

WILMER, CUTLER & PICKERING

Washington ■ Baltimore ■ New York ■ London ■ Brussels ■ Berlin

November 22, 1999

TELECOMMUNICATIONS LAW UPDATES

FCC IMPOSES “LINE SHARING” REQUIREMENT

On November 18, 1999, the FCC adopted a much-anticipated “line sharing” requirement, under which incumbent local telephone companies must provide a “data channel” within the local loop to competing providers of high-speed Internet access. Non-telco providers of digital subscriber line (“DSL”) services — led by Covad, NorthPoint, and Rhythms NetConnections — argued to the FCC that they suffer a severe competitive disadvantage compared to incumbent local telephone companies. Incumbents could offer their customers a package of traditional voice service and DSL service over a single line. In contrast, DSL providers wishing to offer just data (and not voice) services have been able to sell DSL only to customers who are willing to pay for a second telephone line. Even if a competitive provider did offer basic voice services in addition to DSL, it would have to persuade customers not only to sign up for DSL, but to switch to a new local phone service, in order to match incumbents’ ability to supply voice and data services over a single line.

The FCC’s line-sharing requirement will make it far easier for new entrants to compete with incumbents’ DSL services. Customers now will be able to continue purchasing local telephone service from their existing phone company and at the same time obtain DSL service over the same line from a different provider. The FCC based its line-sharing ruling on section 251(c)(3) of the Communications Act, which authorizes it to require incumbents to make elements of their networks available to com-

petitors on an unbundled and nondiscriminatory basis. The FCC concluded that the ability of new entrants to provide DSL is “impaired” without access to the loop frequencies used for data transmission.

While it is possible for competitive data providers to purchase unbundled loops and offer both DSL and voice service over a single line, just as incumbents do, the FCC found that alternative unrealistic, reasoning that the new entrant would have to make significant investments in circuit-switched technology on top of the investments needed to provide DSL service. In the FCC’s view, competitive providers should not have to enter two markets at once in order to compete in the DSL business. Incumbent local telephone companies had argued that competitive data providers have the options of partnering with new entrants interested in providing voice service or investing in new voice-over-DSL technology (to avoid the need to invest in circuit-switching equipment altogether). But the FCC found these options insufficient to alleviate the impairment perceived by the agency.

The FCC did not specify the exact price that competitors will pay for access to an unbundled data channel. Nor did it discuss how incumbents will recover the costs of implementing a line-sharing requirement. But the FCC did state that it will issue a pricing methodology to guide the statutorily required negotiation and state arbitration process. Under that methodology, the price competitors pay for the data channel will be roughly equivalent to the percentage

of loop costs that incumbents allocate to their own DSL services. In most cases, that figure has been close to zero. If the phone companies adhere to that allocation, the price of an unbundled data channel will be nominal.

The statutory negotiation and arbitration process — in which price and other terms and conditions will be formally established — can take up to nine months to run its course. But the FCC indicated that it will encourage state commissions to issue interim orders that require incumbents begin offering line sharing to competitors on the 180th day following a competitor's request for negotiation. The FCC estimated that it will take up to 180 days to work out the various operational issues associated with line sharing, such as installation, billing, and customer service procedures. But it wants line sharing to begin as soon as these operational issues are ironed out. If state public utility commissions heed the FCC's call to order line sharing on an interim basis, before the arbitration process is complete, such requirements would be effective until the state commission enters a final order no more than 90 days later. The FCC said that competitive providers may request line sharing immediately, even before the FCC's rules take effect.

The FCC's decision to order line sharing will provide a significant boost to competitive data providers. The FCC hopes that the real winners will be consumers, who the agency expects will benefit from faster deployment of DSL service, lower prices, and better service. Some observers fear that residential voice competition will suffer, because new entrants will gain a strong incentive to provide DSL service only, for which they will pay a negligible cost for the use of the incumbent's network. Competitive voice carriers, by contrast, will continue paying the full cost of an unbundled loop. Incumbent phone companies also have argued that the prospect of different carriers applying different power sources to a single line threatens to degrade the quality of customers' voice services. The FCC and new entrants have dismissed these concerns.

Incumbent phone companies are certain to challenge the legality of the FCC's order. They are expected to argue that the FCC has exceeded its authority under the Communications Act and that the order is deficient for various procedural reasons. An appeal most likely will take more than a year to complete. If the order is not stayed in the interim, the impact on the market and on prices for competitive DSL service may be evident shortly.

Lynn R. Charytan (202/663-6455)
Matthew A. Brill (202/663-6559)

This letter is for general informational purposes only and does not represent our legal advice as to any particular set of facts, nor does this letter represent any undertaking to keep recipients advised as to all relevant legal developments. For further information on these or other telecommunications matters, please contact one of the lawyers listed below:

Scott Blackmer
Lynn Charytan
John Harwood
William Lake
Daniel Phythyon
William Richardson

202-663-6167
202-663-6455
202-663-6333
202-663-6725
202-663-6545
202-663-6038

SBlackmer@wilmer.com
LCharytan@wilmer.com
JHarwood@wilmer.com
WLake@wilmer.com
DPhythyon@wilmer.com
WRichardson@wilmer.com