

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

In the Matter of

**Lockheed Martin Corporation,
COMSAT Corporation, and
COMSAT Digital Teleport, Inc.**

Assignors

And

**Intelsat Ltd., Intelsat (Bermuda), Ltd.,
Intelsat LLC, and Intelsat USA License Corp.,**

Assignees

**Applications for Assignment of
Earth Station Licenses and
Section 214 Authorizations**

IB Docket No. 02-87

**File Nos. ISP-PDR-20020405-00010
SES-ASG-20020405-00552 et seq.
SES-MOD-20020405-00568 et seq.
0000838233
ITC-ASG-20020405-00185**

To: International Bureau

PETITION OF WORLDCOM AND SPRINT TO CONDITION GRANT

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PETITION OF WORLDCOM AND SPRINT TO CONDITION GRANT

WorldCom, Inc. (“WorldCom”) and Sprint Communications Company L.P. (“Sprint”) hereby petition the Commission to condition grant of the above-referenced applications (“Application”) regarding acquisition of certain assets of COMSAT World Systems and certain associated business units (collectively “COMSAT”) by the above-referenced Intelsat companies (collectively “Intelsat”).

I. Summary and Introduction

The U.S. market for wholesale, unbundled Intelsat space segment services is not competitive. Although the legal right to acquire Intelsat space segment via direct access has been in place for nearly two and a half years, the practical ability to acquire such space segment via direct access has been painfully limited. COMSAT has been able to use its control over Intelsat capacity accessible from the United States to maintain large and unjustifiable mark-ups on wholesale Intelsat services without losing significant market share. Indeed, COMSAT's own data indicates that it still controls 82 percent of current U.S. Intelsat usage.

COMSAT's dominant share of U.S. wholesale Intelsat services is significant because the market for such services remains a distinct market. The Commission continues to regulate COMSAT as dominant on "thin routes" (involving many of the world's least developed countries and regions) where adequate competitive alternatives to Intelsat services do not exist; and in a variety of circumstances on other routes, fiber optic cable and other satellite systems do not provide a viable alternative to Intelsat services. Indeed, WorldCom and Sprint would have no reason to purchase Intelsat services at COMSAT's inflated prices if viable competitive alternatives were available.

The proposed Intelsat/COMSAT merger would increase these competitive concerns. The transaction would involve a horizontal combination of the largest U.S. provider of wholesale Intelsat services (COMSAT, with an 82 percent market share) with the second-largest provider (Intelsat, with the remaining 18 percent market share), giving the merged entity control over the availability and pricing of all Intelsat capacity available from the United States. Further, the transaction would also involve a vertical integration of wholesale space segment and retail

businesses, increasing the ability of the combined entity to impose a price squeeze on competitors.

In order to address these concerns, the Commission should condition grant of the Application on requirements that Intelsat offer non-discriminatory pricing of Intelsat services to U.S. customers (both for services now sold via COMSAT and for future services) and that Intelsat remain subject to incentive-based regulation of non-competitive services that it offers in the United States.

II. The Commission Must Require Non-Discriminatory Pricing by Intelsat-COMSAT in Order to Protect Competition

A. COMSAT Continues To Use Its Control Over the U.S. Market for Intelsat Services To Maintain U.S. Prices Well Above the World Price

Despite the claims of Intelsat and COMSAT in the Application, the U.S. market for wholesale, unbundled Intelsat space segment services is not competitive. The market is characterized by the continuing dominance of COMSAT, insufficient opportunity for direct access to Intelsat and, as a result, inflated wholesale prices.

The Commission mandated direct access to the Intelsat system effective December 1999,¹ and Congress confirmed that decision in the ORBIT Act, which was signed into law in March 2000.² Although the legal right to acquire Intelsat space segment via direct access has been in place for nearly two and a half years, the practical ability to do so has been painfully limited. As

¹ *Direct Access to the INTELSAT System*, 14 FCC Rcd. 15703 (1999) (“*Direct Access Order*”).

² Open-Market Reorganization for the Betterment of International Telecommunications Act, § 641(a), Pub. L. No. 106-180, 114 Stat. 48 (2000) (codified at 47 U.S.C. §§ 761 *et seq.*) (“ORBIT Act”) (“Beginning on the date of enactment of this title, users or providers of telecommunications services shall be permitted to obtain direct access to INTELSAT telecommunications services and space segment capacity through purchases of such capacity or services from INTELSAT.”).

a result, U.S. carriers and consumers have yet to realize most of the benefits of direct access. COMSAT has been able to deny these benefits, and maintain unjustifiable mark-ups on Intelsat services, through its control over the U.S. market for Intelsat services and the Intelsat capacity accessible from the United States.

The data in the Application indicate that COMSAT still controls 82 percent of current U.S. Intelsat usage.³ This enormous market share, by an entity charging a mark-up above prices available everywhere else in the world, would not be possible in a competitive marketplace. Yet, COMSAT is able to use its market power to retain this dominant position even for Intelsat services to carriers like WorldCom and Sprint, which operate their own Intelsat earth stations and for which COMSAT provides no facilities and adds virtually no economic value.⁴

At present, Sprint does not use direct access at all and WorldCom does not use direct access for the Intelsat IDR and IBS circuits that comprise the bulk of its usage of Intelsat services.⁵ The inability of U.S. users to take advantage of direct access stems from COMSAT's nearly 40 year monopoly over access to Intelsat, and COMSAT's ability to project that monopoly into the future long after its *de jure* monopoly had been terminated. COMSAT was able to extend its monopoly beyond the formal expiration date by obtaining almost all U.S.

³ Application at 28 n. 53 ("More recent data indicates that Intelsat's direct customer services account for about 18 percent of U.S. usage on the system.").

⁴ COMSAT may provide value-added services to some customers but WorldCom and Sprint do not seek nor require such services, and therefore perceive no material value from such services. In any event, the policy behind direct access is that companies like WorldCom and Sprint should have the opportunity to buy unbundled space segment capacity directly from Intelsat just as their foreign competitors do.

⁵ IDR and IBS represent approximately 65 percent by value of WorldCom's usage of Intelsat services. WorldCom uses direct access to a moderate extent for Intelsat leased transponder services. Leased transponder services represent approximately 35 percent by value of WorldCom's usage of Intelsat services, and WorldCom obtains about 11 percent of these services (or 3.85% of its total usage of Intelsat services) by direct access.

Intelsat capacity while it still had its monopoly. In the period after the *Direct Access Order*, most orders by U.S. customers for direct access circuits were rejected by Intelsat because COMSAT had already cornered nearly all of the capacity. Some of this capacity was sitting idle in COMSAT's capacity pool waiting for captive buyers – who would have no choice but to pay a premium above the underlying Intelsat Utilization Charge (“IUC”). Congress addressed this situation in the ORBIT Act by requiring the Commission to:

complete a rulemaking ... to determine if users or providers of telecommunications services have sufficient opportunity to access INTELSAT space segment capacity directly from INTELSAT to meet their service or capacity requirements. If the Commission determines that such opportunity to access does not exist, ***the Commission shall take appropriate action to facilitate such direct access ...***⁶

In its rulemaking conducted pursuant to this statutory provision, the Commission concluded that ***“U.S. users and providers of telecommunications services currently do not have sufficient opportunity to access INTELSAT capacity directly to meet their service or capacity requirements.”***⁷ Despite this unequivocal conclusion, the Commission did not “take appropriate action to facilitate such direct access” as mandated by the ORBIT Act, but instead pursued a “commercial solution” involving negotiations between COMSAT and potential direct access customers, without any specific guidelines for conduct of the negotiations.⁸ The result, not surprisingly, was that COMSAT did little or nothing to facilitate direct access, enabling it to retain 82 percent of the market at significant premium prices above the IUC available in virtually every market outside the United States.

⁶ ORBIT Act, § 641(b) (emphasis added).

⁷ *Availability of INTELSAT Space Segment Capacity to Users and Service Providers Seeking To Access INTELSAT Directly*, 15 FCC Rcd. 19160, 19175 (2000) (“*Intelsat Portability Order*”) (emphasis added).

⁸ *Id.*, 15 FCC Rcd. at 19176-80.

Against this commercial and regulatory backdrop, and given the practical unavailability of direct access, WorldCom's "least worst" option was to sign a contract with COMSAT in 2000 that provided for substantial volume and term commitments in exchange for partial relief from the large mark-ups that COMSAT proposed over the IUCs. Because of the size of the volume commitments required, WorldCom has not recently been able to pursue direct access at all for IDR or IBS circuits.⁹ While the term of this contract with COMSAT recently expired so that new capacity or renewals are not covered, WorldCom will for several years continue to have substantial commitments for circuits purchased previously under the contract.

Not dissimilarly, Sprint continues to be subject to volume commitments for Intelsat IDR circuits under a ten-year contract that it signed in 1993 in order to get the best rates available at that time. For other Intelsat services, Sprint has not been able to use direct access because of similar long-term contracts and the substantial unavailability of capacity discussed above.

In sum, for Intelsat capacity purchased through COMSAT, WorldCom and Sprint pay charges that are significantly in excess of the underlying IUCs, notwithstanding the fact (as noted above) that COMSAT acts as a pure reseller and provides no facilities or economic value to the carriers in connection with such services. Meanwhile, since Intelsat's privatization in July 2001, Intelsat has begun to offer promotional pricing to its large customers that includes discounts as large as 30 percent below the stated IUCs. As a result, for many Intelsat services, WorldCom and Sprint now pay to COMSAT prices up to 50 percent more than they would pay if purchasing

⁹ Initially, WorldCom was able to purchase a very small number of IDR and IBS circuits through direct access. However, WorldCom eventually had to novate these contracts from Intelsat to COMSAT to satisfy the volume commitments that COMSAT had been able to impose on WorldCom.

those services directly from Intelsat. Other U.S. carriers and customers presumably face similar elevated pricing by COMSAT.

The anomalous and discriminatory nature of these pricing discrepancies is illustrated by the fact that they do not exist in most markets outside the United States. Foreign carriers that were formerly Intelsat signatories, such as British Telecom, France Telecom, Deutsche Telekom and Teleglobe are all able to purchase space segment at standard Intelsat discounts. Similarly, alternative European carriers, who have had direct access to Intelsat for years and have not faced COMSAT's monopoly access, enjoy the same competitive advantages over U.S. carriers.

B. The Acquisition of COMSAT by Intelsat, Without Appropriate Safeguards, Would Injure Competition in the U.S. Market for Intelsat Services

If the proposed acquisition of COMSAT by Intelsat is consummated, the inflated COMSAT pricing described above would have further adverse effects on competition, in several significant respects.

First, once Intelsat and COMSAT are a single integrated entity, there would be no competitive justification at all for any discrepancy – let alone the current huge discrepancy – between the prices offered by Intelsat and those charged under legacy COMSAT contracts. Such discriminatory pricing by a single entity would be commercially impossible under conditions of fair competition, and is inconsistent with the non-discrimination principles in Sections 201 and 202 of the Communications Act.¹⁰ Intelsat and COMSAT might attempt to justify such pricing based upon term commitments and contractual obligations of WorldCom and Sprint or the role of COMSAT as a reseller of Intelsat services, but such arguments clearly must fail. The

¹⁰ See 47 U.S.C. §§ 201(b), 202(a).

contractual obligations of WorldCom and Sprint, as discussed in Section II.A above, were the result of COMSAT's exercise of monopoly power. Indeed, both Congress and the Commission recognized as much – Congress by mandating a proceeding on space segment portability in the ORBIT Act and the Commission by concluding in that proceeding that insufficient opportunity for direct access to Intelsat capacity was available in the U.S. market. Likewise, any basis for a COMSAT resale mark-up on Intelsat services has always been weak because the size of COMSAT's mark-up is determined by its economic power rather than by any real value added¹¹ – but at present COMSAT does act as a reseller (and alternative source) of Intelsat services. Even this thin justification would disappear once Intelsat and COMSAT are the same entity.

Second, the proposed transaction would involve a horizontal merger in the wholesale market for Intelsat service in the United States – combining by far the largest provider of such services (COMSAT) with the second-largest provider (Intelsat). As noted above, COMSAT alone has 82 percent of this market, and Intelsat has the other 18 percent. Accordingly, the acquisition would substantially increase the market power of the merged entity in selling such services, with respect to both price and capacity. With respect to price, even though in practice direct access has not been widely available to U.S. customers, the potential availability of direct access has imposed at least limited discipline on COMSAT. Although the contractual prices that WorldCom agreed to with COMSAT in 2000 were well above the underlying IUCs, they were nevertheless below the COMSAT prices available to WorldCom before the *Direct Access Order*. The proposed merger of Intelsat and COMSAT would give the merged Intelsat/COMSAT control over the availability and pricing of all of the Intelsat capacity available from the United

¹¹ The Commission rejected COMSAT's cost-based justifications for most of its mark-up in the *Direct Access Order*. See *Direct Access Order*, 14 FCC Rcd. at 15727-38.

States. By purchasing COMSAT's dominant franchise, Intelsat would no longer have any incentive to offer pricing to WorldCom, Sprint and other customers that is more attractive than that offered by COMSAT. Likewise, the merger of the businesses of Intelsat and COMSAT would eliminate any price discipline on COMSAT.

Third, the proposed transaction would also involve a significant vertical integration, as Intelsat and COMSAT recognize:

By combining Intelsat's longstanding experience in providing raw space segment capacity with COMSAT's marketing acumen, ground services, and network management services, the combined enterprise will be able to much more quickly take advantage of the same business efficiencies that its competitors now enjoy.¹²

Intelsat has recently confirmed that it intends to use the acquisition of COMSAT to introduce retail services.¹³ Integration of absolute upstream control of Intelsat space segment with new downstream capacity for retail distribution to customers will greatly increase the ability of the combined entity to impose a price squeeze on competitors who must purchase Intelsat services as an input. The Commission has repeatedly recognized the competitive risks of such a price squeeze.¹⁴

Intelsat and COMSAT argue at length in the Application that competition from other providers of international satellite-based and terrestrial telecommunications services mitigate

¹² Application at 22.

¹³ Bruce Branch, *Intelsat Adds Terrestrial Service to Satellite Offerings*, Communications Daily, May 22, 2002, at 8-9 (quoting John Stanton, Intelsat Global Sales & Marketing President).

¹⁴ See, e.g., *Ameritech Corp. and SBC Communications, Inc.*, 14 FCC Rcd 14712, 14814, n.429 (1999); *NYNEX Corp. and Bell Atlantic Corp.*, 12 FCC Rcd 19985, 20044 (1997); *Developing a Unified Inter-carrier Compensation Regime*, 16 FCC Rcd 9610, 9649 (2001).

these competitive concerns.¹⁵ However, the existence of such competition would not remedy clear discrimination between generally-available Intelsat prices and legacy COMSAT prices.

Furthermore, in many respects the U.S. market for Intelsat services remains a separate market from the markets for the purportedly competitive services that Intelsat and COMSAT identify in the Application. The Commission has recognized this fact by continuing to regulate COMSAT as a dominant carrier on “thin routes” where adequate competitive alternatives to Intelsat services do not exist.¹⁶ Indeed, COMSAT is the *only* international carrier regulated as dominant for reasons other than a foreign affiliation. In addition, even on other routes, fiber optic cable does not provide a viable alternative to Intelsat services where: (1) fiber optic transmission involves complex or inefficient routing (e.g., Eastern Europe), (2) fiber optic transmission facilities do not reach the entire country (e.g., China, India, Russia) (3) there is insufficient cable capacity to meet demand (e.g., parts of Latin America) or (4) only one cable is available and satellite capacity is required to provide diversity of routing to minimize the effects of network outages (e.g., Colombia, El Salvador, Honduras, Jamaica, Netherlands Antilles, South Africa, Uruguay, Vietnam).

Other satellite systems also do not provide substantial competition to Intelsat’s core services, in particular on the same developing country routes where fiber optic cable is unavailable or not an adequate substitute for Intelsat services. Typically, national carriers in developing countries have limited earth station facilities that communicate exclusively or

¹⁵ Application at 24-32.

¹⁶ See *COMSAT Corporation, Petition Pursuant to Section 10(c) of the Communications Act of 1934, as amended, for Forbearance from Dominant Carrier Regulation and for Reclassification as a Non-Dominant Carrier*, 13 FCC Rcd. 14083 (1998) (“*COMSAT Dominance Order*”); *COMSAT Corporation, Policies and Rules for Alternative Incentive Based Regulation of COMSAT Corporation*, 14 FCC Rcd. 3065 (1999) (“*Alternative Rate Regulation Order*”).

primarily with Intelsat satellites. Such carriers also usually have a financial incentive to continue to rely on Intelsat because they are typically former Intelsat Signatories who remain shareholders of privatized Intelsat. WorldCom and Sprint cannot switch from Intelsat to another satellite system operator unless their foreign correspondent agrees to do the same. Moreover, no other satellite system can match Intelsat's reach to over 1000 earth stations around the world and coverage of 99 percent of the globe.¹⁷

Put differently, WorldCom, Sprint and other COMSAT customers would have no reason to purchase Intelsat services at COMSAT's inflated prices if viable competitive alternatives were available. It is primarily on thin routes (involving many of the world's least developed countries and regions) and in other circumstances where there is no viable competitive alternative to Intelsat that Intelsat services are heavily consumed by Sprint, WorldCom and other major U.S. carriers that offer global network services. Accordingly, a requirement of fair, non-discriminatory pricing for wholesale services by the merged Intelsat-COMSAT for such services is crucial to protecting the public interest.

C. The Commission Should Require Non-Discriminatory Wholesale Pricing by the Merged Intelsat-COMSAT

Because of the existing conditions in the U.S. market for Intelsat services that are described in section II.A and the further effects of an Intelsat acquisition of COMSAT that are described in section II.B, the Commission should condition grant of the Application on certain requirements of non-discriminatory pricing by the combined Intelsat-COMSAT.

¹⁷ See *Direct Access Order*, 14 FCC Rcd. at 15706.

First, the Commission should condition any acquisition on Intelsat offering non-discriminatory pricing for the remaining duration of the committed terms of wholesale Intelsat circuits that are currently purchased through COMSAT. Under this condition, the prices for such circuits should be at the same non-discriminatory level offered by Intelsat (*i.e.*, the IUCs) at the time that the circuits were initially purchased. This condition would eliminate the existing price discrimination and ensure that all customers of the merged entity are treated equally. Such a condition is particularly appropriate given that any justification for COMSAT to be able to charge a resale mark-up on Intelsat services for which it provides no facilities and virtually no economic value added would disappear once COMSAT becomes a part of Intelsat. The condition also would not require the “abrogation or modification of any contract.”¹⁸ Rather, Intelsat would have the choice of whether or not to proceed with its proposed acquisition, as conditioned to promote the strong public interest in non-discriminatory pricing.¹⁹

Second, the Commission should condition the acquisition on a requirement that the merged Intelsat/COMSAT offer U.S. customers the same services at the same prices as it offers to other customers around the world. For example, once a WorldCom or Sprint circuit between the U.S. and Pakistan is no longer covered by a contract with COMSAT (or its successor), ***the same circuit*** should be made available to WorldCom or Sprint at a non-discriminatory wholesale

¹⁸ 47 U.S.C. § 765(c).

¹⁹ In providing that “***nothing in this section*** shall be construed to permit the abrogation or modification of any contract,” 47 U.S.C. § 765(c) (emphasis added) clearly does not impair the Commission's general authority under the Communications Act to impose appropriate conditions on a transfer of control like the one requested in the Application. Moreover, the D.C. Circuit has held that an order eliminating rate discrimination does not abrogate contracts. *Western Union International, Inc. v. FCC*, 568 F.2d 1020 (D.C. Cir. 1977), *cert. den.* 436 U.S. 944 (1978).

price. Intelsat/COMSAT should not be permitted to continue their current game of saying that there is no available capacity except from its COMSAT affiliate at a premium price, because COMSAT (or its successor) has a “contract” with Intelsat for such capacity.

Third, for new space segment capacity sold by the merged Intelsat/COMSAT, the Commission should condition the acquisition on Intelsat (1) offering prices to U.S. customers that are no higher than those offered to Intelsat’s own separate subsidiaries engaged in downstream operations, and (2) providing the same IDR-IBS exchangeability (i.e. “mapping”) given to Intelsat’s own customers. In order to permit enforcement of this condition, the Commission should require any Intelsat entity selling wholesale space segment capacity to file publicly the prices that it offers to any retail affiliate (or imputes to itself with respect to retail services).²⁰ Such a requirement would be significantly less burdensome than accounting safeguards that the Commission requires in other circumstances involving dominant carriers that supply a wholesale input.²¹ This requirement is necessary in particular to prevent a price squeeze by the merged entity.

III. The Commission Should Ensure That Intelsat-COMSAT Remains Subject to Incentive-Based Price Regulation on “Thin Routes”

In the *Alternative Rate Regulation Order*, the Commission accepted COMSAT’s proposal for certain incentive-based price caps on Intelsat services on “thin routes”:

²⁰ This should not be a significant burden for Intelsat, given that representatives of Lockheed Martin Corporation, the parent corporation of COMSAT, have informed WorldCom that Intelsat intends to operate separate wholesale and retail subsidiaries after its merger with COMSAT.

²¹ See *Implementation of the Telecommunications Act of 1996: Accounting Safeguards Under the Telecommunications Act of 1996*, 11 FCC Rcd. 17539 (1996).

- reduction of prices for switched voice services by the greater of (a) four percent per year or (b) the amount of price reductions for such services on competitive routes; and
- no future price increases for private line services or occasional-use video services.²²

In the Application, Intelsat confirms that it “will comply with the *Alternative Rate Regulation Order*,”²³ and WorldCom and Sprint welcome this commitment. Given that there is no disagreement on this point, these obligations should be a condition of the grant of the Application. Furthermore, the Commission should make clear that the above commitments will be obligations with respect to *Intelsat prices*, not current COMSAT prices. That is, Intelsat must be required to apply these price reductions and price caps on an annual basis to its own current prices, and the prices of all its affiliates. Application of these rules using current COMSAT prices as the basis would give Intelsat the ability to increase prices substantially.

IV. Conclusion

For the reasons set out above, the Commission should condition grant of the Application on requirements that:

- for the remaining duration of the committed terms of Intelsat circuits that are currently purchased through COMSAT, the prices charged by the combined Intelsat/COMSAT for such circuits should be at the same non-discriminatory level that would have been available directly from Intelsat (*i.e.*, the IUCs) at the time that the circuits were initially purchased;

²² *Alternative Rate Regulation Order*, 14 FCC Rcd. at 3071-77.

²³ Application at 31.

- for new space segment capacity sold by the merged Intelsat-COMSAT, the services offered shall be the same as those offered by Intelsat elsewhere in the world, and the wholesale prices offered by Intelsat to U.S. customers shall be:
 - the same as those offered to other unaffiliated customers for capacity on the same satellite(s), and
 - no higher than those offered to Intelsat's own downstream operations; and
- the existing incentive-based regulation of COMSAT rates shall apply to the prices of the merged Intelsat-COMSAT, using current Intelsat prices as the base prices.

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I, Matthew R. Evans, hereby declare that the foregoing Petition was sent this 24th day of May, 2002 by email or first-class mail (indicated by *) to the following:

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