building factor, cost of capital, and busy hour conversion factor (which assumes no local calling occurs on weekends), to determine local transport rates that it used to determine local switching rates. Id. ¶ 59. Verizon also assumed an even more preposterously low utilization factor in setting the local transport rates than it assumed in setting its local switching rates. In contrast to the FCC's model, in the Universal Service proceeding which assumes that 90% of circuit equipment will be in use and 100% of fiber cable, the model Verizon developed for the purposes of determining the rates to charge its competitors assumes that only 50% of each will be in use, and the rest spare. Id. ¶ 62. Finally, Verizon also used an inflated factor to account for the fact that cables follow roads rather than the most direct path between two points – called the route-to-air multiplier. Id. ¶¶ 66-68.

As with Verizon's "cost studies" for local switching, there is no justification for the assumptions and inputs Verizon chose in setting its local transport rates. Correcting these five errors alone would lower Verizon's Massachusetts per minute peak and off-peak common transport rates by 62.2%. Id. ¶ 60. In other words, Verizon's Massachusetts local transport rates do not merely fail the statutory requirement of being cost-based, they are almost three times higher than cost-based prices. As is true for its switching rates, the gross inflation of Verizon's transport rates is inconsistent with cost-based rate-setting under any definition of cost-based.

Additionally, Massachusetts' loop rates are approximately \$1.50 higher than loop rates across the Verizon region,<sup>41/</sup> a comparison which suggests that the loop rates are suspect. As WorldCom and AT&T repeatedly explained before the DTE, Massachusetts' loop charges are not the "least cost network configuration" as required by TELRIC. 47 C.F.R. § 51.505(b)(2). One plain source of error was Massachusetts' 1996 decision to accept NYNEX's assertion that fiber should always be used in the feeder portion of the loop, even when the feeder length was relatively short, when it was uncontested that at short distances copper was the "least cost" technology for loop feeder. Currently, technological changes since 1996 require that when loop rates are re-considered, the appropriate question should be the proper configuration of a forward-looking loop plant in the year 2000. And there is no fair dispute that changes in digital loop carrier technology, including the use of GR-303 for significantly higher concentration, requires different modeling than that contemplated in 1996, and will result in significantly lower prices. That modeling needs to be done promptly in Massachusetts.

The Commission need not address the question of whether a section 271 application should be denied because the studies supporting the rates are outdated. Here the application should be denied because the switching and transport rates have never been TELRIC-compliant. The DTE needs to reconsider those rates promptly to bring them into compliance with the law. Since there is no fair dispute that loop rates too are not now TELRIC-compliant (whether or not they ever were in the first instance), they too should be reconsidered promptly.

### **3. Application Of Verizon's Network Element Rates Causes A Price Squeeze And Stifles Competition.**

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<sup>41/</sup> Proferes Decl., Att.1. We do not mean to suggest that loop rates in other states are themselves at TELRIC.

There is virtually no UNE-P competition in Massachusetts. Verizon claims there are a grand total of 5,900 residential UNE-P customers in the state<sup>42/</sup> – a smaller number than WorldCom subscribes in Texas New York, and Pennsylvania on a single day. This absence of competition follows ineluctably from Massachusetts’ failure to adopt cost-based pricing. Companies generally do not sell goods or services in a market unless they believe they can at some point do so profitably, and widespread residential service in Massachusetts using Verizon network elements is a losing proposition for every carrier except Verizon.

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<sup>42/</sup> Taylor Decl., Att. A. Table 1.



The pricing in Massachusetts is so bad for the average residential customer that even a CLEC that sells residential service for the same price as Verizon would not make enough money to pay for the cost of the elements it leases to provide the service. Verizon's wholesale price is higher than its retail price. As a result, before a CLEC even considers its own internal costs or any profit, it is already deeply under water in Massachusetts. The table attached at Proferes Decl., Att. 1, at 1, vividly describes the situation faced by a carrier that would provide UNE-P service in Massachusetts. The table describes the monthly revenue a carrier would receive if it provided a basic service with one feature at the same price Verizon charges (including revenue it would receive for providing access for intraLATA and interLATA calls), and then subtracts from that the so-called "Telco" costs, that is, the costs to lease unbundled network elements. What the table shows is that a competing carrier in Massachusetts would lose on average \$10.84 each month for each customer it served, even before it considered its own costs. Those costs, including marketing costs, costs of customers who do not pay their bills, and other operational costs, are in excess of \$10/month for typical carriers, and when added to the Telco costs, they show that UNE service in Massachusetts is a losing proposition of staggering proportion.<sup>43/</sup>

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<sup>43/</sup> Verizon in the past has tried to hide the debilitating effect of its pricing by adding intraLATA toll and long-distance revenues to the revenue side of the equation. But CLECs do not have to lease BOC facilities to provide intraLATA toll and long-distance service, so revenue obtained from those services has no place in a comparison meant to show how unprofitable it is to provide local service using unbundled network elements. To be sure, to provide these services,

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CLECs need to pay access charges to the local carrier for the use of its local facilities. Thus, as indicated above, access charge revenues (or, imputed savings from not having to pay BOC access charges) are therefore added to the potential revenue obtained from providing local service in all of WorldCom's calculations.

Even if a CLEC were to take advantage of the so-called “promotional” rate offered to Z-Tel (which is using UNE-P to serve a high-end niche market), the result is no different. The gross margin – the revenue a CLEC would expect to receive after paying for Telco costs, but before it considers its own internal costs and profit – is still well under water, a negative \$3.73/month/line. See Proferes Decl., Att. 1, at 1. Verizon’s admission that no other carrier has taken advantage of the “promotional” switching usage rates provided in the Z-Tel agreement, Mudge Decl. ¶ 12, confirms that the cost of UNEs even with the reduced Z-Tel rates for switching usage still precludes any broad-based entry into the residential market by leasing unbundled network elements.<sup>44/</sup>

And while Verizon charges a great deal more to its wholesale customers than it does to its retail customers for the same product, it is not because of artificially low retail rates. A state might theoretically set basic retail residential rates so low (and allow the incumbent to recover its costs by charging above-cost rates for other services), that CLECs could not profitably compete with the ILEC even if the UNEs were fairly priced at or near cost. Whatever the appropriate federal regulatory response should be to such a situation, it is not present in Massachusetts.

Massachusetts’ basic retail rates are not particularly low – indeed they are higher than the retail rates in Texas and Pennsylvania, states in which WorldCom can profitably compete for customers

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<sup>44/</sup> There is only one way to enter the market relying on UNEs rates, and that is through the strategy being followed by Z-Tel, which we assume is responsible for most or all of the 5,900 residential UNE-P lines leased in the state. That strategy involves selling a high-cost, feature-rich package of local and long-distances services to customers who want such a high-end package and are willing to pay a premium for it. Thus on its webpage Z-Tel offers a \$59.99/month package that includes many features, and apparently believes that in this manner it can generate revenues sufficient to cover the extraordinarily high telco costs in the state. Time will tell whether Z-Tel is successful with this strategy. What is clear now is that this is a niche product for a small niche market, and could never be the basis of providing a broad-scale alternative to Verizon’s local service. See Proferes Decl. ¶ 25 n.5.

in a significant portion of the state even with wholesale rates that are themselves flawed in many respects. In Massachusetts, the problem is undeniably with the UNE pricing.<sup>1/</sup>

**4.      The Massachusetts DTE Has Repeatedly Refused To Correct Its UNE Rates.**

Nor are CLECs likely to enter the Massachusetts market on the hope that UNE pricing might improve someday. The DTE rubber-stamped Verizon's out-of-line rates, and then, unlike state commissions in New York, Texas and Pennsylvania, repeatedly declined to review them as

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<sup>45/</sup> Nor do the Friday the 13<sup>th</sup> switching rates appear to change the competitive landscape. While no reliable analysis of any kind can be performed on Verizon's new numbers in this short a time, preliminary analysis of the new switching rates suggests that they do not produce margins that would support competition in Massachusetts. Proferes Decl. ¶ 44 & n.9. Like the Z-Tel rates that preceded them, the new rates appear to be little more than a cynical effort to win section 271 entry without offering any prospect of local residential competition to the great majority of the state's consumers. While the New York and Texas rates are just good enough to allow competitive entry, Massachusetts' new rates appear to be bad enough to prevent it. That, of course, makes all the difference in the world.

the evidence mounted that they were grossly defective. Indeed, the DTE has shown scant interest in promoting local residential competition generally.

Here is what the record reveals:

- The DTE set interim rates in the last quarter of 1996.<sup>46/</sup> In the hearings<sup>47/</sup> and briefs<sup>48/</sup> before the interim rates were set, MCI and AT&T identified and challenged virtually every flaw in NYNEX's studies that WorldCom raises today, and proposed switching rates much more consistent with the rates in place elsewhere across the country. Specifically, they challenged:
  - Cost of capital calculations;<sup>49/</sup>
  - Switch vendor discounts;<sup>50/</sup>
  - Building factor;<sup>51/</sup>

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46/ Phase 4 Order (VZ-MA App. H, Tab 162).

47/ Ankum Test. (VZ-MA App. H, Tab 53); Ankum Rebut. Test. (VZ-MA App. H, Tab 105).

48/ MCI's Phase 4 Br. (VZ-Ma App. H, Tab 145).

49/ Ankum Rebut. Test. at 20-26 (VZ-MA App. H, Tab 105); MCI Phase 4 Br. at 22-24 (VZ-Ma App. H, Tab 145).

50/ MCI's Phase 4 Br. at 20-22 (VZ-Ma App. H, Tab 145).

51/ Ankum Rebut. Test. at 7-8 (VZ-MA App. H, Tab 105).

- Utilization factor;<sup>1/</sup> and
- Reliance on Bellcore proprietary “SCIS” model for switching costs.<sup>1/</sup>

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<sup>52/</sup> Ankum Rebut. Test. at 35-38 (VZ-MA App. H, Tab 105); MCI’s Phase 4 Br. at 25 (VZ-Ma App. H, Tab 145).

<sup>53/</sup> Ankum Rebut. Test. at 3, 51 (VZ-MA App. H, Tab 105); MCI’s Phase 4 Br. at 8 (VZ-Ma App. H, Tab 145).

- On December 4, 1996, the DTE adopted without change virtually every element of NYNEX's cost study and the rates it produced. The one exception was its adoption of a cost-based cost of capital. The DTE rejected every other CLEC challenge, for the most part by simply ignoring them.<sup>54/</sup> On the most fundamental problem with the rates – the refusal to take into account switching discounts NYNEX received, the DTE specifically rejected any forward-looking calculation of switching costs, concluding that it would be too “speculative to assume what the manufacturers’ discounts would be if a TELRIC network were being constructed today.”<sup>55/</sup>
- On December 31, 1996, NYNEX, MCI and AT&T sought reconsideration of the DTE Order. MCI argued that the DTE “improperly accepted the very modest discount that NYNEX currently pays for the incremental additions to its current electronic equipment and not for new switches.”<sup>56/</sup> NYNEX argued that the DTE's cost of capital – virtually the only matter of significance on which it had not prevailed – was too low.

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<sup>54/</sup> Phase 4 Order (VZ-MA App. H, Tab 162).

<sup>55/</sup> See id. at 37.

<sup>56/</sup> See MCI's Motion for Reconsideration at 2 (quoting Proprietary Exhibit 1) (VZ-MA App. H, Tab 175).

- On February 5, 1997, the DTE denied MCI's motion for reconsideration without reaching its merits. At the same time it granted NYNEX's motion, raising the cost of capital from 11.38% to 13.5%.<sup>1/</sup>

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57/ VZ-MA App. H, Tab 194.



- On March 27, 1998, AT&T filed a motion with the DTE to reconsider UNE switching rates, because in New York Bell Atlantic finally had been forced to disclose the actual discounts it received on its switches, leading Bell Atlantic's own expert to concede that the New York switching costs were excessive because an insufficient discount had been applied, and that Bell Atlantic had misrepresented the facts when it asserted that it could not take advantage of the larger discounts.<sup>1/</sup> MCI supported AT&T's motion, and both carriers challenged Bell Atlantic's Massachusetts switching rates as excessive.<sup>1/</sup> Initially, DTE said that it would revisit its UNE rates to address the issues raised by MCI and AT&T. But on a subsequent motion by Bell Atlantic, the DTE reversed course and simply converted the interim rates into permanent rates without making a single adjustment or addressing a single one of the CLECs' claims.<sup>1/</sup> At the same time, the DTE informed the parties that it would not consider the switching rates again until December 2001.<sup>1/</sup>
- Throughout 1999, WorldCom and other CLECs in a coalition named "Breakthrough Massachusetts" met repeatedly with DTE and other Massachusetts officials to try to have pricing revisited. DTE representatives initially signaled a willingness to proceed with an expedited proceeding to address the most egregious pricing problems, but subsequently changed their minds.<sup>1/</sup>
- On March 13, 2000, when it had become increasingly clear that the switching rates were having a disastrous effect on local competition, AT&T filed yet another motion challenging the switching rates and asking the DTE to review them. It once again challenged vendor discounts, the excessive installation factor, and the high cost of capital. WorldCom submitted comments in support of the motion, and then on May 19, 2000 submitted additional comments asking the DTE to open an investigation of the rates, focusing on these same issues. WorldCom even submitted testimony that showed fixing these errors could be done quickly in just a

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<sup>58/</sup> VZ-Ma App. F, Tab 12.

<sup>59/</sup> Transcript of 09/24/98 Hearing at 30-32 (VZ-MA App. F, Tab 107) (switch vendor discounts); id. 95-107(same); id. 184-202 (same); id. 130-38 (cost of capital); id. 180-85 (criticism of SCIS); Ankum Rebut. Test. at 2-7 (VZ-MA App. F, Vol. 4, Tab 59); BA-MA's Motion to Adopt Permanent UNE Rates at 4 (VZ-MA App. F, Tab 128) (MCI asking DTE to review switch vendor discount calculation as NY PSC had).

<sup>60/</sup> Order Granting BA-MA's Motion to Adopt Permanent UNE Rates at 11-16 (VZ-MA App. F, Tab 157).

<sup>61/</sup> Id. at 16.

<sup>62/</sup> Proferes Decl. ¶ 31.

few months. On May 30, the Massachusetts Attorney General filed comments in support of AT&T's petition.<sup>1/</sup> The DTE summarily denied the petitions, declaring that its rates were TELRIC compliant, but providing no explanation why it believed this to be the case.<sup>1/</sup>

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<sup>63/</sup> VZ-MA App. B, Tab 425.

<sup>64/</sup> DTE's Letter Denying AT&T's Petition to Reduce UNE Rates (VZ-MA App. B, Tab 481).

On July 18, 2000, in the state section 271 proceeding, WorldCom filed a pricing declaration demonstrating one final time the price squeeze caused by the switching rates, and identifying the critical errors in Verizon's cost studies: the switch discounts, the cost of capital, inflated installation factor, busy hour conversion factor and inadequate utilization rate.<sup>65/</sup> It argued that prompt correction of a few critical inputs would address at least the most draconian consequences of the illegal rate, and that correcting these errors need not long delay Verizon's efforts to enter its long-distance market.<sup>66/</sup> The DTE once again failed to take any action.

As the FCC stressed in its approval of Verizon New York's section 271 application, the local competition commitment of state commissions does matter. There, in response to AT&T claims that the switching rates were defective, the FCC found highly relevant that the New York PSC "engaged in extensive fact-finding in its rate case, and specifically considered AT&T's assertions about switching discounts. As a result, Bell Atlantic's switching prices were greatly reduced, with a final result that is very close to AT&T's estimated switching prices." NY Order ¶ 246. The FCC "stress[ed] that we place great weight on the New York Commission's active review and modification of Bell Atlantic's proposed unbundled network element prices, its commitment to TELRIC-based rates, and its detailed supporting comments concerning its extensive, multi-phased network element rate case." Id. ¶ 238. Here, in stark contrast, there has been no active review, no modification of the Verizon rates (except one upward modification at

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<sup>65/</sup> VZ-MA App. B, Tab 455.

<sup>66/</sup> Id. at 9-10.

Verizon's request), no commitment to TELRIC-based rates, and no proceedings that accomplished anything other than to rubber stamp Verizon demands.

## **II. VERIZON HAS NOT MET ITS BURDEN OF PROVING THAT IT HAS SATISFIED OTHER CHECKLIST OBLIGATIONS.**

Evaluation of market conditions in a market that is closed because of an insurmountable barrier to entry like pricing is a difficult task, and for that reason the Commission in rejecting section 271 applications has declined to offer extensive analysis of issues beyond those found to be dispositive of the application. OK Order ¶ 65. But in the event the Commission here decides to address issues beyond pricing, it needs to do so without losing sight of the effect unlawful pricing has had on the market. Potential problems identified in New York or Texas, where there are proactive and pro-competition state commissions, and where there is real commercial experience through which the true nature of those problems can be probed, may carry a different weight than those same problems when they arise in Massachusetts. As the Commission recently observed, "[w]e look at each application on a case-by-case basis and consider the totality of the circumstances, including the origin and quality of the information before us, to determine whether the nondiscrimination requirements of the Act are met." TX Order ¶ 46.

With these precepts in mind, we turn to additional factors which the Commission may address in the course of resolving this application.

### **A. Verizon Has Not Established That Its OSS Is Operationally Ready.**

As a result of the price squeeze and resulting low levels of UNE-based competition in Massachusetts, Verizon has little commercial experience with its Operations Support Systems ("OSS") for UNEs. That limited commercial experience is insufficient to demonstrate that Verizon's OSS is operationally ready. Verizon's New York experience and KPMG's third-party

test also do not show the readiness of Verizon's OSS; to the contrary, they raise concerns that Verizon's OSS is not ready. "The Commission consistently has found that nondiscriminatory access to OSS, is a prerequisite to the development of meaningful local competition." NY Order ¶ 83. There is not a sufficient basis to conclude that such OSS exists in Massachusetts.

### **1. Verizon's Limited OSS Experience.**

Verizon processes very few orders through its OSS. In July, the most recent month for which Verizon presents data, Verizon processed a total of 5,000 UNE-P orders – and only 4 of them were transmitted via EDI. Kwapniewski Decl. ¶¶ 6, 27. But EDI is the interface of choice for CLECs attempting to provide service at commercial volumes. And UNE-P is the only mode of entry with the potential to provide ubiquitous mass-market service to residential customers in the near term. Thus, Verizon has almost no experience with the one method of entry that could provide meaningful state-wide competition. In contrast, in New York, Verizon processed 70,000 UNE orders in the month prior to its application, most of which were transmitted via EDI. NY Order ¶ 169. Similarly, in Texas, SWBT had processed a relatively high volume of UNE-P orders prior to its application. TX Order ¶ 249.

The Commission has emphasized that a BOC must show the readiness of its OSS to process UNE-P orders, as well as UNE-L orders and resale orders, and it must be able to do so via EDI as well as by a graphical user interface ("GUI."). Verizon's commercial experience provides no such proof. Kwapniewski Decl. ¶¶ 26, 29.

Neither should Verizon be allowed to rest indiscriminately on its successful section 271 application in New York to show the readiness of its OSS. Verizon's OSS in New York is different in important respects from its OSS in Massachusetts. Approximately 20% of the business rules in Verizon's Local Service Ordering Guide ("LSOG") 4 interfaces vary from state

to state, and a much higher percentage of the LSOG 2 business rules are non-uniform. Id. ¶¶ 31-32. Verizon acknowledges that the back-end OSS differs in a number of ways as well, as it must since Massachusetts and New York use different legacy systems. Id. ¶¶ 33-35. It is impossible to know for sure the extent or effect of these differences since Verizon chooses not to address them in its application, and there is only very limited commercial experience with the OSS to know whether the results of transactions are identical. For this reason, during the OSS test in Massachusetts, WorldCom asked the DTE not only to fix pricing but to order a commercial experience period after pricing is fixed to ensure that Verizon OSS works. The DTE declined. Furthermore, the Verizon OSS that exist today in both Massachusetts and New York are substantially different than the OSS in place in New York at the time of its section 271 review. Subsequent to that review, Verizon was forced to scrap key OSS components that failed, and its new LSOG 4 systems did not even exist at the end of 1999. Consequentially, findings about Verizon's New York OSS a year ago are of only limited relevance to the question facing the FCC here.

Verizon therefore must rely largely on KPMG's third-party test to show the readiness of its OSS. Although the Commission has in the past emphasized that commercial experience is the best means of showing OSS is operationally ready, it has also indicated that third-party tests can also provide evidence of readiness. But the Commission has never previously approved a section 271 application where the BOC had commercial experience as minimal as exists in Massachusetts. Certainly, where the BOC's limited commercial experience results from barriers to competition that the BOC itself has erected – here, illegally high UNE prices – the Commission should not be satisfied with a third-party test as a substitute for real commercial experience. At a minimum, it should demand that the third-party test be especially rigorous.

## 2. Defects in the KPMG Test.

The KPMG test does not meet this standard. To the contrary, the KPMG test, unlike KPMG's tests in New York and Pennsylvania, was limited in scope and did not thoroughly investigate issues within its narrow scope. The test nonetheless did reveal important defects in Verizon's OSS that are obscured beneath KPMG's conclusory assertions that Verizon's performance is satisfactory.

KPMG did not conduct a full test of Verizon's LSOG 4 interfaces, the interfaces CLECs will use if significant competition is to develop in Massachusetts. Kwapniewski Decl. ¶¶ 63-65. For example, KPMG did not evaluate line loss notifications – the process by which Verizon notifies CLECs if one of their customers switches to another carrier, and a process that has proven flawed in actual operation in the Verizon region.<sup>67/</sup> And KPMG did not apply the performance measures developed in New York to assess the existence of the missing notifiers which had such a significant competitive consequence there. Furthermore, KPMG did not conduct any volume or stress test of the LSOG 4 systems. Id. ¶ 43 & n.7, ¶ 66.

Moreover, KPMG failed to conduct a true military style test. KPMG uncovered a multitude of problems during the course of testing and opened Observations or Exceptions with

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<sup>67/</sup> Id. ¶ 66. Verizon also continues to erroneously disconnect WorldCom customers for non-payment of Verizon bills when the customers were Verizon customers. Id. ¶¶ 152-153. KPMG did not test this either.

respect to many of them. Yet KPMG often closed these Observations or Exceptions without Verizon having performed a root cause analysis of the problem or implementing any permanent fix. Id. ¶¶ 58-61. Some of the problems KPMG uncovered made it into KPMG's Final Report. But in that Report these problems are masked beneath KPMG's generic conclusion that Verizon's performance was satisfactory – a conclusion at odds with KPMG's specific findings. Id. ¶¶ 50-56. KPMG found, for example, that Verizon returned inaccurate information on pre-order address validation transactions 64% of the time, failed to return 2% of pre-order transactions at all, and returned unhelpful error messages on invalid pre-order transactions. Id. ¶¶ 51-53. In each of these instances, however, as well as many others, KPMG concluded Verizon's performance was satisfactory without determining the cause of the problem it reported, requiring Verizon to implement a fix, or retesting any change that Verizon did implement. Again, WorldCom asked the DTE to mandate analysis to get to the "root cause" of the problem discovered. Again, the DTE declined.

### **3. The Persistent Problem of Missing Notifiers.**

KPMG also found problems that are even more troublesome because they correlate with problems WorldCom has experienced in New York or Pennsylvania, where WorldCom has now launched service. First, KPMG found that on approximately 2.3% of orders, Verizon failed entirely to return provisioning completion notices ("PCNs") and/or billing completion notices ("BCNs"). Kwapniewski Decl. ¶ 41. Verizon returned another 25% of BCNs late under KPMG's measure of timeliness – return within 24 hours of posting of the bill. Id. The existence of any missing and late notifiers is alarming in light of WorldCom's experience with Verizon. As this Commission well knows, when WorldCom first ramped up service in New York, it began experiencing a problem with missing notifiers. After section 271 approval, Verizon failed to



return tens of thousands of notifiers, causing substantial negative impact to customers. The Commission and the New York PSC then intervened, and Verizon was able to significantly reduce the missing notifier problem in New York. Yet when WorldCom launched service in Pennsylvania months later, the problem appeared there. As of September 28, Verizon had not yet returned BCNs on 23.1% of WorldCom's August orders in Pennsylvania for which BCNs were past due. Id. ¶ 45. As of October 6, Verizon had not yet returned BCNs on 14.7% of the orders WorldCom placed between September 3 and September 15. Id.

In light of WorldCom's current problems in Pennsylvania with Verizon's latest OSS, there is no basis for assuming that the New York fix of earlier OSS will prevent a missing notifier problem from arising in Massachusetts if order volumes increase there. Id. ¶ 46. Indeed, such a problem may already exist. KPMG's limited data suggest the existence of such a problem, and KPMG's data likely significantly understate the scope of that problem. Verizon has refused to import the relevant metrics to Massachusetts, and Verizon's failure to include these measures makes it impossible to determine whether it is failing to return notifiers during commercial operation. Id. ¶ 42 & n.7. It also vastly limits the ability of CLECs and regulators to track any future problems and minimize the scope of those problems. Given Verizon's past problems with missing notifiers, Verizon's failure to demonstrate that such a problem will not exist in Massachusetts is reason enough to reject Verizon's section 271 application.

This is especially so in light of Verizon's continued poor performance in assisting CLECs to resolve missing notifier problems. This Commission spent significant time establishing a process by which Verizon would reflow missing notifiers. Yet in Pennsylvania, Verizon is taking far too long to reflow notifiers WorldCom identifies as missing, or is reflowing the wrong notifiers altogether. Kwapniewski Decl. ¶ 122. This mirrors WorldCom's experience in New York with

respect to the limited volume of missing notifiers that continue to exist. Despite meeting with Verizon every week, WorldCom still has not received notifiers missing since June. Id. The same help desk that is performing poorly with respect to Pennsylvania and New York orders also is used in Massachusetts. Indeed, during the KPMG Massachusetts test, KPMG submitted trouble tickets on notifiers it was missing, and never received those notifiers. Id. ¶ 124.

#### **4. Inadequate Technical Assistance.**

The inadequate performance of Verizon's help desk with respect to missing notifiers points to a more general problem – Verizon's overall failure to provide adequate assistance to CLECs. Verizon's help desk is generally inadequate, its documentation is poor when initially released, and Verizon is failing to follow its change management process for its upcoming release of ExpressTrak, a major new OSS system.

**Help Desk.** Verizon's help desk not only fails effectively to resolve trouble tickets submitted on missing notifiers, it fails effectively to resolve other trouble tickets as well. Kwapniewski Decl. ¶¶ 118-122. WorldCom has long had this problem in New York, and, as a result of the experience of WorldCom and other CLECs, on July 24 Verizon created a new help desk. Yet the new help desk is performing no better. In Pennsylvania, the help desk is taking weeks to resolve trouble tickets despite repeated invocation of the escalation process. Id. ¶¶ 120-121. There is no reason to expect the performance to be any better in Massachusetts. KPMG's data from testing show that Verizon took long periods of time to resolve even critical trouble tickets. Id. ¶ 118. Verizon's limited commercial data do not show the contrary. Although WorldCom has consistently advocated such a measure, Verizon does not report on the timeliness of its resolution of trouble tickets. Id. ¶ 128.

**Inadequate Documentation.** Verizon fails adequately to assist CLECs in a second way as well: Verizon consistently releases documentation that is manifestly deficient. Verizon's initial documentation for its LSOG 2 interfaces was of extremely poor quality. Kwapniewski Decl. ¶ 74. Then, when Verizon released documentation for its initial LSOG 4 release, KPMG found that "a substantial portion of the documentation in the LSOG 4 Pre-order and Order Business Rules and the EDI Pre-Order and Order Guides is incomplete, incorrect or unclear." VZ-MA App. I, Tab 2, Exception 4 (emphasis added). Id. ¶ 75. In the next release, Verizon's June 2000 LSOG 4 release, KPMG (through Hewlett Packard) again found a high number of documentation errors. Id. ¶ 79. Based on these errors, KPMG concluded that "CLECs cannot properly format EDI transactions and communicate with Bell Atlantic." Exception 12. KPMG also observed problems with the test decks Verizon used for its February and June releases. Id. ¶ 85.

KPMG's findings parallel WorldCom's own experience in Pennsylvania and New York. WorldCom tested Verizon's June release for both Pennsylvania and New York and found numerous documentation errors. As a result of these documentation errors, along with coding problems on Verizon's side of the interface, more than 75% of WorldCom's LSOG 4 pre-order test scenarios failed at the beginning of testing, and more than 40% failed even at the time the release was scheduled to go into production. Kwapniewski Decl. ¶ 81.

According to KPMG, Verizon eventually corrected the documentation problems that KPMG uncovered. But the poor quality of Verizon's documentation when it is first released imposes significant costs on CLECs. Those documentation problems, coupled with Verizon coding errors, lead to an unstable test environment in which both CLECs and Verizon are forced to make repeated changes to the coding of their interfaces during testing. Id. ¶¶ 86-87. This substantially increases the cost of testing, as does the time CLECs spend ferreting out

documentation problems and discussing them with Verizon. Id. ¶¶ 87-91. Indeed, WorldCom estimates that half of the time it spent testing Verizon's June release resulted from Verizon's documentation and coding problems. Id. ¶ 89. The costs are increased further by the lengthy period Verizon often takes to correct documentation and the mistakes it frequently makes in the "corrected" documentation. Id. ¶¶ 94-100. Moreover, the existence of extensive documentation errors may delay CLECs' ability to implement an interface altogether, and, if the errors are not caught, can cause significant production problems once the interface is operational. Id. ¶ 91.

**Inadequate change management.** Verizon's difficulties in implementing significant interfaces and systems changes are likely to cause even greater problems in coming months. Verizon is currently rolling out a new back-end system called ExpressTrak that will affect major components of its OSS. Yet Verizon has shared only limited information on this system with CLECs. Even though Verizon has already begun implementing the system for wholesale customers in some states, it has not followed the change management process for implementing ExpressTrak, which requires early release of documentation and a CLEC comment period. Verizon also has not provided – or even promised to provide – a regression test deck to the CLEC community or a CLEC test period to demonstrate that the code is functioning properly. Verizon's change management process does little good if Verizon does not include major releases such as ExpressTrak in that process. Id. ¶¶ 102-115.

The Commission has emphasized that BOCs must provide adequate technical assistance to CLECs. TX Order ¶¶ 96-97. That includes an effective help desk, complete and accurate documentation, a stable test environment based on thorough internal testing, and an effective change management process. Id. ¶¶ 106-107, 113, 132; NY Order ¶¶ 102, 109, 126. Verizon provides none of these. Although the Commission found Verizon's technical assistance to be

adequate at the time of the New York section 271 proceedings, subsequent experience has revealed important deficiencies. Verizon must resolve these deficiencies prior to approval of further section 271 applications.

## **5. Other OSS Problems – Flow-Through and Outages.**

**Flow-Through.** Verizon relies on far too much manual intervention in processing orders. Its flow-through rate is below 50% in its reported performance measures – well below what existed in New York at the time of Verizon’s section 271 application there. Kwapniewski Decl. ¶ 156. Similarly, during testing KPMG found a flow-through rate of commercial orders of only 35%.

Verizon asserts that the same orders that flow through in New York will also flow through in Massachusetts. But there is no evidence that this is so. While KPMG relies on test data to conclude that orders which are supposed to flow through actually do, the commercial data evaluated by KPMG show that fewer than 60% of the types of orders that are supposed to flow through actually do. *Id.* ¶ 158. Although Verizon attempts to attribute this to CLEC problems, Verizon refused to provide KPMG a break-down of the orders that fell out for manual processing. Moreover, unlike in New York, Verizon does not report data in Massachusetts on flow-through achieved – the percentage of orders that are supposed to flow through which actually do flow through. *See infra* pp. 51-52; Kinard Decl. ¶ 51.

In any event, even if Verizon’s flow-through capabilities were identical in Massachusetts and New York, Verizon’s flow-through rate would still be too low. Despite promising during New York section 271 proceedings to improve flow-through dramatically in subsequent months, Verizon has not done so in New York. And while, based on these assurances, the Commission found Verizon’s flow-through in New York to be adequate, it should not do the same in

Massachusetts. Unlike in New York, Verizon simply does not have enough commercial experience in Massachusetts to demonstrate that it is capable of handling commercial volumes of orders with today's high level of manual intervention. Kwapniewski Decl. ¶¶ 155-57.

**Interface outages.** Yet another problem that has become manifest with Verizon's OSS since the time of Verizon's New York application is the limited availability of Verizon's pre-ordering and maintenance and repair systems. As a result of both scheduled and unscheduled outages in Verizon's GUI and back-order OSS, WorldCom has been unable to access Verizon's OSS more than 10% of the time during prime time hours from November 1999 through September 2000. Kwapniewski Decl. ¶¶ 136-138. In its NY Order, the Commission found that New York's standard of 99.5% availability during prime time hours was "a reasonable and appropriate measure of whether Verizon's interfaces are sufficiently available to afford an efficient competitor a meaningful opportunity to compete." NY Order ¶ 155. Since then, Verizon has come nowhere close to providing access to its OSS 99.5% of the time. Although the New York measurement technically includes only availability of the interface, not the back-end systems, unavailability of either has the same impact on CLECs. Kwapniewski Decl. ¶¶ 131-132. CLECs cannot sell or transmit orders or requests for repairs when the OSS is unavailable. Verizon has not disputed that its OSS is unavailable more than 10% of the time when back-end availability is taken into account.

Finally, Verizon's OSS has a number of other important defects. In both New York and Pennsylvania, Verizon's "SMARTS Clock" function for providing due dates consistently offers due dates to CLECs for installation of new service that are far beyond what is reasonably acceptable. Kwapniewski Decl. ¶¶ 142-44. Verizon's telephone number reservation function often returns the message that numbers – which are necessary for installation of new service – are

unavailable. Id. ¶ 145. Verizon returns UNE loop bills only in paper format, often fails to transmit bills to WorldCom and then assesses late payment charges for failure to pay on time, loses track of payments WorldCom has already made, fails to transmit all bills during the same time period each month, and imposes inaccurate charges on bills. Id. ¶¶ 165-74.

In sum, Verizon has not yet demonstrated that its OSS is operationally ready. Verizon has virtually no commercial experience in Massachusetts with OSS for UNE-P. The KPMG test was too limited in scope and insufficiently rigorous to substitute for that lack of commercial experience. If anything, that test points out remaining problems in Verizon's OSS – including in particular the continuing difficulty Verizon has with missing notifiers – that should have been fixed and retested before KPMG determined that the OSS was satisfactory.

**B. Verizon's Performance Measurements and Performance Remedy Plan Will Not Prevent Backsliding.**

Verizon's performance reporting and remedy plan also are inadequate to carry its burden of proving checklist compliance, and provide another reason that this application should be denied.<sup>1/</sup>

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<sup>68/</sup> Inadequate performance measurements implicate checklist compliance because they demonstrate a BOC's failure to prove that is providing the relevant network elements. They also implicate concerns relevant to the public interest test, since inadequate measurements and inadequate penalties make it more difficult to assure that a BOC's performance will not deteriorate after long-distance entry. To avoid duplicative briefing, WorldCom addresses all performance measure issues here rather than to cover some here and some in the following section addressing the public interest test.

**1. The Commission Cannot Rely on Verizon's Performance Reports Because the Data Have Not Been Verified, Individual CLEC Data Are Not Reported, and Verizon Does Not Report Many Critical Metrics.**

Verizon's application for section 271 authorization relies on its performance as reported in accordance with measures developed in the "Carrier to Carrier" Working Group sessions overseen by the New York PSC and subsequently adopted by Massachusetts regulators. Although these measures are designed to show whether Verizon is providing service on reasonable and nondiscriminatory terms that will enable local competition, Verizon's reports often do not accomplish this purpose.

First, although this Commission has held that "the reliability of reported data is critical," TX Order ¶ 428, Verizon's raw data has not been independently verified. See KPMG Final Report, at 646 (VZ-MA App. I, Tab 1) (discussing the so-called "Data Integrity" testing, noting that "[t]he accuracy of the raw data itself was not verified, except during the transaction test, where it was only indirectly verified"). This stands in sharp contrast to the testing in New York, where this Commission expressed confidence in the data because New York PSC staff had performed extensive data reconciliation and worked through numerous problems. NY Order ¶ 422; see also TX Order ¶ 429 (expressing confidence in data because of thorough validation by third-party tester). In Massachusetts, by contrast, the DTE expressly admitted that it lacked the resources to perform data replication, despite indications that KPMG had discovered problems in even its limited replication efforts. See Order Adopting Performance Assurance Plan, DTE 99-271, at 33 (DTE filed Sept. 5, 2000) (VZ-MA App. B, Tab 559); see also NY Order ¶ 422. This Commission has stressed the continuing importance of scrupulous data verification, stating that



“because the Performance Remedy Plan rests entirely on [the BOC’s] performance as captured by the measurements, the credibility of the performance data should be above suspicion.” TX Order

¶ 429. Because independent verification of Verizon’s raw data is entirely lacking, the Commission should not credit any of the reported data.

The lack of independent data verification is all the more serious because, in contrast to New York prior to section 271 approval, Verizon-Massachusetts thus far has provided only CLEC aggregate results for the carrier to carrier performance measures in Massachusetts. Consequently, there is no mechanism for individual CLECs to verify the accuracy of Verizon’s reports on any measures. The ability to verify a BOC’s data often reveals discrepancies. In Pennsylvania, for example, where state regulators have required individual CLEC results to be provided, WorldCom found that Verizon had not reported the more than 500 UNE-P orders that WorldCom had placed in August 2000, the month that WorldCom entered the local residential market in that state. See Kinard Decl. ¶ 6. No such verification has been possible here.

There are other significant problems with Verizon’s performance reporting. For a number of significant measures, Verizon has simply not provided any results at all for Massachusetts. Other key areas, including some addressed in New York, are not addressed by any metrics in Massachusetts. And even where performance has been reported, some existing metrics do not capture the most relevant information regarding consumer-affecting service. These shortcomings not only call into doubt Verizon’s current compliance with the requirements of section 271, they compromise the equally important guarantee that Verizon remain in compliance after long-distance entry. Cf. NY Order ¶ 16; MI Order ¶ 22.

For example, among the measures included in the Performance Assurance Plan (“PAP”) adopted in New York, and mirrored in Massachusetts, is OR-5-03, reporting Achieved Flow

Through.<sup>1/</sup> But although the Achieved Flow Through metric is in place, and although Verizon's New York affiliate has been reporting its performance – and paying substantial penalties – in accordance with this measure since last fall, Verizon Massachusetts has yet to report any performance results under this measure. Kinard Decl. ¶ 8. Verizon attributes its failure to report to the fact that there is an ongoing review in New York to address certain aspects of this measure which CLECs would like to see improved. Guerard/Canny Decl. ¶ 55. This is simply an evasion. Verizon New York is providing this information today. All aspects of the New York PAP are subject to review and revision, and indeed, the Carrier to Carrier proceedings create a climate for ongoing revision of all metrics to keep up with changing market conditions. Allowing Verizon to wait for the “definitive” version of a metric will allow it to evade reporting any performance at all. Verizon's foot dragging leaves CLECs and this Commission without necessary information to judge whether Verizon is providing nondiscriminatory access to UNEs.<sup>1/</sup> Moreover, by failing to

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69/ This metric is one of two comprising the Massachusetts PAP Special Provision on UNE flow-through, to which \$5.4 million of the total annual remedies available under the PAP are tied. See Guerard/Canny Decl., Att. C, Ex. 8 at 2.

70/ “Missing evidence” should be construed against Verizon as the party who controls it and withholds it, and as the party with the burden of proof in this proceeding.

report its results, Verizon will stymie the effectiveness of relevant part of the PAP, because Verizon cannot be held to pay penalties if it does not report its sub-standard performance.<sup>1/</sup>

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<sup>71/</sup> As described below, infra p. 58, Verizon also has not yet reported results for two DSL metrics ordered by the NYPSC eight months ago and adopted by Massachusetts. See Kinard Decl. ¶ 9.

Unfortunately, neither the New York PAP nor the Massachusetts PAP contains a self-executing mechanism to require Verizon to pay penalties if it does not begin reporting on an ordered metric within a reasonable period of time. CLECs in this circumstance therefore will have to return to the state commissions to seek relief. This is a particular concern in Massachusetts, where the DTE has demonstrated an intention to rely in large part on proceedings occurring in New York to update the PAP and where there is no reason to believe that it will devote the resources necessary to aggressively police Verizon's anticompetitive behavior.<sup>1/</sup> Until this problem is fixed, the effectiveness of the Massachusetts PAP is compromised.

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<sup>72/</sup> WorldCom has recently asked the New York PSC to amend its PAP to require Verizon to pay penalties if it does not begin reporting results within four months of being ordered to implement a new metric. See WorldCom, Inc.'s Comments on Verizon New York's Performance Assurance Plan and Change Control Assurance Plan, Case 99-C-0949 (NYPSC filed Sept. 15, 2000) (Kinard Decl. Att. 3); Kinard Decl. ¶ 10.

The experience with Verizon in New York during this first year after section 271 approval proves the need for quick and effective implementation of new performance metrics and remedies. As this Commission knows well, severe problems with missing EDI notifiers required this Commission to intervene and seek solutions that resulted in an Order and Consent Decree requiring rapid remediation. This crisis also prompted the New York PSC to add a new Special Provision for EDI Measures to its PAP, supported by an additional \$24 million in possible bill credits for violations.<sup>1/</sup> The New York PAP was amended to replace one metric and to add three new measures relating to notifiers. This permitted for the first time accurate tracking of Verizon's performance in this critical area, and increased the overall amount available under the New York PAP to about 44% of Verizon-NY's ARMIS-reported profits. And although Verizon-NY is no longer subject to this Commission's Consent Decree on this problem, the PAP provisions remain in force and Verizon continues to report its performance to state regulators in New York.

Despite the clear, severe impact of the missing notices problem in New York, the Massachusetts PAP fails to incorporate the three new metrics or a Special Provision for EDI

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<sup>73/</sup> See Order Directing Market Adjustments and Amending Performance Assurance Plan, Cases 00-C-0008, 00-C-0009, and 99-C-0949 (NYPSC filed March 23, 2000) (Kinard Decl., Att. 4); Kinard Decl. ¶ 11. By contrast, the Massachusetts PAP fails to expressly reserve to that state's regulators even the power to reallocate money among provisions of the PAP to address unanticipated performance problems.

Measures. These omissions are particularly problematic because as indicated above, supra pp. 42-44, even without the benefit of these metrics, there is reason to believe that the missing notifier problem has re-emerged in Massachusetts.<sup>1/</sup> Unfortunately, there is no mechanism in place in Massachusetts to monitor this known problem area, now or after section 271 approval.

Flaws in other metrics further undermine the conclusions about Verizon's performance that Verizon seeks to draw from them. See Kinard Dec. ¶¶ 16-29. Of particular concern to WorldCom is the decision to use a biased retail analog to measure interconnection performance, a flaw that is aggravated by the decision to aggregate inbound and outbound trunks on some measures. The result is that these measures fail to capture the real story of competition-affecting service problems. See id. ¶¶ 17-25. In addition, Verizon several times excuses poor reported performance by blaming it on distortion caused by differences between CLEC business mix and its own. The solution to this complaint, however, is further disaggregation of performance results, which would require Verizon to demonstrate parity by comparison of service on like orders. Verizon should not allowed it to obfuscate its results and use a failure in the metric as a substitute for proof of good performance. See id. ¶¶ 28-29. These residual problems with performance

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<sup>74/</sup> Specifically, as described above, KPMG testing in Massachusetts indicates similar problems in receiving Billing Completion Notices, which are critical to allow CLECs to begin charging their customers for service without fear of double billing. See also KPMG Final Report, at 53-54 (VZ-MA App. I, Tab 1); Kinard Dec. ¶ 12.

metrics must be resolved before Verizon can be said to have proven adequate performance, because they form the basis for post-entry protection of CLECs under the PAP.

## 2. **The Remedies in the PAP Are Inadequate.**

While Massachusetts purports to set its remedial caps at levels proportionate to New York,<sup>1/</sup> it has failed to do so. First, in Massachusetts, the Department has expressly held that remedies under the PAP are an alternative to remedies available under the Consolidated Arbitrations – the proceeding that set the contractual remedies available for most CLECs for poor performance suffered individually. By contrast, in New York, PAP remedies supplement liquidated damages available to individual CLECs under interconnection agreements. This Commission expressly held in approving Bell Atlantic’s New York section 271 application that the New York PAP’s monetary caps were adequate because of the combined deterrent effect of other available legal strictures, including liquidated damages in interconnection agreements.<sup>1/</sup> In Massachusetts, however, this additional deterrent is missing. Moreover, in setting the overall cap

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<sup>75/</sup> As in New York, the use of arbitrary remedy caps undermines the overall effectiveness of the Massachusetts PAP. See Kinard Decl. ¶ 35.

<sup>76/</sup> NY Order ¶ 430 (explaining that it may permit section 271 entry even though a state PAP alone provides less than full protection against anticompetitive behavior because of additional incentives for ILEC compliance including “payment of liquidated damages through many of its individual interconnection agreements.”); see also TX Order ¶ 424. Despite this fact, as seen, the New York PSC still found it necessary to increase the overall amount of money available under the PAP when faced with the severe missing notice issue.

at 36% of ARMIS-reported local profits, Massachusetts did not take into account the \$24 million in additional penalties added in New York with the new EDI Measures, which raises the PAP remedies there to about 44% of ARMIS local profits. As a result, the Massachusetts PAP carries less deterrent effect than the New York plan. See Kinard Decl. ¶¶ 31-32.

The Massachusetts PAP also allows Verizon to delay remedy payments through a fundamentally flawed “waiver” process. Unlike New York’s waiver procedure, the waiver procedures contains no required time lines.<sup>1/</sup> Nor has Verizon ameliorated this problem by promising to make PAP payments on a disputed issue during the pendency of a waiver adjudication. Moreover, while the Massachusetts DTE properly ordered Verizon to strike or better define the “CLEC action” waiver category in its PAP compliance filing, see Order Adopting Verizon’s Performance Assurance Plan at 31 (VZ-MA App. B, Tab 559), echoing this Commission’s observation that this category should be more clearly defined, see NY Order ¶ 441 n.1355, Verizon’s clarification is inadequate, as it provides it even greater opportunities to derail the self-executing nature of the PAP.<sup>1/</sup>

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<sup>77/</sup> See Guerard/Canny Decl. Att. C, at 27 (setting deadline only for filing of waiver request); cf. NY Order ¶ 441.

<sup>78/</sup> For example, among the examples of CLEC behavior that might merit a waiver, in



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Verizon's view, are "poor order quality, such as missing codes, incorrect codes, or misspelled directory listings." Guerard & Canny Decl. Att. C, at 26. However, these factors would not affect Verizon's liability, and so should not be grounds for a waiver. See Kinard Decl. ¶ 34. Another of Verizon's "examples" of CLEC-caused delay is "inadequate testing" – a standard obviously subject to interpretation and not otherwise defined. And indeed, that all of these are just "examples" indicates that Verizon still reserves the ability unilaterally to institute waiver proceedings and thus put off payment of penalties essentially at will, eviscerating the self-effectuating nature of the PAP.

Finally, in New York the PAP gives the NPSC the ability to shift the penalty dollars in the PAP as it sees fit. Like other competition-enhancing procedures, a PAP works best when it is supported by an active, pro-competition state commission, and the New York PAP was quite properly evaluated in that context. Here, in contrast, the Massachusetts PAP does not allow the DTE to move penalty dollars within the PAP as needed, and in any event the DTE has neither shown the will nor devoted the resources to ensuring the continued development of local competition shown by the NY PSC.

**3. The PAP Is Inadequate to Prevent Backsliding for Advanced Services.**

The Massachusetts PAP is particularly inadequate to prevent backsliding with respect to the provision of advanced services. As we discuss below, Verizon's ability to provide line sharing and line splitting is unproven, and its reported performance on DSL provisioning in general is well below the required levels. For this reason, it is particularly important that the PAP provide adequate incentives to prevent backsliding with respect to these services after Verizon's section 271 approval.

Unfortunately, it does not. The current PAP contains no metrics whatsoever with respect to line sharing, a deficiency that Verizon itself has recognized as in need of remedy in New York.<sup>1/</sup>

While neither the New York nor Texas plans included such measures when those carriers received section 271 approval, neither of those carriers was obligated to provide line sharing at the time of its application, and thus backsliding on that service was not an issue. Verizon, however, is currently required to provide line sharing. See TX Order ¶ 321. Having adequate

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<sup>79/</sup> See Letter Comments of Verizon-NY in Case 99-C-0949, regarding Annual Review of the New York Performance Assurance Plan at 1 (NYPSC filed Sept. 15, 2000) (Kinard Decl., Att. 5); Kinard Decl. ¶ 13.

PAP protections for CLECs seeking this service is critical, since Verizon has little practical experience provisioning line sharing, and will not even implement OSS enhancements to support flow-through orders for this service in Massachusetts until at least April 2001.<sup>1/</sup> KPMG also did no testing of this service – all factors that should preclude granting Verizon’s section 271 application and require that sufficient remedy provisions be available before Verizon’s application is granted.

Likewise, although the New York PAP did not expressly address DSL at the time of Verizon-NY’s section 271 approval, this Commission required an independent showing of nondiscriminatory DSL provisioning in all subsequent section 271 applications. See NY Order ¶¶ 330-335; TX Order ¶ 282. Independent anti-backsliding safeguards for DSL are also vital. See TX Order ¶ 422 n.1224 (noting revision of Texas performance remedy plan to include DSL measures between time of first Texas filing and decision on second Texas filing.) In this area, while the Massachusetts PAP includes some DSL measures, Verizon has not in fact been

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80/ See Order, Massachusetts D.T.E. 98-57-Phase III, Investigation by the Department on its own motion as to the propriety of the rates and charges set forth in M.D.T.E. No. 17, filed with the Department by Verizon New England, Inc. d/b/a Verizon Massachusetts on May 5 and June 14, 2000, to become effective October 2, 2000, at 20-21 (DTE filed Sept. 28, 2000) (attached hereto at Tab F) (“Massachusetts DSL Order”).

reporting its performance in either New York or Massachusetts with regard to two of the four critical measures on DSL that are included in the present PAPs in both states. Kinard Decl. ¶ 9.<sup>1/</sup>

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<sup>81/</sup> Verizon New York apparently concedes that some additional DSL measures must be incorporated into a proper PAP. See Letter Comments of Verizon-NY in Case 99-C-0949, regarding Annual Review of the New York Performance Assurance Plan at 1 (NYPSC filed Sept. 15, 2000) (stating as part of annual PAP review that additional DSL measures should be added to New York PAP) (Kinard Decl. Att. 5); Kinard Decl. ¶ 15.

Recognition of DSL as a separate mode of entry into the residential broadband market is necessary to ensure that Verizon will facilitate the development of advanced services after its section 271 approval, a key goal of the 1996 Act. The demand for DSL services continues to grow exponentially as access to the Internet and use of e-mail become more prevalent and critical to how people obtain information and communicate. As a result, CLECs' meaningful, sustained entry into the market depends on Verizon meeting its commitments to support CLEC DSL offerings. The Mode of Entry components are designed to measure Verizon's performance with regard to the different ways a competitor can enter the local exchange market. Treating DSL as its own Mode of Entry makes sense because DSL-based services differ significantly from analog voice service, the current focus of the PAP. In addition, a separate DSL Mode of Entry provides another means of ensuring that the performance metrics and level of DSL performance required by this Commission in its prior section 271 approvals are implemented and enforced, and will enable state regulators to ensure that Verizon supports the full suite of DSL-based services that are and will become available.<sup>1/</sup>

It is equally important that any dollars placed at risk for a DSL mode of entry category be in addition to the existing dollars at risk in the PAP. Otherwise, if the total amount at risk under the Plan remain constant, increasing the amount at risk for DSL performance would necessarily decrease the amount at risk for traditional analog voice service. This would diminish Verizon's incentive to provide voice services or voice related UNEs at appropriate levels. In fact, the result of reallocating dollars at risk instead of adding new dollars for the new DSL metrics could easily

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<sup>82/</sup> Rapid roll-out of DSL-based services by BOCs including Verizon and SBC make it critical that there be a powerful economic incentive for BOCs to facilitate competition for advanced services.

be that in both instances – for voice and data services – the amount of bill credits at risk will be too low to motivate Verizon to ensure that its delivery of services and unbundled network elements will promote competition.

**C. DSL Issues Have Not Been Sufficiently Resolved To Permit Competition.**

Verizon argues repeatedly that its application should be approved because it is analogous to the application submitted by Bell Atlantic in New York last year. But while the FCC declined to require BA-NY to provide a separate showing of its DSL-related service because the issue had only recently been raised in New York and the technology was only then emerging, the Commission has mandated an independent showing of nondiscriminatory DSL provisioning in all subsequent section 271 applications. See NY Order ¶¶ 330-335; TX Order ¶ 282. Verizon fails to make that showing here.

This Commission looks primarily for proof of nondiscriminatory DSL performance through “comprehensive and accurate reports of performance measures,” specifically addressing DSL and approved by state commissions. TX Order ¶ 282; NY Order ¶¶ 333-335. As explained above, Verizon has not supplied such proof. Verizon has yet to report any results for two of four DSL measures designated as critical under the Massachusetts PAP. Kinard Decl. ¶ 9. And those measures of loop provisioning and maintenance for DSL on which Verizon has reported results demonstrate an almost uniform absence of parity.<sup>1/</sup> Verizon’s excuses cannot substitute for a

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<sup>83/</sup> Verizon-MA’s DSL track record is quite short, as it began disaggregating DSL results for loop provisioning and maintenance only in the second quarter of this year, after KPMG had evaluated the performance metrics. See KPMG Final Report, at 674 (VZ-MA App. I, Tab 1) (noting metrics not disaggregated for two-wire xDSL). KPMG did not replicate the metrics for 2 wire DSL services. See Transcript of 8/29/2000 Hearing at 3385-3388 (VZ-MA App. B, Tab 547) .

KPMG’s testing of DSL functionality was also limited. In particular KPMG’s testing of

genuine track record of nondiscriminatory service. On this record, Verizon fails to prove that it offers nondiscriminatory access to loops for DSL.<sup>1/</sup>

In addition to its required showing regarding provisioning of stand-alone DSL-capable loops, Verizon is the first section 271 applicant that is also obligated to provide line sharing, making “the high frequency portion of the loop separately available . . . [in] those instances in which the incumbent LEC is providing, and continues to provide, voice service on the particular loop to which the requesting carrier seeks access.” TX Order ¶ 324. To do so, it must show that it has “implemented the loop facility and OSS modification necessary to accommodate requests for access to the line sharing unbundled network element as required by our December 9, 1999 Line Sharing Order.” TX Order ¶ 321. But Verizon has not made the necessary changes to its OSS to support flow through of orders for line sharing, without which CLEC orders can be mishandled or delayed due to manual processing, and has indicated that it cannot do so until at least April 2001.<sup>1/</sup> Indeed, as the Massachusetts DSL Order makes clear, implementation of line

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pre-ordering and ordering functions, especially for residential service, was primarily conducted using LSOG 2 and not LSOG 4, the latest OSS interface. Compare, e.g., KPMG Final Report at 18, 73 (VZ-MA App. 1, Tab 1) (testing loop qualification under LSOG 2) with id. at 22, 78 (same under LSOG 4, confined to business); id. at 21, 76 (volume testing under LSOG 2 confined to business; no volume testing under LSOG 4). KPMG’s testing is plainly inadequate under the Common Carrier Bureau’s standard that an adequate “third-party test would test significant volumes of xDSL orders.” Sept. 27, 1999 letter from Lawrence E. Strickling, Chief, Common Carrier Bureau, to Nancy E. Lubamersky, U S West (attached hereto at Tab G).

<sup>84/</sup> As an alternative to proof of actual nondiscriminatory performance as measured by state-approved standards, this Commission has indicated that the establishment of a “fully operational” separate affiliate for advanced services “may provide significant evidence” of nondiscrimination. TX Order ¶ 282; NY Order ¶ 331. But Verizon’s advanced services affiliate is not yet operational in Massachusetts, and will not be fully so for some time to come. See Lacouture/Ruesterholz Decl. ¶ 111.

<sup>85/</sup> See Massachusetts DSL Order at 20-21.

sharing OSS is not required by the state until April 2001, or one month after Verizon implements the changes in Pennsylvania, whichever is later, meaning that Massachusetts CLECs still lack a firm date for this critical deployment.

Moreover, Verizon has provided virtually no evidence of its ability to provide line sharing with an unaffiliated data CLEC, pointing only to a limited trial offering and the results of Verizon-NY's provisioning to Verizon's own data affiliate in that state. See Lacouture/Ruesterholz Decl. ¶¶ 111-114, 116. Indeed, at the time of its filing with this Commission, Verizon's tariff regarding line sharing had not been ruled on by the Massachusetts DTE and was not in effect. And not only does Verizon lack any significant commercial experience with CLEC line sharing, KPMG did no testing of its line sharing capability, so there is little assurance that Verizon can in fact provide this service today. Given the critical and growing role of advanced services offering in the overall local service market, these failures should preclude Verizon's section 271 approval at this time.

Verizon also fails to prove that it can or will accommodate line splitting that would allow a data CLEC and a voice CLEC to use the same loop to provide data and voice services, respectively. The Massachusetts DTE terms this configuration "line sharing between two CLECs." Massachusetts DSL Order at 35. A customer who receives voice service from Verizon



and data from a data CLEC, and who wishes to change her voice carrier to WorldCom without disturbing her data service is apparently just plain out of luck.<sup>1/</sup>

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<sup>86/</sup> See Transcript of 8/1/2000 Hearing at 224-25 (VZ-MA App. E, Tab 405). Verizon admitted that no physical work is required as a technical matter to transfer the voice portion of a line sharing arrangement to a CLEC but nonetheless has refused to commit to permit this conversion.

To make matters worse, subsequent to Verizon's application being filed, at Verizon's request the DTE has ruled that Verizon "is not obligated to provide line sharing between two CLECs"<sup>1/</sup> and rejected "the CLECs' request to permit a CLEC's UNE-P arrangement to remain intact after line splitting."<sup>1/</sup> Instead, the DTE concludes that Verizon need only allow "line splitting" in the sense that the same CLEC can provide both voice and data over a single loop. See Massachusetts DSL Order at 39.<sup>1/</sup> At Verizon's request, the DTE has given it an open door to evade even its minimum UNE-provisioning obligations with respect to joint CLEC efforts to provide voice and data on a single loop.

This is a clear violation of FCC rules. This Commission has concluded that to comply with the requirements of the section 271 checklist, an ILEC must "provide requesting carriers with access to unbundled loops in a manner that allows the requesting carrier 'to provide any telecommunications service that can be offered by means of that network element.'" TX Order ¶ 325. "As a result, incumbent LECs have an obligation to permit competing carriers to engage in

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87/ Massachusetts DSL Order at 39.

88/ Id. at 38.

89/ The DTE held that where a customer who has voice service from Verizon and data service from a CLEC on the same line, using line sharing, decides to terminate his relationship with Verizon, the data CLEC's only option is to lease the entire loop from Verizon. At that point, the DTE held, it is the data CLEC's option to enter into a voluntary line sharing agreement with a voice CLEC, but Verizon has no obligations with respect to this arrangement. Id. at 39.

line splitting over the UNE-P where the competing carrier purchases the entire loop and provides its own splitter.” Id. (emphasis added). In other words, when one CLEC is collocated and provides the splitter, DSLAM, and data service, a BOC has an obligation to provide a cross-connect to bring the voice channel of the loop back from the CLEC collocation to the ILEC switch, and then to lease to another CLEC the combination of cross-connect, unbundled switching and unbundled shared transport necessary to provide a complete UNE-P voice service.

Verizon contends that it satisfies this requirement because “nothing precludes CLECs from engaging in a line splitting arrangement by ordering the necessary unbundled network elements to offer integrated voice and data service.” Lacouture/Ruesterholz Decl. ¶ 186. But given that Verizon successfully lobbied the DTE to rule that line splitting between two CLECs is not required, this vague statement gives no assurance that Verizon is committed to compliance with the FCC’s rule. It is one thing to promise that if a data CLEC wishes to lease a DSL-capable loop and bring it into its own collocation cage, it is free to split the line and hand off the voice channel to a voice provider, who would then provide its own transport and switching to provide voice service. But Verizon fails to promise that it will enable the voice carrier in this configuration to use Verizon’s own switching and shared transport to provide a voice service – in other words, Verizon fails to promise that the CLEC voice provider will still be able to use the UNE platform to provide voice service.

Moreover, even if the DTE had ordered line splitting over the UNE-P – which it has not – and even if Verizon had committed to provision it – which it has not – Verizon still would be required to prove that it actually can provision it. And Verizon points to no procedures in place that prove it is actually capable of providing this combination of elements in a timely manner. Instead, as indicated above, Verizon relies on its general evidence of provisioning individual

elements. Lacouture/Ruesterholz Decl. ¶ 186. This is palpably inadequate. Verizon provides no evidence of how line splitting over UNE-P would be ordered, how it would be provisioned, how the various actions that would need to be taken by the Verizon and the two CLECs would be coordinated, what the charges would be to the two CLECs who order the service,<sup>1/</sup> or how quickly the work would be performed.

In sum, Verizon has failed to “explain clearly the method” by which CLECs can order and combine UNEs at cost-based rates. LA II Order ¶ 141. This obligation follows from Verizon’s basic obligation to demonstrate that it can provision UNEs for combination in an efficient, accurate, and timely manner. See SC Order ¶ 146. Until Verizon concretely explains how and on what terms these elements will be offered in a manner that permits this configuration, it cannot be

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<sup>90/</sup> The Commission has noted that the “cross-connect rates, as well as rates associated with other elements such as cable support and installation, . . . can have a significant impact on . . . total service provisioning costs,” and that unless the relevant prices and procedures are firmly established, a BOC “could load excessive overhead costs onto this critical input.” In re Local Exchange Carriers’ Rates, Terms and Conditions for Expanded Interconnection Through Virtual Collocation for Special Access and Switched Transport, CC Docket No. 94-97, Report and Order, 10 F.C.C.R. 6375, ¶ 72 (1995).

said to be offering, let alone providing in a nondiscriminatory manner, access to unbundled elements in a manner that allows data and voice to be provided on the same circuit.

This is an issue of critical competitive importance to WorldCom and other voice providers who intend to provide their local customers high-speed data services by teaming with one of the so-called “data CLECs” that specialize in DSL-based data services. Verizon’s failure to provide this combination of elements is in and of itself a sufficient reason to deny this application.

### **III. THE PUBLIC INTEREST WOULD NOT BE SERVED BY GRANTING THIS APPLICATION.**

Verizon has failed to demonstrate that its entry into the in-region long-distance market is in the public interest. As a direct consequence of network element pricing that is neither cost-based nor forward-looking, Verizon does not presently face substantial residential local competition in Massachusetts. If Verizon is allowed to enter the long-distance market now, any incentive it has to improve its pricing and the competitive situation in its local market will disappear. On the other hand, long-distance customers would see only marginal benefits as a result of Verizon’s entry into that market. On balance, therefore, the public will be much better served by denying this application and requiring Verizon to open its local market before it wins long-distance entry.

#### **A. Legal Standard.**

The term “public interest” in a regulatory statute “takes meaning from the purposes of the regulatory legislation.” NAACP v. FPC, 425 U.S. 662, 669 (1976). The Act is premised on the public policy judgment that competition is superior to regulation in efficiently allocating resources and maximizing consumer welfare in the telecommunications market.<sup>1/</sup> The Act relies upon

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<sup>91/</sup> The Conference Report explained that the Act was intended

competition in the local exchange market to bring benefits to consumers in that market and to minimize the ability of incumbent local exchange firms to engage in anticompetitive conduct in all telecommunications markets. Congress thus intended that in making the various public interest determinations required under the Act the Commission would consider whether the proposal at issue “will promote competition.” Conf. Rep. No. 104-458, at 113 (Jan. 13, 1996). The public interest test thus serves as a critical “reality check” to ensure that local markets are truly open to competition before in-region long-distance entry is permitted.

The Commission has therefore properly concluded that the public interest test requires “an assessment of whether all procompetitive entry strategies are available to new entrants,” and whether “the BOC has undertaken all actions necessary to assure that its local telecommunications

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to provide for a pro-competitive, deregulatory national framework designed to accelerate rapidly private sector deployment of advanced telecommunications and information technologies and services to all Americans by opening all telecommunications markets to competition. . . .

Conf. Rep. No. 104-458, at 113 (Jan. 31, 1996).

market is, and will remain, open to competition.” MI Order ¶¶ 386-387. Critically, the Commission also has made clear that competitive pricing is “a relevant concern in [its] public interest inquiry under section 271(d)(3)(C).” Id. ¶ 287.

**B. The State of Local Competition.**

**1. Local Residential Competition in Massachusetts is Lacking.**

While the Commission has eschewed reliance on a metrics test, it has recognized that the absence of actual competition in large segments of a market is critical in the evaluation of whether BOC authorization to offer long-distance services in its region is in the public interest. [FCC Cite] As the Department of Justice explained, “[t]he lack of competitive entry into local markets, however, suggests that local markets are not yet fully open, and it will be necessary to ask why entry is not occurring.” DOJ OK Eval. 43.

Verizon faces de minimis local residential competition in many parts of Massachusetts. Most customers in Massachusetts lack a viable alternative to Verizon for local exchange service. According to Verizon’s own figures, there are only 5,900 UNE-P residential lines in Massachusetts, which means that only 0.2% of the state’s residential consumers receive UNE-P-based services. This is a trivial number of lines – WorldCom and AT&T provision more UNE-P lines than that in Texas, New York and Pennsylvania on a typical day. See Proferes Decl. ¶ 23. Even crediting Verizon’s numbers, CLEC residential customers amount to less than 3 percent of the nearly 3 million residential lines served by Verizon at the end of 1999. See Kelley Decl. ¶ 9. These numbers demonstrate that the state of competition in Massachusetts is far from vibrant, but instead are a clear indication that many parts of the local exchange market in Massachusetts are effectively closed.

Massachusetts is a state that would be high on WorldCom's entry list if the barriers to entry were removed.<sup>1/</sup> Massachusetts consumers are missing out on the very real benefits local competition brings. Individual savings vary with usage and customer location, but WorldCom local residential customers in New York, for example, who subscribe to a flat rate plan can save 40% over Bell offerings. See id. ¶ 10.

Moreover, most of WorldCom's new residential local customers have chosen WorldCom as their carrier for both local and long distance services, increasing their convenience and savings. Customers who choose WorldCom to carry their intrastate toll as well as interstate long distance receive the same low rates for both, minimizing confusion. In addition to the local savings reported above, they also receive access to the lowest WorldCom long distance rates.

WorldCom has also recently launched an innovative "all distance" product, OneCompany Advantage, which includes unlimited local calls, long distance calls at seven cents/minute, and one hour of free calling on Sunday, among other features. Another version of this product offers the same features as well as 200 free minutes of long-distance each month. Customer reaction to this innovative product has been outstanding. Verizon makes dubious claims about the consumer benefits of its long-distance entry, but the fact remains that WorldCom's bundled product offers both better long-distance and better local rates than Verizon's in New York and SBC's in Texas. See Proferes Decl. ¶¶ 13-21. It is hardly surprising that consumers benefit more when regulators

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<sup>92/</sup> Proferes Decl. ¶ 22.



pry open the monopoly local market than when they allow an additional competitor into the already competitive long-distance market.

## **2. The Absence of Residential Competition is Caused by Deficient UNE Pricing.**

There is one overriding reason why most Massachusetts consumers are deprived of the benefits of local competition. Leasing unbundled elements from Verizon is currently the only feasible means of broad-based entry into Massachusetts, but existing UNE pricing makes such broad-based entry economically impossible. Proferes Decl. ¶¶ 22-32. The UNE platform offers CLECs flexibility to offer innovative products to consumers that resale does not, and permits pervasive market entry, which pure facilities-based offering does not. Id. ¶ 8.

As indicated above at supra pp. 31-33, in Massachusetts, a price squeeze prevents WorldCom from entering the local exchange market. Under the rates approved by the Massachusetts Commission, even as improved with the Z-Tel switching discount, WorldCom would lose on average \$4.00 each month for each customer it served, even before it considered its costs. When those internal costs are considered, they reflect that UNE service in Massachusetts is a losing proposition of staggering proportion. Proferes Decl. ¶ 25

Because WorldCom and other CLECs who would use UNE-P are prevented from profitably entering the Massachusetts local market due to the entry barriers erected by Verizon, Verizon's application to enter the long-distance market is contrary to the public interest. Getting the unbundled network element prices right prior to long-distance entry involves far less regulatory oversight than attempting to address after the fact the anticompetitive behavior that will occur due to premature entry. Once Verizon is authorized to enter the long-distance market, its incentives to cooperate with regulators and its rivals evaporate.

### **3. Neither Cable Telephony Nor Resold Services Provide Broad-Scale Competition Within Massachusetts' Residential Market.**

Neither cable telephony nor resale provide an answer to the problem created by the absence of UNE-P competition in Massachusetts. The evident problems with cable are its limited reach and lack of consumer acceptance. Verizon states that AT&T serves 2.1 million cable subscribers with a cable network that passes 80% of all Massachusetts households and “has been upgraded to provide telephony services.” Taylor Decl. ¶ 19 & Att. A. But both of these assertions are false. According to the DTE’s own figures, AT&T has only 60% of the 1.9 million Massachusetts cable subscribers.<sup>1/</sup> More importantly, much of AT&T’s cable plant has not been upgraded to provide telephone service. In truth, AT&T’s cable telephony product is available to no more one-third of the households in Massachusetts, Kelley Decl. ¶ 23, and less than 3% of residential lines are currently served through cable telephony. Id. ¶ 20.

Verizon’s claim that AT&T can provide cable telephony to 80% of the households in Massachusetts is based on a pair of assumptions that Verizon must know to be false. First, Verizon apparently has supplemented AT&T’s cable subscribership by counting as AT&T’s the network of an entirely different company – Cablevision. It is true that AT&T and Cablevision have announced their intention to “swap” cable properties, and if that swap occurs, then AT&T will have approximately an 80% share of Massachusetts cable television subscribers. But as yet, there is no evidence that AT&T has even reached a formal agreement with Cablevision, let alone completed the transaction.

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<sup>93/</sup> See spreadsheet at <http://www.magnet.state.ma.us/dpu/catv/index.htm>

Second, and more troubling, Verizon falsely states that a combined AT&T/Cablevision network is already fully upgraded for telephony. The truth is that AT&T has not yet even completed the upgrade of its own network. Moreover, there is no evidence that any part of the Cablevision network is ready to provide telephony. The upgrading of cable networks to provide telephony is a costly, time-consuming operation. It will in all probability take some time to complete the upgrade that Verizon casually asserts has already occurred. Kelley Decl. ¶¶ 20-23.

Even where cable telephony is available, it provides only a second choice for consumers in addition to Verizon, while UNE-P permits multiple competitors. And even when fully upgraded, cable will never provide ubiquitous service because cable does not go everywhere – rural portions of Massachusetts have no cable TV and little prospect of ever having cable telephony. Nor is it likely that cable facilities, much less cable telephony, reach all the households even in areas generally served by cable. For all of these reasons, cable is not a sufficient alternative to UNE-P service.

The resale story is even less attractive. The Commission has recognized that resale presents fewer competitive opportunities for CLECs than UNE service, noting the inability of resellers to offer products that are not offered by incumbent LECs and the limited ability of resellers to differentiate their products from those offered by incumbent LECs on the basis of price. First Report and Order, ¶ 322. Practical experience confirms this conclusion: WorldCom has learned in New York and Texas that popular competitive products are those that are different from the Bell's products.<sup>1/</sup> The Department of Justice's economic expert also concluded that

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<sup>94/</sup> Kelley Decl. ¶ 11.

resale is a less attractive entry alternative that is less effective in disciplining the behavior of incumbents and exerting downward pressure on retail prices than UNE-P entry.<sup>1/</sup>

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<sup>95/</sup> Schwartz Decl. ¶ 177 (“Competitive Implications of Bell Operating Company Entry Into Long-Distance Telecommunications Services”), attachment to DOJ Okla.Eval.

The experience thus far in Massachusetts demonstrates that resale is an unprofitable entry mode for CLECs. Resale has attracted less than 5% of the state's residential and business customers, and most of those customers are business customers. This is an especially insignificant showing given the fact that resale has been available since 1996 at prices that compare favorably to Massachusetts' UNE prices. Kelley Decl. ¶ 11. The fact remains that resale pricing, even "good" resale pricing, does not allow for profitable entry.<sup>1/</sup> Nor is resale an effective provisional strategy – allowing entry until there are either competing facilities or cost-based UNE prices. The cost of constructing resale OSS, and then the cost of converting customers to some other system after it is made available, is simply too high. Id.

#### **4. Granting This Application Will Not "Force" CLECs Into Massachusetts.**

In a last-ditch effort to persuade the FCC that entry will lead to some public benefit, Verizon speculates that if the FCC grants this application it will "forc[e]" WorldCom to "get off the dime" and compete in the Massachusetts residential market. Verizon Br. at 61; see also Taylor Decl. ¶ 22. Verizon evidently assumes that WorldCom will take this step because it will view the losses that it will suffer in local markets as a fair price to pay to retain long-distance and intra-LATA toll customers.

But the record establishes that it is not fear of erosion of long-distance and intraLATA toll customers that has dictated WorldCom's local market entry decisions, but the existence of working OSS and competitive wholesale prices in the local market.

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<sup>96/</sup> Id.; Proferes Decl. ¶ 8.

WorldCom entered the New York local market in December 1998, and the Pennsylvania market in August 2000, a full year before Verizon won long-distance authority in New York and well before Verizon applied for such authority in Pennsylvania. Similarly, WorldCom began its development efforts in Texas many months prior to SBC's first section 271 application in that state. The fact of the matter is that Bell long-distance entry or no, WorldCom wants the growth and profits that local residential markets offer, and where there is competitive pricing and working OSS, WorldCom will take advantage of these opportunities. Proferes Decl. ¶ 35.

Equally false is Verizon's related claim that to protect their long-distance base WorldCom and the other long-distance carriers will have no choice but to enter markets like Massachusetts once Verizon long-distance entry is granted. Once again, WorldCom's actual market behavior disproves that proposition, because WorldCom is not in fact soliciting local customers in significant portions of New York and Texas, and all of Connecticut where the pricing does not support local entry, even though Verizon, Southwestern Bell and SNET, respectively, are actively competing for WorldCom's long-distance customers in these same sections of these states. Id. ¶ 36.

If WorldCom is not willing to compete for millions of New York consumers in the face of Verizon competition where it anticipates its gross margin would be a positive \$4.70/customer/month, there is no reason to think Verizon's section 271 entry will "force" WorldCom to compete for Massachusetts' local residential customers when the anticipated

statewide gross margin for all but 2% of the population that live in downtown Boston is below that number. See Proferes Decl. ¶ 44.<sup>1/</sup>

**C. The State of Long Distance Competition.**

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<sup>97/</sup> This is especially so when there is no added capital cost of attracting rural New York and Texas customers, since WorldCom has products and systems in place and is providing local service in the state.

While large segments of the Massachusetts local residential market remain tightly shut, “in the long-distance arena, the marketplace is competitive and robust.”<sup>1/</sup> Consequently, consumers do not necessarily benefit when an additional competitor is added to the long-distance market, and Verizon’s claim that the experience in New York proves otherwise is based on a selective, misleading and outdated set of comparisons about long-distance competition in New York. See Proferes Decl. ¶¶ 13-21; Kelley Decl. ¶ 53.

On the other hand, the potential risks to long-distance competition of premature entry by Verizon are substantial. As the Commission has recognized, authorizing a BOC to enter the in-region long-distance market reinstates the anticompetitive incentives that historically repressed competition in the long-distance market. See In re Access Charge Reform, CC Docket No. 96-262, First Report and Order, 12 F.C.C.R. 15982, ¶ 278 (1997). In the absence of significant local competition, Verizon will have the incentive and ability to withhold its cooperation from long-distance competitors, drive up its competitors’ costs, and reduce the quality of service its competitors provide to customers. An open local exchange market will best prevent competitive harm to the long-distance market by in-region entry by Verizon.

In sum, the harm to consumers resulting from Verizon’s premature entry into the local market greatly outweighs the marginal gain to consumers from having another long-distance

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<sup>98/</sup> Oral Testimony of William E. Kennard, Chairman, FCC, Before the Senate Commerce Comm., 1999 WL 332555, at 5 (rel. May 26, 1999).



carrier to choose from. For that reason, it does not serve the public interest to grant this application now.

### **CONCLUSION**

Verizon Massachusetts' application should be denied.

Respectfully submitted,

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October 16, 2000

## **CERTIFICATE OF SERVICE**

I, Mark D. Schneider, hereby certify that I have this 16th day of October, 2000, caused a true copy of Comments of WORLDCOM, Inc. and Appendices to be served on the parties listed below:

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Before the  
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Washington, D.C. 20554

In the Matter of	)	
	)	
Application by Verizon New England Inc.	)	
Bell Atlantic Communications, Inc.	)	
(d/b/a Verizon Long Distance), NYNEX	)	CC Docket No. 00-176
Long Distance Company (d/b/a Verizon	)	
Enterprise Solutions), and Verizon Global	)	
Networks Inc., for Authorization to Provide	)	
In-Region, InterLATA Services in Massachusetts	)	
_____	)	

**COMMENTS OF WORLDCOM, INC. ON THE  
APPLICATION BY VERIZON FOR AUTHORIZATION TO PROVIDE  
IN-REGION, INTERLATA SERVICES IN MASSACHUSETTS**

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TAB	DECLARANT	SUBJECT
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B	Declaration of Mark T. Bryant	Pricing
C	Declaration of Karen A. Kinard	Performance Remedy Plan
D	Joint Declaration of Patty Kwapniewski and Sherry Lichtenberg	Operations Support Systems
E	Declaration of A. Daniel Kelley	Public Interest

**TABLE OF ADDITIONAL EXHIBITS**

TAB	DESCRIPTION
F	Order, Massachusetts D.T.E. 98-57-Phase III, Investigation by the Department on its own motion as to the propriety of the rates and charges set forth in M.D.T.E. No. 17, filed with the Department by Verizon New England, Inc. d/b/a Verizon Massachusetts on May 5 and June 14, 2000, to become effective October 2, 2000 (DTE issued Sept. 28, 2000)
G	Sept. 27, 1999, letter from Lawrence E. Strickling, Chief, Common Carrier Bureau, to Nancy E. Lubamersky, U S West

## TABLE OF CITATION FORMS

FCC Orders	
<u>First Report and Order</u>	<u>In re Implementation of the Local Competition Provisions in the Telecommunications Act of 1996</u> , CC Docket Nos. 96-98 & 95-185, First Report and Order, 11 F.C.C.R. 15499 (1996).
<u>LA I Order</u>	<u>In re Application of BellSouth Corporation, et al. Pursuant to Section 271 of the Communications Act of 1934, as amended, to Provide In-Region, InterLATA Services in Louisiana</u> , CC Docket No. 97-231, Memorandum Opinion and Order, 13 F.C.C.R. 6245 (1998).
<u>LA II Order</u>	<u>In re Application of BellSouth Corporation, BellSouth Telecommunications, Inc., and BellSouth Long-distance, Inc., for Provision of In-Region, InterLATA Services in Louisiana</u> , CC Docket No. 98-121, Memorandum Opinion and Order, 13 F.C.C.R. 20599 (1998).
<u>MI Order</u>	<u>In re Application of Ameritech Michigan Pursuant to Section 271 of the Communications Act of 1934, as amended, to Provide In-Region, InterLATA Services in Michigan</u> , CC Docket No. 97-137, Memorandum Opinion and Order, 12 F.C.C.R. 20543 (1997).
<u>NY Order</u>	<u>In re Application by Bell Atlantic New York for Authorization Under Section 271 of the Communications Act to Provide In-Region, InterLATA Services in the State of New York</u> , CC Docket No. 99-295, Memorandum Opinion and Order, 15 F.C.C.R.3953 (1999), <u>aff'd</u> , <u>AT&amp;T Corp. v. FCC</u> , 220 F.3d 607 (D.C. Cir. 2000).
<u>OK Order</u>	<u>In re Application of SBC Communications Inc. Pursuant to Section 271 of the Communications Act of 1934, as amended, to Provide In-Region, InterLATA Services in Oklahoma</u> , CC Docket No. 97-121, Memorandum Opinion and Order, 12 F.C.C.R. 8685 (1997)
<u>Represcription Order</u>	<u>In re Represcribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers</u> , CC Docket No. 89-624, Order, 5 F.C.C.R. 7507 (1999).
<u>SC Order</u>	<u>In re Application of BellSouth Corporation, et al. Pursuant to Section 271 of the Communications Act of 1934, as amended, to Provide In-Region, InterLATA Services in South Carolina</u> , CC Docket No. 97-208, Memorandum Opinion and Order, 13 F.C.C.R. 539 (1997), <u>review denied</u> , <u>BellSouth Corp. v. FCC</u> , 162 F.3d 678 (D.C. Cir. 1998)

<b>FCC Orders</b>	
<u>TX Order</u>	<u>In re Application by SBC Communications Inc., Southwestern Bell Communications Services, Inc. d/b/a Southwestern Bell Long Distance Pursuant to Section 271 of the Telecommunications Act of 1996 To Provide In-Region, InterLATA Services in Texas</u> , CC Docket No. 00-66, Memorandum Opinion and Order, FCC No. 00-238 (rel. June 30, 2000)
<u>USF Tenth Report and Order</u>	<u>In re Federal-State Joint Board on Universal Service</u> , CC Docket No. 96-45, Tenth Report and Order, 14 F.C.C.R. 20156 (1999)
<b>Declarations and Affidavits</b>	
Breen Decl.	Joint Declaration of Maura C. Breen on Behalf of Verizon (Verizon Tab 5)
Browning Decl.	Joint Declaration of Susan C. Browning on Behalf of Verizon (Verizon Tab 4)
Bryant Decl.	Declaration of Mark T. Bryant on Behalf of WorldCom (Tab B hereto)
Guerard and Canny Decl.	Joint Declaration of Elaine M. Guerard and Julie A. Canny on Behalf of Verizon (Verizon Tab 3)
Kelley Decl.	Declaration of Dan Kelley on Behalf of WorldCom, Inc. (Tab E hereto)
Kinard Decl.	Declaration of Karen A. Kinard on Behalf of WorldCom (Tab C hereto)
LaCouture and Ruesterholz Decl.	Joint Declaration of Paul A. LaCouture and Virginia P. Ruesterholz on Behalf of Verizon (Verizon Tab 1)
Kwapniewski Decl.	Joint Declaration of Patty Kwapniewski and Sherry Lichtenberg on Behalf of WorldCom Inc. (Tab D hereto)
McLean and Wierzicki Decl.	Joint Declaration of Kathleen McLean and Raymond Wierzicki on Behalf of Verizon (Verizon Tab 2)
Mudge Decl.	Declaration of W. Robert Mudge on Behalf of Verizon (Verizon Tab 7)
Proferes Decl.	Joint Declaration of Patricia Proferes, John Nolan, Paul Bobeczko, and Thomas Graham on Behalf of WorldCom Inc. (Tab A hereto)
Taylor Decl.	Declaration of William E. Taylor on Behalf of Verizon (Verizon Tab 6)
<b>DOJ Evaluations</b>	
<u>DOJ Okla. Eval.</u>	Evaluation of the United States Dept. of Justice, <u>In re Application of SBC Communications, Inc., et al. to Provide In-Region, InterLATA Services in the State of Oklahoma</u> , CC Docket No. 97-121 (filed May 21,

	1997)
<b>Other Record Materials</b>	
DTE 7/27/00 Letter	DTE's Letter Denying AT&T's Petition to Requesting the Review and Reduction of UNE Recurring Charges (VZ-MA App. B, Tab 481)
<u>Massachusetts DSL Order</u>	Order, Massachusetts D.T.E. 98-57-Phase III, Investigation by the Department on its own motion as to the propriety of rates and charges set forth in M.D.T.E. No. 17, filed with the Department by Verizon New England, Inc. d/b/a Verizon Massachusetts on May 5 and June 14, 2000, to become effective October 2, 2000 (DTE Sept. 28, 2000)
<u>Order Instituting New Proceeding</u>	<u>In re Joint Complaint of AT&amp;T Communications of New York Inc., et al.</u> , Order Denying Motion to Reopen Phase 1 and Instituting New Proceeding, Case 95-C-0657 <u>et al.</u> (NYPSC Sept. 30, 1998) (VZ-MA App. B, Tab 455, Exh. F)
<u>Phase 4 Order</u>	<u>Consolidated Petitions of New England Telephone and Telegraph Co.</u> , Phase 4 Order, D.P.U. 96-73/74, 96-75, 96-80/81, 96-83, 96-94 (DTE Dec. 4, 1996) (VZ-MA App. H, Tab 162)
<u>Phase 4-A Order</u>	<u>Consolidated Petitions of New England Telephone and Telegraph Co.</u> , Phase 4-A Order, D.P.U. 96-73/74, 96-75, 96-80/81, 96-83, 96-94 (DTE Feb. 5, 1997) (Byrant Decl., Att. 2)
Sayer Decl.	Declaration of Nancy Sayer, <u>In re NYNEX Corp. And Bell Atlantic Corp., Application for Consent to Transfer Control</u> , Tracking No. 960205, 960221 (FCC filed Oct. 22, 1996) (Bryant Decl., Att. 3).