

**DESCRIPTION OF TRANSACTION,  
PUBLIC INTEREST SHOWING,  
AND RELATED DEMONSTRATIONS**

This Exhibit is being filed in connection with a series of applications seeking the approval of the Federal Communications Commission ("FCC" or "Commission") to the transfer of control of FCC authorizations held by subsidiaries of Tele-Communications, Inc. ("TCI"), and entities controlled by TCI to AT&T Corp. ("AT&T").<sup>1</sup> The applications are being filed pursuant to an Agreement and Plan of Restructuring and Merger, dated as of June 23, 1998 (the "Agreement").<sup>2</sup> Through the use of facilities that are the subject of its FCC authorizations and licenses, TCI owns, operates, controls and has interests in various cable television systems throughout the United States. Although specific applications seeking FCC consent to the transfer of control of these authorizations are being filed on the appropriate FCC forms for each service, the proposed transactions and public interest considerations supporting the FCC's approval of the applications are constant throughout each application. As the public interest showing below clearly demonstrates, the Merger will foster new facilities-based competition in the provision of local telephone service and result in the provision of new and enhanced services to the public without reducing competition in any service or market.

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<sup>1</sup> The FCC authorizations controlled by TCI for which FCC consent is currently being sought include licenses in the cable television relay service, satellite transmit and receive earth station service, microwave service, private radio service and international common carrier service.

<sup>2</sup> The Agreement is among AT&T, Italy Merger Corp., a direct wholly-owned subsidiary of AT&T ("Merger Sub"), and TCI, with respect to the merger of TCI with and into AT&T's Merger Sub (the "Merger"). AT&T and TCI will file a copy of the Agreement in the docket for this proceeding established by the FCC.

Under the terms of the Agreement, and following a reorganization of certain of TCI's assets, AT&T will become the parent company of TCI. TCI will continue to exist as a wholly-owned subsidiary corporation of AT&T, and all the common stockholders of TCI will exchange their shares of TCI common stock for shares of AT&T common stock. Specifically, AT&T will create Merger Sub, a wholly-owned subsidiary which does not hold any FCC authorizations, and will merge that company with and into TCI, with TCI being the surviving company of its merger with the subsidiary. Following the Merger, each issued and outstanding share of TCI common stock will be converted into a right to receive shares of AT&T, including, in particular, shares of certain tracking stocks. The authorizations and licenses held by TCI subsidiaries will continue to be held by those subsidiaries, as controlled by AT&T.

**I. DESCRIPTION OF THE TRANSACTION.**

**A. The Merger Parties.**

*AT&T.* AT&T is the largest provider of domestic and international long distance telephone service in the United States and operates in more than 250 countries and territories around the world. AT&T provides these long distance communications services to residential, business and government customers. In addition to its long distance services, AT&T's other

communications services include local telephone, wireless and Internet access services. AT&T's total revenues from its communications services amounted to \$51.3 billion in 1997.<sup>3</sup>

AT&T primarily provides domestic and international long distance service to residential and business customers nationwide. In 1997, AT&T earned \$46.2 billion in revenue from its long distance services, including \$22.2 billion from business long distance service and \$24 billion from residential long distance service. Its combined revenues from these long distance services represented approximately 90% of its total of \$51.3 billion in revenues from communications services.

Prior to its acquisition of Teleport, AT&T provided local telephone service -- local exchange and exchange access services -- on a very limited basis. As the FCC concluded in Teleport, AT&T provides local telephone service to a "relatively small" number of business and residential customers.<sup>4</sup> In 1997, for example, AT&T's total revenues for its local telephone services were only approximately \$68 million, notwithstanding expending in excess of \$3 billion in its attempt to provide local service. AT&T currently provides residential local telephone service

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<sup>3</sup> The following description of AT&T's communications services will be supplemented by AT&T's 1997 Annual Report and 1997 Form 10-K filed with the Securities and Exchange Commission on March 27, 1998, copies of which will be filed in the docket for this proceeding established by the FCC. AT&T's provision of communications services and qualifications to be an FCC licensee also are a matter of record before the FCC, having been addressed within the last several months at the time AT&T sought approval for its acquisition of Teleport Communications Group, Inc. ("Teleport"). See Teleport Communications Group Inc., and AT&T Corp., FCC 98-169, released July 23, 1998 ("Teleport"), at ¶¶ 3-7.

<sup>4</sup> Teleport, FCC 98-169, at ¶ 4.

by purchasing and reselling service from other facilities-based local exchange companies, including primarily incumbent local exchange carriers ("ILECs"). AT&T currently provides such resale service to approximately 325,000 residential customers in 8 states.<sup>5</sup> AT&T has curtailed its active marketing of resold local residential exchange services, and has an attrition rate among its local residential customers of approximately three percent (3%) per month.

Prior to its merger with Teleport, AT&T also provided or planned to deploy facilities-based local calling services directed primarily to large and medium-sized businesses. AT&T provides one such local telephone service directed toward large business customers called "AT&T Digital Link" ("ADL"). As of August of 1998, through its ADL service, AT&T provides limited outbound and inbound service to its business customers in 10 states.<sup>6</sup> AT&T's revenues from its ADL service were approximately \$26 million for the first half of 1998. Additionally, AT&T initially had planned to deploy synchronous optical equipment-based facilities ("SONET Rings") in a limited number of areas to provide local exchange and exchange access service to its business customers. After two years and \$150 million in expenditures on its first market, Chicago, AT&T recognized only a limited footprint in Chicago, with four customers and a projected 1998 revenue of less than \$1 million.

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<sup>5</sup> In the Continental United States, these states are California, Connecticut, Georgia, Illinois, Michigan, New York and Texas. AT&T does not provide residential service to more than 100,000 customers in any state; in Illinois, AT&T serves less than 65,000 customers. In 1997, AT&T's revenue from its residential local service did not exceed \$10 million in any state; in Illinois it was approximately \$8.7 million. AT&T also provides limited local service in Alaska.

<sup>6</sup> These ten states are California, Connecticut, Florida, Georgia, New Jersey, New York, North Carolina, Pennsylvania, Tennessee and Texas. AT&T provides outbound local calling service, with no service offering regarding inbound traffic, in an additional 32 states.

On July 23, 1998, pursuant to prior Commission consent, AT&T acquired Teleport, the nation's largest competitive local exchange carrier ("CLEC"), primarily to address entry into the local exchange and exchange access market for business customers. At the time of its acquisition, Teleport had initiated the development of local telephone networks in 83 metropolitan areas in approximately 28 states throughout the United States.<sup>7</sup> From these operations, Teleport had earned revenues of \$494.3 million in 1997.<sup>8</sup> At the time of the merger of Teleport and AT&T, Teleport served approximately 16,500 buildings nationwide. Less than 100 of these buildings, however, were multiple dwelling units, and, at the time of its acquisition, Teleport provided residential local telephone service to only 12,000 customers nationwide.<sup>9</sup>

AT&T also provides wireless mobile telephone services in the United States, through its ownership and operation of AT&T Wireless Services, Inc. ("AT&T Wireless"). Currently, through its cellular and personal communications service offerings, AT&T Wireless serves approximately 6.6 million customers with revenue in 1997 of approximately \$4.4 billion.

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<sup>7</sup> These states include Alabama, Arizona, California, Colorado, Connecticut, Florida, Georgia, Illinois, Indiana, Kansas, Maryland, Massachusetts, Michigan, Minnesota, Missouri, Nebraska, New York, New Jersey, North Carolina, Ohio, Oregon, Pennsylvania, Rhode Island, Tennessee, Texas, Utah, Washington and Wisconsin. The following description of Teleport's services will be supplemented by its 1997 Annual Report and 1997 Form 10-K filed with the Securities and Exchange Commission on March 9, 1998, copies of which will be filed in the docket for this proceeding established by the FCC.

<sup>8</sup> Teleport earned approximately \$163 million in revenue in New York, \$55 million in revenue in California and \$29 million in revenue in Illinois.

<sup>9</sup> AT&T also provides Internet access service to approximately 1.25 million customers through AT&T WorldNet Service, a service introduced by AT&T, and CERFNet, a service acquired with Teleport. AT&T WorldNet and CERFNet provide access to the Internet to residential and business customers through dial-up and dedicated connections.

AT&T Wireless serves numerous metropolitan markets, and its top ten markets in terms of customers served are New York City, Miami, Dallas, Seattle, Pittsburgh, Minneapolis, Portland, Tampa, Denver and Sacramento.

*TCI.* TCI, through its subsidiary TCI Communications, Inc. ("TCI-C"), is one of the largest providers of cable television service in the United States, and delivers a wide range of video products, including local broadcast stations; national, regional, and local cable programming services; premium movie and pay-per-view channels and sports programming services to homes and businesses nationwide.<sup>10</sup> In addition, TCI, through its Liberty Media Group and the TCI Ventures group, holds interests in companies that produce video programming services and that provide content-enriched high-speed Internet data services. TCI's total revenues for 1997 amount to approximately \$7.6 billion.

Through subsidiaries under its control, TCI-C provides cable television service to approximately 12.7 million customers, passing approximately 20.9 million homes.<sup>11</sup> TCI-C also holds minority interests in, or is a party to joint ventures with, other cable television operators. These non-controlled entities provide cable television service to approximately 7.5 million

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<sup>10</sup> The following description of TCI's services and investments will be supplemented by its 1997 Annual Report and 1997 Form 10-K filed with the Securities and Exchange Commission on March 27, 1998, copies of which will be filed in the docket for this proceeding established by the FCC.

<sup>11</sup> TCI's reports regarding the number of customers it serves and the number of homes passed by its cable television systems is based upon the most conservative interpretation of the FCC's ownership attribution rules.

additional customers, and pass approximately 13.2 million additional homes. TCI-C's revenues from its cable television operations totaled approximately \$5.8 billion in 1997, approximately 76% of TCI's total revenue for that year.

TCI provides virtually no long distance telephone service<sup>12</sup> and is engaged in limited tests of local exchange service. TCI's local exchange operations are offered only on a trial basis. TCI currently provides such local exchange service to approximately 4,724 residential customers in the communities of San Jose, California; Dallas, Texas; Hartford, Connecticut and Arlington Heights, Illinois, with the majority of those customers located in Hartford. TCI has proposed to dispose of its interest in its cable operations and ancillary local telephone operations in Hartford, Connecticut, in a transaction with Cablevision Systems Corp.,<sup>13</sup> and had no current plans to expand its telephony operations prior to the proposed Merger. In 1997, TCI's total revenues for local exchange services were less than \$1 million. TCI also operates common carrier microwave services, which are used primarily to provide for carrier-to-carrier services and video backhaul transport in 18 states. These operations include service to 275 customers and generated approximately \$36 million in revenue in 1997.

TCI, through the Liberty Media Group, also holds interests in various companies that provide video programming. These companies include: Discovery Communications, Inc.;

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<sup>12</sup> One of TCI's subsidiaries, WTCI, provides a limited amount of business long distance service in Wyoming on a resale basis.

<sup>13</sup> The parties have entered into a letter of intent and are currently negotiating definitive documents regarding this proposed transaction.

USA Networks; BET Holdings, Inc.; Fox/Liberty Networks, LLC; QVC, Inc.; MacNeil/Lehrer Productions and Encore Media Group. TCI, through the TCI Ventures Group, also indirectly holds an approximately 39% equity interest and approximately 71% voting interest in @Home, which provides content enriched Internet cable services over cable television infrastructure. Having begun commercial operation in September 1996, @Home's primary offering allows residential subscribers to connect their personal computers via cable modems to a new high-speed broadband network that uses a hybrid fiber-coaxial cable ("HFC") plant to transmit data at higher speeds than typical dial-up services. The @Home service is an "always on" connection and provides unique local and national multimedia programming content and data services. By mid-1998, approximately 8 million homes had access to the HFC plant required for the delivery of @Home's service.<sup>14</sup> As of August 1998, @Home had launched its service in portions of 35 cities and communities in the United States and Canada and had approximately 147,000 subscribers. During this same period, @Home's accumulated deficit had risen to approximately \$94 million.

Finally, TCI, through the TCI Ventures Group, currently holds minority interests in certain partnerships (collectively, "Sprint Spectrum") which provide personal communications services ("PCS") under the Sprint brand of Sprint Corp. ("Sprint").<sup>15</sup> TCI, Sprint, and the other

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<sup>14</sup> @Home currently has entered into distribution arrangements with 15 cable companies that serve approximately 58.5 million homes in the United States and Canada. These cable companies are TCI, Cox, Cablevision Systems Corp., Comcast, Rogers, Shaw, InterMedia Partners, Jones Intercable, Garden State Cable, Century Communications, Marcus Cable, Bresnan Communications, Insight Communications, Cogeco Cable and Lenfest Communications.

<sup>15</sup> At present, TCI, through its subsidiary TCI Spectrum, holds a 30% interest in the limited partnership Sprint Spectrum Holding Co. L.P. ("Sprint Holdings"). Sprint, through its

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parties in Sprint Spectrum, have agreed upon a restructuring of Sprint Spectrum pursuant to which Sprint Spectrum would be contributed to Sprint in exchange for a new class of Sprint common stock to be designated as "Sprint PCS Tracking Stock."<sup>16</sup> Sprint currently intends to sell Sprint PCS Tracking Stock in a public offering. In connection with the restructuring, TCI will receive registration rights for its Sprint PCS Tracking Stock. As a result, following the expiration of any "standstill" or "lock-up" period, TCI would be in a position to sell its Sprint PCS Tracking Stock into the public markets.<sup>17</sup>

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<sup>15</sup> (...continued)

subsidiary, Sprint Enterprises, holds a 40% interest in Sprint Holdings. The remaining 30% interest in Sprint Holdings is split equally between Cox Telephony Partnership (a Cox subsidiary) and Comcast Telephony Services (a Comcast subsidiary). The same partners hold identical interests in MinorCo, L.P. ("MinorCo") which holds the remaining 1% interest in Sprint PCS. Sprint Holdings and MinorCo in turn own 99% and 1% interests respectively, directly and indirectly. Sprint Holdings also owns a 99% interest in a series of operating subsidiaries, through which the PCS network known as "Sprint PCS" operates. In a separate venture, TCI, through its subsidiary TCI Philadelphia Holdings, Inc., owns a 35.3% interest in two partnerships, PhillieCo I and PhillieCo II (together "PhillieCo," and together with Sprint Holdings, the "Sprint Ventures"). Sprint Enterprises, in turn, owns a 47.1% interest in PhillieCo. The remaining interest (17.6%) is owned by Cox, through its subsidiary, Cox Communications Wireless, Inc.

<sup>16</sup> In 1995, Sprint, TCI and other cable partners considered building a national wireless and wireline telephone network, utilizing PCS technology and cable network infrastructure to offer local telephone and specialized data transmission services. In early 1996, however, Sprint Spectrum decided to focus solely on providing wireless telephony services. As a result, the existing cable local loop facilities were no longer integral to the venture's business plan. In May 1998, Sprint and the cable partners, including TCI, therefore agreed to the restructuring plan.

<sup>17</sup> In addition to reducing TCI's interest in Sprint's PCS ventures and ensuring that TCI will not be actively involved in those ventures, the restructuring increases the liquidity of TCI's investment while giving Sprint access to the equity markets as an alternate source of funds for the considerable capital investment that is still needed to buildout its PCS network. Requiring Sprint to redeem TCI's interests for cash or other considerations immediately necessarily would have reduced the investment that Sprint could commit to developing its PCS service. Similarly, TCI's sale of its PCS stock in a short period following the restructuring would greatly increase the amount of stock being offered in the marketplace and could create an amount of available stock in  
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Sprint already has sought and obtained FCC consent to the initial phases of this restructuring.<sup>18</sup> Assuming the restructuring is consummated prior to the Merger, TCI's interest will have been restructured such that it would own approximately 23.8% of the outstanding shares of Sprint PCS Tracking Stock, which shares would have only approximately 2.38% of the voting power of Sprint PCS Tracking Stock. TCI's shares of the Sprint PCS Tracking Stock would constitute less than a 1% voting interest in Sprint's outstanding capital stock.

**B. Description of the Merger.**

Pursuant to the Agreement, TCI will merge with AT&T's Merger Sub. In connection with the Merger, the assets and businesses of AT&T and TCI (the "Merger Parties") will be attributed to either of two groups: the Liberty Media Group or the Common Stock Group. The Liberty Media Group will continue to hold, among other things, its video programming businesses and TCI's minority interest in Sprint's PCS ventures.<sup>19</sup>

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<sup>17</sup> (...continued)

the public market that would impair Sprint's own ability to issue new PCS stock as a source of capital. Either requirement would have an adverse effect on Sprint's ability to raise the capital necessary to build out the PCS network, and thus necessarily would undermine the public policy objective of promoting competition in the mobile telecommunications marketplace.

<sup>18</sup> See Public Notice, Report No. LB-98-54, released July 17, 1998; Public Notice, Report No. LB-98-65, released August 31, 1998.

<sup>19</sup> Prior to the Merger, and subject to shareholder approval, TCI plans to combine its Liberty Media Group with its TCI Ventures Group, whereby each outstanding share of Ventures will be exchanged for .52 shares of Liberty. Subsequently, TCI will combine the business operations of the two groups, and the new combined group will be called Liberty Media Group. Immediately prior to the merger, the new Liberty Media Group (reflecting the combined businesses of Liberty  
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The Common Stock Group initially will consist of what is now AT&T and TCI's cable television, telephone and Internet businesses. Subsequent to the Merger, AT&T plans to create a third group, the "AT&T Consumer Services Company" ("AT&T Consumer Co"), that will include the cable television, local residential telephone, domestic long-distance residential telephone, international residential telephone and residential Internet businesses, along with AT&T's consumer residential wireless mobile communications business. The Common Stock Group will continue to reflect the remainder of AT&T's current network and business services.<sup>20</sup>

In structuring this transaction, one of the intentions of the Merger Parties was to separate the performance of the Liberty Media Group's businesses from those of AT&T's other businesses. This will be reflected in the composition and structure of the management and the

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<sup>19</sup> (...continued)

Media and TCI Ventures) will transfer its investment in @Home, the National Digital Television Center and its ownership of Western Tele-Communications, Inc., to the TCI Group. Although AT&T will be the legal owner of the assets and the businesses of the Liberty Media Group, the businesses of the Liberty Media Group will continue to be managed by the managements of Liberty and Ventures that are in office prior to the Merger. Such management will have substantial control of the business and affairs of the Liberty Media Group following the merger as a result of agreements negotiated in connection with the Merger.

<sup>20</sup> AT&T stockholders will be asked to approve amendments to the AT&T Charter to authorize new "tracking stocks" in connection with the Merger; one of which is intended to reflect the performance of the assets and businesses of the Liberty Media Group. Subsequent to the Merger, AT&T plans to create another "tracking stock" to reflect the performance of AT&T Consumer Co. "Tracking stock," a device which has been used for approximately 15 years, is typically issued by diversified corporations. Although it is common stock of the parent issuer, it is intended to reflect the businesses and assets of a distinct business segment or group of assets of the issuer. The underlying business or asset tracked by the stock is commonly referred to as a "group," as in the "Liberty Media Group." AT&T's use of tracking stock will allow the public to invest selectively, and to evaluate separately, the discrete businesses of the Liberty Media Group, AT&T Consumer Co and the Common Stock Group.

board of directors of post-Merger AT&T, as well as in other aspects of the transaction. Mr. C. Michael Armstrong, who is AT&T's Chairman and CEO, will remain Chairman and CEO of AT&T. Mr. John Zeglis, who is currently AT&T's President, and Mr. Leo J. Hindery, Jr., who is TCI's current President, are expected to become Chairman and President, respectively, of AT&T Consumer Co. On a day-to-day basis, the Liberty Media Group will continue to be managed by its current management. Dr. John C. Malone, TCI's current Chairman and CEO, will serve as Chairman of the Liberty Media Group. Mr. Robert R. Bennett, currently President and CEO of Liberty Media Corporation, will be President and CEO of the Liberty Media Group.

Several factors will facilitate the Liberty Media Group's operational independence. First, for at least the first seven years after the Merger, directors appointed by TCI prior to the Merger will make up a majority of the Board of Directors of Liberty Media Corporation ("LMC"), through which substantially all of the Liberty Media Group's business will be managed. Second, members of the LMC Board cannot be removed by AT&T (which indirectly will be the sole stockholder of LMC following the Merger), except for cause. Third, after consummation of the Merger, AT&T's Board of Directors will increase in size by one member. AT&T has agreed that this additional director (who initially will be Dr. Malone) will be a person who, by virtue of his or her background and experience, will understand and reflect issues of concern to the Liberty Media Group and the holders of Liberty Media Group tracking stock.<sup>21</sup> Fourth, AT&T's Board also will establish a Capital Stock Committee, which will have three members, one of whom will be the Liberty Representative and the other two of whom will be independent directors of AT&T

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<sup>21</sup> This director is hereafter referred to as the "Liberty Representative."

who are not affiliated with AT&T's management.<sup>22</sup> Fifth, AT&T will adopt a policy statement that its cash dividend policy will be to distribute, subject to the limitations in the AT&T Charter, dividends and distributions received by AT&T from businesses included in the Liberty Media Group to the holders of AT&T Liberty Media Group tracking stock. Sixth, certain inter-group liabilities, obligations and other inter-group relations will be limited by contract, which will act as a "firewall" between the groups. Finally, the Agreement and underlying Merger-related documents expressly provide that the Liberty Media Group and the Common Stock Group can compete with each other in their lines of business and have no obligation to provide financial support or share corporate opportunities with each other. Although the Merger therefore will allow AT&T to integrate its telecommunications business with TCI's cable networks and thereby build a facilities-based local residential telecommunications network, the structure of the transaction specifically will establish and preserve the Liberty Media Group as a separately managed business group engaged in its current video programming businesses and any other business it elects to enter.

## **II. THE MERGER ANALYSIS.**

As detailed below, the proposed Merger will expand and accelerate AT&T's ability to compete with ILECs in providing local telephone service to residential customers. By integrating AT&T's telecommunications businesses with TCI's cable business, the Merger will

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<sup>22</sup> The AT&T Board will delegate authority to the Capital Stock Committee to interpret, make determinations under and oversee the implementation of key policies, including a "fair dealing" standard that governs dealings among the three groups.

provide AT&T with vital access to TCI's cable facilities thereby benefitting consumers currently dependent on ILECs for local service. With a significant investment of capital to upgrade those cable facilities to allow two-way toll quality voice telephone communications, AT&T eventually will be able to compete with ILECs where TCI currently has facilities. As a result, the Merger will increase the availability to consumers of a wide array of packaged and a la carte services -- including local, long distance and wireless telecommunications service, as well as video and content-enriched high-speed Internet services.

**A. Defining the Analysis and the Relevant Services.**

Because the proposed transaction between AT&T and TCI does not involve a horizontal merger in any market, the Merger Parties do not believe that it is necessary for the FCC, in determining whether the Merger is in the public interest, to conduct the three-stage analysis of the potential competitive effects of the Merger that it employed in NYNEX Corp., Transferor, and Bell Atlantic Corp., Transferee, 12 FCC Rcd. 19985 (1997) ("Bell Atlantic/NYNEX"). Instead, in approving the Merger, the FCC certainly would be justified in relying on the substantial public interest benefits that flow from increased competition from a new facilities-based provider of local exchange and exchange access service as envisioned by the Telecommunications Act of 1996. Nevertheless, in the interest of expediting the FCC's consideration of this series of applications seeking FCC consent to the transfer of control of TCI's licenses, the Merger Parties have provided two sections of analysis that each independently support the grant of those applications.

The first section provides the three-stage analysis set forth in Bell Atlantic/NYNEX, as well as in MCI Communications Corp. and British Telecommunications PLC, 12 FCC Rcd. 15351 (1997) ("MCI/BTI"), and, recently, Teleport, FCC 98-169, released July 23, 1998. This analysis involves: (a) defining the possible relevant product and geographic markets; (b) determining the most significant competitors in these markets, including actual competitors and currently precluded significant competitors; and (c) performing a competitive analysis. In performing the competitive analysis, the FCC has sought to determine whether the merger will reduce competition either by enabling the combined entity to achieve unilateral market power or by reducing the number of competitors in any relevant market to a number that facilitates the competitors' collective exercise of market power through coordinated interaction. The FCC also has sought to determine if a proposed merger will actually be procompetitive, by enabling a competitor more quickly or efficiently to compete with a dominant firm or serve as a stronger maverick in preventing coordinated interaction in furtherance of the collective exercise of market power.<sup>23</sup>

Prior FCC opinions and orders suggest that the FCC might consider as potentially relevant for analysis under the Commission's market analysis framework the following seven types of services: (1) local exchange and exchange access services, which have separate residential and business components and which comprise a variety of local service areas; (2) domestic long distance services; (3) United States international telephone services; (4) wireless mobile

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<sup>23</sup> See Bell Atlantic/NYNEX, 12 FCC Rcd. at 20008-20; MCI/BTI, 12 FCC Rcd. at 15367-76; Teleport, FCC 98-169, ¶¶ 11-19.

telephone services, which comprise a variety of local service areas; (5) multichannel video programming distribution services; (6) video programming; and (7) Internet services.

In addition to its competitive analysis, the FCC also considers other more general public interest benefits that will result from a proposed merger, including, among other things, the pro-competitive effect that the merger will have on the quality, and price of services provided to the public. The FCC weighs any potential competitive or other harms from a proposed merger against these benefits to determine whether, on balance, the proposed transaction is in the public interest.<sup>24</sup> In the section following its three-stage analysis, the Merger Parties therefore set forth significant public interest benefits that support the grant of their applications independent of the FCC's assessment under the Bell Atlantic/NYNEX framework.

## **B. Competitive Analysis.**

### **1. Local Exchange and Exchange Access Services.**

*Residential Telephone Services.* By enabling AT&T to provide facilities-based local telephone service to residential customers that neither AT&T nor TCI could provide as expeditiously on their own, if ever, the Merger greatly enhances, rather than impedes, competition for residential local exchange and exchange access services. As the FCC has found, "incumbent

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<sup>24</sup> See Bell Atlantic/NYNEX, 12 FCC Rcd. at 20001, 20007; MCI/BTL, 12 FCC Rcd. at 15367; Teleport, FCC 98-169, at ¶¶ 11-12.

local exchange carriers are the sole actual providers of local exchange and exchange access services to the vast majority of residential and small business customers in most areas of the United States."<sup>25</sup> In 1996, ILECs earned more than 98% of all local exchange and exchange access revenues nationwide, and any competition from CLECs generally has focused on large business customers in large cities, not on residential or small business customers.<sup>26</sup> In fact, the FCC has found no evidence suggesting the existence of any significant actual competitors to the ILECs with respect to the provision of residential local telephone service in the geographic areas where AT&T is present.<sup>27</sup>

Currently, AT&T and TCI each provide an extremely limited amount of residential local exchange and exchange access services in, collectively, eight states in the United States. TCI presently is engaged in limited telephony trials in California, Connecticut, Illinois and Texas, and AT&T provides residential services in those states, as well as Alaska, Georgia, Michigan and New York. AT&T's residential service is limited almost entirely to resold local exchange service to approximately 325,000 customers, in circumstances where it is no longer actively marketing its service.<sup>28</sup> For its part, TCI has established only four test-bed local exchange services in Hartford, Connecticut; Arlington Heights, Illinois; San Jose, California and Dallas, Texas. TCI has

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<sup>25</sup> Teleport, FCC 98-169, at ¶ 24; see Bell Atlantic/NYNEX, 12 FCC Rcd. at 20032-33.

<sup>26</sup> See id. at ¶ 24 n.80; Trends in Telephone Service, February 1998, at 28, 32.

<sup>27</sup> See Teleport, FCC 98-169, at ¶ 24 n.81.

<sup>28</sup> See supra at 3-4. AT&T also provides very limited local service in Alaska and Teleport serves a de minimis number of multiple dwelling units.

proposed to transfer the Hartford, Connecticut operations to Cablevision Systems Corp. as part of TCI's proposed disposition of its interest in the Hartford cable television system.<sup>29</sup> The San Jose and Dallas trials are very limited in nature, serving a total of less than 400 customers, and are focused solely on multiple dwelling units. At the time of its decision to enter the Agreement, TCI had no plans to expand its telephony offerings beyond these very limited trials.

Given the very limited residential local exchange and exchange access offerings of AT&T and TCI, the Merger will have no adverse competitive effect. The Chicago metropolitan statistical area ("MSA") is the only area where both of the Merger Parties provide local telephone service worthy of analysis.<sup>30</sup> AT&T and TCI face significant competition from the ILEC in the MSA, Ameritech, and together AT&T and TCI are de minimis participants. Ameritech reported total local revenues for 1997 in Illinois of approximately \$2.19 billion, a figure that is more than fifty times the Merger Parties' total local exchange revenue in Illinois, even including Teleport's business operations.<sup>31</sup> Ameritech reported approximately 6.25 million subscribers lines in Illinois as of the close of 1996, or approximately 85% of all local telephone lines in Illinois.<sup>32</sup> Almost all

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<sup>29</sup> See supra at 7. The overwhelming majority of TCI's local telephone customers, less than 5,000 in total, are located in Hartford.

<sup>30</sup> Although TCI provides very limited telephone service to customers in California and Texas and Teleport serves isolated multiple dwelling units in certain states, the amount of service is de minimis, and does not warrant analysis.

<sup>31</sup> AT&T earned less than \$40 million from its sale of local telephone service in Illinois in 1997. AT&T earned \$8.7 million from its local resale operations in Illinois in 1997, and Teleport earned less than \$30 million from its local exchange services directed to business customers in Illinois.

<sup>32</sup> See Trends in Telephone Service, July 1998, at 98.

of the remaining 15% of local telephone lines were held by independent local telephone companies.<sup>33</sup> Ameritech thus currently has over 100 times the number of subscriber lines as AT&T and TCI have residential customers in Illinois,<sup>34</sup> and AT&T's share of the local residential revenues and traffic in the Chicago MSA is no greater than one percent. Thus, even where both AT&T and TCI have initiated some residential local exchange service, they remain very small, and face a dominant competitor.<sup>35</sup>

The Merger unquestionably will promote competition in the provision of local residential telephone service in areas where TCI has existing cable infrastructure. As a result of the Merger, AT&T and TCI together will be able to provide a competitive facilities-based local telephone service to consumers on a schedule that greatly exceeds the pace AT&T or TCI independently could provide such service. AT&T and TCI anticipate combining their assets to invest in and develop advanced wireline facilities that will compete directly with ILECs to provide toll-quality voice and high-speed data communications to America's homes. TCI contributes its residential wireline network and architecture that currently serves approximately 12.7 million homes through cable systems controlled by TCI. AT&T contributes its experience in providing

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<sup>33</sup> Id. Fifty-five other independent local telephone companies reported approximately 1.15 million additional lines in Illinois. Id.

<sup>34</sup> Together, the Merger Parties currently serve less than 62,000 residential customers in Illinois. See supra at 3,7.

<sup>35</sup> AT&T and TCI also face potential competition in the residential local exchange market from other previously precluded carriers, including other ILECs in Illinois, adjacent ILECs such as Bell Atlantic, MCI Communications Corp. ("MCI") and Sprint. See Bell Atlantic/NYNEX, 12 FCC Rcd. at 20029-33; Teleport, FCC 98-169, at ¶ 25.

toll-quality voice and data traffic, switching technology, a brand name that can compete with incumbent local telephone companies and capital to cover the significant costs of the upgrade of TCI's facilities to provide for two-way voice telephony. Together, AT&T and TCI plan to use TCI's local network, enabling AT&T to provide facilities-based residential service without designing and constructing such a local network from ground zero. AT&T's telephony resources and capital thus can be used to bring a new facilities-based competitor to local exchange and exchange access services where TCI has cable television facilities, and enable AT&T to emerge as a new competitor for the local residential telephone services at a pace and scope that could not be achieved otherwise.<sup>36</sup>

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<sup>36</sup> AT&T's attempts in recent years to develop the capacity to provide local telephone services have met with limited success. Until January 1998, AT&T tried to initiate competition in the provision of local telephone service through the provision of Total Service Resale ("TSR"), under which AT&T purchased services from an ILEC, and then resold those services to customers in competition with the ILEC. AT&T never considered TSR a long-term solution, however, because it required paying access charges to the ILECs for the origination and termination of long-distance telephone calls. Moreover, AT&T discovered through experience that TSR was impractical, given the difficulties associated with working with their ILEC competitors. After spending over \$3 billion on the initiation of local telephone service as of 1997 to achieve less than \$70 million in total revenues, AT&T abandoned further efforts to develop TSR in early 1998. AT&T's efforts to use unbundled network elements ("UNEs") to serve these and other customers also have been hampered by the difficulty in obtaining compliance by the ILECs with the FCC's implementing regulations and the Eighth Circuit's invalidation of the rule requiring ILECs to provide CLECs with UNEs and UNE combinations. See *Iowa Utilities Board v. FCC*, 120 F.2d 752 (Th Cir. 1997), *cert. granted*, 118 S.C. 879 (1998). As noted above, AT&T's plans to create a facilities-based network through its ADL service and SONET Rings technology were directed primarily to larger business customers, and, given the tremendous expense and time necessary to develop a local network, unlikely to result in local residential telephone service competition at any time in the near future. Finally, while AT&T's acquisition of Teleport will assist it in reaching urban businesses and a limited number of multiple dwelling units, it was never intended to enable AT&T to compete on a wide scale in the provision of local residential exchange services.

Business Services. The Merger will not impede competition for the provision of local exchange and exchange access services to businesses. As with residential service, the FCC has found that "[i]ncumbent LECs also continue to dominate the larger business market for local exchange and exchange access services."<sup>37</sup> As with residential service, AT&T and TCI presently provide a very limited amount of local exchange and exchange access services to larger businesses in the United States, especially when their operations are compared to the ILECs. The ILECs still earn in excess of 96% of the business revenues from the provision of local exchange services, and still control approximately 10 times the number of fiber miles controlled by the CLECs.<sup>38</sup> For its part, the FCC has never recognized TCI as a significant provider of telephony services to businesses, and the Merger thus does not eliminate a competitor in this service.

The Merger Parties, however, do face potential competition from other carriers besides the ILECS that previously were not significant competitors in providing this service. The FCC has stated that "numerous new entrants are rapidly entering this market, especially in central business districts in urban areas, and that any number of these other new entrants have both the capabilities and the incentive to compete effectively."<sup>39</sup> In the context of competition for larger businesses, AT&T and TCI face competition from a number of other CLECs in addition to that of its predominant ILEC competitor. For example, as recognized by the Commission in Teleport, in

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<sup>37</sup> Teleport, FCC 98-169, at ¶ 26.

<sup>38</sup> See Trends in Telephone Service, February 1998, Table 9.1, Chart 9.1; Teleport, FCC 98-169, at ¶ 27.

<sup>39</sup> Teleport, FCC 98-169, at ¶ 27.

AT&T's top ten service areas, there are currently between 5 and 12 operational CLECs, including Focal Communications Corp.; MCI Local Service; Metromedia Fiber Networks; MeTel; RCN Corporation; USN Communications, Inc.; WinStar Communications, Inc. and WorldCom, Inc.<sup>40</sup> In Chicago, the Merger Parties will face competition from more than 10 CLECs, including Allegiance Telecom Inc.; Focal Communications Corp.; Jones Lightwave; Metromedia Fiber Network Inc.; MGC Communications; Teligent; USN Communications; Winstar; MCI Metro and WorldCom. With the Merger, AT&T is not eliminating any of these potential CLEC competitors and these other new entrants will be "at least as significant a competitive force as either of the merging parties."<sup>41</sup>

This is especially accurate in this case, where TCI's facilities and local network will be useful primarily for providing residential local telephone service, and AT&T's business local exchange service will be provided predominantly through Teleport's facilities and through AT&T's ADL service. AT&T's share of 1997 local revenue in business local exchange services was less than 1%,<sup>42</sup> a figure that is constant in both New York state and Chicago. TCI's business service is even more limited. Even in the service areas where AT&T and TCI have their greatest local large business activity, their combined current presence is practically insignificant. In the New York City metropolitan area, AT&T's business revenues, including the revenues of Teleport, do

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<sup>40</sup> Teleport, FCC 98-169, at ¶ 27.

<sup>41</sup> Bell Atlantic/NYNEX, 12 FCC Rcd. at 20019; Teleport, FCC 98-169, at ¶ 27.

<sup>42</sup> Teleport, FCC 98-169, at ¶ 36.

not exceed 4% of local telephony service, and TCI-controlled cable systems do not provide local exchange service in the New York City metropolitan area.

As the FCC concluded in Teleport, rather than impede competition, the merger of companies with complimentary assets is likely to enable the merged entity to more quickly mount a challenge to the dominant position currently held by the ILEC service provider.<sup>43</sup> The current efforts of AT&T and TCI in the business local exchange service are nominal, but with TCI's network and architecture, and AT&T's brand name and other assets, the merged entity will be more likely to establish itself as a viable competitor in the provision of both residential and business local exchange services.

## 2. Domestic Long Distance Services.

Although AT&T is the largest provider of long distance services in the United States, the Merger does not pose any threat to competition for long distance services because TCI is not, and had no plans at the time it entered the Agreement to be, a competitor in the provision of long distance services.<sup>44</sup> Second, the FCC has recognized that AT&T's share of long distance services has declined steadily over the past 15 years, so much so that in 1995, the FCC reclassified

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<sup>43</sup> Teleport, FCC 98-169, at ¶ 39.

<sup>44</sup> In its merger analysis to date, including its decisions in NYNEX/Bell Atlantic and Teleport, the FCC has not even recognized TCI as a precluded competitor likely to provide competition for national long distance communications. See supra, at 7 & n.12 (WTCI provides very limited long distance service in Wyoming).

AT&T as a non-dominant carrier.<sup>45</sup> AT&T's share of long distance operating revenues eroded from 90.1% in 1984 to 44.5% in 1997, and was 51.8% in 1995 when AT&T was declared non-dominant.<sup>46</sup> AT&T's share of switched access minutes eroded from 80.2% in 1984 to 51.4% in 1997, and was approximately 55% in 1995 when AT&T was declared non-dominant.<sup>47</sup> Because the Merger will have no effect on AT&T's ability to supply long distance services, there is no reason to revisit the conclusions in the AT&T Domestic Non-Dominance Order in considering the instant transfer of control applications.

Third, the FCC has recognized that hundreds of other firms actually provide long distance service, and expects that previously precluded firms will be strong competitors when they are permitted to provide domestic long distance service. As the FCC has acknowledged, at least three other major service providers have competitive national, coast-to-coast fiber-optic networks (Sprint, MCI and WorldCom) and at least four other current service providers are currently constructing national coast-to-coast fiber-optic networks (Qwest Communications International, Inc., IXC Communications, Inc., Williams Communications Group, Inc., and Level 3 Communications, Inc.).<sup>48</sup> Further, as the FCC has noted, numerous other competitors provide

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<sup>45</sup> AT&T Domestic Non-Dominance Order, 11 FCC Rcd. 3271, 3273 (1995). Other factors such as customer "churn" would further demonstrate the competitiveness of the long distance market.

<sup>46</sup> Long Distance Market Shares, June 1998, at 16, Table 3.2.

<sup>47</sup> Id. at 2-3, Table 1.1.

<sup>48</sup> Teleport, FCC 98-169, at ¶ 28. In 1997, MCI's share of operating revenues for the long distance service was 19.4%, Sprint's share was 9.7% and WorldCom's share was 6.7%. See Long Distance Market Shares, June 1998, at 16, Table 3.2.

long distance service in large regional areas, including Excel Telecommunications, Inc.; Frontier Corp.; Cable & Wireless, Inc.; GTE and other non-Regional Bell Operating Companies.<sup>49</sup> Finally, the Regional Bell Operating Companies ("RBOCs"), competitors that have previously been precluded from entering certain service areas, are expected to be strong competitors at the time that they are permitted to enter the long distance market upon compliance with the requirements of the Telecommunications Act of 1996. Accordingly, the proposed Merger will not affect competition for domestic long distance telephone services. In particular, the Merger will neither give AT&T unilateral market power nor increase the likelihood of coordinated action among competitors.

### **3. United States International Telephone Services.**

Although AT&T is the largest provider of international telephone service in the United States, the Merger similarly will not reduce competition for the provision of international telephone services. First, as with domestic long distance service, TCI is not a significant competitor in the provision of international telephone service and had no plans to become a meaningful provider of international telephone service prior to the effective time of the Merger. Indeed, in its merger analyses to date, including MCI/BTI and Teleport, the FCC has not recognized TCI as a precluded competitor likely to provide competition for international telephone services. Second, the FCC has recognized that AT&T's share of international telephone

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<sup>49</sup> From 1984 to 1997, the market share of the more than 600 companies providing long distance service other than the four largest carriers had increased from 2.6% to 19.8%. Long Distance Market Shares, June 1998, at 16, Table 3.2.

traffic from the United States has decreased from 100% in 1984 to less than 50% in 1996, after it was declared a non-dominant international carrier.<sup>50</sup>

Finally, as the FCC has noted, "there are hundreds of carriers that" compete in providing international telecommunications services.<sup>51</sup> As of 1996, 47 carriers offered international services using their own facilities or leased lines and more than 300 additional firms offered international service on a resale basis.<sup>52</sup> GTE and other non-Regional Bell Operating Companies are currently competitors, and the RBOCs are likely to provide strong competition at some time in the future, certainly within each of their LEC regions.<sup>53</sup> The proposed Merger thus will not diminish competition for international telephone services.

#### 4. Wireless Mobile Telephony.

AT&T, through its ownership and control of AT&T Wireless, holds numerous licenses to provide commercial mobile radio service ("CMRS") in service areas throughout the

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<sup>50</sup> Teleport, FCC 98-169, at ¶ 31 & n.107; Trends in Telephone Service, February 1998, at 24; AT&T International Non-Dominance Order, 1 FCC Rcd. 17963, 17964 (1996). As indicated with respect to long distance service, other factors such as customer "churn" would demonstrate further the competitive nature of this service.

<sup>51</sup> Teleport, FCC 98-169, at ¶ 30.

<sup>52</sup> Id. In 1996, MCI had a market share of 20.3%, Sprint a market share of 8.9% and WorldCom a market share of 4.4%. Trends in Telephone Service, February 1998, at 26. Carriers other than the largest four international telephone service providers earned 18.1% of the revenues in this market. Id.

<sup>53</sup> Teleport, FCC 98-169, at ¶ 30.

United States.<sup>54</sup> Although AT&T is one of the largest providers of wireless mobile telephone services, and TCI currently holds indirectly a minority interest in Sprint's PCS ventures, the Merger will not pose any threat to competition or result in a violation of the FCC's rules.<sup>55</sup>

TCI, through certain subsidiaries, currently holds a minority interest in partnerships that operate Sprint's PCS business, including Sprint's domestic PCS wireless mobile telephone service.<sup>56</sup> TCI originally obtained this interest as part of a plan by Sprint and several cable television companies to build a national wireless and cable telephone network that would have combined Sprint's wireless technology with the cable companies' local networks. The plan to associate Sprint's wireless facilities and the cable networks has been abandoned, however, and, independent of its decision to merge with AT&T, TCI and other cable partners entered into a series of agreements with Sprint providing for a restructuring of their interests in Sprint's PCS operations. The restructuring will reduce significantly TCI's voting and equity interests in the Sprint Ventures, provide TCI with liquidity for its interest in Sprint's PCS ventures, and eliminate any active management or day-to-day operational role for TCI in those PCS ventures.

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<sup>54</sup> The licenses held by AT&T Wireless are a matter of record in its FCC Forms 430 filed at the FCC, and have been identified in an attachment to the FCC Form 704 applications seeking FCC consent to the instant Merger. AT&T Wireless' largest CMRS areas include New York City, Miami, Dallas, Seattle, Pittsburgh, Minneapolis, Portland, Tampa, Denver and Sacramento.

<sup>55</sup> Section 20.6 of the FCC's rules generally limits to 45 MHz the amount of broadband CMRS spectrum that a may be "attributable" to any licensee with significant overlap in any geographic area. 47 C.F.R. § 20.6(a). Any stock interest amounting to 20 percent or more of the equity, or outstanding stock, or outstanding voting stock of a broadband PCS, cellular or Specialized Mobile Radio ("SMR") licensee is "attributable." *Id.* § 20.6(d)(2).

<sup>56</sup> See *supra* at 8-10 & n.15.

Specifically, as part of Sprint's PCS restructuring, TCI will exchange its current partnership interests for Sprint PCS Tracking Stock amounting to a 2.38% voting interest and a 23.8% equity ownership interest in Sprint's PCS business.<sup>57</sup> TCI's Sprint PCS Tracking Stock will constitute less than a 1% voting interest in Sprint's outstanding capital stock. As a condition of restructuring, Sprint will conduct a public offering to raise between \$500 and \$525 million, to be invested in its PCS business. This offering will dilute TCI's interest even further, probably to a voting interest of less than 1% of the Sprint PCS Tracking Stock.<sup>58</sup> Moreover, under the terms of the restructuring agreement, TCI will receive rights to register for sale its stock in Sprint's PCS venture on a priority basis, beginning on the later of either (i) 90 days after Sprint PCS completes its initial public offering or (ii) 180 days after the restructuring is completed. Thus, when the restructuring takes place as anticipated, TCI will have the ability after the Merger to sell part or all of its interest in Sprint's PCS business in a timely and economically reasonable manner.<sup>59</sup>

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<sup>57</sup> The FCC already has approved the transactions that are proposed for Sprint's restructuring of its PCS ventures. See Public Notice, Report No. LB-98-65, released August 31, 1998.

<sup>58</sup> The initial public offering is a condition of the restructuring, and depending on the specific terms of the offering, will reduce TCI's equity interest in the Sprint PCS Tracking Stock to near 20%.

<sup>59</sup> TCI's sale of its investment immediately, however, would be ill-advised and actually hurt competition in the provision of wireless mobile telephone services. As indicated above, as part of its restructuring, Sprint is seeking to obtain large amounts of new capital to complete its nationwide PCS network, which will help to improve its ability to compete with, among others, AT&T. Requiring TCI to sell its interest likely would dilute significantly the value of new Sprint stock in the market, thereby impairing Sprint's ability to raise capital by issuing new stock. Under the restructuring agreement, TCI therefore has agreed, among other things, to remain a passive investor in Sprint's PCS ventures until the restructuring is completed. Any attempt by TCI to force a sale before Sprint's PCS restructuring is completed would harm competition in CMRS, and could result in a suit for specific performance for a breach of TCI's contractual obligations.

Additionally, for any time after the Merger that the Liberty Media Group retains its interest in Sprint PCS, AT&T Consumer Co will operate its CMRS business independently from Liberty Media Group's minority financial investment interest in Sprint PCS. As described above, following the Merger, the Sprint investment will be held by the Liberty Media Group, and therefore will be insulated from AT&T Wireless' CMRS business.<sup>60</sup> The Agreement thus eliminates any operational or financial link between AT&T Wireless and the Liberty Media Group's potential interest in Sprint PCS, making inapplicable the concerns underlying the FCC's spectrum aggregation limits in Section 20.6 of its rules.<sup>61</sup>

Nevertheless, and regardless of whether the FCC determines that TCI's interest in Sprint and AT&T's interest in AT&T Wireless should be aggregated subsequent to the Merger, AT&T will come into compliance with Section 20.6 in either of two ways, depending upon the

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<sup>60</sup> See *supra* at 10-13. As noted above, Liberty Media Group will be separately managed from the Common Stock Group and AT&T Consumer Co. Among other things, for at least the first seven years after the Merger, designees of TCI appointed prior to the Merger will make up a majority of the Board of Directors of LMC, and cannot be removed by AT&T except for cause. Additionally, the separate groups can compete with each other in their lines of business and have no obligation to provide financial support or share corporate opportunities.

<sup>61</sup> There are a number of reasons why TCI's interest after Sprint's restructuring would not be attributable to AT&T, or, if attributable, why the FCC could waive any prohibited cross-interest. See 47 C.F.R. § 20.6(d) & note 3. First, TCI's *voting* interest in Sprint PCS Tracking Stock is far less than the 20% voting interest that triggers attribution of TCI's interest in Sprint to AT&T. 47 C.F.R. § 20.6(d)(ii). Second, TCI's 23.8% passive *equity* interest in Sprint's PCS Tracking Stock need not trigger attribution to AT&T, because the Liberty Media Group which will hold stock in Sprint will be operated and tracked separate from the Common Stock Group and AT&T Consumer Co, which will hold AT&T Wireless' CMRS business. Third, Liberty Media group will not be involved in the operations of the Sprint PCS ventures and will not be in a position to influence Sprint PCS on a regular basis. Finally, any restrictions on the sale of TCI's interest in Sprint PCS were imposed to provide Sprint with the better opportunity to raise capital for its PCS operations, and thus increase its ability to provide service.

timing of the consummation of the Merger and the planned Sprint restructuring. First, after the Merger and the restructuring, pursuant to its registration rights with respect to the Sprint PCS stock, the Liberty Media Group could sell a part of its interest in Sprint PCS and bring its equity interest below 20%.<sup>62</sup> See 47 C.F.R. § 20.6(e). Second, the Liberty Media Group could place the Sprint PCS stock into a qualifying voting trust pending such a sale. *Id.* § 20.6(d)(ii). In either event, given the proposed Sprint restructuring, regardless of the FCC's interpretation of the application of Section 20.6 to post-Merger AT&T, AT&T would come into compliance with the FCC's spectrum aggregation limits. Alternatively, if the Sprint restructuring does not occur as planned, in order to facilitate Sprint's raising of capital for its PCS business, the FCC could grant an appropriate temporary waiver until such time as the Liberty Media Group could sell its Sprint PCS stock on commercially reasonable terms that would not adversely impact Sprint's ability to raise capital.<sup>63</sup>

TCI has no other presence in wireless mobile telephony, and, given the restructuring of its interest in Sprint's PCS ventures, is not currently a potential provider of

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<sup>62</sup> As an initial matter, Sprint's restructuring will reduce TCI's voting interest in Sprint PCS Tracking Stock below 3%, and any subsequent public offerings will reduce TCI's equity interest in that stock below 23.8%.

<sup>63</sup> The Sprint restructuring and its timing are subject to other conditions, including Sprint stockholder approval and completion of an initial public offering, that are beyond the control of AT&T. Any temporary waiver that would be necessary as a result of changes or delays in Sprint's restructuring would enhance competition for wireless mobile telephone services by preserving Sprint's ability to raise capital needed to make it a more effective competitor. The duration of any such waiver would be governed by the timing of Sprint PCS's restructuring and its public offering.

wireless mobile telephone services absent the Merger.<sup>64</sup> For this reason, the Merger will not harm competition for wireless mobile telephone services. Moreover, wireless mobile telephone service is an intensely competitive business. In each local service area, there are at least five, and possibly more, CMRS competitors. Two cellular service providers with at least 25 MHz are licensed in each service area, and three PCS service providers with at least 30 MHz are licensed in each service area. Other CMRS providers are viable entrants and providers of competitive service, including national SMR service operators such as Nextel Communications, and other licensees of D, E and F Block PCS Spectrum. At least one of these competitors is an incumbent LEC cellular service provider. Accordingly, the Merger should not increase the likelihood of either unilateral action by a dominant player or concerted action among competitors.

#### **5. Multichannel Video Programming Distribution Services.**

Although TCI-C is one of the largest providers of cable television service in the United States, AT&T does not compete in the distribution of multichannel video programming and had no plans to enter this business prior to its Agreement to merge with TCI. In 1996, AT&T had entered into an agreement with DirecTV, then a nascent DBS system owned primarily by Hughes Electronics Corporation. In return for its investment of \$140 million, AT&T received a 2.5% equity interest and the exclusive right to market DirecTV to AT&T's customers. In

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<sup>64</sup> TCI and the other cable companies that initially invested in the Sprint Ventures have entered into "standstill" agreements with Sprint, dated May 26, 1998, under which TCI and its affiliates may not either acquire voting securities in Sprint before the restructuring closes, or for 10 years after the restructuring closes, if such acquisition would lead to TCI holding more than 1.5% of the then outstanding voting securities of Sprint.

December of 1997, however, prior to these merger discussions with TCI and for business reasons that were unrelated to the Merger, AT&T sold its entire interest in DirecTV back to one of Hughes' subsidiaries.<sup>65</sup>

Second, there are numerous actual and potential competitors in the business of multichannel video programming distribution ("MVPD") that currently would be "at least as significant a force" as AT&T in the MVPD service. More than 12 million television homes currently receive service from alternative MVPD providers, including DBS providers such as DirecTV, which is now the nation's largest DBS service provider. That figure is expected to increase by at least 50%, and perhaps double, by the year 2000.<sup>66</sup> Moreover, ILECs are previously precluded competitors that can be expected to compete for MVPD customers. Ameritech, for example, has constructed and commenced the provision of cable television service in parts of Michigan, Ohio and Illinois.

Indeed, the Merger is likely to encourage competition by accelerating the ILEC's plans for the distribution of their multichannel video programming services. As a result of the Merger, within the next several years, AT&T likely will be able to provide packaged (and separate) voice and video services to residential consumers. Although ILECS such as Ameritech

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<sup>65</sup> Among other things, experience proved that the costs of marketing DirecTV were much higher, and the subscription rates through AT&T were much lower, than had been initially projected, rendering the venture unprofitable for AT&T.

<sup>66</sup> See NCTA Comments, Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming, Notice of Inquiry, CS Docket No. 98-102, filed July 31, 1998, at 6; Cablevision: The Handbook for the Competitive Market, Vol. III, 1998, at 10.

have begun the process of delivering video programming to the home, the Merger should provide additional motivation for the ILECs to expedite the provision of their own video service. The Merger thus should stimulate MVPD competition rather than restrain it.<sup>67</sup>

## **6. Video Programming.**

The Merger will not adversely affect competition in the provision of video content and programming. As noted above, TCI, primarily through Liberty Media Corporation and also through indirect interests, has affiliates that provide video content and programming, including Discovery Communications, Inc.; BET Holdings, Inc.; Fox/Liberty Networks, LLC; QVC, Inc.; Encore Media Group and other programming sources. AT&T, however, does not produce video programming or content, and is not a likely new video programming provider absent the Merger. The Merger therefore will not in any way reduce the number of providers of video programming services.

Nor does the Merger pose the threat of creating a dominant player capable of exercising unilateral market action. First, Liberty Media Corporation does not possess majority voting control of any programmers, except Encore Media Group and TCI Music, Inc. Second,

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<sup>67</sup> Furthermore, more than 95% of all television markets are served by at least 5 local broadcast television stations that provide free over-the-air video programs, and most television markets in the United States are served by at least 10 free over-the-air television stations. Moreover, the over-the-air broadcast stations will launch digital service beginning in a few months, which will increase still further their competitive presence in the MVPD marketplace, as the transition to digital broadcasting is phased in for different broadcaster in different markets over the next several years.

numerous other actual competitors exist, including seven television networks (Disney/ABC, CBS, NBC, Fox, WB, UPN, and PaxNet), various independent television production companies, and many other cable programmers. AT&T currently has no ownership interest in these or any other programmers, and thus the Merger does not increase the likelihood that any group of programmers will be able to adversely affect competition for video programming through the exercise of concerted action.<sup>68</sup>

## 7. Internet Services.

Through its AT&T WorldNet service and the CERFNet service that it acquired with Teleport, AT&T provides Internet access to approximately 1.25 million customers, out of an estimated 40 to 50 million Internet service subscribers and 90 to 100 million Internet service users. As discussed above, TCI indirectly holds an interest in @Home, which provides content enriched, high-speed Internet cable services over a cable television network to less than 150,000 subscribers. In light of the relatively small size of the new AT&T and TCI Internet businesses and the highly competitive nature of this dynamic industry, the Merger will not have an adverse effect on competition for the provision of Internet access and content services.

As an initial matter, AT&T and @Home combined represent less than 3% of the estimated Internet customers in the United States, a figure dwarfed by numerous other actual and

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<sup>68</sup> As discussed above, after the Merger, the video programming business of TCI will be held through the Liberty Media Group, which will be operated separately from the cable television operations of AT&T Consumer Co.

potential providers of Internet services. The nation's largest Internet service provider is WorldCom's UUNet, which provides Internet access and services to, among others, America OnLine ("AOL"), CompuServe and the Microsoft Network ("MSN"). AOL itself has 12 million customers, nearly ten times AT&T's customers and 80 times the customers of @Home; CompuServe alone adds an additional 2 million customers to AOL's reach. For its part, MSN has approximately 1.4 million customers. Other significant Internet service providers include GTE Internetworking, PSINet, EarthLink Sprint Internet, MCI Internet, MindSpring Enterprises, Erols and NETCOM On-Line Communications Services, Inc. Another venture, "Road Runner," is also on its way to establishing itself as an Internet service competitor.<sup>69</sup> The ILECs also are developing competitive broadband Internet service businesses through their Asynchronous Digital Subscription Line ("ADSL") and Integrated Services Digital Network ("ISDN") services. Ameritech (Michigan and Illinois), BellSouth Communications (Southeast United States), and Bell Atlantic (Pennsylvania, New York, Massachusetts and the District of Columbia) all have current Internet service operations or have announced plans to offer such service within the next year. Finally, others, including SBC Communications and US West.net, provide service or can be expected to provide competitive service in the near future.

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<sup>69</sup> Road Runner, the owners of which include Time Warner (37%), MediaOne (34%), Microsoft and (10%) and Compaq (10%), has access to at least 27 million homes, although only approximately 7.5 million of those homes currently are passed by upgraded, two-way HFC cable.

**C. Conclusion.**

As is demonstrated above, the proposed Merger will not reduce competition in any service, but will promote competition for many, if not all, of these services. In particular, as a result of the Merger, AT&T and TCI plan to combine their complementary assets and expertise to produce new competition to ILECs with respect to the provision of residential local exchange and exchange access service. The Merger is likely to enable the post-Merger AT&T to mount more quickly a challenge to the dominant position currently held by ILEC service providers, thereby increasing competition for both the local residential and business telephone services. With respect to Internet services, the Merger should create a stronger participant that will provide new and differentiated services in an effort to challenge the more established competitors.

The Merger also will not adversely affect competition in the provision of other services provided by the Merger Parties. Competition in the provision of wireless mobile telephone services, multichannel video programming distribution services and video programming services will not be affected adversely, because only one of the Merger Parties is an actual or potential participant in the provision of these services. With respect to these services as well, the Merger will enhance competition rather than restrict it.

### III. PUBLIC INTEREST BENEFITS.

The Merger will produce substantial public benefits that justify expeditious approval of the applications to transfer control of the subject FCC authorizations to AT&T. As demonstrated above, after the expenditure of billions of dollars on the effort to provide local exchange and exchange access services, the Merger will bring AT&T to the next level as a potential provider of local telecommunications services.<sup>70</sup> Combining the complementary operations and strategies of AT&T and TCI-C will put the Merger Parties in a position, within a foreseeable time period, to compete against the ILECs in the provision of residential telephony services and to develop and offer the next generation of Internet Protocol ("IP") telephony, broadband data and cable services. The transaction thus will promote the primary goals of the Telecommunications Act of 1996, by fostering facilities-based competition for the delivery of two-way local residential voice communications and advanced broadband services.

Through the combination with TCI and the continued evolution of AT&T's nationwide backbone network, AT&T will be able to obtain significantly accelerated entry into residential local telephony, "next generation" IP telephony, and diversified digital data and video services. TCI will have instant access to AT&T's capital, expertise and established telephony brand to support the combined company's new product offerings and marketing efforts. In sum, the Merger Parties plan to be the first fully-integrated residential communications services

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<sup>70</sup> See *supra* at 3-4, 18-22 (discussing AT&T's TSR, ADL and SONET Ring services).

provider with a national product including the ability to provide long distance, video, local, wireless, Internet and other data services on a packaged, as well as individualized, basis.

Upgrading the TCI cable infrastructure to provide broadband video, voice and IP products and services will not occur overnight, and it will occur at a substantial cost. To achieve these benefits, the Merger Parties first will need to complete the upgrade of TCI's cable infrastructure to provide for the delivery of advanced video and data transmissions. The Merger will provide TCI with the financial certainty that its upgrades will proceed on schedule following the Merger, or, if possible, on an expedited basis. Following the Merger, AT&T plans to upgrade the TCI network and architecture to a high-speed system that will carry two-way voice services with the toll-quality clarity and reliability that will be necessary to convince customers to switch from their current ILEC carriers. AT&T also will add innovative equipment to TCI's networks, including enhanced switching and other systems. Ultimately, AT&T will participate with its vendors in the development and deployment of new multi-purpose digital customer terminals with technology that will permit the complete integration of voice, data and video service. Consumers then will be able to access a complete range of services, including digital and "downloadable" video programming, World Wide Web and Internet access, shopping, on-line bill paying, interactive programming and other forms of electronic commerce, in addition to a full range of local and long distance voice services utilizing toll-quality IP telephony.

As has been discussed in Section II above, the upgrade contemplated by TCI prior to the decision to merge with AT&T involved the creation of additional capacity, content-

enriched high-speed data services, and impulse pay-per-view video, but not, in the near term, voice telephony. The network upgrade envisioned by AT&T will include voice telephony through a series of phased introductions. The initial phase will involve the deployment of equipment, compatible with a circuit switched network, at the customer premise and hub location and relies on the circuit switched network for transport of the call. An interim phase involves the deployment of IP-based equipment at the customer premise and hub location, but continues to rely on a circuit switched network. The ultimate phase will utilize end-to-end packet architecture for the delivery of telephony.

As an initial matter, the Merger Parties believe that TCI will need to expend approximately \$1.8 billion between 1998 and 2000 to upgrade its current facilities to increase channel capacity, provide high-speed data, and pay-per-view video. This upgrade, however, does not include voice telephony. AT&T anticipates that \$400 to \$500 million of the estimated \$1.8 billion upgrade will be expended by TCI prior to the Merger to upgrade the TCI network, so that perhaps one-third of TCI's existing cable plant will be upgraded by the consummation of the Merger. Assuming an expeditious approval of the Merger, it is anticipated that the Merger Parties will complete approximately 60% of the two-way cable upgrade by year-end 1999, and 90% of the upgrade by year-end 2000.

To increase channel capacity, TCI must deploy fiber optic facilities closer to the customer. This will be done by extending the fiber node -- the facility at which the high capacity fiber optic cable from the cable headend or hub connects to the lower capacity coaxial cable --

closer to the home. Under TCI's existing architecture, each fiber node services from 2,000 to 10,000 homes. In TCI's upgraded system, the fiber nodes will be deployed closer to homes, such that each fiber node will serve an average of 600 homes. In this upgrade, TCI also will deploy the equipment needed to provide the cable network with two-way capabilities. This replacement of equipment includes installation of new equipment at the headend or hub and at the fiber node, and deployment of two way amplifiers in the coax network. In addition to these two main components of the upgrade, TCI will replace cable and other equipment where needed in order for the network to handle more capacity.

While TCI's business plans absent the Merger included upgrading its network to provide increased programming capacity, high speed data, and pay-per-view video, TCI did not have plans, nor the capital in the short term, to upgrade the facilities and establish the marketing infrastructure necessary to provide telephony over cable. For its part, to provide facilities-based local exchange service expeditiously, AT&T needs control of a local loop that has been previously unattainable. Thus, but for the proposed Merger, the telephony upgrade to TCI's network would not have occurred at any time in the near future and AT&T would not have wired access to the homes of potential customers. To add telephony capability to TCI's upgraded network, AT&T currently estimates that it will expend less than \$600 and potentially as low as \$300 per subscriber to deploy the necessary customer premise IP telephony facilities and other infrastructure represented in the final phase of its upgrade to TCI's network. To the extent that AT&T, in the effort to get service to its customers as soon as possible, offers cable telephony on an interim basis

through the use of existing circuit switched technology, AT&T estimates that it will need to expend approximately \$750 per subscriber.

As noted, while AT&T's ultimate plan calls for the development of an end-to-end packet network, AT&T initially will need to deploy cable telephony in conjunction with its existing switched circuit network in 1999 and 2000. To provide cable telephony in a circuit switched environment, AT&T still will need to deploy certain customer premise equipment and new terminals at hub locations in order to convert signals to a standard format interface to the public switched network during the initial phase of its facilities-based local telephony service. These converted signals will travel through the Merger Parties' transport facilities to an existing AT&T switch or to the switch of another carrier if AT&T does have local switching facilities. From the switch, the call will be routed to the appropriate interexchange or local carrier.

While AT&T intends to move to the final phase of its local telephony plans as quickly as possible, AT&T may need to include an interim IP phase. In this phase, AT&T will use IP-based equipment with the TCI network, but in order to transport the call over the Merger Parties' facilities, the signal will be converted to the standard interface and directed over the public switched network. In its final phase, AT&T will provide cable telephony using IP packet technology in its central office and the network. Under this architecture, AT&T will deploy IP telephony-based equipment at the customer premise and at the hub. New IP-based packet equipment will be installed at AT&T's central office, including packet switches. In this final

phase, calls will be directed over AT&T's IP-based packet network if the caller is presubscribed to AT&T; other calls will be directed to the appropriate carrier's network.

AT&T will achieve certain economies of scale through the Merger that will both expedite its ability to provide new and differentiated services and make those services more economically efficient to provide. As an initial matter, as indicated above, AT&T has access to an existing wired network with access to approximately current cable television customers. Beyond simply obtaining access to TCI's wireline infrastructure, AT&T and TCI can accomplish the upgrade of TCI's infrastructure to provide for both two-way voice and digital video and data transmissions at the same time. AT&T also can, in certain instances, connect TCI's facilities to Teleport's switches, thereby using Teleport's switches and transport facilities to carry the local traffic of post-Merger AT&T's voice customers. This architecture will enable AT&T to spread the high fixed costs associated with these facilities over more lines and services, thereby enhancing AT&T's ability to price its products more competitively against entrenched local carriers. Given the positive effects of the Merger on competition as well as the public benefits of new services to consumers from the transaction, the Merger is undoubtedly in the public interest.<sup>71</sup>

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<sup>71</sup> It should be noted that, although the Merger Parties' plans for the Merger are ambitious, they are also limited and will take time to complete. Moreover, despite building upon the networks acquired through the mergers with Teleport and TCI, AT&T will still not be able to provide "all distance" service nationwide. As noted above, TCI currently provides cable television service to approximately 12.7 million subscribers, and passes approximately 20.9 million homes. In addition, TCI has interests in, but does not manage or control, systems serving approximately an additional 7.5 million subscribers, and passing an additional 13 million homes. AT&T will need to continue to explore alternative approaches to be able to provide a competitive product in other locations. The proposed merger plans of AT&T and TCI, however, once consummated and implemented, will go far in providing new and needed competition for local residential telephone

(continued...)

#### IV. ADDITIONAL MATTER

As the Commission is aware, TCI's subsidiaries and affiliates hold a number of licenses to operate cable television relay system, satellite earth station, private and common carrier point-to-point microwave, common carrier and private business radio station authorizations. The proposed Merger results in a transfer of control of all of these authorizations. Although the applications covering the authorizations are intended to be complete, the licensees involved in the proposed transaction may have on file and may file additional applications for new or modified authorizations or other facilities that may be processed or granted by the FCC in the ordinary course during the pendency of the subject transfer of control applications.

Given the ongoing regulatory activity of TCI, including the need for TCI to file numerous applications with the FCC during the period in which the instant transfer of control applications will remain pending at the FCC, the Merger Parties request that grant of the instant transfer of control applications include the authority for AT&T to acquire control of: (1) any authorization issued to TCI or its subsidiaries and affiliates during the Commission's consideration of the transfer of control applications and the period required for consummation of the transaction following approval; (2) construction permits held by licensees involved in this transfer of control that mature into licenses after closing and that may have been omitted from the transfer of control applications; and (3) applications that will have been filed by such licensees and that are pending

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<sup>71</sup> (...continued)

service, and in serving the public interest by facilitating the development and availability of a full range of higher quality telecommunications services for consumers.

at the time of consummation of the proposed transfer of control. Such action would be consistent with prior decisions of the Commission.<sup>72</sup>

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<sup>72</sup> See, e.g., Teleport, FCC 98-169, at ¶ 58; Craig McCaw and AT&T, 9 FCC Rcd. 5836, 5909 n.300 (1994); American Teleservices, Mimeo No. 3061 (Com. Car. Bur.), released March 23, 1984, at ¶ 14; RAM Communications Holdings of Texas, Inc., Mimeo No. 2604 (Com. Car. Bur. 1984), at ¶ 6.