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

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FEDERAL COMMUNICATIONS COMMISSION
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In the Matter of	)	
	)	
GTE CORPORATION,	)	
	)	
Transferor,	)	
	)	
and	)	File No. 98-184
	)	
BELL ATLANTIC CORPORATION,	)	
	)	
Transferee,	)	
	)	
For Consent to Transfer of Control	)	

JOINT REPLY OF BELL ATLANTIC CORPORATION AND GTE CORPORATION TO PETITIONS TO DENY AND COMMENTS

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EXECUTIVE SUMMARY

The proposed merger of Bell Atlantic and GTE will bring dramatic benefits to consumers, in the form of greater competition for local, advanced voice and data, long distance, and Internet services in markets throughout the nation, as well as bundled product offerings tailored to the demands of the modern telecommunications marketplace. These substantial benefits, moreover, would be unachieveable without the merger, as they flow from the particular combination of GTE's facilities-based national network, Bell Atlantic's base of large business customers, and the ability of the combined company to create a nationally recognized brand.

The principal opponents of this procompetitive merger, not surprisingly, are those carriers that are already serving, or positioning themselves to serve, the emerging market for bundled telecommunications services. These opponents have failed to identify any basis for this Commission to conclude that the merger is not in the public interest. They have not even attempted to refute the most critical procompetitive gains created by the merger -- benefits in the national market for bundled services and in the markets for advanced data and Internet services -- and their attempts to portray the merger as anticompetitive are tired and unavailing. Simply put, the Applicants have demonstrated that the merger will enhance competition, and the opponents have failed in their attempt to show otherwise. Accordingly, Bell Atlantic and GTE respectfully ask that the Commission grant the Applications.

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The merger of Bell Atlantic and GTE is strongly in the public interest, because it will produce substantial procompetitive gains in nearly every major telecommunications market, will allow the merged company to introduce a wider range of Internet and data services, and will spur broad-scale local competition in markets across the country. The GTE-Bell Atlantic merger will combine complementary capabilities to create a national facilities-based provider of the advanced services demanded by business customers, and will thus add a much-needed player to the concentrated national market for bundled telecommunications services. Moreover, the merger will bring broad, sustained, and effective competition to the local franchise territories of BellSouth, U S WEST, SBC, and Ameritech.

The comments filed in opposition to the merger serve only to prove that the marriage of GTE and Bell Atlantic will produce these real procompetitive benefits. The most vociferous objections have come from competitors who stand the most to lose from GTE-Bell Atlantic's combined ability to offer a national bundle of advanced data, voice, and Internet services -- the Big Three interexchange carriers AT&T, MCI WorldCom, and Sprint. Each of these three companies has itself merged its way to participation in the national market for bundled services, and is now attempting to fend off, for as long as possible, the full competitive potential of a united GTE-Bell Atlantic.

But the Big Three's assertions that the merger might produce anticompetitive consequences are insupportable. *First*, the merger will produce no loss of potential competition in GTE and Bell Atlantic's franchises. Neither GTE nor Bell Atlantic has plans to enter each other's markets, nor would they be among the most significant potential competitors if they did. *Second*, although the Big Three assert that the merger will enhance GTE and Bell Atlantic's incentive to engage in anticompetitive conduct in downstream markets, these identical claims have been repeatedly rejected by the Commission.[1] *Finally*, despite the efforts of AT&T, Sprint, MCI WorldCom and others to relitigate every interconnection dispute they have had with GTE or Bell Atlantic, their grab bag of specific grievances is the subject of other ongoing proceedings and has *no* nexus with the merger. The merger of GTE and Bell Atlantic presents no risk to competition, and certainly none that can eclipse the nationwide procompetitive gains it will bring to consumers of local, data, long distance, and Internet services, and is, therefore, decidedly in the public interest.

I. THE MERGER WILL PRODUCE DRAMATIC PROCOMPETITIVE BENEFITS IN EVERY TELECOMMUNICATIONS MARKET.

A. GTE-Bell Atlantic Will Be the First ILEC To Challenge the Big Three in the National Provision of Full-Service Telecommunications.

One of the most significant procompetitive benefits of the GTE-Bell Atlantic merger -- the creation of a new, fourth player in the national market for facilities-based bundled telecommunications services -- is not seriously contested by the merger's opponents. This emerging market, which is currently controlled by the Big Three, is of critical importance to the fulfillment of the Telecommunications Act's competitive goals, including the development of broad local competition.

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[1] *See In re Southern New England Telecommunications Corp.*, CC Docket No. 98-25, at ¶ 37 (Oct. 23, 1998) (hereafter *SBC/SNET Order*); *In re Applications of NYNEX Corporation and Bell Atlantic Corporation for Consent to Transfer Control,* FCC 97-286, 12 F.C.C.R. 19985, at ¶¶ 115-24 (Aug. 14, 1997) (hereafter *Bell Atlantic/NYNEX Order*); *In re Applications of Pacific Telesis Group and SBC Communications for Consent to Transfer Control*, FCC 97-28, 12 F.C.C.R. 2624, at ¶¶ 53-57 (Jan. 31, 1997) (hereafter *SBC/PacTel Order*).

There can be no dispute that the merger's primary opponents, AT&T, Sprint, and MCI WorldCom, are believers in the emerging national market for facilities-based bundled services -- a market that includes Internet backbone and connectivity services, advanced voice and data services, long distance service, and local telephone service. Each one of the Big Three has announced acquisition after acquisition to fill voids in their facilities-based product offerings and grow the scale of their existing businesses. The most obvious example is the merger of MCI and WorldCom, which combined the second and fourth largest long distance providers and -- but for the actions of this Commission and other regulators -- would have combined the first and second largest Internet backbones. WorldCom itself built its Internet backbone business by acquiring UUNet, ANS, and CompuServe, and gave itself local capability by purchasing MFS, Brooks Fiber, and now MCIMetro. Now that these acquisitions have been consummated, MCI WorldCom has launched a national "On-Net" advertising campaign asserting that it alone is able to offer a fully-integrated bundle of Internet, data, and voice services over a "wholly owned" and seamless global network."[2] In MCI WorldCom's own words, "Only one company has it," and its opposition to the GTE-Bell Atlantic merger is a veiled attempt to keep it that way.[3]

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[2] MCI WorldCom two-page advertisement, Wall St. J., Nov. 5, 1998, at B18-19 (hereafter MCI WorldCom Advertisement); *see also* MCI WorldCom 12-page advertising supplement, Wall St. J., Oct. 1, 1998, at R6-7 ("With MCI WorldCom On-Net, you get one connection for everything. Instead of separate lines for local, long distance, international voice and data, there's only one network, one contract and one company to take full responsibility. *Somewhere a choir of angels is singing*[!]. . . . No handoffs to other carriers. One network. One contract. One company. Nothing could be simpler. Or more cost-efficient.") (emphasis added).

[3] MCI WorldCom Advertisement, *supra* note 2, at B18-19.

Likewise, AT&T -- perhaps the most notable supporter of a national facilities-based strategy -- has announced or consummated *six* acquisitions or joint ventures in the last few years. After expanding its wireless footprint by acquiring McCaw, AT&T recently announced a second cellular acquisition, agreeing to purchase Vanguard Cellular. In 1998 alone, AT&T announced that it will acquire Teleport Communications Group -- a local service provider -- and Tele-Communications, Inc., the second largest cable company in the United States and a direct gateway into one-third of the nation's homes.[4] AT&T also recently formed a $10 billion joint venture with British Telecommunications, allowing it to expand its international capabilities, and, just this month, announced a $5 billion deal to purchase IBM Global Networks -- an Internet backbone provider. There is no dispute over why AT&T is pursuing this relentless acquisition strategy. As the *New York Times* recently reported:

> Shortly after he arrived at AT&T, the No. 1 long distance company, [AT&T's Chairman C. Michael] Armstrong said the company needed to strengthen its strategies for breaking into the local communications market, for expanding its international presence and for beefing up its advanced data services, especially those based on Internet technologies.
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> . . .
>
> I.B.M.'s Internet service, which is a major part of its data network, has more than a million individual users in 59 countries. More important, it has local ports into its network all over the world. *This is a big plus in attracting the large corporate customers that are the grand prize for telecommunications companies.*[5]

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[4] *See* Rebecca Blumenstein & Stephanie N. Mehta, *AT&T Says it Shouldn't Have to Grant Internet Access Via Upgraded Cable Lines*, Wall St. J., Nov. 17, 1998, at B6 ("TCI and its various partners potentially give AT&T access to one-third of American homes.").

[5] Seth Schiesel, *AT&T Buying I.B.M. Network*, N.Y. Times, Dec. 9, 1998, at C1 (emphasis added).

The Commission itself has recognized that there is an emerging market for "global seamless services," that there is a "consumer benefit associated with bundling," and that competition in this market is limited to "only a handful of major competitors world-wide."[6] Competition in this market is not keeping pace with the demand for bundled Internet, data, long distance, and local services.[7] GTE market research establishes that 86 percent of large business customers are interested in purchasing multiple telecommunications services from one provider and 68 percent are interested in having a single supplier serve all of their offices, regardless of geographic location.[8] This research is confirmed by numerous reports from independent analysts and industry experts,[9] and by first-hand testimonials from large business customers.[10]

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[6] *Bell Atlantic/NYNEX Order* ¶ 112; *In re Merger of MCI and British Telecommunications,* GN Docket No. 96-245, 12 F.C.C.R. 15351, at ¶ 91 (Sept. 24, 1997); *see also id.* ¶ 56-57 ("global seamless services market . . . will prove to be one of growing importance over time"); *In re Sprint Corporation*, File No. ISP 95-002, 11 F.C.C.R. 1850, at ¶ 84 (Jan. 1, 1996).

[7] *See* Reply Declaration of Thomas W. Hazlett (attached as Appendix D) (explaining why a properly conducted event study of the stock market confirms that GTE-Bell Atlantic's merger is viewed as increasing competition with the Big Three).

[8] *See* Joint Declaration of Jeffrey C. Kissell and Scott M. Zimmerman ¶ 5-6 (attached as Appendix B) (hereafter Kissell-Zimmerman Declaration).

[9] *See* Declaration of David J. Teece ¶¶ 13-18 (attached as Appendix A) (hereafter Teece Declaration); *see also Business Branding & Bundling Telecommunications Services,* Strategis Group (visited Dec. 18, 1998) <http://www.strategisgroup.com/ press/pubs/bbz.html> (79 percent of business telecommunications managers would prefer to receive a bundle of two or more services from a single provider).

[10] *See, e.g.*, Letter from Occidental Petroleum Corp. in Support of GTE-Bell Atlantic Merger at 1 (Nov. 18, 1998) ("This merger is a positive attempt to address telecommunication user needs and interest. As a user, it will satisfy my requirements for access to services on a regional, national, and global basis. It will provide the full bundle of telecommunications capabilities. These are the clear signals that I not only hear from my peers but that I strongly endorse.");

Nevertheless, only a small percentage of business customers currently purchase a full bundle of telecommunications services from one provider.[11] The merger will allow GTE-Bell Atlantic to compete on equal footing with the Big Three in this critical emerging market by enhancing its capabilities in three key market segments: advanced voice and data services, Internet services, and long distance service.

1. The Merger Will Allow GTE-Bell Atlantic To Deploy a Broad Range of Advanced Data Services and Bring These Services To New Markets Across the Country.

The merger will allow GTE and Bell Atlantic to integrate their data traffic onto a unified national network, which will bring a number of substantial benefits to consumers. *First*, the merger will allow the combined company to expand into far more cities than either company is currently planning to reach. Both GTE and Bell Atlantic have projected the amount of traffic they can expect to generate by offering service in cities across the United States. GTE is currently planning to build points of presence (POPs) on its Global Network Infrastructure (or GNI -- GTE's national network) in cities across the United States, but predictably, many cities fall below the traffic volume cut-off required to justify the necessary investment. These traffic projections were reviewed by our expert economist, David Teece, who concluded that, when aggregated, the combined company's projected traffic volumes would be large enough to justify

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Letter from Bear Stearns & Co. in Support of GTE-Bell Atlantic Merger at 1 (Nov. 19, 1998) ("We believe that the merger will foster competition, thus providing Bear Stearns with product and service choices that were previously unavailable to us. We look to the new company to provide a blanket of services to cover our company instead of the patchwork solutions that we are forced to assemble today.").

[11] *See* Kissell-Zimmerman Declaration ¶ 5.

bringing advanced voice and data services to at least 11 new markets that neither company alone could reach. If the new company were to add these markets to the GNI -- 9 of which are outside of the Northeast -- that would create roughly a 15 percent increase in the geographic coverage of GTE's network.[12]

Second, by aggregating GTE and Bell Atlantic's traffic onto a single network, the merger will lower the unit cost of providing advanced services by at least 10 percent, making the combined company's offering more competitive than either company's alone.[13] This unit cost reduction is only a fraction of the total GNI efficiencies that will be realized, because it only accounts for data traffic, and not Bell Atlantic's large combined volume of long distance and Internet Protocol traffic.[14]

Finally, the merger will extend to Bell Atlantic customers the advantage of connecting to a national -- as opposed to a regional -- facilities-based network. This benefit is substantial because many large business customers will only purchase advanced services from suppliers that offer national facilities-based coverage. Indeed, facilities-based providers enjoy a number of advantages over resellers:

- *Ability to provide a full-range of services.* Some services in high demand by large business customers -- and particularly by multi-locational Fortune 500 companies -- are not available for resale on competitive terms. Virtual Private Network services (VPN),

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[12] *See* Teece Declaration ¶¶ 47-48.

[13] *See id.* ¶ 49.

[14] *See id.*

for example, are not available for resale on terms that can compete with the Big Three's retail offerings.[15]

- *Broader geographic coverage*. Even those services that are available for resale are not available in as many locations as can be reached by a facilities-based provider. For example, if Bell Atlantic wished to achieve national ATM reach, it would have to resell services from multiple wholesalers, increasing its costs for billing, back-office support and back-haul, and rendering its ATM offering uncompetitive. Because GTE is planning to place ATM switches in dozens of cities outside of the Northeast (and could place them in numerous additional cities if Bell Atlantic's traffic is added to the GNI), the merger will dramatically expand GTE-Bell Atlantic's ability to compete for out-of-franchise customers.[16]

- *Lower unit cost.* Facilities-based providers of advanced data services also enjoy a lower unit cost than resellers, stemming from their ability to aggregate larger amounts of traffic onto a single network and make network investment decisions driven by their own (as opposed to resellers' generic) marketing strategies.[17]

- *Ability to provide service guarantees.* Resellers are handicapped in their ability to provide service guarantees to customers -- something that most large businesses will not do without. Facilities-based providers can provide these guarantees readily, because they have the ability to engineer and control their own networks and can therefore react quickly and directly if trouble occurs.[18]

These procompetitive benefits, none of which is contested by the merger's opponents, will be substantial. Because these services are designed, in significant measure, to link a customer's distant offices, large business customers want to purchase them from a company with a network that reaches as many markets as possible. By allowing GTE-Bell Atlantic to reach more markets than either could alone, the merger will make the combined company a more

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[15] *See* Second Declaration of Debra R. Covey ¶¶ 5-6 (attached as Appendix C).

[16] *See id.* ¶ 7.

[17] *See id.* ¶ 4.

[18] *See id.* ¶ 8.

competitive provider of advanced data services to customers seeking to link a number of remote locations. This capability, in turn, will make GTE-Bell Atlantic a more powerful competitor in out-of-franchise local markets, because it will allow the new company to compete effectively for business customers with anchor offices or affiliates in out-of-franchise locations.[19]

2. The Merger Will Bring New Services To Internet Customers -- Including Internet Telephony -- and Will Help Ensure That the Market for Internet Backbone Service Remains Competitive.

As AT&T's recent agreement to purchase IBM Global Networks demonstrates, Internet services are an integral element of the bundle demanded by both business and residential customers. GTE's own market research indicates that, among businesses that spend $60,000 or more on telecommunications services per year, 43 percent want Internet services to be provided as part of a product bundle.[20] As these businesses get larger -- particularly among Fortune 500 companies -- demand for Internet services approaches 100 percent.[21] By combining GTE's national high-speed facilities-based Internet backbone network with Bell Atlantic's customer relationships and marketing channels, the merger will enable GTE-Bell Atlantic to compete effectively against the Big Three in the markets for Internet backbone, connectivity, and hosting services.

Not one of the commenters disputes that the merger will allow GTE-Bell Atlantic to offer a broad range of Internet services to customers in new markets across the United States,

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[19] *See id.* ¶¶ 9-10.

[20] *See* Kissell-Zimmerman Declaration ¶ 6.

[21] *See id.* ¶ 7.

including CyberID, Site Patrol, and Universal Messaging -- all of which are directed at residential and small business customers.[22] Moreover, the merger will speed the introduction of Internet telephony as a competitive alternative to local and long distance telephone services. GTE and Bell Atlantic have highly complementary Internet telephony programs: GTE has developed much of the required technology, while Bell Atlantic owns a number of patents in the area that, when integrated with GTE's system, will make the service more efficient. Bell Atlantic also has technology and expertise managing gateways between IP telephony and PSTN networks, and providing Internet-based customer interfaces for operations support services -- capabilities GTE lacks. When these assets are combined with GTE's national IP network, the combined company will be in a unique position to offer Internet telephony as a competitive alternative to local and long distance service to business and residential customers across the country.

The merger of GTE and Bell Atlantic will also help to guarantee that the market for Internet backbone services remains competitive.[23] Because GTE Internetworking (GTEI) is the smallest backbone provider in the top tier, it faces a risk of losing its competitive position – a result that would create anticompetitive levels of concentration in the backbone market. This risk is only exacerbated by AT&T's proposed acquisition of IBM Global Network. Two of the three largest Internet backbone networks are controlled by MCI WorldCom and Sprint. The only other player in the top tier -- Cable & Wireless -- has yet to prove its competitive mettle; but if

[22] *See* Declaration of John T. Curran ¶ 4 (Oct. 2, 1998) (filed with original Application).

[23] *See id.* ¶¶ 7-8.

the difference between the price it paid for internetMCI ($1.8 billion for a 20 percent market share) and the price AT&T is offering to pay for IBM ($5 billion for a 2 percent market share) is any guide, Cable & Wireless is unlikely to remain a significant competitive force for long.[24] This leaves only GTEI -- which is significantly smaller than the three largest backbones -- as a bulwark against the Big Three's successful acquisition of oligopolistic control over the market for Internet backbone service.[25]

3. The Merger Will Allow GTE-Bell Atlantic To Provide National Facilities-Based Long Distance Service More Quickly and Efficiently Than Either Could Alone.

The GTE-Bell Atlantic merger will also have significant procompetitive benefits in the market for long distance service. Because GTE and Bell Atlantic will be able to consolidate their traffic onto one network, the merged company will be able to provide nationwide long distance service -- and all of the other advanced services provided over its national network -- at a lower unit cost.[26] The merger will therefore make GTE-Bell Atlantic's long distance service more competitive.

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[24] The price that an acquiror pays for an Internet backbone is both a function of the value of the network's customer base and the acquiror's ability to maintain that backbone's standing in the marketplace. (A company that has little use for an asset, no matter how valuable, will not be able to outbid a more efficient user of that asset.) Because Cable & Wireless was MCI's hand-picked successor -- selected in a back-room deal rather than a competitive bidding process -- and because their agreement was saddled with a number of conditions designed to weaken Cable & Wireless as an effective competitor, the low purchase-price paid for internetMCI strongly suggests that Cable & Wireless was intended to be little more than a shell.

[25] *See* Teece Declaration ¶¶ 52-54.

[26] *See id.* ¶ 49.

None of these points is disputed by the Big Three. Instead, they assert that the market for long distance service is already competitive -- relying presumably on the Commission's decision to approve the MCI WorldCom merger -- and hence would not benefit from the addition of a new facilities-based competitor.[27] This assertion is false.[28] In reaching its conclusion that the long distance market is *on the road to competition*, the Commission relied on the fact that new entrants, like GTE, were building national long distance networks.[29] But GTE can fulfill its role as a check on the Big Three's market power only if it can operate its network at an efficient unit cost -- something that it will have difficulty doing without concluding its merger with Bell Atlantic. Moreover, this response ignores the vital role that long distance service plays in the service bundle; 67 percent of large business customers want long distance service to be provided by the same carrier that supplies their other telecommunications services.[30] Without an efficient, competitively priced long distance offering, GTE and Bell Atlantic risk being frozen out of the already concentrated national market for bundled services.

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[27] *See, e.g.*, Petition to Deny of Sprint Communications Company L.P. at 67 (hereafter Sprint).

[28] *See, e.g.,* Paul W. MacAvoy, *The Failure of Antitrust and Regulation to Establish Competition in Long-Distance Telephone Service* 182 (1996) (describing "pattern of current coordinated price-setting behavior of the three large interexchange carriers").

[29] *See In re Application of WorldCom and MCI for Transfer of Control*, CC Docket No. 97-211, at ¶ 42 & n.119 (Sept. 14, 1998) (hereafter *MCI WorldCom Order*).

[30] *See* Kissell-Zimmerman Declaration ¶ 6.

4. Section 271 Is No Impediment To GTE-Bell Atlantic's Entry Into the Market for Bundled Services.

The Big Three and other commenters claim that the GTE-Bell Atlantic merger should be blocked because Bell Atlantic has not explained how it will comply with the 1996 Act's section 271 requirements. Their claims do not provide a basis for halting the transaction.

As an initial matter, the Commission recently approved SBC's acquisition of SNET over similar objections. It did so based on those parties' commitment to take whatever steps were needed to ensure that SBC complied with section 271 and related FCC orders.[31] Here, GTE and Bell Atlantic are equally committed to complying with all their legal obligations, including those that arise under section 271 with respect to the Bell Atlantic territories.

Moreover, contrary to the claims of the Big Three, Bell Atlantic has opened its local markets and is well on its way to obtaining section 271 relief. Its first application -- for New York -- will be filed with the FCC in the first quarter of 1999. That application will be unlike any filed previously. Beyond the fact that New York already is the most competitive local telephone market in the United States, the application will build on almost three years of extensive evidentiary proceedings at the state level that have resolved hundreds of issues raised by competitors. The application will include proof that each of the 14 checklist items not only is available, but actually is used by competitors, and that Bell Atlantic's operations support systems, and the interfaces to access them, can handle levels of demand in excess of current

[31] *See SBC/SNET Order* ¶ 37.

levels.[32] This proof includes both actual commercial experience successfully processing several thousand orders per day, and *two* thorough tests by independent third parties -- the most recent of which is being conducted under the supervision of the New York Commission and the Department of Justice. Moreover, the application will be based on a number of additional measures that Bell Atlantic agreed to in a pre-filing statement to the New York Commission[33] -- measures that go well beyond the requirements of the 1996 Act and that the Chairman of the New York Commission and the Department of Justice have made clear will cause them to support the application.[34] As a result, even competing local carriers agree that Bell Atlantic is entitled to long distance relief in New York.[35]

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[32] *See, e.g.,* Letter from Randal S. Milch, Bell Atlantic, to John C. Cary, Secretary - New York Public Service Commission, and Accompanying Joint Affidavit Case 97-C-0271 (Sept. 11, 1998); Results of Competitive Analysis, Case 97-C-0271 (Jan. 15, 1997) (identifying all 14 checklist items as being used by competitors).

[33] *See* Pre-Filing Statement of Bell Atlantic-New York, *In re Draft Filing of Petition for InterLATA Entry pursuant to Section 271 of the Telecommunications Act of 1996*, Case 97-C-0271 (filed with New York Public Service Commission, Apr. 6, 1998).

[34] *See* New York Public Service Commission News Release, *PSC Chairman Supports Conditions for Bell Atlantic's Entry Into Long Distance* (April 6, 1998) ("[I]f Bell Atlantic-New York meets all the steps outlined in its pre-filing . . . the local telecommunications market in New York will be fully and irreversibly open to competition and I would recommend that Bell Atlantic be permitted to enter into the long distance market."); Letter from Joel I. Klein, U.S. Department of Justice, to John O'Mara, Chairman - New York Public Service Commission (April 6, 1998) ("T]he Department of Justice has announced it will support applications under Section 271 based on a showing that the local telecommunications markets in a state are fully and irreversibly open to competition . . . . [I]t is our view that the Pre-Filing Statement filed by Bell Atlantic-New York, if fully and properly implemented, should support a conclusion that the New York local telephone market is 'fully and irreversibly open to competition.'").

[35] *See Pledging Allegiance to telco competition; Royce Holland, MFS's former chief, in the telecom game again*, Network World (Dec. 7, 1998) (Quoting Allegiance CEO Royce Holland:

In addition, Bell Atlantic will draw upon its New York experience to file prompt applications in a number of additional states -- a process that already has begun. For example, Bell Atlantic already has submitted pre-filing statements patterned on the New York model in two additional states -- Pennsylvania and New Jersey -- and proceedings in those states currently are underway.

Nor is there any question that Bell Atlantic has opened its local markets. The actions of competitors themselves are the best proof of this fact. Not only have competitors raised capital and invested in facilities in Bell Atlantic's region -- or in the case of the long distance incumbents, invested billions to buy local competitors with a major presence in Bell Atlantic's region[36] -- but they already are in business and operating. In fact, competitors already have captured approximately 1.3 million lines in Bell Atlantic's service areas, almost 800,000 of which are being served over the competitors' own facilities. Another half million of these lines are being served through resale, and over 60,000 lines are being served over unbundled loops. In addition, the number of interconnection trunks has grown to approximately 470,000 and more than 650 collocation sites already have been completed.

Consequently, Bell Atlantic reasonably expects to win long distance relief in the vast majority of its states prior to consummating its merger with GTE. It is possible, of course, that

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"If Bell Atlantic does everything it is promising the New York Public Service Commission it will do, then I expect Bell Atlantic will get approval by the first quarter next year to get into long distance.").

[36] For example, AT&T acquired TCG for $11.3 billion and is paying $48 billion for TCI, while MCI WorldCom acquired MFS and Brooks Fiber for a combined $39.4 billion.

the multi-stage long distance approval process may still be underway in one or more states by the time the companies determine to close the merger. If that turns out to be the case, Bell Atlantic may request limited interim relief from the Commission until it completes the long distance approval process in any remaining states.

The Big Three assert that the Commission is categorically barred from providing any measure of temporary relief. But this claim is contradicted by the plain terms of the Act and by Commission precedent. The Commission's authority to grant Bell Atlantic the limited relief it might require is expressly set forth in 47 U.S.C. § 153(25), which defines a "LATA" as "a contiguous geographic area . . . established or modified by a Bell operating company after [the Act's date of enactment] and approved by the Commission." Relying on this provision, the Commission has concluded that it does have authority to modify LATA boundaries and indeed, since passage of the 1996 Act, has "approved a significant number of LATA boundary modifications."[37]

The Commission could grant precisely the same kind of temporary relief here. For example, the long distance incumbents devote much of their attention to GTE's Internet backbone business, which they say is subject to section 271. Even assuming that is true, this is a perfect example of a market in which interim relief would be especially appropriate. An interim LATA boundary modification would ensure that the significant procompetitive benefits

[37] *In re Deployment of Wireline Services Offering Advanced Telecommunications Capability*, Notice of Proposed Rulemaking, CC Docket No. 98-147, at ¶ 190 (Aug. 7, 1998).

that the merger promises for Internet services will be realized while Bell Atlantic completes the section 271 approval process in one or more remaining states.

There is nothing radical or new about this result. In administering the Modification of Final Judgment (MFJ), Judge Greene granted numerous requests to modify LATA boundaries -- allowing traditionally interLATA services to be provided over a wider geographic area -- when doing so would enhance competition or speed the development of new telecommunications services.[38] That is precisely the result here. The merger of GTE and Bell Atlantic will bring a powerful new competitor to the markets for advanced voice and data, Internet, and long distance services. It would be affirmatively harmful for competition to stymie GTE-Bell Atlantic's ability to provide these services once the Commission has determined that Bell Atlantic has opened its local markets to competition in other 271 proceedings.

Nevertheless, the Big Three assert that 47 U.S.C. § 160(d) is an absolute bar to granting such relief.[39] Section 160(d) does not establish such a categorical rule; it only provides that the

[38] *See, e.g., United States v. Western Elec. Co.*, No. 82-0192 (D.D.C. Apr. 28, 1995) (wireless services); *United States v. Western Elec. Co.*, 1986-1 Trade Cas. 67,148 (paging services); *United States v. Western Elec. Co.*, No. 82-0192 (D.D.C. Feb. 26, 1986) (paging services); *United States v. Western Elec. Co.*, 1987-1 Trade Cas. (CCH) 67,452 (cellular services); *United States v. Western Elec. Co.*, No. 82-0192 (D.D.C. Feb. 18, 1993) (cellular services); *United States v. Western Elec. Co.*, No. 82-0192 (D.D.C. Sept. 20, 1994) (video and audio programming by satellite and other means); *United States v. Western Elec. Co.*, No. 82-0192 (D.D.C. Sept. 21, 1993) (cable service); *United States v. Western Elec. Co.*, No. 82-0192 (D.D.C. Oct. 24, 1994) (same); *see also United States v. Western Elec. Co.*, No. 82-0192 (D.D.C. Nov. 14, 1988); *United States v. Western Elec. Co.*, No. 82-0192 (Feb. 15, 1991); *United States v. Western Elec. Co.*, No. 82-0192 (May 11, 1994); *United States v. Western Elec. Co.*, 604 F. Supp. 256, 261 (D.D.C. 1984).

[39] *See, e.g.*, Petition of AT&T Corp. to Deny Application at 40-41 (hereafter AT&T); Sprint at 56-59.

"Commission may not forbear from applying the requirements of Section . . . 271 . . . until it determines that those requirements have been fully implemented." Bell Atlantic, in seeking a limited and temporary LATA boundary modification pursuant to clear statutory authority, would not be asking the Commission to "forbear" from applying 271. If the Commission were to grant a limited LATA boundary modification, Bell Atlantic would not be providing "interLATA" services, and thus no forbearance from section 271 would be necessary.

B. The Merger Will Create an Effective National Provider of Local Telephone Service.

By marrying a broad range of complementary capabilities, the merger of GTE and Bell Atlantic will create a strong local competitor able to enter out-of-franchise markets across the United States *swiftly and effectively*. Within 18 months of the merger's approval, GTE and Bell Atlantic are seeking to provide on an economic basis a complete bundle of services -- including advanced data and voice, Internet, long distance, and local services -- to business customers in 21 cities spanning the territories of every other RBOC.

GTE-Bell Atlantic will likewise offer a bundle of services to residential customers in cities where it is economically feasible to do so. In the first instance, GTE and Bell Atlantic have identified four target cities for possible expansion into the consumer market as Bell Atlantic receives its 271 approvals: Chicago, Miami, San Francisco, and Los Angeles. These cities, which were selected because they share calling affinities with New York and other cities in the Northeast, will be the first wave in a broader roll-out of bundled services for consumers. Cities that exchange significant amounts of traffic with GTE and Bell Atlantic's other major markets will quickly be added to this list as it becomes economically feasible to do so.

The merger of GTE and Bell Atlantic will give the combined company four new assets or capabilities that will make it a more effective out-of-franchise competitor:

1. *Ability to provide a full suite of facilities-based services.* As described above, the merger will allow GTE-Bell Atlantic to provide the complete bundle of facilities-based services demanded by anchor large business customers in more locations, and at a lower cost, than either company could alone.[40]

2. *Relationships with anchor customers.* The merger will also allow the combined company to market this full bundle of services to Bell Atlantic's large business customers in the Northeast that have offices or affiliates out-of-franchise. These customers have a great demand for bundled services, and want to purchase them from a provider that can offer facilities-based service to all of their remote locations. By bringing together Bell Atlantic's customer relationships and GTE's network capabilities, the merger will make it much more economical

[40] Throughout their submissions, AT&T, Sprint, and MCI WorldCom attempt to conflate the GTE-Bell Atlantic merger and the SBC-Ameritech merger and assert that the two mergers will have an identically deleterious impact on the public interest. *See, e.g.,* Comments of MCI WorldCom, Inc. at iii (hereafter MCI WorldCom). But the analogy between the two mergers is not apt. While the SBC-Ameritech merger would join two adjacent regional companies offering similar services, the GTE-Bell Atlantic merger is a marriage of GTE's national facilities-based Internet, data, and long distance network with Bell Atlantic's customer base. In short, the SBC-Ameritech merger combines two like firms; the GTE-Bell Atlantic merger combines two companies with dramatically different, yet highly complementary capabilities.

for the new company to provide local service to those customers in the 21 out-of-franchise cities identified by GTE's Chairman.

Bell Atlantic serves the headquarters of 175 of the Fortune 500 companies; GTE's ILEC franchise covers only 20.[41] Nevertheless, the merger's opponents contend that both GTE and Bell Atlantic could acquire the necessary number of anchor customers to reach most or all of the merged company's 21 target cities. In particular, the Big Three assert that, because "[l]arge business customers are sophisticated, . . . there is no reason to believe that GTE would have a competitive handicap in pursuing large businesses outside GTE's in-region service area."[42] Likewise, they assert that Bell Atlantic could follow its customers out-of-franchise on its own, and that none of the deficiencies in its suite of services, "separately or in combination, has the effect of precluding Bell Atlantic from pursuing its 'anchor customers' out-of-region without GTE."[43]

These assertions entirely ignore the substantial competitive disadvantage GTE and Bell Atlantic suffer without the ability to offer a full menu of facilities-based services throughout the country. GTE cannot target large business customers in Bell Atlantic's territory successfully because it lacks the ability to provide facilities-based local service to customers in the

[41] *See* Kissell-Zimmerman Declaration ¶ 15.

[42] Sprint at 63-64; *see also, e.g.*, Declaration of Stanley M. Besen, Padmanabhan Srinagesh and John R. Woodbury at 36 (hereafter Besen-Srinagesh-Woodbury Declaration).

[43] Sprint at 65; *see also, e.g.*, Declaration of Kenneth C. Baseman and A. Daniel Kelley ¶ 62 (hereafter Baseman-Kelley Declaration) ("Bell Atlantic, which under this theory is providing the important increments in traffic, would have had incentives for out-of-region entry even without the GTE merger.").

Northeast.[44] Likewise, without the ability to provide facilities-based Internet and advanced data services outside of its region, Bell Atlantic cannot compete effectively in the market for multi-locational customers.

The Big Three's claim that both GTE and Bell Atlantic could go it alone is also belied by an examination of the large business market in each of the 21 target cities. As detailed in the Kissell-Zimmerman and Teece Declarations,[45] GTE has prepared an illustrative analysis of the economics of entry into two of the markets that GTE Chairman Charles Lee identified to Congress: one in which the combined company will have some facilities and existing brand recognition; and another, in which the merged company will have neither facilities nor brand recognition. The results of GTE's analysis were overwhelming: Entries that were profitable for neither company alone *were* profitable for the merged company. Under one studied scenario, facilities-based entry in a medium-sized market employing an existing wireless switch was

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[44] Indeed, GTE's current out-of-franchise local exchange plans do not include the Northeast and, otherwise, are exceedingly limited. To date, GTE has only marketed local service to small business customers on a resale basis -- not to consumers or large businesses -- in eight near-franchise markets. In 1999, GTE is planning to provide out-of-franchise service in only one additional city. *See* Kissell-Zimmerman Declaration ¶ 13. Nevertheless, the Big Three point to hortatory statements in GTE's annual report, and made by GTE executives, to support their argument that GTE can mount a national out-of-franchise attack. *See* AT&T at 45; MCI WorldCom at 17-18. These statements do not bear the weight the Big Three try to lay upon them. For example, the Big Three tout GTE's statement that it will provide service "without regard to franchise boundaries," AT&T at 45 -- but that statement says nothing about the *scope, depth or pace* of GTE's out-of-franchise offering. Likewise, the Big Three's invocation of GTE's statement that it "can go it alone and win" -- a statement that was referring only to "GTE's ability to succeed in the competitive marketplace" -- says nothing about whether the merged company would be a *more effective* out-of-franchise competitor. *Id.*

[45] *See* Teece Declaration ¶¶ 41-43; Kissell-Zimmerman Declaration ¶¶ 16-19.

profitable for the combined company after 4.6 years, but was not for either company alone.[46] Moreover, the merger will allow GTE and Bell Atlantic to recover their initial investment, and earn a positive return, in a very short time frame.[47] Thus, in a second studied scenario, a facilities-based entry into a large market relying on the placement of a new switch turned profitable after only three years, whereas the analysis showed that neither company alone would be profitable within any reasonable planning horizon.

Because all of the other cities on GTE's target list fit one of the two profiles matching the studied entry cities, these examples show the benefits of the merger for the combined company's out-of-region entry plans. Moreover, this analysis comports with the Big Three's own statements before the Commission. As MCI WorldCom stated in its effort to secure approval for *its own* merger:

> For meaningful, facilities-based competition to develop, what is required is not more competitors, but *stronger* competitors. The merger will create a more forceful local competitor by combining two companies with complementary advantages. MCI has a broad-based marketing experience, and an expansive residential and large business base. WorldCom has a diverse business base and the local networks of MFS Communications, Inc. and Brooks Fiber Properties, Inc. Because the merged company can expand and accelerate the reach of its local facilities and draw on the existing customer base of the two companies, it will be far better able to compete in more locations than would either entity standing alone.[48]

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[46] *See id.* ¶ 17.

[47] *See* Kissell-Zimmerman Declaration ¶ 18.

[48] Second Joint Reply of WorldCom, Inc. and MCI Communications Corporation, CC Docket 97-211, at v (March 20, 1998).

3. *Broader deployment of GTE's bundled service operations support systems.* The merger will allow GTE-Bell Atlantic to take advantage of GTE's experience in developing its bundled service platform. GTE has spent two years building and operating this platform -- experience that should prove valuable in supporting GTE-Bell Atlantic's out-of-franchise strategy.[49]

4. *Creation of a new national brand.* Finally, the merger will allow GTE-Bell Atlantic to create a national brand at a much lower cost then either company could alone. Neither GTE nor Bell Atlantic has significant levels of brand recognition out-of-franchise. GTE, for example, has only 26 percent unaided brand recognition among consumers out-of-franchise and only 29 percent recognition among business executives out-of-franchise.[50] Yet, neither company alone can expect to generate enough return on its advertising investment to justify the creation of a national brand, because neither has the national presence required to serve a national customer base.[51] The combined company, on the other hand, will be able to develop a national brand more cheaply than either could alone by building on GTE and Bell Atlantic's complementary in-region brand strengths and capitalizing on enhanced marketing and advertising efficiencies.[52] This efficiency is substantial and, when coupled with the fact that

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[49] *See* Kissell-Zimmerman Declaration ¶ 20.

[50] *See id.* ¶ 24.

[51] For this reason, the Big Three's assertion that GTE and Bell Atlantic have the resources to build a national brand misses the mark. *See, e.g.,* Sprint at 21.

[52] *See* Kissell-Zimmerman Declaration ¶¶ 27-29.

GTE-Bell Atlantic will be able to earn a much greater return on its out-of-franchise advertising dollars, will make the combined company a far more powerful out-of-franchise competitor.[53]

The Big Three -- who have themselves invested hundreds of millions of dollars to build their own national brands -- attempt to minimize this benefit by making a number of arguments that are contrary to fact and flatly inconsistent with their own behavior. *First,* the Big Three argue that "the Commission should not put much faith in the claims of large 'global' . . . companies that they do not have strong brands. Both GTE and Bell Atlantic have strong brands."[54] This argument is contradicted by GTE's own marketing studies, identified above.

Second, the Big Three argue that GTE and Bell Atlantic's "brand is certainly well known by the large 'anchor' tenants they claim they need to succeed."[55] This assertion -- which is inconsistent with the marketing data identified above -- ignores the critical distinction between knowing a brand name, and knowing what that name represents. Neither GTE nor Bell Atlantic is known by large business customers *as a national provider of a full bundle of telecommunications services.* Without this kind of brand image, GTE-Bell Atlantic will be unable to convince anchor customers that it is able to serve all of their needs without regard to geographic boundaries. Large business customers will not commit to switch all of their services

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[53] *See* Teece Declaration ¶¶ 31-37.

[54] AT&T at 51-52.

[55] *Id.* at 52.

to GTE-Bell Atlantic without being convinced of this fact, and for large businesses as well as any other customers, brand recognition is a critical part of creating this impression.[56]

It is thus quite clear that the merger of GTE and Bell Atlantic will facilitate a more *rapid* out-of-franchise expansion and will allow the combined company to offer a *broader* range of services to out-of-franchise customers. The merger's opponents repeatedly point to GTE and Bell Atlantic's size as strong evidence that both companies could compete out-of-franchise on their own. MCI WorldCom asserts, in a characteristic accusation, that "CLECs, which are much smaller in revenue and profits, have invested substantial sums in order to attempt to enter the local exchange market that companies like GTE and Bell Atlantic are preventing them from entering."[57] But these accusations misconceive the requirements for broad and effective competitive entry into the territory of every other RBOC within 18 months. GTE and Bell Atlantic do not dispute that alone -- like many other successful CLECs -- each company would have the capabilities to enter a small number of new markets.

It is simply not relevant to the Commission's inquiry whether, given the size of the two companies' market capitalization or annual revenues, GTE and Bell Atlantic could purchase or build independently the capabilities each would need to compete on a national basis. Filling out GTE and Bell Atlantic's portfolios in this way would take *years*, and would bring out-of-franchise entry in a trickle rather than a torrent. By entering rapidly into as many as seven cities

[56] *See* Teece Declaration ¶ 31; Kissell-Zimmerman Declaration ¶ 23.

[57] MCI WorldCom at 14.

per RBOC, the GTE-Bell Atlantic merger will spark competition throughout the territories of BellSouth, U S WEST, SBC, and Ameritech.

C. Merger Synergies and Sharing of Best Practices.

Three years after the merger's close, GTE and Bell Atlantic estimate that the combined company will achieve $2 billion in annual revenue synergies, $2 billion in annual cost synergies, and $0.5 billion in annual capital synergies. Additional detail supporting these synergy estimates is provided in the Reply Declaration of Doreen Toben, attached as Appendix E.

The Big Three argue that GTE and Bell Atlantic's synergy estimates "are not sufficient to demonstrate either the magnitude of any gains attained subsequent to the merger or that the gains [a]re merger related."[58] But efficiency claims need only be concrete and nonspeculative, and are sufficient if verifiable by "reasonable means."[59] As MCI WorldCom asserted in support of its own merger -- and contrary to the Big Three's self-serving statements here -- efficiencies need not

> be individually quantifiable and audited. It would be unreasonable for Applicants to be held to this unreasonable standard: the efficiencies that will result from the merger are based on

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[58] Besen, Srinagesh & Woodbury Declaration ¶ 50; *see also, e.g.*, Sprint at 81 ("[n]o support" for synergies "is provided, and thus the applicants have not satisfied their burden of proof"). The Big Three assert, for example, that public interest gains stemming from the sharing of best practices "could occur without a merger" by "contractually exchanging best practice technology." *Id.* at 83-84. But the merger alone allows GTE and Bell Atlantic's best practices to be diffused. Because there is no way for firms operating at arms-length to see into one another's operations with any clarity, contractual arrangements for sharing best practices cannot be as effective as full integration. Only by placing GTE and Bell Atlantic under unified management can the companies' best practices be shared fully.

[59] *Bell Atlantic/NYNEX Order* ¶ 158.

> reasonable projections . . . . Obviously, future synergies are based on reasonable projections, and are necessarily subject to some uncertainty. WorldCom has traveled this road before and it has established a record of fulfilling, if not exceeding, the estimated synergies related to its acquisitions. It is particularly significant that, in estimating these projected savings, WorldCom relied on its substantial experience in acquiring other telecommunications carriers.[60]

In approving the MCI WorldCom merger, the Commission relied on proposed synergies and procompetitive benefits indistinguishable from those here to "conclude that Applicants have made a sufficient showing here of potential benefits to find that, on balance, the merger is in the public interest, convenience, and necessity."[61] Indeed, the Commission approved the MCI WorldCom merger primarily because,

> as a result of combining certain of the firms' complementary assets, the merged entity will be able to expand its operations and enter into new local markets more quickly than either party alone could absent the merger. For example, the Applicants claim that MCI Metro and Brooks Fiber will accelerate local city network deployment in secondary markets by 1-2 years. The complementary assets of the merged entity include MCI's national brand name, marketing experience and broad residential base, and WorldCom's extensive local exchange facilities, small and medium business customer base and foreign networks. We also find persuasive Applicants' assertions that the merger will allow them to service multi-location customers over their own networks, and that this will enable such customers to receive higher quality and more reliable services than each company is currently able to offer separately.[62]

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[60] Joint Reply of WorldCom, Inc. and MCI Communications Corporation, CC Docket No. 97-211, at 99-100 (Jan. 26, 1998)

[61] *MCI WorldCom Order* ¶ 197.

[62] *Id.* ¶ 199.

The merger of GTE and Bell Atlantic will achieve precisely the same procompetitive benefits -- from accelerating entry into all RBOC local markets within 18 months, to combining complementary brand assets and customer bases, to creating a new competitor able to provide a complete bundle of "higher quality and more reliable services" to "multi-location customers." The $4.5 billion in annual merger synergies identified by GTE and Bell Atlantic will help to finance all of these procompetitive ventures, and offer a compelling reason to approve the requested license transfer.

II. THE MERGER WILL NOT PRODUCE ANTICOMPETITIVE EFFECTS.

Beyond attempting to cast doubt on the numerous procompetitive benefits the merger promises to generate, the Big Three and other opponents seek to convince the Commission that the merger will give rise to a host of anticompetitive consequences. Broadly speaking, these anticompetitive arguments fall into two categories. *First*, the Big Three raise horizontal concerns about the impact of the merger: They contend that the merger will reduce competition in the market for local service by removing a potential competitor in certain markets,[63] by increasing the supposed incentives of GTE and Bell Atlantic to engage in anticompetitive behavior,[64] and by curtailing the ability of the Commission and other regulators to detect such behavior.[65] *Second*, the Big Three posit a variety of vertical concerns -- *i.e.*, concerns that the

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[63] *See, e.g.*, AT&T at 22-30; MCI WorldCom at 21-25; Sprint at 11-25.

[64] *See, e.g.*, AT&T at 12-14, 19-20; MCI WorldCom at 30-32; Sprint at 27-31.

[65] *See, e.g.*, AT&T at 20-22; MCI WorldCom at 32-37; Sprint at 40-55.

merged company will exploit its strength in the market for local service to attain unfair advantage in the markets for interLATA[66] and Internet services.[67]

These arguments are undoubtedly familiar to the Commission, because they differ little from those that have been raised in opposition to prior transfer applications, including SBC/PacTel, Bell Atlantic/NYNEX, SBC/SNET and, most recently, SBC/Ameritech.[68] The Commission has declined to block mergers on the strength of these arguments in the past, and the Big Three offer no persuasive reason to view the arguments any more favorably this time around. Under the Commission's well-settled standards, in order for a merger to be blocked on the ground that it will have anticompetitive effects, it must be shown that any incremental effect the merger would assertedly have on the Applicants' incentive and ability to engage in anticompetitive behavior is so severe as to outweigh the benefits to consumers that will flow

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[66] *See, e.g.,* AT&T at 30-33; MCI WorldCom at 37-39; Sprint at 31-33.

[67] *See, e.g.,* MCI WorldCom at 39-52.

[68] Indeed, Sprint does not even attempt to disguise the fact that it is resorting to stock anti-merger material, and has simply re-filed the same affidavits it recently submitted in opposition to the SBC-Ameritech merger. As noted above, the rationales for these two mergers, and the likely competitive effects, are not similar.

from the merger.[69] As we show in this section, and in the accompanying declarations,[70] the GTE-Bell Atlantic merger's opponents have not come close to meeting that standard.

C. The Horizontal Concerns Posited By the Merger's Opponents Do Not Withstand Scrutiny.

The Big Three contend that GTE and Bell Atlantic should be prohibited from joining forces because the merger would reduce competition in the market for local service. The merger will, in fact, have no such effect.

1. The Merger Will Not Eliminate One of the Most Significant Potential Competitors in Each Applicant's Territory.

The opponents' first contention -- that the merger will remove one of the most significant potential competitors in each Applicant's territories -- was anticipated and addressed at length in the Applicants' Public Interest Statement.[71] As explained therein, the local service areas of GTE and Bell Atlantic do not overlap, and the two companies do not compete against each other in the market for local service; the only issue, therefore, is one of potential competition, and even

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[69] *See SBC/PacTel Order* ¶ 42 ("[T]he basic competitive issue in this proceeding is not the market power or potential misconduct of [the Applicants] at present, but the incremental increase in that power or misconduct that will result from the proposed transfer."); *Bell Atlantic/NYNEX Order* ¶ 118, 120 (same); *id.* ¶ 2 ("A merger will be pro-competitive if the harms to competition . . . are outweighed by benefits that enhance competition."); *MCI/WorldCom Order* ¶ 10 (same).

[70] Declaration of Kenneth J. Arrow (attached as Appendix F) (hereafter Arrow Declaration); Declaration of Robert H. Gertner and John P. Gould (attached as Appendix G) (hereafter Gertner-Gould Declaration); Declaration of Robert W. Crandall and J. Gregory Sidak (attached as Appendix H) (hereafter Crandall-Sidak Declaration); Declaration of Jacques Crémer and Jean-Jacques Laffont (attached as Exhibit I) (hereafter Crémer-Laffont Declaration).

[71] GTE-Bell Atlantic Public Interest Statement at 24-33 (Oct. 2, 1998) (hereafter Public Interest Statement).

that issue is limited to certain areas of Pennsylvania and Virginia where GTE has some franchises located near Bell Atlantic territories.

The relevant question under the potential competition doctrine is whether the merger would result in the elimination of a "most significant market participant" -- *i.e.*, a potential competitor that would (in the absence of the merger) be "likely to have substantial future competitive significance" in the relevant market, *and* whose competitive role in that market could not be assumed by other present or potential market participants.[72] Given the large number of actual and potential competitors, neither GTE nor Bell Atlantic qualifies as such a potentially significant, let alone irreplaceable, competitor in the other's markets in Pennsylvania and Virginia.

As noted in the Public Interest Statement and in the accompanying Declaration of Jeff Kissell and Scott Zimmerman, GTE has no plans to enter Bell Atlantic's territory to offer local exchange service; likewise, Bell Atlantic has no plans to enter GTE's predominantly rural or suburban territories.[73] Unable to point to any actual plans of GTE and Bell Atlantic to make a significant entry into each others' territories, the opponents of the merger instead attempt to establish that, as ILECs operating in adjacent territories, GTE and Bell Atlantic are (on paper) uniquely "well poised" to make such entry -- and so well positioned as to constitute "most

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[72] *SBC/SNET Order* ¶ 18-19; *Bell Atlantic/NYNEX Order* ¶ 7; *MCI/WorldCom Order* ¶ 19-20.

[73] Public Interest Statement at 29-33.

significant market participants" in each others' territories.[74] This attempt fails. The purported advantages of ILECs in general, and adjacent ILECs in particular, are illusory.

As Professors Gertner and Gould explain in their accompanying declaration, the contention that ILECs enjoy significant advantages as potential entrants is contradicted by the available evidence (indeed, ILECs face certain disadvantages).[75] The Big Three point to ILECs' supposed "expertise in established complex systems to handle administrative capabilities (billing, order taking, customer care, etc.)" as an advantage not enjoyed by other possible non-ILEC entrants.[76] In reality, however, both of the inputs needed to provide such effective "back office" services are readily available to non-ILECs: The equipment needed for basic CLEC back-office systems can be purchased from a wide variety of well-established and experienced suppliers, and any specialized knowledge needed to run a local exchange business -- *i.e.*, human capital -- is likewise readily available (as individuals with ILEC experience can be, and frequently are, hired by CLECs). Such human capital, of course, may also be acquired by purchasing an ILEC.[77] Moreover, ILEC operations support systems are not readily adaptable for use in an out-of-franchise strategy that places any reliance on resale or unbundled network elements; entirely new platforms must be developed. And because any actual ILEC-specific

[74] *See*, *e.g.*, AT&T at 24.

[75] *See* Gertner-Gould Declaration ¶¶ 2, 17-43.

[76] Sprint at 11; *see also* AT&T at 23.

[77] *See* Gertner-Gould Declaration ¶¶ 21-22.

information is available through interconnection negotiations and other regulatory processes, CLECs have equal access to any data that would aid their competitive efforts.[78]

Market evidence confirms the insight that ILEC experience does not provide a carrier with a *per se* advantage over other potential local service competitors. As noted above, if ILEC experience provided any great advantages, then purchasing an ILEC would be an appealing strategy for a CLEC bent on entering the local telephone business. However, two of the Big Three -- MCI WorldCom and AT&T -- have announced their intention to enter the local telephone business, yet have spent large sums to acquire CLECs or cable companies with *no ILEC experience whatsoever*, and at the same time have not purchased any independent ILECs. The opponents' own actions thus belie their claim that ILEC status confers important advantages on potential entrants in the local service market.[79]

The Big Three are equally mistaken in arguing that because GTE and Bell Atlantic are not merely ILECs, but *adjacent* ILECs, in parts of Pennsylvania and Virginia, they enjoy special advantages that make them the most likely entrants into each other's territories. As an initial matter, the two Applicants have widely differing operations and customer bases in those two Commonwealths -- Bell Atlantic's presence is concentrated in urban areas, while GTE serves customers primarily in rural or sparsely populated areas and smaller towns that are well removed from the larger urban centers. AT&T nonetheless claims ILECs have an advantage insofar as they can use remote switching modules and digital loop carriers to serve customers within a 125-

[78] *See id.* ¶¶ 24-26.

[79] *See id.* ¶ 32.

mile radius of their existing switches. As Gertner and Gould demonstrate, however, this is no unique advantage: A large number of other ILECs and CLECs have facilities situated within 125 miles of GTE and Bell Atlantic customers in Pennsylvania and Virginia. Indeed, fully 100 percent of GTE customers in the two states that reside within 125 miles of a Bell Atlantic switch are also within 125 miles of 10 other firms' switches.[80] The statistics for Bell Atlantic customers residing within 125 miles of GTE facilities are comparable.[81]

In addition to trumpeting the 125-mile radius theory, AT&T claims that Bell Atlantic and GTE have a name-recognition advantage over other potential competitors in Pennsylvania and Virginia. But in Bell Atlantic's states outside of GTE's franchise, GTE has only 15 percent unaided brand recognition among consumers and 17 percent among business executives.[82] Likewise, in GTE's Pennsylvania and Virginia franchises, Bell Atlantic has only 14 percent unaided recognition among consumers and 15 percent among business executives.[83] Other potential entrants like the Big Three have brand names that are far better known.[84]

It bears emphasizing, moreover, that the Commission's *Bell Atlantic/NYNEX Order* in no way established a rule that adjacent ILECs necessarily enjoy special advantages as potential entrants into each other's service areas. For a host of case-specific reasons, the Commission

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80 *Id.*

81 *Id.*

82 *See* Kissell-Zimmerman Declaration ¶ 24.

83 *See id.* ¶ 24.

84 *See id.* ¶¶ 21-26; Teece Declaration ¶¶ 31-37.

there concluded that the mass market local services offered by Bell Atlantic represented the "'second choice' alternative for a significant number of customers" in NYNEX's LATA 132 territory.[85] Significantly, moreover, our opponents do not, and cannot, contend that those special factors are present in Bell Atlantic and GTE's adjacent territories.

As stated in the Public Interest Statement, the number of actual and potential entrants in Bell Atlantic and GTE's territories is large. Because Bell Atlantic and GTE's status as ILECs (even adjacent ILECs) gives them no unique advantages as potential entrants in each other's service territories, neither can properly be considered a potentially significant, and certainly not an irreplaceable, competitor in the other's Pennsylvania or Virginia territories.

2. The Merger Will Not Increase Any Supposed Incentives of Bell Atlantic and GTE To Engage in Anticompetitive Behavior.

In addition to arguing that the merger would eliminate a potential competitor, the Big Three offer two theories as to why the supposed incentives of Bell Atlantic and GTE to engage in discriminatory conduct will increase as a result of the merger. *First*, relying on materials previously submitted by Sprint in opposition to the pending SBC-Ameritech transfer application -- namely, a declaration by Michael L. Katz and Steven C. Salop -- the opponents assert that the merged entity will have a greater incentive to engage in unlawful exclusionary behavior in local service markets than either GTE or Bell Atlantic would alone, because the merged entity's wider footprint would supposedly allow it to "internalize" the "spillover" effect of discriminatory

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[85] *Bell Atlantic/NYNEX Order* ¶ 108; *see also id.* ¶¶ 73-77.

behavior that presently goes uncaptured.[86] *Second*, the Big Three contend that allowing this merger to proceed would (especially if the SBC-Ameritech merger were also approved) produce a situation in which the resulting powerful entities would enter into a "non-aggression pact," declining to compete in each others' territories for fear of retaliatory entry.[87]

Neither of these arguments provides a basis for the Commission to find that the merger is not in the public interest. The accompanying Declarations of Robert W. Crandall and J. Gregory Sidak and of Jacques Crémer and Jean-Jacques Laffont demonstrate that the Katz-Salop theory is devoid of empirical support, ignores the effectiveness of regulatory safeguards, and even on its own terms is deeply flawed as a matter of game theory analysis.[88] It would be economic caprice for the Commission to use such a hypothetical "spillover" model -- one that cannot even produce coherent predictions of exclusionary conduct -- to inform the agency's public interest review of the merger.

The opponents' "non-aggression pact" argument is likewise wholly speculative, theoretically unsound, and belied by reality.[89] *First*, there is simply no empirical support for the suggestion that ILECs have tacitly agreed not to compete in each others' territories. ILECs nationwide face considerable competition from a host of providers, including CLECs and other

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[86] Declaration of Dr. Michael L. Katz and Dr. Steven C. Salop, *Using a Big Footprint to Step On Competition: Exclusionary Behavior and the SBC-Ameritech Merger* (Oct. 14, 1998); *see also* AT&T at 12-14; Sprint at 25-31.

[87] *See* AT&T at 8, 33-36; MCI WorldCom at 31-32.

[88] *See* Crandall-Sidak Declaration ¶¶ 21-33; Crémer-Laffont Declaration.

[89] *See* Arrow Declaration ¶¶ 45-50.

ILECs (or their affiliates). *Second*, the claim that ILECs have reached, or will reach, such "non-compete" agreements is also flatly inconsistent with our opponents' theory that GTE and Bell Atlantic are likely entrants into each other's territories. *Finally*, the argument rests on an outdated view of the telecommunications marketplace. In the post-1996 Act world, ILECs face competition in their local markets from a host of CLECs, including large national entities such as MCI WorldCom, Sprint and AT&T. Accordingly, any "non-aggression pact" concluded by ILECs would be quickly rendered useless and dangerously counterproductive, because the colluding ILECs would be overrun by competition from CLECs and would (by virtue of their pact) be unable to respond by seeking new revenue sources in the other colluding ILEC's territory. In short, the Commission's public interest analysis should not be sidetracked by the Big Three's unfounded and theoretically unsound speculation about "spillovers" and "non-aggression pacts."[90]

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[90] In addition to the spillover and non-aggression pact theories, the Big Three argue -- surely more as a rhetorical point than a serious one -- that the merger will increase the new company's incentive and ability to engage in anticompetitive behavior because GTE would be able to "teach" Bell Atlantic its approach to negotiation, regulation and litigation (which approach, these opponents assert, is obstructionist). *See, e.g.*, AT&T at 14-16; *compare* Rebecca Blumenstein & Stephanie N. Mehta, *AT&T, Known for Its Gentlemanly Ways, Gets Tough*, Wall St. J., Dec. 21, 1998, at B4. As we explain in Part III and Appendices J and K, the opponents' complaints about GTE's practices in this regard are predictable, tired and unfounded. Moreover, the Commission has consistently refused to sanction licensees for engaging in tough negotiations and vigorous advocacy, and any attempt to do so would raise serious constitutional questions. *See, e.g., SBC/PacTel Order* ¶¶ 36-37.

3. The Merger Will Not Hinder the Ability of This Commission or Other Regulators To Detect and Deter Any Anticompetitive Conduct.

The Big Three contend, finally, that the merger should be blocked because it will reduce by one the number of ILECs and thereby hamper the Commission's ability to regulate through the use of benchmarks.[91] This argument falls short of the mark. Even if a meaningful benchmark were eliminated as a result of the merger -- which will not be the case -- that would provide no sound policy justification for disapproving the Application. Benchmarking may be a useful regulatory tool, but a small loss in the effectiveness of one regulatory tool in certain circumstances cannot justify the great loss of procompetitive benefits that would follow from disapproval of the GTE-Bell Atlantic merger. Moreover, in contending that the merger will eliminate an important benchmark, the opponents exaggerate both (1) the importance of benchmarking in modern telecommunications regulation and (2) the change in the number of relevant benchmarks that would result from a merger of Bell Atlantic and GTE.[92]

First, the opponents overstate the importance of benchmarking by ignoring important changes that have occurred in the telecommunications industry since the passage of the 1996 Act, the effect of which has been to reduce the importance of the types of benchmarks relied on in the past by the FCC and state regulatory agencies. One significant change, for example, is the imposition upon ILECs of the obligation to allow entry by CLECs through the process of interconnection negotiations and arbitrations: The interconnection obligation has rendered cross-

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[91] *See, e.g.*, Sprint at 46-49, MCI WorldCom at 32-36.

[92] *See* Arrow Declaration ¶¶ 5-39.

company comparisons considerably less important than they were prior to the 1996 Act, and has effectively expanded the number of relevant benchmarks.[93] Each interconnection agreement must be agreed to by the CLEC, as well as the relevant ILEC and state regulatory agency. Each interconnection agreement includes specific performance standards and a detailed schedule of charges; all such agreements are public. The 1996 Act thus makes each separate state commission a benchmarking authority and each separate operating company, rather than the ultimate regional holding company, the relevant benchmark. In addition, in many instances, the Commission has benchmarked what ILECs do for competitors against what they do for themselves. Thus, the Act has actually created a far greater number of benchmarks than the seven RBOCs created by the MFJ.

Second, even with respect to issues for which cross-company comparisons (instead of ILEC-CLEC comparisons) remain important, the Big Three overstate the significance of the loss of GTE as a benchmark. The Commission itself has concluded on many occasions that there are important differences between GTE and the RBOCs for regulatory purposes. In 1987, for example, the Commission stated that "an analysis of GTE's service areas demonstrates that although in the aggregate GTE is smaller in size to each BOC, unlike the BOCs, its service areas are distributed nationwide in a large number of noncontiguous geographical areas."[94] More

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[93] *See id.* ¶¶ 11-13.

[94] In the Amendment to Sections 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry) and Policy and Rules Concerning Rates for Competitive Common Phase II Carrier Service and Facilities Authorizations Thereof Communications Protocols under Sections 64.702 of the Commission's Rules and Regulations, Report and Order, 2 F.C.C.R. 3072, at ¶ 203 (1987).

recently, Chairman Kennard noted that "GTE always has been treated differently [than the RBOCs] because it is smaller and less geographically focused."[95] Indeed, the Commission just last week reaffirmed its view that the different characteristics of GTE and the BOCs justify different regulatory treatment.[96] Because of these differences between GTE and the RBOCs, GTE's value as a benchmark for RBOCs is limited. And even to the extent that independent LECs such as GTE have relevance as benchmarks for the RBOCs on certain issues, a multitude of independent LECs -- including Sprint's LEC subsidiaries, ALLTEL, Frontier, Cincinnati Bell and others -- will remain after the merger.[97]

B. The Merger's Claimed Adverse Vertical Concerns Are Likewise Illusory.

In addition to the claimed horizontal concerns, the Big Three contend that the proposed merger raises vertical concerns -- namely, that Bell Atlantic and GTE would seek unlawfully to leverage their presence in the market for local services to gain unfair advantage in downstream markets. Our opponents' contentions on this score are, for the most part, merely a rehash of the hackneyed arguments that ILECs can discriminate against rivals by engaging in price squeezes (raising local access prices) or non-price discrimination (such as degradation of signal transmission quality). The Commission has repeatedly rejected those arguments as a basis for

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[95] *Kennard Says FCC Will Seek Sec. 271 Stay, Then 'Use Every Tool,'* Washington Telecom Newswire, Jan. 2, 1998.

[96] *See* Brief for the United States and the Federal Communications Commission in Opposition to Certiorari in Nos. 98-652 and 98-653, *SBC Communications Inc., et al. v. FCC, et al.* (U.S. Dec. 18, 1998) at 18-20.

[97] *See* Arrow Declaration ¶¶ 20-21.

blocking proposed mergers,[98] and should do so again here. The only new twist on the vertical effects theme is MCI WorldCom's contention that the merged entity will somehow be better able to leverage its local exchange presence into a dominant position in the market for Internet service. This novel iteration of the vertical-discrimination argument is even less persuasive than its traditional form.

1. The Merger Will Not Increase the Merged Entity's Ability To Discriminate, Either By Raising Local Access Prices or By Non-Price Means.

Several opponents, and particularly the Big Three, contend that the Application should be denied because a combined GTE-Bell Atlantic will have the incentive and ability to discriminate against its rivals in downstream markets by charging rivals elevated prices for necessary access services as well as by engaging in non-price discrimination.[99] As in the earlier cases, the opponents' argument is flawed in two fundamental respects. *First*, there is no evidence that ILECs have actually engaged in discriminatory acts of the price squeeze or non-price variety, much less the sort of empirical support that would be necessary for the Commission to base its decision on this argument. *Second*, and even more importantly in this context, our opponents are unable to establish that the new company would have any greater incentive or ability to engage in these types of discriminatory conduct *as a result of the merger*.

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98 *See, e.g.*, *SBC/PacTel Order* ¶¶ 52-57; *Bell Atlantic/NYNEX Order* ¶¶ 117-20; *SBC/SNET Order* ¶¶ 23-24.

99 AT&T at 30-33; MCI WorldCom at 36-52; Sprint at 31-40.

The suggestion that ILECs can succeed in a strategy of price-squeeze discrimination against rivals in downstream markets is fanciful. Numerous regulatory safeguards are in place to guard against the danger of price squeezes: The price of access is regulated, and existing imputation and structural separation rules already prevent price squeezes. The Commission has previously concluded that these safeguards are adequate to protect against the alleged danger of price squeezes,[100] and the evidence strongly confirms that assessment.[101] For example, GTE presently provides long distance service, yet the opponents are unable to point to any diminution in competition in the long distance market or any other evidence that GTE is engaging in price squeezes. Bell Atlantic, likewise, has been providing interLATA toll service in the corridors from New Jersey to New York and Pennsylvania and intraLATA toll service in competition with the long distance carriers with no evidence that it has engaged in a price squeeze.

Even if these existing safeguards were somehow incapable of detecting all price discrimination, it bears emphasizing just how difficult it would be for an ILEC successfully to execute a price squeeze. As Crandall and Sidak explain, an ILEC pursuing a price squeeze strategy would have to engineer a squeeze that, at a minimum, was sufficiently severe and lengthy (but all the while undetectable) as to drive some current competitors from the market.[102] If the ILEC did not succeed in driving one or more carriers from the market, then the new low-price equilibrium would simply remain in place, to the benefit of consumers. And even driving

[100] *See, e.g., SBC/PacTel Order* ¶ 53; *Bell Atlantic/NYNEX Order* ¶ 117.

[101] *See* Crandall-Sidak Declaration ¶ 32-37.

[102] *Id.* ¶ 36.

a competitor from the market would not guarantee success, since the fiber-optic capacity of the ousted carrier would remain -- ready for another carrier to purchase at fire-sale prices and use to undercut the ILEC's noncompetitive prices. The Big Three fail to acknowledge these difficulties, and cannot explain how an ILEC could employ a price squeeze to drive IXCs from the market.

The case for non-price discrimination is equally unconvincing. *First*, as the Commission stated in the *Bell Atlantic/NYNEX Order*, such non-price discrimination would violate several provisions of the Communications Act.[103] Most of these forms of non-price discrimination would be entirely detectable. Indeed, the theory of non-price discrimination is based on the implicit, and implausible, assumption that an ILEC could engage in some form of technological discrimination that is detectable by customers (who would have no incentive to switch to the discriminating carrier if they could not detect the degradation), but undetectable by rivals (including large, sophisticated firms like the Big Three) and regulators.[104]

Second, as with price-squeeze discrimination, the evidence suggests that even if ILECs had an incentive to engage in non-price discrimination, they have been utterly unable to do so in practice. If the Big Three are correct that ILECs have an incentive to engage in non-price discrimination, that incentive would be present in the markets in which ILECs provide access service to other carriers that compete with them in downstream markets. In particular, the theory should apply to cellular service, where for many years an ILEC-owned wireless carrier competed

[103] *Bell Atlantic/NYNEX Order* ¶ 120.

[104] *See* Arrow Declaration ¶ 58.

with a non-wireline carrier that relied on the ILEC for local access. Non-wireline carriers, however, have successfully competed against ILEC-owned cellular providers for many years, and new wireless carriers, such as PCS and EMSR firms, are successfully competing against these same cellular carriers, though they too must rely on the ILEC for local access. The absence of any evidence that non-price discrimination has occurred, or has had any effect on competition, is telling. Such evidence would presumably be plentiful if ILECs indeed engaged in this practice.[105]

As is customary, therefore, the proponents of the price-squeeze and non-price-discrimination arguments are unable to point to any empirical support for the claim that ILECs have the incentive and ability to engage in such behavior. However, even if the opponents were able to show that ILECs possess those incentives and abilities, that would not constitute grounds for the Commission to find that the merger is not in the public interest, because the relevant question in the context of a transfer application is not whether discrimination is theoretically possible, but rather whether the merger would increase the combined company's incentive or ability to engage in such a strategy.[106] The Commission, for example, rejected the price squeeze and non-price discrimination arguments in its *SBC/PacTel* and *Bell Atlantic/NYNEX* orders,

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[105] *See* Arrow Declaration ¶¶ 56-60.

[106] *See SBC/PacTel Order* ¶ 54 ("[T]he pertinent issue in this proceeding is the incremental increase in the scope of the price squeeze that the proposed transfer will make possible for the first time.").

finding that the ILECs' incentive and ability to engage in such forms of downstream discrimination did not increase as a result of the merger.[107]

The Big Three have attempted to cobble together a theory of how the merger supposedly aggravates the potential for such discriminatory behavior -- the Katz-Salop theory -- but that contrived theory does not withstand scrutiny, as discussed above. Moreover, the merger will not increase any incentive to discriminate against long distance carriers because the merger only increases the number of calls that are *terminated* by GTE-Bell Atlantic. The suggestion that a LEC even in theory can induce a customer *at the terminating end* of a communication to change long distance carriers by degrading interLATA traffic ignores reality. With limited exceptions, the customer at the originating end, not the terminating end, chooses the interLATA carrier; consequently, the terminating-end customer is not likely to respond to perceived poor service quality by switching to a different long distance carrier (indeed, if anything, the terminating-end customer would be likely to blame the LEC for the problem). Congress recognized this reality in section 271 when it prohibited a BOC only from "provid[ing] interLATA services *originating* in any of its in-region States,"[108] and from terminating traffic in-region only for 800 service and similar calls where "the *called party* . . . determine[s] the interLATA carrier."[109]

Even if there were some added incentive or ability to discriminate in the transmission of interLATA calls when an ILEC both originates and terminates the call, the magnitude of that

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[107] *Id.* ¶¶ 54, 57; *Bell Atlantic/NYNEX Order* ¶¶ 118, 120.

[108] 47 U.S.C. § 271(b)(1) (emphasis added).

[109] *Id.* § 271(j) (emphasis added).

increase in this case would be insignificant under the Commission's standards. Sprint contends that "the new firm would terminate 43% of the minutes that it controls on the originating end, which compares to a weighted average of 36% for the two companies separately."[110] In the *SBC/PacTel Order*, however, the Commission found that an increase "of only six to seven percentage points" in the percentage of calls served at both ends by one firm raises no competitive concerns.[111] Similarly, in *Bell Atlantic/NYNEX*, the Commission was unpersuaded that the merger would have any effect on the incentive or ability to discriminate, even though the merger resulted in a "substantially greater percentage" of calls originated and terminated by the new company.[112]

For all of these reasons, the opponents of the GTE-Bell Atlantic merger are no more successful than opponents of mergers past in asserting that this union will enhance the incentives or ability of the combined entity to engage in price squeezes or non-price discrimination against rivals in downstream markets.

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[110] Sprint at 33.

[111] *SBC/PacTel Order* ¶¶ 46, 53, 57.

[112] *Bell Atlantic/NYNEX Order* ¶¶ 118, 120. To the extent our opponents are concerned with the *percentage* of long distance traffic that Bell Atlantic both originates and terminates, that percentage will actually *decrease* as a result of the merger: GTE's footprint is widely dispersed, and a very large percentage of the traffic that originates inside GTE's territory terminates with RBOCs other than Bell Atlantic.