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March 26, 1999

NOTICE OF EX PARTE PRESENTATION

Ms. Magalie Roman Salas
Secretary
Federal Communications Commission
Portals II Building
445 Twelfth Street, S.W.
Washington, D.C. 20554

Re: *In the Matter of Applications for Transfer of Control to SBC Communications Inc. of Licenses and Authorizations Held by Ameritech Corporation, CC Docket No. 98-141*

Dear Ms. Salas:

Please be advised that today John I. Stewart, Jr. and the undersigned, on behalf of SBC Communications Inc., and Antoinette Cook Bush, on behalf of Ameritech Corp., met with Linda Kinney of Commissioner Ness' office, in connection with the above-referenced applications. The purpose of the meeting was to present and discuss the attached memorandum, which addresses the issue of benchmarking and the claim that the SBC-Ameritech merger will impede the Commission's ability to regulate. The memorandum persuasively demonstrates that, in the context of this proposed merger, the benchmarking argument is purely theoretical, and, furthermore, that the merger will not impede the Commission's ability to regulate, by benchmarks or otherwise.

In accordance with the Commission's rules governing ex parte presentations, an original and one copy of this notification are provided herewith. Please call me directly should you have any questions.

Respectfully submitted,

Todd F. Silbergeld

Attachment

cc: Linda Kinney, Esq.

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Dear Ms. Salas:

Please be advised that yesterday, John I. Stewart, Jr. and the undersigned, on behalf of SBC Communications Inc., and Lynn Starr and Mark Del Bianco, on behalf of Ameritech Corp., met with Thomas C. Power of Chairman Kennard's office, in connection with the above-referenced applications. The purpose of the meeting was to present and discuss the attached memorandum, which addresses the issue of benchmarking and the claim that the SBC-Ameritech merger will impede the Commission's ability to regulate. The memorandum persuasively demonstrates that, in the context of this proposed merger, the benchmarking argument is purely theoretical, and, furthermore, that the merger will not impede the Commission's ability to regulate, by benchmarks or otherwise.

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cc: Thomas C. Power, Esq.

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Dear Ms. Salas:

Please be advised that yesterday, John I. Stewart, Jr. and the undersigned, on behalf of SBC Communications Inc., and Lynn Starr and Mark Del Bianco, on behalf of Ameritech Corp., met with Paul Gallant of Commissioner Tristani's office, in connection with the above-referenced applications. The purpose of the meeting was to present and discuss the attached memorandum, which addresses the issue of benchmarking and the claim that the SBC-Ameritech merger will impede the Commission's ability to regulate. The memorandum persuasively demonstrates that, in the context of this proposed merger, the benchmarking argument is purely theoretical, and, furthermore, that the merger will not impede the Commission's ability to regulate, by benchmarks or otherwise.

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Todd F. Silbergeld

Attachment

cc: Paul Gallant, Esq.

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Re: *In the Matter of Applications for Transfer of Control to SBC Communications Inc. of Licenses and Authorizations Held by Ameritech Corporation, CC Docket No. 98-141*

Dear Ms. Salas:

Please be advised that yesterday, John I. Stewart, Jr., Lawrence Fullerton and the undersigned, on behalf of SBC Communications Inc., and Lynn Starr and Mark Del Bianco, on behalf of Ameritech Corp., met with several members of the Commission's staff (see attachment) in connection with the above-referenced applications. The purpose of the meeting was to present and discuss the attached memorandum, which addresses the issue of benchmarking and the claim that the SBC-Ameritech merger will impede the Commission's ability to regulate. The memorandum persuasively demonstrates that, in the context of this proposed merger, the benchmarking argument is purely theoretical, and, furthermore, that the merger will not impede the Commission's ability to regulate, by benchmarks or otherwise.

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Respectfully submitted,

Todd F. Silbergeld

Attachments

cc: FCC Staff in Attendance

ATTACHMENT A

EX PARTE PRESENTATION • CC DOCKET NO. 98-141

March 25, 1999

FCC Staff in Attendance

Tom Krattenmaker, Office of Plans and Policy

Bill Dever, Common Carrier Bureau

Johanna Mikes, Common Carrier Bureau

Claire Blue, Common Carrier Bureau

Pamela Megna, Office of Plans and Policy

Bill Rogerson, Office of Plans and Policy

Donald K. Stockdale, Jr., Common Carrier Bureau

To-Quyen Truong, Common Carrier Bureau

Patrick DeGraba, Office of Plans and Policy

Audrey Wright, Common Carrier Bureau

Michelle Carey, Common Carrier Bureau

# # #

BENCHMARKING TALKING POINTS

In the context of this merger, the "benchmarking" argument is purely theoretical. The merger will not impede the Commission's ability to regulate, by benchmarks or otherwise.

1. Opponents of the merger have argued that it will result in the "loss" of an important regulatory benchmark, but the Commission will continue to have access to the same types of information about SBC's and Ameritech's operating companies that it already has.

    - SBC and Ameritech will maintain their current operating company structure.

    - Pre-merger data for the separate companies will remain available for historical analysis and comparison.

    - Detailed data such as those included in various ARMIS reports are collected at the operating company and study area levels, not the holding company level, and will thus continue to be available for the separate companies after the merger.

    - The Commission's regulatory decisions are based, where necessary, on separate data about the relevant operating companies, even where they are co-owned. For example, in the collocation and access tariff cases cited by Sprint, the Commission explicitly relied on separate (and different) operating-company information for SBC's separate subsidiaries, and for Bell Atlantic North and Bell Atlantic South.

2. Opponents have argued that the merger will "blunt" the incentives of the merged companies to increase productivity, but that theoretical argument is at odds with regulatory and marketplace realities.

    - The Commission has adopted price cap adjustment methodologies to minimize any such disincentive effect, and the theory's chief proponent has conceded that future X factor adjustments cannot be fully taken into account by price cap carriers, as the theory assumes.

- In the current marketplace, with its gigantic integrated global communications companies such as AT&T/TCG/TCI, MCI/WorldCom, and Sprint, the merged companies' incentive to increase productivity for competitive reasons will overwhelm any theoretical disincentive.

3. During the FCC Roundtable on the Economics of Mergers Between Large ILECs, Dr. Rogerson posed the question of whether there are any actual examples of RBOC benchmarking to support the theory propounded by the economists opposing the merger. The cases the economists cited in response do <u>not</u> show that the Commission has relied on RBOC benchmarks to reach its regulatory decisions.

   - The <u>only</u> example they cite in which Ameritech supposedly served as an outcome-determinative benchmark on a technical feasibility issue, the Interim Number Portability decision, is no such thing. States in numerous RBOCs' regions had already mandated the number portability technique at issue, Ameritech was not the only ILEC supporting it, the decision did not even relate to the technical feasibility of the competing techniques, and the Commission explicitly held that its ultimate decision was mandated by statutory requirements, regardless of the economic feasibility of the competing techniques.

   - None of the other examples they cite are cases in which the Commission reached its decision because of a single RBOC benchmark. Most involve comparisons at the operating company level, and potentially considered all ILECs or LECs. For example, the Commission's 1997 physical collocation decision relied on data from individual BOCs and non-BOC LECs, including a Sprint operating company and GTE. Its 1998 access tariff decision relied on data from seven non-BOC LECs, as well as separate data from five different operating units of RBOCs SBC and Bell Atlantic.

   - Even though there will be one fewer separately owned RBOC after the merger, the Commission will continue to be able to reach regulatory decisions based on all relevant information, just as it has continued to do after the mergers between SBC and Pacific and between Bell Atlantic and NYNEX.

4. As local markets continue to become more competitive, even comparisons between RBOC operating companies will become less relevant to regulatory

decisionmaking, and whole new classes of benchmarks and performance information will be available to both regulators and competitors.

- Direct comparisons with the practices of LECs in the same market, including both the ILEC and other CLECs, are more significant than comparisons with regional holding companies, or even operating companies, in other markets.

- Numerous interconnection and access agreements are available for comparison and adoption by CLECs.

- Detailed performance measures and reports are also available, and more will soon be available, to allow comparisons between an ILEC's treatment of its own retail operations and its treatment of CLECs, and between its treatment of one CLEC versus others, in the same market.

- New entities will increasingly be available to serve as "benchmarks" themselves, including both CLECs and SBC/Ameritech as it enters out-of-region markets.

- State commissions generally rely on self-referential comparisons rather than using foreign RBOCs as benchmarks. For example, the California PUC refused to impose a particular number portability requirement on GTE and Pacific based on an argument that other BOCs had adopted the practice, but later imposed it after GTE and Pacific offered similar service options to CLECs in interconnection agreements.

- The Department of Justice, in its evaluations of Section 271 applications, has emphasized the importance of self-referential comparisons rather than RBOC-to-RBOC comparisons. It has also worked with SWBT to develop 66 performance measures, which SWBT now reports to DOJ and the FCC on a monthly basis, that allow a direct comparison of the ILEC's retail performance and its treatment of CLECs on a wide variety of service criteria.

- These measurements and reporting systems -- together with enforcement remedies -- have been adapted in voluntary negotiations with the PUCs and CLECs in Texas and California and will be extended to all of the states in which SBC's BOCs provide service. In addition, SBC will implement this comprehensive

measurement, reporting, and enforcement regime in Ameritech's states following the merger.

- This comprehensive performance measurement regime, and the associated enforcement remedies that go along with it, create a strong incentive for ILECs not to discriminate against CLECs in the provision of any service and render undetected discrimination essentially impossible.

5. The competitive gains that will be realized by the merger far outweigh the theoretical possibility of the "loss" of a separately owned RBOC benchmark.

SUPPLEMENTAL MEMORANDUM REGARDING REGULATORY BENCHMARKING ISSUES

Submitted By
SBC Communications Inc.
and
Ameritech Corporation

March 25, 1999

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SUPPLEMENTAL MEMORANDUM REGARDING REGULATORY BENCHMARKING ISSUES

I. INTRODUCTION

This Memorandum addresses in further detail[1] one aspect of the "benchmarking" argument that was raised during the course of the Economic Roundtable conducted by the Commission on February 5, 1999. Specifically, economists opposing the merger asserted that there were "voluminous" examples of the Commission's reliance on RBOCs as benchmarks in prior proceedings.[2] On even a cursory review of the purported examples, however, the assertion turns out to be unsupportable.

Perhaps in recognition of this fact, opponents of the merger also argued that, because deregulation of local telephone markets under the 1996 Act is so new, the Commission should deny the merger just in case Ameritech might be useful as a "benchmark" in some unspecified, hypothetical regulatory issue that might arise in

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1 SBC and Ameritech have already addressed the various forms of the benchmarking argument that were originally made by opponents of the merger. See Joint Opposition of SBC Communications Inc. and Ameritech Corporation to Petitions to Deny and Reply to Comments, CC Docket No. 98-141, at 53-63 (Nov. 16, 1998) ("SBC/Ameritech Reply"); Schmalansee/Taylor Reply Aff. ¶¶ 51-82; Rivera Reply Aff. The merger's opponents appear now to have retreated from numerous aspects of their argument, focusing instead on the issues addressed here.

2 Transcript, Round Table on the Economics of Mergers Between Large ILECs Held on February 5, 1999, Docket No. CC-98-141 ("Tr.") 47, 58 (Farrell).

the future.[3] But it is clear that, in the transition to competitive local markets, the key comparisons are not between RBOCs. Rather, they are comparisons of how an ILEC treats CLECs vis-à-vis itself, and comparisons among all LECs, both BOC and non-BOC, and both ILEC and CLEC. There is no evidence that RBOCs -- as simply the parent companies of particular ILECs -- are or will be an important, much less crucial, source of benchmark comparisons.

The opponents' arguments about the potential loss of benchmarks for regulatory decisionmaking are purely speculative and contrary to fact, and cannot provide a legally sufficient basis to disapprove or impose conditions on this merger.

II. THE MERGER WILL NOT IMPEDE THE COMMISSION'S ABILITY TO REGULATE.

Historically, the FCC has reached key regulatory decisions on the basis of information and analyses that do not depend on the number of separately-owned RBOCs. The Commission has looked, instead, at data on the operating company level, as to which detailed economic and performance information will continue to be reported. Indeed, in the case of ILECs owned by RBOCs, the amount and scope of such information – and the number of "benchmarks" – has increased dramatically in the past year as a result of Section 271 implementation activities by the Department of Justice and the state commissions. SBC's ILECs, for example, are now submitting voluminous information to the Department, the Commission, and

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3 See Tr. 33, 62 (Sheperd), 45 (Farrell).

CLECs on a monthly basis reporting on their performance on a full range of service criteria deemed useful for evaluating competition issues.[4]

A. At the Roundtable, Opposing Economists Narrowed the Scope of the Issue.

During the discussion of the benchmarking argument at the Roundtable, Sprint's economist Dr. Joseph Farrell acknowledged that, if the merger is necessary and sufficient to permit the introduction of the vigorous out-of-region competition that will flow from the implementation of the National-Local Strategy, the merger should be approved notwithstanding his argument about benchmarking.[5] Economist Robert Litan, who opposes the merger, argued that the ultimate question was only how heavily to weigh the potential harm from a loss of benchmarking data in the overall evaluation against the benefits that will flow from the merger.[6] Indeed, there was consensus that any perceived potential harms from a reduction in benchmarking ability would have to be weighed against the benefits of the merger.[7] As explained below, any assertion of potential harm from the supposed loss of Ameritech as a benchmark is insubstantial speculation, wholly unsupported by evidence.

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4 This extensive new performance measurement, reporting, and enforcement regime is described in a separate paper being prepared for the Commission's Staff.

5 Tr. 67, 69 (Farrell); see also Tr. 55 (Noll).

6 Tr. 68 (Litan).

7 See Tr. 49 (Crandall), 52 (Carlton), 55 (Noll), 67 (Farrell), 68 (Litan).

The Roundtable discussion revealed that even the economists critical of the merger believe that the loss of some benchmarking data as a result of the merger would be significant only in limited respects. For example, economist Roger Noll did not believe that economic data collected from RBOCs forms meaningful "average practice" benchmarks for regulatory decisions,[8] arguing only that benchmarks can be used in the context of "best practices" regulation to evaluate whether a proposed practice is technically feasible.[9] Dr. Farrell explained that benchmarks, in the form of practices of other firms that are not direct competitors of the regulated company, are only one of three potential sources of information the Commission may consider in seeking to determine what practices are feasible.[10]

The benchmarking issue thus has been narrowed by the discussion to the question of whether the "loss" of Ameritech as an independently owned RBOC would so affect the Commission's ability to determine whether a proposed practice is technically feasible as to outweigh the benefits presented by the merger. Dr. Rogerson further focused the analysis of this question by asking whether there are any actual examples of the Commission's past use of such a benchmarking

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8 See Petition to Deny of Sprint Communications Company L.P., CC Docket No. 98-141 (filed Oct. 15, 1998) ("Sprint Petition"), Declaration of Joseph Farrell and Bridger M. Mitchell ("Farrell/Mitchell Decl."), at 10-13.

9 Tr. 55-57 (Noll); see Sprint Petition, Farrell/Mitchell Decl. at 14-22.

10 Tr. 45-46 (Farrell).

approach.[11] Dr. Farrell's response, referring to two FCC decisions cited in Sprint's opposition to the merger, demonstrates the ultimate speciousness of the benchmarking issue, even in its newly distilled form.

B. The FCC's Current Use of Benchmarks Does Not Depend Upon Having a Minimum Number of Independently Owned RBOCs.

In response to Dr. Rogerson's question, Dr. Farrell highlighted two instances in particular -- involving number portability and shared transport -- as examples of the FCC's use of benchmarks to determine the technical feasibility of a proposed practice.[12] On closer reading, however, neither case supports his argument. Nor do the other examples cited by Dr. Farrell in his Declaration in support of Sprint's opposition to the merger.[13]

1. Number Portability.

Dr. Farrell first cited the case Sprint described as the "prime example" of the need for inter-RBOC benchmarking,[14] the Commission's number portability reconsideration decision.[15] In that case, the Commission confirmed its prior determination that one method of providing long-term number portability, the

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11 Tr. 57-58 (Rogerson).

12 Tr. 58 (Farrell).

13 Sprint Petition, Farrell/Mitchell Decl. at 14, 17-21, 23-26.

14 Sprint Petition at 34.

15 In re Telephone Number Portability, First Memorandum Opinion and Order on Reconsideration, 12 FCC Rcd 7236 (1997).

"QOR" system, did not meet the performance criteria it had previously adopted for number portability solutions.[16] Sprint asserted that while "six RBOCs, GTE, and USTA" petitioned for permission to use the QOR approach, "[a] single exception (Ameritech) planned to deploy the LRN method" of number portability.[17] Sprint further asserted that "[t]he Commission concluded, based on this experience, that it was feasible for all ILECs to implement the LRN method."[18]

In these assertions, Sprint is flatly wrong. This is simply not an example of the Commission's relying on the practice of a single RBOC as a "benchmark" to conclude that a proposed regulatory requirement is technically feasible and therefore should be imposed on all RBOCs.[19]

The number portability decision fails to support Sprint's argument for the following reasons, among others:

- The decision applied to all LECs (including CLECs), not just RBOCs,[20] so that many hundreds of companies could have served as potential "benchmarks" if needed, and the "loss" of a single independently owned RBOC through merger would not have significantly diminished the number of available comparisons.

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16 Id. at 7243 ¶ 13.

17 Sprint Petition, Farrell/Mitchell Decl. at 14-15.

18 Id. at 15 (emphasis added).

19 Indeed, although Dr. Farrell described the case as a "telling example" of best-practice benchmarking, he ultimately claimed merely that "it seems unlikely" the Commission would have reached the same conclusion had Ameritech not taken the position it did. Id. But even this watered-down conclusion is inconsistent with the Commission's own decision, as explained below.

20 In re Telephone Number Portability, First Report and Order and Further Notice of Proposed Rulemaking, 11 FCC Rcd 8352, 8353 ¶ 1 (1996).

- The LRN method had been developed by AT&T, not Ameritech,[21] and was supported by numerous parties, including other LECs, not just Ameritech.[22]

- Seven states (including California, New York, Colorado, Maryland, and Georgia, as well as Illinois and Ohio) had already imposed LRN as the required method of providing long-term number portability.[23]

- The decision did not even involve the question of the technical feasibility of the LRN method. It held only that the short-term cost savings of the QOR method were not so clearly substantial that they justified overriding that method's conceded noncompliance with the performance criteria.[24]

- The FCC reached this decision based on a close analysis of estimates of short-term cost savings presented by various incumbent LECs, including GTE, and the opposing analyses presented by MCI, AT&T, and others.[25]

- The Commission's sole mention of Ameritech in its whole discussion of this issue was the comment that "at least one incumbent LEC, Ameritech, has already decided it is beneficial" to deploy LRN initially.[26] But the Commission's supporting footnote cited filings by Ameritech and others stating that "support for LRN has by no means been confined to ...Ameritech among the RBOCs."[27] Indeed, the filings included an agreement to use LRN in Illinois that had been signed not only by Ameritech but also by ILECs Sprint/Centel and GTE, and by CLECs MCIMetro, MFS, and TCG.[28]

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21 Id. at 8359 ¶ 13.

22 Id. at 8377 ¶ 46.

23 First Memorandum Opinion and Order on Reconsideration, 12 FCC Rcd at 7240 ¶ 8.

24 Id. at 7265-66 ¶ 47.

25 Id. at 7255-63 ¶¶ 33-43.

26 Id. at 7258 ¶ 38. The FCC appeared to suggest that Ameritech had made this choice with the expectation that the short-term increased costs of not using QOR would be offset by longer-term savings as local competition increased. Id.

27 Id. at 7258 n.120.

28 Further Comments of Ameritech (filed March 29, 1996) (cited at 12 FCC Rcd 7258 n.120), at 7 & n.12 and Attachment A.

- In its conclusion, the Commission explicitly rejected the "benchmarking" approach Sprint now asserts. It held that even if Ameritech's apparent position were incorrect, and long-term costs were lower for the QOR method, as asserted by other ILECs, that method would still be prohibited because of the harm it posed for competitors.[29]

Thus, this is not an example of the Commission's reliance on the practice of one RBOC, Ameritech, to conclude that a regulatory requirement imposed on all LECs is technically feasible. The Commission's decision to prohibit QOR was based on its critical analysis of the cost estimates presented by various ILECs, on the fact that numerous states would otherwise have to revisit their prior number portability decisions, and on the Commission's view that the statute elevated competition concerns over potential cost savings. Even if Ameritech had not argued the position it did, those reasons would have led to the same conclusion.

2. Shared Transport.

The other case cited by Dr. Farrell provides even less support for his benchmarking argument. In the shared transport decision,[30] the Commission reaffirmed its prior decision that "it is technically feasible to provide access to interoffice transport facilities between end offices and between end offices and

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29 12 FCC Rcd at 7258 ¶ 38, 7265-66 ¶ 47.

30 In re Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, Third Order on Reconsideration and Further Notice of Proposed Rulemaking, 12 FCC Rcd 12460 (1997).

tandem switches."[31] It noted that all ILECs agreed, except Ameritech.[32] As to Ameritech's argument that it was not technically feasible to do so because it could not accurately bill such transport, the Commission held that (1) billing concerns are irrelevant to a determination of technical feasibility, and (2) Ameritech had in any event already proposed a method of providing such transport in a separate proceeding.[33]

Given that the Commission rejected the arguments of Ameritech about technical feasibility, and that there were apparently numerous other carriers that had already provided the service,[34] it is hard to imagine how the case could be read to support an argument that the merger between SBC and Ameritech would affect the Commission's regulatory abilities.

3. The Remaining "Examples."

Attachment 1 to this Memorandum is a chart showing, for each of the cases cited in the Declaration of Joseph Farrell and Bridger M. Mitchell, whether the regulatory analysis turned on only an RBOC-to-RBOC comparison and whether the

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31 Id. at 12477 ¶ 26.

32 Id. at 12477 n.77.

33 Id. The Commission quite plainly did not base its decision on a finding, as Dr. Farrell would have it, that "Bell Atlantic, on the other hand, was just doing it." See Tr. 58 (Farrell).

34 Indeed, the Commission had first concluded that the service was technically feasible on the basis of evidence that "the larger LECs, IXCs, and CAPs" had already worked out similar interconnection. In re Implementation of the

(continued...)

outcome of the analysis would have differed had Ameritech been owned by SBC at the time. In none of the cases would the "loss" of Ameritech as a separately owned RBOC "benchmark" have been material to the regulatory outcome.

This is so because the Commission generally considers all available data and analyses in reaching its decisions, including information about non-RBOC LECs, and data are usually considered at the operating company level, not the holding company level. For example, in evaluating the reasonableness of LEC charges for physical collocation services,[35] the FCC relied on direct cost estimates of fourteen LECs (including a Sprint operating company, Central), not merely the six RBOCs that existed at that time.[36] Indeed, the FCC noted that the variation among operating companies, including those with a common owner, mandates treating each operating unit as a separate benchmark.[37] The Commission has continued this

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(...continued)

Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, 11 FCC Rcd 15499, 15719 ¶ 442.

35 See Sprint Petition, Farrell/Mitchell Decl. at 23-24, 39.

36 In re Local Exchange Carriers' Rates, Terms, and Conditions for Expanded Interconnection Through Physical Collocation for Special Access and Switched Transport, 12 FCC Rcd 18730, 18799 (1997). The fourteen LECs included RBOCs Ameritech, Bell Atlantic, BellSouth, NYNEX, Southwestern Bell, and U S West, and BOCs Pacific Bell and Nevada Bell (whose RBOC parent Pacific Telesis had recently been acquired by SBC), along with non-BOC LECs Central (Sprint), Cincinnati Bell, GTE, Lincoln, and Rochester. Id. n.282.

37 Id. at 18734 n.5 ("Although Nevada and Pacific both are owned by Pacific Telesis Group, the two operating companies have separate and very different tariffs, and are treated separately").

approach in its recent Order on the Deployment of Advanced Telecommunications Services, declaring that it will presume that a collocation method used by any incumbent LEC, or ordered by any state commission, is technically feasible for other ILECs.[38]

Similarly, the joint ownership of various operating companies did not impede the Commission's regulatory analysis in a recent case cited by Sprint involving the penetration rates of second lines.[39] The Commission referred to an average penetration rate developed on the basis of data from each of fifteen LECs, including Aliant, CBT, Citizens, Frontier, GTE, SNET, and Sprint LTCs.[40] Moreover, the FCC relied on individual data from separate operating units of RBOC holding companies, data that showed significant variation within the RBOCs themselves: Bell Atlantic-North (7.00%) and Bell Atlantic-South (11.90%); and Southwestern Bell (8.67%), Pacific Bell (15.71%), and Nevada Bell (8.56%).[41]

Opponents of this merger also featured the FCC's 1997 revision of its access charge productivity "X-Factor" for price cap LECs as an important example of the

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38 See News Release, FCC Adopts Rules to Promote the Deployment of Advanced Telecommunications Services, (CC Docket No. 98-147), Report No. CC 99-6 (March 18, 1999).

39 In re 1998 Annual Access Tariff Filings: Southwestern Bell Telephone Company Revisions to Tariff F.C.C. No. 73 13 FCC Rcd 13977 (1998). See Sprint Petition, Farrell/Mitchell Decl. at 26-27.

40 13 FCC Rcd at 13980 ¶ 9.

41 Id.

need for maintaining separately owned RBOCs.[42] There, however, the Commission used industry-wide data for price cap LECs for the ten years beginning with 1986, and derived the productivity factor from multi-year averages.[43] Data for each operating company were combined and averaged to arrive at the final factor, and therefore the result would not have been affected had there been one fewer separate RBOC holding company owner.[44]

C. Today the Most Important "Benchmarks" for Access and Interconnection Come From the ILEC Itself and From CLECs, Not From Other RBOCs.

Some opposing economists suggested in effect during the Roundtable discussion that the Commission should deny the merger because competitive local markets are still new, and the Commission should freeze the number of "benchmarks" at their current number in case they would be useful in some future,

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42 Sprint Petition, Farrell/Mitchell Decl. at 12-13, 39-40.

43 In re Price Cap Performance Review for Local Exchange Carriers: Access Charge Reform, 12 FCC Rcd 16642, 16696-97, ¶¶ 137-141 (1997).

44 Sprint asserted that an RBOC's incentive to improve productivity would be marginally diminished by becoming larger through merger. As SBC and Ameritech have explained previously, that analysis is faulty. See SBC/Ameritech Reply at 61-62. Moreover, Sprint's theoretical argument is contradicted by actual experience, and its predicted disincentivizing effects can be avoided by straightforward regulatory measures within the Commission's power. See id., Schmalensee & Taylor Reply Aff. at ¶¶ 73-77. The Commission itself has concluded as much, by undertaking to use measures designed to avoid such an effect in its next performance review. 12 FCC Rcd at 16708 ¶ 167. And Dr. Farrell has further retreated from his argument, effectively conceding that the disincentive is masked because "nobody can really know for sure how the X factor will be adjusted and when," and now arguing only that that fact does not make the X factor "completely exogenous." Tr. 65, 66 (Farrell) (emphasis added).

unspecified regulatory proceeding.[45] This is an absurd rationale on which to deny consumers the benefits this merger will provide. Any reasoned analysis would focus not on the mere fact that local markets are changing but on the specific ways in which these changes affect the regulators' needs for information and the sources of data that will be available. Such an analysis would reflect the reality that performance measures designed to compare the access and interconnection the Bell Operating Companies provide to CLECs on a state-by-state basis with that provided to their own retail operations have become the new "benchmarks."

1. Regulatory Issues at the Federal Level.

For interconnection and access issues, the ILEC itself, along with its collection of approved interconnection agreements, is the relevant benchmark for the FCC, for state public utilities commissions, and for competitors. Parity between CLECs and the ILEC, measured against mutually acceptable performance standards, has become the standard for comparison. Moreover, for many interconnection issues, such as technical feasibility questions or service performance measures, which are primarily considered by state commissions, CLECs themselves are now available as additional benchmarks.

One corroborating perspective is found in the Justice Department's participation in the Commission's regulation of the transition to competition, as

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45 See Tr. 33, 62 (Sheperd), 45 (Farrell).

explained further in Attachment 2 to this Memorandum. In its evaluations of Section 271 petitions, DOJ has come to rely on intra-RBOC comparisons, on direct measures of local competition, and on standards set by the BOC's performance for its own retail operations. For example, in its most recent filing, concerning BellSouth's second application for Louisiana,[46] the Department presented an evaluation based on numerous comparisons between BellSouth's performance for CLECs and its performance for itself. The Department argued that the critically important "benchmarks" are internal (not external) performance standards that can be used for evaluating future performance.[47] DOJ also made comparisons with practices in BellSouth's other states.[48] Of all the comparative benchmarks the Department referred to, only one involved the performance of another BOC (not an RBOC), and that was in connection with another single-state Section 271 application, which the Department also had opposed.[49] The Department has followed a similar approach in other Section 271 evaluations it has filed.[50]

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46 Evaluation of the United States Department of Justice, CC Docket No. 98-121 (filed Aug. 19, 1998) ("Louisiana II").

47 Id. at 38-39.

48 Id. at 17, 23 & n.45

49 Id. at 28 n.52 (stating that Ameritech had provisioned many more unbundled local loops in Michigan at the time it filed its unsuccessful 271 application than BellSouth had provisioned in Louisiana). The Department also referred to the test methodology employed by consultants for Bell Atlantic-New York, which it considered superior to BellSouth's consultant's methodology. Id. at 37 n.75. Neither of these is an RBOC-to-RBOC comparison.

50 See Attachment 2.

The Department of Justice also has agreed with SBC on a "comprehensive list of performance measures" that "would be sufficient, if properly implemented, to satisfy the Department's need for performance measures for evaluating a Section 271 application."[51] Virtually all of the sixty-six agreed performance measures are reported in a form that permits comparison between service to the CLEC and service to all CLECs, SWBT itself, or both. None contemplates RBOC-to-RBOC comparisons.

These performance measure reports are being filed monthly with the FCC and the Department of Justice, and they are available to CLECs who have entered interconnection agreements. In Texas, and the other states served by Southwestern Bell Telephone Company, they have been supplemented after discussions with CLECs and the Texas PUC, and SWBT now reports in those states on 105 measures. Similarly, PacBell has worked with CLECs and its State PUC to adapt the DOJ measures for use in California and Nevada. As we explain in a separate paper being prepared for the Commission's Staff, the bulk of the data provided in these monthly reports are newly available bases for evaluating compliance with local market competition measures, and the existence of these additional performance measurement and reporting systems eliminates the possibility that

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51 Letter from Donald J. Russell, Chief, Telecommunications Task Force, Antitrust Division, to Liam S. Coonan, SBC, dated March 6, 1998 (a copy of which appears at SBC/Ameritech Reply, Appendix B, "SBC Response to Specific Allegations," Attachment 1).

ILECs could engage in undetected discrimination against CLECs or otherwise deny CLECs a meaningful opportunity to compete. The merger will not reduce the availability of this extensive new information at all. Indeed, it presents an opportunity to spread the beneficial effects of such an approach across an even broader region.

2. Regulatory Issues at the State Level.

Similarly, state commissions are placing increased importance on comparisons that are based on self-referential ILEC performance standards and comparisons with ILEC treatment of CLECs. For example, the California Public Utilities Commission, in its Interim Opinion on Local Number Portability,[52] considered a request by MCI that Pacific and GTE California be required to offer "flex-DID" as a way to facilitate new competition. MCI argued that Ameritech, Bell Atlantic, and NYNEX all offered Interim Number Portability using flex-DID.[53] The Commission nonetheless declined to require the offering, accepting the ILECs' concerns that the cost of the service would be relatively high and the demand was unproven.[54] Rather than basing a decision on the offering of the service by carriers

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52 Order Instituting Rulemaking on the Commission's Own Motion Into Competition for Local Exchange Service, D.96-04-052, 65 CPUC2d 542, 1996 Cal. PUC LEXIS 272 (1996).

53 Id., 1996 Cal. PUC LEXIS 272 at *14-*15.

54 Id. at *16-*18.

in other states, the Commission commenced a technical workshop to investigate the potential for CLEC-DID service.[55]

The following year, the California Commission considered the issue again, and ordered that Pacific and GTEC make available to all CLECs certain alternative forms of INP that included a "Flex DID" service.[56] The Commission did so, however, not on the basis that other RBOCs allegedly offered the service, but because technical progress had been made during and after the workshops it had ordered, and in particular because Pacific and GTEC had subsequently offered the service as part of interconnection agreements with MCI and others.[57] Thus, the most direct and relevant comparisons were the regulated ILECs' own dealings with themselves and other CLECs.

Another example is found in a further decision in the same proceeding, this time regarding access by third-party vendors to data that included the addresses of new ILEC and CLEC customers whose numbers were unpublished.[58] Independent directory publishers argued that the LECs should be required to provide access to

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55 Id. at *109.

56 Order Instituting Rulemaking on the Commission's Own Motion Into Competition for Local Exchange Service, D.97-10-029, 1997 Cal. PUC LEXIS 918, *31-*32 (1997).

57 Id.

58 Order Instituting Rulemaking on the Commission's Own Motion Into Competition for Local Exchange Service, D.97-01-042, 1997 Cal. PUC LEXIS 42 (1997).

such data on the grounds, *inter alia*, that Ameritech and certain Bell Atlantic subsidiaries offered such access.[59] But the California Commission, in ordering Pacific and GTEC to provide such access, did not cite this factual assertion. It relied instead on the argument that the LECs should be required to provide the same information to third party competitors that they provide to their own directory affiliates, and that information includes the addresses of nonpublished number customers.[60] Again, the material comparison for regulatory decisionmaking purposes was to the LEC's treatment of itself, not to other RBOCs' policies.

3. Non-RBOC "Benchmarks."

Although opposing economists at the Roundtable discussion attempted to belittle the role of non-RBOC comparisons,[61] there is also a growing body of ILEC and CLEC market experience that will be available for FCC reference if necessary. This includes the market practices and experience of Sprint, the second largest non-RBOC local exchange company. As IXCs and other CLECs expand their entry into local exchange business -- Sprint through its "ION" initiative, AT&T through TCG, TCI, AT&T Wireless, and its partnerships with Time Warner and others, and MCI/WorldCom through its constituent CLECs, including MFS and Brooks -- they

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59 Id. at *22-*23.

60 Id. at *19, *44.

61 See Tr. 48 (Farrell) (conceding that the merger would have little effect "[f]or some purposes" where numerous firms could continue to provide regulatory comparisons, but arguing that for other purposes comparisons with ILECs and CLECs "may not do you a lot of good.")

are setting "benchmarks" in their own negotiations, both those with ILECs and those with other CLECs through which they are becoming providers of wholesale services. CLEC interconnectors and wholesalers will continue to emerge in voice markets, as they have in the Internet arena. The FCC and the state commissions do, and certainly should, examine the interconnection policies, tariffs, and terms of these new entrants, and compare them with what ILECs offer.[62] The number of available comparisons will thus continue to expand, not contract, a trend that will in no way diminish as a result of the merger of SBC and Ameritech.[63]

4. Regulatory Issues in the Future.

"Benchmarks" of any kind will become increasingly irrelevant as competition replaces regulation. Indeed, the further into the future one looks, the less the need for any benchmarks, as the regulator's role is supplanted by new market entry and competition. Several of the economists at the Roundtable agreed with this observation, including, in particular, Dr. Noll.[64] The regulatory changes that have introduced new competition have also both accelerated and been accompanied by

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62 For example, in Application of NEXTLINK Pennsylvania, L.L.P., for Authority to Operate as a Competitive Local Exchange Carrier, 1998 Pa. PUC LEXIS 53, *36-*38 (1998), the Pennsylvania Public Utility Commission imposed an obligation on the CLEC to report its compliance with certain performance standards to the ILEC, as well as vice versa.

63 The implementation of the merged company's National-Local strategy will also accelerate the creation of new CLEC "benchmarks," both outside and within its home region.

64 Tr. 55 (Noll); see Tr. 69 (Farrell), Tr. 49-50 (Crandall), Tr. 59 (Carlton).

rapid technological developments that dramatically increase the opportunity for bypass of local facilities. And this dynamic marketplace has led to the vertical integration of the principal interexchange carriers into huge global telecommunications competitors capable of providing local exchange, long distance, data, wireless, and a variety of bundled services to customers.

Under this new marketplace structure and the new regulatory paradigm, even the intra-RBOC and non-RBOC "benchmarks" will have little if any significance as time goes on. As competition continues to increase, the importance of regulation by the FCC and state commissions will diminish apace, and so too will any need for benchmarks.[65] For example, the importance of access charges is declining, simply because long distance carriers will increasingly reach their customers through CLECs rather than ILECs. Similarly, as Internet and enhanced-service traffic continues to increase, the importance of benchmarking access charge rates will decline further.[66]

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65 See Tr. 55 (Noll).

66 Cf. In re Regulatory and Policy Problems Presented by the Interdependence of Computer and Communications Services and Facilities, 28 F.C.C.2d 267 (1971), aff'd in pertinent part sub nom. GTE Service Corp. v. FCC, 474 F.2d 724 (2d Cir. 1973); In re Amendment of Section 64.702 of the Commission's Rules and Regulations (Second Computer Inquiry), 77 F.C.C.2d 384, modified on recon., 84 F.C.C.2d 50 (1980), further modification on recon., 88 F.C.C.2d 512 (1981), aff'd sub nom. Computer and Communications Indus. Ass'n v. FCC, 693 F.2d 198 (D.C. Cir. 1982), aff'd on second further recon., FCC 84-190 (released May 4, 1984).

Benchmarks will also be entirely irrelevant to new competitive services that the FCC does not regulate at all, such as high-speed access services offered by ILECs through separate subsidiaries today. While serving as the FCC's chief economist, Sprint's economist argued that innovative services should be walled off from the culture of regulation and entitlement.[67] In this dynamic, competitive environment, the FCC will rely less and less on benchmarking one ILEC's performance against another's.

III. THE CONCERNS EXPRESSED BY THE COMMISSION IN ITS BELL ATLANTIC/NYNEX DECISION ARE NOT PRESENTED HERE.

It is clear from the preceding discussion that the benchmarking concerns expressed by the Commission in Bell Atlantic/NYNEX[68] are simply not presented by this merger in the current environment. In the increasingly competitive local exchange business, SBC/Ameritech has no incentive to reduce its productivity and thereby distort the aggregate measures of the industry's performance.[69] It is economically irrational to believe that SBC's operating companies -- or any large

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67 "Prospects for Deregulation in Telecommunications – Mildly Revised Version, May 30, 1997," <http://www.fcc.gov/bureaus/OPP/Speeches/jf050997.html>.

68 In re Applications of NYNEX Corporation and Bell Atlantic Corporation For Consent to Transfer Control of NYNEX Corporation and Its Subsidiaries, 12 FCC Rcd 19985 (1997).

69 See Id. at 20060 ¶ 150 (suggesting that a merger between Bell Companies would indirectly increase the "blunting effect on productivity incentives").

LEC -- would decline to improve productivity when faced with increasing competition.[70]

To the contrary, the record reflects SBC's recognition that sheer size will not and cannot attract and maintain customers -- only its productivity and service will. For this reason, following its merger with Pacific Telesis, SBC took numerous measures to increase the quality and efficiency of Pacific's services, including the following: [71]

- Sharing of R&D resources, resulting in improvements in ADSL services and introduction of new products in California, including Anonymous Call Rejection, Calling Name Delivery, and Usage Sensitive Three-Way Calling.
- Sharing of best practices in

  (1) wireless services, resulting in new rate structures and more competition;

  (2) customer services, resulting in lower rates of dispatch and trouble reports and lower customer serving time; and

  (3) vertical services, resulting in the introduction of new significantly discounted packages that have contributed to a 42 percent increase in vertical services subscribership.
- Renegotiation of supply contracts, resulting in increased discounts and reduced overall costs.
- Elimination of duplication, allowing cost savings exceeding $120 million.

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70 See SBC/Ameritech Reply, Kahan Reply Aff. at ¶ 37 and Attachment 14 p. 3.

71 See SBC/Ameritech Reply, Kaplan Reply Aff. at ¶¶ 15, 24, 26, 34, 36; Carlton Reply Aff. At ¶ 97.

Similarly, this merger will not increase the likelihood that RBOCs would collectively seek to evade local market-opening regulation, which the FCC cited as another potential concern,[72] for two reasons. First, there is no opportunity to do so, because of the regulatory and marketplace changes described above. The implementation of the interconnection and nondiscrimination requirements of the 1996 Act is going forward on a state-by-state basis, and is accompanied by intensive scrutiny from customer-competitors, including large and sophisticated CLECs and vertically integrated IXCs. The supposition that, with one fewer separately-owned RBOC, the holding companies will now be able to join together to resist local competition where they could not do so before is unrealistic in the extreme.

Second, the whole point of this merger and SBC's National-Local Strategy is to compete against other RBOCs and ILECs out of region. If anything, this merger will make it more, not less, difficult for ILECs to evade FCC regulation.[73] It is indisputable that SBC/Ameritech's entry into cities outside its region will spur competition nationally, including competition against other RBOCs in their own

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72 Bell Atlantic/NYNEX at 20060-62 ¶¶ 152-154 (suggesting that a merger would reduce "diversity of viewpoints" or otherwise encourage ILECs to act collectively to resist opening local markets to competition).

73 During the Roundtable discussion, Dr. Farrell conceded that, if the merger is a necessary and sufficient condition for the implementation of the National-Local Strategy, neither the benchmarking argument nor the other arguments under consideration should be a basis for denying the merger. Tr. 67, 69 (Farrell).

regions.[74] To make its National-Local Strategy work, SBC/Ameritech has an incentive to further the pro-competitive process of the 1996 Act, not to impede it.

IV. CONCLUSION

The "benchmarking" argument made by certain opponents of the merger is unsupported by any evidence that preserving the current number of independently owned RBOCs is material to the regulatory process, particularly on issues raised by the transition to competition.

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74 This new national-local competition will render highly unlikely the specter of the ultimate merger of all RBOCs into one. See id. at 20062 ¶ 156.

ANALYSIS OF SPRINT'S EXAMPLES OF REGULATORY BENCHMARKING
(Farrell & Mitchell[1] October 14, 1998)

F&M PAGE NO.	EXAMPLE (CITATION)	COMPARE RBOC-TO-RBOC?[2]	AFFECTED BY THIS MERGER?[3]	COMMENTS
14-15, 29-30	Number Portability (12 FCC Rcd 7236 (1997))	NO	NO	All LECs, not just BOCs. FCC ruled that LRN would be imposed regardless of whether it produced long-term cost savings for an RBOC. 12 FCC Rcd at 7265-66, ¶ 47.
17-18	Technically Feasible Interconnection (11 FCC Rcd 15499, 15606 (1996))	NO	NO	All ILECs, not just BOCs. Only compare networks using "substantially similar facilities." 11 FCC Rcd 15606, ¶ 204.
18	Access to OSS (11 FCC Rcd 15499, 15763-65 (1996))	NO	NO	All ILECs, not just BOCs. Comparisons state-by-state and ILEC-by-ILEC, including Rochester Telephone and GTE. 11 FCC Rcd 15764-65, ¶ 519, 15765-66, ¶ 520, & n.1269.
18	Shared Transport (12 FCC Rcd 12460, 12477 ¶ 26 & n.77 (1997))	NO	NO	All ILECs, not just BOCs. All except Ameritech had adopted the practice, and Ameritech had admitted it was feasible. 12 FCC Rcd 12477 n.77.
18-19	Open Architecture (referred to in 12 FCC Rcd 19965, 20058a n.275 (1997))	NO	NO	All BOCs and AT&T. FCC ultimately adopted flexible requirements, because of uncertainty about the feasibility of Ameritech's (or others') particular ONA arrangement as conditions changed. See Computer III Phase I Order, 104 FCC2d 958, 1061-63, 1067 (1986); BOC ONA Order, 4 FCC Rcd 1, 107-08 ¶ ¶ 208-209 (1988).
19	Trunk-Side Interconnection (2 FCC Rcd 2910, 2914 (1987))	NO	NO	All LECs, not just BOCs. Based feasibility assumption on reported concession of "numerous landline companies." 2 FCC Rcd 2914 ¶ 31.
19-20	Cageless Collocation (13 C.R. 1, 35-36 (1998))	NO	NO	All ILECs, not just BOCs. More than one BOC , including SBC, were offering cageless or shared cage collocation. 13 C.R. 35 ¶ 139.
20	Operating Expenses (Jan. 9, 1997, FCC Staff Analysis)	NO	NO	All ILECs, not just BOCs. Staff mentioned comparison as one of several possible methods, including using Pacific's 1994 expenses as a reference. The Use of Computer Models for Estimating Forward-Looking Economic Costs ¶ ¶ 66-69.
20-21	Line of Business Restrictions (Default Traffic Example) (50 Fed. Reg. 25982, 25987 (June 24, 1985))	NO	NO	FCC adopted balloting and allocation plan "modeled after" Northwest Bell's to replace a post-divestiture default system leaving AT&T in place as IXC unless another was selected. All BOCs reported that they were already implementing ballot systems. 50 Fed. Reg. 25983 n.13.

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23-24, 42-43	Collocation (12 FCC Rcd 18730 (1997))	NO	NO	All ILECs, not just BOCs. Used comparison data at operating company level. 12 FCC Rcd 18799 & n. 282
25	Overhead Costs (10 FCC Rcd 1960 (1994))	NO	NO	All Tier 1 LECs, not just BOCs. Basis for company-specific adjustment factors was company's own overhead costs for comparable services. 10 FCC Rcd 1973-76.
26-27	Non-Primary Lines (13 FCC Rcd 13977 (1998))	NO	NO	All LECs, not just BOCs. Used comparison data at the operating company level, even within RBOCs. 13 FCC Rcd 13980.
31-32, 38-41	Price Cap Productivity X-Factor (12 FCC Rcd 16642 (1997))	NO	NO	All price cap LECs, not just BOCs. Used industry-wide average data over ten-year period. 12 FCC Rcd 16696-97 ¶¶ 137-141
Non-FCC Examples:				
21	Equal Access (cited in 739 F.Supp. 1 (D.D.C. 1990))	YES	NO	Enforcement of judicial decree requirements applying only to RBOCs. NYNEX performance found lacking in comparison with rest of regional companies. 739 F.Supp. at 8.
21	Overhead Costs (CPUC R.93-04-003, I.93-04-002)	NO	NO	Sprint witness testified he was "not pointing to any one company" but was "looking across a broad range of companies over several years." June 5, 1998 Tr. 7950.
22	European access prices (EC 98/511/EC (July 29, 1998)	NO	NO	Average of three country-wide rates used to establish general range of interconnection rates. Recommendation 98/511/EC, amending Recommendation 97/195/EC, OJ L 228, 15. 8. 98.
22, 36-37	UK Water Company Merger (Wessex Water PLC and South West Water PLC (October 1996))	NO	NO	Applying explicit statutory mandate not to approve any merger that would reduce number of separate price benchmarks, unless "substantially greater" public interest benefit shown. Report on Proposed Merger at 11 ¶ 2.30.

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[1] Petition to Deny of Sprint Communications Company L.P., Attachment C, "Benchmarking and the Effects of ILEC Mergers," Decl. of Joseph Farrell and Bridger M. Mitchell, filed in FCC CC Docket No. 98-141, Oct. 15, 1998.

[2] Does the example involve an RBOC-to-RBOC comparison only?

[3] Would the example have produced a different regulatory result if Ameritech had been owned by SBC at the time?

APPENDIX

This Appendix examines and summarizes the use by the Department of Justice of comparison "benchmarks" for purposes of evaluating the performance of applicants in meeting the Department's standard for satisfying Section 271. The Department has filed comments, pursuant to Section 271(d)(2)(A) of the Communications Act, regarding each of five Bell Operating Company applications to the FCC for authority to provide in-region interLATA services under Section 271(c)(1).[1] The way in which the Department has exercised its statutory responsibility under Section 271(d)(2)(A) confirms the lack of relevance of RBOC-to-RBOC comparisons in the current regulatory environment.

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[1] *See* Evaluation of the United States Department of Justice, *In re Second Application by BellSouth Corporation, BellSouth Telecommunications, Inc., and BellSouth Long Distance, Inc., for Provision of In-Region, InterLATA Services in Louisiana*, CC Docket No. 98-121 (Aug. 19, 1998) ("Louisiana II"); Evaluation of the United States Department of Justice, *In re Application by BellSouth Corporation, BellSouth Telecommunications, Inc., and BellSouth Long Distance, Inc., for Provision of In-Region, InterLATA Services in Louisiana*, CC Docket No. 97-231 (Dec. 10, 1997) ("Louisiana I"); Evaluation of the United States Department of Justice, *In re Application by BellSouth Corporation, BellSouth Telecommunications, Inc., and BellSouth Long Distance, Inc., for Provision of In-Region, InterLATA Services in South Carolina*, CC Docket No. 97-208 (Nov. 4, 1997); Evaluation of the United States Department of Justice, *In re Application of Ameritech Michigan Pursuant to Section 271 of the Telecommunications Act of 1996 to Provide In-Region, InterLATA Services in the State of Michigan*, CC Docket No. 97-137 (June 25, 1997); Evaluation of the United States Department of Justice, *In re Application of SBC Communications Inc. et al. Pursuant to Section 271 of the Telecommunications Act of 1996 to Provide In-Region, InterLATA Services in the State of Oklahoma*, CC Docket No. 97-121 (May 16, 1997).

1. **Self-Referential BOC "Benchmarks"**

The Department has taken the position that a key requirement for approval of a Section 271 application is a demonstration that the market is "fully and irreversibly open to competition," specifically through the establishment of (1) performance measures and reporting requirements for wholesale performance, (2) performance standards (*i.e.*, commitments or obligations to meet specified levels of performance), and (3) performance "benchmarks." South Carolina Evaluation at 45; *see also* Louisiana II Evaluation at 38. The asserted justification for requiring this showing is the Department's view that "benchmarking" the performance of wholesale systems is "critical to enabling [ ] competitors to succeed in the marketplace." South Carolina Evaluation at 45. *See also* Louisiana I Evaluation at 31. Moreover, the Department asserts that "proper performance measures with which to compare BOC retail and wholesale performance, and to measure exclusively wholesale performance, are a necessary prerequisite to demonstrating compliance with the Commission's 'nondiscrimination' and 'meaningful opportunity to compete standards.'" South Carolina Evaluation at A-6.

When evaluating Section 271 applications for this showing that it views as so "critical," particularly in its more recent filings, the Department has not relied on benchmarks based on comparisons of regional holding companies. Instead, the Department has focused on performance standards that it believes should be set by the BOC itself based on its own retail operations, or on state-specific standards set

for the BOC by the state commission. The Department identifies these self-referential standards as the necessary "benchmarks." For example:

- "[G]iven BellSouth's lack of performance measures in a number of crucial areas, we still are unable to determine whether BellSouth has established enforceable performance standards for these areas or a track record, or benchmark, of wholesale performance." Louisiana I Evaluation at 32-33 (emphasis added).

- "[T]he absence of important data concerning wholesale performance" makes it "impossible to establish a reliable benchmark against which future performance can be measured," and there is no evidence that BellSouth "committed itself in any significant way to specific levels of performance or to any enforcement provisions to remedy inadequate performance." Louisiana II Evaluation at 38-39 (emphasis added).

- "BellSouth has no performance measurements for pre-ordering functions; few measurements for ordering functions; and no measurements for billing timeliness, accuracy and completeness. BellSouth is also missing numerous significant measurements involving service order quality, operator services, directory assistance, and 911 functions. . . . . Collectively, these deficiencies prevent any conclusion that adequate, nondiscriminatory performance by BellSouth can be assured now or in the future." South Carolina Evaluation at 47.

- "[I]mportant gaps in the measures proposed by Ameritech," including "a failure to measure and report actual installation intervals for resale, installation intervals for unbundled loops, comparative performance information for unbundled elements, and repeat reports for the maintenance and repair of unbundled elements," compel conclusion that "Ameritech has yet to establish all of the necessary performance benchmarks to satisfy the Department's competitive assessment." Michigan Evaluation at 40 (emphasis added).

- "[E]ven if SBC's processes were operating at some level, SBC has not established a sufficiently comprehensive set of performance standards, nor supplied its own retail performance information, to permit such a comparison." Oklahoma Evaluation at 60 (emphasis added).

- The Michigan Public Service Commission "defined a set of 12 criteria by which performance standards can be developed" by Ameritech Michigan, noting that while "Ameritech's progress in this regard is incomplete . . . . [we] find its efforts to be significant . . ." Michigan Evaluation at 39-40.

The Department has not suggested that a BOC need go outside its region to establish such benchmarks. At most, BOCs have been invited to look to other states within their region in the absence of actual data for the state in question. For example, the Department has said:

- "As is true with our analysis of wholesale support generally, our insistence on performance benchmarks does not require any particular level of use in Louisiana. Appropriate benchmarks may be established through commercial performance elsewhere in the BellSouth region. In the event that a BOC is not able to set a benchmark through actual use . . . . the Department would consider other means of ensuring adequate performance, including enforceable performance standards and other means of demonstrating wholesale capability, i.e., carrier-to-carrier testing, independent auditing, or internal testing." Louisiana I Evaluation at 33 (emphasis added); *see also* South Carolina Evaluation at 47.

2. Comparisons to Retail Operations

In addition to insisting on the setting of self-referential benchmarks, the Department has relied on comparisons between performance measures of an individual BOC's wholesale and retail operations for purposes of evaluating a BOC's compliance with Section 271 requirements. For example, in evaluating the most recent Section 271 application, from BellSouth Louisiana, the Department compared what the CLECs and what BellSouth itself received with respect to a number of pre-ordering, ordering, and maintenance and repair functions:

- "Since April 1998 . . . only two competitive carriers in Louisiana have used any unbundled loops in conjunction with other self-provided network facilities, and, collectively these carriers have placed in service only about 100 unbundled loops . . ." but "during 1997 alone, BellSouth added 89,000 new access lines, an average of over 240 new lines per day." Louisiana II Evaluation at 8 & n.14 (emphasis added).

- "During the period reported in the application, March-May 1998, CLEC users of BellSouth's LENS pre-ordering and ordering interface seeking to obtain information from customer service records ("CSRs") have experienced average response times nearly twice those experienced by BellSouth's own retail representatives." Louisiana II Evaluation at 29 (emphasis added).

- The "regionwide flow-through rate of 82% for CLEC orders" compared to "BellSouth's own regionwide flow-through rates [of] 96% for its retail residential orders, and 83% for its retail business orders. These numbers, at a minimum, suggest that either the CLECs' residential or business flow-through (or both) are substantially below BellSouth's own rates." Louisiana II Evaluation at 30-31 (emphasis added).

- "For example, for certain simple orders . . . Louisiana CLECs in May 1998 waited an average of eleven days for UNE orders, 1.93 days for residential resale orders, and 1.61 days for business resale orders, compared to only 0.88 days for BellSouth's own residential orders and 1.29 days for BellSouth's business orders." Louisiana II Evaluation at 33 (emphasis added).

- "[F]or Louisiana dispatch orders involving fewer than ten circuits, BellSouth in May 1998 missed provisioning appointments nearly twice as often for CLEC residential resale orders as for its own residential orders" Louisiana II Evaluation at 33 (emphasis added).

- "Based on May 1998 figures for Louisiana, CLEC resold business orders requiring trouble dispatches took over sixteen hours, nearly 40% longer than for BellSouth's own corresponding retail business orders." Louisiana II Evaluation at 34 (emphasis added).

- "[F]or numerous resale categories, the repeat rate for CLECs appears to be significantly worse than for BellSouth's retail business: [ranging from 30% to 97% higher for various categories of dispatch orders]." Louisiana II Evaluation at 35 (emphasis added).

The Department has relied on similar comparisons in evaluating BellSouth's initial Louisiana application, Ameritech's Michigan application, and SBC's Oklahoma application:

- "For example, flow-through continues to be a major problem, with extremely low rates compared to BellSouth's retail performance." Louisiana I Evaluation at 20 n.35 (emphasis added).

- "Ameritech's interconnection performance data clearly show that the end office integration (EOI) trunks used by CLECs to interconnect with Ameritech experience higher blocking rates than do the trunks used within Ameritech's own network." Michigan Evaluation at 25 (emphasis added).

- "SBC has not clearly demonstrated the ability to provision interim number portability ("INP") in a 'non-discriminatory' manner such that a competitor using INP would be able to provide the same level of service to its customers that SWBT provides its own retail customers." Oklahoma Evaluation at 35 (emphasis added).

3. Comparisons to Other States Within and Without the BOC's Region

When the Department does look outside a BOC's individual state to evaluate a Section 271 application, the focus is almost exclusively on the performance of individual operating companies in other states. By far, most of these comparisons are to states within that RBOC's region. For example, in its most recent evaluation of BellSouth Louisiana's collocation efforts, the Department compared BellSouth's performance on these issues in the applicant state with that in its other states:

- "As the Commission noted in its decision on BellSouth's South Carolina application, new entrants have experienced substantial delays in obtaining suitable collocation arrangements in the BellSouth region." Louisiana II Evaluation at 17 (emphasis added).

- "BellSouth has once again not provided sufficient specificity in advance . . . as to how it will charge for physical collocation space in Louisiana" even though "BellSouth *has* offered specific rates for space preparation fees in Georgia . . ." Louisiana II Evaluation at 23 & n.45 (emphasis added).

Where the Department looks outside the RBOC's region, the comparisons generally are based on the performance of an individual BOC operating in a

particular state. For example, in evaluating the prices for interconnection elements offered by Ameritech Michigan, the Department compared Ameritech Michigan's approach to that of other operating companies, not the RBOCs:

- "Ameritech's interim prices determined through arbitration in Michigan are for the most part relatively low compared with those of other BOCs and ILECs, and have not generated the volume of complaints about rate levels encountered in some other regions." Michigan Evaluation at 41 (emphasis added).

The same is true for the Department's evaluations of BellSouth's various applications. In its detailed analysis of BellSouth's South Carolina wholesale support processes, the Department noted in particular the practical limitations of a manual OSS process, citing Pacific Bell's experience in California and a California PUC decision, thereby comparing BellSouth's performance at the operating company level, not at the RBOC level. *See* South Carolina Evaluation at A-6 n.7 and A-28 to A-29 & n.44. The Department also indirectly compared the electronic interfaces of BellSouth to those developed by SBC, but this, too, was an operating company-to-operating company comparison, as the basis for the Department's analysis was the interfaces SBC had submitted as part of its Oklahoma application. *See* South Carolina Evaluation at A-5 & n.6 and A-11. The Department's out-of-region references in the Louisiana II evaluation were similarly state-specific. *See* Louisiana II Evaluation at 28 n.52 ("In contrast, Ameritech had provisioned 16,000 unbundled local loops ("ULLs") in Michigan alone at the time of its application there.").