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Telecommunications Law Update

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FCC Issues Long-Awaited Decision Concerning Local Telephone Competition

On August 21, 2003, a divided Federal Communications Commission (“FCC”) released its long-awaited Triennial Review Order (“Order”), addressing the rights of new entrants to the market for local telephone service (known as “competitive local exchange carriers” or “CLECs”) to continue to lease the network facilities (known as “unbundled network elements” or “UNEs”) of incumbent local exchange providers (“ILECs”) at wholesale discounts, including the entire platform of network elements (the “UNE-Platform” or “UNE-P”). It took the FCC six months to release the Order because of a sharp split between FCC Chairman Michael K. Powell and the three FCC commissioners in the majority, led by Commissioner Kevin J. Martin, over whether ILECs should continue to be required to lease the UNE-Platform to CLECs at the current discounted wholesale rates. Broadly speaking, and subject to certain limitations, the majority decided to preserve that right where CLECs provide local voice service to residential and small business customers. However, ILECs obtained regulatory relief in the broadband arena and in the market for providing local voice service to medium and large business customers. And the FCC provided a greatly expanded role for state regulators.

In the Order, the FCC reexamined many of the obligations it imposed on ILECs following enactment of the 1996 Act. Looking at current market conditions, the FCC addressed whether CLECs would still be economically or operationally “impaired” (the statutory standard) if they no longer could lease a particular ILEC network facility at the current discounted wholesale rates. For the most part, the FCC’s conclusions depended on the class of customers served (residential versus large business customers) and the type of telecommunications service provided (voice service versus high-speed data transmission). Although the FCC made some “national findings” concerning CLECs’ need to

rely on the ILEC network, it delegated to state regulators the power to make market-, location-, or route-specific “granular” determinations as to whether CLECs should have continued access to particular ILEC network facilities.

Some of the key rulings in the Order are:

Circuit Switching for Mass Market Customers. The FCC made a national finding of “impairment” requiring ILECs to continue to offer unbundled circuit switching – a key UNE-Platform element – to CLECs seeking to serve residential and small business customers (“mass market” customers). However, the FCC left the door open for a future determination at the state level that such impairment is not present in a particular market or has been eliminated. First, the FCC’s impairment conclusion resulted in part from the difficulty it perceived in converting large numbers of individual customers from ILEC switches to CLEC switches. The FCC directed state regulators to approve within nine months a new “batch” process that would facilitate such conversions, unless the state finds that the existing process already causes no impairment in particular markets. In addition, the states must undertake market-specific review of CLECs’ ability to rely on their own switches. The FCC established certain “triggers” and other criteria that states could use to determine that CLECs were not impaired in particular markets. Even where the states conclude that CLECs do remain impaired in the provision of service without unbundled switching for mass market customers, the states must determine whether such impairment can be addressed through temporary rather than permanent steps, such as offering unbundled switching on only a short-term basis.

Circuit Switching for Medium or Large Business Customers. The FCC made a national finding that CLECs

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are not impaired without access to unbundled circuit switching when serving medium- to large-business (“enterprise”) customers over high-capacity loops. However, if state regulators reach a different conclusion for specific markets, they may petition the FCC within 90 days of the effective date of the Order for the continuation of this unbundling requirement in particular markets.

Broadband Networks. The FCC eliminated most requirements for unbundling “next generation” networks, equipment, and facilities used to provide broadband services, including fiber to the home loops, hybrid fiber/copper loops, and packet switching. The FCC based its decision in large part on Congress’ goal of encouraging investment in broadband infrastructure. Even in the limited circumstances where fiber loops are subject to unbundling, only a narrowband voice channel must be unbundled.

Copper, DS1, DS3, and Dark Fiber Loops and Transport. The FCC ruled that optical, high-capacity fiber loops serving enterprise customers need not be unbundled, but that dark (or “unlit”) fiber as well as high-capacity DS-3 and DS-1 lines would remain subject to unbundling, unless states found that barriers to entry did not exist for specific customer locations. The FCC similarly discontinued ILECs’ obligation to provide optical level transport to CLECs. By contrast, the FCC made a national finding of impairment with respect to DS1 transport and DS3 transport (up to capacity of 12 DS3s), and thus presumptively retained ILECs’ unbundling obligations for these network facilities. States, however, must consider on a route-by-route basis whether the unbundling obligation should be eliminated.

Line Sharing and Line Splitting. The Order eliminates the requirement that ILECs provide other carriers with access to the high-frequency portion of the loop for use in providing DSL services (known as “line sharing”). During a three-year period, however, CLECs may continue to add line sharing customers at transitional, gradually increasing rates. In addition, the Order grandfathers existing line sharing customers. The Order also continues to require ILECs to permit and facilitate “line splitting” arrangements, under which one CLEC uses the voice portion of the loop while another uses the data portion.

Enhanced Extended Links. The FCC ruled that CLECs may order new combinations of unbundled elements, including enhanced extended links (or “EELs”), where they satisfy certain requirements designed to prevent them from using EELs to carry long-distance traffic to avoid paying special access fees.

Section 271 Requirements. The FCC held that where unbundling of a certain network element is a prerequisite for a BOC to provide long-distance service under Section 271 of the 1996 Act, the unbundling requirement continues under Section 271, notwithstanding a finding of lack of impairment under Section 251. However, once the “no impairment” finding has been made, the ILEC must offer the element only at a “just and reasonable” market price, not the discounted price mandated under Section 251.

TELRIC Clarification. The FCC also clarified certain aspects of “TELRIC” (for Total Element Long-Run Incremental Cost), the methodology under which UNEs are priced by state regulators. Among other things, the FCC ruled that the cost of capital and depreciation components of TELRIC should reflect the risks and conditions an ILEC would face in the theoretical, fully competitive market that TELRIC assumes, rather than the actual market as it exists today. The FCC did not mandate the use of particular asset lives in calculating an ILEC’s depreciation expense; the Commission did suggest, however, that states might want to consider the use of “accelerated” depreciation to better capture the relevant risks of providing UNEs. In addition to these clarifications, the FCC stated that it would commence a rulemaking proceeding in the near future to consider broader changes to TELRIC.

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These are only some of the key points of the FCC’s 576-page order, which industry participants are just beginning to digest. We will be releasing additional updates examining in greater depth many of these findings and their impact on telecommunications law and the telecommunications industry.

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:

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