

SMALL BUSINESS ACCESS TO COMPETITIVE TELECOMMUNICATIONS SERVICES

HEARING BEFORE THE SUBCOMMITTEE ON REGULATORY REFORM AND OVERSIGHT OF THE COMMITTEE ON SMALL BUSINESS HOUSE OF REPRESENTATIVES ONE HUNDRED SEVENTH CONGRESS FIRST SESSION

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THURSDAY, NOVEMBER 1, 2001

HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS,
SUBCOMMITTEE ON REGULATORY REFORM AND OVERSIGHT,
Washington, DC.

The subcommittee met, pursuant to call, at 2:15 p.m. in room 2360, Rayburn House Office Building, Hon. Mike Pence (chairman of the subcommittee) presiding.

Chairman PENCE. I would like to welcome everyone, especially our witnesses, to this fourth in a series of hearings on telecommunications which is being conducted by the Subcommittee on Regulatory Reform and Oversight of the Committee on Small Business here in the House of Representatives.

This hearing is on the subject of small business access to competitive telecommunications services, and I will welcome each of the witnesses individually. I thank you very much for being here and for your interest in participating in the public process.

I will alert you as a housekeeping matter that we have votes that are expected to imminent, and in the event there are votes, we will adjourn and the Chair and any of the other members that are present will simply recess and return in the hopes of not inconveniencing any of our witnesses or those in attendance any further. Let me also say for those of you that are aware of the anthrax contamination in my office that I am confident the attending physician has urged me that I am not contagious in any way, in any way carrying any airborne antibodies with me, so those of you in the back of the room can move forward and make yourself comfortable.

Five years ago the Telecommunications Act of 1996 was signed into law. When it was enacted, promises from congressional leaders, the President and industry was that the legislation would create a revolution in the provision of telecommunications services.

A revolution certainly has occurred and an entirely new economy based on the Internet has developed in the past five years. Hundreds of new companies have been formed to break into what was once perceived as an impenetrable monopoly, the local telephone market, unfettered competition in the telecommunications market, and the benefits of lower prices and better services, particularly for small business owners throughout the country, remains a distant goal, not a near-term reality.

Some experts believe that the competitive goals in the '96 Act will not be met without facilities-based competition. There is no doubt that facilities-based competition will play a key role in pro-

viding competition to the incumbent local telephone companies, yet facilities-based competition is not the only option.

As the Supreme Court noted in *AT&T v. Iowa Utilities Board*, the 1996 Act “imposes no such limitation; if anything, it suggests the opposite.”

Three of the witnesses today are competitors of incumbent local telephone companies that started after the enactment of the 1996 Act. Their business models are based on the fact that the facilities-based competition is not mandated by the act. They will explain how they purchase unbundled network elements that constitute the foundation of local telephone service from incumbent local telephone companies, reassemble those elements along with elements that they provide themselves, and sell that package to provide competitive local telephone service.

A key component of providing local telephone service is access to switching so that telephone calls can be routed properly. In its initial order implementing the 1996 Act, the Commission designated switching as an unbundled network element that incumbents must sell to competitors should they so request it.

The Supreme Court determined that the Commission misinterpreted the '96 Act and forced the agency to develop a new list of unbundled network elements. The Commission did that, and determined that incumbents would no longer be required to sell switching as an unbundled network element to competitors who wish to serve customers with more than four telephone lines. The Commission determined that switching service was sufficiently available from sources other than incumbents for all customers except small businesses and residents.

The decision violated the Small Business Act, plainly put, and the Regulatory Flexibility Act, as was pointed out in a detailed letter by a predecessor in this subcommittee, and the immediate past chairman of the Small Business Committee, the Honorable Jim Talent.

The Commission failed to follow the Small Business Act when it determined that small businesses were only those businesses that have fewer than four telephone lines, nor did the Commission properly assess the economic impact of the decision on small competitors, and whether there were any potential alternatives that might be less burdensome on them.

The telecommunications companies will explain how their businesses are dramatically and adversely affected by the Commission's decision, and how they have been now waiting for nearly two years to get a decision on the reconsideration of the issue.

During the pendency of this proceeding, they have been unable to expand because the rules governing their businesses remain in flux. In turn, this harms the ability of these companies to provide service to many small businesses. More importantly, if the Commission decides to extend its current rules to all areas of the country rather than the central business districts of the 50 largest cities, it could prevent competition from flourishing in many smaller cities like Muncie and Anderson, that represent hubs of the congressional district that I serve.

The final witness will explain to us that the needs of a small law firm or any other small business do not necessarily comport with

those of larger businesses or residential customers. That conclusion appears to be obvious to everyone but the Commission, which historically fails to distinguish between small businesses and residential customers. The proceeding at issue here simply continues that illogical and unsupported precedent.

A bit of a personal word. There has been some concern expressed to this committee in the days preceding this hearing that this hearing may turn into an opportunity to attack the RBOCs. Allow me to say that this is not a hearing held for that purpose. It is not held for the purpose of allowing competitors of RBOCs to do that. Rather, this hearing is specifically and exclusively about the regulatory actions of the FCC.

The Commission as of today should be on notice that this Chairman and this subcommittee expect the laws of this Congress to be obeyed. If the Commission fails, the commissioners can expect that they will be explaining their decision to this subcommittee in the near future.

Let me thank the witnesses again for taking time out of their busy schedules and making a trek to Washington, D.C. under these unusual circumstances and during this unusual time in our history. And with that, I will introduce our first witness who will be recognized for five minutes, and I believe it is Gregori, I always ask.

You activate your microphone, Mr. Gregori, on the pad, and the lights in front of you, by way of housekeeping, will notify you when you get within about 30 seconds of finishing with the yellow and the red. It does not mean immediately stop. It means you can wrap up your comments in an orderly way.

Joseph Gregori is the chief executive officer of InfoHighway Communications Corporation, which is an integrated communications provider, offering voice data and end communication services to primarily small and medium-sized business customers. The company offers competitively priced, high quality one-stop shopping for local and long distance telephone services, high speed data, and network design and wiring services.

Prior to joining InfoHighway in September of 1998, Mr. Gregori was the chief operating officer for Price Cellular Corporation, a publicly traded wireless communications provider with operations in over 20 markets throughout the United States of America.

Mr. Gregori is a CPA, and an honors graduate of Adelphi University. He began his professional career in public accounting, and was employed in the audit division of Deloitte & Touche.

And Mr. Gregori, you are most welcome and are recognized for five minutes.

STATEMENT OF JOSEPH A. GREGORI, CHIEF EXECUTIVE OFFICER, INFOHIGHWAY COMMUNICATIONS CORP.

Mr. GREGORI. Thank you. Good afternoon.

You now know I am Joseph Gregori and I am the CEO of InfoHighway Communications. I would like to thank the Chairman and other members of the committee for allowing me the opportunity to speak with you today.

Our company is one of the many CLECs that provide telecommunications alternatives to the small business community. The

FCC currently has rules in place that limit our ability to serve the small business market, and worse, is considering new rules that could further limit our ability to compete for small businesses. This limitation will in fact threaten our entire industry's existence as a competitive alternative for the small business community.

A quick further overview of our company. As you heard, we provide telecommunications services, primarily in the northeastern part of the country, from Massachusetts down through New York, New Jersey, Pennsylvania, Baltimore, Washington and right here in the D.C. area.

According to the New York State Public Service Local Competition Report for the year ended December 2000, InfoHighway Communications was the twenty-third largest competitive provider in New York State, out of over 100 responding companies. Currently we have in excess of 5,000 customers that are mostly small businesses. Our typical customer might be the local print shop, the neighborhood travel agency, or your doctor's office.

Our strategy has been to bundle together local and long distance voice services while we slowly and deliberately build out our own data network to deliver high speed internet access utilizing digital subscriber line technology, also known as DSL.

This smart build approach allows us to build market share and cash flow while making the necessary long-term investment in building networks. To date, we have invested over \$7 million in network facilities.

Our company does not have the resources to build a ubiquitous voice and data network to compete with the incumbents. Those companies, as you know, have had over 100 years to build that, most of the time protected by regulation from any competition.

We now hear from the likes of Verizon that they welcome competition—but only from competitors their own size, those companies able and willing to duplicate their network. Of course, no company can do that, especially in today's environment.

Further, Wall Street and the private equity markets have no appetite today for "Field of Dreams" type builds, build new data networks, build new voice networks and we will finance them. That era is gone.

The FCC needs to hear from you and others concerned about the state of, or lack of, competition in the local markets, particularly for the small business customer.

We lease facilities from Verizon and utilize unbundled network elements, commonly referred to as UNEs, combining UNEs in what is referred to as the unbundled network element platform, or UNE-P. These offerings are expressly provided for in the 1996 Act and time and time again state and federal regulatory bodies have ruled they must be offered to competitors.

Let me share with you a little bit about the state of competition in New York which has many times been showcased as the success story for local competition.

My view is that New York State probably is the most competitive state in the nation. However, if you examine the facts and put them together, rather than look at them just simply as statistics, and consider especially the huge role of UNEs and UNE-P, you come away with a very different perspective.

The New York State PSC issued this yearly report titled "Analysis of Local Exchange Competition." On the surface, the report looks encouraging, but closer examination, coupled with the state of our economy, tell us competition is in trouble.

The report indicates, as you would expect, Verizon-New York still accounts for most of the local revenues; in fact, \$5.1 billion or 82 percent, and AT&T ranks number two. No surprise. However, what is startling is that AT&T is a distant second with \$168 million or approximately 2.7 percent of the total revenues in that market. In over five years, AT&T has less than three percent share of the New York local telecom market.

If a company the size of AT&T with its resources and brand recognition cannot obtain more than 2.7 percent, one has got to ask why.

By contrast, the same report indicates that Verizon-New York has now captured 20 percent of the long distance residential market in the first year since it entered that market. Are they that good at marketing and everyone else so inept?

The irony is that what is pointed to as competition from the CLECs in New York has resulted primarily from the use of leased facilities from Verizon. Approximately 80 percent of all the competitive lines in New York use leased facilities, and this is precisely the option that the FCC is foreclosing.

I implore you to take up our case. Thank you. I appreciate your time.

[Mr. Gregori's statement may be found in the appendix.]

Chairman PENCE. Thank you, Mr. Gregori, and we will hold any questions about your testimony until after we have heard from all of the witnesses.

Richard Burk is also with us today. Mr. Burk began his telecommunications career with Southwestern Bell in 1978 as an account executive in Southwestern Bell's marketing group. In 1984, Mr. Burk joined Value Line of Longview, a competitive long distance company. As president there, he honed the skills of technical operations, regulatory affairs, accounting, finance, marketing and other aspects of operating a competitive small business.

From Longview, Mr. Burk went on to become vice president of operations for American Telco, a Houston, Texas-based privately held regional long distance provider. While there, he negotiated the first post-telecommunications act local interconnection agreement with a Bell Company.

In 1996, Mr. Burk joined USLD Communications in San Antonio, Texas, which is a Texas-based long distance provider. As vice president of strategic development, he oversaw the company's pursuit of authority to enter local markets in 22 states and negotiated interconnection agreements with Southwestern Bell, Pacific Bell and others. Under Mr. Burk's direction USLD purchased and implemented a state-of-the-art local switch and was in the process of developing a strategy to convert its resale customers to UNE-P when it was acquired by Qwest.

After leaving Qwest in 1998, Mr. Burk started Network Intelligence, Incorporated, the company known today as NII Communications. He is the president and chief executive officer of NII,

which is a competitive local exchange carrier serving nearly 7,000 small business customers throughout the State of Texas.

And Mr. Burk is most welcome to the subcommittee and is recognized for five minutes.

STATEMENT OF RICHARD E. BURK, PRESIDENT AND CEO, NII COMMUNICATIONS

Mr. BURK. Thank you very much, Mr. Chairman. I appreciate the opportunity to speak to the subcommittee.

I have been characterized as a veteran of the industry. I have been around it a long time. But in 1999, my wife and I invested our life savings in starting NII, which is really a small business still today, probably one of the smaller companies up here. We are going to do about \$20 million in revenue this year. We are real proud of that. But relative to telecom companies, that is not real big.

But I also think we are probably, as of the last few months, kind of operating on a break-even basis. We are not losing money, and that is also fairly unique in the telecom business, and we are real proud of that as well. And one of the reasons that is the case is that UNE-P has been offered in Texas on pretty much an unfettered basis as a result of the 271 negotiations and what is known as the T2A. However, that is in jeopardy now. Some time limitations have expired and the commission there is considering whether or not it should now adopt the restrictions placed on it by the FCC.

And those restrictions are very onerous to us. They cloud your ability to go into the major markets, and we are very concerned that they may spread to all markets.

Our 7,000 customers are spread across approximately 250 small towns in Texas. I have a lot of customers and employees in the districts of Representative Combest and Representative Gonzalez, who are on your subcommittee, and it matters to them.

Rather than reiterate all of my testimony, attached to my testimony is letters from 22 of our customers which we did not spend a lot of time obtaining; we just asked some of them what they thought, but I want to read you some excerpts out of three of them because I think they really speak to the issue.

Mr. Jim Gerab, who is the president of Prestige Home Health Care wrote me this letter, it is handwritten, and it is in your testimony. It says, "Dear Richard: As you know how important competition is, I wanted to take out the time to thank you. NII has allowed my company enough savings to be able to put in place a health care package for our employees. Keep up the good work. Thank you."

Drew Longmeyer of Longmeyer Plumbing in Abilene, Texas, just part of their letter says, "Well, the second bill of NII is in and you are not right about the savings. We saved even more than you said we would. Spending 70 to 80 dollars more a month might not seem significant to a larger company, but it makes a big difference to our small company. In our case, it is the payment for equipment we have needed but could not afford." And he goes on to talk about some other aspects of our service.

And in these letters you will find the customers like us to varying degrees, but a common thread among all of these customers is that they are very adamant and appreciative of the fact that they have had a choice as a result of what is going on. In fact, John Timms, the president of Isabelle's European Day Spa, Inc. says, "As an owner and operator of two successful Day Spas, I tip my hat to whoever has made it possible to finally get out from underneath the thumb of Southwestern Bell." And he says some other things.

But those are just example—I really recommend that you read all of those letters because it really speaks to what is going on out there. The reality is that the economic model that produces the benefits for the small business today is UNE-P.

Now, my company offers a fully integrated set of services. We provide local service, long distance, and dial-up internet access in places where many other companies do not provide it. We also offer broad-band DSL, web hosting and web site design. So it is a complete package for small businesses, but the fact of the matter is they do not really have a choice absent what the UNE-P providers are providing.

The statistics that Mr. Gregori quoted awhile ago relative to the long distance penetration in local competition in Texas are very similar to what they are in New York, and these are the two best markets in the country for competition.

Our plan was to be in a number of states other than Texas, and we have had to rethink those plans based on the availability of capital and that capital is restricted by the regulatory cloud that hangs over our industry, particularly if you are using the UNE-P strategy.

So thank you for hearing us, and I will be glad to answer questions when it is time.

[Mr. Burk's statement may be found in the appendix.]

Chairman PENCE. Thank you, Mr. Burk.

And we will enter all the correspondence into the record without objection.

Mr. BURK. It is attached to the testimony.

Chairman PENCE. Mr. Robert Curtis is with us. He is currently president of Z-Tel Network Services, and has served as senior vice president, strategic planning, since July 1999. From May 1998 to June 1999, Mr. Curtis was vice president for business development and legal affairs at Z-Tel. From September of 1995 to April of 1998, he was an attorney at the Houston office of Fulbright & Jaworski, L.L.P., where he specialized in antitrust and complex federal litigation. Mr. Curtis graduated from Duke University School of Law in 1995, and like the Chairman, started his career in the legal profession, but then got an honest job. At least in Mr. Curtis' case, that is true. [Laughter.]

Mr. Curtis, you are recognized for five minutes.

**STATEMENT OF ROBERT A. CURTIS, PRESIDENT, Z-TEL
NETWORK SERVICES, INC.**

Mr. CURTIS. Thank you, Mr. Chairman, for the opportunity to testify today.

I would like to talk today about an FCC rule that denies small businesses access to services which, if they were available, would

increase their efficiency, profitability, and the service quality they are able to provide their customers.

Z-Tel is one of the largest competitive providers in the telecommunications industry. We have 250,000 subscribers today. We are in 35 states. In the last two years, we have grown our revenue from about zero to \$300 million a year.

We are a child of the Telecom Act of '96. Although we began life as a software development company, with the goal of developing and providing innovative software applications to end users, we quickly discovered that the best way to do that was to provide contact with our software to the end users' telephone. So we are really a company that tries to combine two worlds; existing telephone with new and creative software applications.

Consequently, we have invested over \$100 million in software investment, and employ about 85 software development engineers in our offices in Atlanta.

But that business plan could not exist without something like the unbundled network element platform. There are two ways that a telecom company can choose to deploy capital today. It can either choose to rebuild an existing legacy network, which is a fine business strategy, but not Z-Tel's.

Or you can choose to take that same capital, deploy it in a different way, try to create innovative things, whether it is an innovative billing system, whether it is a different data network, or whether, in our case, there is simply innovative software applications to ride on top of the existing network, and that is really the method we have chosen to take.

So Z-Tel is here to explain how this ill-conceived FCC rule harms and discriminates against small businesses, because the rule prohibits these small businesses from receiving our services.

First of all, this rule arbitrarily denies access to some of Z-Tel's services simply based on how many lines they have, whether it is three or more, or whether they are in some areas but not others. Consequently some small businesses have access to applications that we think would enhance their businesses while others do not through, as far as we can tell, arbitrary factors. We think that is discriminatory.

But there are also some breeds of service that Z-Tel has on the drawing board, applications that we more or less have working in our development shops that we cannot deploy right now. One of the things we really want to try to solve is the problem with many branch offices in disparate parts of the country. Because we have a footprint in 35 states, we would be able to connect insurance branch offices with a voice recognition platform so that insurance agents could be reached by intelligent messaging capabilities, by voice recognition communicate with themselves, and communicate with different insurance branches. But we are not able to offer a ubiquitous solution to the insurance agent industry—State Farm would be an example—because some of those branch offices have more than four lines in the top 50 MSAs, so we cannot offer a ubiquitous solution.

Same sort of thing with the banking industry. We would love to take our software and deploy an application that would send a message to every person who receives their social security check on

the day that check clears the bank. But to do that we have got to offer the application to the entire industry, not just the small branch bank that happens to be in Waco. That is where a tremendous amount of our advantage could come from, offering ubiquitous service in small towns where other companies are not deploying any facilities at all. But to make this work at all, you have got to be able to provide the service to all business of that type, whether it is in Waco or whether it is in downtown Manhattan, and the existing FCC rule completely prohibits the roll-out of that service.

It also prohibits the growth of a company like Z-Tel because telecom is very much an economies of scale business. If we are required to develop a product which we can only hope to offer to a subset of the small business market, it really decreases our incentive for developing products that would be good for businesses wherever they are and however many lines they have. It also, frankly, is a scary thing for a company like Z-Tel to have to consider selling phone service to a company who may actually grow because if we sell phone service today to someone who is in Manhattan and they have three lines, we actually would have to give them back to Bell Atlantic or to Verizon when they got their fourth line. That is what the FCC rule requires. It certainly does not promote us competing for small business customers in New York.

So we think this rule is bad policy, it discriminates against small businesses, and it precludes companies like ours from being even more aggressive in our development of innovative services for those businesses.

Thank you for your time.

[Mr. Curtis's statement may be found in the appendix.]

Chairman PENCE. Thank you, Mr. Curtis.

Our final witness on this panel before the Chair has some questions for our witnesses is Laurence May who graduated from Franklin Marshall College in 1972 with a B.A. in government, Phi Beta Kappa. He is a 1975 graduate of New York University School of Law where he was business editor of the New York University Law Review.

And for the past 14 years, 12 as a member of the firm, Mr. May has been associated with Angel & Frankel, P.C. It is a boutique law firm located in New York City which specializes in business reorganizations, and creditor and debtor rights.

Mr. May has served on various committees, including the committee to review civil procedures for the United States District Court for the Eastern District of New York, and has widely lectured on bankruptcy-related topics.

And it is delightful to have you here, Mr. May, and you are recognized for five minutes.

STATEMENT OF LAURENCE MAY, PARTNER, ANGEL & FRANKEL

Mr. MAY. Thank you, Mr. Chairman. I am still searching for my honest job, but I would like to thank you, Mr. Chairman, and members of the committee for offering me this opportunity to speak to you this afternoon.

Our firm is a small business operating in New York City. We employ approximately 20 people, including the attorneys on staff, and we have four partners, and I am one of the four partners.

Our local telephone service is now being provided through 16 or 17 local business lines by InfoHighway Communications, Mr. Gregori's company. In addition, InfoHighway Communications provides us with our high speed internet access and our e-mail service as well. And we anticipate that when our long distance contract expires next month we will probably transfer our long distance service to InfoHighway as well.

InfoHighway also provides us with credit card service on long distance calling which has been rather important for us in the fact that we have been doing a lot of traveling in our practice recently, and at rates that we were never offered by any other carrier.

As a small law firm with, I think, a fairly sophisticated practice in the area of business reorganization and debtor and creditor rights, we find ourselves competing constantly with much larger firms. We have to distinguish ourselves based upon our pricing and the service that we can provide to our clients, and in fact, we use that as a test to the vendors that we hire to provide services to us.

Prior to InfoHighway, local telephone service had been provided to us by Verizon or one of its pre-merger predecessors. We generally had the sense that our account, we thought fairly sizeable, was of insufficient size to be of particular importance to such a large company. When InfoHighway approached us to provide local phone services to us, it took the time to understand our business, to explain how we can control our costs. It took the time to prepare a very detailed cost analysis for us, and met with me and members of our firm and people on our staff to explain how our services could be enhanced and how we could have services provided to us at a lower rate.

Our firsthand experience with InfoHighway led us thereafter to transfer our data services to the company. I have no recollection in all the years that we have been dealing with various phone providers of any other representatives coming to us and discussing our account or suggesting ways in which we could better manage our costs.

We really did not think we had a viable alternative in local service until we met InfoHighway, and we are pleased that they are around to offer us this alternative.

We find it convenient, moreover, and efficient to deal with one representative telecom vendor, one who can handle all of our various requirements. I think other small businesses need and want the same kind of services that we now enjoy from InfoHighway. We do not have the resources and I suspect others in our situation have the same issue, or the staff to deal with telecom communication issues which would arise and do arise when we have multiple vendors. We have less influence, obviously, than larger firms, so it is important that we have vendors who are attuned to our problems and help us compete in the legal marketplace.

When we have questions or when there is a service problem, we have over the past several months and years found InfoHighway's response to be the best of any provider that we have experienced either before or since.

Let me give you an example of one way in which InfoHighway has helped us save money. Our local calling plan has line fees which are a lot less than we previously were paying with our other providers. Our prior calling plan incorporated three-minute requirements which InfoHighway does not.

Given that we are a law firm that does thousands of phone calls each year, many of which are less than one minute in time, the fact that we are able to be billed on a minute-by-minute basis rather than the three-minute minimum saves us substantial amounts of money.

With InfoHighway, we have a choice as to local phone service providers. But it is equally important to us that we can look to InfoHighway for high speed data services through its DSL lines. As you may or may not be aware, the United States Bankruptcy Court for the Southern District of New York is a pioneer in the electronic filing of documents. Much of our practice is with that court, and it is critical for us that we have access to reliable and reasonably priced high speed data services so that we can file and retrieve documents and keep apprised of developments in cases in which we are involved. InfoHighway has admirably addressed our needs in this respect.

I do not claim, Mr. Chairman, to understand all of the issues before this committee, but I do know that as a small business having a choice for local phone service has proved important to us. I encourage you and the members of this committee to take the necessary action to be sure that in the future there is more, not less, competition in this marketplace.

Thank you, Mr. Chairman.

[Mr. May's statement may be found in the appendix.]

Chairman PENCE. Thank you. The Chair very much appreciates Mr. May's presentation, and especially his sense of humor. Let me begin with some questions for our last witness, except I have a series of questions for some of the competitive providers that are here to help me understand this a bit better.

But from a practical standpoint, how did you come to find out about InfoHighway at your firm.

Mr. MAY. Well, I had known Mr. Gregori before he was with InfoHighway. I believe we had used some of his services at Price Cellular. And through that connection and prior connections, he came to us and explained to us what he could offer with InfoHighway.

Chairman PENCE. Just as a curiosity, when you told Verizon that you were planning on switching, did they—in the economic model that you are operating in, did they respond in a competitive way? Did they offer any of the incentives that were on the table with InfoHighway?

Mr. MAY. Not that I can recall, Mr. Chairman.

Chairman PENCE. How many law firms that you deal with in your practice have more than three telephone lines?

Mr. MAY. I imagine almost every one; the substantial majority of the firms have multiple, multiple lines; even smaller firms.

Chairman PENCE. Would you characterize those nonetheless as small law firms, small businesses?

Mr. MAY. Well, we deal quite frequently with large firms, but firms that I am familiar with of our size and small firms of say five to 30 lawyers, which I would clearly characterize as small business firms, have multiple lines, and most of them which do bankruptcy work in the Southern District also require the high speed DSL services as well, and have multiple lines as well.

Chairman PENCE. Well, so by inference, I sense that you would answer affirmative to the necessity of DSL services and this kind of service to be in the business you are in?

Mr. MAY. Yes, it is essential.

Chairman PENCE. Thank you.

To Mr. Gregori, a very broad question, and I may pose this to some of the other competitive providers that are here, if the FCC maintains the current restrictions on the availability of switching as a UNE, how would it affect the plans of UNE-P carriers to expand?

Mr. GREGORI. Well, I am going to hone in on the last phrase. To expand?

The industry today is struggling to survive. So under the current guidelines, the current rules, we are hanging on. The people before you are very experienced, seasoned individuals that have been through it before, and we are executing at the very, very basic levels to struggle through it and give life. We need relief in this area.

Any further restrictions, candidly, we close up shop.

Chairman PENCE. Same question to Mr. Burk, and feel free to elaborate.

Mr. BURK. Well, a lot of our customers are outside the top 50 MSAs, although we do have customers in—quite a few in San Antonio, Houston and Dallas, but a large percentage of our customers are outside that area.

And having a significant portion of the lines in those areas not available to us makes it very difficult to market there. We market with a direct sales force and it is hard to tell a salesman you can sell the guy on this side of the street, but not on that side of the street. If a guy has got three dry cleaners, you can say, I can provide service in two of them, but not in the third one it is nonsensical to the customer, and it makes it very difficult to market in those areas.

But from a cost standpoint, our costs are de-averaged, so our costs for UNEs are lowest in those largest markets and highest in those smallest markets. And like the RBOC, the revenues that you get in the largest markets help you to be able to provide service in the smallest markets.

So the net effect of it is that we have had to restrict our marketing into the smallest towns in Texas because of the cloud over our ability to provide service in the largest towns. We do not want to get what I would call exposed by adverse selection in the cost model, because the retail pricing works exactly the opposite. The lowest rates are in the smallest towns, and the highest rates are in the biggest towns.

So it kind of puts you in a bind, and so what I would say is if you wanted to do away with barber shops, you do not have to outlaw barber shops, you just have to tax scissors. And so what hap-

pens here is that marginal difficulties in providing this service impact the overall business model.

As you can see in my experience, I have done resale, and there is not enough margins to sustain that in the competitive business, and I have done facility-based competition. And facility-based competition is a great idea, but it does not work for all customers because it does not have any ubiquity that was spoke of by some of our competitors. Regardless of the size of town, there is no economic model that I have been able to look at, and I have looked at a bunch of them, that says you can provide service to small businesses on your own switch no matter what city you are in if you are providing just analog telephone services, which is what most businesses still need primarily.

Hopefully, we will have a broad-band solution that allows us to provide this service economically on a broad scale, but you need competitors and a market for the technologists to build that equipment for. If the competitors go away, that technology is never coming on line.

Chairman PENCE. Mr. Curtis.

Mr. BURK. Long answer to a short question.

Chairman PENCE. It is a good answer. Thank you.

Mr. CURTIS. Same question?

Chairman PENCE. Please. Would you like me to restate it?

Mr. CURTIS. No. No, thank you.

We would probably focus on the residential market, which we are already in. We would probably either completely rethink our business strategy in most states, again because our product is set and the way we approach a problem really requires ubiquity at the moment.

There are a few states where state legislators appear to have been taking, and state PSCs—have been taking, a lead. Illinois recently passed a wonderful telecom bill which removes the restriction.

As I think Richard had mentioned earlier, Texas, at least until recently, had no restriction. That is a bit in doubt. And while there is some restriction, it is modest in New York. So we could focus on states that are taking a leading role instead of having to depend on the FCC.

But if the FCC restriction stays in place, we would not be able to offer the kinds of services that customers have asked us to provide, and it would dramatically curtail a plan to expand in to the business market.

Chairman PENCE. My question to Mr. Gregori would be how has the delay—specifically the delay in the FCC's decision-making affected your business plans?

Mr. GREGORI. Well, the uncertainty of the decision, which way is it going to go, has a direct impact on the capital markets. There are specialty lenders into our group who understand exactly what the limitations are and are kind of waiting in the wings to determine what is the outcome. Should they continue to support and lend into this sector to help grow the marketplace, or should they kind of curtail now their lending and stand on the sidelines until it is resolved?

It also impacts the amount of dollars we are willing to commit to marketing, and just how fast we could grow the business. We think we deliver a really terrific set of value proposition to our small business customers, both in terms of price and service, and at the end of the day we think we could win provided the restrictions were lifted.

Chairman PENCE. I know we have a vote imminent, and we will adjourn the hearing a few minutes after that call comes.

But let me ask Mr. Curtis for starters, but anyone of the providers can grab at this. What evidence does the FCC have that you are aware of, if any, to demonstrate that small businesses are only those with less than four telephone lines? Can you inform the Chair of the Commission's view of this?

Mr. CURTIS. Be happy to take a swing at it, Mr. Chairman.

First of all, let me say that whatever was the case in 1999, when this rule was imposed, I think most of us can agree that the world is a dramatically different place for telecom providers in the winter of 2001 than it was in 1999.

Let me also say the best evidence I have seen and the most thorough study of what constitutes in the telecom world a small business, and there are differences based on the sort of circuit that one provides, or the number of lines that one would provide, things like that, the best evidence I have seen is in a document filed by the PACE Coalition that argues for 24 lines, which is the digital level. I think that is overwhelmingly the strong evidence in the record, and I would encourage you to take a look at that.

Chairman PENCE. Mr. Burk, same question.

Mr. BURK. Yes, I would agree. As well as belonging to PACE, I have been actively involved in this for quite awhile, and I am unaware of any substantial evidence that supports the three-line restriction.

The one piece of evidence that I would also like to point to that I think we would all agree with, given the state of competition today, I cannot understand the rationale for limiting access to any UNEs anywhere. There is no real basis to do that. I would like to know just exactly where it is that we have too much competition.

Mr. GREGORI. If I could state——

Chairman PENCE. Please.

Mr. GREGORI [continuing]. What I perceive to be the obvious. I have three children. I have an internet line at home, a fax line, and three phone lines. I have already exceeded as an individual the limitations imposed by the FCC for small businesses. I do not think they make any sense in today's world.

Chairman PENCE. Well, judging from the buzzers our time has passed very quickly. I do want to make a formal note that any of the witnesses or any interested parties, that this hearing record will be open for 14 days after the hearing to submit additional remarks, and witnesses and interested parties are encouraged to do so.

I am extremely grateful to the competitive providers and to Mr. May for all of your practical experience in this regard. Though a freshman in Congress, I follow in the footsteps not only of the former Chairman of the Committee on Small Business, Jim Talent, who had a passion and a burden for seeing to it that small busi-

nesses could compete in the regulatory morass that this city tends to create, but also I follow in the footsteps of Congressman David McIntosh, who was Chairman of the Regulatory Reform and Oversight Subcommittee of the House Government Reform and Oversight Committee, and I want to assure you that we are going to proceed with the very simple business of making sure that the Commission is held accountable, that they respond to former Chairman Talent's inquiry, and that we move this process along to the extent that it is within our power to encourage that happening.

Your testimony today has contributed very significantly to my understanding and appreciation of that. It is important that you all know that I am a real believer in the free market. I greatly admire all four of the entrepreneurs that are represented here, having started a small business in my basement 10 years ago, with more than three phone lines. I appreciate what you do, and particularly Mr. Burk, you sharing those heartfelt comments from your customers. I know the value of that to you, it was very meaningful. It was meaningful to me.

But know that in this competitive marketplace, I do not see good guys and bad guys, apart from the government. And what I want to make sure is that the government does not become the bad guy but lives up to the obligations of the law, and you have assisted us in very meaningful ways today to see to it that the FCC does just that.

So thank you very much for being here, and this hearing of the Subcommittee on Regulatory Reform and Oversight stands adjourned.

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

MIKE PENCE, INDIANA
CHAIRMAN

ROBERT BRADY, PENNSYLVANIA
RANKING MEMBER

Congress of the United States
House of Representatives
107th Congress
Committee on Small Business
Subcommittee on Regulatory Reform
and Oversight
2361 Rayburn House Office Building
Washington, DC 20515-6515

Statement of Mike Pence
Chairman
Subcommittee on Regulatory Reform and Oversight
Committee on Small Business
United States House of Representatives
Washington, DC
November 1, 2001.

Five years ago, Telecommunications Act of 1996 was signed into law. When it was enacted, promises from Congressional leaders, the President, and industry was that the legislation would create a revolution in the provision of telecommunications services. A revolution certainly has occurred; an entirely new economy based on the Internet has developed in the past five years. Hundreds of new companies have been formed to break into what was once perceived as an impenetrable monopoly – the local telephone market. Unfettered competition in the telecommunications market and the benefits of lower prices and better services, particularly for small business owners throughout the country, remains a distant goal not a near-term reality.

Some experts believe that the competitive goals of the 1996 Act will not be met without facilities-based competition. There is no doubt that facilities-based competition will play a key role in providing competition to the incumbent local telephone companies. Yet, facilities-based competition is not the only option. As the Supreme Court noted in *AT&T v. Iowa Utilities Board*, the 1996 Act “imposes no such limitation; if anything it suggests the opposite....”

Three of the witnesses are competitors of incumbent local telephone companies that started after the enactment of the 1996 Act. Their business models are based on the fact that facilities-based competition is not mandated by the Act. They will explain how they purchase unbundled network elements that constitute the foundation of local telephone service from incumbent local telephone companies, reassemble those elements along with elements that they provide themselves, and sell that package to provide competitive local telephone service.

A key component of providing local telephone service is access to switching so that telephone calls can be routed properly. In its initial order implementing the 1996 Act, the Commission designated switching as an unbundled network element that incumbents must sell to competitors should they so request it. The Supreme Court determined that the Commission misinterpreted the 1996 Act and forced the agency to develop a new list of unbundled network elements. The Commission did that and determined that incumbents would no longer be required to sell switching as an unbundled network element to competitors who wish to serve customers with more than four telephone lines. The Commission determined that switching service was sufficiently available from sources other than incumbents for all customers except small businesses and residences.

The decision violated the Small Business Act and the Regulatory Flexibility Act as was pointed out in a detailed letter by Jim Talent, the immediate past Chairman of the Small Business Committee. The Commission failed to follow the Small Business Act when it determined that small businesses were only those businesses that have fewer than four telephone lines. Nor did the Commission properly assess the economic impact of the decision on small competitors and whether there were any potential alternatives that might be less burdensome on them.

The telecommunications companies will explain how their businesses are dramatically and adversely affected by the Commission decision and how they have been now waiting for nearly two years to get a decision on the reconsideration of this issue. During the pendency of this proceeding, they have been unable to expand because the rules governing their business plans remain in flux. In turn, this harms the ability of these companies to provide service to many small businesses. More importantly, if the Commission decides to extend its current rules to all areas of the country rather than the central business districts of the 50 largest cities, it could prevent competition from flourishing in many smaller cities, such Muncie and Anderson in my district.

The final witness will explain to us that the needs of a small law firm or any other small business do not necessarily comport with those of larger businesses or residential customers. That conclusion appears to be obvious to everyone but the Commission which historically fails to distinguish between small business and residential customers. The proceeding at issue here simply continues that illogical and unsupported precedent.

The Commission is on notice that this Chairman and this Subcommittee expect the laws of Congress to be obeyed. If the Commission fails the Commissioners can expect that they will be explaining their decision to this Subcommittee.

Let me thank the witnesses for taking time out of their busy schedules and make the trek to Washington, DC. I look forward to their testimony and will now recognize the gentleman from Pennsylvania, Mr. Brady, for any opening remarks he may have.

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WRITTEN TESTIMONY OF
JOSEPH GREGORI
CHIEF EXECUTIVE OFFICER
INFOHIGHWAY COMMUNICATIONS CORPORATION

Before the
Subcommittee on Regulatory Reform and Oversight
Committee on Small Business
U.S. House of Representatives

November 1, 2001



Good Afternoon,

My name is Joseph Gregori and I'm the CEO of a privately held company, InfoHighway Communications Corporation.¹ I'd like to thank the Chairman and members of the Subcommittee for allowing me the opportunity to speak with you today.

Our company is one of many smaller CLECs, although I must point out this group of competitors is shrinking by the day, that provide telecommunications alternatives to the Small Business Community. In fact, our business plan was created and funded to service the Small Business sector. And, of course, we are a Small Business.

The Federal Communications Commission ("FCC") currently has rules in place that limit our ability to serve the small business market, and worse, is considering new rules that could further limit our ability to compete for small businesses. Further limitation will in fact threaten our entire industry's existence as a competitive alternative to the incumbent local telecom monopolies.

Let me give you an overview of our Company. We provide telecommunications services, local, long distance and data offerings primarily in the Northeast, including Massachusetts, New York, which is our corporate headquarters, New Jersey, Pennsylvania, Maryland and Washington, DC. We began operations in 1996 with almost no financing and in September of

InfoHighway Communications Corporation
1333 Broadway, Suite 1001, New York, NY 10018 • (212) 566-2100 • Fax: (212) 566-2136

¹ Neither I nor my company has received any federal grant, contract, or subcontract in the current year or in the preceding two years.



2000, were successful in recapitalizing the Company wherein we raised \$45 million and continued our expansion plan. According to the NYS Public Service Commission Local Competition Report for the year ended December 2000, InfoHighway was the 23rd largest competitive provider in New York, out of over 100 responding companies. Currently we have in excess of 5,000 customers that subscribe to such services as local, long distance, high speed internet access, web hosting, email, data cabling and other products.

Our primary market focus is the small business customer segment -- those customers that traditionally have been underserved that require alternatives and solutions to compete in today's fast paced business environment. Our typical business customer has between 5 and 10 lines for voice service and spends approximately \$300 to \$400 per month on phone service. A typical customer is the local print shop, your neighborhood travel agent, or the doctor's office.

Our strategy has been to bundle together local and long distance voice services while we slowly and deliberately build our own data network to deliver high speed internet access utilizing digital subscriber line technology, also known as DSL. This technology enhances the old copper telephone network to be able to offer newer and faster data services.

Our "smart build" approach allows us to build market share and cash flow while making the necessary long-term investment in building networks. To date, we have invested in excess of \$7 million in network facilities and related equipment.

Another integral part of our approach is our focus on customer service and delivering new value in traditional products that are essential to the success of small businesses. In the



telecommunications sector, we are the equivalent of a small business and we understand as well as anyone the need for cost efficient solutions and customer care.

Our Company does not have the resources to build a ubiquitous voice and data network to compete with Verizon or any other local monopoly on a large scale. Those companies - such as Verizon and SBC - have had more than 100 years to build their networks, most of the time protected from competition by government regulation. The ability to replicate such a network is beyond any company's ability in today's environment. Not only is the capital not available, the obstacles facing competition in the local market are still significant.

We now hear from Verizon that they welcome competition – but only from competitors of their own size, those companies willing and able to duplicate Verizon's network. Of course, no company can duplicate Verizon's network, particularly in the near term. Further, Wall Street and the private equity markets no longer have any appetite for funding business plans that support "Field of Dreams" networks - i.e., "build it and they will come." It is my belief that the 1996 Telecom Act was passed to spur competition and provide for new services, more choice, and enhanced networks coupled with the delivery of new technologies to serve the public. The FCC needs to hear from you and others concerned about the state of, or lack of, competition in the local markets, particularly for the smaller business customer.

We lease facilities from Verizon and utilize Unbundled Network Elements, commonly referred to as UNEs, combining UNEs in what is referred to as the Unbundled Network Element Platform, or UNE-P. These offerings are expressly provided for in the 1996 Act and time and time again, State and Federal regulatory bodies have ruled they must be offered to competitors. The FCC is



currently reviewing its UNE rules with the possible outcome to further restrict their availability. To do so will undoubtedly limit competition, especially in the small business sector, and choke an industry which is already in jeopardy.

Let me share with you the state of competition in New York, which has been showcased as a success story for local competition.

My view on the state of competition in New York is that compared to other states, it is one of the most competitive, if not the most competitive, markets in the nation. However, if you examine the facts and put them together, rather than simply look at individual statistics, you come away with a very different perspective, especially if you consider the huge role of UNEs and UNE-P in the analysis of competition.

The New York State PSC issues a yearly report titled "Analysis of Local Exchange Competition." On the surface, the report looks encouraging, but closer examination, coupled with the current state of our economy, points out that competition clearly is in deep trouble.

As one would expect, Verizon-NY still accounts for most of the local revenues with \$5.1 billion, or 82%, and AT&T ranks number two. Significantly, however, AT&T is a very distant second -- AT&T's comparable revenue for the period is \$168 million, or approximately 2.7% of the total revenues in the market. It is over five years since the 1996 Telecom Act became law and AT&T has less than a 3% share of the New York local telecom market. If a company the size of AT&T with its resources and brand recognition can't obtain more than a 2.7% market share in five and one half years, one must ask why.

InfoHighway[™]

In contrast, this same report indicates that Verizon –NY has now captured 20% of the long distance residential market in the one year since it entered the market. Is Verizon that good at marketing and every other competitor so inept?

Moreover, the New York report indicates the number of local exchange lines served by competitors in 2000 reached 2,946,947, or 20.9% of the market. However, what isn't obvious without review is that three of the largest communications providers in this category are AT&T, MCIWorldcom and Sprint, who collectively account for roughly one-half of all the competitive lines. The report indicates that Sprint has already exited the residential market, and both AT&T and MCIWorldcom have publicly indicated they are considering similar actions if the competitive landscape is not leveled. What does that say about the state of local competition and the hurdles faced by smaller companies?

The exiting of the local residential market in New York by Sprint and others, including the possibility of such by the largest competitors, is likely the precursor of things to come. The same report states, and I quote, "In the first half of 2001, at least 45 telecommunications companies authorized to provide service in New York State filed for Chapter 11 protection."

The irony in all of this is that competition from CLECs in New York has resulted primarily from the use of leased facilities from Verizon. Approximately 81% of the competitive lines in New York use facilities leased from Verizon - and it is precisely this option that the FCC is considering foreclosing.

If there is one point I would leave you with it is this; the state of competition is in jeopardy, and if the FCC limits further the use by competitors of the incumbent telcos' network facilities (i.e. UNEs) it will drastically reduce or effectively eliminate



competition in the local market. In particular jeopardy is competition for the small business customer that has more than three local lines, which is in fact most small businesses.

I implore you to take up this competitive cause and encourage the FCC to expand the availability of UNEs and adopt rules that encourage competition and promote the interests of all businesses, including the small business owners, who more than any other segment, need and will benefit from robust competition.

Respectively submitted,

Joseph Gregori

**WRITTEN TESTIMONY OF
RICHARD BURK
PRESIDENT & CHIEF EXECUTIVE OFFICER
nii communications**

**Before the
Subcommittee on Regulatory Reform and Oversight
Committee on Small Business
U.S. House of Representatives**

November 1, 2001

Good morning Mr. Chairman and members of the Subcommittee. Thank you for the opportunity to speak to you today. My name is Richard Burk. I have a long history of participation in the competitive telecommunications industry. Over the past twenty-three years I have served in many capacities for a wide range of telephone companies. My resume clearly demonstrates that, during this stay, I have endeavored to foster or create the kind of telephone company that is oriented towards its customers' issues. My testimony here today will highlight the importance of the Unbundled Network Element Platform, or UNE-P, in use today by my company and many others as the means of successfully achieving these ideals in the relatively young competitive local exchange market.

I first joined Southwestern Bell in 1978 where I became an Account Executive and Industry Consultant within their marketing organization. There I received training on how to apply telecommunications technology as a solution for any number of business problems. At divestiture in 1983 I recognized a seemingly limitless opportunity to finally bring choice and unique telecommunications solutions to small businesses and small business owners. After all, this was a market whose dynamics had been strictly dictated until then by the sole-source provider.

I joined Value Line of Longview in 1984, a competitive long distance company, where I served as President. There I honed the skills of technical operations, regulatory affairs, accounting and finance, marketing, and many other aspects of operating a competitive small business. As it should be, our business plan called for us to seek out markets and consumers that were

otherwise ignored, thus under-served. We targeted those customers who needed greater value from their communications companies than what they were receiving. Our company became quite successful, and our customer base of contented small businesses profited and grew with us.

From Longview I went on to become Vice President of Operations of American Telco, a Houston-based privately held regional long distance provider offering service across the state. Again, we carved our niche in the competitive long distance market by carefully identifying what long distance customers wanted, and then set out to provide them with it.

In 1996, I once again saw what appeared to be a limitless opportunity to bring solutions to an under-served market. I negotiated the first post-Telecom Act local interconnection agreement with a Bell Company for American Telco. I then became an independent consultant to several other companies that were anxious to enter the local telephone market, but unsure of the intricacies of the new legislation and inexperienced in the technicalities involved in providing local telephone services.

In 1996, I joined USLD Communications, a San Antonio-based long distance provider. As Vice President of Strategic Development, I oversaw the company's pursuit of authority to enter local markets in twenty-two states. We negotiated interconnection agreements with Southwestern Bell, Pacific Bell, US West and NYNEX. We set into motion a two pronged market entry strategy, employing resale as well as a facilities-based approach to providing local service. Many in our industry recognized the opportunity presented by the UNE-P market entry strategy and were

extremely excited about it. The FCC's rules, however, were thwarted by legal challenges and the RBOCs had no intention of voluntarily offering a viable UNE-P product for competitive local service providers.

As of 1998, USLD provided local service to nearly 100,000 access lines across the country on a resale basis. Also under my direction, USLD purchased and implemented a state-of-the-art local switch in its offices in San Antonio, and was in the process of developing a strategy to convert our resale customers to UNE-P when the company was acquired by LCI Communications that year. LCI was then acquired by Qwest who later acquired US West and immediately abandoned their customers in the competitive local exchange market.

After leaving Qwest in 1998, I took my life's savings and started network intelligence, inc., the company known today as nii communications. The concept of providing service to small businesses and small business owners using the Unbundled Network Element Platform (UNE-P) was the most viable option for providing service to this market. I knew from experience that providing resale local service would not support gross margins that were significant enough to price standard services competitively. I also knew that the lack of control over local network elements robbed local resellers of the opportunity to use access revenues from long distance carriers to offset the expense of providing local telephone service, as the incumbent had done for years. Furthermore, control over individual access elements is essential to a CLEC who wishes to customize service for his target market.

However, from my experience at USLD, I was also keenly aware of the expense associated with deploying one's own local switching, as well as the geographic limitations associated with such a strategy. It was clear to me that UNE-P would allow me to compete for local customers anywhere, as long as I was willing to bear the same costs for these underlying elements as the incumbent LEC. Using my own switching I could only compete for large customers in major metropolitan areas.

I am here today as President and CEO of nii communications, a competitive local exchange carrier based in San Antonio, Texas, serving nearly 7,000 small business customers throughout our state in over 250 communities, as small as Floydada and as large as Houston. I am also a founding member of the Promoting Active Competition Everywhere (PACE) Coalition, a policy forum assembly for UNE-P CLECs across the nation. I currently serve as Vice Chairman of CompTel, which I believe is the leading representative association of telecommunications providers in the U.S. For four years I also served as President of TEXALTEL, our state's competitive carrier trade association. I am a survivor. Our company has grown to a twenty million dollar a year self sustaining enterprise by serving our customers, overcoming the obstacles in our path and not spending more money than we could afford.

We negotiated our first interconnection agreement at nii in February 1999, and we billed our first customer only three months later. Since day one, nii's target market has always been the small business man or woman, typically with three or four telephone lines, like insurance offices, delicatessens, auto repair centers, etc. In addition to local telephone service,

we offer bundled packages of long distance, analog internet service, DSL broadband service, web design and web hosting. Our strategy is to become that small business' single source communications provider. Until now we have targeted small businesses in second and third tier markets such as Abilene, Amarillo, Waco and Wichita Falls. We are, in fact, a small business serving small businesses.

Texas has temporarily been shielded from the FCC's current restriction on UNE-P availability due to a provision negotiated between SWBT, local competitors, and the Texas PUC, codified in the "Texas 271 Agreement," or T2A. The T2A is the collaborative interconnection agreement first made available to CLECs by SWBT as a pre-condition of SWBT's approval to enter the long distance market in Texas. In this agreement, SWBT pledged to refrain from imposing the FCC's restriction on the availability of UNE-P for several years. This has allowed UNE-P CLECs to serve small business customers with four or more business lines in these markets, as initially envisioned by Congress in the Telecommunications Act of 1996. However, this provision has lapsed and UNE-P providers in these areas, including nii communications are in jeopardy of losing their right to continue providing service to some of their customers. We are hopeful that the Public Utility Commission of Texas (Texas PUC) will recognize that, with the suspension of the FCC's restriction, Texas has managed to become the second most competitive local telecom market in the country, with more than 1 million lines moving away from the incumbent and to CLECs since January 2000.

Implementation of the federal UNE-P restriction in Texas would put nearly 500,000 small business lines out of practical reach for UNE-P providers. Several of nii's existing customers would be forced off nii's network because they become "over-qualified" under this rule.

Despite the candid example of AT&T, which flourished decidedly as a company while competition took hold in the long distance market in the mid to late 80's, Southwestern Bell is not interested in engendering true local competition. Because of this, the FCC's restriction serves their interest. If nii is required to deploy its own network in order to service small businesses, we would go broke, like many before us. How impractical would it be for the deli shop on our service, with a main voice line, a fax line for catering orders, and a modem line for credit card validations, to be forced back to the RBOC when their success some day requires them to install a fourth line? Doesn't that contradict the spirit of Congress' local competition initiatives? Despite what anyone thinks, there are no other switching alternatives available to a UNE-P provider, even in these top 50 MSAs. To date, no alternate facilities-based CLEC has ever approached nii communications, with its 26,000 switch ports currently under lease from SWBT, with a wholesale solution or alternative to the RBOC. These new facilities-based local carriers thus far have only managed to economically provide service at a T-1 level, and as a consequence the FCC's rule has the effect of severely restricting if not eliminating entirely competition for small businesses with between four to twenty lines.

The RBOCs act as though they fear that customer choice is ultimately not in their best interest - that is why they seek to perpetuate their

stranglehold on their customers, as they have for sixty-seven years. By deploying proprietary networks using monopoly proceeds, by endorsing legislation that would allow them to skirt the open network obligations under the 1996 Telecom Act, through policy strategies aimed at frustrating new competitive providers, the RBOCs act to limit rather than broaden the choices of local telecommunications subscribers. Ironically, the RBOCs disingenuously claim that the UNE-P market entry strategy provides CLECs with an unfair competitive advantage in entering local markets, one that exceeds the designs of the drafters of the Telecommunications Act of 1996. Yet they have never attempted to "take advantage" of UNE-P themselves by adopting the strategy as a means of entering other local markets. Oddly, in fact, GTE had begun to execute such a market entry strategy into other local service areas in Texas, but abruptly cancelled the program when it was acquired by NYNEX/Bell Atlantic. Ameritech gave every appearance of an interest in competitively entering SWBT and other RBOC markets - until it was acquired by SWBT and all such plans came to a halt. Qwest has pulled all of its competitive local service out of Texas, including that which it inherited from USLD. Congress' idea that the behemoths would compete against each other for the customer's business has sadly misfired, as they now focus mainly on shoring up their own possessions.

I have provided copies of letters from twenty-two of our small business customers that state why having a choice is important to them. Several of them mention the fact that because we have saved them money they have been able to add new office equipment, purchase more telecommunications services, and even add a health care plan for their employees. There are also many that expound on how they prefer our

customer service to their previous carrier. The fact that we are saving small business owners money and time is very important, but what every one of these letters is a testament to is that we are offering these customers a choice. I am glad that these customers like us, but if they didn't they at least have the opportunity to do something about it. As Mr. John Timms of Isabelle's European Day Spa, Inc. said , " I 'tip my hat' to whoever has made it possible to finally get out from underneath the 'thumb' of Southwestern Bell."

Thank you for allowing me to address you today on this important small business issue.

**WRITTEN TESTIMONY OF
ROBERT A. CURTIS
PRESIDENT, Z-TEL NETWORK SERVICES, INC.
BEFORE THE SUBCOMMITTEE ON
REGULATORY REFORM AND OVERSIGHT
COMMITTEE ON SMALL BUSINESS
U.S. HOUSE OF REPRESENTATIVES
NOVEMBER 1, 2001**

Thank you, Mr. Chairman, for the opportunity to testify today. My name is Robert Curtis, President of Z-Tel Network Services, and I am here today to discuss a matter of great importance – whether American small businesses will have access to competitive and innovative local telecommunications services that can help them grow their businesses and revive the American economy. In particular, I am here to talk about an FCC rule that, if changed, would allow Z-Tel and companies like us to offer innovative and cost-effective innovative local services to American small businesses, from the flower shop on the Upper West Side of Manhattan to the rancher supply store in Waco, Texas.

Z-Tel is the largest competitive provider of residential local phone service in the nation, with over a quarter of a million subscribers. We are the only phone company in the country that can sell local service in 35 states and to nearly 70% of the homes and businesses in the U.S. In a little over two years, we have achieved over \$300 million in annualized revenues and were recently named the No. 1 company on the “Fast 50 Rising Star List” of technology companies headquartered in Florida. We have invested over

\$100 million to develop advanced, innovative messaging services that allow our subscribers to use their telephone in simple yet powerful ways. Z-Tel wants to and could provide these innovative local services to small businesses in all cities and towns across the United States.

Even before the current economic downturn, this Committee has been appropriately concerned about the ability of small businesses to access cost-effective, powerful and innovative telecommunications services. But in the current economic situation, that access is now a question of survival for many firms. Across the country, small businesses are struggling with reduced margins, increased pressure to cut costs, and an investment climate that directly threatens their survival.¹ Perhaps more than ever, small businesses now need access to new local telecommunications services that will help them realize profitability and growth – services that are simple-to-use, flexible, innovative and cost-effective ways of managing calls from customers, messages, and contact lists.

Z-Tel's local services can do that, but a Federal Communications Commission rule restricts Z-Tel from selling our services in the fifty largest metropolitan areas of the country. If the rule were changed, small businesses nationwide would have access to telecommunications tools that will help them not only cut costs but grow their businesses virtually overnight.

¹ For example, a recent survey by Phoenix Management Services Inc. found that 42% of bankers claimed that the risks of the post-September 11 environment make them less likely to lend to small businesses. "Will Jittery Lenders Dial Back Credit?", *Businessweek Small Biz*, Nov. 5, 2001 at 5. Small businesses are expecting lower sales and optimism has reached not seen since 1993. Naween A. Mangi, "The Aftermath," *Businessweek Small Biz*, Nov. 5, 2001 at 17.

Let me give you a real-world example of how changing the rule would help a particular small business. A local insurance sales agent for a national insurance company could utilize Z-Tel service to direct her telephone to look for her in her office first, then on her cell phone and then at home, without having to provide her clients with three different phone numbers. She will have peace of mind that she will never miss another call from a client or claims agent. She would be able to use her "Z-Line" to call the insurance company and all branch offices long-distance for free. In addition, instead of having to juggle names and addresses in a cellphone, PDA, datebook, or pager, the agent would have a single, Web-based contact list of her customers, underwriters, and claims agents. Her contact list would be so tightly integrated into her local phone service that she could call any of them with the touch of a button and eventually through voice recognition technology. Finally, she could be notified when she has new voice messages via email, cell phone, pager or instant messenger – however she chooses. In short, the insurance agent could handle more claims, more sales, and more contacts than ever before – all without adding staff, overhead, or capital.

But Z-Tel does not sell that product to insurance agents today. Not because we cannot do so technologically or operationally – but because the FCC rule effectively prevents us from selling it to insurance agents located in the top 50 markets. Without the ability to sell this product in the largest cities, Z-Tel cannot achieve sufficient economies of scale to develop and roll out a specialized product for insurance agents outside those cities. If the FCC rule were changed, Z-Tel could provide insurance agents these revolutionary tools that would make their local telephone service an effective tool to drive sales, build customer loyalty, and cut costs.

Mr. Chairman, I appreciate your commitment to local telephone competition, and I am sure you recognize the tremendous benefits these services and innovations could bring small businesses. Small businesses have historically been a bastion of economic growth in the United States. During this time of economic distress, they should have access to as many tools as possible that would help them grow and increase profitability. A cost-effective and innovative local telecommunications service is one of those tools, and there is no legitimate reason to make small businesses wait.

Small Businesses and the Promise of the 1996 Act

In 1996, Congress passed the landmark Telecommunications Act, which established a national policy in favor of competitive entry into all telecommunications markets for all Americans. Many of the members of this Committee voted for that legislation, and all who did so no doubt thought that American small businesses stood to benefit greatly by the development of competition for local phone service.

Indeed, local telecommunications services for small businesses is a large and virtually untapped market. According to industry statistics, businesses purchase over **47 million** analog local dial tone telephone lines, at an average monthly rate of \$75-100/month per line. That represents a market opportunity of **\$40-55 billion per year**.

But simply because a market is big does not mean that it is easy to serve. To provide local telecommunications service to small businesses, a provider must be able to: (1) sell an attractive and cost-effective product; (2) install service quickly and reliably, without any hiccups, delays, or loss of dial tone; (3) provide comprehensive customer service; and (4) efficiently meet the ever-changing demands of small businesses.

Before Congress passed the 1996 Act, the only companies that could meet those demands cost-effectively were the local telephone monopolies. These incumbents own and control pervasive and ubiquitous local networks that reach into virtually every home and business nationwide. The incumbents owe this dominant market position to 60-plus years of state-sanctioned and guaranteed local monopolies. Before the 1996 Act, small businesses were virtually at the mercy of the local telephone companies.

The 1996 Act was designed to jump-start competition for small businesses and all other consumers. In particular, the 1996 Act required that the phone companies provide shared – or “unbundled” – access to their local networks to new, competitive service providers. By providing new competitors access to these pervasive and ubiquitous local networks, new competitors like Z-Tel would be able to develop the economies of scale and scope necessary to develop new applications and services and to compete with the incumbent phone companies for residential and small business customers.

The unbundling policies of the 1996 Act were based on innovative regulatory actions already taken by several state public utility commissions, such as Illinois, New York and Michigan. Prior to the Act, those states and others had made great strides in establishing unbundling policies that favored local entry into those states.

Without unbundling, the task of entering the local market to serve mass-market consumers would be well-nigh impossible. From every business and home in America, a copper wire runs back to the local telephone company office – and there are millions of miles of these copper cables across the country. The 1996 Act makes those wires available for lease to entrants as “unbundled local loops.” Each of these wires runs to one of thousands of incumbent switches, each of which are interconnected in an immense

and redundant switching fabric. Unbundling permits a new entrant to lease capacity on those switches in order to serve a particular customer – what is called “unbundled local switching.” Without unbundled access, consumers and small businesses would have to wait years for competitors to string brand new telephone wires on poles, build their own central offices and switches, and build all the accompanying back-office systems before new, competitive services would be made available. At best, competition would exist in a piecemeal fashion for high-revenue business customers. At worst, competition would not happen at all, because competitors would not be able to compete against the pervasive monopoly network with a patchwork quilt of smaller, less-robust networks.

Unbundling policy gives new companies the ability to share the economies of scale and scope that the local phone companies built up during over decades of state-sanctioned monopoly status. Unbundling truly places the customer first, because it allows new entrants to gain market share and provide innovative services to customers immediately. In the current economic climate and its devastating impact on many small businesses, small businesses need access to these innovative products now more than ever before.

And Z-Tel is prepared to deliver those services – today.

About Z-Tel and Z-Tel's Innovative Services

Z-Tel was founded after the 1996 Act was passed. Initially, Z-Tel was a software company that was focused on bringing the power of the Internet to your home telephone. The 1996 Act offered us the opportunity to deploy this truly revolutionary service to individuals and small businesses.

In particular, the unbundling policy of the 1996 Act meant that we could develop advanced software applications and sell those services *without* having to replicate the Public Switched Telephone Network. And because the 1996 Act applied nationwide, we were confident that when we developed these applications, we would be able to sell them nationwide, to all mass market, residential and small business consumers.

So, in addition to developing our innovative applications, Z-Tel quickly began the process of becoming a competitive local phone company nationwide. We chose as our market entry method a combination of unbundled network elements known as the “unbundled network element platform,” or “the Platform.” The Platform provides the ability for a new company like Z-Tel to offer and sell a local dial tone service to *any* subscriber in a state – once we have entered a state, the availability of our service is not simply limited to large cities or towns.

Z-Tel launched our innovative service in summer 1998 in New York - the first state where the incumbent had implemented the Platform. In November 1999, the FCC ordered that the local telephone companies implement the unbundled network element platform nationwide, subject to one very important restriction discussed below.

In a little over two years, we have gone from a company with miniscule revenues to one with an annual run-rate of over \$300 million, making us one of the fastest growing companies in the history of the telecommunications industry. Today, we can offer service to over 87% of the lines owned and controlled by the Bell Companies.

Z-Tel’s residential service, called Z-LineHOME, offers a bundle of local dial tone, long-distance services, enhanced voice mail and Web-based communications features. For approximately \$50/month, consumers can enjoy the benefits of an all-

inclusive product that provides features like prioritized call forwarding, caller ID, three-way calling, and integrated messaging. Customers can access messages in a number of methods. For example, they can access voice mail through the Web or messages through a wireless pager or e-mail. Z-Tel also offers a lower-cost alternative for individuals that do not want all or only some of these features.

Z-Tel is also developing new ways to use the telephone. For example, we have launched a community voice portal service that gives organizations the ability to communicate effectively and efficiently with their distributed members. In Tampa, Florida, the YMCA and its members can utilize Z-Tel's technology to distribute information instantly about planned meetings, classes, or opportunities. For example, a parent can immediately find out if his son's basketball practice is cancelled. The YMCA does not have to try and reach all of the parents on the team. The parent can direct his Z-Line to inform him of the cancelled practice however the parent wants – by an e-mail, page, voice mail, or text message.

These advances in communications technology for consumers are exactly what Congress envisioned when it passed the Telecommunications Act of 1996.

The tragic events of September 11 have demonstrated the benefits and reliability of Z-Tel's services. New York is our largest market, and our customers there were able to utilize our messaging features to communicate with their loved ones and friends during the crisis. Our subscribers were able to use the Internet to retrieve voice mail messages or direct those messages or calls to their pager, PDA or wireless phone. In seconds, customers could access their address books and send and retrieve messages; these customers did not have to struggle through a multi-hour commute to reach their address

books. And since our customer's contact and messaging information is stored in a Z-Node hundreds of miles away, it remained as accessible and useful as the day before the attacks. That redundancy is crucial, especially for those customers that may still not be able to return home or report to work.

The Restriction on the Platform and its Impact on Small Businesses

Imagine what a small business could do with Z-Tel's technology. With only one call or text message, a plumber could inform all of his customers on that day's route about the fact that he is stuck in traffic and will be delayed an hour. A pharmaceutical sales agent could maintain one comprehensive address book, accessible through the Web, that would allow her to track incoming and outgoing calls and messages without having to juggle a day-planner, telephone, PDA and pager. A dentist could efficiently and automatically remind customers of upcoming appointments. A sales manager could inform his or her entire outside sales force of a product enhancement or staff meeting with one single call. All of this could be done while lowering operating costs and increasing efficiency.

But small businesses today generally do not have access to Z-Tel's applications. FCC Rule 51.319(c)(2) (47 C.F.R. 51.319(c)(2)) expressly limits our ability to utilize the Platform to serve certain small business customers in the Top 50 metropolitan statistical areas. In particular, the FCC rule prevents our access to "unbundled local switching" – a constituent and critical part of the unbundled network element platform combination of elements – in the most commercially dense portions of the Top 50 MSAs to customers that have more than three telephone lines. Without access to unbundled local switching,

Z-Tel cannot utilize the Platform combination of elements to deliver our services to our customers. Without a doubt, **if this FCC policy were changed, small businesses would have near-immediate access to innovative and cost-effective services like Z-Tel's.**

Given your position, Mr. Chairman, I am sure you speak with small businessmen frequently. The next time you are meeting with a group of them, please ask them how many of them have only three telephone lines in their office. Only a minority – if any – will raise their hands. And then ask them whether they would realistically consider buying telephone service from a company that could only provide them three telephone lines.

The idea that *any* small business believes that it will always require, for the foreseeable future, only three telephone lines is laughable and almost not worth debating. And a policy that expects a company like Z-Tel can profitably provide a service that requires us to disconnect service or move that customer to another network provider once that customer wants a fourth line is unrealistic. Yet the rule stands.

The theory behind the FCC's restriction is that for some "larger" small businesses – those with more than three lines – Z-Tel should offer its services not through the Platform but by building a new, multimillion voice network switch. As a result, the rule takes away our immediate ability to utilize the Platform to serve many small businesses. In essence, Z-Tel is denied the ability to serve these small businesses on the basis of an industrial policy, *circa* 1999, that we should instead build a particular type of telecommunications network in a particular way that has been shown only to be useful and cost-effective to serve large customers.

This industrial policy has a significant impact on how Z-Tel does business. Since our inception, Z-Tel has tried to offer local service on a *national* basis to these mass-market consumers. To make that business case work, and to achieve the required economies of scale, we need to have a uniform method of providing our services to customers. We cannot profitably juggle one method of entry in some neighborhoods against a different method of entry in other neighborhoods. On the other side, we cannot engage in a mass marketing campaign that is just targeted at a certain, small component of potential small business consumers.

Imagine if the Food and Drug Administration implemented a rule that required McDonald's to hand-churn cheese sold in all their restaurants in Downtown Milwaukee. Say the FDA decided that this rule was in the public interest because there was ample supply of dairy products in Wisconsin so that there would be no need to import pre-processed cheese. What do you think McDonald's reaction would be – would it churn the cheese by hand? Would it stop selling cheeseburgers in Milwaukee? Or would it simply close all of its restaurants in the affected zone?

In the wake of this substantial reduction in our potential market, Z-Tel and other Platform entrants were faced with a similar decision. While our applications are extremely well suited for small businesses, Z-Tel initially decided not to roll out a small business product at all. We decided we could not identify enough small businesses with less than three lines in the Top 50 MSAs to make selling that service in those large cities worthwhile.

And without the ability to sell a service in the Top 50 markets – which account for over 88% of the U.S. population, – companies like Z-Tel did not provide small business

everywhere – even those beyond the large cities targeted by the FCC – innovative and cost-effective services.

As I mentioned above, small businesses need access to cost-effective telecommunications tools now more than ever. Z-Tel stands ready and willing to provide these services to small businesses, and we are now beginning to deploy some forms of small business services in areas where the legal right to enter by means of the Platform has been secured.

Most notably, Z-Tel recently launched its small business product in Illinois. This summer, the Illinois General Assembly passed a state law that provides unrestricted access to the unbundled network element platform. In doing so, Illinois re-asserted its position as a leader in developing pro-competitive telecommunications policy. Small businesses all across Illinois now have another tool to grow their business and cut costs.

Z-Tel expects to move forward on a state-by-state basis with this product, focusing on states and regions like Illinois where state policymakers have recognized the benefits of the Platform method of entry. Small businesses in these states stand to benefit greatly by increased access to new, innovative local services.

But even the most optimistic state-by-state process sacrifices critical economies of scale necessary for more advanced services. More importantly, this state-by-state process requires many small businesses to wait. The FCC policy needs to change.

Availability of the Platform Promotes Competitive Entry at All Levels

As discussed above, many states took the lead in promoting competitive entry prior to the 1996 Act, and several states such as Illinois have recently acted to bring

competition to the mass market despite the FCC restriction. In addition, state commissions in New York and Texas have adopted policies that encourage the use of the Platform. According to FCC statistics, consumers in the two latter states now enjoy considerably **more** competitive entry than most other states.²

A recent FCC Local Telephone Competition Report found that competitive entrants provided service to 20% of the lines in New York State – and that the majority of those lines were provided to residential and small business consumers. In Texas, entrants had garnered 12% of the market – again, the majority to residential and small business customers. Both figures are substantially in excess of the national average for competitive entry. And these levels of penetration would not have been possible without the availability of the Platform and state commission policies in favor of Platform entry.

Critics of the unbundled network element platform form of entry focus in on the availability of one particular unbundled network element that is a part of the Platform combination – unbundled local switching. These critics argue that requiring incumbent telephone companies to lease access to their local switches provides a disincentive for new entrants to spend millions of dollars deploying their own switches. This argument fails in several respects.

First, the availability of unbundled local switching does not appear to have any adverse impact on deployment of new switches by competitors. Z-Tel recently analyzed the total level of CLEC switch deployment in the Verizon region and found that there are actually **more new CLEC switches** (on a per-capita basis) in markets where the FCC's restriction does not apply than in markets where the restriction does apply. As a result, if

² Federal Communications Commission, Common Carrier Bureau, Industry Analysis Division, *Local Telephone Competition: Status as of December 31, 2000*, Table 6 (May 2001).

the purpose of the rule is put in place an environment in which carriers purchase and deploy advanced, digital switches, that goal would actually be better served by repealing the restriction than in maintaining it.

Second, the argument of these critics assumes that it is a simple matter to offer competitive service to over 160 million telephone lines nationwide by deploying new switches. Building pervasive switching capacity and operational capabilities to support a robust competitive environment for all of these 160 million telephone lines is, frankly, not possible any time soon. Critics have simply not shown that capacity and infrastructure are anywhere close to the mechanized and cost-effective provisioning levels needed to support competitive entry at this scale.

Regrettably, small businesses are the unwitting victims of the FCC's industrial policy. Because the FCC rule requires entrants to serve certain small businesses by a different form of network deployment than how we serve others, many small businesses do not now have access to innovative and cost-effective services. There is simply no valid public policy reason as to why an auto dealer in urban Detroit cannot benefit from the same innovative local telecommunications services that a hardware store in Traverse City uses to grow its business.

Conclusion

In summary, I would like to thank you, Mr. Chairman, and the Committee for your dedication to local telecom competition and your consideration of this matter. New companies like Z-Tel want to and can offer innovative and cost-effective telecommunications solutions to the nation's small businesses.

I am proud of what Z-Tel has accomplished in a little over two years. Hundreds of thousands of residential subscribers now enjoy our easy-to-use services, and small businesses are asking for a comparable small business product. But the three-line restriction and other efforts to derail the Platform stand in our way.

Small businesses constitute an important and sizeable portion of the American economy. Our research indicates that a typical small business could potentially save over 30% per month by subscribing to Z-Tel's service. At a time when policymakers are searching for ways to jump-start and grow the economy, imagine what economic stimulus would result if all small businesses cut their local telecom costs by that 30%.

But current federal policy is forcing many small businesses to wait for these benefits. This policy is based on an industrial policy that companies like Z-Tel should provide service to small businesses with more than three telephone lines only after we spend millions of dollars constructing a new telecom network. Not only is this FCC policy inconsistent with the purpose of unbundling, but it also puts small businesses in the middle. While applications are written the services can be speedily available, small businesses must wait for these new features for reasons unrelated to their day-to-day struggle to stay in business during the current economic downturn.

It is as if the FCC forcing small businessmen to take castor oil – with the unspecific promise that their immediate telecommunications needs will “get better” in the future.

To fulfill the true promise of competition – one that will benefit *all* mass-market consumers, both residential and small businesses alike – policymakers must constantly

re-examine the real world consequences of their decisions. This FCC policy needs to be re-examined and changed.

I thank you for your attention and would welcome any further questions.

WRITTEN TESTIMONY OF

LAURENCE MAY

PARTNER

ANGEL & FRANKEL, P.C.

Before the
Subcommittee on Regulatory Reform and Oversight
Committee on Small Business
U.S. House of Representatives
November 1, 2001

Good afternoon.

My name is Laurence May and I am a partner at the law firm of Angel & Frankel P.C.¹ On behalf of my firm, I'd like to thank the Chairman and all the members of the Subcommittee for permitting me to address you this afternoon.

Our firm is a small business operating in New York City. We employ approximately 20 people, including attorneys, and I am one of 4 partners. Our local telephone service, through 16 or 17 local business lines, and our high-speed Internet access and e-mail, are now provided by InfoHighway Communications. When our long distance contract expires next month, we anticipate transferring that service to InfoHighway as well. InfoHighway also provides us with additional services, such as calling cards, at very favorable rates, which had not been offered to us by larger carriers.

¹ Neither I nor my law firm has received any federal grant, contract, or subcontract in the current year or in the preceding two years.

As a small law firm with a sophisticated practice in the area of business reorganization and debtor and creditor rights, we compete with much larger law firms. We are forced to pay close attention to the price and service levels we give to our clients and we look for the same attributes in our vendors. Prior to InfoHighway, our local telephone service had always been provided by Verizon, or one of its pre-merger predecessors. We did not find them particularly responsive to our needs and our experiences with them suggested that our account was of insufficient size to be of importance to them.

When InfoHighway Communications approached us to provide local service, it took the time to understand our business, and importantly, how we could control our costs. It took the time to prepare a detailed cost analysis for us and offered several suggestions on how to save money. Further, it alerted us to the fact that we were paying for services we never used and that in one respect we were paying two carriers to provide access to the same

service. In fact, when we learned more about and experienced first-hand the high level of service it provided, we decided to consolidate our existing data services with InfoHighway. This resulted in further cost savings. I have no recollection of a Verizon representative ever calling on us to discuss our account or suggesting ways to better manage costs. We did not think we had a viable choice in local service until we met InfoHighway and we are pleased that it is around to offer an alternative.

InfoHighway Communications has brought us choice in local service and just as importantly, it has helped us to lower our costs.

We like dealing with one representative telecom vendor who can handle all of our requirements. Small businesses need and want full service telecom vendors. We do not have the resources or staff to deal with the telecommunications issues arising out of arrangements with multiple vendors. As a small firm, with less economic influence than larger firms, it is important that we have

vendors who help us compete in the legal marketplace. When we have questions or when there is a service problem, we have found InfoHighway's response to be the best of any telecom provider. It is a good feeling when you know your vendor cares and is working hard for your business.

InfoHighway Communications has offered us a better alternative at a better value than other providers. Let me give you an example. On our local calling plan our line fees are less than Verizon's and we pay only for the minutes we use. Our prior Verizon calling plan incorporated a three minute minimum for every call.

InfoHighway's calling plan charges us only by the minute. For a law firm which has thousands of calls annually which are of less than three minutes duration, the difference can be considerable. Also, regional calls with InfoHighway are priced more affordably than Verizon. So, there are three ways we are saving money; (1) on

line fees, (2) paying only for minutes we use, and (3) saving on regional calls. Very soon we will save more money when we have InfoHighway provide our long distance service as well.

With InfoHighway, we, like larger businesses, have a choice as to local phone service providers. But it is important to us that InfoHighway can also provide us with high-speed data services through its DSL lines. As you may or may not be aware, the United States Bankruptcy Court for the Southern District of New York is a pioneer in the electronic filing of documents. Much of our practice is in that Court and it is critical that we have access to reliable and reasonably priced high speed data services so that we can file and retrieve documents and keep apprised of developments in cases in which we are involved. InfoHighway has admirably addressed our needs in this area.

I don't claim to understand all of the underlying issues before you, but I do know that as a small business, we believe having a

choice for our local phone service is important. I encourage you to take the necessary action to be sure that there is more, not less, competition in the market in the future. There should be more companies like InfoHighway Communications serving the needs of the small business community.

Thank you.



October 31, 2001

House Subcommittee on Regulatory Reform Oversight
of the Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515-6515

Dear Chairman Manzullo, Congresswoman Velazquez
and members of the Committee on Small Business:

The Association for Local Telecommunications Services ("ALTS") submits the following letter to the House Committee on Small Business in connection with its subcommittee hearing November 1, 2001 on Small Business Access to Competitive Telecommunications Services. ALTS requests that this letter be submitted as part of the formal record of this proceeding.

ALTS is a national industry trade association that represents competitive local exchange carriers (CLECs) that provide local voice and broadband telecommunications services to businesses and residential customers. Many ALTS companies have built their business plans to serve primarily small business customers – a customer base that was largely ignored until competitive companies began serving them after the passage of the 1996 Telecommunications Act.

ALTS understands that the primary focus of this hearing is to investigate the extent to which the FCC may have run afoul of its obligations, pursuant to the Regulatory Flexibility Act, the Small Business Act, and section 257 of the Communications Act, in adequately analyzing the impact on small business entities in its *UNE Remand Order*.¹ In particular, the issue being addressed is whether the Regulatory Flexibility Analysis included in the FCC's order properly explored the impact on small businesses of the FCC's unbundling rules setting forth the circumstances under which competitive telecommunications carriers would have access to unbundled local switching.

In the FCC's *UNE Remand Order*, the FCC determined, in relevant part, that CLECs without access to unbundled local switching are not impaired in their ability to serve customers with four or more lines in the most densely populated zones in the top 50 metropolitan statistical areas ("MSAs") where the incumbent local exchange carrier ("ILEC") provides nondiscriminatory access to the enhanced extended link (or "EEL"). ALTS believes the FCC did not run afoul of the Regulatory Flexibility Act or the Small Business Act in adopting its decision to limit competitor access to unbundled local switching. In fact, as the record indicates, carriers have almost complete access to unbundled local switching except in very limited environments where consumers have access to carriers with competitive switching facilities.

¹ *Local Competition Provisions of the Telecommunications Act of 1996*, 15 FCC Rcd 3696 (1999) ("*UNE Remand Order*").



The Regulatory Flexibility Act and the Small Business Act were designed to protect against unnecessary, onerous regulation of small business entities. The *UNE Remand Order* only implements the provisions of section 251(c) of the Communications Act. This provision requires the FCC to promulgate rules to ensure that competitive carriers are afforded nondiscriminatory access to incumbent networks. The FCC prepared an exhaustive Regulatory Flexibility Analysis to assess the impact of its rules on every potentially affected small business entity. ALTS believes that the FCC appropriately addressed its obligations to ensure that small businesses are not adversely affected, and ALTS believes, as the FCC determined, that no small business would be adversely affected by its rules implementing section 251(c)(3) and 251(d)(2) of the Telecommunications Act.

The rules implementing section 251(c), as set forth in the *UNE Remand Order*, including the rule limiting available of unbundled local switching, impose regulatory obligations only on large ILECs, the carriers that control the essential bottleneck facilities. None of these carriers satisfy the definition of a small business entity. In fact, these are among the largest, most powerful companies in the nation. The FCC's implementing rules impose no regulatory obligations on competitive carriers of any size or on any small business customers. These parties are the beneficiaries of the FCC's unbundling rules, including the FCC rule to unbundle local switching. In fact, the FCC seems to have made painstaking efforts to ensure that carriers serving residential and small business customers outside the top 50 MSAs, would have unrestricted access to unbundled local switching, where competitors have not yet been able to deploy competitive switching facilities. Only in the most densely populated, business customer orientated markets is access to local switching slightly limited. In these markets, competitive carriers have deployed competitive switching facilities. Furthermore, the rules do not adversely affect small rural incumbent carriers, exempted from many of the unbundling obligations to which larger ILECs are subject.

It is important to note that ALTS represents the carriers that depend on access to ILEC networks. We believe there is a qualitative difference between access to unbundled local switching, which does not require significant capital expenditures and major construction, and access to the transmission facilities, which were built over the past 100 years through guaranteed monopoly profits. No competitor could replicate the millions of miles of network transmission facilities. Access to these transmission facilities as well as timely and cost effective access to incumbent offices for access to these facilities and for interconnection are still absolutely essential to foster competition in local telecommunications markets.

ALTS is already on record in support of the FCC's decision to unbundle local switching as set forth in the *UNE Remand Order*. The balance struck by the FCC was adequately supported by the evidence in the record and is based on sound policy grounds. ALTS believes it is important for the FCC to foster facilities-based competition, and the current FCC rules accurately reflect the reality that competitive carriers are deploying switching facilities in the top 50 markets. The record is clear that new entrants can and do efficiently enter the local market in large MSAs to serve business customers of all sizes using self-provisioned switches. If the FCC were to impose unnecessary regulation on the wholesale switching market it would only distort market outcomes and it could discourage further switch deployment.



ALTS members have been attempting to bring facilities-based competition to local market sectors by deploying their own facilities to the fullest extent possible. Obviously, CLECs cannot replicate the ILEC network overnight. Therefore, CLECs must rely, to some extent (but hopefully to an increasingly smaller extent over time), on some of the piece-parts of the ILECs' networks until it is economically viable to deploy additional facilities of their own. Facilities-based CLECs have endeavored to deploy, at a minimum, their own switches, and are, more and more, deploying their own transport and loop plant facilities.

In the *UNE Remand Order*, the FCC considered a number of factors in its examination of the supply of local switching from non-incumbent LEC sources. The FCC considered the number and location of competitive switches and the ability of competitive LECs to serve discrete market segments, such as residential customers, using self-provisioned or third-party switches.² The FCC found that "a significant number of competitive switches" had been deployed in the top 50 MSAs.³

The FCC held that incumbent LECs need not provide unbundled switching in the top 50 MSAs, subject to certain qualifications. Those qualifications were designed to ensure that this "exception" to the Commission's unbundling rules would be appropriately tailored to ensure that competitive carriers would have access to unbundled local switching where necessary and to ensure that small business customers would have access to a multiplicity of competitive carriers. First, the Commission limited the exception to only the densest calling zones within the top 50 MSAs.⁴ Second, to promote competition for the residential market, the Commission limited the exception to customers with four or more lines.⁵ Finally, to qualify for the exception, the Commission required incumbent LECs to provide competitors nondiscriminatory access to the EEL.⁶ The Commission reasoned that the EEL would allow competitive carriers to decrease their collocation costs and increase their efficiencies by transporting aggregated loops to their central switching facilities, thus eliminating an impairment that might otherwise result from the Commission's exception to the unbundled switching rules.⁷

The FCC ruling relieved ILECs of their obligation to provide unbundled local switching in at least some of the areas in which there is evidence that competitors are able to economically self-provision switches, thereby furthering one of the primary goals of the 1996 Act -- facilities-based competition. At the same time, it encouraged new investment by facilities-based

² See *UNE Remand Order* ¶¶ 276-299.

³ *Id.* ¶ 281.

⁴ *Id.* ¶¶ 284-285.

⁵ *Id.* ¶¶ 290-298.

⁶ *Id.* ¶¶ 288-289.

⁷ *Id.* ¶ 288.

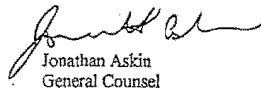


competitors, thus sending efficient entry signals to the marketplace and allowing for increased innovation. Nor did the Commission's ruling harm residential competition, as ILECs must continue to provide access to unbundled switching for "virtually all residential customers."⁸

ALTS has stressed to the FCC that its resources would be better expended on efforts to ensure that the other wholesale inputs necessary for provisioning local telecommunications services are available on terms and conditions that allow switch-based entry to expand beyond the most densely populated areas. It is critical that the ILECs abide by the FCC requirements to provision necessary network elements, such as loops and transport, to the extent that CLECs cannot readily replicate and deploy these elements on their own. In addition, as provided for under the FCC's rules, collocation must be available on a reasonable basis and ILECs must provision the EEL in a manner that allows CLECs to compete. In this way, CLECs can, over time, assemble more and more of the components necessary to deploy their own stand-alone networks, and cease to rely on the ILEC network. Through these efforts, the competitive alternatives for services, technologies and providers will continue to increase.

ALTS thanks the committee for holding this hearing and for allowing our comments to be submitted as a part of the record.

Sincerely,



Jonathan Askin
General Counsel

⁸ *Id.* ¶ 293.