COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

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APPLICATION OF

VERIZON VIRGINIA INC.
AND VERIZON SOUTH INC.

CASE NO. PUC-2007-00008

For a Determination that Retail
Services are Competitive and
Deregulating and Detariffing of the Same

ORDER ON APPLICATION

On January 17, 2007, Verizon Virginia Inc. ("Verizon Virginia") and Verizon South Inc. ("Verizon South") (collectively, "Verizon" or "Company") filed an application with the State Corporation Commission ("Commission") requesting "that the Commission, pursuant to 5 VAC 5-20-80(A) and Va. Code § 56-235.5(E), declare certain retail services competitive and deregulate and detariff those services" ("Application").[1] Exhibit VA-1 to the Application "lists these retail services, which are generally classified in Verizon's Alternative Regulat[ory] Plan as [Basic Local Exchange Telephone Services ('BLETS'), Other Local Exchange Telephone Services ('OLETS')], and Bundled Services. Verizon does not seek to have its switched access, special access, E911 or Lifeline[2] services declared competitive."[3]

Verizon states that the "retail telecommunications market in Virginia is robustly competitive. Intermodal technologies now offer multiple physical connections to the customer, in turn enabling a variety of competing telecommunications platforms, including cable telephony, cable modem, wireless, fixed wireless, traditional [competitive local exchange carrier

[1] Application at 1.

[2] Verizon refers to this service in its tariff as the Virginia Universal Service Plan.

[3] Application at 1 (footnote added).

('CLEC')] broadband, traditional CLEC telephony, Verizon broadband, and broadband over powerline, over which dozens of competitive providers vie to meet Virginians' communications needs."[4] The Company concludes that its "retail services are competitive statewide," and that "competition or the potential for competition in the marketplace is or can be an effective regulator of the price of Verizon's retail services."[5]

In addition, the Company asserts that "[g]iven the pervasive and effective competition Verizon faces for its retail voice services across the Commonwealth, the Commission should not stop at reclassifying those services as competitive. It should exercise the further discretion the Code grants to deregulate and detariff those services."[6] Verizon states that "[o]nce the Commission determines in this case that services are competitive under Va. Code § 56-235.5(F), (*i.e.*, 'when it finds competition or the potential for competition in the market place is or can be an effective regulator of the price of those services'), regulatory mechanisms intended to approximate market forces are no longer required."[7] The Company further contends that, "[i]ndeed, in a competitive market, regulations developed under a monopoly regime can hinder a company's ability to provide adequate service at reasonable and just rates by preventing it from responding to changes in the marketplace as rapidly as its competitors."[8]

On February 7, 2007, the Commission issued an Order for Notice and Hearing that, among other things: (1) established a procedural schedule for this case; (2) permitted any person to submit written or electronic comments on the Application on or before April 20, 2007;

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[4] *Id.*

[5] *Id.* at 7-8 (typeface and case modified).

[6] *Id.* at 17.

[7] *Id.* at 18.

[8] *Id.*

(3) scheduled a public hearing to commence on July 23, 2007 to receive testimony from members of the public and evidence on the Application; and (4) required the Company to provide notice of its Application. The Commission also requested participants to address the following nine questions, noted that this case is not necessarily limited to these questions, and provided Verizon an opportunity to supplement its Application in response to these questions:

> (1) The Commission may determine that telephone services are competitive "on a statewide or a more limited geographic basis," or "on the basis of a category of customers." What is the appropriate market(s) for the Commission to consider in determining whether Verizon's retail services are competitive?
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> (2) What market test(s), if any, should be used to determine that (a) competition, or (b) the potential for competition, in the appropriate market "is or can be an effective regulator of the price of those services?"
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> (3) What constitutes an effective competitor in the relevant market, such that the competitor's presence reasonably meets the needs of consumers pursuant to § 56-235.5 F of the Code of Virginia ("Code")?
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> (4) In determining whether competition or the potential for competition effectively regulates the prices of services, what "other factors," if any, should the Commission consider to be relevant in addition to "(i) the ease of market entry," and "(ii) the presence of other providers reasonably meeting the needs of consumers?"
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> (5) If and where the Commission finds telephone services to be competitive, should the Commission deregulate, detariff, or adopt a modified form of regulation for those services pursuant to § 56-235.5 E of the Code? What factors should the Commission consider in determining which methods are in the public interest for such competitive services?
>
> (6) How should the Commission monitor, pursuant to § 56-235.5 G of the Code, the competitiveness of any telephone services it finds to be competitive?

(7) For any telephone services it finds to be competitive, what competitive safeguards should the Commission adopt pursuant to § 56-235.5 H of the Code?

(8) Are any of the above questions not relevant to the legal and/or factual determinations that the statute requires the Commission to make?

(9) Are there other issues that are relevant to the Commission's implementation of the applicable statutory criteria in this proceeding?

On or before April 20, 2007, the Commission received numerous written or electronic comments from individuals and from the Board of Supervisors of Tazewell County, Cavalier Telephone, LLC ("Cavalier"), Communications Workers of America ("CWA"), NTELOS Companies ("NTELOS"), and the Town of Bluefield, Virginia. The Commission also received numerous comments subsequent to April 20, 2007.

Verizon, the Commission's Staff ("Staff"), and the following respondents submitted pre-filed testimony in this case: Board of Supervisors of Fairfax County ("Fairfax County"); United States Department of Defense and all other Federal Executive Agencies ("DOD/FEA"); Cox Virginia Telcom, Inc. ("Cox Telcom"); Cavalier; XO Virginia, LLC ("XO"); Sprint Communications Company of Virginia, Inc., Sprint Spectrum, LP, Sprint Com, Inc., Nextel Communications of the Mid-Atlantic, Inc., and NPCR, Inc., doing business as Nextel Partners (collectively, "Sprint Nextel"); CWA; and the Division of Consumer Counsel, Office of the Attorney General ("Attorney General"). Verizon submitted pre-filed rebuttal testimony, and an errata thereto, on July 16 and 25, 2007, respectively.

The public evidentiary hearing was held on July 23-27 and August 6-7, 2007. Lydia R. Pulley, Esquire, Jennifer L. McClellan, Esquire, Joseph M. Ruggiero, Esquire, Ann Marie Whittemore, Esquire, Scott Angstreich, Esquire, and David Hill, Esquire, appeared on behalf of

Verizon. Douglas C. Nelson, Esquire, and David E. Anderson, Esquire, appeared on behalf of Sprint Nextel. E. Ford Stephens, Esquire, and Cliona Mary Robb, Esquire, appeared on behalf of Cox Telcom. Joseph Creed Kelly, Esquire, appeared on behalf of CWA. T. Scott Thompson, Esquire, K.C. Halm, Esquire, and Brian A. Nixon, Esquire, appeared on behalf of XO. Stephen T. Perkins, Esquire, Frances McComb, Esquire, Troy Savenko, Esquire, and Noah Bason, Esquire, appeared on behalf of Cavalier. Peter Q. Nyce, Jr., Esquire, appeared on behalf of DOD/FEA. Dennis R. Bates, Esquire, appeared on behalf of Fairfax County. C. Meade Browder, Jr., Esquire, Ashley Beuttel Macko, Esquire, and Kiva Bland Pierce, Esquire, appeared on behalf of the Attorney General. Robert M. Gillespie, Esquire, and Raymond L. Doggett, Jr., Esquire, appeared on behalf of the Staff.

The following public witnesses testified at the hearing: Douglas Henigin, of Henrico County; Heyward C. Thompson, of Buchanan; Claude W. Reeson, of Surry County and representing the Surry County Chamber of Commerce; George Hunnicutt, of Wise County; and Irene Leech, of Elliston.

The following witnesses testified for Verizon: Robert W. Woltz, Jr.; William M. Newman; Harold E. West; Jeffrey A. Eisenach, Ph.D.; William E. Taylor, Ph.D.; Margaret Detch; and Mark S. Calnon, Ph.D. Harry Gildea testified for DOD/FEA. Bion C. Ostrander and Charles Buttiglieri testified for CWA. Trevor R. Roycroft, Ph.D., testified for the Attorney General. James A. Appleby testified for Sprint Nextel. Martin W. Clift, Jr., testified for Cavalier. Stephen D. Sinclair and Susan Hafeli testified for Fairfax County. Jonathan Flack and Joseph Gillan testified for Cox Telcom. Steven C. Bradley, Chris Harris, Kathleen A. Cummings, and Ben Johnson, Ph.D., testified for the Staff. The participants agreed to allow the

pre-filed direct testimony of Gary Case, on behalf of XO, to be admitted to the record without cross-examination.

The following participants submitted post-hearing briefs on or before September 14, 2007: Verizon; DOD/FEA; CWA; Sprint Nextel; Cavalier; Fairfax County; Cox Telcom; XO; Attorney General; and the Staff.

Verizon "requests that the Commission declare the services listed in Exhibit 13 as competitive under Va. Code § 56-235.5(F), detariff them pursuant to Va. Code § 56-235.5(E), deregulate them pursuant to Va. Code § 56-235.5(E) by declaring that they are no longer subject to Verizon's Deregulation Case, and provide such other relief as appropriate."[9]

DOD/FEA states that "Verizon's proposals to virtually eliminate regulatory surveillance are a vital concern to DOD/FEA as a major user of telecommunications services provided by this carrier and other carriers in Virginia," and DOD/FEA "urges the Commission to reject Verizon's proposals."[10]

CWA states that the "Commission should reject Verizon's radical and unprecedented proposal for complete statewide deregulation and detariffing of all retail services" and "should use this proceeding to adopt a methodology for competitive analysis, and reject Verizon's application."[11]

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[9] Verizon's September 14, 2007 Post-Hearing Brief at 260.

[10] DOD/FEA's September 14, 2007 Post-Hearing Brief at 2-3 (case and typeface modified).

[11] CWA's September 14, 2007 Post-Hearing Brief at 22.

Sprint Nextel "urges the Commission to lower Verizon's composite intrastate switched access rates to a level equal to the composite economic cost of providing local switching, tandem switching and common transport as a competitive safeguard."[12]

Cavalier and XO assert that "the evidence in this case does not support the full, or even partial, grant of Verizon's Application" and that "[o]n key issues, Verizon's evidence fails to satisfy the standards set forth by the Legislature, and as a result, Verizon's Application should be denied, in its entirety."[13]

Fairfax County "respectfully request[s] that the Application filed by Verizon dated January 17, 2007, be dismissed or denied because it contains insufficient facts to support a finding by the Commission that competition would be an effective regulator of price pursuant to Va. Code Ann. § 56-235.5(E) and (F) (2003) in the public interests and for failure to contain adequate safeguards to protect market competition and consumers pursuant to Va. Code Ann. § 56-235.5(H) (2003)."[14]

Cox Telcom "respectfully requests that the Commission deny Verizon's request to make its retail services competitive and for deregulation and detariffing of the same throughout the state," and "[s]hould the Commission endeavor to proceed with retail telephone deregulation, Cox Telcom respectfully requests that it consider the policy guidelines offered in [Cox Telcom's Post-Hearing] brief."[15]

The Attorney General states that: (a) it "supports Verizon's request as it applies to Bundles in the Virginia Beach, Richmond, Roanoke, and Washington-Arlington-Alexandria

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[12] Sprint Nextel's September 14, 2007 Post-Hearing Brief at 14.

[13] Cavalier's and XO's September 14, 2007 Joint Post-Hearing Brief at 31.

[14] Fairfax County's September 10, 2007 Post-Hearing Brief at 12.

[15] Cox Telcom's September 14, 2007 Post-Hearing Brief at 16.

Metropolitan Statistical Areas ('MSAs') . . . subject to modest safeguards as required by statute;" and (b) "[h]owever, because the evidence reveals there are not yet sufficient alternative providers available to reasonably meet the needs of consumers of BLETS (and OLETS) – provided outside of a package or bundled offering – those services cannot be classified as competitive pursuant to the statute, and [the Attorney General] cannot support deregulating those services at this time."[16]

The Staff "respectfully urges the Commission to not grant Verizon's Application," and "[i]n lieu of the blanket classification of Verizon's services as competitive, the Staff suggests a careful examination of specific services, in cohesive local markets, where customers are able to make meaningful telecommunications choices."[17]

NOW THE COMMISSION, having considered the record, the pleadings, and the applicable law, is of the opinion and finds as follows. The Application is granted in part and denied in part as set forth herein. We have evaluated the evidence presented in this case according to the statutory criteria set forth below, and we find that the pricing and service provisions approved herein satisfy such criteria.

Statutes Governing this Case

The General Assembly has established four levels of regulation over incumbent local exchange carriers ("ILECs") in Virginia. First, traditional regulation which, while largely unused in recent years, remains a legal alternative.[18] Second, the General Assembly has provided for a form of regulation that allows for much more flexibility than traditional regulation for ILECs,

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[16] Attorney General's September 14, 2007 Post-Hearing Brief at 3-4.

[17] Staff's September 14, 2007 Post-Hearing Brief at 16.

[18] *See* Va. Code § 56-235.2.

through the use of alternative regulatory plans.[19] Third, the General Assembly has allowed, though not mandated, deregulation of an unspecified scope when and where this Commission finds that "competition or the potential for competition" exists for a telephone service or services and "is or can be an effective regulator of the price" of the telephone service or services.[20]

Further, the General Assembly has directed this Commission, in its actions with regard to local exchange telephone service, to "promote competitive product offerings, investments, and innovations from all providers of local exchange telephone services in all areas of the Commonwealth. . . ."[21]

Considering together the various statutes that govern this case, we find that the General Assembly has set forth a general policy that directs this Commission to favor, within the parameters of those statutes, the promotion of competition for local exchange telephone services and to recognize in our regulatory structures competition where it already exists or may soon realistically exist. In promoting competition and deregulating as competition develops, however, we find that the General Assembly has also directed this Commission to proceed carefully and cautiously.[22] The General Assembly could have repealed all forms of regulation and completely deregulated all telephone services in Virginia, yet the General Assembly has not done that.

In its Application, "Verizon respectfully requests that the Commission declare the services listed in Exhibit VA-1 as competitive under Va. Code § 56-235.5(F), detariff them pursuant to Va. Code § 56-235.5(E), deregulate them pursuant to Va. Code § 56-235.5(E) by

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[19] *See* Va. Code § 56-235.5 B-D. Section 56-481.2 of the Code also references the Commission's authority to adopt alternative forms of regulation for the "incumbent local exchange company" under Va. Code § 56-235.5.

[20] Va. Code § 56-235.5 E-F ("Subsection E" and "Subsection F"). A fourth level of regulation, not applicable to Verizon, is available to small investor-owned telephone utilities. *See* Va. Code § 56-531 *et seq.*

[21] Va. Code § 56-235.5:1.

[22] *See, e.g.,* Va. Code § 56-235.5 G-H ("Subsection G" and "Subsection H").

declaring that they are no longer subject to Verizon's Alternative Regulatory Plan, and provide such other relief as appropriate."[23]

In this regard, Subsection E specifically provides as follows:

> The Commission shall have the authority, after notice to all affected parties and an opportunity for hearing, to determine whether any telephone service of a telephone company is subject to competition and to provide, either by rule or case-by-case determination, for deregulation, detariffing, or modified regulation determined by the Commission to be in the public interest for such competitive services.

Subsection F further directs the Commission as follows:

> The Commission may determine telephone services of any telephone company to be competitive when it finds competition or the potential for competition in the market place is or can be an effective regulator of the price of those services. Such determination may be made by the Commission on a statewide or a more limited geographic basis, such as one or more political subdivisions or one or more telephone exchange areas, or on the basis of a category of customers, such as business or residential customers, or customers exceeding a revenue or service quantity threshold, or some combination thereof. The Commission may also determine bundles composed of a combination of competitive and noncompetitive services to be competitive if the noncompetitive services are available separately pursuant to tariff or otherwise. In determining whether competition effectively regulates the prices of services, the Commission shall consider: (i) the ease of market entry, (ii) the presence of other providers reasonably meeting the needs of consumers, and (iii) other factors the Commission considers relevant. . . .

In addition, Subsection G places the following monitoring requirement on the Commission:

> The Commission shall monitor the competitiveness of any telephone service previously found by it to be competitive under any provision of subsection F above and may change that conclusion, if, after notice and an opportunity for hearing, it finds

[23] Application at 23-24.

> that competition no longer effectively regulates the price of that service.

Next, Subsection H directs the Commission to adopt safeguards pursuant to the following:

> Whenever the Commission adopts an alternative form of regulation pursuant to subsection B or C above, or determines that a service is competitive pursuant to subsections E and F above, the Commission shall adopt safeguards to protect consumers and competitive markets. At a minimum these safeguards must ensure that there is no cross subsidization of competitive services by monopoly services.

Finally, Va. Code § 56-235.5:1 specifically mandates as follows:

> The Commission, in resolving issues and cases concerning local exchange telephone service under the federal Telecommunications Act of 1996 (P.L. 104-104), this title, or both, shall, consistent with federal and state laws, consider it in the public interest to, as appropriate, (i) treat all providers of local exchange telephone services in an equitable fashion and without undue discrimination and, to the greatest extent possible, apply the same rules to all providers of local exchange telephone services; (ii) promote competitive product offerings, investments, and innovations from all providers of local exchange telephone services in all areas of the Commonwealth; and (iii) reduce or eliminate any requirement to price retail and wholesale products and services at levels that do not permit providers of local exchange telephone services to recover their costs of those products and services.

Verizon's Application to Deregulate and Detariff Statewide Most Local Telephone Services

Verizon's Application asks this Commission to deregulate and detariff essentially all local residential and business telephone services throughout its Virginia service territory.[24] We note at the outset that it appears only two other states, Rhode Island and South Dakota – both much smaller and far more homogeneous than Virginia – have deregulated local telephone service on a

[24] *See* Application at 1.

scale comparable to that which Verizon asks this Commission to do and it does not appear that *any* state has detariffed essentially all local telephone services.[25]

In support of its application, Verizon asserts that the appropriate market for local telephone services in Virginia is statewide and that the statewide telephone market is currently characterized by either competition or the potential for competition.[26] For example, Verizon states that "96 percent of households in Virginia have access to two or more communications platforms, 90 percent have access to 3 [sic] or more, and 78 percent have access to four or more," and that "99 percent of Virginia households have access to two or more competitive providers, 92 percent have access to five or more and 73 percent have access to eight or more."[27]

We agree in general with Verizon that the telecommunications market in Virginia has changed significantly over the past quarter century since the "modified final judgment"[28] began the restructuring of the old Bell system telephone monopoly. We find that new competitors, including cable television companies and CLECs, and new technologies (wireless telephone, Voice over Internet Protocol ("VoIP"), WiFi, WiMax, *etc.*) have collectively enabled significant competition to emerge that offers many consumers an alternative to purchasing telephone service from those ILECs that are the descendants of the former Bell system monopoly.

Competition to an ILEC such as Verizon presently comes from a number of sources. There are four types of CLECs, many of which fall under the jurisdiction of the Commission. First, a CLEC may resell the tariffed service offerings of Verizon. Second, a CLEC may

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[25] *See* Exhs. 52 and 53; Ostrander, Tr. at 913.

[26] Application at 7-8.

[27] Verizon's September 14, 2007 Post-Hearing Brief at 94-95.

[28] *United States v. American Telephone & Telegraph Co.*, 552 F. Supp. 131 (D. C. Dist. 1982).

purchase "Wholesale Advantage" from Verizon through a commercial contract.[29] Both resellers and Wholesale Advantage competitors rely primarily on the facilities and services of the ILEC in providing services to their end-user customers.

Third, a CLEC may also utilize a combination of its own facilities and facilities leased (*i.e.*, unbundled network element loops ("UNE-L")) from the ILEC. Cavalier is an example of such a UNE-L competitor. Finally, a CLEC, such as a cable television provider which chooses to offer telephone services, may operate its own wireline-based network as Comcast and Cox have done in much of their respective service areas in Virginia.

In addition, competition or the potential for competition to an ILEC's local telephone services can come from alternative mediums and/or technologies to provision telephone services that are not traditional wireline-based. Included in this category are mobile wireless telephone providers (*i.e.*, cellular). Emerging technologies such as WiFi and WiMax, which allow certain providers (*e.g.*, T-Mobile Hotspot and ClearWire) to utilize a wireless broadband technology to offer telephone services to some customers, also fit into this category. In addition, "over the top" VoIP providers, such as Vonage, can provide voice services to customers over an end-user's existing broadband connection.

In beginning our analysis, we recognize that Virginia is not an island unto itself, immune from national economic and industry trends. Nationally, the evidence indicates that wireline connections peaked at 192.4 million in December 2000 and declined to a reported 172 million by

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[29] Wholesale Advantage is the term Verizon uses for its commercially available unbundled network element-platform ("UNE-P") type service that it is no longer required to offer under its unbundling obligations pursuant to Section 251 of the Telecommunications Act of 1996. *See, e.g., In the Matter of Unbundled Access to Network Elements; Review of Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers,* W.C. Docket No. 04-313, FCC 04-290: Rel. February 4, 2005; West, Exh. 12 at 13, 88-89; Exh. 21C.

June 2006.[30] Usage of the traditional wireline network is decreasing, with ILEC interstate switched access minutes of use declining by a substantial 29% between 2000 and 2005, and the total number of local calls carried by large ILECs reported to the Federal Communications Commission ("FCC") falling from 554 billion to 336 billion, a decline of 39%, during roughly the same time period, (*i.e.*, 1999-2005).[31] At the same time, wireless connections nationally have increased dramatically. From June 2000 to June 2006, wireless subscriptions increased 140%, from 90.6 million to 217.4 million and now exceed total wireline connections.[32]

Competition has been advancing in Virginia. Verizon has lost landline connections in significant numbers, even as the population in Virginia has grown.[33] What is less clear is how many of Verizon's lost landline connections represent a one-for-one loss of a customer from Verizon to a competitor.[34] Some lost lines no doubt represent losses to changing technology rather than to competitors. Many Verizon business customers who once purchased additional landlines from Verizon dedicated to FAX usage, now use email rather than FAX for document transmittal and no longer need a dedicated FAX line, even though they remain revenue-producing customers of Verizon. Some of Verizon's residential customers who have children have traded in the second "children's" line for a wireless phone for the children, even as they remain revenue-producing Verizon customers for the primary landline service to the home.

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[30] NRRI Report Assessing Wireless and Broadband Substitution in Local Telephone Markets, June 2007 ("NRRI Report"), Exh. 271 at 32.

[31] *Id.*

[32] *Id.*

[33] *See, e.g.*, Application at 2; West, Exh. 12C at 37; Roycroft, Tr. at 1033.

[34] "Growth of wireless and broadband does not, by itself, imply that consumers are substituting them for wireline service. Nonetheless, the growth of other platforms at a time when the wireline platform is experiencing decline in connections and usage, supports the hypothesis that *some* substitution is taking place" (emphasis added). NRRI Report, Exh. 271 at 34, n.93.

Other customers have dropped their second lines that were previously dedicated primarily to dial-up internet access and purchased DSL or other broadband (*e.g.*, Verizon's fiber-based service, "FiOS") lines from Verizon. In both cases, these customers remain revenue-producing customers of Verizon.

The evidence does demonstrate that the number of wireless customers in Virginia has grown substantially,[35] and unquestionably some of Verizon's wireline customers have "cut the cord"[36] entirely and converted into exclusively wireless customers either of Verizon Wireless[37] or its competitors. Some Verizon customers have switched to VoIP providers,[38] which Verizon counts as wireline losses even though Verizon may retain these customers and some of their revenues.[39] Some customers have switched to those cable television providers now offering telephone service. Cox, for example, has a significant market share of the local telephone market in the areas of Virginia in which it competes, including Virginia Beach/Norfolk, Roanoke County, and Northern Virginia.[40] Other Verizon landline customers undoubtedly have switched to CLECs.[41] Determining the exact number of Verizon customers who have switched to

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[35] *See, e.g.,* West, Exh. 12 at 58.

[36] According to a May 2007 report by the National Center for Health Statistics based on the National Health Interview Survey of over 13,000 households, 12.8% of households nationally had only wireless telephones during the second half of 2006 (citation omitted). NRRI Report, Exh. 271 at 33. Other studies by Forrester Research and In-State/MDR report lower percentages of "cord cutters," 8% and 9.4%, respectively. West, Exh. 12 at 63-64. Evidence in this case, however, indicates that the Virginia percentage of complete "cord cutters" is even lower, about 6%. *See* Application at 2.

[37] Verizon Wireless, a majority of which is owned by Verizon, is one of the largest wireless providers in Virginia. *See, e.g.,* Taylor, Tr. at 818, 2101-2102.

[38] If Verizon loses a customer to an "over the top" VoIP provider, that customer may continue to generate revenues for Verizon if that customer uses Verizon's underlying DSL service for VoIP.

[39] *See, e.g.,* Taylor, Tr. at 858-859.

[40] *See, e.g.,* West, Exh. 12C at 41-42.

[41] *Id.,* at 91-92.

competitors for local telephone service is likely to be unachievable, however, since neither wireless, VoIP, nor broadband providers are under the primary jurisdiction of this Commission and have only a limited obligation to submit customer or line data.

Consequently, we need to analyze and review more closely each major source of statewide competition cited by Verizon.

Competition from CLECs and Traditional Interexchange Carriers

As discussed previously, CLECs compete by utilizing several methods. A number of CLECs compete by purchasing the tariffed retail services of Verizon at a discount and then reselling those services to their own retail customers. Other CLECs purchase Wholesale Advantage and/or UNE-L service from Verizon as a means to offer service to their customers. We find that these CLECs, which must rely on service and facilities leased from Verizon in order to provide retail service in Virginia, should not be considered "facilities-based" providers for purposes of our discussion and findings herein.[42]

In addition, national data indicates that the ability of CLECs to compete with ILECs was adversely affected by FCC action regarding the ILECs' obligation to offer UNE-P at total element long run incremental cost (generally referred to as "TELRIC") prices to CLECs.[43] Indeed, the national share of CLEC wireline connections was actually lower in June 2006 than in June 2004 and after ten years of facing competition from CLECs, ILECs still held a national market share of wireline connections of more than 80%.[44]

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[42] Cable companies are discussed in the following section.

[43] *See* NRRI Report, Exh. 271 at 48, n.141; *In the Matter of Unbundled Access to Network Elements; Review of Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers,* W.C. Docket No. 04-313, FCC 04-290: Rel. February 4, 2005.

[44] *See* NRRI Report, Exh. 271 at 48.

Generally, CLECs represent a type of local telephone service closely comparable in price, service quality and reliability to that offered by Verizon's traditional landline network. The evidence demonstrates that certain CLECs are currently competitors to Verizon in some local geographic markets in Virginia, but the actions in 2005 of the FCC with regard to UNE-P make it far more likely that competition from CLECs as a category of competitor will decrease, not increase, in Virginia. Verizon is correct that we must make a "forward looking" analysis of the market that considers trends and market dynamics, and not just look at static market shares or statistics.[45] Consequently, considering the evidence of trends and market dynamics and as further analyzed below, we find that CLECs as a category of competitor do not meet the "potential for competition" standard in Subsection F in geographic areas where they are not currently present and therefore do not represent a statewide competitor to Verizon. They are, nonetheless, a close substitute for Verizon's landline service, and we include them as a competitor in geographic areas where they are present, as discussed further below.

As far as competition from historically traditional interexchange carriers, two of the largest and most aggressive competitors to Verizon for telephone service five years ago, MCI and AT&T, have both been acquired by ILECs. Verizon itself purchased MCI, eliminating MCI as a competitor in Virginia. AT&T was purchased by SBC[46] and the evidence demonstrates that AT&T is presently not an aggressive or active competitor in Virginia for wireline-based residential telephone service.[47] We do not find that other regional Bell Operating Companies such as today's AT&T or Qwest, or former interexchange carriers such as MCI and the "old"

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[45] *See* Application at 5; Verizon's September 14, 2007 Post-Hearing Brief at 46.

[46] SBC chose to rename itself AT&T after the purchase.

[47] *See* Petition of AT&T Communications of Virginia, LLC for Approval to Exceed Price Ceilings, filed on January 3, 2007, Case No. PUC-2007-00001, at 3-4; Cummings, Tr. at 1408-10.

AT&T, meet the "potential for competition" standard under Subsection F to be considered statewide competitors to Verizon for mass market, residential wireline telephone service.

Competition from Cable Television Companies

Verizon cites cable companies as a significant statewide source of competition for local telephone service.[48] Cable television providers that choose to offer traditional telephone or internet-enabled telephone service offer a product that is comparable, though not identical, to Verizon's wireline service in terms of reliability and service quality. We find that of all the intermodal platforms, stand-alone cable telephony services come the closest to providing the functional equivalent to traditional wireline services.[49] Cable companies own their own wireline network and provide local telephone service either through traditional circuit-switched technology (technically as a CLEC), or increasingly through the use of IP-based technology that is fully connectible to the public switched telephone network ("PSTN").

We find that cable telephony is a competitive option that may reasonably meet the needs of consumers under Subsection F in terms of reliability and service quality. Verizon is correct that telephone service from cable companies is available in many of the larger urban and suburban areas of Virginia, *e.g.*, Fairfax, Virginia Beach, Richmond, and Roanoke County. In many small cities, towns, and rural areas of Virginia, however, local telephone service is not available from the cable company; indeed, in some areas of Virginia there is no cable provider at

[48] *See, e.g.,* Application at 11; West, Exh. 12 at 41-51.

[49] *See, e.g.,* Johnson, Exh. 192P at 45. For some cable customers, we note that E-911 service may be negatively affected after a prolonged electric power outage to the customer's home.

all.[50] Verizon argues that even though a cable company may not be currently offering local telephone service, the threat that a cable company *could* choose to offer local telephone service should Verizon raise its rates too high should be considered as meeting the statutory standard of "potential for competition."[51] We find, however, that the capital and human resources investments necessary for a cable company to offer local telephone service are significant barriers to entry under Subsection F and are unlikely to be made simply because Verizon raises prices for basic local telephone service.[52] We further find that sparsely populated counties or towns in which no cable company has heretofore found economic incentives sufficient to justify investing millions of dollars to build a cable television network are unlikely, to say the least, to attract a cable company willing to invest millions of dollars in order to compete with Verizon for local telephone service, a fact acknowledged by Verizon Witness Eisenach.[53] Thus, contrary to Verizon's assertion that cable companies currently present *statewide* competition to Verizon for local telephone service, we find that competition from cable television companies to Verizon is non-existent in many of the more rural geographic areas of Virginia. We find that to be considered under the statute as competitors to Verizon for local telephone service, a cable company must be present in the local market and currently offering telephone service.

Verizon states that "[t]he record contains overwhelming evidence that cable provides a competitive alternative to Verizon's services *where a provider has upgraded its network to*

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[50] Verizon states that 90% of Virginia households are passed by cable (taking Verizon's statement as true, we note that means that at least 10% of Virginia households are not), but only 60% are passed by cable providers presently offering telephone service. *See* Exh. 19. In the 96 counties Verizon witness Dr. Taylor identified as counties in which Verizon has operations, 60 of those counties do not have cable telephone services available to consumers. *See, e.g.*, Roycroft, Ex. 129P at 56.

[51] *See* Eisenach, Tr. at 515-518; Verizon's September 14, 2007 Post-Hearing Brief at 46-47, nn.57, 58

[52] *See, e.g.,* Johnson, Tr. at 1573-1574.

[53] Eisenach, Tr. at 480-483, 518-519.

provide digital voice or broadband services."[54] We agree with Verizon that where a cable company has upgraded its network to provide telephone service, it represents a competitive alternative to Verizon. We would add that we find that to be the case whether the cable company offers a traditional circuit-switched telephone service (which would make the cable company technically a CLEC) or uses IP-based technology to connect to the PSTN. In our competitiveness test adopted herein, we include cable companies as facilities-based competitors to Verizon where there is a cable provider that has upgraded its network to offer telephone service.

Verizon also asserts that:

> where a cable company has deployed broadband facilities, it is a current competitor to Verizon's voice services, even if it has not yet deployed telephony . . . [T]he broadband services permit an end user to use 'over-the-top' VoIP services in lieu of a wireline phone. . . .[55]

We discuss below whether a cable provider should be included as a competitor to Verizon simply because it offers a broadband internet connection, even when it does not offer telephone service of its own.

On the other hand, we disagree with the Attorney General that a cable company (or, for that matter, a CLEC or wireless provider) must be offering a stand-alone BLETS product at roughly the same price as Verizon to be considered a competitor to Verizon.[56] We find that if a cable company is presently offering local telephone service in a geographic market area, in any price or bundled configuration, it meets the "potential for competition" standard in Subsection F

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[54] Verizon's September 14, 2007 Post-Hearing Brief at 19 (emphasis added).

[55] *Id.* at 21 (citing Verizon Witness Eisenach at Tr. 478-83, 599).

[56] Attorney General's September 14, 2007 Post-Hearing Brief at 8-10, 13-15.

to be considered a competitor to Verizon that can effectively regulate Verizon's prices. Since that cable company has already invested the capital and human resources necessary to offer telephone service, there are no significant barriers to entry to prevent that cable provider from competing directly on price with Verizon for BLETS, should Verizon raise its BLETS prices.

Competition from Wireless Telephone Providers

Verizon cites wireless telephone providers as statewide competitors for its local telephone service.[57] As noted above, the evidence shows that the number of wireless customers has grown substantially in Virginia. Verizon's own evidence demonstrates, however, that while the overall number of wireless lines has grown, very few Virginia consumers have "cut the cord" entirely and replaced landline telephone service with wireless service as their only platform for local telephone service.[58] As stated in the NRRI Report introduced by Verizon: ". . . growth in wireless and broadband do not, by themselves, provide conclusive evidence of competition with or substitutability for wireline service. . . ."[59]

For various reasons wireless telephone service may not be a reasonable substitute under Subsection F for landline service for many consumers; for example, wireless service does not provide the same level of reliability as landline telephone service, particularly inside the home or office structure.[60] Further, while significant technological progress has been made, wireless 911 service has yet to reach the standard of landline E-911 service, and this represents a major public safety issue that we cannot ignore when determining whether wireless telephone service is a statewide substitute to Verizon's landline service that "reasonably meets the needs of consumers"

[57] *See, e.g.,* Application at 1-3, 10-12; West, Exh. 12 at 51-67, 114-119.

[58] *See, e.g.,* Application at 2; West, Exh. 12C at 7.

[59] NRRI Report, Exh. 271 at 48.

[60] *See, e.g.,* Roycroft, Exh. 129P at 58-62, 66-72.

under the statutory standard in Subsection F.[61] Because of these reliability and public safety concerns, we find that wireless cannot be considered a statewide substitute for Verizon's wireline services at this time.[62]

Nevertheless, while wireless is not a perfect substitute for Verizon's landline service, we believe it would underestimate the actual amount of competition to Verizon if we did not include wireless competition at all in determining market competitiveness. We find that wireless service is an adequate substitute for *some* consumers, and this number is growing. Wireless service is not just an option for the laughing teenagers often featured in wireless companies' television advertising. It may be an increasingly preferred option for small businesses like plumbers, carpenters, sales persons, home builders and realtors, who have their offices in their cars, trucks or on their own persons. Moreover, a competitor does not have to be a perfect substitute to Verizon's landline service to act as a price regulator of Verizon's local telephone service under Subsection F. As discussed in more detail below, we find that it is appropriate to include wireless competition to Verizon in the geographic market areas in which it is available in the competitiveness test we adopt herein.

Competition from Broadband-enabled Telephone Providers

Whenever a home or business has a broadband connection, the potential exists for the consumer to purchase telephone service from a VoIP provider. That potential exists whether the consumer purchases the broadband "pipe" from Verizon itself, from the cable company, from a provider using wireless technology such as WiMAX or WiFi, or from a provider using a

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[61] *Id.* at 68-69.

[62] In addition, we note that there are areas of Virginia in which wireless service may not be regularly available. *See, e.g.,* Thompson, Tr. at 111 (public witness); Roycroft, Exh. 129P at 61-62 (citation omitted).

Broadband over Power Line ("BPL") platform. Verizon cites VoIP as a major source of statewide competition for their local landline telephone service.[63]

At the outset, we find that so-called "peer to peer" VoIP services, such as Skype-to-Skype, cannot be considered as competitors to Verizon for local telephone service because calls can only be made between Skype users. These types of "peer to peer," or "computer to computer," calling schemes do not include calls to the PSTN and thus cannot be considered as reasonably meeting the needs of consumers under Subsection F. So competition to Verizon that would qualify under the statute must come from the "over the top" VoIP providers such as Vonage that use another provider's broadband "pipe" into the home and which offer telephone service that connects to the PSTN.

As discussed above, it is difficult to determine the exact number of customers in Virginia who have switched from Verizon to VoIP providers such as Vonage, since such VoIP providers are not under the jurisdiction of this Commission. There is a lack of persuasive evidence in this record demonstrating that VoIP providers have currently gained any significant foothold in the local telephone market in Virginia. On the contrary, what evidence is available appears to show that the market share of "over the top" VoIP providers in Virginia is so small that such providers cannot be considered as serious statewide competitors to Verizon for local telephone service at this time.[64] Further, Vonage, which according to Verizon is "reputed to be the leading broadband telephony provider [(*i.e.*, VoIP competitor)] in the United States,"[65] thus likely in Virginia as well, has recently lost two patent infringement lawsuits brought by Verizon and

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[63] *See, e.g.,* Application at 3; West, Exh. 12 at 78-87, 120-125.

[64] *See* Eisenach, Tr. at 1871-1873; Exh. 210C.

[65] West, Exh. 12 at 83.

Sprint Nextel.[66] Another significant VoIP provider in Virginia, SunRocket, Inc., has ceased providing VoIP services to its customers.[67]

Verizon cites the BPL platform as facilitating the growth of broadband-enabled competition.[68] We find that providing local telephone service over power lines is not at this time a major source of competition to Verizon in Virginia nor a realistic threat of potential competition in the foreseeable future. According to Verizon, BPL is offered only in Manassas, Radford, and in parts of Amherst and Nelson counties.[69] Further, there is no evidence whatsoever in this record that the largest owners of power lines in Virginia, Dominion Virginia Power and Appalachian Power Company, have any plans to use their networks to offer widespread BPL service in the near future, either as direct providers of service or as lessors of their facilities. That could obviously change as BPL technology continues to develop and BPL could conceivably become a major source of broadband availability in the future, because the network is already in place throughout Virginia, but we find it is not at this time nor likely in the imminent future.

Apart from the availability of broadband, even when the consumer has a broadband connection, "over the top" VoIP providers do not presently provide nearly the same level of reliability, service quality or, most importantly, 911 service, as landline telephone service, to be

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[66] *See Verizon Services Corp. v. Vonage Holdings Corp.*, 503 F.3d 1295 (Fed. Cir. 2007), affirming in part judgment of U.S. District Court in *Verizon Services Corp. v. Vonage Holdings Corp.*, 2007 U.S. Dist. LEXIS 26714 (E.D.Va. April 6, 2007); *Sprint Communs. Corp. LP v. Vonage Holdings Corp.*, Case No. 05-2433 (Kan. Dist. Ct. September 25, 2007).

[67] *See* Eisenach, Tr. at 1784.

[68] "[BPL] technology has the potential of being 'a ubiquitous third pipe to the home.'" West, Exh. 12 at 103 (citation omitted).

[69] *Id.* at 106-107.

considered as reasonably meeting the needs of consumers, as the statute requires us to consider.[70] We believe it likely that the continuing development of VoIP technology will result in improvements to reliability and 911 service in the future, and as those technological improvements take place, VoIP service may become more of a reasonable substitute for landline telephone service, but present-day reliability and public safety concerns with VoIP cannot be ignored.

Nevertheless, just as we found above that totally excluding wireless competition would underestimate the amount of actual competition to Verizon, we also find that totally excluding actual or potential competition from broadband-enabled providers would underestimate competition to Verizon as well, and thus we find that VoIP should be included in our competitiveness analysis, as we discuss below.

The key issue in determining whether VoIP is a *statewide* competitor to Verizon is, of course, broadband penetration, for the simple reason that "over the top" VoIP cannot pose a threat of competition to Verizon unless the customer both has a broadband connection available *and* has chosen to purchase broadband internet service. As Verizon Witness Eisenach stated:

> The question is 'is voice telephone service available,' and it's not available if there's no broadband. VoIP – over-the-top VoIP – is not available if there's no broadband, [] and if there is broadband then over-the-top VoIP is available to a hundred percent of – depending on how you want to look at it, either a hundred percent of the households where the broadband is available or, *at a minimum, a hundred percent of the households who already subscribe to broadband.* So broadband is simply a proxy – the broadband availability is simply a proxy for looking at VoIP availability, and VoIP is clearly a telephone service.[71]

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[70] *See, e.g.,* Roycroft, Ex. 129P at 88-92; Gillan, Tr. at 1274.

[71] Eisenach, Tr. at 1834 (emphasis added).

We agree with Dr. Eisenach that broadband availability is an initial proxy for VoIP availability. As Dr. Eisenach also recognized, however, for a consumer to have access to "over the top" VoIP service, a consumer not only must have broadband available, but *also must have chosen to purchase a broadband internet connection.* We find that actual broadband penetration by household and by business is an important indicator of the scope of competition to Verizon posed by VoIP. Thus, we find it appropriate to include "over the top" VoIP in our market competitiveness test as a competitor to Verizon for local telephone service when it is both available and the customer has chosen to purchase broadband internet service.

Statewide Competition to Verizon's Local Telephone Service Is Not Uniform and Should Be Considered in Smaller Geographic Areas, by Product/Service Categories, and by Types of Customers

Verizon is the largest ILEC in Virginia and faces significantly more competition today compared to that which its corporate ancestors faced a quarter century ago. We find that while competition or the potential for competition for local telephone service has increased significantly, the degree varies substantially by geographic area, by product and service, and by type of customer. It is not yet advanced in *all* geographic areas of Virginia and for *all* products and services and types of customers sufficient to fulfill the statutory standards in Subsections E and F that we must follow in considering Verizon's request for complete deregulation and detariffing of virtually all local telephone services on a statewide basis. We agree with the NRRI Report introduced by Verizon that "a whole state is generally too large to be used to define the geographic market. . .,"[72] particularly in a state as large and economically diverse as Virginia, and that "larger ILECs' service territories are also likely to exhibit too much variation in

[72] NRRI Report, Exh. 271 at 47.

competitors to be considered as the geographic market."[73] Consequently, we find that, given the evidence, the applicable statutes require that we consider Verizon's request for deregulation and detariffing of most local telephone services by geographic markets smaller than Verizon's statewide service territory, by categories of products and services, and by types of customers.[74]

Further, even if we did agree to Verizon's request to consider its entire Virginia service territory as one market, the evidence shows that many geographic areas of Virginia lack a facilities-based competitor to Verizon, and as we found above, the barriers to entry for facilities-based wireline competitors such as cable companies are substantial. While cable and CLEC competitors present significant competition to Verizon where they exist, we find that neither cable nor CLEC providers meet the "potential for competition" statutory standard in geographic areas of Virginia in which they currently are not present at all, or in the case of cable, present but not offering telephone service. Further, while we find that wireless and broadband-based competitors such as "over the top" VoIP should be considered in determining competitiveness – and we include them in our competitiveness test herein – most other states that have deregulated local telephone service have required at least one competitor in their market competitiveness tests to be "facilities-based," effectively either a cable company or a CLEC that owns its own wireline network.[75]

We believe that to fulfill our statutory obligations given us by the General Assembly, we should deregulate with caution and with due attention to safeguards to protect both consumers and competition, as required by Subsections G and H. Accordingly, this Order:

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[73] *Id.*

[74] As discussed below, we find that competition to Verizon's bundled services may appropriately be considered on a statewide basis. We also find below that the "enterprise market" is appropriately considered to be statewide.

[75] *See* Exhs. 52, 53, 308. "Competition, for the most part, is defined as the existence of at least one facilities-based competitor and another carrier competing with the incumbent." Exh. 53 at 2.

(i) deregulates where the facts demonstrate that the statutory standards have been met,
(ii) maintains regulation where the statutory standards have not been met,
(iii) establishes an expeditious administrative process for additional deregulation in the future when and where additional evidence of competitiveness warrants deregulation pursuant to the findings in this Order, and
(iv) establishes safeguards for competition and consumers and a process for monitoring competition in the future, as required by statute.

BLETS, OLETS and Bundled Services Defined

Verizon identifies over 180 specific services that it requests the Commission to declare competitive. Verizon separates these services into the following categories, which are in accordance with the categorization in Verizon's Alternative Regulatory Plan: BLETS; OLETS; and Bundled Services.[76]

First, Verizon lists seven BLETS for Verizon Virginia and eight BLETS for Verizon South that the Company requests be declared competitive on a statewide basis.[77] The category BLETS includes basic telephone service, sometimes referred to as "Plain Old Telephone Service," or "POTS," to continue the parade of telephonic acronyms. For purposes of this Order, we exclude (1) pay telephone services, and (2) Extended Local Service from our determinations herein regarding competition for BLETS. We find that pay telephone services are sufficiently distinct from other BLETS to warrant separate analyses; in this regard, we note that Verizon may file a request with the Commission under its Alternative Regulatory Plan or pursuant to Va.

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[76] *See* Exh. 13.

[77] Verizon Virginia's BLETS are listed as: (1) Residential Dial Tone Line, and any included local calling allowance (flat rate, message rate or measured rate); (2) Business Dial Tone Line, and any included local calling allowance (flat rate, message rate or measured rate); (3) Centrex Exchange Access; (4) Exchange Usage; (5) Extended Area Calling; (6) Extended Local Service (ELS); and (7) Pay Telephone Lines. Verizon South's BLETS are listed as: (1) Residential Dial Tone Line, and any included local calling allowance (flat rate, message rate or measured rate); (2) Business Dial Tone Line, and any included local calling allowance (flat rate, message rate or measured rate); (3) Centrex Exchange Access; (4) Residential, Business and Centrex Local Calling Plans that include: Basic Calling Plan, Community Plus Calling Plan, and Premium Calling Plan; (5) Customer Owned Coin and Coinless – Operated Telephones – Line Service; (6) Customer Owned Pay Telephone Coin Line Service (COPT); (7) Exchange Usage; and (8) Extended Local Service (ELS). *Id.*

Code § 56-235.5, with supporting data specific to these services, to reclassify them as competitive. The rates for Extended Local Service are separately governed by Va. Code § 56-484.2, and, as a result, Verizon's Alternative Regulatory Plan does not permit the Company to increase any tariffed Extended Local Service rates outside the provisions of Va. Code § 56-484.2; likewise, we find that Extended Local Service rates shall continue to be established pursuant to Va. Code § 56-484.2.

Next, Verizon lists over 80 services as OLETS for Verizon Virginia and over 70 services as OLETS for Verizon South that the Company requests be declared competitive on a statewide basis. As a brief example, the OLETS listed by Verizon include services such as: Custom Calling Services (*e.g.,* call forwarding, caller I.D., and call waiting); Answering Bureau Services; Billing and Collection Analysis; Do Not Disturb; Easy Number Call Routing; Fixed Call Forwarding; Home Business Service; Operator Verification; Operator Call Completion; Remote Call Forwarding; Repeat Dialing; Selective Call Screening; Analog Channel Services; Custom Operating Center Services; CyberDS1 Service; Digital Data Services; High Capacity Digital Service – DS1; and High Capacity Digital Service – DS3. We note that there is significant, yet not complete, overlap in OLETS identified for Verizon Virginia and Verizon South.[78]

Finally, Verizon lists eight Bundled Services for Verizon Virginia and six Bundled Services for Verizon South that the Company requests be declared competitive on a statewide basis.[79] These services generally represent a designated group of services or products offered to

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[78] *See* Exh. 13.

[79] Verizon Virginia's bundled services are listed in Exh. 13 as: Verizon Affiliate Bundle Discount; Verizon Local Package; Verizon Local Package Extra; Verizon Regional Essentials; Verizon Regional Package Extra; Verizon Regional Package; Verizon Regional Value; and Unlimited Local and Toll Usage for Business. Verizon South's bundled services are listed in Exh. 13 as: CENTRANET CustoPAK Service & Assoc. Features; Verizon Local Package; Verizon Local Package Extra; Verizon Regional Package Extra; Verizon Regional Package; and Unlimited Local and Toll Usage for Business.

customers at a package or set price, which may consist of BLETS, OLETS and/or competitive services or products.

Residential and Business Markets

We find that the mass market residential and business local telephone services and products are separate product markets in Virginia and should be treated separately in this Order, consistent with Subsections E and F. We note that several of the states (and Canada) that have deregulated local telephone services to varying extents have treated mass market residential and business services separately in their deregulation frameworks.[80] We further treat the so-called "enterprise" business market separately, for the reasons discussed below.

Appropriate Geographic Market Area for Residential BLETS and OLETS

Subsection F authorizes us to make a finding of competition "on a statewide or a more limited geographic basis, such as one or more political subdivisions or one or more telephone exchange areas . . . ." Pursuant to this statute, and based on the evidence provided in this proceeding, we find that an appropriate geographic market area ("GMA") for determining the competitiveness of residential BLETS and OLETS should be telephone exchange areas.

While the statute itself uses political subdivisions or telephone exchange areas as examples of less-than-statewide geographic units, Verizon asks us to use "MSAs" and "non-MSAs" if we use a smaller than statewide geographic area to determine competitiveness.[81] We find, however, that while an MSA may encompass a collection of telephone exchanges or political subdivisions, an MSA is too large and economically diverse to be an appropriate geographic market area for making a competitiveness determination under Subsections E and F.

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[80] *See* Exhs. 52, 53, and 308.

[81] *See* Verizon's September 14, 2007 Post-Hearing Brief at 64-69. For ease of reference in this Order hereinafter, references to "MSAs" also include those geographically-defined areas that Verizon refers to as "non-MSAs."

We note, for examples, that the Virginia Beach-Norfolk-Newport News MSA includes the Surry and Windsor exchanges and the Richmond MSA includes the King and Queen and King William exchanges. Rural exchanges such as these on the perimeters of MSAs are not similar enough in economic and demographic characteristics to the more urban and suburban exchanges in those MSAs, such as Virginia Beach and Richmond, for us to find that those still-rural exchanges are similarly situated in terms of currently having – or likely to have – competitive options comparable to those available, or likely to be available, to consumers in the more densely populated jurisdictions.[82] Rather, we find that Verizon will not be able effectively to discriminate, in its service offerings, against customers in these rural exchanges if the exchange itself is required to meet the competitiveness test set forth below.

The NRRI Report white paper cites the U.S. Department of Justice ("DOJ") merger guidelines for an appropriate market definition that is, in both product and geographic space, described as the "smallest market in which a hypothetical monopolist could exercise market power."[83] Market power is, of course, the ability of a seller of a product or service to impose and sustain a price above that which would obtain in a competitive market.

We find that telephone exchange areas – units specifically listed in the Code of Virginia – most closely fit the definition of an appropriate geographic market as contained in the DOJ merger guidelines, which is a recognized definition and the one specifically cited in the NRRI Report introduced as Verizon Exhibit 271, which also asserts that using the entire state as the market is generally inappropriate.[84]

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[82] *See, e.g.,* Johnson, Exh. 192C at 21-22; Johnson, Tr. at 1517-1518; Reeson, Tr. at 118-121 (public witness).

[83] NRRI Report, Exh. 271 at 21 (citation omitted).

[84] *Id.* at 47.

Since MSAs generally encompass on a regional basis a number of telephone exchanges, Verizon can still demonstrate that an entire MSA is competitive by showing that the individual exchanges within that MSA satisfy the test set forth below. Our market competitiveness test, however, which is similar to those applied in several states that have adopted procedures to deregulate local telephone service, will ensure that *each* local exchange area will have at least one facilities-based competitive option to Verizon, which could not be guaranteed in every exchange if we used only MSAs as the geographic market area.

Finally, we note that the statute does not require a finding, prior to a determination of competitiveness, that *each* consumer in the chosen GMA has the *same* competitive alternatives. Indeed, we recognize that any finding of competitiveness in a geographic area listed by the statute may result in at least one or more individual consumers who do not share in all the competitive alternatives available to others in that same area. We find, however, that telephone exchange areas meeting the criteria below represent sufficiently small enough geographic areas for us to be satisfied that Verizon will not be able effectively to discriminate, in its service offerings, against consumers who do not have the same competitive alternatives as others in the exchange. That is, we conclude that if the competitiveness test below is satisfied for a specific local telephone exchange area, then competition or the potential for competition is or can be an effective regulator of the price for all consumers in that area.

Competitiveness Test for Residential BLETS

Subsection F states that the Commission:

> *may determine telephone services of any telephone company to be competitive when it finds that competition or the potential for competition in the market place is or can be an effective regulator of the price of those services . . . In determining whether competition effectively regulates the prices of services, the Commission shall consider: (i) the ease of market entry, (ii) the*

> *presence of other providers reasonably meeting the needs of consumers, and (iii) other factors the Commission considers relevant. . .*

As set forth above, we do not find that "competition or the potential for competition in the market place is or can be an effective regulator of the price"[85] for residential BLETS on a statewide basis. Rather, based on the record developed in this case, we find that competition or the potential for competition can be an effective regulator of the price for residential BLETS in a telephone exchange area if *each* of the following criteria is satisfied:

a. A minimum of 75% of the households in the telephone exchange area can choose residential local telephone service from among at least two (2) competitors to Verizon;

b. A minimum of two (2) of the competitors to Verizon in part "a" must offer residential local telephone service that may be purchased by the residential consumer without a corresponding requirement to purchase non-telecommunications services (*e.g.*, video or broadband internet service) from that competitor; and

c. At least 50% of the households in the telephone exchange area can choose a facilities-based competitor that owns its own wireline network facilities.

Examples of an acceptable facilities-based competitor in "c" above would include (1) a cable telephony provider that owns its own network, or (2) a CLEC provider that owns its own network and is not dependent on Verizon for leasing UNE-P or UNE-L facilities to the CLEC. Wireless or "over the top" VoIP providers are not included as facilities-based providers for purposes of this Order, for the reasons further discussed below.

[85] Va. Code § 56-235.5(F).

Examples of an acceptable competitor in "a" above could be a cable company, CLEC,[86] or any wireless provider not affiliated with Verizon[87] which offers residential local telephone service. Since "over the top" VoIP providers are only available to customers who have access to, and have chosen to purchase, broadband internet service, for "over the top" VoIP to qualify as a competitor for local telephone service to Verizon in a telephone exchange, at least 75% of the households in Verizon's service territory in the exchange must have chosen to purchase broadband internet service, whether via DSL, cable modem, wireless (WiMAX or WiFi), BPL or Verizon's own fiber to the home product. "Over the top" VoIP cannot be an effective competitor to Verizon unless broadband penetration is substantial throughout the exchange, which means that broadband is not only available, but consumers have chosen to purchase broadband internet service.

In requiring at least one facilities-based competitor to have a substantial presence in the exchange area, we apply Subsection F's directive to "consider ... the presence of other providers reasonably meeting the needs of consumers . . . ." As discussed above, we find that for many consumers of basic local telephone service, reliability of service and, in particular, reliable 911 service, are reasonable needs. Neither wireless nor VoIP provides the same level of consistent reliability and, in particular, 911 service reliability, that is delivered by Verizon's

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[86] We do not include herein resellers, which simply resell another provider's (often Verizon's) services and which do not provide sufficient competition to Verizon to be considered a competitor under this test. Resellers do not represent an acceptable competitor in part "a."

[87] We find that requiring the wireless competitor not to be affiliated with Verizon (which owns a majority share in Verizon Wireless), will result in a more accurate indicator of actual or potential competition to Verizon's landline service. While Verizon Wireless competes with other wireless providers such as AT&T and Sprint Nextel, Verizon Wireless can cooperate and market jointly with Verizon's other services, including landline. Just as we found that not including wireless at all could understate the amount of competition to Verizon's landline service, we also find that including Verizon Wireless as a competitor to Verizon for local telephone service could overstate the amount of competition in a geographic market area.

wireline service or, to a lesser extent, cable providers.[88] Most importantly, for purposes of acting as a price regulator of Verizon's BLETS, we find that a competitor that owns its own wireline network presents the strongest actual or potential competition to Verizon's wireline service.

While wireless and "over the top" VoIP telephone services do not provide the same level of consistent reliability and E-911 service as Verizon's landline service so as to be a reasonable product substitute for all consumers under Subsection F, we do find that, in particular, wireless service, and to a lesser extent, VoIP, are acceptable substitutes for enough consumers to act as price regulators of Verizon's local telephone service under Subsection F when wireless and VoIP competitors are sufficiently present in an exchange. Consequently, we include wireless providers as acceptable competitors under the competitiveness test we adopt herein. We also include "over the top" VoIP as a competitor wherever broadband penetration, defined as households having a broadband internet service, has reached 75% in the exchange.

As discussed above, we do not find it necessary under Subsection F that each and every competitor to Verizon offer an array of products and services identical to Verizon or at prices identical to Verizon's stand-alone BLETS in order to act as a price regulator of Verizon's local telephone services and products. Consistent with Subsection F's directive to consider "competition or the potential for competition," we find that including cable, CLEC, wireless and VoIP providers in the competitiveness test as acceptable competitors fulfills the statute's "potential for competition" criterion, even though none may be presently offering an exact duplicate of Verizon's BLETS product offerings at prices identical to Verizon's. Each competitor presently offering residential telephone service represents a potential threat to match or undercut Verizon's pricing.

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[88] *See, e.g.,* Roycroft, Exh. 129P at 58-70, 88-92; Johnson, Exh. 192P at 36-40, 43-45.

Further, Subsection F requires us to consider "the ease of market entry" in determining competitiveness. Accordingly, while we do not require that each competitor presently offer an identical array of BLETS at prices identical to Verizon's, we do require in our competitiveness test that at least two competitors already are substantially present in the telephone exchange area offering residential telephone service. We find that the statute does not allow us to include in our competitiveness determination the mere threat that a cable company or CLEC not already present in an exchange will decide to make the substantial capital investment necessary to enter a market simply in response to price increases for BLETS by Verizon.

We note that the "two competitor" test, with at least one required to be facilities-based,[89] which we adopt herein, is well within the mainstream of competitiveness tests used in the majority of other states (and Canada) that have deregulated their BLETS to various extents.[90] We also note that the "two competitor" test we adopt herein is similar in some respects to the competitiveness test in the federal Cable Act of 1992, discussed by Verizon Witness Eisenach[91] and cited in Verizon's Post Hearing Brief.[92]

The test we adopt herein does not depend upon extensive collection of provider line counts or detailed market share data, which would be difficult to obtain since VoIP and wireless competitors do not have a legal obligation to provide actual line counts to this Commission.

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[89] The facilities-based competitor is potentially a third competitor if it is available to at least 50% but less than 75% of the households in the exchange.

[90] *See* Exhs. 52, 53, and 308. Texas uses a "three competitor" test, but Texas has no requirement that most consumers' households in the GMA have access to all three competitors. Canada requires two competitors to the ILEC, with availability of each to at least 75% of households in the GMA. We find that the Canadian requirement of 75% availability is a more accurate indicator of actual or potential competition in the GMA as required by § 56-235.5(F) than the Texas "three competitor" test, with no such availability requirement.

[91] *See* Eisenach, Tr. at 1678-82, 1735-44.

[92] Verizon's Post-Hearing Brief at 92-93 (citing the Cable Act of 1992). *See also* 47 U.S.C. § 543(1)(l).

Instead, this test looks at the availability of competitive options to Virginia consumers and seeks to ensure that consumers in each exchange have at least two alternatives for residential local telephone service other than Verizon landline before that exchange is declared competitive.

Further, we find that the competitiveness test described herein is sufficient to protect consumers in an exchange area from the exercise of market power by Verizon for BLETS. The requirement that at least two other competitors be available to at least 75% of the households in the exchange area (with an additional requirement that at least 50% of the households have access to a facilities-based provider) will prevent Verizon from raising its BLETS prices without incurring a significant risk of losing customers. Consequently, in an exchange area meeting this test we find that "competition or the potential for competition" can act as a regulator of Verizon's BLETS prices, in accordance with Subsection F, even though there may be some consumers in the exchange area who do not have access to one or more of the competitors to Verizon in the exchange.

We could not make this finding had we accepted Verizon's proposal to consider as the appropriate market area Verizon's entire statewide service territory or the MSAs proposed by Verizon. Statewide or even within an MSA, there would be far too many households without access to sufficient competition to Verizon for our competitiveness test to act as an effective deterrent to Verizon's potential exercise of market power. A local exchange area, however, is sufficiently small so that we can be reasonably confident that the competitiveness test adopted herein will act as an effective deterrent to the exercise of market power by Verizon for BLETS.

We believe that this market test will deter the exercise of market power in exchanges declared competitive. We have a duty under Subsection G, however, to monitor continually our determinations. For example, if evidence comes to this Commission that Verizon is charging

higher prices for BLETS to customers in an exchange who do not have access to a facilities-based competitor to Verizon than is charged to customers in that exchange who do, that evidence would be relevant to the question of whether Verizon still retains – and is exercising – market power in that exchange.[93] Under Subsection G, this Commission retains the authority to act as it deems necessary in such a situation.

In contrast to Verizon's request for statewide deregulation, we find that the "two competitor" test we adopt herein, as applied to a telephone exchange area, satisfies the statutory requirement for finding that "competition or the potential for competition" can be an effective regulator of price, as set forth in Subsection F, and is more likely to meet Subsection F's injunction that consumers will have options from competitors that "reasonably" meet their needs and that potential competitors will not face substantial barriers to entry.

We also find that this test satisfies the statutory requirement to encourage the offering of competitive products and services as set forth in Va. Code § 56-235.5:1.

Findings of Competitiveness

We find the following exchanges, categorized below by MSA for ease of reference, meet the competitiveness test for residential BLETS outlined herein:

Richmond MSA

- Ashland
- Bethia
- Chester
- Manakin
- Mechanicsville
- Midlothian
- Old Church

[93] Historically, Verizon has offered basic dial tone service (and other BLETS) at the same tariffed price(s) in a given exchange. Therefore, all customers in an exchange are able to obtain service at the same price even if all customers do not have all the same options. While we would expect that the "tariffed" price in an exchange would likely remain uniform at least in the near term, it is possible some customers could receive lower prices under promotions, which would not necessarily raise concern about market power.

- Providence Forge
- Richmond
- Sandston
- Rockville
- Varina

Roanoke MSA

- Roanoke
- Bent Mountain

Virginia Beach-Norfolk-Newport News MSA

- Gloucester
- Great Bridge
- Hayes
- Hickory
- Hampton
- Princess Anne
- Newport News
- Norfolk/Virginia Beach
- Peninsula
- Poquoson
- Portsmouth
- Toano
- Williamsburg

Washington-Arlington-Alexandria MSA

- Alexandria-Arlington
- Braddock
- Engleside
- Fairfax-Vienna
- Falls Church-McLean
- Haymarket
- Herndon
- Independent Hill
- Lorton
- Manassas
- Nokesville
- Occoquan

We have identified these telephone exchanges using various exhibits presented in this proceeding.[94] Our findings of competitiveness for these exchanges, however, do not represent findings that other telephone exchange areas in Verizon's service territory in Virginia do not meet the competitiveness test set forth above. Additional exchanges will be considered on a case-by-case basis under the administrative process outlined herein when and/or if Verizon submits specific tariffs with supporting data formatted and responsive to the competitiveness test described herein for additional exchanges.

We note that the telephone exchanges listed above and found competitive represent collectively approximately 62% – a majority – of Verizon's residential lines in Virginia, as measured by Verizon's total residential access lines.[95]

We further note that, while the evidence in this proceeding demonstrates that each exchange listed above currently meets our competitiveness test, should Verizon merge with, purchase, or be purchased by, a major competitor in any of these exchanges, or if this Commission receives credible evidence that the exchange cited above no longer meets the competitiveness test established herein, we will re-evaluate our findings of competitiveness in the telephone exchanges potentially affected by such events, consistent with our statutory duty under Subsection G to monitor our findings of competitiveness. Should this Commission decide that an exchange area previously declared to be competitive no longer meets our test, such services in that area shall go back to being regulated under Verizon's Alternative Regulatory Plan.

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[94] *See, e.g.,* Exhs. 16C, 17, 18C, 19, 20, 21C, 22C, 23C, 24C, 25, 28, 29, 30C, 31C, 32C, 33C, 34C, 35C, 36C, 37C, 38C, 39C, 40C, 41C, 42C, 43C, 44C, 45C, 94C, 95C, 96C, 170C; Harris, Exh. 188C, Attachment CH-4.

[95] This calculation was derived from Staff Witness Harris' direct testimony, Exh. 188C, Attachment CH-4.

Competitiveness Test for Business BLETS

Large businesses who comprise the so-called "enterprise market" have the purchasing power to attract numerous competitors for their telephone business, and they typically have the legal and financial resources to protect their interests once a contract with a telecommunications provider has been executed. We are concerned, and we believe the General Assembly is equally concerned, about the tens of thousands of small businesses who make up the backbone of Virginia's economy, and who do not have the purchasing power or the legal or financial resources of the largest telephone customers.

Further, CLECs may use T-1 or DS-1 lines to serve small and medium-sized businesses and may provision those by purchasing wholesale special access lines from Verizon or another provider. We found in Case No. PUC-2005-00051 (Verizon-MCI merger case) that Verizon's purchase of MCI would eliminate the largest competitor to Verizon in Virginia for wholesale special access and would thus reduce the competitiveness of the wholesale special access market in Virginia.[96] To mitigate the impact of this significant reduction in competition, we attached a condition to our approval of the Verizon purchase of MCI.[97] We also ruled that this condition would be lifted immediately upon receiving sufficient proof from Verizon that the wholesale special access market in Virginia had become competitive.[98] To date, Verizon has not attempted to prove that the wholesale special access market in Virginia is competitive. In this proceeding,

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[96] *See Joint Petition of Verizon Communications, Inc. and MCI, Inc. for approval of agreement and plan of merger*, Case No. PUC-2005-00051, 2005 S.C.C. Ann. Rept. 260, 268 (October 6, 2005).

[97] The Commission required MCI to "continue to offer to wholesale customers in Virginia its available intrastate and interstate special access, private line or its equivalent, and high capacity loop and transport facilities, without undue discrimination, at pre-merger terms and conditions and at prices that do not exceed pre-merger rates." *Id.*

[98] *Id.*

Verizon acknowledged, however, that the competitiveness of the wholesale special access market affects the retail price of certain business services such as T-1 and DS-1 lines.[99]

Consistent with these concerns, we believe that caution in deregulating business BLETS and OLETS is required. We believe that the test for competitiveness below – and the price caps during the transition period discussed *infra* – will give Virginia's small and medium-sized business customers the ability to protect themselves during the transition to a more competitive telephone market place statewide.

We do not find that "competition or the potential for competition in the market place is or can be an effective regulator of the price"[100] for business BLETS on a statewide basis. Rather, based on the record developed in this case, we find that competition or the potential for competition can be an effective regulator of the price for business BLETS in a telephone exchange area if the competitiveness test below is met. That is, we find that a similar "two competitor" test for competitiveness as established herein for mass market residential BLETS should also apply to the mass market business BLETS offered by Verizon, using the same GMA described above, *i.e.,* telephone exchange area, as follows:

a. A minimum of 75% of the businesses in the telephone exchange area can choose local telephone service from among at least two (2) competitors to Verizon;

b. A minimum of two (2) of the competitors to Verizon in part "a" must offer local telephone service that may be purchased by the business customer without a corresponding requirement to purchase non-telecommunications services (*e.g.*, video or broadband internet service) from that competitor; and

c. At least 50% of the businesses in the telephone exchange area can choose a facilities-based competitor that owns its own wireline network facilities.

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[99] Verizon Witness West, answering question from Commissioner Christie, Tr. at 439.

[100] Va. Code § 56-235.5(F).

The limitations on the competitors that qualify under this test are the same as the limitations found above regarding residential BLETS. For "over the top" VoIP to count as a competitor, broadband penetration, defined as businesses who have purchased a broadband internet service, must be at least 75% in the telephone exchange area.

In addition, for purposes of this business BLETS competitiveness test, the following services are treated as separate business BLETS: (1) Individual Line; (2) PBX Trunk; and (3) Centrex services.[101] Accordingly, the above competitiveness test must be separately applied to each of these three business BLETS in order for that business BLETS to be declared competitive in a telephone exchange. For example, if a specific telephone exchange satisfies the above test for Individual Line service but not for Centrex services, then only Individual Line services can be declared competitive in that exchange.

Findings of Competitiveness

We find the following telephone exchange areas, categorized below by MSA for ease of reference, meet the competitiveness test for Individual Line business BLETS:

Roanoke MSA

- Roanoke

Virginia Beach-Norfolk-Newport News MSA

- Great Bridge
- Hampton
- Newport News
- Norfolk/Virginia Beach
- Peninsula
- Poquoson
- Portsmouth
- Princess Anne
- Williamsburg

[101] Such distinctions can be found in Exh. 13 and in the tariff cited therein by Verizon.

Washington-Arlington-Alexandria MSA

- Alexandria-Arlington
- Braddock
- Engleside
- Falls Church-McLean
- Fairfax-Vienna
- Herndon

We have identified these telephone exchanges using various exhibits presented in this proceeding and tariffs previously filed with the Commission.[102] Our findings of competitiveness for Individual Line business BLETS in these exchanges, however, do not represent findings that other business BLETS in those exchanges, or other telephone exchange areas in Verizon's Virginia service territory, do not meet the competitiveness test set forth above for any of the three separate business BLETS. Additional geographic market areas will be considered on a case-by-case basis under the administrative process outlined herein when and/or if Verizon submits specific tariffs with supporting data formatted and responsive to the competitiveness test described herein for additional exchanges and/or business BLETS.

We also note that the telephone exchanges listed above and found competitive for Individual Line business BLETS collectively represent approximately 57% – a majority – of Verizon's individual business lines in Virginia, as measured by Verizon's total business access lines.[103]

Administrative Process

We do not intend to require Verizon to initiate an entirely new formal proceeding for each telephone exchange area for which it intends to submit evidence that it believes meets the

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[102] *See, e.g.,* Exhs. 16C, 17, 18C, 19, 20, 21C, 22C, 23C, 24C, 25, 28, 29, 30C, 31C, 32C, 33C, 34C, 35C, 36C, 37C, 38C, 39C, 40C, 41C, 42C, 43C, 44C, 45C, 94C, 95C, 96C, 170C; Harris, Exh. 188C, Attachment CH-4.

[103] This calculation was derived from Staff Witness Harris' direct testimony, Exh. 188C, Attachment CH-4. This percentage may be understated because it does not include individual line services purchased by enterprise customers in exchanges not declared competitive.

competitiveness tests for mass market residential and business BLETS that we have set forth in this Order. Rather, Verizon may submit tariffs with supporting data to the Commission's Division of Communications, which will determine administratively if such submissions are in accordance with this Order.

In this regard, we direct the Staff to implement an administrative process by which Verizon may submit tariffs to the Division of Communications it believes meet the competitiveness tests set forth in this Order for each exchange. The process shall include the following requirements: (1) Verizon shall file proposed tariffs with supporting data and an effective date 45 days from the date of filing with the Division for each telephone exchange and applicable services that it requests to be declared competitive;[104] (2) the Division shall accept or reject the proposed tariff(s) within 45 days unless both Verizon and the Division agree to extend the effective date for an additional 45 days; (3) if the Division accepts the proposed tariff(s), the tariff(s) shall go into effect on the initial or extended effective date; (4) if the Division rejects the proposed tariff(s), the Division must notify Verizon of the rejection and describe the reasons for such rejection within 45 days of the date of filing or extension; (5) any tariff(s) rejected by the Division are rejected without prejudice; (6) Verizon may challenge the Division's determination by filing a petition within 30 days of the Division's determination with the Commission pursuant to the Commission's Rules of Practice and Procedure, 5 VAC 5-20-10 *et seq.*; (7) any interested person may challenge the Division's acceptance of a tariff pursuant to the Commission's Rules of Practice and Procedure; and (8) the Commission's website (and any other means deemed

[104] For those BLETS and OLETS in exchanges determined to meet the competitiveness test pursuant to this Order, it is only necessary for Verizon to file the applicable tariff revisions.

appropriate by the Division) shall be used to provide information to the public of each tariff filing by Verizon and the Division's determination.[105]

This administrative process will ensure that Verizon's proposed tariffs are handled in a timely and efficient manner, and that all interested persons have a reasonable opportunity for notice of the filing and determination, as well as an opportunity subsequently to challenge the Division's acceptance or rejection of the tariff pursuant to the Commission's Rules of Practice and Procedure.

Deregulation of Residential and Business BLETS and Price Ceilings in Geographic Market Areas Deemed Competitive

In telephone exchanges determined to be characterized by competition or the potential for competition under the tests set forth above, residential and/or business BLETS shall be deregulated as to price.

To protect *residential* consumers from the possibility of large rate increases for basic telephone service during the transition to a more deregulated, competitive market, we apply the following safeguard, pursuant to Subsection H: The price of residential BLETS as defined herein shall not increase more than one dollar ($1.00) per year, on a per-line basis, during a transition period that shall run from January 1, 2008 through December 31, 2012, or five years.[106]

To protect *business* consumers during the transition to a more deregulated, competitive market, we apply the following safeguard pursuant to Subsection H: The price of business BLETS as defined herein shall not increase more than three dollars ($3.00) per year, on a per-

[105] We expect the Division to make such available as quickly as possible, recognizing that it may be necessary to develop procedures to do so.

[106] We also note that, in reference to a price cap, Verizon Witness Woltz stated as follows: "If you don't believe three years is long enough . . . you could make it five." Tr. at 2186.

line basis, during a transition period that shall run from January 1, 2008 through December 31, 2012, or five years.[107]

To fulfill our statutory monitoring duties discussed below, we direct that Verizon shall continue to file tariffs for residential and business BLETS offered in telephone exchanges determined to be competitive. Verizon shall make such tariff filings in a manner comparable to those for CLECs as set forth in the CLEC regulations.[108]

Finally, we have considered other safeguards proposed by participants in this proceeding for BLETS and for other services, and we find that such additional safeguards are not necessary at this time "to protect consumers and competitive markets" under Subsection H.

OLETS

As noted above, Verizon identifies over 150 OLETS that the Company requests be declared competitive on a statewide basis. As with individual "wireline a la carte" BLETS, Verizon argues that the Commission should not treat individual "wireline a la carte" OLETS as a product market separate and apart from bundled wireline services.[109] As with BLETS, however, we find that individual OLETS represent specific "telephone services" (as that term is used in Subsections E and F) provided to Virginia consumers, and that it is reasonable to apply the standards required in Subsections E and F to individual OLETS. We find that there is insufficient evidence – if any – in the record on each specific OLETS for us to conclude that

[107] The average business BLETS price is approximately three times the residential BLETS price, so this increase represents a comparable increase to the residential BLETS price increase of one dollar per year during the transition period. For example, in the Norfolk-Virginia Beach exchange, the monthly business individual line price is $53.18, and the monthly residential individual line price is $16.37. *See* Verizon Virginia Inc. Local Exchange Services Tariff, S.C.C.-Va.-No. 202, Section 2 at 7, 30c, and 31.

[108] *See* 20 VAC 5-417-10 *et seq.*

[109] *See* Verizon's September 14, 2007 Post-Hearing Brief at 78-80.

competition or the potential for competition in the market place is or can be an effective regulator of the price for each individual OLETS on a stand-alone basis.[110]

OLETS, however, are often provided in association – direct or indirect – with BLETS. In this regard, we find that competition or the potential for competition can be an effective regulator of price for residential and business services designated as OLETS by Verizon in a telephone exchange area for which BLETS (residential or business) has been declared competitive – *if the OLETS is offered by Verizon in association with a BLETS that is declared competitive* (*i.e.*, can only be purchased if the customer already purchases the BLETS). Therefore, if a residential or business BLETS is declared competitive in an exchange under the competitiveness tests above, then we find that an OLETS, offered in association with that competitive BLETS, shall also be declared competitive and price deregulated in that same exchange.

In this regard, based on a review and analysis of Verizon's tariffs on file with the Commission, we find that the following OLETS can be offered in association with the applicable residential and/or business BLETS:[111]

Verizon Virginia - Residential

- Community Choice Plan
- Custom Calling Services
- Call Gate Service
- Call Mover Service
- Do Not Disturb Service

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[110] This discussion of OLETS excludes Directory Assistance Services, which are further addressed below.

[111] An individual OLETS may be associated with only a specific BLETS or in many instances more than one BLETS. This is particularly true for business BLETS since there are several different line products (*i.e.*, individual line, PBX trunk, and Centrex). For example, Break Rotary Hunt may be associated with all three types of business BLETS but will be made competitive only for the specific business BLETS that is made competitive in a given exchange. On the other hand, a service such as Direct Inward Dialing is associated with PBX Trunks, therefore would only be considered competitive in an exchange where PBX trunks are made competitive.

- Fixed Call Forwarding
- FX/FZ/FCO Services
- ISDN-BRI
- Maintenance Visit
- Non-List and Non Published Numbers
- Operator Call Completion Services
- Operator Service – Emergency & Troubles
- Operator Verification
- Operator Verification with Interrupt
- Optional Intercept Arrangements
- Preferred Telephone Number Service
- Remote Call Forwarding
- Repeat Dialing (Busy Redial)
- Select Forward
- 700/900 Blocking
- Temporary Suspension of Service
- White pages additional and bold listings

Verizon Virginia – Business

- Break Rotary Hunt
- Call Gate Service
- Call Mover Service
- Call Screening
- Centrex Extend
- Community Choice Calling Plan
- Custom Calling Services
- Custom Redirect Service
- Direct Inward Dialing
- Fixed Call Forwarding
- Four wire Service Terminating Arrangements
- FX/FZ/FCO
- Home Business Service
- Hunting Arrangement
- Identified Outward Dialing
- Line Side Answer Supervision
- Local Conference Service
- Maintenance Visit
- Make Busy Arrangements
- Messaging Services Interface and Premier Messaging Services Interface
- Non-List and Non Pub Numbers
- Number to Number Referral Service
- Operator Call Completion Services

- Operator Service – Emergency and Trouble
- Operator Verification
- Operator Verification and Interrupt
- Optional Intercept Arrangements
- PBX Night, Sunday, Etc. Arrangement
- Preferred Telephone Number Service
- Remote Call Forwarding
- Repeat Dialing (Busy Redial)
- Select Forward
- Selective Call Screening
- Split Supervisor Drop
- Switched 56 Kilobit Service
- Switched Redirect Service
- Temporary Suspension of Service
- Transfer Arrangements
- Unlimited Local Usage for Business
- White Page Additional and Bold Listings
- Work-At-Home Billing Service

Verizon South - Residential

- Anonymous Call Block
- Automatic Busy Redial
- Automatic Call Return
- Call Forwarding
- Call Tracing
- Call Waiting (all types)
- Caller ID-Name and Number5
- Caller ID – Number
- Calling Number ID/Anonymous Call Rejection
- Customized Number
- Customized Personal Intercept
- Detail Message Billing
- Dial DataLink
- Distinctive Ring
- Do Not Disturb
- Duplicate Bill Charge
- FX/FCO Services
- Intercept
- ISDN- SL and BRI
- Line Status Verification
- Maintenance Visit
- Metro Additive

- Non-List & Non-pub Numbers
- Operator Call Completion Services
- Operator Service- Emergency & troubles
- Operator Verification
- Optional Calling Plans
- Phone Number Referral Service
- Priority Call
- Referral Service
- Reminder Service
- Selective Call Screening
- Service Performance Guarantee
- Three Way Calling
- Toll Restriction Service
- Verification with Call Interrupt
- White Pages Additional Listings & Bold Type

Verizon South - Business

- Anonymous Call Block
- Automatic Busy Redial
- Automatic Call return
- Automatic Line Service
- Call Forwarding
- Call Block
- Call Waiting
- Caller ID-Name & Number
- Caller ID Number
- Caller ID/Anonymous Call Rejection
- Custom Redirect Service
- Custom Routing Service
- Customized Code Restrictions
- Customized Number
- Customized Personal Intercept
- Detail message Billing
- Dial DataLink
- Direct Inward-Outward Dialing Service (DIOD) (only with PBX trunks)
- Direct Inward Dialing (only with trunks)
- Distinctive Ring
- Do Not Disturb
- Duplicate Bill Charges
- Enhanced Call Forwarding
- FX/FCO service
- ISDN- SL & BRI

- Line Status Verification
- Maintenance Visit
- Metro Additive
- Non List & Non pub numbers
- Off premise extensions
- Operator Call Completion Services
- Operator Service- Emergency & Troubles
- Operator Verification
- Optional Calling Plans
- Phone number Referral
- Priority Call Redirect Service
- Referral Service
- Reminder Service
- Remote Call Forwarding
- Selective Call Screening
- Service Performance Guarantee
- Single Line Intercom
- Three Way Calling
- Toll Restriction Service
- Verification with Call Interrupt
- White Pages Additional Listings and Bold Type

We do not find that it is in the public interest to detariff OLETS at this time; rather, the tariff requirements applicable to CLECs under 20 VAC 5-417-50 shall apply to Verizon for OLETS deregulated as to price hereunder. In addition, as required above with BLETS, Verizon shall file revised tariffs, if necessary, for residential and business OLETS applicable in the telephone exchanges determined to be competitive. Verizon shall make such tariff filings in a manner comparable to those for CLECS set forth in the CLEC regulations.[112]

Bundled Services

As noted above, Verizon lists eight bundled services for Verizon Virginia and six bundled services for Verizon South that the Company requests be declared competitive.[113] We

[112] *See* 20 VAC 5-417-10 *et seq.*

[113] *See* Exh. 13.

find that the market for bundled services is characterized by either competition or the potential for competition throughout Verizon's service territory in Virginia. Not only do Verizon's bundled services face competition or the potential for competition from other providers of bundled telephone services in the various geographic market areas of Virginia found to be competitive under the tests we adopt herein, but just as importantly, Verizon's bundled services face pricing constraints in its entire service territory from the pricing of Verizon's individual BLETS and OLETS offerings. We find that the Attorney General's proposal to find bundles competitive only in the four largest MSAs does not account for the pricing constraints on Verizon's bundles from its individually priced and available BLETS and OLETS. We also find that the Attorney General's proposed advertising restrictions are not necessary since we have defined the geographic market area as smaller than an MSA.[114]

Subsection F reads in part:

> *. . . The Commission may also determine bundles composed of a combination of competitive and noncompetitive services to be competitive if the noncompetitive services are available separately pursuant to tariff or otherwise. . .*

We find that competition or the potential for competition in the market place is or can be an effective regulator of the price – on a statewide basis – for Verizon's bundled services. Accordingly, we deregulate bundled services as to price effective immediately throughout Verizon's service territory in Virginia. We do not find, however, that it is in the public interest to detariff these services. Verizon shall continue to file tariffs for bundled services in a manner comparable to the tariff requirements for bundled services contained in the CLEC regulations.[115]

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[114] *See* Attorney General's September 14, 2007 Post-Hearing Brief at 20-23.

[115] *See* 20 VAC 5-417-50.

Enterprise Market Services

The enterprise market can colloquially be described as the "big business" market. Enterprise customers are those which represent a large enough volume of business that they can negotiate their own deal with Verizon or another telephone provider, usually through a competitive bid or procurement process. We find that (i) an appropriate GMA is statewide, and (ii) in the enterprise market, competition exists throughout Verizon's Virginia service territory.[116] Even if a large corporate customer is located or has locations in a rural area, there is no shortage of telecommunications providers willing to compete for what may be a multimillion-dollar account.[117] Enterprise customers also generally have more legal and financial resources with which to protect their interests and enforce their contractual agreements with Verizon than do small business or residential consumers.

We find that competition or the potential for competition in the market place is or can be an effective regulator of the price – on a statewide basis – for telephone services in the enterprise market. For purposes of this Order, we adopt Verizon's definition that "the enterprise market consists of medium-sized and large business customers that typically procure services through a formal or informal competitive procurement or bidding process that solicits multiple bids."[118] We find that the presence of other providers reasonably meeting the needs of these medium-sized and large business customers through a formal or informal competitive procurement or bidding process that solicits multiple bids can serve as an effective regulator of the price for these telephone services.

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[116] *See, e.g.,* Taylor, Exh. 99C at 97-104.

[117] *See, e.g.,* Roycroft, Tr. at 1048-1050.

[118] Verizon's September 14, 2007 Post-Hearing Brief at 73 (citing Calnon, Tr. at 2145).

We also find that it is in the public interest to allow Verizon to offer its services on a contractual basis in the enterprise market on a statewide basis.[119] These contracts would not be regulated under Verizon's Alternative Regulatory Plan. As noted above, however, Subsections G and H require the Commission to "monitor the competitiveness of any telephone service previously found by it to be competitive" and to "adopt safeguards to protect consumers and competitive markets" that "[a]t a minimum . . . ensure that there is no cross subsidization of competitive services by monopoly services." Accordingly, Verizon is ordered: (1) to retain records regarding services provided to customers under contract in the enterprise market; and (2) to make such records and any agreements or contracts available to the Commission's Division of Communications upon request.

Construction Charges

The Staff contends that Verizon's construction charges are not competitive. We do not herein declare such services as competitive and likewise do not deregulate or detariff such charges. Indeed, at the hearing and on brief, Verizon clarified that it "is not seeking to have [construction] services declared competitive."[120]

Directory Assistance

Verizon states that its "Directory Assistance Services ('DAS') enable customers to obtain local telephone numbers and listings of residential and business customers of Verizon, independent companies and CLECs."[121] Verizon asserts that "DAS should be part of the same

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[119] Enterprise customers, however, would not be precluded from purchasing services available pursuant to tariffs.

[120] Verizon's September 14, 2007 Post-Hearing Brief at 15 n.16.

[121] *Id.* at 146. Verizon explains that "[t]hese services include: (1) local directory assistance or '411', which enables customers to obtain assistance in determining telephone numbers and listings of customers who are located in Verizon's service area; (2) Connect Request, which provides local directory assistance customers with the option of having the requested telephone number automatically dialed for them; and (3) List Service, which provides telephone numbers in written form." *Id.* at n.154.

product market as all of its other retail services (BLETS, OLETS and Bundles)" and that "[c]ompetition to provide local exchange service necessarily entails competition to provide related DAS."[122] Verizon also contends that "[e]ven if DAS were a separate product market, however, it should be declared competitive."[123]

We find that DAS is a sufficiently distinct product to warrant treatment by the Commission as a separate "telephone service" under the provisions of the Code set forth above. In this regard, we find that competition or the potential for competition in the market place is or can be an effective regulator of the price – on a statewide basis – for DAS. We also find that, with the exception of the current three free call allowance, it is in the public interest to deregulate the price of DAS on a statewide basis. Specifically, we take judicial notice of our recent proceeding involving widespread errors and omissions in Verizon's directories, both for business and residential listings.[124] While we expect Verizon to do better in the future, to protect consumers, we find that it is reasonable to continue to require Verizon to offer the first three directory assistance calls per month at no cost to the consumer.

Price Floors and Cross-Subsidization

First, we find that the price floor restrictions set forth in Section K 2 of Verizon's Alternative Regulatory Plan shall no longer apply to the services declared competitive pursuant to this Order. As argued by Verizon, the price floor requirement does not apply to any of Verizon's competitors.[125] In addition, since the residential and business market test requires

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[122] *Id.* at 146-147.

[123] *Id.* at 147.

[124] *See Commonwealth of Virginia, ex rel. State Corporation Commission, Ex Parte: In the Matter of Investigating Directory Errors and Omissions of Verizon Virginia Inc. and Verizon South Inc.*, Case No. PUC-2005-00007, Order Approving Offer of Settlement (February 13, 2007).

[125] *See* Verizon's September 14, 2007 Post-Hearing Brief at 197.

there to be a facilities-based carrier serving at least 50% of households or businesses in an exchange, we believe that the price floor requirement is no longer warranted because Verizon's ability to exercise market power has been greatly diminished and it should be allowed to respond adequately to pricing signals from other competitors. We note that the significantly lowered intrastate switched access charges of both Verizon and the CLECs are an important component in this assessment as well.

Next, Subsection H requires the Commission to "adopt safeguards to protect consumers and competitive markets. At a minimum these safeguards must assure that there is no cross subsidization of competitive services by monopoly services." To be sure, and as explained by the Company, "Verizon is not asking the Commission to totally eliminate prohibitions on cross-subsidies, as it cannot change the Code."[126] Indeed, cross-subsidy prohibitions apply to both ILECs and CLECs and shall continue to apply to Verizon. Verizon notes that the Commission's CLEC rules, at 20 VAC 5-417-60(E), state as follows:

> Should the commission determine that a new entrant has a monopoly over any of its services, whether or not those services are telephone services, it may order the new entrant to file annually with the Division of Communications data to demonstrate that its revenues from local exchange telecommunications services cover the long run incremental costs of such services in the aggregate.[127]

Based on Verizon's position as the largest provider of telephone services in the Commonwealth, along with our removal of Verizon's current price floor requirement for competitive services in exchanges that are determined to be competitive, we find that it is reasonable – and a minimum safeguard to "ensure that there is no cross subsidization of competitive services by monopoly services" as required by Subsection H – to require Verizon to

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[126] *Id.* at 198.

[127] *Id.* at n.235 (quoting 20 VAC 5-417-60(E)).

continue to file annually with the Division of Communications data to demonstrate that its revenues from competitive local exchange telecommunications services in the aggregate cover the direct incremental costs of such services, as it is currently required to do under Section K 3 of its Alternative Regulatory Plan.

Future Proceeding to Monitor the Status of Competition

Subsection G states:

> *The Commission shall monitor the competitiveness of any telephone service previously found by it to be competitive under any provision of subsection F above and may change that conclusion, if, after notice and opportunity for hearing, it finds that competition no longer effectively regulates the price of that service.*

To fulfill our statutory duty under this provision, we intend to initiate a proceeding on or before March 1, 2012. This proceeding will take place prior to the removal of the price caps on mass market residential and business BLETS in those telephone exchange areas previously found to meet the competitiveness tests for residential and business BLETS set forth in this Order and deregulated. We agree with Verizon that the telecommunications market is dynamic, not static. This future proceeding will give the Commission and all interested parties and the public an opportunity to review the status of the telecommunications market in Virginia at that time, to review the economic and technological changes that will undoubtedly have taken place during the next four years, and to make any changes deemed appropriate to the findings, conclusions and directions contained in this Order or any subsequent order on this topic, as well as any tariffs accepted under the administrative process established herein. It will provide one additional and essential layer of protection for Virginia's telephone consumers prior to moving into a much more extensively deregulated telephone market place.

Intrastate Switched Access Charges

Ensuring reliable, easy and low-cost interconnection of calls between competing providers is an essential element of promoting competitive offerings from all telecommunications providers, as Va. Code § 56-235.5:1 requires us to do. We acknowledge the testimony from Sprint Nextel that the issue of Verizon's intrastate switched access charges needs to be addressed.[128] While the specific cost levels of Verizon's intrastate access charges are not before us in this proceeding, we find that as we move towards a much more competitive and deregulated telecommunications market in Virginia, the access charge levels of Verizon and other ILECs in Virginia should be reviewed and, where and if found appropriate, access charges should be adjusted, to promote increased competition. Accordingly, we subsequently will initiate an appropriate regulatory proceeding to review the intrastate access charges currently charged by Verizon Virginia and Verizon South.[129]

Service Quality Rules

The Staff raised a concern in this case with regard to the continued applicability of the Commission's service quality rules and the Commission's continued oversight of service quality under § 56-247 of the Code.[130] In addition, CWA asserted that "there are service quality problems under the current form of regulation, and so it is extremely difficult to conclude that deregulation will result in improved service quality" and that "[m]arket forces alone cannot protect all classes of customers from poor service, and therefore the Commission should continue to regulate service quality to protect customers from further deterioration of service quality and

[128] *See* Appleby, Exh. 133.

[129] We take judicial notice of the recent proceeding initiated by Sprint Nextel to lower Embarq's intrastate access rates. *See* Case No. PUC-2007-00108. Thus we do not need to, in this Order, direct a review of Embarq's access rates.

[130] *See* Bradley, Exh. 187P at 4.

escalating rates."[131] Verizon, however, acknowledges that the Commission "could simply clarify in its Order in this case that [service quality] rules continue to apply to specific detariffed services until it expressly rules otherwise.[132] Because we have not detariffed any of Verizon's services herein, the Commission's service quality rules will continue to apply to Verizon.

Furthermore, Verizon states that even if the Commission granted Verizon the relief it seeks in this proceeding, "the Commission would retain its broad authority to review the market and any complaints over Verizon's rates or services, and take corrective action should the market fail to protect either consumers or competitors[,]" and, "[l]ikewise, the Commission would retain authority to enforce its generic rules applicable to public service companies and local exchange carriers."[133] Indeed, the Commission's rules on service quality will continue to apply to Verizon, and Verizon will still be subject to the Commission's broad authority to enforce Verizon's basic statutory duties by taking corrective action in the event that market forces fail to provide sufficient protections.[134]

Verizon's Alternative Regulatory Plan

Services declared competitive pursuant to this Order are no longer regulated under Verizon's Alternative Regulatory Plan. Such services shall remain tariffed consistent with the rules for CLECs, and so that this Commission can fulfill its statutory duties under Subsection G. In addition, services previously classified as competitive under Verizon's Alternative Regulatory Plan are no longer subject to such plan. All future tariff filings for previously classified

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[131] CWA's September 12, 2007 Post-Hearing Brief at 18.

[132] Verizon's September 14, 2007 Post-Hearing Brief at 186 n.222.

[133] *Id.* at 186 (citing Va. Code §§ 56-235.5(G) and 56-247) (footnote omitted).

[134] *See, e.g.*, Va. Code §§ 56-234 and 56-235.

competitive services shall be made in a manner consistent with the CLEC regulations, although the present tariffing status shall remain unchanged for such services.

Provider of Last Resort

Finally, we clarify that nothing in this Order modifies Verizon's statutory and regulatory obligations as the provider of last resort in its service territory, and we note that Verizon has not requested otherwise.

Accordingly, IT IS HEREBY ORDERED THAT:

(1) The Application is granted in part and denied in part as set forth herein.

(2) Retail services of Verizon Virginia and Verizon South are declared competitive and deregulated as set forth herein.

(3) This matter is dismissed.

AN ATTESTED COPY hereof shall be sent by the Clerk of the Commission to all persons on the official Service List in this matter. The Service List is available from the Clerk of the State Corporation Commission, c/o Document Control Center, 1300 East Main Street, First Floor, Tyler Building, Richmond, Virginia 23219.

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