comply with both of these requirements. Ameritech Michigan also will comply with the Commission's requirements with respect to marketing on in-bound calls for new local exchange service. See Non-Accounting Safeguards First Report and Order, ¶ 292. In addition, ACI and Ameritech Michigan will comply with the customer information privacy requirements of Section 222 of the Act and any related rules or regulations issued by the Commission. See Julian Aff., ¶¶ 26-29.

Finally, both Ameritech Michigan and ACI employees will receive training regarding their obligations under Section 272 and the Commission's regulations and copies of applicable compliance materials. See Julian Aff., ¶¶ 30-34; La Schiazza Aff., ¶¶ 43-48.

VI. AMERITECH'S APPLICATION IS CONSISTENT WITH THE PUBLIC INTEREST, CONVENIENCE AND NECESSITY.

The "public interest" standard undoubtedly gives the Commission reasonable discretion to assess Ameritech's Application based on the entire record, including the views of the MPSC and the Department of Justice. See In the Matter of Amendment of Section 73.202(B), MM Docket No. 96-141, Report and Order, ¶ 3 (November 1, 1996) (satisfaction of the public interest standard is based on the "totality of the evidence"); In re Application of General Tel. Co. of Cal., 4 F.C.C.R. 5693, ¶ 58 (1989) ("totality of the circumstances"). At the same time, the Supreme Court has "consistently held that the use of the words 'public interest' in a regulatory statute is not a broad license to promote the general public welfare." NAACP v. Federal Power Comm'n, 425 U.S. 662, 669 (1976). Rather, "the words take meaning from the purposes of the regulatory legislation." Id. Thus, the term "public interest" in Section 271(d)(3) of the Act must derive its "content and meaning" from "the purposes" for which it was "adopted." Id.[29]

The purpose of the 1996 Act, expressed in the first sentence of the Conference Report, is to "accelerate rapidly" the deployment of telecommunication services "by opening all telecommunications markets to competition." H.R. Conf. No. 104-458, 104th Cong., 2d Sess. 113 (1996) (emphasis added). One of the "principal" goals of the 1996 Act, therefore, is to "increase[ ] competition" in "long distance services."[30] As Senator Pressler, the lead manager of the Senate bill, put it, "what we are trying to do here is to get everyone into everyone else's business." 141 Cong. Rec. S7894 (daily ed. June 7, 1995) (statement of Sen. Pressler)). See also 142 Cong. Rec. S713 (daily ed. Feb. 1, 1996) ("Congress fully expects the FCC to recognize and further its intent to open all communications markets to competition at the earliest possible date") (statement of Sen. Breaux).

Prior to passage of the 1996 Act, those who opposed new competition in the provision of long distance services repeatedly raised hypothetical risks associated with Bell company entry into the long distance business. In the 1996 Act, Congress put an end to such speculation. Congress established specific criteria, which, when met, allow such a Bell company to enter the long distance business. Rejecting the "metric" test for determining whether local exchange

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[29] For this reason, the "appropriate" standard that the Department of Justice uses to evaluate a Section 271 application (Section 271(d)(2)(A)) should be consistent with the purposes of the Act and the statutorily prescribed role of the Commission in making a decision on the Application.

[30] Local Competition First Report and Order, ¶ 3.

services were open to competition,[31/] Congress prescribed a "competitive checklist" test (Section 271(c)(2)(B)) with objective standards that are designed to accelerate, not delay, competition in long distance services. In addition, Congress facilitated new long distance competition by prescribing specific structural and regulatory safeguards that would ensure that Bell company entry will enhance competition in the long distance industry, thereby ending the lengthy debate over what specific safeguards would be needed to achieve that objective. See 142 Cong. Rec. H1149 (daily ed. Feb. 1, 1996) (statement of Rep. Fields, explaining that Congress "needed a checklist that would . . . move the deregulated framework even faster than ever imagined").

With these principles in mind, there can be no doubt that Ameritech's entry into long distance is "consistent with the public interest." Ameritech's entry will bring competitive pricing, increased choice and more innovative services to consumers. And Ameritech has complied fully with the statutory safeguards — including the competitive checklist and the separate affiliate and accounting requirements — that Congress determined were sufficient to ensure that a Bell company could not use its position in the local exchange to impede competition in the provision of any telecommunication services. In short, as we demonstrate

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31/ See 141 Cong. Rec. H8454 (daily ed. Aug. 4, 1995) (statement of Rep. Bunn) (noting that a threshold test, requiring BOC competitors to capture 10% of the local exchange business as a condition for BOC interLATA relief, had been expressly rejected in the House).

below, the benefits of Ameritech's entry into long distance far outweigh any perceived competitive risks.

A. The Competitive Benefits of Ameritech's Entry into Long Distance Services Are Substantial.

In passing the Telecommunications Act of 1996, Congress concluded that increasing the level of competition in all sectors of the telecommunications marketplace, including long distance, will bring enormous benefits to all consumers. Congress had it right. To ensure that the benefits of the Act flow to consumers in Michigan, the Commission must permit Ameritech to compete with the incumbent long distance carriers for all telecommunications services.

1. The Current Concentrated Structure and Noncompetitive Performance of the Long Distance Industry.

Long distance is a business that generates over $80 billion in revenues annually and affects virtually every consumer in the United States. Although no longer a one-carrier monopoly, the long distance industry remains highly concentrated, dominated by three firms: AT&T, MCI and Sprint. AT&T currently takes in over half of the total long distance revenue in the United States, while MCI and Sprint together take in over a quarter. See FCC, Long Distance Market Shares: Second Quarter, 1996, Table 5. The long distance business, in short, is a "tight oligopoly" under any standard. Northern Natural Gas Co. v. Federal Power Comm'n, 399 F.2d 953, 964-65 & n.20 (D.C. Cir. 1968) (market in which share of four largest firms exceeds 50%, and share of largest firm exceeds 20%, is a "tight oligopoly") (citing

C. Kaysen & D. Turner, Antitrust Policy 72 (1959). See also P. Areeda, H. Hovenkamp & J. Solow, 2A Antitrust Law 21 (1995).

Moreover, the potential harm to consumers of services produced by firms in a highly concentrated industry has become a reality in the long distance sector of the telecommunications industry. What passes for "competition" in the long distance industry has engendered lots of advertising in recent years, but has produced little benefit to consumers. See Crandall/Waverman Aff., ¶¶ 5, 7. Between 1990 and 1995, the long distance carriers raised prices six times in rigid lock-step — "each time that AT&T raised its basic rates, MCI and Sprint quickly matched the increase." AT&T Nondominance Order, FCC 95-427 (Oct. 23, 1995). Indeed, even the imminent threat of Bell company entry into long distance has not restrained the incumbents' pricing practices: The three major long distance carriers raised prices twice in 1996, significantly increasing the rates for most consumer calls. MacAvoy Aff., ¶ 16.

These pricing practices result in significant losses to consumers — the very group that Congress sought to benefit through passage of the 1996 Act. Trends in price-cost margins — that is, the margins by which prices exceed the marginal costs of providing services — are a direct indication of the extent of competition in an industry. MacAvoy Aff., ¶¶ 10, 12, 31-32, 36. A decline in concentration in an industry should result in a decline in price-cost margins as the industry becomes more competitive. Id. But precisely the opposite has occurred in the long distance industry. The market shares of AT&T, MCI and Sprint have declined during the period from 1989 through 1995. Id., ¶¶ 12, 21-28. During that same period, however, the major carriers' price-cost margins have increased systematically for long distance services originating and terminating in Ameritech's service area. Id., ¶¶ 12, 47-62, 98. This inverse relationship between a significant decline in concentration in the long distance industry and a significant increase in the price-cost margins of the major carriers in the long distance industry demonstrates that the industry is not performing in a competitive manner and that prices for long distance services are well above competitive levels. Id., ¶¶ 10, 12, 16, 39, 47-62, 98.[30/] And the lack of competition in the provision of long distance services costs consumers in Michigan hundreds of millions of dollars annually. Id., ¶¶ 8, 11-13, 91-97, 99.

Moreover, the harm to consumers from the failure of the major carriers to compete vigorously for long distance services goes beyond the consumer welfare losses attributable directly to noncompetitive pricing practices. As William Baumol, an economist who frequently testifies for AT&T, has noted, there has been a significant "loss from denial or postponement of consumers' access to new communication services" that a BOC, such as Ameritech, "would or might offer but for the [interexchange] restrictions." W. Baumol & J. Sidak, Toward

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30/ Moreover, the noncompetitive pricing practices of the major long distance carriers apply to both standard service offerings and discount plans. See MacAvoy Aff., ¶¶ 12, 63-81. See also id., ¶ 80 ("Price-cost margins set out in the discount plans offered by AT&T, MCI, and Sprint on MTS services increased over the last ten years, even though that period was marked by substantial decline in concentration among the major sources of supply of those services. Discount plans did not push margins down toward the competitive level, in line with falling concentration, as would result under competitive market conditions. Discount plan margins increased in the 1990s, as did margins under standard plans, moving markets away from and not in the direction of increased competitive performance").

Competition in Local Telephony 131 (1994). The lack of competitive pressure in the long distance business "deprive[s] consumers of the benefits of increased competition," including the "achievement of cost efficiencies" and "the dynamic efficiencies from innovation." Spulber, Deregulating Telecommunications, 12 Yale J. on Reg. 25, 64-65 (1995). In short, the poor competitive performance of the long distance industry denies consumers the benefits of competitive pricing, innovative service offerings, and more efficient services.[31]

The welfare of consumers of telecommunications services should be the critical component of any "public interest" inquiry into whether Ameritech should be permitted to enter the long distance market. The consumer welfare loss from the noncompetitive practices of the entrenched long distance carriers plainly disserves the public interest. But it would be naive in the extreme to expect the long distance carriers voluntarily to (i) cease their noncompetitive pricing strategies and (ii) expand the scope of their services. MacAvoy Aff., ¶ 82. In a free market economy, it is competition that drives competitive prices and more and better services. As fundamental principles of economic theory dictate, the long distance business needs an infusion of significant new competition to force the entrenched carriers into offering more

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[31] In addition to paying supracompetitive prices for long distance services, consumers must bear the cost of inefficiencies that are directly attributable to the noncompetitive conditions in the long distance industry. For example, AT&T has imposed a $5.00 minimum calling requirement in order for its business customers to get a single bill from Ameritech which lists both the customer's local service charges from Ameritech and the customer's long distance charges from AT&T. Of course, in a competitive environment, AT&T would be unable to charge this "price" for a simple consumer convenience. Harris/Teece Aff., p. 77.

innovative services at competitive prices. Crandall/Waverman Aff., ¶¶ 3, 8; MacAvoy Aff., ¶¶ 10-13, 16, 82.

2. The Consumer Benefits of Near Term Ameritech Entry into Long Distance Telecommunications.

As the Supreme Court has noted, "unrestrained interaction of competitive forces [will] yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material progress." Northern Pac. Ry. v. United States, 356 U.S. 1, 4 (1958). With this principle in mind, it is simply undeniable that Ameritech's entry into long distance will increase consumer welfare. The new competition that Ameritech will bring to the long distance industry will drive prices toward competitive levels, increase consumer choice, stimulate improved customer service and product innovation, and bring the benefits of advances in telecommunication services to a broader group of consumers.

To begin with, entry by Ameritech into long distance will create pressures that will drive prices in the long distance industry toward competitive levels. As studies of other concentrated industries marked by poor competitive performance demonstrate, Ameritech's entry will have a significant procompetitive impact on performance in the concentrated long-distance industry. Crandall/Waverman Aff., ¶¶ 14-57, 104-113; MacAvoy Aff., ¶¶ 8, 10-13, 82-84, 91-96. Ameritech will have to adopt procompetitive strategies to capture customers from the entrenched long distance carriers. Crandall/Waverman Aff., ¶ 112; MacAvoy Aff., ¶¶ 10, 12, 16. The incumbent long distance carriers will then be forced to adopt pro-consumer strategies — such as more competitive pricing and more attractive services — to combat the inevitable erosion of their customer base. Crandall/Waverman Aff., ¶ 110; MacAvoy Aff., ¶¶ 83, 93. This competitive struggle — which Congress envisioned in passing the 1996 Act — will generate enormous consumer welfare gains. MacAvoy Aff., ¶¶ 8, 10-13, 82-83, 91-99 (the annual gain to consumers in the Michigan area alone will amount to hundreds of millions of dollars); Crandall/Waverman Aff., ¶¶ 3, 5, 7-8, 103-114 (predicting that Ameritech's entry into long distance will lead to a significant gain in consumer welfare).[32/]

Moreover, the benefits that Ameritech's entry into long-distance will bring to consumers go beyond increased price competition. Ameritech's struggle for a share of long distance revenues, which can be achieved only by attracting customers from the entrenched carriers, will stimulate new, competitive service offerings. As a new entrant, Ameritech will seek to improve customer service and develop innovative telecommunications services in order to satisfy existing consumer needs and create new consumer demand. Harris/Teece Aff., pp. 76-78, 81-82; Crandall/Waverman Aff., ¶¶ 3, 8, 103. Ameritech has every incentive to bring these competitive benefits to the long distance business. It will be starting with a zero market share.

32/ Robert Crandall and Leonard Waverman have determined, on the basis of publicly available information (most of it from AT&T itself), that (i) there is an enormous difference between the long run incremental cost of AT&T's long distance service and the revenues AT&T derives from the service; (ii) this difference is absorbed by huge — some would say "bloated" — administrative and marketing costs and excessive returns on capital; and (iii) based on what has happened in other industries and other telecommunications markets that can fairly be characterized as tightly oligopolistic in the same fashion as today's long distance business in the United States when a strong, new rival (like Ameritech) enters the fray, this "bloat" will shrink and prices will be driven toward competitive levels. Crandall/Waverman Aff., ¶¶ 5-7, 14-57, 81-91, 98, 102, 105.

To attract customers, Ameritech will have to make its offerings more attractive than those of the entrenched long distance carriers. In other words, Ameritech will have to give consumers what they want — more and better services at competitive prices. And, unlike many other actual and potential entrants into the long distance business, Ameritech is in a unique position to provide these benefits to Michigan consumers, because Ameritech brings both telecommunications expertise and significant financial resources to the competitive struggle.

Furthermore, market studies reveal a strong consumer demand for "one-stop shopping" — that is, a consumer preference for a single provider of both local and long distance services. See Harris/Teece Aff., pp. 19-20 (recent studies show that the vast majority of consumers prefer to purchase these telecommunications services from a single provider). Ameritech's entry into long distance will enable it to provide consumers with this benefit, by providing them with a wider range of choices as to where to make that "one-stop." Ameritech's entry also will force the entrenched long distance carriers to pass through to consumers the benefit of the efficiencies inherent in one-stop shopping — including efficiencies in marketing, billing, and customer service. Harris/Teece Aff., pp. 79-81.

In addition, Ameritech's entry into long distance will bring the benefits of increased efficiency to groups of consumers that are not the principal targets of the long distance carriers. AT&T, MCI and Sprint already are targeting high-volume, high-margin business and residential customers. If permitted to joint market local exchange and long distance services, Ameritech will bring the benefits of one-stop shopping to a broader group of consumers. At the same time, Ameritech's aggressive efforts to service its entire customer base undoubtedly will force the long distance carriers to compete more vigorously for small business and residential customers. Harris/Teece Aff., pp. 78-79; Crandall/Waverman Aff., ¶ 106.

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As demonstrated above, the incumbent long distance carriers will be forced to react to Ameritech's entry in a more competitive fashion. A fortiori, any delay in Ameritech's entry into long distance will cause direct injury to the very consumers that Congress sought to protect. All of the costs associated with the poor competitive performance of the long distance industry — including limited consumer choice, lock-step price increases, and high price-cost margins — will continue to be borne by the consumers of telecommunications services. This clearly is not in the public interest.

B. The Competitive Risks of Ameritech's Entry into Long Distance Services Are Remote.

The incumbent long distance carriers typically have opposed the entry of the BOCs into the long distance business on the ground that the BOCs were in a position to use the local exchange "bottleneck" to discriminate against unaffiliated long distance carriers or cross-subsidize the BOC's own long distance operations. Whatever its theoretical merit in earlier years, today the argument is wholly without substance. In passing the 1996 Act, Congress established a specific framework for BOC long distance entry precisely to end this long debate. As the Commission has recognized, "[t]he Act prescribes structural and nonstructural safeguards that are intended to protect ratepayers, consumers, and competitors against the effects of potential improper cost allocation and discrimination." Accounting Safeguards Report and Order, ¶ 4.

Under the 1996 Act, there is no "metric" test for entry into long distance. Rather, the test is whether the local exchange is open to competition. And under the Act, it is implementation of the interconnection and competitive checklist requirements that opens the so-called "bottleneck" to competition. Non-Accounting Safeguards First Report and Order, ¶ 205. As demonstrated above in Sections III and IV, Ameritech has fully implemented these requirements.

Moreover, as we discuss below, there exist additional statutory, regulatory and technological constraints that effectively eliminate any residual concerns that Ameritech's entry into long distance might thwart competition for local or long distance telecommunications services.

1. The Michigan Legislature and the MPSC Have Played a Leading Role in Opening the Local Exchange to Competition.

In 1991, more than four years before Congress passed the 1996 Act, the Michigan Legislature substantially revised the Michigan telecommunication laws to remove legal and regulatory barriers to entry into the local exchange business.[33] The Michigan Act expressly authorized local competition in the provision of telecommunications services. Mich. Comp. Laws, § 484.2103. To foster increased competition in telecommunications services, the

[33] Mich. Comp. Laws §§ 484.2101 to 484.2605, effective Jan. 1, 1992 ("the Michigan Act"). See Wilk/Fetter Aff., ¶¶ 21-22.

Michigan Act authorized the MPSC to exercise its regulatory authority in a flexible manner, and, indeed, to deregulate a particular service if it found that "competition among providers of that service is sufficient to protect the public interest." Id., § 484.2208(2). The Michigan Act also adopted an extensive list of new requirements for local exchange carriers designed to create a level playing field for competing telecommunications providers.[34/]

In late 1995, the Michigan Act was amended to add an Article 3A that expressly deals with the interconnection of local exchange service providers. Among other things, the new Article required the unbundling of basic local exchange services by January 1, 1996 (Mich. Comp. Laws, § 484.2355); virtual collocation for competing providers of local exchange service (id. § 484.2356); regulations regarding the resale of basic local exchange services (id., § 484.2357); number portability (id., § 484.2358); termination of local traffic and rates therefor (id., § 484.2359); agreements regarding, and establishment of rates for, directory assistance (id., § 484.2360); and access by competing providers to databases on a nondiscriminatory basis (id., § 484.2363). See Wilk/Fetter Aff., ¶¶ 38-41, 45, 54-55, 66.

[34/] Thus, for example, a local exchange provider may not "[d]iscriminate against another provider by refusing or delaying access to the local exchange" (Mich. Comp. Laws, § 484.2305(a)); "[r]efuse or delay interconnections or provide inferior connections to another provider" (id., § 484.2305(b)); "[d]egrade the quality of access provided to another provider" (id., § 484.2305(c)); "[d]evelop new services to take advantage of planned but not publicly known changes in the underlying network" (id., § 484.2305(e)); "[r]efuse or delay a request of another provider for information regarding the technical design, equipment capabilities and features, geographic coverage, and traffic patterns of the local exchange network" (id., § 484.2305(f)). The Michigan Act also contains an express prohibition against the cross-subsidy of unregulated services. Id., § 484.2308.

Pursuant to the initial Michigan Act, and subsequent to the 1995 amended version, the MPSC has conducted various proceedings addressing local competition to ensure that competitors may readily enter the local exchange business and that customers will be able to send and receive calls without changing their phone numbers, regardless of their choice of carriers.[35]

In October 1994, the MPSC licensed City Signal, Inc. (now called Brooks Fiber) as a "co-carrier" providing "basic local exchange services" in competition with Ameritech in Grand Rapids.[36] On February 23, 1995, the MPSC entered the City Signal/Ameritech Interconnection Opinion establishing, on a transitional basis, the rates, terms and conditions that govern interconnection between Ameritech, Brooks Fiber, and other local exchange competitors. Interconnection arrangements would be available, without unreasonable discrimination, to any new providers entering the market. Id. at 85. See Wilk/Fetter Aff., ¶ 79. The MPSC also imposed, on an interim basis, reciprocal compensation provisions for terminating local telephone calls of the other company's customers, because "mutual compensation arrangements are critical

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[35] See generally In the matter of the application of CITY SIGNAL, INC., for an order establishing and approving interconnection arrangements with AMERITECH MICHIGAN, No. U-10647, 1995 Mich. PSC LEXIS 32 (Mich. Pub. Serv. Comm'n Feb. 23, 1995) ("City Signal/Ameritech Interconnection Opinion").

[36] See In re Application of City Signal, Inc., No. U-10555, 1994 Mich. PSC LEXIS 267 (Mich. Pub. Serv. Comm'n Oct. 12, 1994).

for the further development of local exchange competition." City Signal/Ameritech Interconnection Opinion, at 27.[37]

The initiatives taken by the MPSC and Ameritech to open the local exchange business in Michigan to the forces of competition were augmented, of course, by the passage of the 1996 Act and the Commission's regulations promulgated thereunder. As discussed in detail above in Sections III and IV, Ameritech has negotiated interconnection agreements with MFS, Brooks Fiber, US Network and WinStar Wireless; it has completed arbitrations with AT&T, MCI, TCG and Sprint; and, most importantly, Ameritech has fully implemented the competitive checklist.

2. The 1996 Act Does not Require that Competing Carriers Be of a Particular Size and Scope, or that a Particular Level of Competition Be Established.

There is no requirement in Section 271(c) that there be any particular level of actual competition in the local market, or that a competing provider be of a particular size or that its service be of a particular scope.[38] To the contrary, Congress expressly rejected such "metric"

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[37] In a follow-up Opinion and Order, issued June 5, 1996, the MPSC considered various interconnection issues generic to basic local exchange service competition. See In the matter, on the Commission's own motion, to establish permanent interconnection arrangements between basic local service providers, No. U-10860 (Mich. Pub. Serv. Comm'n June 5, 1996). Among other things, the Commission ordered Ameritech and GTE to file new studies justifying their rates for unbundled loops and ports. See id. at 7-8. At the same time, the Commission rejected MCI's proposed rates for termination of local traffic, and ordered Ameritech and GTE to file local traffic termination cost studies. Id. at 11. See Wilk/Fetter Aff., ¶ 80.

[38] The Department of Justice agrees. It "oppose[s] use of a metric test that requires the Bell operating company to have lost a specific market share or specific number of customers." "The Section 271 InterLATA Entry Process: Some Further Thoughts,"
(continued...)

tests, in favor of interconnection agreements and satisfaction of the "competitive checklist" requirement. For example, Senator Kerry proposed that competing providers of telephone exchange service must serve "a substantial number of business and residential customers." 141 Cong. Rec. S8319 (daily ed. June 14, 1995). The amendment was tabled on a motion by Senator Stevens, who argued that such a requirement would add "another burden to future competition." 141 Cong. Rec. S8321 (daily ed. June 14, 1995). See also 141 Cong. Rec. H8454 (daily ed. Aug. 4, 1995) (statement of Rep. Bunn) (noting that a threshold test, requiring that BOC competitors capture 10% of the local exchange business as a condition for BOC interLATA relief, was explicitly rejected by Congress). Congress, therefore, emphatically rejected the imposition of a "metric" test as a condition of interLATA authorization under Section 271. See Harris/Teece Aff., pp. 6-7.

3. Competing Providers Are Entering the Local Exchange Business in Michigan at a Rapid Pace.

As a result of the procompetitive actions already taken by this Commission, the MPSC, and Ameritech, there is no doubt that the local exchange services business in Michigan is open to competition and that powerful competing providers are entering that business and expanding their presence at a rapid pace. Some 13 competing providers have been certified as local

[38](...continued)
Remarks by David Turetsky, Deputy Assistant Attorney General, Antitrust Division, U.S. Department of Justice, before the Regional Oversight Committee, US West Region Regulatory Commissions, Minneapolis, Minnesota, Sept. 30, 1996, p. 14.

exchange carriers by the MPSC, and additional applications are pending.[39] Of the authorized carriers, Brooks Fiber, MFS/Worldcom, MCI Metro and TCG currently are providing facilities-based service in Michigan and have interconnection arrangements with Ameritech. See Harris/Teece Aff., p. 31. Facilities-based wireless transport services are provided by WinStar. Id. Local exchange service resellers currently operating in Michigan include US Network, LCI, Building Communications, and Coast-to-Coast. Id.

Indeed, the most powerful, sophisticated and well-financed telecommunications companies in the world, including AT&T, MCI and Sprint, are entering the local exchange business in Michigan. See Harris/Teece Aff., pp. 39-46, 62-67. An arbitrated interconnection agreement with AT&T has been approved by the MPSC, the MPSC has rendered a final decision in the Ameritech/MCI arbitration, and an agreement with Sprint is expected to be approved within the next few weeks.

AT&T, for example, has one of the best known brand names in the country as a result of a massive nationwide advertising budget, part of which targets Michigan. See Harris/Teece Aff., p. 63. Last June, the Chairman of AT&T, Robert E. Allen, issued what The Wall Street Journal termed a "bare-knuckled challenge" to the Bell operating companies in which Allen said that AT&T plans "to take at least a third" of the $90 billion local phone market within several years. Wall St. J., June 12, 1996, p. A3. Chairman Allen declared that AT&T is "streamlined

[39] See MPSC News Release, Dec. 20, 1996; Ameritech MPSC Submission, Attachment A, Response to Question No. 1, p. 11 n. 10, supra; Wilk/Fetter Aff., ¶¶ 74-75.

for competition" and that it "is going after the local service market with everything we've got." Id.

To make good on this competitive challenge, AT&T is devoting substantial resources to provide local exchange service to both business and residential customers in Michigan. For example, it is building a wireless network in southeastern Michigan to provide local service in 1997. See Harris/Teece Aff., pp. 62-63. In August 1996, AT&T signed an agreement with TCG, under which TCG provides local network access to AT&T in 9 markets, including the greater Detroit metropolitan area. See id., p. 47. This agreement will enable AT&T to bypass Ameritech's local network by diverting its traffic to TCG. See Gilbert/Panzar Aff., ¶ 77.

MCI Metro, currently owned by the second largest interexchange carrier in the United States, began offering facilities-based local service to business customers in Detroit in June 1996. See Harris/Teece Aff., p. 39. With 60 route-miles of SONET-based network, extensive switching capabilities, and 16 offices and operations across Michigan, MCI has made a substantial investment in its local exchange network in the State. Id. It has made arrangements with Ameritech in the Detroit area for the purpose of exchanging local traffic and is currently offering local exchange service to Detroit businesses (especially those whose buildings are on the company's SONET network). MCI Metro's initial local service products include basic local exchange service, business lines (including a "feature rich" line provisioned like Centrex), private branch exchange (PBX) trunks and access services to businesses. Id., p. 41. MCI

Metro frequently has said that it plans to offer local service to residential customers in various parts of the country. Id., pp. 43-45.

With the addition of local services, MCI, already a provider of long distance service, is the first carrier to have made "one-stop shopping" a reality for its business customers with the introduction of networkMCI One. This is an integrated package of services, including local, long distance and international services, plus additional services, such as cellular, internet access, paging data services and conferencing. Last summer, MCI advertised in Detroit newspapers that

> MCI is now providing local service in Detroit and, along with it, the sort of efficiencies and economies that businesses here could never take advantage of before. Like the opportunity to get an array of communication products and services — local, long distance, international, data, conferencing, cellular, paging and Internet — all on one bill. And all accompanied by the highly competitive volume discounts and customer assistance only MCI can offer. Competition is always good for business. In this case, it's going to be particularly good for yours.[40]

Detroit is one of 13 markets where networkMCI One is available today. See Harris/Teece Aff., pp. 41-42.

Sprint, the third largest interexchange carrier in the United States, also provides local exchange service. Sprint's local telephone operations, which serve 6.8 million residential and business customers in 19 states, adopted the Sprint name in May 1996. See Harris/Teece Aff., p. 66. With annual revenues of $12.9 billion, and with its PCS authorizations and alliances with cable television system owners (TCI, Comcast Corporation, and Cox Communications) and

[40] Ameritech MPSC Submission, Attachment A, Response to Question No. 6, Exhibit 6.2.

competitive access providers (including TCG), Sprint is very well positioned to compete in the era of integrated telecommunications services. Id.

Other prominent entrants into the Michigan local exchanges business, described in detail in Section III.C, supra, include Brooks Fiber, TCG, and MFS, an affiliate of MFS/Worldcom, the fourth largest facilities-based long distance company in the United States. See Harris/Teece Aff., pp. 33-38, 46-50.

Among resellers, USN Communications has entered into a broad-based local service resale agreement with Ameritech. The ten-year agreement regarding Michigan commits USN to resell a minimum of 100,000 Ameritech lines during that period. See Harris/Teece Aff., p. 55.[41]

A number of providers in Michigan already have established a significant presence by providing telecommunications services along with cable television service through agreements with owners of large multi-dwelling units ("MDUs"), including apartment buildings and condominiums. See Harris/Teece Aff., pp. 50-53. Ameritech's competitors, including Southwestern Bell, GE Capital-Res Com, OpTel, People's Choice TV and Brooks Fiber, have

[41] Michigan is one of eight states in which Frontier Telemanagement, a long distance and local services reseller, has been concentrating its efforts. In 1995, Frontier acquired seven companies and merged with another, ALC Communications, creating the fifth largest long distance company in the country, with annual revenues of more than $2.5 billion. See Harris/Teece Aff., p. 56. In the second quarter of 1996, Frontier began marketing its local services to business customers in Michigan. Id. Frontier has developed an integrated package of services, including long distance, voice mail, toll-free 800 and 888, paging, cellular and local. Id.

negotiated telecommunications service contracts with large real estate owners, providing springboards for integrated service offerings, combining local service, long distance service, cable television and a variety of vertical features. Id.

In addition to the competing carriers that are actually providing local service, several others (including LCI International, Continental Cable, BRE Communications and Comcast Telephony) have been certified by the MPSC to provide local service, and other applications are pending before the MPSC (including those of Coast-to-Coast Telephone and Tele-Phone Communications Inc.).[42] Continental Cable, for example, which has been acquired by US West, is expected to begin providing local telecommunications services in 1997 to both business and residential customers in 44 Michigan communities, including several in the Detroit area.[43] Its cable network in the area passes 465,000 homes that the company hopes to hook up to its own telecommunications service. See Harris/Teece Aff., p. 71. The company currently is upgrading its cable TV network with fiber optic cables. Id.

In short, the implementation by Ameritech of the competitive checklist, in conformity with the Commission's interconnection regulations and in the context of the MPSC's longstanding procompetitive policies, has opened the local exchange "bottleneck" to competition. As a result, some competing providers already have entered the local exchange business in

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42/ See Ameritech MPSC Submission, Attachment A, Response to Question No. 1.

43/ See Ameritech MPSC Submission, Attachment A, Response to Question No. 2, p. 4; Harris/Teece Aff., pp. 71-72.

Michigan, and the most powerful competitors are poised to enter on a large scale. The local exchange business in Michigan clearly is open to competition.

4. The 1996 Act, and Regulatory and Technological Constraints, Make it Virtually Impossible for Ameritech to Impede Competition in Long Distance Services.

As demonstrated above, Ameritech has complied with the Telecommunications Act of 1996 and implemented the applicable orders of the Commission and the MPSC. As a result, other telecommunications carriers are free to provide local exchange services in Michigan and, as discussed above, are lining up to do so. In addition, statutory, regulatory and technological constraints make it virtually impossible for Ameritech to use its position in local exchange services to obstruct competition in the provision of long distance services.

a. Safeguards Against Cross-Subsidization

Any assessment of the risk that Ameritech could use cross-subsidization to impede competition in long distance services should begin with a dose of economic common sense. Ameritech's long distance affiliate — which would begin with no customers — could not obtain market power in long distance services through cross-subsidization unless cross-subsidization would enable it to (1) embark on a predatory pricing scheme that would drive AT&T, MCI and Sprint out of long distance, and (2) then raise long distance prices significantly above competitive levels without losing significant sales.[44] As the Supreme Court has noted, even

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44/ See United States v. Western Electric Co., 900 F.2d 283, 296 (D.C. Cir.), cert. denied, 498 U.S. 911 (1990).

in unregulated industries, such "predatory pricing schemes are rarely tried, and even more rarely successful."[45] With these principles in mind, Ameritech obviously could not undertake a successful predation scheme against the entrenched long distance carriers, especially given the regulatory oversight to which it is subject.

AT&T, MCI and Sprint currently take in the vast bulk of total long distance revenue in the United States. These carriers have massive investments in network infrastructure, low incremental operating costs and substantial financial resources (including high operating margins) with which to combat any predation scheme. Ameritech, by contrast, will be a new entrant with zero market share in a business in which every customer already has a carrier. The Commission itself has recognized that, under these circumstances, "the danger of successful predation by BOCs in the interexchange market is small."[46] It should come as no surprise, therefore, that even prior to the 1996 Act, AT&T candidly acknowledged that "there is little reason to fear that Ameritech could monopolize the interexchange market — driving AT&T, MCI and Sprint out of business."[47]

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[45] Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 589 (1986).

[46] Non-Accounting Safeguards First Report and Order, ¶ 258. See also Gilbert/Panzar Aff., ¶¶ 83-86 (analyzing why Ameritech could not recover the significant costs it would incur in any attempted predation scheme).

[47] Comments of AT&T in Response to Ameritech's Motions to Remove the Decree's Interexchange Restriction, p. 26 (filed with the Department of Justice, Feb. 15, 1994). As AT&T's expert economist, Professor Sullivan, acknowledged, "[n]or is there anything to suggest that any market participant has (or is in a position to) price in a predatory manner — that is to set prices below incremental costs with the expectation of recouping
(continued...)

It is clear, therefore, that Ameritech could not undertake a successful "cross-subsidy/predation" scheme against the incumbent long distance carriers. And various statutory safeguards ensure that Ameritech would be unable to misallocate costs on the enormous scale that would be required to even attempt a predation scheme against AT&T, MCI and Sprint. Under Section 272 of the Act, for example, Ameritech will be able to provide in-region long distance service only through its separate affiliate, ACI, and ACI must operate independently from Ameritech and subject to Commission-prescribed accounting requirements. As the Commission recently recognized, this structural separation requirement and the Commission's accounting rules "will effectively prevent predatory behavior that might result from cross-subsidization."[48]

In addition, Section 272(d)(2) of the Act mandates an audit every two years "to determine whether [a BOC] has complied" with the separate affiliate safeguards, and the audit results will be open to public inspection and public comment before the FCC and the relevant state regulatory body. As the Commission has noted, such structural safeguards serve to "protect against potential anticompetitive behavior."[49]

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[47](...continued)
consequent losses through monopoly prices once competitors have been disciplined or dispatched." Id., App. C at 14-15.

[48] Accounting Safeguards Report and Order, ¶ 28.

[49] Non-Accounting Safeguards First Report and Order, ¶ 167. Moreover, under regulations that pre-date the 1996 Act, improved accounting requirements mandated by the Commission's rules further reduce the risk that any cost misallocation scheme would go (continued...)

Moreover, cross-subsidization is unlawful under Michigan's regulatory scheme. See Wilk/Fetter Aff., ¶¶ 27-63 (discussing how the Michigan Telecommunications Act specifically prohibits use of local exchange revenues to cross-subsidize other products or services offered by Ameritech or an affiliate). Thus, monitoring by the MPSC, which is armed with significant enforcement authority (see id., ¶¶ 40-42, 45), will overlap with similar monitoring by competitors and the Commission to protect against any possible risk of cross-subsidization. Furthermore, Ameritech could not increase its rates for local exchange services, a necessary step in any cross-subsidization scheme to deploy below-cost rates for long distance services, without satisfying the formidable conditions required for MPSC approval of a rate increase. See id., ¶¶ 53-63.

The normal market protection against a "cross-subsidy/predation" scheme — combined with the separate affiliate requirements of the Act, the Commission's accounting rules and monitoring by State regulators — makes it virtually impossible for Ameritech to engage in any undetected cross-subsidization scheme. In addition, Ameritech could not use interexchange access revenues to cross-subsidize long distance rates because under the Commission's pure price

[49](...continued)
undetected. As the court noted in United States v. Western Elec. Co., 993 F.2d 1572, 1580-81 (D.C. Cir.), cert. denied, 510 U.S. 984 (1993), the Commission "has acted since the break-up [of AT&T] to tighten its accounting rules, especially its treatment of joint costs, all tending to increase the chances of catching any attempts at cost-shifting." The Commission now has concluded that its "existing accounting safeguards . . . prevent subsidization of competitive nonregulated services." Accounting Safeguards Report and Order, ¶ 275.