IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

Nos. 00-1012, *et al.*, & 00-1015, *et al.*

UNITED STATES TELECOM ASS'N, *et al.,*

PETITIONERS,

v.

FEDERAL COMMUNICATIONS COMMISSION
and UNITED STATES OF AMERICA,

RESPONDENTS.

ON PETITIONS FOR REVIEW OF ORDERS OF THE
FEDERAL COMMUNICATIONS COMMISSION

PETITION FOR REHEARING OR REHEARING *EN BANC*

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July 8, 2002

CERTIFICATE AS TO PARTIES, RULINGS, AND RELATED CASES

(A) PARTIES and AMICI

Because this case involves direct review of informal rulemakings, a list of parties appearing before the Commission is not supplied.

The parties appearing before the Court in Case Nos. 00-1012, 01-1075 and 01-1103 are:

Petitioner in No. 01-1012 is the United States Telecom Association ("USTA").

Petitioner in No. 01-1075 is SBC Communications Inc.

Petitioners in 01-1103 are the Verizon telephone companies.

Respondents in these cases are the Federal Communications Commission ("Commission") and the United States of America.

Intervenors in these cases are:

Association of Communications Enterprises
Association for Local Telecommunications Services
AT&T Corporation
Bell Atlantic telephone companies (now Verizon telephone cos.)
(in No. 01-1012)
BellSouth Corporation
Birch Telecom, Inc.
Competitive Telecommunications Association
Covad Communications Co.
GTE entities (now Verizon telephone cos.) (in No. 01-1012)
ICG Communications, Inc.
Network Access Solutions Corporation
Qwest Corporation
Rhythms NetConnections, Inc.
Sprint Corporation
WorldCom Inc.

The parties appearing before the Court in Case Nos. 00-1015 and 00-1025 are:

Petitioner in No. 00-1015 is the United States Telecom Association ("USTA").

Petitioner in No. 00-1025 is Qwest Communications International Inc.

Respondents in these cases are the Federal Communications Commission (Commission") and the United States of America.

Intervenors in these cases are:

Association for Local Telecommunications Services
AT&T Corporation
Bell Atlantic telephone companies (now Verizon telephone companies)
BellSouth Corporation
CO Space Services, LLC
GTE entities (now Verizon telephone companies)
ICG Communications, Inc.
MCI WorldCom, Inc. (now WorldCom Inc.)
MGC Communications, Inc. d/b/a Mpower Communications Corp.
Network Access Solutions Corporation
Qwest Corporation
Rhythms NetConnections, Inc.
SBC Communications Inc.
Telecommunications Resellers Association (now Association of Communications Enterprises)

(B) RULINGS BEFORE THE COURT:

Deployment of Wireline Services Offering Advanced Telecommunications Capability, 14 FCC Rcd 20912 (1999) ("*Line Sharing Order*"), on reconsideration, 16 FCC Rcd 2101 (2001) ("*Line Sharing Reconsideration Order*"); *Implementation of the Local Competition Provisions of the Telecommunications Act of 1998,* 15 FCC Rcd 3696 (1999) (the "*Local Competition Order*").

(C) RELATED CASES

The orders under review have not previously been before this Court. Counsel are not aware of any related cases that are pending before this Court or any other courts.

**STATEMENT OF THE ISSUE
AND ITS IMPORTANCE**

In *United States Telecom Ass'n v. FCC*, 290 F.3d 415 (D.C. Cir. 2002) ("*USTA*"), a panel of this Court set aside two Federal Communications Commission orders implementing provisions of the Telecommunications Act of 1996 that direct the Commission to "determin[e] what network elements" incumbent local exchange carriers ("incumbent LECs" or "ILECs") must make available for lease to new competitive LECs ("CLECs"). 47 U.S.C. § 251(d)(2); *see* § 251(c)(3).[1] The FCC and the United States respectfully move for rehearing or rehearing *en banc* of the panel's May 24, 2002 decision. The Court should grant rehearing in this case, which is of unquestioned national importance to the FCC's ongoing implementation of the 1996 Act's local competition provisions, to correct two errors.

First, the panel's decision is, at a minimum, fundamentally in tension with recent and pertinent Supreme Court authority dealing with closely related substantive requirements of the 1996 Act. Less than two weeks before the panel issued its decision in this case, the Supreme Court, in *Verizon Telephone Cos. v. FCC*, 122 S.Ct. 1646 (2002) ("*Verizon*"), had affirmed the FCC's "TELRIC" methodology for determining the cost-based prices that incumbent LECs may charge new competitive LECs for access to the unbundled network elements ("UNEs") that are the subject of this case. *See* 47 U.S.C. § 252(d)(1). Finding the pertinent language of the statute to be ambiguous, the

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[1] *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, Third Report and Order and Fourth Further Notice of Proposed Rulemaking, 15 FCC Rcd 3696 (1999) ("*Local Competition Order*"); *Deployment of Wireline Services Offering Advanced Telecommunications Capability, et al.*, Third Report and Order in CC Docket No. 98-147 and Fourth Report and Order in CC Docket 96-98, 14 FCC Rcd 20912 (1999) ("*Line Sharing Order*").

Court applied the deferential review standards of *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 843-45 (1984), to afford the FCC broad discretion to implement the pro-competitive goals of the 1996 Act. The Court dismissed conflicting economic theories on the likely impact of the Commission's network element pricing rules on investment incentives as "the stuff of debate for economists and regulators, [rather than judges]," and the Court emphasized that its role on review was limited to determining *not* whether the Commission "picked the best way" to implement the statute but whether it "made choices reasonably *within the pale of statutory possibility*." *Verizon*, 122 S.Ct. at 1687 (emphasis added).

The decision of the panel in this case stands in marked contrast to the Supreme Court's decision in *Verizon* and this Court's decisions in other cases applying the judicial review principles of *Chevro*n. Here, the panel overstepped the bounds of proper judicial review by reading section 251(d)(2) to curtail the FCC's discretion on the basis of virtually the same highly contested economic assumptions that the Supreme Court in *Verizon* had held not to foreclose the availability of UNEs at prices based on TELRIC costs. *Compare USTA*, 290 F.3d at 422, 424-25, 427, 429, *with Verizon*, 119 S.Ct. at 1167 n.20, 1672 & n.27, 1675-76 & n.33. This error alone compels rehearing.

Second, the panel's decision also requires rehearing because it can be read to establish, on the basis of a misreading of the Supreme Court's decision in *AT&T Corp. v. Iowa Utilities Board*, 252 U.S. 366 (1999), an unwarranted restriction on the FCC's implementation of the Act's network element provisions that is, at a minimum, in tension with other provisions of the 1996 Act. The panel's strong implication that a new entrant cannot be "impaired" in the provision of services unless the element at issue has "(in some degree) ... natural monopoly" characteristics, *USTA*, 290 F.3d at 427, is not compelled by the statutory text. Moreover, such a limitation would be inconsistent with the "necessary" standard in section 251(d)(2)(A) and the section 271 "competitive checklist" for Bell company entry into the long-distance market. The panel's assumption that the Act also requires that implicit retail cross-subsidies must be given weight in determining impairment is inconsistent with the universal service reform provisions of section 254.

BACKGROUND

1. Section 251(d)(2) provides, in pertinent part:

> In determining what network elements should be made available ..., the Commission shall consider, at a minimum, whether --
>
> * * *
>
> (B) the failure to provide access to [nonproprietary] network elements would *impair* the ability of the telecommunications carrier seeking access to provide the services that it seeks to offer.

47 U.S.C. § 251(d)(2) (emphasis added).

In *Iowa Utilities Board*, the Supreme Court remanded the FCC's first attempt to construe section 251(d)(2), because the Commission had made two interpretive errors regarding the proper standard for non-proprietary network elements: (1) it improperly had excluded consideration of a requesting carrier's ability to self-provision a network element or to obtain it from other non-ILEC sources, 525 U.S. at 389; and (2) it improperly had "assum[ed] that *any* increase in cost (or decrease in quality) imposed by denial of a network element ... causes the failure to provide that element to 'impair' the entrant's ability to furnish its desired services." 525 U.S. at 389-90 (emphasis added). In light of these errors, the Court remanded to the FCC the task of "determin[ing] on a rational basis which network elements must be made available, taking into account the objectives of the Act and giving some substance to the ... 'impair' requirement[]." 525 U.S. at 391-92. The Court expressed *no* view about whether the Commission on remand could compel access to the same network elements that were included on its initial list under a proper application of the statutory unbundling standard. 525 U.S. at 392.

In a separate opinion concurring in the result with respect to unbundling (and dissenting in certain other respects), Justice Breyer asserted that "compulsory sharing can have significant administrative and social costs inconsistent with the Act's purposes," including "diminish[ing]" incentives of both incumbents and new entrants to invest in network facilities. 525 U.S. at 428-29. He concluded that the 1996 Act did not permit the FCC to interpret "the definition of what must be shared [to extend] beyond that which is *essential*." 525 U.S. at 430 (emphasis added). No other member of the Court joined in Justice Breyer's separate opinion.

2. In the orders on review here, issued following the *Iowa Utilities Board* remand, the FCC adopted a new unbundling standard designed to implement section 251(d)(2) in light of the Supreme Court's opinion. 47 C.F.R. § 51.317. Under the revised unbundling standard, the Commission *first* must determine whether lack of access to a (non-proprietary) network element would "impair" the requesting carrier's ability to provide the services it seeks to offer. "A requesting carrier's ability to provide service is 'impaired' if, *taking into account the availability of alternative elements outside the incumbent LEC network*, ... lack of access *materially diminishes* a requesting carrier's ability to provide the services it seeks to offer." 47 C.F.R. § 51.317(b)(1) (emphasis added). *Second*, in determining whether a requesting carrier's ability to provide service is "materially diminish[ed]" by the lack of access to a network element, the Commission compares ILEC network elements with alternative elements from other sources in light of relative cost, relative timeliness of deployment, relative quality, relative ubiquity, and relative impact on network operations. 47 C.F.R. § 51.317(b)(2).[2]

The FCC concluded that the impairment inquiry "cannot" practicably be conducted for "every potential carrier seeking access to each network element on a case-by-case basis." *Local Competition Order*, para. 54 & n.98; *see also id.*, para. 65. The Commission, however, did tailor UNE requirements to take account of geographic and customer segment limitations where the record warranted. *See Local Competition Order*, paras. 276-78 (establishing geographic and customer segment limitations on the availability of the switching element). Overall, the application of the revised unbundling standard, including but not limited to the "impairment" analysis, led the FCC to specify a revised list of network elements that is in some respects narrower and in other respects broader than the original list the Commission had promulgated. *See USTA*, 290 F.3d at 420-21.[3]

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[2] Section 251(d)(2) requires the FCC to consider impairment "at a minimum," and the revised unbundling standard also permits the FCC to take into account the effect of unbundling on the Act's goals: (i) the rapid introduction of competition; (ii) facilities-based competition, investment, and innovation; (iii) reduced regulation; (iv) market certainty; and (v) administrative practicality. 47 C.F.R. § 51.317(b)(3).

[3] Recognizing that market conditions would change over time, the FCC promised to revisit its unbundling determinations in three years. *Local Competition Order*, para. 15. The Commission currently is following up on that commitment in its *Triennial Review* proceeding, where the agency "seek[s] to ensure that our regulatory framework remains current and faithful to the pro-competitive, market-opening provisions of the 1996 Act in light of our experience over the last two years, advances in technology, and other developments in the markets for telecommunications services." *Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers* (CC Docket Nos. 01-338, 97-98, and 98-147), FCC 01-361, Notice of Proposed Rulemaking, para. 2 (December 20, 2001) ("*Triennial Review*").

3. On review, the panel remanded the *Local Competition Order* and vacated and remanded the *Line Sharing Order*, finding two facets of the FCC's decisions unlawful: (1) the Commission's analysis of cost disparities as they relate to impairment, and (2) the Commission's adoption (with respect to most but not all network elements) of uniform national unbundling obligations that apply across geographic markets and customer classes. *USTA*, 290 F.3d at 422-28.

First, the panel held that "[a] cost disparity approach that links 'impairment' to universal characteristics [faced by start-up companies in many industries], rather than one linked (in some degree) to natural monopoly," is inconsistent with the statute. *Id.* at 427. The Court concluded that the Commission's standard was unlawful, because it permits reliance on differences between ILEC and CLEC scale economies that exist "*in the early stages of entry*" even if there may be no scale economies "'*over the entire extent of the market.*'" *Id.* (quoting 2 Alfred E. Kahn, *The Economics of Regulation: Principles and Institutions* 119 (1989)) (emphasis supplied by Court).

Second, with respect to uniform national unbundling obligations, the panel read the Supreme Court's holding in *Iowa Utilities Board* as "requiring a more nuanced concept of impairment" than the FCC had adopted in response to that holding. *USTA*, 290 F.3d 425-26. Specifically, the panel faulted the FCC for allegedly requiring unbundling "in many markets where there is no reasonable basis for thinking that competition is suffering from any impairment of the sort that might have [been] the object of Congress's concern." *USTA*, 290 F.3d at 422. The panel particularly criticized the FCC for not taking into account “market-specific variations in competitive impairment [that result from] the cross-subsidization [of ILEC retail rates] often ordered by state regulatory commissions, typically in the name of universal service." *USTA*, 290 F.3d at 422. Relying heavily on the economic assumptions asserted in Justice Breyer's separate opinion in *Iowa Utilities Board*, the panel rejected the FCC's conclusion that nationwide rules would help advance congressional goals, among other things, by encouraging rapid competitive entry in local telephone markets, as well as investment in facilities-based competition by both new entrants and incumbents. *USTA*, 290 F.3d at 424-25.

ARGUMENT

The Court should grant rehearing with respect to both the *Local Competition Order* and the *Line Sharing Order* because (1) the panel's discussion of the effect of UNE availability and pricing is, at a minimum, fundamentally in tension with the Supreme Court's decision in *Verizon* and general principles of *Chevron* review, and (2) limitations that the panel's decision can be read to impose have no basis in the statutory text and appear to be inconsistent with several provisions of the 1996 Act.

1. The panel properly sought to determine whether the Commission, in implementing the "necessary" and "impair" standards of section 251(d)(2), had applied "some limiting standard, rationally related to the goals of the Act" and had responded to the Supreme Court's skepticism that Congress meant for the Commission to provide "blanket access to incumbents' networks" on an unrestricted basis. *See Iowa Utilities Board*, 525 U.S. at 390. In doing so, however, the panel ran afoul of the Supreme Court's admonition in *Verizon* that reviewing courts have a properly limited role under the principles of *Chevron*, 467 U.S. at 843-45, especially in a case like this one involving disputed economic arguments and a complex technical and regulatory background.

Moreover, the panel adopted specific economic and policy assumptions that the Supreme Court itself in *Verizon* specifically rejected as a basis for imposing limitations on incumbents' obligations to make network elements available to requesting carriers at cost-based prices.

First, faced with evidence of significant real-world competitive investment under the existing unbundling regime, the *USTA* panel opined that the FCC had an obligation to confront the issue of "how such investment compares with what would have occurred in the absence of the prospect of unbundling." *USTA*, 290 F.3d at 425. By contrast, addressing essentially the same argument in *Verizon*, the Supreme Court did not require the FCC to prove that its choice will maximize facilities investment. Rather, the Court stated: "We, of course, have no idea whether a different … scheme would have generated even greater competitive investment…, but it suffices to say that a regulatory scheme that can boast such substantial competitive capital spending … is not easily described as an unreasonable way to promote competitive investment in facilities." *Verizon*, 122 S.Ct. at 1675-76. *See also id.* at 1678-79, 1685 (noting that it is the petitioner that bears the burden of demonstrating that the agency's interpretation of its governing statute is unreasonable).

Second, the panel assumed that network element unbundling requirements necessarily will create investment disincentives for both incumbents and new entrants. *USTA*, 290 F.3d at 427 ("each unbundling of an element imposes costs of its own, spreading the disincentive to invest in innovation"). *See also id.* at 424-25, 429. By contrast, the Supreme Court in *Verizon* held that the Commission could reasonably conclude that network element unbundling at rates set in accordance with TELRIC would *encourage* investment by both types of carriers. *See Verizon*, 122 S.Ct. at 1667 n.20, 1672 & n.27, 1675-76 & n.33. The Court recognized that the availability of costly-to-duplicate network elements at TELRIC prices could "avoid the risk of keeping more potential entrants out," while "induc[ing] them to compete in less capital-intensive facilities." 122 S.Ct. at 1672 n.27. And so long as such a regime "brings about some competition, the incumbents will continue to have incentives to invest and to improve their services to hold on to their existing customer base." *Id*. at 1676 n.33.

Third, the panel assumes that a TELRIC-based price for a network element is a “price below true cost” that will exacerbate the perceived investment disincentives of unbundling. *USTA*, 290 F.3d at 424. But the Supreme Court had just upheld TELRIC as a reasonable measure of the incumbent’s economic cost of providing a network element -- one that would encourage new entrants to make efficient decisions whether to lease or build and spur ILEC and CLEC investment. *See Verizon*, 122 S.Ct. 1676 n.33, 1687; *see also id.*at 1673 (“[a]ny ... cost difference [between historic cost and TELRIC] is an inefficiency”).

Although the Supreme Court's treatment of each of these parallel arguments in *Verizon* arose on review of TELRIC pricing for UNEs rather than of the FCC’s standards for specifying required UNEs, the underlying analysis is the same. The Supreme Court has recognized -- and, indeed, it is a matter of common sense -- that "[r]ates ... do not exist in isolation. They have meaning only when one knows the services to which they are attached." *American Telephone and Telegraph Co. v. Central Office Telephone, Inc.*, 524 U.S. 214, 223 (1998). The panel’s insistence on its economic assumptions with respect to network element unbundling is, at a minimum, in tension with the Supreme Court's deference to the FCC's analysis of network element pricing in *Verizon*.

This Court could resolve the tension between *USTA* and *Verizon* on rehearing by following the well-established *Chevron* step 2 analysis, 467 U.S. at 843-45, that was the basis for the Supreme Court's decisions in *Verizon* and *Iowa Utilities Board*:

> Whether the FCC picked the best way to set [UNE] rates is the stuff of debate for economists and regulators versed in the technology of telecommunications and microeconomic pricing theory. The job of judges is to ask whether the Commission made choices *reasonably within the pale of statutory possibility* in deciding what and how items must be leased and the way to set rates for leasing them.

Verizon, 122 S.Ct. at 1687 (emphasis added). Similarly, shortly *after* the *USTA* panel's decision, a different panel of this Court applied *Chevron* step 2 review in another closely related case involving the Commission's construction of the statutory obligation of incumbents to permit the physical collocation of equipment "necessary for … access to unbundled network elements." 47 U.S.C. § 251(c)(6). Declining to undertake the "freewheeling policy inquiry that *Chevron* deference was crafted to avoid," a different panel of this Court explained that "we 'defer to the Commission's interpretations if they are reasonable and consistent with the statutory purpose.' … Our deference is particularly great where, as here, the issues involve 'a high level of technical expertise in an area of rapidly changing technological and competitive circumstances.'" *Verizon Telephone Companies v. FCC*, D.C. Circuit Nos. 01-1371, *et al.*, slip op. at 9, 11 (June 18, 2002) (citations omitted).

By contrast -- even though the *USTA* panel acknowledged the "extraordinary complexity" of the Commission's task of implementing the network element unbundling provisions and the fact that Congress had given it "no detail" as to how to carry out that task, 290 F.3d at 421-22 -- the panel stepped directly into the “debate for economists and regulators” and engaged in precisely the kind of “freewheeling policy inquiry” that *Chevron* forbids.

2. Rehearing is also compelled because two aspects of the panel's decision (relevant cost disparities and retail cross-subsidies) reflect a misreading of the Supreme Court's *Iowa Utilities Board* decision and can be read to conflict with provisions of the 1996 Act.

a. The panel's discussion of relevant cost disparities -- while stopping just short of holding that the statutory impairment standard necessarily incorporates the "essential facilities doctrine" from antitrust law -- can be read to discount entirely the relevance of cost disparities that do not reflect "natural monopoly" characteristics, *i.e.,* declining average costs over the entire range of the market. *USTA*, 290 F.3d at 426-28. The panel appears to draw this conclusion from its view that the Supreme Court, in *Iowa Utilities Board*, had "implicitly" adopted the economic assumptions articulated in Justice Breyer's separate opinion. *USTA*, 290 F.3d at 427. But no other member of the Supreme Court joined Justice Breyer's opinion and the panel's reading finds no support in the statutory text.

First, reading "impairment" to turn on natural monopoly-related cost disparities creates an inconsistency within section 251(d)(2). That provision contains different standards for unbundling proprietary and non-proprietary elements -- a strict "necessary" standard for the former (section 251(d)(2)(A)) and a less stringent "impair" standard for the latter (section 251(d)(2)(B)). Almost by definition, sustainable competitive provision of service in the face of a natural monopoly is likely impossible without unbundling or other regulatory intervention. Thus, requiring unbundling of non-proprietary elements only where such monopoly exists would mean that entrants would not merely be "impaired" without access to the UNEs; those UNEs also would be "necessary" (*i.e.*, indispensable) to the entrant's efforts to provide service in competition with the incumbent natural monopolist. In other words, the linking of impairment to natural monopoly would appear to leave no distance between those distinct standards.

Moreover, read to suggest that unbundling must turn on natural monopoly cost characteristics, the panel's decision is in tension with section 271. Section 271's "competitive checklist," which Bell incumbents must satisfy in order to enter the long-distance market, includes requirements that the Bells grant access, not only to the loop (an element that is widely agreed to have natural monopoly characteristics), but also to transport, switching, and signaling (which some parties say do not have such characteristics). *See* 47 U.S.C. §§ 271(c)(2)(B)(iv), (v), (vi), & (x). The inclusion of these elements on the competitive checklist -- as well as the limitation on the FCC's authority to forbear from enforcing the checklist until the requirements of section 271 have been "fully implemented" (47 U.S.C. § 160(d)) -- suggests at a minimum that Congress viewed such unbundling as having competitive benefits warranting consideration by the FCC, not (absent natural monopoly characteristics) as being merely a cost to be "inflict[ed] on the economy." *Compare USTA,* 290 F.3d at 429.

Finally, the panel misreads *Iowa Utilities Board* to the extent that it relies on that decision to suggest that the Commission must adopt some kind of natural-monopoly limitation on the impairment analysis. Contrary to the panel's apparent view, when the

Supreme Court in *Iowa Utilities Board* rejected the FCC's initial unbundling standard (which had equated impairment with "any" cost disparity), the Court appeared to suggest that it would be open to a *quantitative* (as opposed to *qualitative*) measure of cost disparities. In other words, a large cost disparity (whether indicative of natural monopoly or not) might be probative of impairment, while a small cost disparity might not. Such a reading follows from the Supreme Court's acknowledgment that, while the telecommunications industry is not characterized by "perfect competition," if it were perfectly competitive, any "increased cost" would equate with impairment. *Iowa Utilities Board*, 525 U.S. at 390. And it is confirmed in the *Verizon* opinion, which explains that the *Iowa Utilities Board* Court had faulted the Commission for requiring incumbents "to lease any network element that might reduce, *however slightly*, an entrant's marginal cost of providing a telecommunications service." *Verizon*, 122 S.Ct. at 1669 (emphasis added).[4] The panel's contrary reading derives entirely from its erroneous view that the *Iowa Utilities Board* majority "implicitly" (290 F.3d at 427) had adopted the very same assumptions of Justice Breyer about investment incentives that the Court, in *Verizon*, said the FCC was entitled to reject. *Compare Iowa Utilities Board*, 525 U.S. at 428-30 (opinion of Breyer, J.), *with Verizon*, 122 S.Ct. at 1667 n.20, 1672 & n.27, 1675-76 & n.33, 1687.

[4] The *Verizon* decision also confirms the absence of a natural monopoly limitation by acknowledging that the availability of UNEs at cost-based prices is particularly needed in order to reduce entry barriers for "the hundreds of *smaller entrants* (without the resources of a large competitive carrier such as AT&T or Worldcom)." 122 S.Ct. at 1672 n.27 (emphasis added); *see also id.* at 1668 n.20. As the panel recognized, natural monopoly is tied to economies of scale "*over the entire extent of the market*," not to the cost characteristics of particular entrants. *USTA*, 290 F.3d at 427 (citation omitted) (emphasis in original).

b. The panel's discussion of retail cross-subsidies can be read to curtail, if not effectively to preclude, findings of impairment while implicit universal service subsidies remain in incumbents' retail rates.[5] But the 1996 Act does not permit, much less require, the FCC to protect the "cross subsidies in aid of universal service" that characterized the old Bell System monopoly. *See Verizon*, 122 S.Ct. at 1656. To the contrary, the Supreme Court in *Iowa Utilities Board* expressly rejected the argument that the 1996 Act's unbundling provisions should be limited in ways not supported by the statutory text in order to prevent incumbents from being left "holding the bag for universal service." *Iowa Utilities Board*, 525 U.S. at 393-94. Providing subsidies that may be needed to support universal service is the function of section 254, not section 251. *Id*.

A broad interpretation of the panel's holding would conflict with the more sensible and natural reading of how section 251(c) relates to section 254. Congress understood that competition flowing from implementation of section 251(c) -- including the obligation of ILECs to offer unbundled network elements -- would be a driving force in subsequently removing implicit subsidies from retail rates so that universal service could be preserved entirely through explicit subsidies that are sustainable in a competitive environment. *See generally Federal-State Joint Board on Universal Service* (CC Docket No. 96-45), 12 FCC Rcd 8776, 87-85 (para. 14) (1997), *aff'd in pertinent part*, *Texas Office of Public Utility Counsel v. FCC*, 183 F.3d 393 (5th Cir. 1999); *Southwestern Bell Telephone Co. v. FCC*, 153 F.3d 523, 536-37 (8th Cir. 1998). A broad reading of the

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[5] The panel questions how impairment can occur in areas where incumbent retail rates are below cost, since "any competition will be wholly artificial." *USTA*, 290 F.3d at 422. And the panel suggests that, in areas where ILEC retail rates are above cost, the FCC should view as a CLEC cost advantage the contributions that the ILEC's above-cost rates make to subsidized rates in other areas. *Id*. at 422-23.

court's discussion of retail cross-subsidies and impairment would appear effectively to reverse that sequence -- in some cases precluding unbundling until cross-subsidies are removed. Reading the statute to require such a reversal in sequence would be particularly irrational because the States rather than the FCC have direct authority to regulate ILEC retail rates. *See* 47 U.S.C. § 152(b).

CONCLUSION

For the foregoing reasons, this Court should grant rehearing, or in the alternative, rehearing *en banc.*

Respectfully submitted,

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