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July 30, 1999

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

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

Re: *Ex Parte* Comments of AT&T Corp. & MediaOne Group, Inc.
MM Docket No. 92-264 (Horizontal Ownership Limits)
CS Docket No. 98-82 (Cable Attribution Rules)

Dear Ms. Salas:

AT&T Corp. ("AT&T") and MediaOne Group, Inc. ("MediaOne") submit this *ex parte* letter to address a recent development -- AT&T's proposed acquisition of MediaOne -- that underscores the fundamental point made by both companies in comments filed in the above-captioned proceedings.[1] The proposed acquisition focuses attention on the fact that upgraded cable systems are capable of providing multiple services, including competitive local telephony, and that cable regulations developed in the isolated environment of video have the potential to frustrate the development of advanced cable networks and the deployment of these services. In particular, a rule prohibiting a single cable operator from having controlling or minority interests in cable systems that pass more than 30 percent of the nation's cable homes would undermine the fundamental objective of the Telecommunications Act of 1996 (the "1996 Act") -- and the strategic driver of AT&T's cable investments -- to bring about local telephone competition. And, as the attached Public Interest Showing demonstrates, such a rule could have that

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[1] In order to assist the Commission in its deliberations in these two proceedings, AT&T/MediaOne attach hereto, and requests inclusion in the record of the horizontal ownership and cable attribution proceedings, the "Description of the Transaction, Public Interest Showing and Related Demonstrations," filed in *Transfer of Control of FCC Licenses from MediaOne Group, Inc. to AT&T Corp.* (filed July 7, 1999) ("Public Interest Showing").

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anticompetitive effect without in any way furthering the video programming competition goals that motivated Congress to adopt the horizontal cable ownership limits.

Notwithstanding Congress' and the Commission's efforts to encourage local telephony competition, incumbent local exchange carriers ("ILECs") retain monopoly control over local exchange and exchange access service areas nationwide. Although competition for the largest business customers is beginning to develop in some urban areas, competition for residential and small business ("mass market") local exchange and exchange access service has been virtually non-existent.[2]

AT&T is committed to reversing this situation and ensuring that "residential local exchange competition becomes a reality sooner rather than later."[3] In addition to the assets committed to the acquisition of TCI and its proposed acquisition of MediaOne, AT&T has committed to invest billions of dollars of shareholder assets to upgrade its networks to provide facilities-based local telephone competition. As the Commission has recognized, "AT&T is one of only a few firms that currently possesses the experience, brand name assets, and financial resources that are essential for quick and substantial entry into the retail residential local exchange and exchange access markets."[4]

However, as explained in the attached Public Interest Showing, in order to provide local telephony competition on a broad scale, it is critical that AT&T acquire the facilities of MediaOne. By combining its strong telephony brand, sophisticated knowledge of marketing telephony services, and technical expertise in establishing and managing telephone networks, with MediaOne's cable systems, AT&T will be able to provide an alternative to the ILECs' services for residential customers far more quickly and effectively

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[2] Memorandum Op. and Order, *In re Application of Teleport Communications Group, Inc., Transferor, and AT&T Corp., Transferee*, 13 FCC Rcd. 15236, at ¶ 24 (1998) (ILECs "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.").

[3] Memorandum Op. and Order, *Applications for Consent to Transfer of Control of Licenses and Section 214 Authorizations from Tele-Communications, Inc., Transferor, to AT&T Corp., Transferee, 14 FCC Rcd. 3160*, at ¶ 48 (1999)*("AT&T-TCI")*.

[4] *Id.* at ¶ 47.

than either company could separately.[5] In fact, by acquiring MediaOne, AT&T will gain *immediate* access -- and the ability to provide competitive, facilities-based local exchange services -- to millions of consumers in service areas where it currently has no facilities and cannot provide competitive local telephony.[6]

Moreover, the acquisition of MediaOne is critical to enable AT&T to spread the enormous investment required to deploy cable telephony to a wider customer base. As demonstrated in the Public Interest Showing, deployment of cable telephony requires a large fixed investment in the development of engineering protocols and operating standards and practices; construction and furnishing of central offices, transport facilities, and databases; hiring and training of installation and maintenance crews; and establishment and staffing of customer care centers. Similarly, the costs of marketing new services to residential consumers are substantial. The economies that AT&T will achieve as a result of its acquisition of MediaOne are particularly important because, although the acquisition will give AT&T a "footprint" roughly the same size as an Ameritech-SBC-PacBell, AT&T for several reasons will begin with many *fewer* customers than such an ILEC. First, cable

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[5] MediaOne has faced a number of obstacles in developing competitive local exchange telephony, including lack of brand recognition (and, accordingly, consumer confidence), lack of telephone network management expertise, and the absence of telephone marketing and customer care service expertise. Thus, MediaOne today has only approximately 26,000 telephone customers and a penetration level of less than 3 percent of the homes ready for its telephone service, despite having invested approximately $4.1 billion to upgrade its system to provide telephony. *See* Public Interest Showing at 21-24.

[6] The benefits of local telephony competition could not be achieved without the acquisition. This is so primarily because attempts to contract with MediaOne to allow AT&T to lease its facilities to provide cable telephony would be much less efficient than full integration when the parties are trying to deal with rapidly evolving technologies and service. This is particularly true where, as here, there is technology and service convergence -- no one can predict very far into the future what technologies and services are going to develop increased demand and what that means for efficient allocation of cable bandwidth. Without knowing the answers to these questions, potential joint venture partners have difficulty resolving issues such as how much bandwidth would be reserved for services to be provided by one joint venturer and how much bandwidth would be reserved for services to be provided by the other joint venturer. *See* Public Interest Showing at 31-32.

and telephone service have dramatically different penetration rates: on average, 94 percent for telephone and 65 percent for cable television. Thus, even when a cable company passes as many houses as a telephone company, it has almost 30 percent fewer customers. Second, as a new entrant into telephony, cable companies start with *no* telephone customers. Third, cable companies must expend enormous sums of money to research, develop, and implement broad scale cable telephone networks while ILECs already have ubiquitous, working networks in place.

Under these circumstances -- where Congress has placed such a heavy emphasis on the development of local telephone competition and the ability of AT&T to expand its ownership of cable systems is so obviously critical to achieving that goal -- it is imperative that the Commission reexamine its suspended horizontal ownership rules from this broader perspective. In particular, AT&T/MediaOne recommend that the Commission make at least the following changes: 1) consistent with the underlying purposes of the rules, attribute to an MSO only those cable systems for which the MSO actually does or could control programming choices or purchase programming; 2) consistent with the Commission's proposal in the *Further NPRM*, measure an MSO's horizontal concentration level as a percentage of all MVPD subscribers; and 3) significantly raise the 30 percent limit. These changes would allow the Commission to satisfy the underlying purposes of the horizontal rules without sacrificing the enormous benefits in terms of local telephony competition that AT&T and other companies could achieve through increased cable system ownership.

Congress enacted the cable horizontal ownership limit based on the concerns that cable operators could: (1) exercise monopsony power to force unfair concessions from programmers;[7] and (2) vertically foreclose entry by programmers, thereby reducing program diversity.[8] Thus, as the Commission has acknowledged, the purpose of the

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[7] See H.R. Rep. No. 628, 102nd Cong. 2d Sess. 42-43 (1992) ("[T]he size of certain MSOs could enable them to extract concessions from programmers, including equity positions, in exchange for carriage.").

[8] See S.Rep. No. 92, 102nd Cong, 1st Sess. 32 (1991) ("[T]here are special concerns about concentration of the media in the hands of the few who may control dissemination of information ... and will slant information to their own biases or ... provide no outlet for unorthodox or unpopular speech because it does not sell well, or both.").

horizontal ownership limit relates entirely to the ability of cable operators adversely to affect programming competition and diversity.[9] As the attached Public Interest Showing makes clear, AT&T's proposed acquisition of MediaOne implicates neither of those concerns.

As an initial matter, existing and growing competition from non-cable MVPDs, which serve as alternative outlets for video programming, sharply constrains (if not eliminates) the ability of any cable operator to engage in conduct that would be harmful to the programming business. As demonstrated in the Public Interest Showing, MVPD competition has grown rapidly in the nearly six years since the horizontal rules were adopted. Consider, for example, that DBS had not even been launched when the rules were adopted and today two of the seven largest MVPDs are DBS companies, DirecTV and Echostar. DBS is growing 20 times as fast as cable (and winning two of every three new customers when competing against cable), obtaining exclusivity rights to valuable sports and entertainment programming, partnering with powerful ILECs to market programming locally, and aggressively entering the Internet access business. It is no wonder that the Justice Department recently found that "consumers view [DBS and cable] as similar and to a large degree substitutable."[10] Other MVPDs, including the ILECs, utilities, SMATV, C-band, and MMDS, provide further competition to cable.

The growth of DBS and other competitors to cable means that programmers now have meaningful alternative outlets for distributing their product. The presence of these alternatives, and the fact that they are growing much more rapidly than cable, necessarily

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[9] See Second Report and Order, *Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992*, 8 FCC Rcd. 8565, at ¶ 10 (1993) ("Congress concluded that [the] degree of [cable] concentration, though low relative to other industries, may enable some MSOs to exercise excessive market power, or monopsony power, in the program acquisition market. Congress was concerned in particular with preventing large vertically integrated cable systems from creating barriers to entry for new video programmers, and from causing a reduction in the number of media voices available to consumers.").

[10] Complaint, *United States v. Primestar, Inc.*, No. 1:98CV01193, at ¶ 63 (D.D.C. May 12, 1998). It is also worth noting that under the Communications Act a cable franchise is deemed competitive if 15 percent of the subscribers in the franchise area get their programming from a non-cable MVPD, and today, on a national basis, 16 percent of all subscribers get their programming from a company other than their cable operator.

reduces any MSO's power to foreclose rival programmers or to obtain unfair concessions from programmers. As the Commission recently observed, "*[w]ith the growth of alternative MVPDs, network programmers gain alternative avenues for distribution of their products, thus reducing cable operators' market power or influence in the purchase and distribution of network programming.*"[11]

In light of the dramatic growth in MVPDs other than traditional cable systems, and consistent with the statutory purpose underlying the ownership limit, it would be arbitrary and irrational for the Commission to retain an ownership rule that fails to take account of all MVPDs. Rather, the Commission should amend the suspended rule to measure a cable operator's horizontal concentration level as a percentage of all MVPD subscribers. The suspended rule, based on cable homes passed, completely ignores the considerable increase in the number of subscribers served by competing MVPDs, most importantly DBS, so that it vastly overstates an MSO's ability to engage in vertical foreclosure or to exercise monopsony power.[12] Indeed, the Commission already has proposed to adopt an MVPD subscriber test in the *Further NPRM*.[13] AT&T/MediaOne fully support that proposal.

Moreover, in analyzing the ability of an MSO to foreclose rival program services or to obtain anticompetitive concessions from programmers, the only relevant systems are those for which the MSO controls programming choices or buys programming. If an MSO cannot force a cable system to decline to carry a rival program service, then the system is irrelevant to that MSO's ability to pursue a vertical foreclosure strategy. Similarly, an MSO derives no power to force anticompetitive concessions from a programmer based on a cable system for which it does not purchase programming, even if the MSO has a minority interest in the system. Thus, it is perfectly consistent with the underlying purposes of the horizontal ownership statute for the Commission to attribute to an MSO

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[11] Memorandum Opinion and Order on Reconsideration and Further Notice of Proposed Rulemaking, *In the Matter of Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992 - Horizontal Ownership Limits*, 13 FCC Rcd. 14462, at ¶ 80 (1998) ("*Further NPRM*") (emphasis added).

[12] Moreover, AT&T/MediaOne believe that it is virtually impossible to define or quantify homes passed. *See* Public Interest Showing at n. 153.

[13] *Further NPRM*, at ¶ 79 (1998).

only those cable systems for which the MSO controls programming choices or purchases programming.[14]

AT&T/MediaOne also urge the Commission to raise the 30 percent limit. Again, the growth of competitive alternatives to cable, particularly DBS, has directly and substantially reduced the theoretical concerns that cable operators could exercise monopsony power or engage in vertical foreclosure to the detriment of the program marketplace.[15] Therefore, the Commission can significantly relax the cable ownership limit without being concerned that this will lead to anticompetitive behavior by large cable operators.[16]

Finally, AT&T/MediaOne would like to emphasize once again that the approaches to the suspended horizontal rules described in this letter are crucial to its ability to expeditiously provide facilities-based local telephony services in competition with the

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[14] As noted in the Public Interest Showing, after the Merger, AT&T will be involved to some extent in the purchase or selection of programming for cable systems with approximately 26.6 percent of current MVPD subscribers (23.7 percent after the Falcon Communications, L.P., Bresnan Communications Co., Ltd. Partnership, and Cox Communications, Inc. transactions are completed). Market shares of this size raise no conceivable concern that AT&T could exercise monopsony power or engage in vertical foreclosure under traditional measurements of market power. *See* Public Interest Showing at 55-60. Nor is there any concern that the proposed acquisition of MediaOne will reduce program diversity. *See id.* at 64-65.

[15] In addition, concerns that a cable operator could impair the programming marketplace are already largely foreclosed by existing regulations, such as the program access, program carriage, must carry, leased access, and channel occupancy rules, which address the very same behavior targeted by the horizontal limit. The Commission has recognized that because these rules "all affect the way the cable television industry currently operates and have a profound effect on current industry structure and performance," it is appropriate "to consider the impact of these provisions in alleviating some of the public interest and anticompetitive concerns about horizontal concentration." *Further NPRM at* ¶ 50.

[16] It is worth noting, in this regard, that in the 1996 Act Congress raised the national broadcast limit from 25 percent to 35 percent.

ILEC monopolies. That fact should guide the Commission as it considers its horizontal rules. Congress spoke most clearly in the 1996 Act about its paramount desire to inject competition into local telephony. The Commission should adopt an approach to cable horizontal ownership that enhances rather than reduces the chances of achieving that goal. Purely theoretical concerns about monopsony and vertical foreclosure provide no basis to deprive a significant number of American consumers of the actual benefits of a vibrant competitor to their local telephone provider.

AT&T and MediaOne look forward to working with the Commission on these issues. Please do not hesitate to contact us if we can be of any assistance.

Sincerely,

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AT&T Corp.

Susan Eid
MediaOne Group, Inc.

cc: Deborah Lathen
Quyen Troung
Darryl Cooper
Sunil Daluvoy

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)
	)
Applications for Consent to the	)
Transfer of Control of Licenses	)
	)
MediaOne Group, Inc.,	)
Transferor	)
	)
To	)
	)
AT&T Corp.,	)
Transferee	)

APPLICATIONS AND PUBLIC INTEREST STATEMENT

DESCRIPTION OF THE TRANSACTION, PUBLIC INTEREST SHOWING AND RELATED DEMONSTRATIONS

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July 7, 1999

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DESCRIPTION OF TRANSACTION,
PUBLIC INTEREST SHOWING,
AND RELATED DEMONSTRATIONS

This Exhibit is being filed in connection with a series of applications seeking the consent of the Federal Communications Commission ("FCC") to the transfer of control of Commission authorizations held by subsidiaries of MediaOne Group, Inc. ("MediaOne"), and entities controlled by MediaOne, to AT&T Corp. ("AT&T").[1] The applications are being filed pursuant to an Agreement and Plan of Merger dated as of May 6, 1999 (the "Agreement").[2] Through the use of facilities that are the subject of its Commission authorizations and licenses, MediaOne owns, operates and controls interests in various cable television systems throughout the United States. As this public interest showing demonstrates, the Merger will foster new facilities-based competition in the provision of local telephone service and result in new, enhanced and competitive services to the public without reducing competition in any service.[3]

Under the terms of the Agreement, AT&T effectively will become the parent company of MediaOne. The stockholders of MediaOne will exchange their shares of stock in MediaOne for shares of AT&T common stock, cash, or a combination of both. Specifically, AT&T will create Merger Sub, a wholly-owned subsidiary that does not hold any Commission

[1] The Commission authorizations controlled by MediaOne for which Commission consent is currently being sought include licenses in the cable television relay service, satellite transmit and receive earth station service, private radio service and international common carrier service.

[2] The Agreement is among AT&T, Meteor Acquisition Inc., a direct wholly-owned subsidiary of AT&T ("Merger Sub"), and MediaOne, with respect to the merger of MediaOne with and into Merger Sub (the "Merger").

[3] Although specific applications seeking Commission consent to the transfer of control of these authorizations are being filed on the appropriate Commission forms for each service, the proposed transactions and public interest considerations supporting the Commission's approval of the applications are the same for each application.

licenses, and will merge MediaOne into that company; Merger Sub will be the surviving company of the Merger, continuing to be wholly owned by AT&T and succeeding to all the assets, liabilities and businesses of MediaOne. The authorizations and licenses held by MediaOne subsidiaries will continue to be held by those subsidiaries, as controlled indirectly by AT&T.

I. INTRODUCTION

The Commission has recognized that one of the principal goals of the Telecommunications Act of 1996 (the "1996 Act" or "Act") was to open local exchange and exchange access service to competition.[4] At the time the 1996 Act was enacted, both the House and the Senate stressed the primary importance of promoting competition in the provision of local telephone service.[5] Nevertheless, more than three years after the passage of the 1996 Act, incumbent local exchange carriers ("ILECs") retain monopoly control over local exchange and exchange access service areas nationwide. Although competition for the largest business customers is beginning to develop in some urban areas,[6] competition for residential and small

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[4] *See, e.g., Defining Primary Lines*, 12 FCC Rcd. 13647, ¶ 25 (1997).

[5] *See* H.R. Rep. No. 104-204, at 48 (1995) (main component of the bill "promotes competition in the market for local telephone service"); S. Rep. No. 104-23, at 5 (1995) (legislation "reforms the regulatory process to allow competition for local telephone services by cable, wireless, long distance" and other entities).

[6] Memorandum Op. and Order, *Applications for Consent to Transfer of Control of Licenses and Section 214 Authorizations from Southern New England Telecommunications Corp., Transferor, to SBC Communications, Inc., Transferee*, 13 FCC Rcd. 21292, ¶ 20 (1998) ("*SBC-SNET*"); Memorandum Op. and Order, *Applications for Consent to Transfer of Control of Licenses and Section 214 Authorizations from Tele-Communications, Inc., Transferor, to AT&T Corp., Transferee*, CS Docket No. 98-179, ¶ 50 (FCC Feb. 18, 1999) ("*AT&T-TCI*").

business ("mass market") local exchange and exchange access service has been virtually non-existent.[7] In approving AT&T's acquisition of Tele-Communications, Inc. ("TCI"), the Commission recognized the profound benefits that mass market consumers would realize from the vigorous competition in residential local exchange service that would result from the combination of AT&T's telephony brand and experience with the network assets of a cable company.[8]

Like the Commission, AT&T is "committed to ensuring that residential local exchange competition becomes a reality sooner rather than later."[9] AT&T has repeatedly demonstrated its commitment to developing competition in local exchange services through the expenditure of substantial capital and effort. Indeed, in pursuit of its goal to provide local telephone service and Internet access alternatives at the mass market level in numerous individual service areas and across the United States, AT&T has taken substantial risks, committing to invest more than $100 billion of shareholder assets that will be necessary to provide facilities-based local telephone competition sooner rather than later. In addition to those associated with the TCI and MediaOne mergers themselves. These assets include billions of dollars expended on capital upgrades to facilities to provide for high quality Internet protocol ("IP") local telephone service, and prior to the initiation of such IP telephony, competition in the

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[7] Memorandum Op. and Order, *In re Application of Teleport Communications Group, Inc., Transferor, and AT&T Corp., Transferee*, 13 FCC Rcd. 15236, ¶ 24 (1998) ("*AT&T-Teleport*") (ILECs "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.")

[8] *AT&T-TCI* ¶¶ 146-47.

[9] *Id.* ¶ 48.

provision of facilities-based, circuit-switched local telephony. As the Commission recognized in *AT&T-TCI*, the best prospect for bringing effective competition to local exchange service areas in the near future is through combinations of complementary assets by emerging entrants into previously foreclosed markets.[10]

For the same reasons that it found that AT&T's acquisition of TCI was pro-competitive and served the public interest, the Commission also should find that the Merger of AT&T and MediaOne is pro-competitive and serves the public interest. Because of the complementary nature of AT&T's and MediaOne's assets, the combined entity will be able to provide an alternative to the dominant ILECs' services for residential customers far more quickly and effectively than either entity could separately. The combination of AT&T and MediaOne will foster competition in local telephony almost immediately in some service areas, where MediaOne's ongoing upgrade of its cable facilities to provide for telephony can be immediately combined with AT&T's superior brand, engineering and network management experience, customer care, as well as scale economies, to provide for competition that simply does not exist today. In other MediaOne service areas, AT&T's capital and telephony experience will expedite the construction and deployment of competitive facilities-based local telephony. The scale and clustering economies that will accompany the combination of the assets of AT&T and MediaOne will create a stronger competitor to ILECs that have the advantage of enormous geographic reach, clustering and home penetration at levels that neither MediaOne nor AT&T could achieve absent the Merger.[11]

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[10] *Id.*

[11] Even with the Merger, AT&T-MediaOne cannot achieve the same levels of clustering and home penetration as the largest ILECs.

The Merger will provide these benefits, as well as other benefits in the video and Internet access services described below, without diminishing competition in the provision of any services, given the complementary, rather than competing, nature of the assets of AT&T and MediaOne. AT&T and MediaOne do not serve the same geographic service areas except in a few insignificant instances of overlap, and the Merger therefore will not eliminate current or probable future competitors. Given the combined market shares of AT&T and MediaOne, the Merger also will not significantly increase concentration in any telephony, video or Internet service. Nor will the Merger give AT&T the ability or the incentive either to exercise monopsony power in video programming or to foreclose access to cable programmers that sell programming in competition with the programming provided by Liberty Media Group, which is independently managed and controlled by the holders of a separate tracking stock within AT&T. Rather, AT&T will have an even greater incentive to provide consumers access to the largest amount of programming possible in order to maximize the value of its cable assets.

For these reasons, the Merger is in the public interest and the applications for consent to the transfer of control of MediaOne's licenses to AT&T should be granted.

II. DESCRIPTION OF THE TRANSACTION

A. The Merger

MediaOne will be merged into Merger Sub, a wholly-owned subsidiary of AT&T, and will no longer exist as a separate entity. MediaOne's shareholders will have the option to

convert their shares into cash, shares in AT&T or a combination of both, based on the shareholder's election.[12]

B. The Merger Parties

AT&T - Telephony. AT&T provides domestic and international long distance telephone services to residential, business, and government customers in the United States and to more than 250 countries and territories around the world. AT&T also provides other communications services, including local telephone, wireless, and Internet access services. AT&T's 1998 communications services revenues were $53.2 billion.[13] In 1998, AT&T earned $22.9 billion in revenue from its business services, $22.6 billion from its consumer services and $5.4 billion from its wireless services.[14]

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[12] Shortly before entering into the Agreement, AT&T also entered into a Letter Agreement with Comcast Corporation ("Comcast"), which contemplates an exchange between AT&T and Comcast of certain cable television systems ("Comcast Exchange"). Upon the consummation of the Merger and the fulfillment of certain other conditions, Comcast will transfer to AT&T cable systems in Ft. Lauderdale and Davie, Florida; Sacramento, California; Chesterfield, Virginia; Chamblee, Georgia; Chicago, Illinois; Westmoreland, Pennsylvania; and the State of Colorado. AT&T will transfer to Comcast cable systems in Naples and Ft. Myers, Florida; Detroit, Michigan; Washington, D.C.; Baltimore and Ocean City, Maryland; the State of New Mexico; Philadelphia, Pennsylvania; and other systems in Michigan or in Nashville, Tennessee. In addition, AT&T currently owns 50 percent of the equity of Lenfest Communications, Inc. and has entered into an agreement to purchase the remaining 50 percent. Subject to certain conditions, Comcast will manage the cable television systems owned or controlled by Lenfest for ten years following AT&T's acquisition of the remainder of Lenfest. Applications for the FCC's consent to the transfers associated with these transactions will be presented in separate filings.

[13] 1998 AT&T Annual Report at 32.

[14] *Id.*

AT&T currently provides local telephone service – local exchange and exchange access services – on a limited basis.[15] At the time of its acquisition of TCI, AT&T offered resold local exchange service to less than one-half of one percent of its total residential customers.[16] At the present time, AT&T resells local exchange service to approximately 220,000 customers in seven states.[17] Although AT&T's revenues from all local telephone services increased, from $562 million in 1997 to $974 million in 1998,[18] revenues from local telephone service continue to comprise only a very small percentage of AT&T's total revenues and of total industry revenues in those markets.[19]

In July 1998, AT&T acquired Teleport, primarily to expand its offering of local exchange and exchange access services for business customers.[20] AT&T and Teleport together accounted for only 0.8 percent of 1997 local exchange and exchange access service revenues for large business customers.[21]

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[15] *See AT&T-TCI* ¶ 3; *AT&T-Teleport* ¶ 4.

[16] *AT&T-TCI* ¶ 3 & n.7 (AT&T resold local telephony to approximately 325,000 customers).

[17] These states include California, Connecticut, Georgia, Illinois, Michigan, New York, and Texas.

[18] 1998 AT&T Annual Report at 42.

[19] AT&T's efforts to compete in the provision of local exchange and exchange access service through resale of ILEC service, interconnection to ILEC facilities, and construction of its own facilities (ADL and SONET Ring), are now a matter of a well-documented record before the Commission. *See generally AT&T-TCI*; *AT&T-Teleport*.

[20] *AT&T-Teleport* ¶ 8.

[21] *Id.* ¶ 36. In addition, Teleport had only a minuscule share of the local exchange and exchange access service residential and small business revenues. *Id.* ¶ 33. At the time of the merger, Teleport operated in 83 cities in the United States, including 29 of the largest 30, providing local exchange and exchange access services primarily to business customers in urban areas and to a relatively small number of residents in multiple dwelling units in high-density areas. *Id.* ¶ 5.

In March 1999, a subsidiary of AT&T merged with TCI, and AT&T became the parent company of TCI. The merger enabled AT&T to integrate its telecommunications business with TCI's cable networks and thereby begin to build facilities-based local residential telecommunications networks where TCI operated cable systems. At the time of the merger, TCI was primarily a cable company, but was engaging in limited tests of local exchange service in San Jose, California; Dallas, Texas; Hartford, Connecticut; and Arlington Heights, Illinois.[22] AT&T has proceeded to upgrade TCI's cable network and deploy local telephony facilities, and already has begun providing facilities-based local exchange telephone service in Fremont, California.[23]

AT&T also provides wireless telephone services through its ownership and operation of AT&T Wireless Services Inc. ("AT&T Wireless").[24] AT&T Wireless operates and holds interests in commercial mobile radio service ("CMRS") systems in 26 of the 30 largest service areas in the United States. In 1998, AT&T Wireless generated revenues of approximately $5.4 billion from a wireless customer base of 9.7 million.[25]

AT&T – Cable Television Systems and Video Programming. AT&T, through its subsidiary TCI, delivers a wide range of video products, including local broadcast stations;

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[22] TCI had announced plans to sell its operations in Hartford, where the majority of its local residential business was located, to Cablevision Systems Corporation.

[23] *See AT&T-TCI* ¶ 148. The initiation of telephone service to residential customers in Fremont is part of a plan to initiate service in 10 areas in the near future.

[24] *Id.* ¶ 4.

[25] 1998 AT&T Annual Report at 32. In addition, AT&T has placed into a trust arrangement, pending sale over a period of time approved by the Commission and the Department of Justice, approximately 23.8 percent of the outstanding shares of Sprint PCS Tracking Stock. *See AT&T-TCI* ¶ 107.

national, regional, and local cable programming services; premium movie and pay-per-view services; and sports programming services to homes and businesses nationwide. AT&T generally divides its interests in cable systems into three categories: owned and operated systems (in which AT&T is the 100 percent owner); consolidated systems (in which AT&T has a greater than 50 percent, but less than 100 percent, interest, and which are consolidated for financial reporting purposes); and non-consolidated systems (in which AT&T has a 50 percent or less interest). A detailed list of these interests, along with the approximate number of cable homes passed and subscribers served, is contained in Appendix A.

Through its indirect 100 percent ownership of the outstanding capital stock of Liberty Media Corporation ("LMC") and several other corporations, AT&T also holds an interest in Liberty Media Group ("Liberty"). LMC and its subsidiaries own assets representing substantially all the assets attributed to Liberty. Liberty has an interest in the following video programming providers: Discovery Communications, Inc., USA Networks, Telemundo Network, Telemundo Station Group, BET Holdings II, Inc., Fox Sports World, Fox Sports World Español, Fox Sports South, Fox/Liberty Networks LLC,[26] QVC, Inc., Regional Programming Partners, Canales ñ, Court TV, MacNeil/Lehrer Productions, TV Guide, Inc., E! Entertainment Television, Style, Odyssey, International Channel, Sunshine Network, and Encore Media Group. Further, Liberty owns a series of common stock representing approximately nine percent or less of the common stock (but less than one percent of the voting power) of Time

[26] In a pending transaction, Liberty will divest its interest in Fox/Liberty Networks (which owns interests in various regional sports and fX, a regional cable television network) in exchange for non-voting American Depository Receipts of News Corporation.

Warner Inc., which owns 74.49 percent of Time Warner Entertainment ("TWE").[27] Liberty also owns interests in a number of foreign programming service providers, including Flextech p.l.c. (UK), Jupiter Programming Co., Ltd. (Japan), MultiThematiques, S.A. (France, Italy, Spain, Poland, Germany), Pramer S.C.A. (Argentina), The Premium Movie Partnership (Australia), and Torneos y Competencias, S.A. (Argentina).

AT&T has issued two classes of separate tracking stocks, Liberty Group A and Liberty Group B, that track the performance of Liberty. The Liberty Group tracking stocks are held by separate public shareholders, and no part of the ownership of Liberty is reflected in AT&T common stock. The Liberty tracking stocks are held by shareholders that held TCI-Liberty tracking stock or TCI Ventures tracking stock prior to the merger of AT&T and TCI, and others that have purchased these publicly-traded shares subsequent to that merger. AT&T indirectly owns 100 percent of the outstanding capital stock of LMC, which, in turn, owns substantially all of the assets of Liberty. However, as a matter of AT&T's publicly disclosed Board policy, all dividends and distributions of Liberty must be passed through to the Liberty tracking stock shareholders by AT&T. Moreover, because the value of Liberty's assets are represented by the value of the Liberty tracking shares, any appreciation in the value of Liberty or its assets will be reaped by the Liberty tracking stock shareholders, not by the holders of regular AT&T common stock. Thus, although AT&T as a legal corporate matter "owns" the assets of Liberty, the regular AT&T common shareholders have no "economic interest" – *i.e.*, the

[27] The Commission has held that Liberty's ownership of Time Warner stock is non-attributable for purposes of the cable ownership rules. *See* Memorandum Op. and Order, *Applications of Turner Broadcasting System and Time Warner for Consent to Transfer of Control*, 11 FCC Rcd. 19595, ¶¶ 17-19 (1995).

right to participate in the profits and losses of Liberty as a going concern – in Liberty. Instead, the economic interest is held by the Liberty tracking stock shareholders.[28]

Similarly, the operation of Liberty's programming assets is conducted separately by Liberty's current management. A majority of LMC's board will be individuals who were on the LMC board prior to the AT&T-TCI merger (or will be selected by pre-merger incumbent directors) for seven years following the AT&T-TCI merger. The LMC officers and Board of Directors decide Liberty's course autonomously.[29] Liberty and AT&T can compete with each other in their lines of business and have no obligation to provide financial support, share corporate opportunities, or otherwise assist each other. Liberty has control over its financing capability and other corporate matters, and AT&T may not "unwind" its ownership of Liberty except by a spin-off to the Liberty tracking stock shareholders.[30] In sum, only Liberty's tracking

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[28] Many of the structural safeguards and infrastructure features that establish Liberty's economic independence have been included in the final judgment entered into with the Department of Justice in connection with the merger of AT&T and TCI (and therefore carry the imprimatur of law).

[29] The only exceptions to this rule are (1) in the context of disputes under the Inter-Group Agreement between AT&T and Liberty, which is governed by the contractual terms of the agreement, and (2) those limited matters that require action at the AT&T Board or committee level, such as the issuance of additional Liberty tracking shares. The scope of the Inter-Group Agreement is limited: The overall purpose of the Inter-Group Agreement is to provide that, to the extent possible (given that Liberty is owned, as a legal and tax matter, directly or indirectly by AT&T), the AT&T Common Stock Group and Liberty shall have no obligations or responsibilities to one another to provide financial support, to offer corporate opportunities, or otherwise to assist one another, except as set forth in the Inter-Group Agreement or in a separate "Intercompany Agreement" (which sets forth, among other things, a supply relationship between Liberty and the AT&T Common Stock Group as to programming services).

[30] For example, AT&T cannot increase the authorized number of shares of Liberty Group tracking stock or dispose of the Liberty Group's underlying assets without the consent of the Liberty Group tracking stockholders, and the proceeds of any issuance of Liberty tracking stock generally must be invested in the Liberty Group. LMC also has the unilateral right to authorize and issue new common and preferred stock, within specified limits.

shareholders have an economic interest in Liberty's programming investments and only Liberty's management has the right to direct the operation of those investments.[31]

AT&T, through TCI, also owns a non-controlling 33 percent equity interest in Cablevision Systems Corp. ("Cablevision"). By virtue of its interest in Cablevision, TCI has an indirect interest in Rainbow Media Sports Holdings, Inc. ("Rainbow"). Cablevision owns 75 percent of Rainbow,[32] which owns American Movie Classics, Romance Classics, Bravo, Bravo International, The Independent Film Channel, AMC Music Pop, MuchMusic and News 12 Network. Rainbow also owns 50 percent of National Sports Partners ("Fox Sports Net") and 60 percent of Regional Programming Partners, which owns several regional sports networks. TCI holds only Class A stock in Cablevision, each share of which has only 1/10th of the voting power of the Class B stock. TCI's voting interest in Cablevision is only approximately 8.9 percent. Although AT&T has the right to nominate two Cablevision directors, there are a total of 15 directors on the board, and a majority of the directors are elected by members of the Dolan family, or by trusts in favor of members of the Dolan family. Thus, Cablevison, not AT&T, controls the Rainbow programming services.

AT&T also owns a 50 percent interest in two cable partnerships with Time Warner Cable – Kansas City Cable Partners and Texas Cable Partners, L.P. Each of the partnerships has a management committee with six members, three appointed by Time Warner Cable and three by AT&T. However, Time Warner Cable is the general manager of the cable

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[31] Liberty also owns a 13 percent interest in General Instrument Corp ("GI"). As described above, Liberty is an operationally and economically distinct entity from AT&T. Therefore, AT&T effectively has no economic interest in, or right to direct the operations of, GI.

[32] NBC Cable owns the other 25 percent of Rainbow.

systems, with sole and exclusive responsibility for the day-to-day management and operations of those systems. Time Warner Cable has the right to take any actions it deems necessary or advisable on day-to-day activities, without obtaining the prior approval of the management committee. AT&T does not purchase programming or control programming decisions on behalf of the partnership systems. Rather, Time Warner Cable makes all programming decisions, subject only to compliance with the following specific requirements: it may not unreasonably favor Time Warner-affiliated programming over similar programming affiliated with AT&T; it must obtain AT&T's consent prior to deleting AT&T-affiliated programming; and, because of commitments made prior to the formation of the partnership, the partnership is required to carry American Sports Classics, Home Shopping Network, MSNBC, Romance Classics, The Box, and Web TV on the systems contributed by AT&T as soon as practicable. Thus, although Time Warner Cable may not unilaterally disrupt the carriage of certain existing programming on partnership systems, and although Time Warner Cable must add certain minimal program services to systems contributed by AT&T when practicable, AT&T has no ability to cause the partnerships to refuse to carry any particular programming service.

AT&T - Internet. AT&T began service as an Internet service provider in 1995, and began offering consumer dial-up access in early 1996 through the AT&T WorldNet Service ("AT&T WorldNet"). AT&T WorldNet, which currently has about 1.8 million customers,[33] focuses on providing Internet access to consumers. Although most consumers access WorldNet

[33] With its acquisition of the IBM Global Network ("IGN"), AT&T also obtained less than 300,000 additional non-corporate billed Internet subscribers in the United States. This number includes customers of other Internet access providers that use the IGN network to provide Internet access to their customers. For purposes of this Public Interest statement, AT&T has included all of these IGN-based customers in its WorldNet figures.