

FCC MAIL SECTION

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Before the
Federal Communications Commission
Washington, D.C. 20554

In re Application of)
)
GTE CORPORATION,)
Transferor,)
)
and)
)
BELL ATLANTIC CORPORATION,)
Transferee)
)
For Consent to Transfer Control of Domestic)
and International Sections 214 and 310)
Authorizations and Application to Transfer)
Control of a Submarine Cable Landing License)
)

CC Docket No. 98-184

MEMORANDUM OPINION AND ORDER

Adopted: June 16, 2000

Released: June 16, 2000

By the Commission: Commissioners Ness and Tristani issuing separate statements;
Commissioners Furchtgott-Roth and Powell concurring in part, dissenting in part, and issuing
separate statements.

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I. INTRODUCTION

1. In this Memorandum Opinion and Order, we consider the joint applications of Bell Atlantic Corporation (Bell Atlantic) and GTE Corporation (GTE) (collectively, Applicants)¹ pursuant to sections 214(a) and 310(d) of the Communications Act of 1934, as amended (Communications Act or Act),² for approval to transfer control of licenses and lines from GTE to Bell Atlantic in connection with their proposed merger.³ In order to persuade us to grant their applications, Bell Atlantic and GTE must demonstrate that their proposed transaction will serve the public interest, convenience, and necessity.⁴ As described in more detail below, Bell Atlantic and GTE supplemented their original applications with an additional filing that included proposed merger conditions to which both parties voluntarily committed.⁵ In addition, the Applicants submitted a proposal to transfer the Internet and related assets of GTE Internetworking, Inc., now known as Genuity, Inc. (Genuity), to an independently owned public corporation so that consummation of the merger would not instantly result in a violation of section 271⁶ of the Telecommunications Act of 1996.⁷

2. We first conclude that the Applicants' proposal to spinoff GTE's Internet

¹ Throughout this Order, we refer to Bell Atlantic and GTE as "the Applicants" or "Bell Atlantic and GTE." We refer to the post-merger combined Bell Atlantic/GTE as "the merged entity," "the merged firm," or "the merged company."

² 47 U.S.C. §§ 214(a), 310(d). Our review is also conducted pursuant to the Cable Landing License Act, 47 U.S.C. §§ 34-39 (*Cable Landing License Act*).

³ See Application of GTE Corporation and Bell Atlantic Corporation for Transfer of Control (filed Oct. 2, 1998) (Bell Atlantic/GTE Oct. 2, 1998 Application); Supplemental Filing of Bell Atlantic and GTE (filed Jan. 27, 2000) (Bell Atlantic/GTE Jan. 27, 2000 Supplemental Filing).

⁴ See 47 U.S.C. §§ 214(a), 310(d). See also *Application of Ameritech Corporation and SBC Communications Inc. for Transfer of Control of Corporations Holding Commission Licenses and Lines Pursuant to Section 214 and 310(d) of the Communications Act and Parts 5, 22, 24, 25, 63, 90, 95, and 101 of the Commission's Rules*, CC Docket No. 98-141, Memorandum Opinion and Order, 14 FCC Rcd 14712, 14736-38, paras. 1, 46-48 (1999) (*SBC/Ameritech Order*); *Application of WorldCom, Inc. and MCI Communications Corporation for Transfer of Control of MCI Communications Corporation to WorldCom, Inc.*, CC Docket No. 97-211, Memorandum Opinion and Order, 13 FCC Rcd 18025, 18026-27, 18030-32 at paras. 1, 8-10 (1998) (*WorldCom/MCI Order*); *Applications of NYNEX Corporation Transferor, and Bell Atlantic Corporation Transferee, For Consent to Transfer Control of NYNEX Corporation and Its Subsidiaries*, File No. NSD-L-96-10, Memorandum Opinion and Order, 12 FCC Rcd 19985, 19987, 20000-04 at paras. 2, 29-32 (1997) (*Bell Atlantic/NYNEX Order*).

⁵ See Proposed Conditions for Bell Atlantic/GTE Merger (filed Jan. 27, 2000) (Bell Atlantic/GTE Jan. 27, 2000 Proposed Conditions).

⁶ Section 271 prohibits Bell Operating Companies (BOCs) such as Bell Atlantic from providing interLATA services within their territories until such time as they have demonstrated compliance with section 271. 47 U.S.C. § 271. Section 271 was added to the Communications Act by the Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996 Act), *codified at* 47 U.S.C. §§ 151 *et seq.* All citations to the 1996 Act will be in accordance with its codification in Title 47 of the United States Code.

⁷ See Bell Atlantic/GTE Jan. 27, 2000 Supplemental Filing.

backbone and related assets into a separate public corporation is sufficient to demonstrate that completion of the merger would not result in a violation of section 271. Under the transaction we approve herein and that the Applicants must complete prior to merger closing, the Applicants will retain shares that represent less than 10 percent of the spun-off entity and that contain a conditional conversion right. Applying a three-part test, we conclude that the merged firm will not own an equity interest or the equivalent thereof of more than 10 percent of Genuity. We further find that the merged firm will not control Genuity, nor will it be providing interLATA services through its post-spin-off relationship with Genuity.

3. In addition, we find in this Order that, absent conditions, the merger of Bell Atlantic and GTE will harm consumers of telecommunications services by (a) denying them the benefits of future probable competition between the merging firms; (b) undermining the ability of regulators and competitors to implement the pro-competitive, deregulatory framework for local telecommunications that was adopted by Congress in the 1996 Act; and (c) increasing the merged entity's incentives and ability to discriminate against entrants into the local markets of the merging firms. Moreover, we also find that the asserted public interest benefits of the proposed merger will not outweigh these public interest harms.

4. The Applicants, however, have proposed conditions that will alter the public interest balance. These conditions are designed to mitigate the potential public interest harms of the Applicants' transaction, enhance competition in the local exchange and exchange access markets in which Bell Atlantic or GTE is the incumbent local exchange carrier (incumbent LEC), and strengthen the merged firm's incentives to expand competition outside of its territories. We believe that the voluntary merger conditions proposed by the Applicants and adopted in this Order will not only substantially mitigate the potential public interest harms of the merger, but also provide public interest benefits that extend beyond those resulting from the proposed transaction. Accordingly, we conclude that approval of the applications to transfer control of Commission licenses and lines from GTE to Bell Atlantic serves the public interest, convenience, and necessity and, therefore, satisfies sections 214 and 310(d) of the Communications Act given these significant and enforceable conditions.

II. EXECUTIVE SUMMARY

5. The applications before us concern the proposed merger of one of four remaining Regional Bell Operating Companies (RBOCs) and an incumbent LEC of a size comparable to that of an RBOC.⁸ We conclude that, with the conditions adopted in this Order, the Applicants have demonstrated that the proposed transfer of licenses and lines from GTE to Bell Atlantic will serve the public interest. We also make the following determinations in support of this conclusion:

⁸ Because of its size, the Commission has consistently referred to GTE as a "first-tier" incumbent LEC and thus included it in the small group of carriers, along with the RBOCs, that have substantial market power. *See SBC/SNET Order*, 13 FCC Rcd at 21302, para. 21 (*citing Policy and Rules Concerning Rates for Dominant Carriers*, CC Docket No. 87-313, Second Report and Order, 5 FCC Rcd 6786, 6818-20 (1990)).

- *Compliance with Section 271.* Because GTE will transfer its Internet backbone and related assets to a separate public corporation (Genuity) prior to merger closing, the proposed transaction will not result in a violation of section 271 of the Act. The merged firm will retain shares of Genuity stock that will comprise less than 10 percent of Genuity's voting, dividend and distribution rights. These Class B shares will contain a contingent right that enables the merged firm to convert the shares into additional shares of up to 80 percent of Genuity only if it obtains section 271 authority with respect to 95 percent of Bell Atlantic's in-region access lines within five years of the merger's closing. We conclude that this conditional conversion right is not an equity interest or its equivalent within the meaning of the Act, for the following reasons:
 - 1) The exercise of the conversion right is genuinely in question. The merged firm will be able to exercise its conversion right only if it obtains section 271 authority with respect to 95 percent of Bell Atlantic's in-region access lines within five years. It also must be in a position to operate Genuity's business consistent with section 271 in all Bell Atlantic in-region states prior to actual conversion. If the merged entity seeks to sell its conversion right prior to satisfying this 95-percent threshold, it must first offer to sell those shares to Genuity in exchange for a debt instrument in an amount equal to its initial investment plus a rate of return based on the Standard & Poor's 500 Index or the fair market value of the shares, whichever is less. If Genuity declines, the merged firm will transfer the shares to a liquidating trustee for disposition, and the merged firm would receive limited sales proceeds that would not exceed the value of its initial investment plus a rate of return based on the Standard & Poor's 500 Index.
 - 2) The interest furthers the purposes of section 271 by increasing the merged firm's incentive to achieve section 271 compliance quickly throughout the Bell Atlantic region. This is reinforced by the requirement that the merged firm forgo ratably any appreciation that is attributable to the period of time prior to section 271 authorization in any state.
 - 3) The interest will not increase the likelihood that the merged firm will discriminate against Genuity's rivals because any discriminatory behavior would be readily detectable, either by an independent auditor or through the section 271 approval process, and may result in appropriate enforcement action.
- *Potential Public Interest Harms.* The proposed merger of this RBOC and major incumbent LEC threatens to harm consumers of telecommunications services in three ways.
 - 1) The merger will remove GTE as one of the most significant potential participants in the local telecommunications mass markets within Bell Atlantic's region, thus substantially reducing the prospect of competition in those markets, which Congress has determined will serve the public interest.
 - 2) The merger will reduce the Commission's ability to implement the market-

opening requirements of the 1996 Act through comparative practice oversight (benchmarking) methods. Contrary to the deregulatory, competitive purpose of the 1996 Act, this will increase the duration of the entrenched firms' market power and raise the costs of regulating them and make it more difficult for the Commission to achieve the Act's deregulatory objective.

- 3) The merger will increase the incentive and ability of the merged entity to discriminate against its rivals, particularly with respect to the provision of advanced telecommunications services, a result that is likely to frustrate the Commission's ability to foster advanced services as it is directed to do by the 1996 Act.
- *Potential Public Interest Benefits.* The asserted benefits of the proposed merger do not outweigh the significant harms detailed above.
 - 1) The Applicants have not met their burden of demonstrating that the proposed merger will produce a public interest benefit by promoting competition in the provision of Internet backbone services because (a) the ultimate recombination of GTE's Internet data business with Bell Atlantic's local customers is entirely speculative and (b) the Applicants have not demonstrated that such combination will result in a benefit to the Internet and data services market.
 - 2) The Applicants have failed to demonstrate that the merger is necessary to obtain the benefits to local competition of its out-of-region expansion plan, in which the merged firm will enter twenty-one out-of-region local markets as a competitive LEC.
 - 3) The Applicants have not demonstrated with any specificity that their merger is likely to produce public interest benefits in the long distance market.
 - 4) The proposed merger produces some public interest benefits to the market for wireless communications. The recently completed merger of Bell Atlantic and Vodafone created a carrier with a substantial wireless footprint, and the addition of GTE's wireless markets to this footprint will afford consumers in these markets the option of selecting Bell Atlantic/Vodafone services.
 - 5) A small portion of the Applicants' claimed cost-saving efficiencies, including consolidation efficiencies, implementation of best practices, faster and broader roll-out of new services, and benefits to employees and communities, are merger-specific, likely, and verifiable.
 - *Conditions.* On January 27, 2000, the Applicants supplemented their initial application by submitting a set of voluntary commitments as conditions of approval of their proposed transfer of licenses and lines. Following a period of public comment regarding their proposed conditions, the Applicants revised their commitments on April 14, 2000, April 28, 2000, and May 19, 2000. Assuming the merged firm's satisfactory compliance with their proposals, implementation of the

conditions adopted herein will further the following goals:

- 1) promote advanced services deployment;
- 2) enhance the openness of in-region local telecommunications markets;
- 3) foster out-of-region local competition;
- 4) improve residential phone service; and
- 5) enforce the Merger Order.

These commitments are sufficient to alter the public interest balance such that the application to transfer licenses and lines is, overall, in the public interest and should be approved.

- *Wireless.* Bell Atlantic and GTE are required by the U.S. Department of Justice (DOJ) and as a condition of this Order to divest one of the cellular telephone licenses in ninety-six Metropolitan Statistical Areas and Rural Service Areas where the two companies have wireless licenses that overlap geographically.
- *International.* The public interest will be served by transferring control of GTE's international section 214 authorizations and submarine cable landing licenses (other than those being transferred to Genuity) to Bell Atlantic, subject to the condition that the merged firm's subsidiaries be classified as dominant international carriers in their provision of service on the U.S.-Gibraltar, U.S.-Dominican Republic, and U.S.-Venezuela routes.

III. BACKGROUND

A. The Applicants

6. *GTE Corporation.* GTE is the nation's largest independent incumbent LEC, providing local exchange and exchange access services in twenty-eight states, with service to more than 26 million access lines.⁹ In 1999, GTE's operating revenues exceeded \$25 billion.¹⁰ Not one of the original RBOCs created during the dismantling of the Bell System, GTE was created from the combination of smaller telephone companies.¹¹ After its initial formation in 1918, GTE evolved and grew as a result of a series of acquisitions of telephone companies, including Peninsular Telephone, Hawaiian Telephone, and Northern Ohio Telephone. In 1990,

⁹ Letter from Pat Koch, Bell Atlantic, to Julie Patterson, Federal Communications Commission, filed May 22, 2000 (Bell Atlantic/GTE May 22, 2000 *Ex Parte* Letter).

¹⁰ *Id.*

¹¹ Bell Atlantic/GTE Jan. 27, 2000 Supplemental Filing, Exhibit B, Attach. 3, Joint Declaration of Marion C. Jordan and Jerry Holland at para. 10 (Bell Atlantic/GTE Joint Jordan/Holland Decl.).

GTE merged with Contel Corporation, and in 1999, GTE acquired a 40 percent ownership interest in the Puerto Rico Telephone Company.¹²

7. In addition to providing local exchange and exchange access services, GTE provides wireless, Internet access, and directory publishing services. Not subject to the interLATA restrictions governing BOCs, GTE entered the long distance market in 1997 through a long-term agreement with LDDS WorldCom.¹³ GTE also has significant investments in communications and information services business in Canada, the Dominican Republic, Venezuela, Argentina, Micronesia, and China.¹⁴

8. In 1997, GTE acquired BBN, a company involved in Internet activities, and purchased fiber-optic capacity from Qwest to develop internetworking capabilities. BBN, which evolved into GTE Internetworking and is now known as Genuity, operates a national Internet backbone network and provides a host of Internet-related services including dedicated and dial-up Internet access and Web hosting and security services.¹⁵

9. GTE holds numerous Commission licenses and operates lines used in interstate and international communications, including domestic and international lines authorized under section 214, and various Title III licenses necessary to operate cellular, paging, PCS, experimental radio, business radio, mobile radio, and microwave services, as well as earth station authorizations.¹⁶

10. *Bell Atlantic.* Bell Atlantic, one of the original seven regional Bell Operating Companies formed as part of the divestiture of AT&T's local operations, is the primary incumbent LEC in thirteen states in the mid-Atlantic and northeastern United States, in addition to the District of Columbia.¹⁷ Through its operating companies, Bell Atlantic services more than 43 million local exchange access lines and had 1999 operating revenues in excess of \$33 billion.¹⁸ In 1997, Bell Atlantic acquired NYNEX Corporation, which had been the incumbent provider of local exchange and exchange access services in the states of the northeastern United

¹² GTE 1999 Annual Report at 2.

¹³ Bell Atlantic/GTE Joint Jordan/Holland Decl. at para. 10.

¹⁴ Bell Atlantic Oct. 2, 1998 Application at 3. GTE is also engaged in ventures unrelated to the communications industry, including financing, insurance, leasing, and other related activities. *Id.*

¹⁵ Bell Atlantic/GTE Oct. 2, 1998 Application, Exhibit A, Declaration of John T. Curran at para. 1 (Bell Atlantic/GTE Curran Decl.).

¹⁶ *Id.*

¹⁷ Bell Atlantic's region includes Maine, New Hampshire, Vermont, Massachusetts, Rhode Island, New York, New Jersey, Pennsylvania, Delaware, Maryland, West Virginia, Virginia, parts of Connecticut, and the District of Columbia. *See* Bell Atlantic/GTE Oct. 2, 1998 Application, Exhibit A, Tab 1.

¹⁸ *See* Bell Atlantic 1999 Annual Report at 6.

States, extending its in-region incumbent LEC activities substantially.¹⁹

11. In addition to local exchange and exchange access services, Bell Atlantic's operating companies provide a wide range of other services, including cellular, personal communications services (PCS), paging, Internet access, and directory publishing services.²⁰ Bell Atlantic's wireless operations include service provided throughout the United States as well as investments in Latin America, Europe, and the Pacific Rim.²¹ In 1999, Bell Atlantic's wireless companies provided service to more than 27 million subscribers.²² Bell Atlantic also has many overseas investments, including direct or indirect financial interests in communications and information services businesses in New Zealand, Mexico, Italy, Indonesia, Thailand, Gibraltar, the Philippines, the United Kingdom, Greece, Slovakia, and the Czech Republic.²³

12. On March 30, 2000, the Wireless Telecommunications and International Bureaus, acting upon delegated authority, granted approval of Bell Atlantic and Vodafone AirTouch, PLC (Vodafone), a U.K. corporation, to transfer control of their U.S. wireless licenses and authorizations to Cellco Partnership (Cellco).²⁴ In doing so, the Bureaus concluded that the transaction would not present competitive concerns, but rather, would likely result in a number of public interest benefits. Cellco is the vehicle through which Bell Atlantic and Vodafone formed a domestic, nationwide wireless business that combines their cellular, PCS, paging, and other wireless properties in the United States.²⁵

B. The Merger Transaction

13. *Proposed Transaction.* On July 28, 1998, Bell Atlantic and GTE announced their Agreement and Plan of Merger (Merger Agreement), under which a wholly-owned subsidiary of Bell Atlantic would merge with GTE, and GTE would be the surviving corporation and would itself become a wholly-owned subsidiary of Bell Atlantic.²⁶ GTE would therefore survive as a wholly-owned subsidiary of Bell Atlantic, and the GTE subsidiaries holding section 214 authorizations, submarine cable landing licenses, or radio licenses would survive as wholly-

¹⁹ See generally *Bell Atlantic/NYNEX Order*, 12 RCC Rcd 19985.

²⁰ Bell Atlantic 1999 Annual Report at 6.

²¹ *Id.*

²² *Id.*

²³ Bell Atlantic/GTE Oct. 2, 1998 Application at 4. Bell Atlantic is also engaged in financing, systems integration services, customer premises equipment distribution, and telecommunications consulting. *Id.*

²⁴ See *Vodafone AirTouch, Plc and Bell Atlantic Corporation*, File Nos. 0000032969 et al., Memorandum Opinion and Order, DA 00-721 (WTB/IB rel. Mar. 30, 2000) (*Vodafone/Bell Atlantic Order*); *FCC Bureaus Approve Bell Atlantic/Vodafone and VoiceStream/Aerial License Transfers and Assignments—Two New National Wireless Competitors to be Created*, Press Release (rel. Mar. 30, 2000).

²⁵ *Id.*

²⁶ Bell Atlantic/GTE Oct. 2, 1998 Application at 2.

owned subsidiaries of GTE.²⁷ Following the merger, approximately 57 percent of the shares of Bell Atlantic would be held by the current shareholders, and approximately 43 percent of the shares of Bell Atlantic would be held by the shareholders of GTE. The board of directors of the merged firm would be comprised of an equal number of members from Bell Atlantic's board and GTE's board.²⁸

14. Together, Bell Atlantic and GTE would serve more than 69 million local access lines, representing more than one third of the nation's total access lines.²⁹ As determined from the December 1999 statistics of both companies, the merged entity would have annual revenues in excess of \$58 billion.³⁰ Accordingly, as measured by revenues, a combined Bell Atlantic and GTE would be the second largest telecommunications company in the country behind only AT&T. Based on the extensive breadth of the companies' operations, the proposed merger between Bell Atlantic and GTE requires the review of several government agencies, including the DOJ, state public utility commissions, and this Commission.

C. The Merger Review Process

1. Department of Justice Review

15. The DOJ reviewed the proposed transaction as part of the pre-merger review process under the Hart-Scott-Rodino Antitrust Improvements Act of 1976.³¹ On May 7, 1999, the DOJ filed a civil antitrust complaint alleging that the proposed transaction would violate section 7 of the Clayton Act by lessening competition in the markets for wireless mobile telephone services in ten major trading areas (MTAs), constituting sixty-five metropolitan statistical areas (MSAs) and rural statistical areas (RSAs) in nine states.³² A proposed final judgment was also filed, requiring either Bell Atlantic or GTE to divest its wireless telephone business in the markets where the two companies' businesses overlap.³³ After Bell Atlantic entered into a partnership with Vodafone to form a national wireless business, the DOJ amended the complaint and proposed final judgment to address the additional cellular overlap areas resulting from Bell Atlantic's affiliation with Vodafone.³⁴ The DOJ concluded that the combined

²⁷ *Id.* at 3.

²⁸ *Id.*

²⁹ *See Trends in Telephone Service*, Federal Communications Commission (March 2000) at 20-3, Table 20.21; *see supra* paras. 6, 10.

³⁰ Bell Atlantic 1999 Annual Report at 6; GTE 1999 Annual Report at 2.

³¹ *See United States of America v. Bell Atlantic Corp.*, 99CV-01119, Motion for Entry of Final Judgment (Apr. 20, 2000).

³² *United States of America v. Bell Atlantic Corp.*, 99CV-01119, Motion for Leave to File Supplemental Complaint (Dec. 6, 1999).

³³ *Id.*

³⁴ *Id.*

effect of the Bell Atlantic/GTE and Bell Atlantic/Vodafone transactions would be to lessen competition in the markets for wireless services in thirteen MTAs and ninety-six MSAs and RSAs in fifteen states.³⁵ On April 20, 2000, the parties submitted to the court a proposed final judgment that requires Bell Atlantic, GTE, or Vodafone to divest wireless assets in ninety-six cellular overlap markets.³⁶

2. State Review

16. The proposed merger of Bell Atlantic and GTE also has required the review of or notification to a number of state governing bodies. Twenty-seven states conducted proceedings examining the proposed transaction, each approving it and many imposing conditions.³⁷ Twenty-three additional states declined jurisdiction over the transaction.³⁸ On March 2, 2000, the California Public Utilities Commission granted the Applicants the final necessary state approval for the proposed merger.³⁹

3. Commission Review

17. Bell Atlantic and GTE filed their initial applications for transfer of control on October 2, 1998, requesting Commission approval of the transfer of control to Bell Atlantic of licenses and lines owned or controlled by GTE or its affiliates or subsidiaries.⁴⁰ More than fifty parties have filed timely comments or petitions to deny the application.⁴¹ In addition, the Commission held a series of three public forums at which a number of parties expressed their views on the proposed merger, including the Applicants, states, economists, and consumer groups, community organizations, and industry participants.⁴²

18. On February 24, 1999, in response to concerns raised by Commission staff, Bell Atlantic and GTE filed a *Report on Long Distance Issues in Connection with their Merger and*

³⁵ *United States of America v. Bell Atlantic Corp.*, 99CV-01119, Motion for Entry of Final Judgment (Apr. 20, 2000).

³⁶ *Id.*

³⁷ "Bell Atlantic-GTE Clear Last State Merger Hurdle with Cal.," Washington Telecom Newswire (Mar. 2, 2000).

³⁸ *Id.*

³⁹ *See id.*

⁴⁰ *GTE Corporation and Bell Atlantic Corporation Seek FCC Consent for a Proposed Transfer of Control and Commission Seeks Comment on Proposed Protective Order filed by GTE and Bell Atlantic*, CC Docket No. 98-184, Public Notice, DA 98-2035 (rel. Oct. 8, 1998) (Oct. 8, 1998 Public Notice).

⁴¹ The parties that filed formal pleadings in this proceeding are listed in Appendix A.

⁴² *See* "Commission to Hold En Bancs Regarding Telecom Mergers," Public Notice, DA 98-2045 (Oct. 9, 1998); "Commission to Hold En Bancs Regarding Telecom Mergers," Public Notice, DA 98-2415 (rel. Dec. 2, 1998) (Dec. 2, 1998 Public Notice); "Chief Economist Names Participants on Economic Round Table Regarding Telecom Mergers," Public Notice, DA 99-119 (rel. Jan. 25, 1999) (Jan. 25, 1999 Public Notice).

Request for Limited Interim Relief. With respect to long distance voice services, Applicants requested that the Commission grant a reasonable transition period to permit GTE to transfer to other interexchange carriers its existing customers within Bell Atlantic's region.⁴³ Applicants also requested that the Commission grant interim relief to enable the merged firm to continue providing interLATA data services through GTE's Internet backbone provider, GTE Internetworking, while the merged company pursued section 271 authority for Bell Atlantic's in-region states.⁴⁴ The Applicants subsequently asked that the Commission hold its Request for Interim Relief in abeyance pending later filings addressing the long distance issues.⁴⁵ On April 14, 1999, Applicants requested that the Commission suspend processing of their merger application pending a further submission following Bell Atlantic's filing with the Commission of its application for section 271 relief in New York.⁴⁶

19. Bell Atlantic and GTE renewed and supplemented their initial application by submitting a January 27, 2000 Supplemental Filing, which included their Internet backbone spin-off proposal and a set of proposed merger conditions to which they voluntarily committed.⁴⁷ Bell Atlantic and GTE subsequently clarified the Internet backbone proposal and their proposed merger conditions through subsequent filings made on April 3, 2000,⁴⁸ April 14, 2000,⁴⁹ April 28, 2000,⁵⁰ May 19, 2000,⁵¹ June 7, 2000,⁵² and June 14, 2000.⁵³ On April 28, 2000, the Commission

⁴³ See Letter from Jennifer L. Hoh, Legal Department, Bell Atlantic, to Magalie Roman Salas, Secretary, Federal Communications Commission, CC Docket No. 98-184 (Feb. 24, 1999) (Bell Atlantic/GTE Feb. 24, 1999 *Ex Parte* Letter).

⁴⁴ *Id.*

⁴⁵ See Letter from Steven G. Bradbury, Counsel, GTE, and Michael E. Glover, Counsel, Bell Atlantic, to Thomas Krattenmaker, Federal Communications Commission, CC Docket 98-184 (filed Apr. 8, 1999) (Bell Atlantic/GTE Apr. 8, 1999 *Ex Parte* Letter).

⁴⁶ See Letter from Steven G. Bradbury, Counsel for GTE, and Edward D. Young, III, Counsel for Bell Atlantic, to Katherine Brown, Federal Communications Commission, CC Docket No. 98-184 (filed Apr. 14, 1999) (Bell Atlantic/GTE Apr. 14, 1999 *Ex Parte* Letter).

⁴⁷ See Bell Atlantic/GTE Jan. 27, 2000 Supplemental Filing; Bell Atlantic/GTE Jan. 27, 2000 Proposed Conditions. See also *Commission Seeks Comments on Supplemental Filing Submitted by Bell Atlantic Corporation and GTE Corporation*, CC Docket No. 98-184, Public Notice (rel. Jan. 31, 2000) (Jan. 31, 2000 Public Notice). The parties filing comments and reply comments are listed in Appendix A.

⁴⁸ See Letter from Steven G. Bradbury, Counsel to GTE, to Magalie Roman Salas, Secretary, Federal Communications Commission, CC Docket No. 98-184 (filed Apr. 3, 2000) (Bell Atlantic/GTE Apr. 3, 2000 *Ex Parte* Letter).

⁴⁹ See Letter from Michael E. Glover, Associate General Counsel, Bell Atlantic, to Magalie Roman Salas, Secretary, Federal Communications Commission, CC Docket No. 98-184 (filed Apr. 14, 2000) (Bell Atlantic/GTE Apr. 14, 2000 *Ex Parte* Letter).

⁵⁰ Letter from William P. Barr, Executive Vice President and General Counsel, GTE, to Magalie Roman Salas, Secretary, Federal Communications Commission, CC Docket No. 98-184 (filed Apr. 28, 2000) (Bell Atlantic/GTE Apr. 28, 2000 *Ex Parte* Letter).

sought further comment on the altered spin-off proposal and modified merger conditions.⁵⁴

IV. PUBLIC INTEREST FRAMEWORK

20. Before approving the transfer of control of licenses and lines in connection with the proposed merger, the Commission must determine, pursuant to sections 214(a) and 310(d) of the Communications Act, that the proposed transfers serve the public interest.⁵⁵ In accordance with the Act's public interest standard, we must weigh any potential public interest harms of the proposed transaction against the potential public interest benefits to ensure that, on balance, the merger services the public interest, convenience, and necessity.⁵⁶ In doing so, we examine, *inter alia*, possible competitive effects of the proposed transfers and measure the effect of the merger on both the broader aims of the Communications Act and federal communications policy.⁵⁷

21. Section 214(a) of the Communications Act generally requires carriers to obtain from the Commission a certificate of public convenience and necessity before constructing, acquiring, operating or engaging in transmission over lines of communication, or before discontinuing, reducing or impairing service to a community.⁵⁸ In this case, section 214(a) requires the Commission to find that the "present or future public convenience and necessity require or will require" Bell Atlantic to operate the acquired telecommunications lines and that "neither the present nor future public convenience and necessity will be adversely affected" by

(Continued from previous page)

⁵¹ Letter from Pat Koch, Bell Atlantic, to Magalie Roman Salas, Secretary, Federal Communications Commission, CC Docket No. 98-184 (filed May 19, 2000) (Bell Atlantic/GTE May 19, 2000 *Ex Parte* Letter).

⁵² Letter from Michael E. Glover, Associate General Counsel, Bell Atlantic, to Magalie Roman Salas, Secretary, Federal Communications Commission, CC Docket No. 98-184 (filed June 7, 2000) (Bell Atlantic/GTE Glover June 7, 2000 *Ex Parte* Letter); Letter from Suzanne Yelen, Counsel for GTE, to Magalie Roman Salas, Secretary, Federal Communications Commission, CC Docket No. 98-184 (filed June 7, 2000) (Bell Atlantic/GTE Yelen June 7, 2000 *Ex Parte* Letter).

⁵³ Letter from Michael E. Glover, Associate General Counsel, Bell Atlantic, to Magalie Roman Salas, Secretary, Federal Communications Commission, CC Docket No. 98-184 (filed June 14, 2000) (Bell Atlantic/GTE Glover June 14, 2000 *Ex Parte* Letter).

⁵⁴ *Commission Seeks Comment on Additional Filings Submitted by Bell Atlantic Corporation and GTE Corporation*, Public Notice, CC Docket No. 98-184, DA 00-959 (rel. Apr. 28, 2000) (Apr. 28, 2000 Public Notice).

⁵⁵ 47 U.S.C. §§ 214(a), 303(r), 310(d). See *WorldCom/MCI Order*, 13 FCC Rcd at 18030, para. 8; *Bell Atlantic/NYNEX Order*, 12 FCC Rcd at 20000, para. 29.

⁵⁶ See *WorldCom/MCI Order*, 13 FCC Rcd at 18031-32, para. 10.

⁵⁷ See *Qwest Communications International Inc. and US WEST, Inc., Applications for Transfer of Control of Domestic and International Sections 214 and 310 Authorizations and Application to Transfer Control of a Submarine Cable Landing License*, CC Docket No. 99-272, FCC 00-91, para. 9 (rel. Mar. 10, 2000) (*Qwest/US WEST Order*).

⁵⁸ 47 U.S.C. § 214(a).

the discontinuance of service from GTE.⁵⁹ Section 310(d) provides that no construction permit or station license may be transferred, assigned, or disposed of in any manner except upon a finding by the Commission that the "public interest, convenience, and necessity will be served thereby."⁶⁰ Accordingly, the Commission must determine that the proposed transfer of licenses from GTE to Bell Atlantic "serves the public interest, convenience, and necessity" before it can approve the transaction.⁶¹

22. The public interest standard under sections 214(a) and 310(d) involves a balancing process that weighs the potential public interest harms of the proposed transaction against its potential public interest benefits.⁶² The Applicants bear the burden of proving by a preponderance of the evidence that, on balance, the proposed transaction serves the public interest.⁶³ In applying this public interest test, the Commission considers four questions: (1) whether the transaction would result in a violation of the Communications Act; (2) whether the transaction would result in a violation of the Commission's rules; (3) whether the transaction would substantially frustrate the Commission's ability to implement or enforce the Communications Act; and (4) whether the merger promises to yield affirmative public interest benefits that could not be achieved without the merger.⁶⁴

23. Our analysis of public interest benefits and harms under parts three and four of the public interest test includes, but is not limited to, an analysis of the potential competitive effects

⁵⁹ 47 U.S.C. § 214(a). See *Implementation of Section 402(b)(2)(A) of the Telecommunications Act of 1996; Petition for Forbearance of the Independent Telephone and Telecommunications Alliance*, CC Docket No. 97-11; AAD File No. 98-43, Report and Order in CC Docket No. 97-11 and Second Memorandum Opinion and Order in AAD File No. 98-43, FCC 99-104 (rel. June 30, 1999) (continuing to require Commission approval for transfers of control, even though blanket section 214 entry certification and streamlined section 214 exit certification have been granted for domestic carriers).

⁶⁰ 47 U.S.C. § 310(d).

⁶¹ *Id.*

⁶² See *Bell Atlantic/NYNEX Order*, 12 FCC Rcd at 20063, para. 157.

⁶³ *Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations from Telecommunications, Inc., Transferor, to AT&T Corp., Transferee*, CS Docket No. 98-178, Memorandum Opinion and Order, 14 FCC Rcd at 3160, 3169-70, para. 15 (1999) (*AT&T/TCI Order*). See also *WorldCom/MCI Order*, 13 FCC Rcd at 18031, para. 10 n.33 (citing 47 U.S.C. § 309(e) (burdens of proceeding and proof rest with the applicant)); *American Telephone and Telegraph Co. and MCI Communications Corporation Petitions for the Waiver of the International Settlements Policy*, File No. USP-89-(N)-086, Memorandum Opinion and Order, 5 FCC Rcd 4618, 4621, para. 19 (1990) (applicant seeking a waiver of an existing rate bears the burden of proof to establish that the public interest would be better served by the grant rather than the denial of the waiver request); *LeFlore Broadcasting Co., Inc.*, Docket No. 20026, Initial Decision, 66 FCC 2d 734, 736-37, paras. 2-3 (1975) (on the ultimate issue of whether the applicants have the requisite qualifications and whether a grant of the application would serve the public interest, as on all issues, the burden of proof is on the licensees).

⁶⁴ See *SBC/Ameritech Order*, 14 FCC Rcd at 14737, para. 48.

of the transaction, as informed by traditional antitrust principles.⁶⁵ Although an antitrust analysis focuses solely on whether the effect of a proposed merger “may be substantially to lessen competition,”⁶⁶ the Communications Act requires the Commission to apply a different standard. The Commission must make an independent public interest determination that includes an evaluation of the merger's likely effect on future competition.⁶⁷ Because Congress has determined that additional competition in telecommunications markets will better serve the public interest, in order to conclude that a merger is in the public interest, the Commission must “be convinced that it will enhance competition, not merely lessen it.”⁶⁸

24. Where necessary, the Commission can attach conditions to a transfer of lines and licenses to ensure that the public interest is served by the transaction.⁶⁹ Section 214(c) of the Act authorizes the Commission to attach to the certificate “such terms and conditions as in its judgment the public convenience and necessity may require.”⁷⁰ Similarly, section 303(r) of the Communications Act authorizes the Commission to prescribe restrictions or conditions, not

⁶⁵ Although the Commission's analysis of competitive effects is informed by antitrust principles and judicial standards of evidence, it is not governed by them, which permits the Commission to arrive at a different assessment of likely competitive benefits or harms than antitrust agencies adduce based on antitrust law. *See FCC v. RCA Communications*, 346 U.S. 86, 96-97 (1953) (“To restrict the Commission's action to cases in which tangible evidence appropriate for judicial determination is available would disregard a major reason for the creation of administrative agencies, better equipped as they are for weighing intangibles by specialization, by insight gained through experience, and by more flexible procedure.”). *See also SBC/Ameritech Order*, 14 FCC Rcd at 14738, para. 49, n.121; *WorldCom/MCI Order*, 13 FCC Rcd at 18034, para. 13 (citing *RCA Communications*, 346 U.S. at 94; *United States v. FCC*, 652 F.2d 72, 81-82 (D.C. Cir. 1980) (*en banc*) (The Commission's “determination about the proper role of competitive forces in an industry must therefore be based, not exclusively on the letter of the antitrust laws, but also on the ‘special considerations’ of the particular industry.”); *Teleprompter-Group W*, 87 FCC 2d 531 (1981), *aff'd on recon.*, 89 FCC 2d 417 (1982) (Commission independently reviewed the competitive effects of a proposed merger); *Equipment Distributors' Coalition, Inc. v. FCC*, 824 F.2d 1197, 1201 (D.C. Cir. 1987); *Northeast Utilities Service Co. v. FERC*, 993 F.2d 937, 947-48 (1st Cir. 1993) (public interest standard does not require agencies “to analyze proposed mergers under the same standards that the Department of Justice . . . must apply.”).

⁶⁶ *See* 15 U.S.C. § 18.

⁶⁷ *See SBC/Ameritech Order*, 14 FCC Rcd at 14738, para. 49; *WorldCom/MCI Order*, 13 FCC Rcd at 18032-33, para. 12; *Bell Atlantic/NYNEX Order*, 12 FCC Rcd at 19987, para. 2.

⁶⁸ *Bell Atlantic/NYNEX Order*, 12 FCC Rcd at 19987, para. 2.

⁶⁹ *See* 47 C.F.R. § 1.110. *See also WorldCom/MCI Order*, 13 FCC Rcd at 18031-32, para. 10; *Bell Atlantic/NYNEX Order*, 12 FCC Rcd at 20001-2, para. 30.

⁷⁰ 47 U.S.C. § 214(c). *See WorldCom/MCI Order*, 13 FCC Rcd at 18032, para. 10 n.35 (citing *MCI Communications Corp.*, File No. I-S-P-93-013, Declaratory Ruling and Order, 9 FCC Rcd 3960, 3968, para. 39 (1994); *Sprint Corp.*, File No. I-S-P-95-002, Declaratory Ruling and Order, 11 FCC Rcd 1850, 1867-72, paras. 100-33 (1996); *GTE Corp.*, File No. W-P-C-2486, Memorandum Opinion and Order, 72 FCC 2d 111, 135, para. 76 (1979)); *Bell Atlantic/NYNEX Order*, 12 FCC Rcd at 20002, para. 30 n.59 (citing *Atlantic Tele-Network, Inc. v. FCC*, 59 F.3d 1384, 1389-90 (D.C. Cir. 1995); *GTE Service Corp. v. FCC*, 782 F.2d 263, 268 (D.C. Cir. 1986); *Western Union Tel. Co. v. FCC*, 541 F.2d 346, 355 (3rd Cir. 1976), *cert. denied*, 429 U.S. 1092 (1977)).

inconsistent with law, that may be necessary to carry out the provisions of the Act.⁷¹ Indeed, unlike the role of antitrust enforcement agencies, the Commission's public interest authority enables it to rely upon its extensive regulatory and enforcement experience to impose and enforce conditions to ensure that the merger will yield overall public interest benefits.⁷²

25. Finally, as noted in the *SBC/Ameritech* and *AT&T-TCI Orders*, many transfer applications on their face demonstrate that the merger would yield affirmative public interest benefit and would neither violate the Communications Act or Commission rules nor frustrate the policies and enforcement of the Communications Act.⁷³ Such cases do not require extensive review by the Commission and interested parties. Because that is not the case with respect to this proposed transaction, we analyze the potential public interest harms and benefits of this proposed merger, absent conditions, in the following sections.

V. COMPLIANCE WITH SECTION 271

26. As an initial matter, we first consider whether the Applicants' proposed transaction would result in a violation of the Communications Act. Section 271 of the Act prohibits a Bell operating company or its affiliate from entering the in-region, interLATA market unless and until the BOC demonstrates that its local market is open to competition by satisfying a checklist of market-opening and other requirements set forth in the statute.⁷⁴ Bell Atlantic is comprised of several Bell operating companies,⁷⁵ and, to date, has obtained section 271 authorization only in New York.⁷⁶ GTE is not comprised of any BOCs and thus, prior to the

⁷¹ 47 U.S.C. § 303(r). See, e.g., *WorldCom/MCI Order*, 13 FCC Rcd at 18032, para. 10 n.36 (citing *FCC v. Nat'l Citizens Comm. for Broadcasting*, 436 U.S. 775 (1978) (*Nat'l Citizens*) (broadcast-newspaper cross-ownership rules properly adopted pursuant to section 303(r)); *U.S. v. Southwestern Cable Co.*, 392 U.S. 157, 178 (1968) (section 303(r) powers permit Commission to order cable company not to carry broadcast signal beyond station's primary market); *United Video, Inc. v. FCC*, 890 F.2d 1173, 1182-83 (D.C. Cir. 1989) (syndicated exclusivity rules adopted pursuant to section 303(r) powers).

⁷² See *WorldCom/MCI Order*, 13 FCC Rcd at 18034-35, para. 14. In addition to its public interest authority under the Communications Act, the Commission shares concurrent antitrust jurisdiction with DOJ under the Clayton Act to review mergers between common carriers. 15 U.S.C. §§ 18, 21(a). In this case, because our public interest authority under the Communications Act is sufficient to address both the competitive issues raised by the proposed merger and its likely effect on the public interest, we decline to exercise our Clayton Act authority for the proposed transaction. See *SBC/Ameritech Order*, 14 FCC Rcd at 14740, para. 53; *WorldCom/MCI Order*, 13 FCC Rcd at 18032, para. 12; *Bell Atlantic/NYNEX Order*, 12 FCC Rcd at 20005, para. 33. See also *United States v. FCC*, 652 F.2d 72, 88 (D.C. Cir. 1980) (en banc).

⁷³ See *AT&T/TCI Order*, 14 FCC Rcd at 3170, para. 16.

⁷⁴ See 47 U.S.C. § 271(a). See also 47 U.S.C. § 271(c) (setting forth the requirements for a BOC to seek authority to provide in-region, interLATA services).

⁷⁵ See 47 U.S.C. § 153(4) (defining "Bell operating company").

⁷⁶ See *Application by Bell Atlantic New York for Authorization under Section 271 of the Communications Act to Provide In-Region, InterLATA Service in the State of New York*, CC Docket No. 99-295, Memorandum Opinion and Order, 15 FCC Rcd 3953 (1999).

contemplated license transfer application, was not subject to section 271's restrictions. At the time of the Application, GTE in fact provided interLATA services nationwide through various subsidiaries.

27. In anticipation of its merger with Bell Atlantic, GTE agreed to exit various interLATA businesses, including resold voice long distance service, in the section 271-restricted Bell Atlantic states before closing the merger.⁷⁷ GTE Communications Corporation, for example, terminated its direct dialing, dial around, 800 toll free, operator, private line and frame relay data services, and agreed to deactivate all calling cards of customers in the affected states and cease origination of calling card calls in that region.⁷⁸ In addition, GTE transferred to unaffiliated carriers the dedicated capacity services provided by GTE Data Services Incorporated, GTE Telecommunication Services, Inc. and GTE Network Services, and interLATA transmission services provided by GTE.net that originated in Bell Atlantic states other than New York. GTE also agreed to divest the retail private line resale business of GTE Telecom Inc. (GTE Telecom) prior to merger close.⁷⁹ With respect to GTE Telecom's private line wholesale services, GTE is seeking Commission approval to transfer corporate control of GTE Telecom to Genuity.

28. Genuity (formerly GTE Internetworking), a wholly-owned subsidiary of GTE, is a facilities-based Internet infrastructure supplier offering a comprehensive set of managed Internet access, web hosting and value-added e-business services, such as virtual private networks for secure data transmission and security services.⁸⁰ It operates a global network consisting of domestic broadband fiber optic cable, points of presence where Internet access is provided to end users and secure data centers. With its extensive network and customer base, Genuity is commonly regarded as a Tier I Internet backbone provider.

⁷⁷ See Letter from Alan F. Ciampornero, Vice President Regulatory Affairs, GTE, to Magalie Roman Salas, Secretary, FCC, CC Docket No. 98-184 (filed Apr. 17, 2000) (describing the interLATA services provided by various GTE subsidiaries that the companies will cease providing before merger close), attached hereto as Appendix E.

⁷⁸ In February 2000, GTE notified its residential voice long distance customers in Bell Atlantic's section 271-restricted states that they could select another long distance provider, and, in late March, started transferring the customers. See Bell Atlantic/GTE Feb. 22, 2000 Reply at 3 n.2. See also *Implementation of the Subscriber Carrier Selection Changes Provisions of the Telecommunications Act of 1996, Sprint Communications Company, L.P., Petition for Waiver*, CC Docket No. 94-129, Order, DA 00-620 (rel. Mar. 17, 2000); *Implementation of the Subscriber Carrier Selection Changes Provisions of the Telecommunications Act of 1996, GTE Service Corp., Petition for Waiver*, CC Docket No. 94-129, Order, DA 00-1113 (rel. May 19, 2000).

⁷⁹ See Letter from Alan F. Ciampornero, Vice President Regulatory Affairs, GTE, to Magalie Roman Salas, Secretary, FCC, CC Docket No. 98-184 (filed Apr. 28, 2000), attached hereto as Appendix F.

⁸⁰ See Letter from Steven G. Bradbury, Kirkland & Ellis, Counsel for GTE, to Magalie Roman Salas, Secretary, FCC, CC Docket No. 98-184 (filed Mar. 9, 2000) (Bell Atlantic/GTE Mar. 9, 2000 *Ex Parte* Letter) at 2; Letter from Patricia E. Koch, Assistant Vice President Federal Regulatory, Bell Atlantic, to Magalie Roman Salas, Secretary, FCC, CC Docket No. 98-184 (filed June 9, 2000) (Form S-1 Registration Statement, Amendment No. 3), at 1-2 (describing services provided by Genuity).

A. Applicants' Spin-off Proposal

29. Under the Applicants' spin-off proposal,⁸¹ GTE will transfer substantially all⁸² of Genuity's nationwide data business to a separate public corporation. Before merging with Bell Atlantic, GTE will exchange its stockholdings in Genuity for shares of a new class of common stock, Class B common stock. Through an initial public offering (IPO) conducted prior to closing the merger with Bell Atlantic, public shareholders will purchase shares of Genuity Class A common stock initially carrying 90.5 percent of the voting rights and the right to receive 90.5 percent of any dividends or other distributions.⁸³ The merged Bell Atlantic/GTE's Class B shares will carry 9.5 percent of the voting rights and the right to receive 9.5 percent of any dividends or other distributions, along with a conversion right and certain investor safeguards.⁸⁴ Subject to satisfying certain conditions, the Class B shares will be convertible into newly-issued shares representing 80 percent of the shares of Genuity outstanding immediately after the IPO.

30. *Conditions to Sale or Exercise of Conversion Rights.* The potential for the holder of the Class B shares to convert those shares into a greater economic interest is subject to a number of restrictions described below.

- *50-Percent Threshold.* Unless and until the merged Bell Atlantic/GTE eliminates section 271 restrictions as to at least 50 percent of total Bell Atlantic in-region lines, the Class B holder will only have the right to convert the shares into Class A stock representing a 10-percent interest in Genuity.⁸⁵ If the merged firm fails to meet this 50-percent threshold within five years from the closing of the merger, the Class B shares will never be convertible into more than a 10-percent interest, and the public shareholders' ownership of at least 90 percent of the company will not be diluted. Thus, if the merged entity were to sell all or a portion of the

⁸¹ See Appendix B (Conditions for Establishment of Genuity as a Separate Corporation; hereinafter Genuity Conditions). The Applicants submitted their spin-off proposal on January 27, 2000 and modified various aspects in *ex parte* submissions to the Commission on April 3, 2000, April 28, 2000, June 7, 2000, and June 14, 2000. See Bell Atlantic/GTE Jan. 27, 2000 Supplemental Filing; Bell Atlantic/GTE Apr. 3, 2000 *Ex Parte* Letter; Bell Atlantic/GTE Apr. 28, 2000 *Ex Parte* Letter; Bell Atlantic/GTE June 7, 2000 Glover *Ex Parte* Letter; Bell Atlantic/GTE June 14, 2000 *Ex Parte* Letter.

⁸² The assets transferred to Genuity would include all of GTE's Internet backbone and related data business, including the nationwide Global Network Infrastructure (GNI), the BBN Planet backbone and related backbone operations, GTE Internetworking's Internet connectivity services for business customers and national modem and frame relay networks, its Web hosting and Internet security services, and various other interLATA data transport services and operations. GTE's dial-up ISP service (GTE.net) and the research and development operations of BBN Technologies would remain in the merged Bell Atlantic/GTE and not be transferred to Genuity. Bell Atlantic/GTE Feb. 22, 2000 Reply at 3 n.2. The Applicants maintain that BBN Technologies performs research, development and consulting services, primarily for government and commercial customers, and that it was not a part of GTE Internetworking's reported financial results from 1999. Bell Atlantic/GTE Mar. 9, 2000 *Ex Parte* Letter at 2-3.

⁸³ Bell Atlantic/GTE June 7, 2000 Glover *Ex Parte* Ex. A at 1.

⁸⁴ *Id.*

⁸⁵ *Id.* "Bell Atlantic in-region lines" refers to the sum of the number of total billable access lines reported in 1999 ARMIS Report 43-04 for the Bell Atlantic operating company in each of Bell Atlantic's in-region states. *Id.* at n.1.

Class B shares before meeting the 50-percent threshold, the shares would be convertible into only 10 percent, or the proportionate lesser amount, of Genuity's then-outstanding shares. Similarly, if Bell Atlantic/GTE were to attempt to convert the Class B shares before satisfying the 50-percent threshold, the shares would be convertible only into Class A common stock representing 10 percent of the then-outstanding shares of Genuity.

- *95-Percent Threshold for Bell Atlantic/GTE Conversion.* If the merged firm satisfies the 50-percent threshold, the ability of Bell Atlantic/GTE itself to convert remains subject to a further restriction. The merged firm can exercise the right to convert the Class B shares into shares representing approximately 80 percent of the shares of Genuity outstanding immediately after the IPO⁸⁶ only if it eliminates section 271 restrictions as to at least 95 percent of Bell Atlantic in-region lines within five years from merger closing, and eliminates any section 271 restrictions with respect to all remaining lines.⁸⁷ If, therefore, Bell Atlantic/GTE satisfies this 95-percent threshold, it can exercise the Class B conversion right for the purpose of immediately bringing Genuity's business into compliance with section 271. As set forth in an agreement between the merged firm and Genuity, however, the merged firm may require Genuity to reconfigure its operations to conform to section 271 in the states for which the merged firm has not obtained section 271 authorization only if those states in the aggregate represent no more than 3 percent of Genuity's revenues and if Bell Atlantic/GTE reimburses Genuity for the costs of coming into compliance with section 271.⁸⁸ Under the proposal, at least 90 days before the merged firm intends to convert and require Genuity to reconfigure its operations, it will notify the Commission and submit to the Chief of the Common Carrier Bureau a plan for how it would reconfigure Genuity's operations in the relevant states.⁸⁹

If the merged Bell Atlantic/GTE entity itself converts the Class B shares, they will convert into the appropriate number of Class C shares, which are identical to Class A shares except that they carry enhanced voting rights (five votes per share). If the merged firm transfers the Class B shares to another entity, that party may only convert them into Class A shares with ordinary voting rights (one vote per share).

Even if the merged firm eliminates these section 271 restrictions and is able to convert, it may not retain the portion of any appreciation that is attributable to Bell Atlantic in-region states during the period before it obtained section 271 authorization for those states.⁹⁰

⁸⁶ The post-conversion interest would be lower than 80 percent if Genuity were to issue additional Class A shares prior to any conversion. *Id.*, Ex. A at 4.

⁸⁷ *See id.*

⁸⁸ *Id.*

⁸⁹ *Id.*

⁹⁰ *Id.* at 2.

Instead, that portion of the appreciation will be transferred to Genuity's public shareholders.⁹¹ The relevant portion of appreciation will be calculated based on the number of Bell Atlantic in-region access lines compared to the number of the merged firm's access lines nationwide.⁹²

- *Options between 50 and 95 percent.* If the merged firm meets the 50-percent threshold but not the 95-percent threshold, it can dispose of all or a portion of its Class B shares,⁹³ but the merged firm can only retain sale proceeds that do not exceed the value of its original investment (or ratable portion thereof) plus a return based on the Standard & Poor's 500 Index.⁹⁴ Nonetheless, if Bell Atlantic/GTE intends to dispose of all or a portion of its shares,

⁹¹ The merged firm will elect to pay the relevant portion of any in-region appreciation by making a payment to Genuity for distribution to the Class A shareholders or by adjusting the conversion ratio to reduce by a corresponding amount the number of shares that the merged firm receives upon conversion. *Id.*

⁹² This would involve first determining Bell Atlantic/GTE's total appreciation, or the gain in value of the Class B shares from the IPO price on an as-converted basis, which would be calculated by a nationally-recognized investment banking firm (which has no prior association with the merged firm) based on the appreciation of the Class A stock adjusted, if necessary, to exclude any change in value attributable to the anticipated payment to Class A shareholders. Next, the appreciation attributable to a 10-percent interest would be subtracted from that total appreciation. Then, for each anniversary of the IPO, the percentage of Bell Atlantic in-region lines still subject to section 271 restrictions will be divided by the total number of Bell Atlantic in-region lines, and then multiplied by 25 percent to account for the portion of Genuity's domestic business operating in Bell Atlantic's region. These annual fractions will be averaged and multiplied by the total appreciation, less 10 percent, with the result adjusted for taxes (as if the merged firm had sold the Genuity stock initially). *Id.*, Ex. A at 3. Although AT&T and the Competition Policy Institute suggest that basing the 25-percent multiplier on the percentage of in-region access lines is flawed, and that a better approach would be to use a multiplier equal to the ratio of Genuity's revenues derived from the Bell Atlantic region as compared with Genuity's national revenues, we note that the 25-percent figure closely approximates the actual percentage of Genuity's 1999 revenues attributable to the Bell Atlantic states other than New York. See Letter from Peter D. Keisler, Sidley & Austin, Counsel for AT&T, to Magalie Roman Salas, Secretary, FCC, CC Docket No. 98-184 at 1-3 (filed June 9, 2000) (AT&T June 9, 2000 *Ex Parte* Letter); Letter from Ronald J. Binz, President, Competition Policy Institute, to Magalie Roman Salas, Secretary, FCC, CC Docket No. 98-184 at 2 (filed June 12, 2000). *But see* Letter from Steven G. Bradbury, Kirkland & Ellis, Counsel for GTE, to Magalie Roman Salas, Secretary, FCC, CC Docket No. 98-184 (filed Apr. 12, 2000) (containing confidential revenue materials). Accordingly, we find that the 25-percent multiplier is a reasonable approximation of the portion of Genuity's business that would be attributable to the Bell Atlantic section 271-restricted states.

⁹³ The merged firm may also exercise its conversion rights as part of a transaction by which it immediately disposes of all or a portion of its interest in Genuity so that its post-conversion interest in Genuity does not exceed 10 percent, subject to the limitations described below, which include offering the remainder first to Genuity and retaining limited sales proceeds. Bell Atlantic/GTE June 7, 2000 Glover *Ex Parte* Letter Ex. A at 3.

⁹⁴ Specifically, if the merged firm sells the Class B shares before it has met the 95-percent threshold, it will not have the right to retain sale proceeds that exceed (i) sale proceeds attributable to a 10-percent interest in Genuity, plus (ii) an amount equal to what the merged firm would have had if it had invested in the Standard & Poor's 500 Index its initial investment in Genuity above a 10-percent interest (based on the IPO price). Similarly, if it sells all its stock except an amount convertible into a 10-percent interest, it can retain only the amount described in clause (ii) above. In either case, Bell Atlantic/GTE would pay the remainder of its sales proceeds to the U.S. Treasury. *Id.*, Ex. A at 4. Although the Applicants' submissions refer to after-tax sales proceeds, we agree with AT&T that using after-tax proceeds would result in a windfall to the merged firm. See AT&T June 9, 2000 *Ex Parte* Letter at 5. Because the Applicants reserved the right to retain S&P 500-based appreciation in the pre-tax value of their initial investment in Genuity above a 10-percent interest, and thus do not account for tax effects from the disposition of Genuity at the front end of the calculation, we believe it is reasonable to adjust the cap at the back end "to reflect (continued....)"

it must first offer to sell the shares to Genuity for an amount that is the lesser of the value of its original investment (or ratable portion thereof) plus a return based on the Standard & Poor's 500 Index or the fair market value of such shares at the time of their disposition.⁹⁵ Genuity may pay the purchase price through a marketable debt instrument that will bear interest at a commercially reasonable rate.⁹⁶ If Genuity declines to purchase Bell Atlantic/GTE's shares, the merged firm would be able to transfer the shares to a disposition trustee for sale to third parties, subject to the limitation on the firm's receipt of sales proceeds.⁹⁷

- *Extension of Conversion Period.* If, at the end of five years, Bell Atlantic/GTE has eliminated section 271 restrictions as to at least 90 percent of total Bell Atlantic in-region lines (or 95 percent but for one state), Bell Atlantic/GTE may file a petition with the Commission requesting an additional year in which to eliminate the remaining section 271 restrictions. The Commission shall have the discretion whether to approve such a petition.⁹⁸

(Continued from previous page)

the fact that GTE would have had to pay taxes when it 'sold' Genuity and would have had less money to invest." Bell Atlantic/GTE June 7, 2000 Glover *Ex Parte* Letter Ex. A at 5. See also Letter from Michael E. Glover, Associate General Counsel, Bell Atlantic, to Magalie Roman Salas, Secretary, FCC, CC Docket No. 98-184 (filed June 14, 2000) (clarifying that the amount the merged firm could retain is calculated without regard to tax consequences but that the payment to the U.S. Treasury would be calculated on a tax-adjusted basis to reflect the fact that the portion of sales proceeds above the cap may be subject to taxes). Therefore, as reflected in Appendix B, we clarify that the Applicants are not entitled to retain pre-tax sales proceeds that exceed the specified amount. We further clarify, however, that to the extent that the Applicants must remit sales proceeds in excess of the cap, that remission will be adjusted to reflect taxes due on any such excess amount.

⁹⁵ The Applicants clarified that their proposal would not prevent Genuity from purchasing the merged firm's shares (either directly from Bell Atlantic/GTE or from the disposition trustee) at a lesser mutually-agreeable price in the event that the value of the shares were less than the specified amount. See Letter from Michael E. Glover, Associate General Counsel, Bell Atlantic, to Magalie Roman Salas, Secretary, FCC, CC Docket No. 98-184 (filed June 8, 2000), at 1. As reflected in Appendix B, we clarify the proposal even further to explicitly provide that Genuity has the right to purchase the shares directly from the merged firm upon its initial offer (prior to involvement of a disposition trustee) at the fair market value, if lower than the specified amount.

⁹⁶ Bell Atlantic/GTE June 7, 2000 Glover *Ex Parte* Letter at 1. Genuity will have 90 days after the date it receives an offer to agree to purchase the merged firm's shares. If Genuity intends to purchase the shares, the merged firm will grant any consents necessary under its investor safeguards, and Genuity will have 180 days after the date it received the offer to make any applicable financial or other arrangements. Although the Applicants do not make representations concerning the interest rate or term of the debt instrument, we clarify in Appendix B that the applicable interest rate and term must be commercially reasonable, or comparable to rates and terms under similar instruments held by companies with debt ratings comparable to Genuity. If necessary, the conversion period will be extended to allow for the sale to Genuity or another party.

⁹⁷ *Id.*, Ex. A at 2-3. To the extent Class B shares are purchased by a person who is not subject to section 271 restrictions, the purchaser would be free to convert the Class B shares into Class A shares immediately.

⁹⁸ As reflected in Appendix B, we clarify that if the merged entity has achieved approvals representing 90 percent of Bell Atlantic in-region access lines (or 95 percent but-for one state), the Commission has discretion whether to grant the merged firm an additional year in which to obtain the remaining section 271 approvals. Although the Applicants' proposal also enables the Commission to toll or extend the conversion period to account for intervening events that delay elimination of section 271 restrictions, we foresee no circumstances under which the Commission would extend the conversion period in such a manner.

Moreover, if at the end of the five-year conversion period, litigation is pending over whether Bell Atlantic/GTE has eliminated section 271 restrictions as to certain lines, and if a court subsequently determines that the company has eliminated such restrictions, then the merged entity shall be deemed to have eliminated those restrictions within the conversion period.⁹⁹

31. *Officers and Directors.* Under the proposed structure for the Genuity board of directors, Genuity ultimately will have a thirteen-member board, twelve of whom are periodically elected by the Class A shareholders. Bell Atlantic/GTE, as the holder of the Class B shares, will designate the other member. In order to establish an independent board, GTE will appoint six directors before the IPO: one will be the CEO of Genuity, one will be designated by GTE (as the Class B designee), and the other four will be independent directors who have no prior relationship with Bell Atlantic or GTE.¹⁰⁰ Within 90 days after the IPO, the four independent directors will select seven additional directors who have no prior relationship with Bell Atlantic or GTE. This will bring the total board membership to 13 directors, a majority of whom will have been selected after the IPO.

32. As soon as possible, but no later than nine months after the IPO, all directors other than the Class B designee will stand for election by the Class A shareholders.¹⁰¹ From that point, every year four of the twelve publicly elected directors will stand for reelection.¹⁰² The Class B director stands for election annually. The Class B director will abstain from any vote until the board consists of at least ten members, and will at no time serve as chairman of the board.

33. The officers and directors of Genuity will owe fiduciary duties to the public shareholders. Incentive compensation for Genuity's managers will be tied to the performance of Genuity and the value of its publicly traded stock, not to the financial performance or stock value of the merged Bell Atlantic/GTE.¹⁰³

34. *Investor Safeguards.* The Class B shares also contain certain investor safeguards designed to protect the merged firm's interest as a minority investor and potential future majority shareholder.¹⁰⁴ The merged company will have these rights only until it converts its Class B shares or no longer has the possibility of converting into more than a 10-percent interest.¹⁰⁵ These safeguards include the right to approve certain fundamental business changes such as a

⁹⁹ Bell Atlantic/GTE June 7, 2000 Glover *Ex Parte* Letter Ex. A at 5.

¹⁰⁰ *Id.*

¹⁰¹ Bell Atlantic/GTE Apr. 28, 2000 *Ex Parte* Letter Ex. A at 1.

¹⁰² *Id.*, Ex. B at 1.

¹⁰³ Bell Atlantic/GTE June 7, 2000 Glover *Ex Parte* Letter Ex. A at 5.

¹⁰⁴ *Id.*

¹⁰⁵ See Appendix B (Genuity Conditions) at Att. 1 (Investor Safeguards). We note that the merged firm's right to receive shares of up to 80 percent if it owns shares of at least 70 percent extends for one year following conversion.

change in control of Genuity or the sale of a significant portion of its assets. Some safeguards require a vote of the Class B shares,¹⁰⁶ while others require Genuity to obtain consent from the merged company.¹⁰⁷ In addition, no single holder or group of Class A shareholders may vote more than 20 percent of the Class A stock.¹⁰⁸ Moreover, insofar as Genuity's business plan does not contemplate the acquisition of a traditional voice long distance service provider, pursuant to these investor safeguard rights, Bell Atlantic/GTE will withhold its consent from Genuity's acquisition of such a carrier absent Commission approval.¹⁰⁹

35. *Financing.* A major source of Genuity's capital would consist of the proceeds from the sale of Class A stock in the IPO. Additional funding required by Genuity's business operations would be raised from the public markets, possibly by issuing additional Class A shares, by issuing debt to the public, or by arm's-length commercial loans, which could include loans from Bell Atlantic/GTE.¹¹⁰ Under the proposal, however, if Bell Atlantic/GTE loans money to Genuity, it could provide no more than 25 percent of Genuity's aggregate debt financing.¹¹¹

36. *Commercial Contracts.* All commercial interactions between the merged Bell Atlantic/GTE (and any affiliates) and Genuity will be pursuant to commercially reasonable contracts. For example, the companies will enter into contracts for the merged company to

¹⁰⁶ A vote of the Class B shareholders is required for: (a) merger, consolidation, sale of all or substantially all assets or similar transactions; (b) bankruptcy or liquidation; (c) authorization of additional stock; (d) amendments to charter or certain by-law provisions that affect the rights of the Class B shareholders; (e) a material change in the nature or scope of Genuity's business; and (f) any action that would make it unlawful for the merged firm to exercise its conversion right. Bell Atlantic/GTE Apr. 28, 2000 *Ex Parte* Letter Ex. C at 1. See Appendix B (Genuity Conditions) at Att. 1 (Investor Safeguards).

¹⁰⁷ Bell Atlantic/GTE's consent is required for: (a) agreements or arrangements that (i) bind or purport to bind the merged firm or any of its affiliates or (ii) contain provisions that trigger a default, or provide for a material payment as a result of the merged firm's exercise of its conversion right; (b) declarations of extraordinary dividends or other extraordinary distributions; (c) issuance of shares, securities convertible into shares or share equivalents, with exceptions that include shares issued in connection with acquisitions so long as the aggregate number of shares does not exceed 30 percent of the shares outstanding immediately after the IPO, shares issued to fund operating needs of up to 5 percent, and shares issued or granted to employees in amounts specified in the registration statement; (d) an acquisition or series of related acquisitions that equal more than 20 percent of the fair market value of Genuity's assets or an acquisition or joint venture that is in excess of \$100 million and is not closely related to Genuity's business; (e) a disposition or series of dispositions that are in excess of 20 percent of the fair market value of Genuity's assets; and (f) incurrence of debt in excess of \$11 billion over a five-year period, with Genuity not incurring more than 35 percent of such debt in any year. Bell Atlantic/GTE Apr. 28, 2000 *Ex Parte* Letter Ex. C at 1. See Appendix B (Genuity Conditions) at Att. 1 (Investor Safeguards).

¹⁰⁸ Bell Atlantic/GTE Apr. 28, 2000 *Ex Parte* Letter Ex. C at 1.

¹⁰⁹ Bell Atlantic/GTE June 7, 2000 Glover *Ex Parte* Letter Ex. A at 6.

¹¹⁰ *Id.*, Ex. A at 5.

¹¹¹ *Id.* This 25-percent limitation would not affect Genuity's ability to purchase Bell Atlantic/GTE's Genuity shares using a debt instrument in the event that the merged firm fails to obtain section 271 approvals representing 95 percent of its access lines and seeks to dispose of its shares.

provide transitional administrative support services. Each contract will have a term of one year or less, and will be terminable at any time by Genuity without penalty.¹¹² In view of the transitional nature of the contracts, the contracts will not be renewed by the parties. Although the contracts enable the merged firm to provide some human resources administrative support, the merged firm will not have any role in hiring or firing Genuity employees.¹¹³ In addition, Genuity will not rely upon any network monitoring from the merged firm after October 31, 2000.¹¹⁴

37. Because a significant portion of Genuity's business is outside the Bell Atlantic region or in New York, where Bell Atlantic has obtained section 271 approval, the companies will enter into a marketing agreement for the period before conversion of the Class B shares. Pursuant to the Purchase, Resale and Marketing Agreement, Bell Atlantic/GTE will market Genuity's services (or the two companies will market their services jointly) as and where permitted by law.¹¹⁵ In New York, for example, where Bell Atlantic has received section 271 approval, the merged firm and Genuity will jointly market Genuity's Internet connectivity services. The Agreement, however, provides that Bell Atlantic/GTE will not provide or joint market any interLATA service of Genuity in any state where Bell Atlantic does not have interLATA authority.¹¹⁶ The Agreement is also non-exclusive, so that either company may purchase from or sell to others.

38. *Independent Auditor.* Under their proposal, the Applicants further commit to hire an independent auditor, acceptable to the Chief of the Common Carrier Bureau, to monitor ongoing compliance with the terms of the spinoff proposal.¹¹⁷

B. Discussion

39. Section 271 of the Act states that "[n]either a Bell operating company, nor any affiliate of a Bell operating company, may provide interLATA services" except as set forth in that section.¹¹⁸ The term "affiliate" is not defined in section 271, but is defined generally in section 3(1) of the Act:

¹¹² *Id.*, Ex. A at 6.

¹¹³ *Id.*, Ex. A at 6-7.

¹¹⁴ *Id.*, Ex. A at 7.

¹¹⁵ *Id.*, Ex. A at 6.

¹¹⁶ *Id.*

¹¹⁷ *Id.*, Ex. A at 7. As discussed in Section VIII, the merged firm's compliance with the spin-off proposal and the ongoing relationship between the companies following the spin-off will be included within the scope of the independent audit required by the merger conditions.

¹¹⁸ Through section 271, Congress made the BOCs' authority to provide in-region, interLATA services contingent upon the BOC opening its local markets to competition by, for example, "providing access and interconnection" to local competitors. 47 U.S.C. § 271.