Supplement to Verizon Symposium Comments

This paper supplements Verizon's previous submission regarding the state of video competition and responds to the Department's follow-up questions. First, it demonstrates that, despite improvements in the past year, the local franchising process continues to pose barriers to entry. Second, it describes Verizon's pricing for its FiOS services. Third, it shows that Verizon's term and package discounts for video services are highly valued by consumers and promote competition.

A. The Local Franchising Process Is Anticompetitive

The Department notes that a Wall Street Journal article reported Verizon has deployed FiOS to a greater percentage of homes in Cablevision's territory (25 percent), which lies mostly in New York where there is no state law making it easier to obtain cable franchises, than in Comcast's and Time Warner's territories (4 percent), which lie partly in states that have enacted laws simplifying and expediting franchise approvals. The Department asks, "[g]iven these statistics, how big of a barrier to entry is the local franchising process," and asks whether there are "statistics showing that your entry is faster in states with state franchising laws than in those without such laws."

As an initial matter, Verizon is willing to provide to the Department on a confidential basis the numbers of lines of FiOS TV it has deployed and is deploying on a state-by-state basis. Those numbers show that Verizon has sought to deploy its competing service both in states with higher and lower entry barriers, and that Verizon's entry has been significantly slowed down by the need to obtain franchises. As of the end of January 2008, Verizon has deployed its FiOS network to 9.7 million homes, and has deployed video capabilities to 8 million homes, yet Verizon is able to sell video services to only about 6 million homes, due principally to delay in obtaining local franchises and other franchise-related requirements (*e.g.*, local franchise geographic areas that are substantially broader than Verizon's central office coverage areas in which seeking a franchise would trigger broader deployment).

In Cablevision's territory, Verizon is marketing FiOS data services to approximately 1.4 million homes yet is able to market video services to only about 1 million of those homes.[1] Cablevision passes approximately 4 million homes in Verizon's local telephone service territory.[2] The vast majority of those homes are unable to benefit from video competition by Verizon.

Most of Verizon's lines are in states that do not have statutes simplifying and expediting franchise approvals. In the last six months of 2007 alone, Verizon has been

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[1] B. Swinburne, *et al.*, Morgan Stanley, *Cablevision Systems; Oversold: FiOS Priced In* at Exh. 5 (Feb. 1, 2008).

[2] *See* S. Wang, *et al.*, Bear Stearns, *Resetting the Bar – 2008 Outlook* at Exh. 9 (Jan. 7, 2008).

forced to conduct individual franchise negotiations with more than 200 LFAs. Each negotiation, even when it takes only a few months, delays and increases the cost of entry.

New York State is the most problematic jurisdiction for Verizon: In 2007, Verizon was able to obtain franchises in only 60 percent of the municipalities that it targeted at the beginning of the year. The *average* time to achieve a franchise is six to twelve months. Many LFAs still demand up-front payments even to begin negotiations – one LFA recently demanded $30,000. There are currently approximately half a dozen LFAs with which Verizon has not been able to begin negotiations because of the large up-front payments they have demanded. Following the grant of a franchise, additional delays occur waiting for New York PSC approval, obtaining letters of credit and insurance certificates, and other process.

Verizon's experience in Massachusetts has been comparable. The franchise application process in Massachusetts is burdensome, with elaborate paperwork required before franchise negotiations can even begin. Many LFAs continue to demand payments or other compensation that exceed permissible levels. As a result, as in New York, the typical negotiation lasts six to twelve months.

Verizon's experience in Pennsylvania has been a little better than in New York or Massachusetts, but it still takes five to nine months to obtain a franchise. In addition, the burdens of negotiations are multiplied because of the large number of small LFAs in Pennsylvania.

By contrast, where states have passed legislation to facilitate new entry, the franchise process poses reduced barriers to entry. In New Jersey, Verizon can begin offering video service within 48 hours after filing a letter with the city and state authorities. In Florida and Indiana, state rules provide for action on an application to provide service within 15 days. In Texas, an application must be acted on within 16 days. In California, state rules require the PSC to approve a franchise application within 45 days, but based on Verizon's recent experience the PSC may act even faster. Under Virginia's rules, Verizon is permitted to begin providing service – with or without an agreement with the LFA – within 75 days. Even though the states in which Verizon obtained its franchises predominantly through state-level franchise streamlining rules account for less than a quarter of Verizon's residential access lines, Verizon has obtained almost half its local franchises in those states – and almost all of those within the last two years. *See* Table 1 below.

Table 1. Franchises for FiOS TV				
State	**Number of Franchises**		**Homes Covered**	
	Obtained Through Negotiation	**Obtained Under State Franchise Expediting Rules**	**Negotiated Franchises**	**Franchises Obtained Under State Expediting Rules**
CA	18	101	525,012	1,899,312
DE	13	NA	313,830	
FL	13	11	847,036	225,504
IN		4		134,698
MA	63	NA	537,021	
MD	49	NA	1,178,605	
NJ	1	348		2,395,337
NY	81	NA	1,125,864	
OR	17	NA	325,130	
PA	217	NA	903,154	
RI	19	NA	258,104	
TX	4	32	18,395	460,121
VA	21	1	1,237,930	72,672
Total	**516**	**497**	**7,284,808**	**5,187,644**

Note: Some states appear under both negotiated and state franchise rules because Verizon began individually negotiating franchises in those states before state rules took effect. RI had a pre-existing state statute that vests franchising authority in a state agency but it is not properly described as "expediting"; franchising in RI takes 12-18 months. In VA, while the franchising reform statute set certain parameters, and allows Verizon to deploy service upon 30 days' notice, a local franchise still must be negotiated.

Verizon's recent experience also confirms that the local franchising process continues to provide opportunities for abuse by cable operators seeking to raise Verizon's cost of entry. Cablevision has continued its efforts to block or delay Verizon from obtaining franchises in New York. There is a two-step process for obtaining a local franchise in New York – first the local government must vote to grant a franchise at a public hearing, and second the New York PSC must approve the franchise. The New York PSC meets only once per month and requires that franchise applications be filed at least three weeks in advance. As a result, even a week's delay in the approval process at the local level could lead to a month or more delay in getting a franchise. Cablevision has exploited this process to manufacture delay on several occasions.

- Village of Huntington Bay. On November 19, 2007, the Village voted to grant Verizon a franchise in a public hearing, and requested a few modifications to Verizon's franchise agreement, putting Verizon's franchise on track for PSC approval on December 12, 2007. One of the requested modifications, involving the PEG Indemnity provision, was in conflict with state regulations, so Verizon together with the Village Attorney and the Mayor drafted a mutually agreeable alternative. On November 28, Cablevision contacted the Village and threatened to file an Article 78 challenge that the agreed-upon alternative was not adopted pursuant to a public meeting and violated the NY Open Meeting law; Cablevision demanded a new hearing and vote on the franchise. Even though there was no merit to Cablevision's claim – the NY Open Meeting Law does not require public hearings for modifications that have already been authorized – the Mayor was reluctant to risk a lawsuit. After a week of discussions, the Mayor agreed with Verizon, but by that time it was too late for Verizon to get PSC approval on December 12, and Verizon was forced to wait an extra month, until January 16, 2008.

- Village of Buchanan. In some franchise agreements, incumbent cable operators have agreed to provide the municipality free Internet services. In those cases, municipalities have typically required Verizon to provide a monetary grant in lieu of Internet service, pursuant to level playing field requirements. Even though Cablevision's agreement with the Village of Buchanan does not require it to provide free Internet service, in October 2007 Cablevision lobbied the Village to demand a monetary grant from Verizon. In large part due to the confusion regarding this issue, the Village delayed a vote on Verizon's application for 14 days, which caused additional delay in obtaining PSC approval.

- Village of Haverstraw. In a public hearing on Verizon's franchise, Cablevision insisted that if Verizon failed to provide the Village the same concessions as Cablevision, Cablevision would immediately eliminate those concessions, even though state law prohibits it from doing so. In addition, Cablevision encouraged the Village to demand the same concessions that other cities were demanding. At the hearing, Cablevision stated: "So, if Verizon doesn't step up, which they have every reason to because they've done it in other communities, if they don't step up, it means not only that you will lose monies or those benefits from Verizon and the opportunity to capture that from Verizon, but it means you'll lose it from us right away." As a result of this threat, Verizon's application was delayed for a month, which caused additional delay in obtaining PSC approval.

The delays attendant on the LFA process harm consumers. Not only are Verizon's FiOS TV offerings superior in quality and often lower priced than those of the cable incumbents, but cable has responded to competition by lowering prices, moderating price increases, and improving service. Where Verizon's entry is delayed, it takes longer for consumers to realize these benefits, which is a permanent loss in consumer welfare. Breaking remaining LFA logjams thus promises concrete, immediate consumer benefit.

B. Verizon's FiOS Pricing

The Department asks whether and by how much Verizon has raised its FiOS prices in Keller, Texas and whether a price increase is anticipated for 2008.

1. Verizon's lead video offer is called the "FiOS TV Premier" package, which provides over 200 digital channels and more than 20 high-definition ("HD") channels. Beginning in January 2008, the price for FiOS TV Premier increased to $47.99

per month for *new* customers. Verizon's almost 1,000,000 *existing* customers were not subject to this increase and instead pay $42.99 per month. A standard-definition cable box costs an additional $4.99 (increased to $5.99 for new customers) per month, and a high-definition box costs an additional $9.99 per month. Verizon also offers a package of 45 movie channels for $12.99 per month and a package of more than a dozen sports channels for $7.99 per month (or both the sports and movie packages together for $15.99 per month).

Verizon's 2008 packages are less expensive than the average prices that cable incumbents charged *in 2005* – before the last three years of cable price increases. According to the FCC's most recent report on cable prices, which reflects cable offerings as of January 2005, consumers of incumbent cable operators' most highly subscribed tier received an average of 74 analog channels and 34 digital channels for an average price of $56 per month, including a standard-definition set-top box.[3] This is $2 to $8 more expensive than Verizon's 2008 rate of $47.98 for existing customers or $53.98 for new customers. Since 2005, cable operators raised their rates an average of 1 to 7 percent in 2006 and again in 2007,[4] and have announced additional increases of 5 to 6 percent for 2008.[5] Despite the repeated price increases, none of the major cable operator has a core offering with as many channels as Verizon's FiOS TV Premier. *See* Table 2 for sample current price and channel comparisons in several individual cable markets.[6]

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[3] *Implementation of Section 3 of the Cable Television Consumer Protection and Competition Act of 1992*, Report on Cable Industry Prices, 21 FCC Rcd 15087, ¶ 23 Table 4 & Attachment 2 (2006).

[4] C. Moffett, *et al.*, Bernstein Research, *U.S. Cable Pricing: Rationality Prevails? Cable Video Rate Increases Running 5-6% for 2008* at 2 (Nov. 30, 2007) (Cablevision raised rates 1.1% in 2007, while Comcast raised rates 5.4% in 2007); L. Singer, *et al.*, SG Cowen & Co., *Cable Pricing Survey – January 2006* at 3-4 (Feb. 22, 2006) (in 2006, Comcast and Cablevision raised rates 6.0%, and 2.3%, respectively, Time Warner raised rates between 0 and 5%); C. Moffett, *et al.*, Bernstein Research, *Comcast: 2006 Basic Video Price Increases Running at 6.7%* at 2 (Dec. 16, 2005) ("A sampling of 14 rate increase announcements – including some in Comcast's largest markets – suggests that expanded basic-analog price increases average 6.7% in 2006 (see Exhibit 1; unweighted arithmetic average). We also note that Comcast has recently confirmed that its total 2006 price increase will be closer to 6%.").

[5] *See* C. Moffett, *et al.*, Bernstein Research, *U.S. Cable Pricing: All the Districts Are In, and Prices Are . . . You Guessed It . . . Going UP. Price Hikes Average 5%* (Jan. 31, 2008) (Comcast is raising rates roughly 6% in 2008 compared with 5.4% in 2007; Time Warner Cable is raising rates an average of 5-6% in 2008; Cablevision is raising rates 4.7% in 2008).

[6] Appendix A contains the cable websites advertising the packages described in Tables 2 & 3 below.

Table 2. Prices of 2008 Digital Video Offerings						
Company	**Market**	**Service**	**Monthly Price (incl. set-top box)**	**Channels**		
				SD	**HD**	**Music**
Verizon[7]	All	FiOS TV Premier	$53.98	155-202		95
		with HD reception	$57.98	155-202	22-29	95
Cablevision	Massapequa Park, NY	Family Cable	$56.45	91	34	48
		iO Package	$67.40	130	36	48
Comcast	Bethesda, MD	Digital Starter Pack	$59.05	118+		48
		with HD reception	$65.55	118+	37	48
Time Warner Cable	Beaumont, CA	Digital Cable Package	$50.45	82-113		45
		with HD reception	$58.90	82-113	21	45
Cox	Virginia Beach, VA	Digital Cable	$59.45	90		48
		with HD reception	$59.45	90	18	48
Charter	Keller, TX	Digital Home	$54.99	110		46
		with HD reception	$61.99	110	16	46
Bright House Networks	Tampa, FL	Digital Cable	$59.45	138		49
		with HD PAK	$65.45	138	40	49

Verizon's video pricing is uniform everywhere it provides service. Cable operators, by contrast, charge different prices market-by-market, which enables them to price discriminate – that is, set their prices higher in markets where they face less competition. As Verizon's initial submission showed, in markets where Verizon has entered, cable operators have responded by reducing their prices, sometimes only for the customers who have Verizon as a competitive option. But even after such decreases, Verizon's pricing and value are often superior to comparable offerings of the cable incumbents. For example, as shown in Table 2, Cablevision's "Family Cable" package costs more than Verizon's FiOS TV Premier ($56.45 with a standard- or high-definition set-top box), and includes fewer channels (only 91 standard-definition plus 34 HD channels). Cablevision's "iO Package" add-on, which provides a total of 130 standard-definition and 36 high-definition channels, costs a total of $67.40.

2. The prices described above are for customers who buy Verizon's FiOS TV as a stand-alone service and who retain the ability to cancel the service at any time. If a customer is willing to make a term commitment of either 12 months or 24 months, or if a customer buys additional services that also use the same fiber facilities, the customer can realize additional savings. Verizon's multi-service package known as the "triple-play bundle" is typically offered at a lower price than comparable packages sold by the cable incumbents. As one analyst found, "the FiOS triple-play bundle is currently being

[7] Verizon prices shown are for new customers. Customers who joined Verizon before 2008 pay $47.98 for FiOS TV Premier and $52.98 for FiOS TV Premier with HD reception.

offered at an approximate 20% discount to the cable triple-play bundle, despite the higher-data speeds and equal, if not slightly superior, video product offering."[8] Table 3 below compares Verizon's Triple Play bundle (FiOS TV Premier, plus high-speed Internet, plus unlimited voice), to comparable bundles that cable operators offer in select Verizon markets. Verizon's bundles are largely uniform nationwide, while cable bundles vary by market. Table 3 includes cable's standard prices – which are uniformly higher than Verizon's – as well as the promotional rates they offer for the first year of service.

Table 3. Entry-Level Triple-Play Bundles with Digital Video

Market	Company	Monthly Rate	Video	Broadband (downstream)	Telephone (local/ domestic LD)
Massapequa Park, NY	Verizon	$99.98*	FiOS TV Premier	20 Mbps	unlimited
	Cablevision	$89.85[P]/ $125.80	iO Package	20 Mbps	unlimited
Bethesda, MD	Verizon	$108.98*	FiOS TV Premier	5 Mbps	unlimited
	Comcast	$99[P]/ $148.45	Digital Starter Pack	6 Mbps	unlimited
Beaumont, CA	Verizon	$104.98*	FiOS TV Premier	5 Mbps	unlimited
	Time Warner Cable	$89.85[P]/ $114.95	Digital Cable Package	6 Mbps	unlimited
Virginia Beach, VA	Verizon	$104.98*	FiOS TV Premier	5 Mbps	unlimited
	Cox	$103.96[P]/ $121.35	Standard/Digital Discovery Cable	5 Mbps	limited LD
Keller, TX	Verizon	$104.98*	FiOS TV Premier	5 Mbps	unlimited
	Charter	$99.97 [P]/ $153.97	Digital Home	5 Mbps	unlimited
Tampa, FL	Verizon	$99.98*	FiOS TV Premier	10 Mbps	unlimited
	Bright House Networks	$99.95[P]	Digital Cable	7 Mbps	unlimited

Monthly rates for Verizon's competitors may not include the cost of a set-top box and remote control.
*Requires a 24-month contract. Verizon monthly price without contract ranges from $125.97 to $137.97.
[P]Promotional rate for the first 12 months.

Verizon's pricing of FiOS services reflects two types of discounts. There are relatively small discounts for consumers who choose to purchase bundles of services on a month-to-month basis: consumers who subscribe to double play bundles including video generally get no discount (except in Indiana where a video double play earns a discount of 5 percent off stand-alone rates without any term contract); consumers who subscribe to triple play bundles can earn discounts of 3-4 percent off stand-alone rates without any term contract (8 percent in Indiana). Greater discounts are available for term contracts: for double-play bundles, consumers receive discounts of 11-33 percent with a 12-month

[8] C.C. King, *et al.*, Stifel Nicolaus, *Market-Weight Stance on Sector Driven by 3 Thematic Concerns and Valuation* at 4 (May 16, 2007).

contract; and discounts of 17-38 percent with a 24-month contract;[9] for triple-play bundles consumers receive discounts of 14-30 percent with a 12-month contract; and discounts of 21-36 percent with a 24-month contract.

Verizon also offers promotions to entice new consumers. For example, Verizon is currently running an online promotion that waives the usual $29.99 activation fee for new customers. Verizon is also offering customers a free 19" Sharp Aquos HDTV set, with an estimated retail value of $450, or a $200 Best Buy gift card, in exchange for signing up with Verizon for a bundle of FiOS TV plus two other Verizon services. Verizon is offering a RCA Camcorder, with an estimated retail value of $129, or a $50 Best Buy gift card, in exchange for signing up with Verizon for FiOS TV plus one other Verizon service.[10]

3. As noted above, Verizon has recently announced rate increases for 2008, but these increases apply more narrowly than the increases incumbent cable operators have announced, and reflect rising costs. Verizon's offerings are uniform nationwide, which means that, unlike with incumbent cable operators, Verizon isn't adjusting its prices according to the degree of competition in any specific geographic market. Verizon plans to increase the number of HD channels it offers from 20 to 150 by the end of 2008. Verizon also has expanded its video-on-demand library to more than 10,000 titles and has introduced interactive services like a powerful new interactive media guide. These improved service offerings have increased the costs Verizon faces to offer service.

For 2008, Verizon raised the rates for FiOS TV Premier from $42.99 to $47.99, but this rate applies only to new contracts. Customers who signed up for FiOS in 2007 will not be subject to any rate increases, and existing customers were given until January 18, 2008 to add new services or sign up for bundles at the 2007 rates. Customers who signed up for FiOS in 2005 and 2006 have not been subject to rate increases in the past three years, and, for 2008, those who subscribed in 2005 or 2006 to FiOS TV plus at least one other Verizon service are not subject to an increase. Those 2005/2006 subscribers who purchase only FiOS TV Premier will be subject to the 2007 rates for FiOS TV premier (*i.e.*, $42.99 rather than $47.99).[11] Thus, unlike incumbent cable operators, Verizon has not increased rates each year, and even its most recent increases were implemented using a tiered approach that limits the increase for customers under existing contracts. By contrast, in any given market, incumbent cable operators typically raise rates across the board for *all* of their customers.

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[9] Verizon's bundled offerings may vary among the nine main geographic regions within its territory: New England, New Jersey, New York/Connecticut, Pennsylvania/Delaware, Potomac, Southeast, Texas, West Coast, and Midwest.

[10] These promotions require a 24-month contract with Verizon.

[11] Although Verizon's 2006 rates are slightly higher than its 2005 rates, those increases were not applied to existing customers at the time; thus, customers who subscribed to FiOS in 2005 have been paying the 2005 rates since that time.

4. Market results demonstrate that consumers highly value Verizon's FiOS TV offerings. As of the end of January 2008, Verizon had approximately 1 million FiOS TV subscribers, which represents 17 percent of the 6 million homes to which the service is currently marketed. In areas where Verizon has been providing FiOS TV for longer periods, its penetration is as high as 30 percent. Based on trends over the past two years, analysts expect that Verizon will achieve more than 25 percent penetration in 2009.[12] By comparison, the two DBS operators combined have achieved only about 30 percent penetration, despite nearly 15 years in operation.[13] Consistent with these facts, in a survey conducted in August 2007, ChangeWave Alliance found that Verizon FiOS subscribers reported the highest customer satisfaction rating among video service providers: 96 percent of Verizon FiOS subscribers surveyed were very/somewhat satisfied, while just 73 percent of Comcast, 72 percent of Cox, 70 percent of Cablevision, 68 percent of Time Warner Cable, and 56 percent of Charter subscribers reported the same level of satisfaction.[14]

Independent analysts confirm that Verizon's service has consistently "drawn raves" from consumers.[15] In its February 2008 issue, Consumer Reports rated Verizon FiOS video, high-speed Internet, and long-distance telephone service the top service available in the country.[16] FiOS video and Internet both gained the top possible ranking in each of four categories – value, reliability, performance, and customer support.[17] These were the "first ever 'perfect' score[s] for a video or broadband provider."[18] In its March 2008 issue, Consumer Reports rated Verizon FiOS number one in the country for high-definition TV service.[19]

C. Verizon's Term and Multi-Product Discounts Are Strongly Preferred By Consumers and Reflect Supply Efficiencies

The fiber facilities that Verizon uses for FiOS services have a long lifetime and have the capability to provide multiple services simultaneously. Verizon sells individual services on the fiber on a month-to-month basis. But, as discussed above, if a consumer commits to a 12- or 24-month contract or purchases multiple services (or does both), Verizon provides a discount compared to the individual cancel-anytime, single-service prices. Customers have been very enthusiastic about receiving service on these terms and

[12] *See* R. Dezego, *et al.*, Bank of America, *Battle for the Bundle: 3Q07 Wrap Up* at 18 (Nov. 20, 2007).

[13] *See id.* at 16.

[14] *See* ChangeWave, *TV Service Battle Royale: Cable, Satellite Fight – But Watch Out for Fiber* (Sept. 11, 2007), http://www.changewave.com/freecontent/viewalliance.html?source=/freecontent/2007/09/alliance-091107-TVServiceBattleRoyale.html.

[15] C. Moffett, *et al.*, Bernstein Research, *Verizon (VZ): Project FiOS . . . Great for Consumers, but What About Investors?* at 3 (Jan. 14, 2008) (Moffett, *Project FiOS*).

[16] *Internet, TV, Phone; Bundling Can Cut Bills*, Consumer Reports (Feb. 2008).

[17] *Id.* at 35.

[18] Moffett, *Project FiOS* at 3 ("We fully concur with the assessment that [FiOS] is a terrific product.").

[19] *High-def TV service*, Consumer Reports at 30 (Mar. 2008).

the discounts in fact reflect substantial supplier efficiencies. Customers also benefit from the intense competition between different bundles.

1. The Department has asked whether consumers "really want" bundles or whether they buy them "in order to get a lower price for one of the component services." As the loose formulation of the question suggests, what consumers "really want," as revealed in their purchasing behavior, necessarily depends on both the product and the price. There is no question that consumers "really want" lower prices, which is one important reason that many scholars suggest a hands-off approach to scrutinizing bundle discounts even when the bundles contain amalgams of unrelated products without substantial supplier efficiencies.[20] However, the evidence regarding Verizon's multi-service bundles suggests that consumers value Verizon's bundles not only for the discounts but also importantly and primarily because they like each of the constituent elements and they like the convenience of receiving a single bill and having a single point of contact for ordering service and resolving any service difficulties.[21]

As noted, the February 2008 issue of Consumers Reports found, based on a survey of 37,166 respondents with a home internet account, 44,457 with TV service, and 26,599 with long-distance phone service, that Verizon FiOS is the number one favorite provider in all three categories.[22] Reflecting the strong consensus, Consumer Reports rated Verizon FiOS the sole "best choice overall."[23] Verizon FiOS customers do not need to opt for an inferior product on any element of the bundle in order to get the lower price; Verizon customers get low price *and* the best quality for each element of the bundle.

According to Consumer Reports, even non-Verizon bundles are good deals for consumers. Its survey found that in general "you needn't compromise service quality to buy a bundle. Subscribers to many companies were reasonably satisfied with all three of the most commonly bundled telecom services."[24] Consumer Reports notes that there are both substantial price and non-price benefits: "You can get a good deal. A bundling mainstay is the one-year, $99-a-month package, typically made up of a premium level of TV service, standard-speed broadband Internet service, and telephone service with a

[20] Antitrust Modernization Commission, Report and Recommendations at 94 (Apr. 2007) ("Antitrust Modernization Report") ("Because they involve lower prices, bundled discounts and bundled rebates typically benefit consumers."); John Thorne, *Discounted Bundling by Dominant Firms*, 13 George Mason L. Rev. 339 (2005).

[21] D. Williams, *et al.*, Jupiter Research, *Multi-play Offerings: Finding and Courting the Quadruple Play Customer* at 2 (Oct. 22, 2007); *id*. at 2 ("Although the price of bundles surely impacts consumers' purchasing decisions, consumers overall expressed strong interest in receiving one bill and personalizing bundles to suit their individual needs."); GfK, Consumer Churn Study, Verizon Marketing Research at 26 (Apr. 2007) ("Service simplicity that comes from a single bundle of services was [] a key factor in customers' decisions to defect.").

[22] *Internet, TV, Phone Bundling Can Cut Bills*, Consumer Reports at 35 (Feb. 2008).

[23] *Id*. at 34.

[24] *Id*. at 33.

variety of calling features. Such deals could save you up to hundreds of dollars a year over the amount you'd pay if you received the three services separately." "Bundling offers convenient consolidation of your telecom bills."[25] Consumer Reports also notes the intensity of competition between bundle providers makes it possible for consumers to negotiate extensions of promotional discounts: "Having signed you up for the cheap bundle, 'the last thing the company wants is to lose you.'"[26]

Other sources describe the increasing consumer popularity of bundles. A recent report by Frost & Sullivan found that, as of 2006, 48 percent of U.S. households subscribed to bundles of two or more services, while 11 percent subscribed to bundles of three or more services.[27] TNS found that 64 percent of U.S. households receive two or more services (excluding long distance) from the same provider.[28] These numbers have been rising rapidly. For example, TNS recently found that the proportion of customers who receive voice, data, and video service from a single provider has tripled in the past two years (2Q05 through 2Q07).[29] A Yankee Group study likewise found that "the number of consumers who purchased multiple subscription services from a single provider reached 54% in 2006; we forecast that will hit 76% by the end of 2007."[30]

Verizon's internal data provide further confirmation that consumers value bundled offerings. Of the customers who subscribed to FiOS as of the end of third quarter 2007, half purchased a bundle of video plus at least one other service (voice and/or data). Another 38 percent purchased a combination of voice and data service. By comparison, only about 11 percent of subscribers take just one FiOS service. A recent Verizon consumer survey of 3,000 households in the FiOS footprint in the New York metropolitan area found that "[b]undle offers which include voice and video produce the biggest draw in any of the pricing scenarios tested" and that regardless of price "customers show a much higher disposition toward a bundle with voice and/or TV than stand-alone Internet."[31] Another study conducted for Verizon found that of the consumers who have switched from Verizon to another provider, 56 percent did so in order to obtain a bundle of three services, and that 82 percent of those customers received a bundled discount.[32]

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[25] *Id*.

[26] *Id*. (quoting Douglas Williams of Jupiter Research).

[27] Frost & Sullivan, *Move Toward Full Convergence – Communication Services for U.S. Residential Markets*, No. 20-62 (2007).

[28] TNS Telecoms, *2Q07 National Market Tracking Report* at 9 (Sept. 2007).

[29] TNS Telecoms 2*Q07 National Market Tracking Report* at 21 (Sept. 2007).

[30] P. Monaghan, Yankee Group, *Driving Value in the Quad Play and the Future of the Communications Bundle* at 3 (Oct. 2007).

[31] *FiOS Symmetrical Speed Pricing in NY, NJ, CT: Summary of Findings* at 6, 7 (Aug. 2007).

[32] TNS Telecoms, *Verizon Consumer Local Churn Study*, July/August 2007 Defectors.

2. From the supplier perspective, offering discounts to customers who make term commitments and buy multiple services on the same fiber facility tracks the economic realities of the supplier's high fixed-cost investment in route-specific facilities.

Many of the general reasons that bundle discounts are ubiquitous in American commerce apply here.[33] "There are obvious business reasons why firms offer A and B together. These include benefits of integration, economies of scope in distributing products, packaging cost savings, reduced transaction costs for businesses and consumers, and increased reliability for consumers."[34] Bundling can also lower costs by reducing uncertainty about aggregate demand, reducing overhead and marketing expenses, and economizing on the quality signaling benefits of well-known brands.[35] Bundling also can substitute for advertising as a short-term way to promote one or more products. For some or all of these reasons, providers of goods and services frequently have both the ability and the incentive to offer bundles of services to consumers at a discount off of the sum of the stand-alone prices for the goods. Many of these justifications for bundled discounts apply to communications service bundles: customers benefit from the reduced transaction costs of a single bill; providers save on billing and customer service costs; and Verizon has been able to capitalize on its hard-earned reputation for outstanding service and network quality.

More specifically, the bundled services here are all provided by a common facility. Many of the costs associated with fiber plant are common costs that do not depend on whether the customer orders a single service such as video or broadband or a bundle of all three services – for example, the cost of installing fiber to a particular residence is the same whether the customer purchases one service or three. Accordingly, Verizon incurs significantly lower costs in providing three services to one customer than it does in providing a single service to three different customers. That cost savings is reflected in the discounts available for bundled services.[36]

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[33] *See* Timothy J. Muris, *Antitrust Law, Economics, and Bundled Discounts*, Comments Submitted to United States Antitrust Modernization Commission at 2 (July 15, 2005), http://www.amc.gov/public_studies_fr28902/exclus_conduct_pdf/050715_US_Telecom-Exclus_Conduct-Bundling.pdf (Muris, *Bundled Discounts*).

[34] David S. Evans & A. Jorge Padilla, *Designing Antitrust Rules for Assessing Unilateral Practices: A Neo-Chicago Approach*, 72 U. Chi. L. Rev. 73, 90 (2005).

[35] *See* Muris, *Bundled Discounts* at 3-4.

[36] *See, e.g.*, William J. Adams & Janet L. Yellen, *Commodity Bundling and the Burden of Monopoly*, 90 Q. J. of Econ. 475, 475-476 (1976); Daniel A. Crane, *Multiproduct Discounting: A Myth of Nonprice Predation*, 72 U. Chi. L. Rev. 27, 39-43 (2005); David S. Evans & A. Jorge Padilla, *Designing Antitrust Rules for Assessing Unilateral Practices: A Neo-Chicago Approach*, 72 U. Chi. L. Rev. 73, 90 (2005); David S. Evans & Michael Salinger, *Why Do Firms Bundle and Tie? Evidence from Competitive Markets and Implications for Tying Law*, 22 Yale J. on Reg. 37, 41-42 (2005), *available at* http://ssrn.com/abstract=550884; Barry Nalebuff, *Bundling As a Barrier to Entry*, 119 Q. J. of Econ. 159, 161 (2004); Lester G. Telser, *A Theory of Monopoly of Complementary Goods*, 52 J. of Bus. 211, 223 (1979).

Furthermore, many of the costs that Verizon incurs in providing all of its services – voice, video, broadband, and wireless – are essentially fixed, that is, they do not vary as Verizon adds additional customers. For example, the cost of wiring a neighborhood for FiOS does not depend on the number of customers in the neighborhood that eventually choose to purchase service; the cost of establishing a video head-end does not vary with each additional customer (existing or new) who decides to order video service. Verizon does not price discriminate in its provision of FiOS services, offering uniform state-wide pricing, in part because consumers welcome the simplicity of uniform pricing and see it as fair. Bundled discounts nevertheless help to enable Verizon to make the broadest range of products available to subscribers with varying preferences.[37] For example, individual A may value video service more highly than her neighbor B, but place a lower value on broadband service than B. Suppose that A values video service at more than the stand-alone price, but would pay only $35 per month for high-speed broadband, which is less than the stand-alone FiOS Internet price; suppose the reverse is true for B. In the absence of a bundled discount, A will not buy broadband service, and B will not buy video service. With the bundled discount, the incremental price of each service in the triple-play bundle is less than the value that the customer places on that service, and both A and B will order the triple-play bundle.

That outcome benefits both Verizon and overall economic efficiency.[38] Verizon benefits because it recovers additional revenue in excess of any incremental cost of serving the additional customer, which contributes to recovery of fixed costs. And more consumers benefit because more consumers are able to purchase additional services at prices that are less than the value the consumers place on those services. At the same time, because consumers also have the option to purchase bundles of voice and one other service – still at a substantial discount – or individual services, consumers have great flexibility to purchase the set of services they value most highly.[39]

There are additional reasons why Verizon offers discounts for customers who order FiOS bundles. The installation of FiOS substantially reduces operational costs.[40] Verizon estimates cost savings of $110 annually per home served over fiber rather than copper – a savings of nearly $10 per month. These savings reflect the labor-cost-intensive nature of service changes on a copper network, which frequently require a truck roll or manipulation of electronics in the network. By contrast, in a fiber network, many customer service changes can be handled without any work by a technician.

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[37] *See* Stefan Stremersch & Gerard J. Tellis, *Strategic Bundling of Products and Prices: A New Synthesis for Marketing*, 66 J. Marketing 55, 70 (2002); Thomas T. Nagel & Reed K. Holden, *The Strategy and Tactics of Pricing: A Guide to Profitable Decision Making*, 245-246 (3d ed. 2002).

[38] Yannis Bakos & Erik Brynjolfsson, *Bundling and Competition on the Internet*, 19 Mktg. Sci. 63, 66-68 (2000) (noting that when information goods have heterogeneous valuations by consumers "bundling substantially reduces the average deadweight loss and leads to higher average profits for the seller.").

[39] The incremental price of FiOS TV for a subscriber to the phone / FiOS Internet bundle is approximately $30; the incremental price of FiOS Internet for subscriber to the phone / FiOS TV bundle is likewise approximately $30.

[40] *See* Moffett, *Project FiOS* at 16.

Verizon's discounts also reflect the substantial cost savings associated with term contracts. Verizon lost approximately 8 percent of its access lines in 2007.[41] Reacquiring customers that have left Verizon's network is very costly – with customer acquisition costs of hundreds of dollars. Verizon is able to grant term discounts to reflect the cost savings associated with reduced churn. That is why Verizon's term discounts are available to new FiOS customers and existing customers.

3. "[V]irtually everyone . . . tends to agree that bundling is pro-consumer. It is a way of discounting, it is a way of waging competition."[42] "[T]he fact that firms without market power often offer bundled discounts suggests that their efficiencies, not schemes to acquire or maintain monopoly power, typically explain their use."[43] Economic analysis shows that bundle-to-bundle competition benefits consumers relative to competition limited to providers of individual services. "Bundle against bundle is ferocious competition."[44] Barry Nalebuff – no unqualified advocate of the competitive benefits of bundling – has found that bundle-to-bundle competition yields dramatically lower prices than competition among providers of stand-alone services.[45] Consumers benefit from bundle-to-bundle competition because the stakes for firms are much higher; if a customer is lost, revenue from multiple services is lost.

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[41] *See* M. Rollins & E. Schmitz, Citigroup Global Markets, *Verizon Communications Inc.* at 11, Fig. 5 (Jan. 28, 2008).

[42] Antitrust Modernization Report at 95 (quoting statement of Robert Pitofsky).

[43] *Id.*; *see also* Richard A. Posner, *Antitrust Law* 253 (2d ed. 2001) ("If the practice is one employed widely in industries that resemble the monopolist's but are competitive, there should be a presumption that the monopolist is entitled to use it as well. For its widespread use implies that it has significant economizing properties, which implies in turn that to forbid the monopolist to use it will drive up his costs and so his optimum monopoly price.").

[44] Barry Nalebuff, *Competing Against Bundles*, in Peter J. Hammond & Gareth D. Myles, *Incentives, Organization, and Public Economics: Papers in Honor of Sir James Mirrlees* 323, 328 (2000); *see also* Ioana Chioveanu, *Strategic Pricing in Oligopoly Markets, Universitat Autonoma de Barcelona Doctoral Dissertation* at 7 (July 2004) ("[B]undle against bundle competition (the market outcome with an elastic demand) generates higher consumer surplus and lower profits than bundle against component competition (the market outcome with an inelastic demand).").

[45] *See* Nalebuff, *Competing Against Bundles*.