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CompTel ASCENT

October 14, 2004

VIA ELECTRONIC FILING

Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, SW
Washington, D.C. 20554

Re: *WT Docket No. 04-70, Cingular/AT&T Wireless Merger*

Dear Ms. Dortch:

Pursuant to Section 1.1206 of the Commission's rules, CompTel/ASCENT ("CompTel") hereby gives notice that on October 13, 2004, its representatives had separate meetings Paul Margie, Legal Advisor to Commissioner Copps; Sam Feder, Legal Advisor to Commissioner Martin; and Jennifer Manner, Legal Advisor to Commissioner Abernathy, and Gavin Gaukroger of Commissioner Abernathy's office. In these meeting, CompTel explained the potential anticompetitive effects of the above-referenced merger, both from a unilateral effects and coordinated effects standpoint. CompTel also explained how some fairly limited conditions (discussed in detail in our October 1st ex parte), if adopted by the Commission as part of its order approving the merger, could offset the significant potential anticompetitive effects of this combination. During the meetings CompTel handed out a copies of its October 1, 2004 merger simulation analysis, and its Reply Comments, filed on May 20, 2004. Both documents are included as attachments to this letter. All of the arguments discussed were previously made in the attached documents. Representing CompTel were Michael Pelcovits of Microeconomic Research & Consulting Associates, and the undersigned attorney.

Sincerely,

Jonathan D. Lee

Jonathan Lee
Sr. Vice President
Regulatory Affairs

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CompTel ASCENT

October 1, 2004

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, SW
Washington, D.C. 20554

Re: *Cingular/AT&T Wireless Merger, WT Docket No. 04-70*

Dear Ms. Dortch:

CompTel/ASCENT ("CompTel") presents the attached merger simulation study to supplement CompTel's earlier comments opposing this merger, and to assist the Commission with its analysis of this transaction. If, as many (including Chairman Powell) contend, wireless and wireline service are substitutes for one another,[1] then the present merger bears careful scrutiny. While arguing against the notion of wireless substitution in this proceeding, it is notable that SBC and BellSouth have asserted the opposite in earlier proceedings before the Commission.[2] CompTel's attached merger simulation study is consistent with other economic analyses of this merger, all of which

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[1] See, *e.g.*, Statement of Chairman Powell on Release of Interim Rules, CC Docket No. 01-338 (August 20, 2004) ("Consumers are using wireless telephones more than they are using wired telephones today—many now use their mobile as their primary phone."). See also, *"And a Child Shall Lead Them"* Remarks of Chairman Powell at the Chicago Economic Club, Chicago, Illinois (December 18, 2003) ("Many young people, for example, are cutting the cord and not subscribing to a local or long distance home telephone service. Instead, they have made their wireless phone, with its highly personalized attributes, their only phone.")

[2] See, *e.g.*, *Comments of SBC Communications*, CC Docket No. 01-338 at 38 (April 5, 2002) ("wireless networks built to serve high end customers initially are now being used to offer a portable substitute for wireline service.") See also, *Comments of BellSouth Communications*, CC Docket No. 01-338 at 22 (April 5, 2002) (FCC must consider intermodal competition "particularly with regard to wireless substitution" in assessing whether competitors are impaired without access to UNEs). Many of the Bell Company filings in CC Docket No. 01-338 claim that wireless and wireline are effective intermodal competitors. See, *e.g.*, Shelanski Declaration accompanying the comments of SBC and BellSouth in the above-referenced proceeding at ¶ 59 ("Switching Appears Yet More Competitive in Light of Wireless Competition"). But see, Affidavit of Richard J. Gilbert filed on Behalf of Cingular and AT&T Wireless, WT Docket No. 04-70 (March 18, 2004), ¶¶ 40-41.

demonstrate a substantial likelihood of significant losses in consumer welfare as a result of the combination of Cingular and AT&T Wireless. Significantly, but not surprisingly, CompTel's simulation, as well as the other studies, only confirms the accuracy and wisdom of BellSouth CEO and Chairman Duane Ackerman's two-years-ago, pre-merger, observation: "Wireless substitution is now a fact. That's okay. We tend to own both."[3]

Nonetheless, however harmful the potential effects of this merger may be, CompTel believes that this merger application presents the Commission with an opportunity to further the long-term policy goals of the Commission without excessively obstructive regulatory action. As CompTel has explained earlier in this proceeding, and explains in greater detail in the attached study, one critical factor which exacerbates the anticompetitive effects of this merger and continues to frustrate the deregulatory goals of this Commission is the anticompetitive behavior—exercised through term and volume special access tariffs—in which the Bell companies engage to foreclose and limit efficient facilities-based competition in the market for wholesale metro transport.

CompTel believes that much of the potential harm of this merger could be mitigated if the Commission would condition its approval of the merger on the elimination of certain anticompetitive provisions that currently exist in BellSouth and SBC term and volume tariffs. Specifically, the FCC should forbid SBC and BellSouth from imposing:

1) Termination, or "shortfall," liabilities that extend beyond the initial term of the volume tariff discount;
2) Volume commitments based on significant percentages of prior purchase requirements;
3) Discounts—especially "first dollar" discounts—predicated on moving circuits off competitive carrier networks;
4) Any restrictions which discourage special access purchasers from using their own fiber facilities, the facilities of a third party, or unbundled network elements from BellSouth or SBC.

These limited conditions will, along with prudent unbundling policies, help to more quickly expand economic opportunities for fiber-based wholesale carriers, the services of which will ultimately benefit all facilities-based providers—retail and wholesale, intermodal and intramodal. Exactly two years ago, Chairman Powell accurately summarized the economic benefit of the competition the Bells currently impede through the exclusionary terms their market power allows them to extract from both wireless and wireline competitors:

> "Only through facilities-based competition can a competitor lessen its dependency on an intransigent incumbent, who if committed to frustrate entry has a thousand ways to do so in small, imperceptible ways.

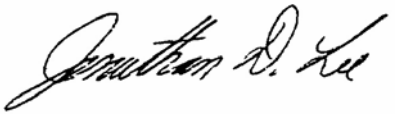
[3] *More Callers Cut off Second Phone Lines for Cellphones, Cable Modems*, WALL STREET JOURNAL B1 (November 15 2001) (quoting Duane Ackerman).

> Only through facilities-based competition can an entity bypass the incumbent completely and force the incumbent to innovate to offset lost wholesale revenues.
>
> Only through facilities-based competition can our Nation attain greater network redundancies for security purposes and national emergencies."[4]

CompTel shares the Commission's vision that consumers deserve all the benefits of vigorous competition between firms using both intermodal and intramodal technologies. This vision, however, cannot be realized unless, or until, retail competitors—of all technologies—have a genuinely competitive wholesale market for key inputs like local transport. SBC and BellSouth have locked down this market—starving alternative facilities providers of the demand they need to successfully expand competitive fiber deployment. This merger will not only be anticompetitive for consumers in the short run, but will enhance the Bells' ability to foreclose efficient facilities-based wholesale competitors—causing harm to nascent intermodal competition—unless the FCC steps in to protect competition.

Fortunately, though, this merger also presents the opportunity for the FCC to demonstrate its commitment to facilities-based intermodal (and intramodal) competition by eliminating anticompetitive strategic conduct by the incumbent monopolies that are a critical barrier to entry by fiber based wholesale carriers. Moreover, the additional competition that the Commission will spur through these limited conditions will inure to the benefit of retail wireless and wireline competitors, and their customers, but also retail providers of the nascent VoIP and BPL services the Commission seeks to further promote. Finally, the conditions CompTel proposes are fully consistent with sound antitrust principles, and provide the least intrusive means for the Commission to limit the anticompetitive effects of the proposed merger.

Sincerely,



Jonathan Lee
Sr. Vice President
Regulatory Affairs

[4] Remarks of Chairman Powell, Goldman Sachs Communicopia XI Conference, New York, NY (October 2, 2002).

A Simulation Analysis of the Effects on Mobile and Wireline Prices of the Cingular-AT&T Wireless Merger

I. Introduction

On February 17, 2004, formal terms were announced for the merger of the second and third largest mobile telecommunications carriers in the United States -- Cingular and AT&T-Wireless.[1] The combined market share of the two firms will equal about 40%, which is about ten percentage-points higher than the current largest mobile carrier Verizon (with about a 30% market share).[2] The merger will also place about 70% of mobile telephony subscribers in the hands of dominant wireline carriers (i.e., the Bell Operating Companies).[3]

There has been considerable debate over the consequences of the proposed merger for end-user prices. An expert hired by Cingular and AT&T-Wireless contends the merger "will not harm [but] will strengthen competition by creating a more efficient and effective competitor."[4] Alternately, a study by the Consumer Federation of America ("CFA") argues the merger "is anticompetitive from every angle" and that "[w]ireless competition will be dramatically reduced by the merger."[5] Financial analysts predict consolidation in the wireless industry will be "beneficial in terms of reduction of price competition and churn" and will "slow [ ] the relentless pace of price competition," but also may create the "potential for a return to scale in sales, advertising and distribution."[6] As with any merger, there are fears of market power and hopes of efficiencies, with the overall consumer benefit of the merger requiring an assessment of the merger's potential consequences.[7]

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1 J. Hall and S. Carew, *Cingular Wins AT&T Wireless for $41 Bln*, REUTERS (February 17, 2003).

2 *Turbulent Marketplace for Telecom Marked by Shifting Market Share; Comcast Holds Largest Provider Share of Customers Spending*, BUSINESS WIRE (April 21, 2004). The 2003 market shares of the national wireless carriers (subscribers, revenues) are: Verizon Wireless (29%, 29%), Cingular (21%, 18%), AT&T Wireless (20%, 20%), Sprint (15%, 16%), T-Mobile (10%, 9%), and Nextel (6%, 9%).

3 *Id*. The combined subscriber shares of the Bell Company owned wireless firms would be 70% and the combined revenue shares of the firms would be 67%.

4 Affidavit of Richard J. Gilbert filed on Behalf of Cingular and AT&T Wireless, WT Docket No. 04-70 (March 18, 2004), at 2, 3: http://www.fcc.gov/transaction/cingular-att_wireless.html.

5 M. Cooper, *Remonopolizing Local Telephone Markets: Is Wireless Next*? Consumer Federation of America (July 2004): http://www.consumerfed.org/localwireless.pdf.

6 R. Katz, *Can Mergers Mend Industry Woes*? AMERICA'S NETWORK (October 1, 2003) and Cellular *Stocks: This Year, Tread With Care*, BUSINESSWEEK EUROPE (January 1, 2004).

7 O. E. Williamson, Economies as an Antitrust Defense: The Welfare Tradeoffs, 58 AMERICAN ECONOMIC REVIEW 18-34 (1968).

To date, only one study of which we are aware presents a formal quantitative analysis of the total effects of the merger. This study, published by the non-profit Phoenix Center for Advanced Legal and Economic Public Policy Studies, reports the results from a financial event study and a merger simulation.[8] An event study assesses the effects of a merger by evaluating the stock price movements on or around announcements related to the merger.[9] Large positive stock price movements for non-merging firms in response to merger announcements indicates that investors believe the merger will increase the profits of rival firms, which is interpreted to mean an investor expectation of reduced competition in the industry. Lower stock prices are interpreted to mean the merger will increase the efficiency of the merging firms and, consequently, disadvantage rivals. Thus, the event study considers both the market power and efficiency consequences of the merger. Over the event dates of the Cingular/AT&T merger, the Phoenix Center estimates a 12.6% cumulate stock price *increase* for the non-merging firms. Using the financial data of the non-merging firms and the methodology proposed by Warren-Boulton and Dalkir (2001), this stock price increase is translated into a retail price increase of 7.9%.[10] Investors, it appears, believe the merger will reduce competition in the wireless industry by much more than it will improve the efficiency of the merging firms.

The Phoenix Center study also predicts the price increases from the merger using a simulation model. A merger simulation employs theoretical economic models of competition and real world data to simulate the effects of a merger between two rival firms.[11] The parameters of the theoretical model are calibrated with real world

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[8] Phoenix Center, *Higher Prices Expected from the Cingular/AT&T Wireless Merger*, PHOENIX CENTER POLICY BULLETIN NO. 11 (May 26, 2004).

[9] See, e.g., F. R. Warren-Boulton and S. Dalkir, Staples and Office Depot: An Event-Probability Case Study, 19 REVIEW OF INDUSTRIAL ORGANIZATION 467 (2001); D. Hosken and John David Simpson, Have Supermarket Mergers Raised Prices? An Event Study Analysis, 8 INTERNATIONAL JOURNAL OF THE ECONOMICS OF BUSINESS 329 (2001); G. Bittlingmayer and T. Hazlett, DOS Kapital: Has Antitrust Action Against Microsoft Created Value in the Computer Industry?, 55 JOURNAL OF FINANCIAL ECONOMICS, 329-359 (2000); G. L. Mullin, J. C. Mullin, W.P. Mullin, The Competitive Effects of Mergers: Stock Market Evidence from the U.S. Steel Dissolution Suit, 26 RAND JOURNAL OF ECONOMICS 314-330 (1995); R. A. Prager, The Effects of Horizontal Mergers on Competition: The Case of the Northern Securities Company, 23 RAND JOURNAL OF ECONOMICS 123-133 (1992); J. M. Woolley, The Competitive Effects of Horizontal Mergers in the Hospital Industry, 8 JOURNAL OF HEALTH ECONOMICS 271-292 (1989); R. Stillman, Examining Antitrust Policy Towards Horizontal Mergers," 11 JOURNAL OF FINANCIAL ECONOMETRICS 225-240 (1983); B. E. Eckbo, Horizontal Mergers, Collusion, and Stockholder Wealth, 11 JOURNAL OF FINANCIAL ECONOMETRICS 241-273 (1983).

[10] Warren-Boulton and Dalkir, *Id.*

[11] See, e.g., J. A. Hausman and G. K. Leonard, Economic Analysis of Differentiated Products Mergers Using Real World Data, 5 GEO. MASON L. REV. 321 (1997); Gregory J. Werden, Simulating Unilateral Competitive Effects from Differentiated Products Mergers, ANTITRUST (Spring 1997), at 27; P. Crooke, L. M. Froeb, S. Tschantz & G. J. Werden, The Effects of Assumed Demand Form on Simulated Postmerger Equilibria, 15 REV. INDUS. ORG. 205 (1999); G. J. Werden and L. M. Froeb, Simulation as an

data such as observed prices, quantities or market shares, and econometric estimates of demand elasticities. The Phoenix Center's merger simulation was based on the Cournot model of oligopolistic competition.[12] Using industry data and the static equilibrium properties of the Cournot model, the Phoenix Center evaluated its Cournot-competition assumption and found it to be a reasonable proxy for competitive interaction in the industry.[13] The Phoenix Center simulation was calibrated using existing market shares and an estimate of industry price and the market elasticity of demand. Assuming no cost efficiencies resulting from the merger, industry price was predicted to rise by 7.1%, reducing consumer welfare by $5.2B annually. Even with a 15% marginal cost reduction, the merger results in a 5.7% price increase and a consumer surplus loss of $4.2B. According to the Phoenix Center study, the merger of Cingular and AT&T Wireless is problematic from an antitrust perspective since the merger is predicted to result is sizeable price increases for wireless services.[14]

In this paper, we add to the formal analysis of the Cingular/AT&T Wireless merger by conducting a merger simulation. While our simulation predicts the effects on wireless prices from the merger, it is extended to assess what effects, if any, the merger could have on prices in wireline telecommunications. This extended effect of the merger is a consequence of the joint ownership of mobile and wireline carriers by dominant firms (i.e., the Bell Operating Companies) and the positive cross-price elasticities between the two telecommunications services (i.e., the two services are substitutes).[15] In other words, if wireless and wireline services are substitutes, then a profit-maximizing firm that sells both services will account for that substitution when it sets price, with the resulting prices being higher than if the two services were sold independently. Perhaps BellSouth CEO and Chairman

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Alternative to Structural Merger Policy in Differentiated Products Industries, in THE ECONOMICS OF THE ANTITRUST PROCESS 65 (Malcolm B. Coate & Andrew N. Kleit eds., 1996).

[12] Cournot competition is described as competition in quantities, whereas Bertrand competition is competition in prices. In both cases, each firm behaves as if its rivals will not respond to the choices of the firm. See S. Martin, INDUSTRIAL ECONOMICS: ECONOMIC ANALYSIS AND PUBLIC POLICY (1988), at 104-17.

[13] Phoenix Center, supra nt. 8, at 11 ("This suggests an α value of about 0.05, which is very close to the Cournot outcome of zero (the industry is slightly less competitive than Cournot)").

[14] A 5% price increase is often viewed as being large enough to warrant attention, but the "small but significant non-transitory price increase" language from the GUIDELINES relates primarily to market definition. MERGER GUIDELINES §1.0: http://www.usdoj.gov/atr/public/guidelines/horiz_book/toc.html. Scheffman and Coleman, for example, note that in one case "a 2-3% price difference was meaningful to customers." D. T. Scheffman and M. Coleman, *Quantitative Analyses of Potential Competitive Effects from a Merger* (June 9, 2003), Presented at FTC/DOJ Joint Workshop on Merger Enforcement, February 17-19, 2004: http://www.ftc.gov/bc/mergerenforce/presentations/040218scheffman02.pdf.

[15] POLICY BULLETIN NO. 11 at 12-13; J. Tirole, THE THEORY OF INDUSTRIAL ORGANIZATION (1995) at Ch. 5.

Duane Ackerman summarized it best: "Wireless substitution is now a fact. That's okay. We tend to own both."[16] As Mr. Ackerman so clearly explains, by owning both the substitution between the two services can be internalized. Our simulation can illustrate the effects of "owning both" on final goods prices.

The results of the simulation analysis are as follows. First, the prices of the merging firms are predicted to increase by no less than 11%. Given the chosen functional form of the demand curves used in the simulation, the prices of the merging parties' rivals do not change so the predicted industry effects are very conservative. Even so, the industry average price rises substantially. Consumer welfare reductions in mobile telecommunications from the merger total $2.7 billion. Even with the predicted reductions in cost from the merger, the merging firms' prices rise by no less than 10%. Second, the merger is predicted to increase the prices of wireline service by 2.4%, despite using extremely conservative assumptions regarding the degree of substitution between wireless and wireline services. On the wireline side, our simulation predicts consumer welfare losses of over $300 million annually.

In the next section we describe in detail our merger simulations. First, we present the econometric model used to estimate the demand elasticities. These elasticities play a key role in the merger simulation. Second, we present the results of the merger simulation on wireless prices assuming no change in the marginal cost of the merging firms. Third, we compute the price effects of the merger assuming the merger results in efficiencies. Fourth, we present the price effects for both wireless and wireline services in our extended simulation. Fifth, we evaluate, in some cases with simulation, some potential negative effects on other markets that this merger could produce. Sixth, consumer surplus losses from the merger are summarized. Conclusions are provided in the final section.

II. The Merger Simulation

The predicted price responses from merger simulations depend heavily on a number of key assumptions, including the form of competition, the shape of demand and cost curves, and the firm-specific demand elasticities (own- and cross-price) and marginal costs. Any predicted price effects from a merger are conditional on the very specific set of assumptions used for the simulation. Our particular set of assumptions is as follows. First, we adopt a product differentiated price-competition model (i.e., Bertrand). Thus, our focus is solely on unilateral price effects; there is no effort to measure the effects on the intensity of price competition or the potential for collusion, which have been historically the primary concern of antitrust analysis. Second, the demand curves are semi-log, a decision based on the econometric analysis used to estimate the own- and cross-price

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[16] *More Callers Cut off Second Phone Lines for Cellphones, Cable Modems*, WALL STREET JOURNAL B1 (November 15 2001) (quoting Duane Ackerman).

elasticities of demand. Third, the own- and cross-price elasticities of demand are based on our own econometric analysis. Fourth, marginal costs are assumed to be constant and are derived from the relevant markup rules based on first-order conditions for profit maximization, using the demand elasticities from our econometric analysis. Other relevant assumptions and inputs are presented in those sections in which they are used.

1. ESTIMATES OF DEMAND ELASTICITIES

The typical econometric demand curve for the Bertrand competitor i with r rivals is

$$q_i = \beta p_i + \gamma \sum_{j=1}^{r} p_j + \Omega X + \varepsilon_i \tag{1}$$

where p_i is the firm i's own-price and p_{-i} is the price of the rival(s) to firm i, **X** is a vector of factors other than own and rival prices that affect demand and ε is the econometric disturbance term. The parameters β, γ, and Ω are all estimated by an appropriate econometric model. From these estimated parameters we can compute the required own- and cross-price elasticities necessary to perform the Bertrand simulation.

More specifically, our econometric analysis begins with the general model specification

$$g\left(\frac{q_i}{Q}\right) = f\left(\alpha_0 + \alpha_1 p_i + \alpha_2 \sum_{j=1}^{r} \frac{s_i}{s_j} p_j + \alpha_3 POPS + \alpha_4 DTM\right) + \varepsilon_i \tag{2}$$

where Q is total industry quantity (so q/Q is market share), s_i is a quality index for firm i (and j), *POPS* is a measure of the total population served by the firm i's network, and *DTM* is dummy variable for the wireless firm T-Mobile.[17] The functions f and g are suitably selected transformations of the variables. Market share rather than quantity is employed because of the rapid growth of wireless

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[17] The individual firm's Form 10-Ks and 10-Qs provide all the quantity and price data. Prices are computed as the annual service revenues divided by end-of-year subscriber lines. This approach to computing price is somewhat problematic for T-Mobile given that its subscriber base is growing rapidly. As an alternate specification, we replaced T-Mobile's price with its reported average revenue per unit (ARPU). The computed elasticities were not much affected (the own-price coefficient increased by about 5% and the cross-price coefficient increased by 2%. Thus, we employ a consistent method for computing price for all firms by using service revenues deflated by lines. Quality data is provided by *J.D. Power and Associates Reports: Verizon Wireless Ranks Highest in Network Quality Performance* (July 29, 2003). POPS data is provided by J. Rockhold, *2002 Who Gets Out Alive*? WIRELESS REVIEW (December 1, 2002): http://www.findarticles.com/p/articles/mi_m0GTV/is_23_18/ai_80848046/print. The data is provided in Exhibit 2.

subscription over the sample period.[18] The cross-price effects are weighted by a quality index, thus making the size of the cross-price depend on the relative quality between firm *i* and each of its rivals.[19] Coefficients α_1 and α_2, respectively, are used to compute the own-price and cross-price elasticities of demand. The exact computation for the elasticity will depend on the specific functional form of functions *f* and *g*.[20]

Rather than impose *a priori* a particular functional form on the regression, we select the functional form with the "best" statistical properties. Candidate transformations considered here include the widely used linear and logarithmic transformations (e.g., lin-lin, log-lin, and log-log). Research shows that the functional form of the demand curve for the simulation is an important determinant of the size of the simulated price effects. We believe that allowing the data to inform us to the most suitable functional form is an improvement over simply assuming a functional form that may have desirable properties for simulation (e.g., such as the frequently used logit demand functional form which allows simulations to be performed with very little information). Five statistical criteria are employed in selecting the best functional form. First, we compare the fit of the models using a measure of R-squared that is comparable across alternate specifications of the dependent variable.[21] Second, following Godfrey et al (1988), we employ RESET.[22] RESET is a general test of specification error and is a powerful test for incorrect functional form.[23] Third, we test the model for heteroskedasticity using White's Test.[24] Fourth, we use Jarque-Bera test to evaluate the normality of the disturbance

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[18] The wireless market has grown from 81.7 million accounts in 2000 to 122.4 million in 2003, a growth rate of almost 50%. This rate of growth is very rapid. By using market shares rather than quantities, we render the dependent variable vector stationary and avoid the significant problems of accounting for growth parametrically.

[19] *J.D. Power and Associates Reports: Verizon Wireless Ranks Highest in Network Quality Performance* (July 29, 2003): http://www.jdpower.com/cc/telecom/jdpa_ratings/wireless/Find.jsp. The scale of the quality index is irrelevant because the ratio is used. For this particular scale, the index has a value of 100 for AT&T. The regression results are not much affected by the inclusion of the quality adjustments, but these adjustments did allow the cross-price effects to vary by price and quality.

[20] The own-price demand elasticities for various functional forms are: a) the Lin-Lin model = $\alpha_2(p_i/q_i)$; b) the Log-Lin model = $\alpha_2 p_i$; and c) the Log-Log model α_2.

[21] A. H. Studenmund, USING ECONOMETRICS (1992) at 227-9.

[22] L. G. Godfrey, M. McAleer and C. R. McKenzie, *Variable Addition and Lagrange Multiplier Tests for Linear and Logarithmic Regression Models*, 70 REVIEW OF ECONOMICS AND STATISTICS 492-503 (1988).

[23] D. Gujarati, BASIC ECONOMETRICS (1995) at 464-6.

[24] *Id* at 379-380.

term.[25] Finally, we appeal to the Davidson-McKinnon J-Test to evaluate which, if any, of the specific functional forms is most desirable.[26]

Table 1 summarizes the results of the model selection tests. Overall, the tests indicate that the Log-Lin (or semi-log) specification is best. The R-squared values are all high and too similar to indicate a preference for a particular model. Only the Log-Lin functional form passes the RESET test (with a null hypothesis of "no specification error") at the 10% significance level, so a clear preference for the Log-Lin specification is indicated by RESET. Both the Lin-Lin and Log-Lin models have homoskedastic disturbances, but the Log-Log form is heteroskedastic.[27] All three functional forms render normally distributed disturbances, so all are suitable on normality grounds. The Davidson-MacKinnon J-Test also shows a clear preference for the Log-Lin functional form, since neither of the t-statistics for the augmented regressions is statistically significant for the Log-Lin form. The Log-Lin form is shown to be preferable to either the Lin-Lin (probability 0.0185) or Log-Log (probability 0.1033) models. Based on this battery of tests, we believe the Log-Lin or semi-log specification is best and, consequently, we use the results from the semi-log models to compute own- and cross-price elasticities. We also base all calculations in the merger simulation on the semi-log demand curve.

Table 1. Functional Form Selection Criteria

Model	*Quasi R^2*	*RESET*	*White*	*J-Bera Test*
Lin-Lin	0.880	0.105	0.508	0.922
Log-Lin	**0.888**	**0.235**	**0.140**	**0.825**
Log-Log	0.892	0.050	0.050	0.825

Davidson-McKinnon J-Test (t-stat probability)

Base Model ↓	Lin-Lin	Log-Lin	Log-Log
Lin-Lin	…	0.0185	0.0152
Log-Lin	**0.2596**	**…**	**0.3009**
Log-Log	0.9848	0.1033	…

The estimated parameters from the semi-log specification are summarized in Exhibit 1. The model exhibits good statistical significance and overall fit. As already mentioned, the disturbance is normal and homoskedastic and the model passes RESET. Given the small sample size (24 observations), we also evaluated statistical significance using a bootstrap procedure.[28] Given the large t-statistics on the price coefficients (both exceeding 4.00 in absolute value), we did not expect the

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[25] *Id* at 143-4.

[26] Id at 490-3.

[27] Heteroskedasticity only affects the efficiency of the estimates and not result in biased coefficients. Thus, the point estimates of the elasticities will be unaffected by heteroskedasticity.

[28] J. MacKinnon, *Bootstrap Inference in Econometrics*, 35 CANADIAN JOURNAL OF ECONOMICS 615-645 (2002).

non-parametric approach to render different conclusions on statistical significance and we were correct. The bootstrapped critical values were about 2.2, so both price coefficients are statistically different from zero regardless of how significance is evaluated. We also bootstrapped the RESET F-statistic, and our conclusions were unchanged.

Table 2. Elasticities, Prices, and Implied Marginal Costs

	Own-Price Demand Elasticity (η_i)	Pre-Merger Price	Marginal Cost	Price-Cost Margin
Verizon	-1.92	45.19	21.65	0.52
Cingular	-2.09	49.33	25.73	0.48
AT&T Wireless	-2.52	59.37	35.81	0.40
Sprint	-2.57	60.52	36.97	0.40
T-Mobile	-1.82	42.97	19.36	0.55
Nextel	-2.71	63.99	40.37	0.37

The own-price and cross-price elasticities are derived from the results of the econometric model summarized in Table 2, with the own-price elasticities of demand being -0.042p_i and the cross-price elasticities being 0.01p_j where p_j is the quality-adjusted price for firm j (each firm has five cross-price elasticities, one for each of its five rivals). The firm-specific elasticities are a function of own-price alone, but the overall demand curve is related (in a statistically significant way) to the prices of rivals (the services are substitutes, as expected).

The estimated elasticities are used to derive marginal costs, based on the first-order condition:

$$1 + \eta_i \left(\frac{p_i - c_i}{p_i} \right) = 0 \,. \tag{3}$$

Armed with the prices, market shares, demand elasticities, and marginal costs, the merger simulation can be conducted. The semi-log demand specification is passed through to the merger simulation, so the relevant first-order conditions reflect this demand model. The additional specifics of the merger simulations are described in the following sections.

2. Simulation of Wireless Prices, No Efficiencies

In our first simulation, AT&T Wireless and Cingular merge, but maintain unique customers bases and separate prices.[29] Incremental costs are assumed to be

[29] It is more profitable for the firm to have two prices rather than one as long as there are variations in demand across customers. Also, there is some evidence that the merged firm intends to operate in the short term using both brands. See E. Morphy, Cingular, *AT&T and AT&T Wireless Resolve Brand Issues*, NewsFactor Network (August 25, 2004) (“"We have worked out an arrangement with AT&T Wireless (NYSE: AWE - news) and Cingular that is designed for us to fully meet our plans

unchanged following the merger. Because of the semi-log demand specification – where elasticities are a function of prices only, not quantities – the optimal prices of Verizon, Sprint, T-Mobile, and Nextel do not change following the merger. This feature of the simulation makes the industry-wide price increases from the merger very conservative since only the merging firms' prices change (the price change is purely unilateral).

In the simulation, following the merger AT&T Wireless and Cingular take into account the cross-price elasticities of demand between them, so post-merger prices for AT&T Wireless and Cingular solve

$$\max \pi^M = \pi^A + \pi^C \tag{4}$$

where π^M represents profit from wireless/mobile services, π^A is profit from AT&T Wireless and π^C is profit from Cingular wireless. The simulation focuses on the joint profit maximization by Cingular and AT&T Wireless, so the computed price increases from this simulation are from the unilateral exercise of market power.

The equation(s) to solve for post-merger prices are

$$D_i(\cdot)\big(1-(p_i-c_i)(-0.0424)\big)+D_j(\cdot)(p_j-c_j)(0.0098)(s_i/s_j)=0 \tag{5}$$

where $D_i(\cdot)=k_i\exp(Z_i)$ is demand for firm i and k_i is the calibration factor that makes D_i exactly equal the observed pre-merger market share and Z_i is the value of the regression equation with inputs for firm i (summarized in Exhibit 1).[30] These equations are solved simultaneously for the merging firms (using Maple mathematics software).

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for serving customers with AT&T-branded wireless services …"). Obviously, if we computed a single price for the merged firm it would lie between the individual firm prices. There is discussion of eliminating overlap in the calling plans of the two carriers, but integrating the other plans. *See* K. Belson and M. Richtel, *For Cingular, Becoming No. 1 Also Poses Risks*, NEW YORK TIMES (Sept. 27, 2004).

[30] To do the simulation, the market shares of AT&T Wireless and Cingular are calibrated by being multiplied by a constant so that, at initial prices, the "predicted" market shares of AT&T and Cingular are exactly equal to 0.175 and 0.192, respectively. This calibration does not affect the elasticities (they are as reported in Table 2). While we do not impose an adding up restriction on market shares, the simulated market shares are very close to 1.00 (ranging from 1.02 to 0.99). So, the model is well behaved in this sense. Linear models, alternately, are generally not so well behaved.

Table 3. Simulated Price Increases

	Pre-Merger Price	Post-Merger Price	% Price Increase
Cingular	$49.33	$54.90	11.3%
AT&T Wireless	$59.37	$68.50	15.4%
Industry Avg.	$52.11	$54.18	4.0%

The pre- and post-merger prices are summarized in Table 3. The simulated price increases are large, with Cingular's price rising 11.3% and AT&T Wireless' price rising by 15.4% as a consequence of the merger. Using calibrated predicted market shares and the post-merger price vector, a price index for wireless service rises from $52.11 to $54.96 (4%) due to the merger induced market share and price changes.[31] Recall that the increase in the wireless industry price index is based solely on the price increases by the merging firms – the prices of the rival firms are unchanged (due to the demand model). Thus, the predicted increase is very conservative.[32]

3. Simulation of Wireless Prices, With Predicted Merger Efficiencies

In the previous simulation, we assumed that marginal costs were unchanged by the merger. By allowing marginal cost to decline for the post-merger firms, the expected price increase from the merger accounting for merger efficiencies can be computed. Based on the testimony filed on behalf of the Cingular and AT&T Wireless, we assume a 1.4% reduction in marginal cost and re-compute the post merger prices.[33] The results are summarized in Table 4.

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[31] Industry wide price was calculated by taking the antilog of the fitted values the regression which are calibrated to sum to one. We then compute a market share weighted average price.

[32] As a rough indicator of how conservative the estimate is, we also simulated the merger using our inputs with a PCAIDS demand model. Other assumptions include a 50% margin for Verizon Wireless, a market demand elasticity of –0.50, and 2003 revenues shares for the firms. The simulated industry price increase was 7.8%.

[33] Gilbert, supra nt. 4, at ¶29 ("Cingular estimates that the efficiencies … will generate operating and capital expense savings of more than $1B in 2006 and more than $2 billion per year in the following years as a merged entity"). Thus, the merger is expected to reduce total costs by about $1B over the next two years (2005, 2006). Merger Guidelines, supra nt. 14 at §3.2. In 2003, the operating cost and capital expenses of Cingular and AT&T Wireless summed to about $35 billion, suggesting a reduction in overall costs of about 1.4% ($1B/$70B). Of course, only reductions in marginal costs are relevant to equilibrium prices and we assume here that all components of total costs are affected by the same amount (1.4%). Also see Affidavit of Steven McGaw filed on Behalf of Cingular and AT&T Wireless, WT Docket No. 04-70 (March 18, 2004), at ¶¶23-27: http://www.fcc.gov/transaction/cingular-att_wireless.html. According to Ralph de la Vega, Chief Operating Officer of Cingular, the integration of the two carriers will probably take two years, suggesting that merger-related savings will not occur in the short term. *See* K. Belson and M. Richtel, supra nt. 29.

Table 4. Simulated Unilateral Price Increases (1.4% Marginal Cost Reduction)

	Pre-Merger Price	Post-Merger Price	% Price Increase
Cingular	$49.33	$54.60	10.7%
AT&T Wireless	$59.37	$67.80	14.2%
Industry Avg.	$52.11	$54.09	3.8%

Assuming a 1.4% marginal cost reduction resulting from the merger, the post-merger prices of Cingular and AT&T Wireless still rise by more than 10%. Cingular's price rises by 10.7% and AT&T Wireless' price rises by 14.2%.[34] The wireless industry price index rises by 3.8%. Recall that the industry price increase assumes that only the prices of the merging firms change, so the predicted increase is very conservative.

4. SIMULATION OF WIRELINE PRICES

As mentioned, the acquisition of AT&T Wireless by Cingular places about 70% of wireless customers in the hands of the dominant wireline telecommunications carriers. Since SBC, BellSouth (Cingular's parent companies) and other ILECs contend that wireless and wireline telecommunications services are substitutes, the merger may have effects on prices in the wireline sector as well.[35] In this section, we describe our methodology to assess the effect of the merger on wireline prices. This analysis should be regarded as somewhat crude, as no data is available for several key inputs to the simulation such as firm-specific cross-price elasticities between wireline and wireless services.

The measurement of wireline price effects is based on the following general conceptual points: 1) wireless and wireline services are assumed to be substitutes; 2) Verizon Wireless is owned by the Bell Operating Company Verizon; 3) Cingular is jointly owned by Bell Operating Companies BellSouth and SBC; 4) the own/cross price elasticity estimates for our companies are independent of wireline price (which varies relatively little among Bell Companies); and 5) the extended

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[34] Even with a large reduction in marginal cost of 5%, Cingular's price rises by 7.4% and AT&T Wireless' price rises by 12.8%.

[35] See, e.g., *Comments of SBC Communications*, CC Docket No. 01-338 at 38 (April 5, 2002) ("wireless networks built to serve high end customers initially are now being used to offer a portable substitute for wireline service.") See also, *Comments of BellSouth Communications*, CC Docket No. 01-338 at 22 (April 5, 2002) (FCC must consider intermodal competition "particularly with regard to wireless substitution" in assessing whether competitors are impaired without access to UNEs). Many of the Bell Company filings in CC Docket No. 01-338 claim that wireless and wireline are effective intermodal competitors. See, *e.g.*, Shelanski Declaration accompanying the comments of SBC and BellSouth in the above-referenced proceeding at ¶ 59 ("Switching Appears Yet More Competitive in Light of Wireless Competition.")

simulation should be logically and mathematically consistent with the previous wireless-only simulation.

For the simulation, we assume the following: 1) Bell Companies already price wireless/wireline services to internalize price effects where relevant; 2) the relevant wireline "price" is not the basic dialtone service price (or POTS, plain old telephone service), but is measured as the revenues on services beyond basic dialtone service less the incremental cost of these additional services. It is these additional services that are unregulated and thus allow for relatively unconstrained price increases. Thus, our wireline "price" is average customer expenditures on wireline services minus the average price for basic residential service.[36] We also express price in terms of a margin and assume the incremental cost of the additional services (long-distance costs and enhanced services) is $4.[37] Prices are summarized in Table 5.[38] For the simulation, we use as price for BellSouth and SBC the line weighted average price (BS 29%, SBC 71%) for wireline service ($13.87).

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[36] Our treatment of wireline price for the simulation is based on the "representative agent" or "average consumer" format. Basic dialtone is not a marginal service for the average consumer. In addition, one must buy dialtone to get all the other services, even long distance, which runs average revenue up to almost twice the basic monthly service rate. Furthermore, estimated elasticities for basic dialtone are estimated to be very small (typically reported to be less than 0.05), and this cannot be used in any profit maximization calculus of first-order conditions. Our approach is also reasonable in that any finding of a price increase for wireline will result in no implied disconnections from the local switched networks.

[37] Average long-distance usage is about 90 minutes and the average transport/access price is assumed to be about $0.02 per minute. See *Trends in Telephone Service,* Federal Communications Commission (May 2004), at Table 14.1. In states where forward looking cost estimates for enhanced features are estimated, the prices are typically about $1-$3 for all features or $0.10 to $0.30 for individual features. For a bundle of all features (excluding voicemail), the cost estimates in the BellSouth region are as follows: Alabama ($1.98), Florida ($2.17), Georgia ($0.78), Mississippi ($2.56), North Carolina ($2.40), South Carolina ($3.04). Individual features such as Caller ID and Call Waiting have costs of $0.22 and $0.03 in Alabama. In California, most features have costs of about $0.17 each. Of course, feature penetration is not 100%, so only some portion of the costs will apply to the average consumer. Most likely, $4 is a high estimate of the incremental cost of these services (if cost is $0.20 and penetration is 30%, then the average cost is $0.06). As the margin on additional services increases (declines), the price effect in wireline will be large (smaller).

[38] Average revenue data is provided by Comptel/Ascent, *Consumers Spent $11 Billion Less in 2003 Than Before Competition*, Comptel/Ascent News Release (March 15, 2004): http://www.comptelascent.org/news/recent-news/031504.html. Average basic dialtone rates are from B. J. Gregg, *A Survey of Unbundled Element Prices in the United States* (July 2003): http://www.nrri.ohio-state.edu.

Table 5. Wireline Simulation Inputs

	Avg. Revenue per Line	Basic Residential Price	Net Price	Wireless/Wireline Revenues
BellSouth	$39.24	$24.20	$14.94	0.31
SBC	$34.28	$20.85	$13.43	0.27
Verizon	$38.04	$25.28	$12.78	0.57

The simulation is based on the assumption that Cingular, which is jointly owned by BellSouth and SBC, operates to maximize joint profits of the owners and thus would solve

$$\max \ \pi = \pi^M + \pi^W \tag{6}$$

over relevant wireless and wireline prices where π^M is mobile profits and π^W is wireline profits. After the merger, BellSouth and SBC now own both AT&T Wireless and Cingular, so they internalize this in their pricing. We assume the cross-price elasticities between wireline (W) and wireless (M) services are $\eta_{WM} = 0$, $\eta_{MW} = 0.10$, where η_{WM} (η_{MW}) is the cross-price elasticity between the quantity of wireline (wireless) services with respect to the wireless (wireline) price. These assumptions imply that the mobile price of a firm does not affect the firm's wireline demand, but the firm's wireline price affects the firm's wireless demand as substitutes (though the effect is assumed to be small).[39] Also, if $\eta_{WM} > 0$, the simulation would produce even higher prices for wireless and wireline services. Given the specification of cross-price elasticities, extending the simulation to include the wireline market has no additional effect on wireless prices ($\eta_{WM} = 0$). However, the merger will cause an increase in wireline prices. We note that this set of assumptions allows us to use our previously calculated marginal costs for wireless services.

Prior to performing the simulation, we use the first-order conditions for Verizon and Cingular to infer the implied firm elasticities of demand for wireline services other than basic dialtone. For Verizon and BellSouth/SBC, we solve

$$\left(\frac{R_W}{R_M}\right)\left[1+\left(\frac{P_W - C_W}{P_W}\right)\eta_W\right]+\left(\frac{P_M - C_M}{P_M}\right)\eta_{MW} = 0 \tag{7}$$

[39] The rationale is that monopoly power is nearly complete in wireline services, but limited by some competition in wireless. Thus, if a firm raises its wireless price, it loses sales to other wireless competitors, not the local wire network. On the other hand, if Verizon, say, or BellSouth or SBC raises wireline prices, they are in effect raising the whole market price of wireline and the only alternative is wireless service. These assumed elasticities also imply that wireline service would not be in the antitrust market for wireless services.

where R is revenues from wireline (W) and wireless (M) services, and the inputs for the equation are summarized above. The solution for Verizon is η_W = -1.51 and for BellSouth/SBC is η_W = -1.43, reasonable figures under the circumstances.

With these inputs, we can now simulate the effect of the AT&T Wireless and Cingular merger on wireline prices. For the simulation, we assume that there are no incremental cost savings and the ratio of wireline to wireless revenues is unchanged (or changes very little). Wireline prices are affected only in the BellSouth and SBC service regions. We also note that: 1) wireline prices are unchanged for Verizon; 2) mobile prices rise only for AT&T and Cingular as before; 3) the only "new" price is for BellSouth/SBC wireline services. Using the elasticity η_W = -1.43, the simulation predicts a wireline price increase of 2.4%, rising from $13.87 to $14.20 per customer-month.

This 2.4% price increase is a very conservative estimate of the effect of an enlargement of mobile operations owned by Bellsouth and SBC since it results solely from the very small cross-price elasticity in which wireline price increases raise mobile demands (η_{MW} = 0.10). As either η_{MW} or η_{WM} rises, the price effects of the merger rise. For wireless to be effective intermodal competition, η_{MW} would presumably have to be much larger than 0.10.[40]

5. Other Effects of the Merger

Our simulation encompasses the plausible consequences of a small, positive cross elasticity of demand on the pricing of wireline services by SBC and BellSouth. However, these firms sell a number of additional, significant products to both consumers and rivals (such as CLECs and rival wireless carriers) that may also be affected by the change in incentives created by the merger. Although we are unable to directly evaluate these effects, it is apparent that they might be important in any evaluation of the social consequences of this merger. From a theoretical point-of-view, the presence of a positive cross-price elasticity (regardless of size) will result in price increases for the conventional reasons, and the merger exacerbates these effects because the prices of all substitute services will be strategic complements for the firms. For example, the Bell Companies sell network elements to rivals, who use these functions to sell communications services in competition with the Bell. By increasing the prices of these elements, the Bell Companies may increase the residual demand for their own services.

Likewise, Bell Companies sell special access services (and/or UNE-Transport) to their wireless rivals. The cost to the Bell Company of selling such services to rivals includes the opportunity cost arising from the use of such services by the rival to

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[40] For an analysis of intermodal competition between wireless and wireline services, see Phoenix Center, *Fixed-Mobile "Intermodal" Competition in Telecommunications: Fact or Fiction*?, PHOENIX CENTER POLICY BULLETIN No. 10 (March 30, 2004): http://www.phoenix-center.org/.

serve customers that would otherwise be the customer of the Bell's affiliated wireless carrier.[41] This opportunity cost rises with the profitability of wireless service and the market share of the Bell-affiliated wireless carrier. Therefore, the higher market share and profitability of wireless service resulting from the merger encourages the Bell Companies to increase prices for special access/transport services (or any other input sold by the Bell Company to its wireless rivals). The same logic applies with equal force to roaming agreements between wireless carriers, since roaming agreements improve the quality of a rival's service. The merger may lead to higher prices in roaming agreements, if not to the elimination of such agreements altogether.

The increase in profitability for Bell-affiliated wireless carriers caused by raising rivals' costs by increasing transport and roaming prices can be crudely illustrated using our merger simulation. For example, assume that by increasing the prices for transport facilities and/or roaming, the marginal costs of the smaller wireless carriers (T-Mobile, Nextel, and Sprint) are increased by 5%. This increase in marginal cost causes post-merger prices of these carriers to increase by the amounts provided in Table 6. Note that the industry price increase is now 4.6% (versus 4% from the default scenario) since the merger-induced price increases are not restricted to the merging firms.[42] Because the higher prices charged by the smaller carriers result in larger market shares for Cingular and AT&T Wireless, the profits of the two merging firms rise as a result of raising rivals costs. An index of profitability for the two merging firms rises by 17.5% (above the profit effects of the merger alone) as a consequence of the raising rivals' cost strategy.[43]

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[41] The economics of selling inputs to rivals is presented in T. R. Beard, G. S. Ford, and L. W. Spiwak, PHOENIX CENTER POLICY PAPER NO. 12, *Why ADCo? Why Now? An Economic Exploration into the Future of Industry Structure for the "Last Mile" in Local Telecommunications Markets*, 54 FEDERAL COMMUNICATIONS LAW JOURNAL 421-460 (2002) (http://www.law.indiana.edu/fclj/pubs/v54/no3/spiwak.pdf).

[42] If we let only the marginal cost of Nextel and T-Mobile rise, then the industry average price increases by 4.4%.

[43] The index of profitability is computed by multiplying each firm's calibrated market share by the margin of price over cost. Shares are calibrated by ensuring that the sum of predicted market shares equals one. Further, since the industry price rises, we adjust the post-merger profit to account for the reduction in total industry quantity using an industry demand elasticity of –0.5. Without raising the cost of rivals, the profits of the merging firms rise by 14.8%.

Table 6. Simulated Price Increases with Raising Rivals Costs
(5% Increase in Marginal Cost)

	Pre-Merger Price	Post-Merger Price	% Price Increase
Cingular	$49.33	$54.60	10.7%
AT&T Wireless	$59.37	$68.50	15.4%
Sprint	$60.52	$62.40	3.1%
T-Mobile	$42.97	$43.91	2.2%
Nextel	$63.99	$65.97	3.1%
Industry Avg.	$52.11	$54.52	4.6%

We emphasize that the absence of a formal treatment of these effects in our analysis does not imply these effects are unimportant or absent. Indeed, these effects should be carefully considered in any evaluation of this proposed business combination.

6. Consumer Welfare Effects

The Antitrust laws are designed primarily to protect consumers. Our simulations suggest that the AT&T Wireless/Cingular merger harms consumers in two ways: 1) increased prices for wireless services and 2) increased prices for wireline services (in the SBC/BellSouth regions). Crude estimates of the consumer welfare effects of the merger can be computed as follows.

For wireline services, Bellsouth and SBC serve about 80.7 million wireline access lines. Using a constant elasticity calibrated demand so $q = k \cdot \exp(.) \cdot p_W^{-1.43}$, a change in price from $13.87 to $14.20 yields a welfare change of

$$\begin{aligned} \Delta CS &= 3.5 \cdot 10^9 \cdot \int_{13.87}^{14.20} s^{-1.43} ds \\ &= \$26{,}425{,}000 / month \end{aligned} \tag{8}$$

or about $317,000,000 per year in the BellSouth and SBC regions.[44]

For wireless services, the effects of the merger are obviously much larger. Assuming a wireless industry elasticity of –0.50 and a price increase from $52.11 to $54.18, the change in consumer welfare is about $227M per month, or about $2.7B annually.[45] Recall, however, that the industry price increase assumes that only the prices of merging firms increase, so the estimate of consumer welfare effects is very conservative. In our raising rivals' cost scenario, the 5% increase in rivals' marginal

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[44] "Calibration" refers to a selection of values for k so that the quantity of services bought equal the observed quantity (80.7 million lines) at current prices.

[45] Consumer welfare changes are computed using pre- and post-merger industry prices, a total market size of 110.3 million lines, and an industry elasticity of –0.5. Calibration is used to ensure that the total quantity is 110.3 million lines at an industry price of $52.11.

cost increases the consumer welfare loss by about 16% above the $2.7B from the benchmark case.

III. Conclusions

In this paper, we have presented a merger simulation of the Cingular/AT&T Wireless merger. The simulation was designed to predict price changes in both wireless and wireline markets, though the price effects for wireless are admittedly crude and limited to residential services only. In wireless, the unilateral price effects are large, exceeding 10% even after accounting for expected merger efficiencies. Consumer surplus in wireless markets is predicted to decline by $2.7 billion despite the very conservative nature of our simulations. In wireline markets, prices are predicted to rise by 2.4%, with about $300 million in annual consumer surplus losses. Our merger simulation is also used to show the possible price, profit, and consumer welfare impacts of a raising rivals' costs strategy effectuated in part by the wireline parents of the merging wireless firms. The profit and welfare effects are shown to be sizeable.

Our results are generally consistent with an earlier study of the merger that used an event study and merger simulation to predict the effects of the merger. That study predicted price increases in the 5% to 8% range, and our results are close to those figures. To date, the only formal quantitative analyses of the merger, including this one, predict rather large price increases even accounting for expected efficiencies.

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Richard P. Saba, Dept. of Economics, Auburn University, and Applied Economic Studies.

September 30, 2004

EXHIBIT 1.

Regression Results		
	Coefficients (Robust t-stat)	Mean [st. dev.]
Constant	-1.258 (-1.54)	…
p_i	-0.042 (-5.98)	51.44 [8.95]
$\Sigma(s_i/s_j)p_{-i}$	0.010 (4.84)	257.11 [19.77]
POPS	-0.004 (-3.37)	228.5 [34.74]
DTM	-1.254 (-6.26)	0.17 [0.38]
MS	…	0.17 [0.08]
ln(MS)	…	-1.91 [0.53]
R^2	0.87	
Obs.	24	

EXHIBIT 2.

Firm	Year	Service Revenues	Subscribers	POPS	J.D. Power Quality Index
Verizon	2003	20336	37.5	248	104.00
Cingular	2003	14223	24.0	211	101.00
AT&T Wireless	2003	15659	22.0	165	100.00
Sprint	2003	11548	15.9	244	95.00
T-Mobile	2003	6755	13.1	273	94.00
Nextel	2003	9892	12.9	230	103.00
Verizon	2002	17747	32.5	248	104.00
Cingular	2002	13922	21.9	211	101.00
AT&T Wireless	2002	14483	20.9	165	100.00
Sprint	2002	10867	14.8	244	95.00
T-Mobile	2002	4245	8.7	273	94.00
Nextel	2002	8186	10.6	230	103.00
Verizon	2001	16011	29.4	248	104.00
Cingular	2001	13229	21.6	211	101.00
AT&T Wireless	2001	12532	18.0	165	100.00
Sprint	2001	8577	13.6	244	95.00
T-Mobile	2001	2926	5.8	273	94.00
Nextel	2001	6575	8.7	230	103.00
Verizon	2000	13000	26.8	248	104.00
Cingular	2000	10424	19.7	211	101.00
AT&T Wireless	2000	9374	15.1	165	100.00
Sprint	2000	5453	9.5	244	95.00
T-Mobile	2000	1520	3.9	273	94.00
Nextel	2000	4995	6.7	230	103.00

The individual firm's Form 10-Ks and 10-Qs provide all the quantity and price data. Prices are computed as the annual service revenues divided by end-of-year subscriber lines. Quality data is provided by *J.D. Power and Associates Reports: Verizon Wireless Ranks Highest in Network Quality Performance* (July 29, 2003). POPS data is provided by J. Rockhold, *2002 Who Gets Out Alive*? WIRELESS REVIEW (December 1, 2002): http://www.findarticles.com/p/articles/mi_m0GTV/is_23_18/ai_80848046/print. The data is provided in Exhibit 2.

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of:	)	
	)	
AT&T Wireless Services, Inc.,	)	WT Docket No. 04-70
Transferor, and Cingular Wireless LLC,	)	
Transferee,	)	
	)	
Applications for Transfer of Control	)	
of Licenses and Authorizations	)	

REPLY COMMENTS OF THE COMPTEL/ASCENT ALLIANCE

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May 20, 2004

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SUMMARY

The proposed merger of Cingular Wireless and AT&T Wireless is not in the public interest and approval should be denied. This acquisition will stifle competition and create additional and unnecessary obstacles for both wireline and wireless carriers. The Applicants fail to bear their burden under Sections 310(d) and 214 of the Communications Act of 1934, as amended, to demonstrate that the proposed transfer of control will serve the public interest. Key to the Commission's public interest analysis is whether the transaction will have significant anticompetitive effects. This analysis is not limited to the discrete market in which the transaction will take place, but all related markets and submarkets that may be affected by the merger, in order to further the procompetitive objectives of the Communications Act.

Of primary concern is the anticompetitive and discriminatory effect the proposed transaction will create in the special access markets. Because interconnection is essential to competition in both the wireless and wireline market sectors, a further breakdown of competition in the special access markets will be particularly damaging. The proposed transaction will give the Applicants, and their ILEC parents, a significantly larger amount of market control than they currently enjoy, and will serve to further concentrate the market for special access services, which already is burdened by anticompetitive and discriminatory conduct. SBC in particular has already demonstrated its ability to impose anticompetitive terms on its special access customers, who have no other choice than to interconnect with SBC. The proposed transaction will not only harm competing carriers, but will harm consumers and the market as a whole.

In addition, the acquisition will also allow the Applicants and their ILEC parents to package bundles of service that no other competitor will be able to match. Congress and the Commission have previously recognized the potential for anticompetitive effects as the result of a vertical relationship between companies. Both SBC and BellSouth already sell bundled services, which include long distance service and voicemail in the same package, and Applicants make no attempt to refute the contention that they intend to exploit their new alliance by selling bundles of wireline, broadband and wireless services.

Moreover, competitors cannot count on procompetitive statutes and regulations to prevent the discrimination that will result from this merger. Existence of statutes and regulations do not prevent them from being violated; in fact, the Commission has previously found SBC responsible for "willful and repeated" violations of merger conditions, despite the existence of regulatory restraints. Also, the regulations themselves are under constant assault by the ILECs; SBC was instrumental in eviscerating the Commission's recent Triennial Review Order. CompTel believes the Commission must eliminate the use of all anticompetitive restraints in the provision of special access as a condition to approving this merger.

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of:	)	
	)	
AT&T Wireless Services, Inc.,	)	WT Docket No. 04-70
Transferor, and Cingular Wireless LLC,	)	
Transferee,	)	
	)	
Applications for Transfer of Control	)	
of Licenses and Authorizations	)	

REPLY COMMENTS OF THE COMPTEL/ASCENT ALLIANCE

The Competitive Telecommunications Association ("CompTel")/Association of Communications Enterprises ("ASCENT") Alliance ("CompTel/ASCENT") hereby supports the Petitions to Deny filed by Thrifty Call, Inc. ("Thrifty Call") and Consumer Federation of America/Consumers Union ("CFA/CU"), and opposes and replies to Cingular Wireless Corporation ("Cingular") and AT&T Wireless Services, Inc.'s ("AWS's") (together, the "Applicants") *Joint Opposition to Petitions to Deny and Comments* filed in the above-captioned matter. Cingular and AWS have failed to establish that the acquisition will enhance competition; specifically, they failed to adequately rebut Petitioners' argument that this merger will provide the Applicants and their ILEC parents with even greater incentive to discriminate in the provision of special access and bundled services. Applicants further failed to demonstrate that the acquisition will serve the public interest. If this acquisition is approved, it will only serve to better facilitate collusion among now-rival companies, and will further concentrate the market for these essential services.

I. Applicants Fail to Bear Their Burden of Proving that the Acquisition Serves the Public Interest.

Under Sections 310(d) and 214 of the Communications Act of 1934, as amended, the Applicants must demonstrate that the proposed transfer of control will serve the public interest. In discharging these statutory responsibilities, the Commission weighs the potential public interest harms of the proposed transactions against the public interest benefits to ensure that, on balance, the transfers of control serve the public interest, convenience and necessity.[1] In making this determination, the Commission considers the competitive effects of the proposed transfers and whether such transfers raise significant anticompetitive issues. Consideration of the competitive effects of the proposed transfer is a key factor in the Commission's public interest analysis.[2] This analysis appropriately reviews and considers the competitive effect on all markets and submarkets within the Commission's purview.[3] The Commission also considers the efficiencies and other public interest benefits that are likely to result from the proposed transfers

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1 *Voicestream Wireless Corporation, Powertel, Inc., Transferors, and Deutsche Telekom AG, Transferee, for Consent to Transfer Control of Licenses and Authorizations Pursuant to Section 214 and 310(d) of the Communications Act and Petition for Declaratory Ruling Pursuant to Section 310 of the Communications Act*, Memorandum Opinion and Order, 16 FCC Rcd 9779, para. 17 (2001).

2 *General Motors Corporation and The News Corporation Limited General Motors Corporation and Hughes Electronics Corporation, Transferors And The News Corporation Limited, Transferee, For Authority to Transfer Control*, Memorandum Opinion and Order, para. 16, FCC 03-330, MB Docket No. 03-124 (Jan. 2004) ("*DirecTV Order*").

3 *In the Matter of GE American Communications, Inc., Application for Consent to Transfer of Earth and Space Station Licenses of Columbia Communications Corp.*, DA 00-1332, para. 5 (June 27, 2000),"[O]ur public interest analysis is not, however, limited by traditional antitrust principles . . . . It also encompasses the broad aims of the Communications Act. . . . To apply our public interest test, then, we must determine whether the merger violates our rules, or would otherwise frustrate our implementation or enforcement of the Communications Act and federal policy. That policy is, of course, shaped by Congress and deeply rooted in a preference for competitive processes and outcomes."

of control of the licenses and authorizations.[4] The applicants bear the burden of proving that the transaction, on balance, serves the public interest.[5]

II. This Acquisition Will Enhance the Ability of the Merged Firm to Lessen Competition In the Wireless Market Through Coordinated Interaction.

Both CFA/CU and Thrifty Call identify aspects of the vertically integrated firm which plausibly will enhance the merged firm's ability to coordinate prices in the downstream wireless markets. CFA/CU points to expanded spectrum capacity which could be used to raise the cost of roaming to rivals who fail to price rationally in the wireless market.[6] Similarly, Thrifty Call identifies the dominant position of SBC and BellSouth in the market for a critical input as a factor that, combined with the significant concentration in the wireless retail market, will enhance the merged firm's ability to facilitate coordination in that market.[7]

Both petitioners raise concerns that are a primary focus of the Horizontal Merger Guidelines analysis—the ability of the merged firm to lessen competition by enhancing the ability of firms in the post merger market to coordinate pricing behavior.[8] The merging parties, however, have (wrongly, in CompTel's opinion) interpreted the concerns of the petitioners as solely focused on the potential of the post-merger firm to "foreclose" competition by driving competitors out of business, or some such unilateral tactic. While these concerns seem to have

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4 *Global Crossing Ltd. (Debtor-in-Possession), Transferor and GC Acquisition Limited, Transferee, Applications for Consent to Transfer Control of Submarine Cable Landing Licenses, International and Domestic Section 214 Authorizations, and Common Carrier and Non-Common Carrier Radio Licenses, and Petition for Declaratory Ruling Pursuant to Section 310(b)(4) of the Communications Act*, Order and Authorization, 18 FCC Rcd 2031, paras. 16-24 (2003).

5 *DirecTV Order* at para. 15.

6 *CFA/CU Petition to Deny* at 11.

7 *Thrifty Call Petition* at 17-18.

8 See Merger Guidelines, Section 2.1 ("A merger may diminish competition by enabling the firms selling in the relevant market more likely, more successfully, or more completely to engage in coordinated interaction that harms consumers.")

more merit than the parties give them credit, the parties have, again, ignored their burden to prove that the merger is in the *public* interest and does not lessen *competition*.

Thus, curiously, in their attempts to "rebut" the observations of CFA/CU and Thrifty Call, the merging parties lead off their defense with statements of other wireless industry participants, all of which seem supportive of the merger.[9] That the other industry participants believe that a better qualified price leader, better able to help rationalize industry pricing, is good for the industry is not surprising. What is surprising, however, is that the parties believe these statements actually support their argument that the merger is in the public interest—particularly, when these statements are all consistent with the self interest of industry members who will be better able to coordinate their market behavior.[10]

Similarly, the parties' reliance on Cingular's relatively low share of new customers in many markets is entirely consistent with the role of Cingular as a potential price leader in these markets.[11] Certainly, with such low shares the parties cannot suggest that Cingular was a particularly aggressive competitor, or "maverick" pricer, to begin with. The combination of AWS and Cingular will, for various reasons, be even better equipped to perform the role of market coordinator.

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9 *Joint Opposition* at 35-36.

10 The statement by the Deutsche Telecom CEO that the merger will increase T-Mobile's chances of exceeding its revenue growth forecast seems especially consistent with a firm that expects more rational, and less competitive, pricing in the newly-structured market.

11 *Joint Opposition* at 37.

A. Control of Critical Inputs Enhances Applicants' Ability to Coordinate Behavior of Downstream Rivals.

Amazingly, Applicants argue that it is inappropriate to deal with special access concerns in the context of a merger proceeding.[12] By focusing exclusively on the ability of SBC and BellSouth to discriminate against rivals of their downstream affiliate, their argument completely misses the point. Central to the Commission's public interest evaluation of a transfer of control is whether the transaction will raise significant anticompetitive issues.[13] As noted previously, the question of whether a merger enhances the likelihood of post-merger coordination in any market is a central concern, and the enhancement of the merged firm's ability to detect "cheating" is as important as the firm's ability to subsequently punish such cheating.[14]

1. Requirements Contracts for Special Access Enhance the Merged Firm's Ability to Detect and Punish Cheating.

A particularly good example of how the merged firm will be better able to monitor and punish cheating in the downstream market for wireless service can be seen in a recent contract tariff filed by SBC, and included here as ***Attachment A***. In addition to the ordinary high volumes, excessive terms, and unreasonable termination liabilities imposed by

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12 *In the Matter of AT&T Wireless Services, Inc. and Cingular Wireless Corporation Seek FCC Consent to Transfer Control of Licenses and Authorizations*, WT Docket No. 04-70, Joint Opposition to Petitions to Deny and Comments, pg. 37 (May 13, 2004) ("*Joint Opposition*").

13 *Infra*, note 2.

14 Merger Guidelines, Section 2.1 ("Successful coordinated interaction entails reaching terms of coordination that are profitable to the firms involved and an ability *to detect and punish* deviations that would undermine the coordinated interaction. Detection and punishment of deviations ensure that coordinating firms will find it more profitable to adhere to the terms of coordination than to pursue short-term profits from deviating, given the costs of reprisal. In this phase of the analysis, the Agency will examine the extent to which post-merger market conditions are conducive to reaching terms of coordination, *detecting deviations from those terms*, and punishing such deviations.") (emphasis added)

most ILEC "contract tariffs,"[15] this tariff includes a special plan, whereby the purchaser can accrue maximal discounts (50% on the carrier's total purchases) if the customer migrates at least 4% of its total volume from competitive sources.[16] To see how this contract would work, consider two wireless carriers, both of which have and equal amount of special access demand with SBC—for example, $1 million per month. However, one of the wireless carriers currently purchases some of its special access demand from competitive sources, and can thus migrate special access circuits to SBC. The carrier who migrates circuits from competitive sources will pay $500,000 per month instead of the $1 million per month paid by the carrier who either does not have enough competitive business to migrate, or chooses not to migrate this business. Given the already-high volume commitments that carriers must make in order to get the best prices, four percent of this already-high amount is likely to constitute almost all of a carrier's special access demand. Indeed, as the Applicants note, "AWS today purchases the vast majority of its special access services from ILECs rather than the 'competitive wholesalers' that Thrifty suggests will be foreclosed."[17]

The more of a given wireless carrier's demand provided by SBC or BellSouth, the easier it is for the merged firm to monitor "cheating" by rivals of the downstream wireless affiliate. This is because any rival firm offering lower prices will be growing its special access demand. The ILEC monopolies, through the use of "requirements" contracts like the contract tariff described here, are thus better able to monitor coordination in a more concentrated wireless

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15 "Typically, such arrangements require AWS to purchase substantial volumes of special access services over 3 to 5 year terms. Onerous penalties attach for failure to meet the volume and term commitments and effectively lock AWS into the ILECs' special services." *Comments of AT&T Wireless, Petition of AT&T for Rulemaking to Reform Regulation of ILEC Special Access Rates*, RM No. 10593 (Dec. 2, 2002) at 8.

16 See SBC Contract Tariff, Section 22.20.3(c).

17 *Joint Opposition* at n. 133, p. 40.

industry by "rewarding" downstream firms who submit to "monitoring" and punishing those that do not. Moreover, the upstream monopolies, in the present case, have targeted those wireless rivals of the merged entity that have shown the greatest willingness to develop a cost structure, and supply sources, independent from the integrated SBC-BellSouth-Cingular-AWS.

Finally, regarding the merged firm's ability to punish cheaters, it is immaterial whether special access price increases, or access degradation, are alone sufficient to provide a suitable "punishment" mechanism, but the Applicants must explain why their excess spectrum capacity—as described by CFA/CU—in conjunction with their special access monopoly is insufficient to discipline "maverick" firms who do not cooperate with the downstream affiliate. Significantly, though, with respect to the contract described above, over time – as wireless competitors to the merged firm migrate all their special access to SBC – the rivals' input costs will double when SBC has completely eliminated competitively supplied special access to the wireless rivals of Cingular-AWS.

B. The Commission's Nominal Authority to Regulate Special Access Is Immaterial To Applicants' Ability to Facilitate Coordination By Use of Their Monopoly Over A Critical Input.

Interconnection to the landline telephone network is key to competition in nearly all sectors of the market, including the wireless sector.[18] Applicants attempt to diminish and ignore the legitimate concerns of Thrifty Call simply by invoking general statutory provisions as if they are magical incantations to ward off scrutiny. Instead of addressing Thrifty Call's concerns, the Applicants have failed to offer any explanation of how anything but the Applicants' good nature

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18 Congress has found that "the right to interconnect an important one which the Commission shall seek to promote, since interconnection serves to enhance competition and advance a seamless national network." Interconnection Between Local Exchange Carriers and Commercial Mobile Radio Service Providers; Equal Access and Interconnection Obligations Pertaining to Commercial Mobile Radio Service Providers, *Notice of Proposed Rulemaking*, 11 FCC Rcd 5020, para. 96 (1995) (*citing* House Report on H.R. 2264 at 261 (1993)).

will constrain them from exercising their enhanced ability and incentive to use their special access monopoly anticompetitively. Applicants cite to statutory provisions and performance metrics, and claim that the existence of these measures alone is sufficient to safeguard the market from discriminatory and anticompetitive conduct.[19] Their argument is illogical. The existence of a law does not prevent it from being broken.

In hiding behind general statutory provisions, the Applicants conveniently fail to acknowledge that they have virtually complete discretion in setting the prices and terms of their special access services. In fact, CompTel (along with Applicant AWS and others) has asked the DC Circuit to issue a Writ of Mandamus to compel the FCC to actually enforce the provisions regarding just and reasonable pricing of special access that the Applicants point to as sufficient to constrain their acknowledged market power.[20] Moreover, while there are indeed general rules prohibiting SBC and BellSouth from engaging in unfair discrimination, these same parties have steadfastly fought any attempts to get them to publicly report provisioning performance so these provisions could be easily enforced. Thus, discrimination in interconnection arrangements, which SBC, for example, has proven capable of in the past,[21] continues to threaten competition.[22]

III. Applicants Have Failed to Demonstrate that the Merger Will Not Harm Competitive Providers of Special Access.

In another instance where the Applicants are quick to diminish, but slow to account for, legitimate concerns expressed by Thrifty Call, the Applicants generally assert that this merger

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19 *Joint Opposition*, pgs. 37-38.

20 *In re AT&T Corp., et al, Petitioners*, No. 03-1397 (D.C. Circuit 2003). The court has ordered briefing on the merits, and is now considering this petition.

21 *Core Communications, Inc. v. SBC Communications Inc., Memorandum Opinion and Order*, 18 FCC Rcd 7568, para. 41 (2003).

22 *In the Matter of AT&T Wireless Services, Inc. and Cingular Wireless Corporation Seek FCC Consent to Transfer Control of Licenses and Authorizations, Petition to Deny of Thrifty Call, Inc.*, WT Docket No. 04-70, pg. 18 (May 3, 2004) ("*Thrifty Call Petition*").

can have no anticompetitive effect on competitive providers of special access service.[23] However, it is far from clear to CompTel (and should be to the Commission as well) how this should be so abundantly clear given the size of this acquisition and the types of anticompetitive vertical restraints currently employed by SBC and BellSouth, and described in Section II. A. 1. above. CompTel represents many competitive providers of wholesale transport services, and disagrees strongly with the Applicants' conclusory dismissals of the concerns expressed by Thrifty Call.

The Applicants first attempt to dismiss Thrifty Call's concern by reciting some general observations about vertical mergers from *The Antitrust Paradox*.[24] However, as CompTel has earlier explained, what we are talking about in this case is a vertical merger further exacerbating the already anticompetitive effects of aggressive vertical restraints. The effects of this particular vertical restraint, in combination with the outright elimination of an aggressive independent purchaser of competitive access services, could, indeed, foreclose business from competitive access providers and thereby limit the ability of these competitors to expand. It is well-recognized in the antitrust literature that the anticompetitive potential of vertical restraints/combinations increases when a dominant upstream supplier also controls (through restraint or combination) a significant share of the downstream market as well.[25]

It is unavailing to simply point out, as Applicants do, that the dollar volume of special access purchases supplied by AWS and other wireless carriers is small compared to the total special access market, controlled by the ILECs. Indeed, without knowing the importance, based on the current "flow share" of competitive access purchases in the relevant markets by AWS and

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23 *Joint Opposition*, pp. 40-41.

24 *Id.* at 40.

25 *See, e.g.*, HERBERT HOVENKAMP, ANTITRUST LAW, PARA. 1802d5 (2002).

the other non-SBC, or BellSouth, affiliated wireless carriers it would seem impossible—using the Applicants' favored method of analysis—to rule out the importance of competitive wireless carriers (including AWS) to the ability of competitive providers of special access to grow their business.

In other words, given the anticompetitive nature of the SBC special access contracts, it is clear that the only volume presently available to competitive access providers in SBC's markets will come from growth telecommunications industries, such as wireless. This is because, given the vertical restraints imposed by SBC, it is unlikely that traditional IXC's, whose revenue continues to erode, will be able to meet their commitments to SBC, migrate circuits from competitors, and still have enough access growth to continue to initiate new special access purchases from competitive providers. Thus, comparing AWS' competitive access purchases to the base of special access revenue most likely understates the importance of AWS to competitive providers in the relevant markets.[26]

IV. The Acquisition Will Promote Anticompetitive Effects in the Market for Many Bundled Services by Giving SBC and BellSouth Market Power Unmatchable by Anyone But Verizon.

Applicants claim that "bundling is procompetitive,"[27] however they fail to acknowledge or address the unprecedented synergies that will be generated by this acquisition. Applicants' assertion that "[t]his transaction will not have any adverse impact on the bundling of wireless

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26 In fact, there is evidence to suggest that AWS—relative to other carriers—was able to divert a substantial amount of purchases to competitive access providers. For example, AWS was able to purchase around 10% of its demand from competitors, while another wireless rival had only been able to divert 4% of its demand to competitors. See presentation of AWS in RM No. 10593, at slide 4, December 18, 2002.

27 *Joint Opposition* at 41.

services with other telecommunications services"[28] oversimplifies the real risk of anticompetitive harm due to the vertical relationship between the companies.

Despite Applicants' claims, not all bundling is procompetitive. Economists believe that when vertically related firms enter into long term or exclusive contracts that inefficiently deter or foreclose entry to a market, consumers may be harmed.[29] Congress also has recognized the potential for anticompetitive effects, and has found that "vertically integrated program suppliers ha[ve] the incentive and ability to favor their affiliated cable operators over nonaffiliated cable operators and programming distributors using other technologies."[30] Moreover, the Commission also recognizes the potential for anticompetitive conduct as the result of a vertical relationship between companies.[31] This acquisition will create an unprecedented vertical relationship among ILECs with an already huge market share that must not be ignored.

As Thrifty Call pointed out in its *Petition to Deny*,[32] local wireline and wireless customer bases and associated facilities can and will be used by Applicants to create bundled service offerings that no other provider can match. In fact, both local and wireless services are already sold by SBC in bundles, which include long distance service and voicemail in the same

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28 *AT&T Wireless Services, Inc., Transferor, and Cingular Wireless LLC, Transferee, Applications for Transfer of Control of Licenses and Authorizations*, WT Docket No. 04-70, File Number: 0001656065, pg. 41 (submitted March 18, 2004) ("*Application*").

29 *In re Promotion of Competitive Networks*, WT Docket No. 99-217, para. 28. (Oct. 25, 2000).

30 *DirecTV Order* at 41 (although "the competitive landscape had changed for the better since 1992, but [ ] vertically integrated programmers continued to have the incentive and ability to favor affiliated cable operators over other MVPDs").

31 *Id.* at para. 124. *See also Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations from Tele-Communications, Inc., Transferor to AT&T Corp., Transferee*, Memorandum Opinion and Order, 14 FCC Rcd 3160, para. 126 (Feb. 18, 1999) (AT&T-TCI could inflict competitive harm by offering a package of bundled products if rivals were unable to offer a similar package).

32 *Thrifty Call Petition*, pg. 19.

package.[33] There is no reason to believe Applicants will not soon bundle wireline, broadband and wireless services. In fact, as recently as yesterday, the Washington Post quoted market analysts on the importance of and the ability to bundle services, particularly the ability to bundle wireline services with wireless services.[34] In their *Joint Opposition*, Applicants make weak assertions that such bundling would not harm competition, but they do not refute Thrifty Call's contention that they intend to sell bundles of wireline, broadband and wireless services.

V. The Commission Must Eliminate the Use of All Anticompetitive Vertical Restraints in the Provision of Special Access by SBC and BellSouth as a Condition to Approving this Merger.

CompTel has, in these comments, demonstrated that the public interest concerns raised by petitioners Thrifty Call and CFA/CU are substantial, deserve consideration, and have not been adequately refuted by the Applicants. Absent conditions to correct these problems, the Commission would be justified in denying the Applicants' request.

Accordingly, CompTel believes that the only way the Commission could potentially approve this merger would be if the Commission would make a tangible commitment to establishing a strong and competitive market for special access provided by competitive facilities providers. The most effective step the Commission could take in this direction would be to eliminate the use of anticompetitive term and volume contracts by all purchasers of SBC and BellSouth special access. The Commission should require SBC and BellSouth to immediately reduce by half the volume commitments in their highest volume contracts, eliminate any

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33 *See* www.bellsouth.com; www.sbc.com for various, combined packages offered. Also see http://www.sbc.com/gen/press-room?pid=4800&cdvn=news&newsarticleid=20648, *Michigan Wins FCC Long Distance Approval* (SBC announces that it will soon offer a full bundle of telecommunications services to customers in nine of the 13 states in which it operates, along with a new service, MinuteShare, "created with BellSouth and Cingular Wireless to enable residential consumers to share a single bucket of minutes for calls made from either their SBC or BellSouth wireline and Cingular wireless phones").

34 Washington Post, Page E05, *AT&T Back in Wireless Business*, (May 19, 2004).

termination liability that prevents customers who have performed under a contract for at least a year from grooming circuits to competitive providers, and eliminate the use of "exclusive" or "requirements" type contracts that encourage "all or nothing" discounting, or provide any non-cost based discounts for the migration of traffic from competitive carriers.

VI. CONCLUSION

For the foregoing reasons, the Commission should deny the merger, or order the requested relief as a condition to approving the merger.

Respectfully submitted,

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May 20, 2004

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22. Pricing Flexibility Contract Offerings (N)

22.20 Contract Offer No. 20 – MVP DS1, DS3 and OCN Service Offer

22.20.1 General Description

MVP DS1, DS3 and OCN Service Offer ("Contract Offer No. 20") is an access discount pricing plan for MVP Customers where subscription is required in four of the SBC Companies: Ameritech Operating Companies, Southwestern Bell Telephone Company, Southern New England Telephone Company and Pacific Bell Telephone Company. This Offering provides a 50% discount off recurring tariff rates for DS1, DS3, and OCN Services that meet the Eligibility Criteria as described in Section 22.20.3 and are subject to the Terms and Conditions as described in Section 22.20.4. Customers will continue to receive MVP discounts provided that they meet their MVP contract obligations in Section 20 of F.C.C. No. 2 Tariff.

Customers must commit to a Current Annual Revenue Commitment (CARC), as described in Section 22.20.5. To ensure that the customer will meet the CARC by end of year 2004 and 2005, the Telephone Company will review revenue quarterly. In the event the customer is not meeting their CARC, the customer will be required to remit payments, via the quarterly True-Up process described in Section 22.20.6, otherwise termination liabilities will apply.

This Contract Offer No. 20 will only be available between November 18, 2003 through January 18, 2004.

22.20.2 Services Available Under Contract Offer No. 20

(A) This Contract Offer No. 20 offers discounts on the recurring rates for the Price Flex eligible DS1, DS3 and OCN Access Services (hereafter referred to as Subject Services) contained in the Tariff Sections listed below, and only in the Metropolitan Statistical Areas (hereafter referred to as MSAs) defined in Section 22.20.4(C).

Service	General / Basic Description	Phase 1 MSAs Rates and Charges	Phase 2 MSAs Rates and Charges
DS1 and DS3 Services	7.2.9	7.5.9	21.5.2.7
Optical Carrier Network (OCN) Point-to-Point Service	7.2.10	7.5.10	21.5.2.7

(N)

(This page filed under Transmittal No. 1369)

22. Pricing Flexibility Contract Offerings (N)

22.20 Contract Offer No. 20 – MVP DS1, DS3 and OCN Service Offer (Cont'd)

22.20.2 Services Available Under Contract Offer No. 20 (Cont'd)

(B) Purchase of the Subject Services listed above pursuant to Contract Offer No. 20 are subject to the specific terms and conditions of Section 22.20.4. Additionally purchase of the services listed above pursuant to Contract Offer No. 20 are also subject to the general terms and conditions of F.C.C. Tariff No. 2 as set forth in Sections 2-General Regulations, 5-Ordering Options for Switched & Special Access Service, 6- Switched Access Service, 7-Special Access Service and 13-Additional Engineering, Additional Labor & Miscellaneous Services. Such general terms and conditions may be modified through the filing of tariff changes at any time during the Term Period, however, such changes will not change the regulations described in Contract Offer No. 20.

Subject Services continue to be governed by the respective terms and conditions of the MVP provisions in section 20, F.C.C. Tariff No. 2 except as noted herein.

22.20.3 Eligibility Criteria for Contract Offer No. 20

(A) Contract Offer No. 20 is only available to Customers who are currently subscribing to MVP, in the following Telephone Companies:

- Ameritech Operating Companies (AIT) F.C.C. No. 2 Section 19 (N)
- Southwestern Bell Telephone Company (SWBT) F.C.C. No. 73 Section 38; and (Nx)
- Pacific Bell Telephone Company (PBTC) F.C.C. No. 1 Section 22.

(B) Customer must also concurrently subscribe to the identical contract offers of Contract Offer No. 20 pursuant to the following tariffs:

- SWBT Tariff F.C.C. No. 73, Section 41, Contract Offer No. 15;
- PBTC Tariff F.C.C. No. 1, Section 33, Contract Offer No. 20; and
- SNET Tariff F.C.C. No. 39, Section 25, Contract Offer No. 1. (Nx)

(N)

(C) A minimum of 4% of the Customer's Current Annual Revenue Commitment, as described in Section 22.20.5, must come from services previously provided by a carrier other than the Ameritech Operating Companies and it's affiliates. This 4% level will be measured at the end of the Term Period, however, the 4% requirement may be demonstrated at any time during the contract period. Customer must adhere to the following Sections (1) and (2). (N)

(xx) Issued under authority of Special Permission No. 03-100 of F.C.C

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22. Pricing Flexibility Contract Offerings (Cont'd) (N)

22.20 Contract Offer No. 20 – MVP DS1, DS3 and OCN Service Offer (Cont'd)

22.20.3 Eligibility Criteria for Contract Offer No. 20 (Cont'd)

(C) (Cont'd)

(1) Customer must provide documentation to demonstrate that the Subject Services have been converted from another carrier to Telephone Company services. Documentation may include but is not limited to: circuit detail records, invoices, and coordinated orders to move the service. The Telephone Company is willing to review other documents that the Customer may deem appropriate to meet this criteria, however only to the extent that it does not result in breach of any non-disclosure agreements which may govern the distribution of such information.

(2) If Customer fails to reach the 4% requirement as measured at the end of the Term Period, the Customer will be deemed to have terminated Contract Offer No. 20 and termination liabilities will apply as set forth in Section 22.20.7.

22.20.4 Terms and Conditions

(A) Term Period

The contract Term Period will commence on the date the Telephone Company receives a completed Letter of Authorization and expires on December 31, 2005 ("Term Period").

This offer is not renewable.

(N)

(N)

22. Pricing Flexibility Contract Offerings (Cont'd)

22.20 Contract Offer No. 20 – MVP DS1, DS3 and OCN Service Offer (Cont'd)

22.20.4 Terms and Conditions (Cont'd)

(B) Application

Subject Services to which the Customer already subscribes as of the commencement of the Term Period will receive discounts effective upon the commencement of the Term Period.

Subject Services purchased after the commencement of the Term Period will receive the discounts only after the service has been provisioned.

Monthly billing credits will be issued for every month in which the Subject Services are purchased in compliance with the eligibility criteria in Section 22.20.3. The Credits will be applied within 30 days after each billing cycle.

(C) This Contract Offer No. 20 is only available for Subject Services located in the following MSAs:

Pricing-Flexibility MSAs: Chicago, Illinois; Detroit/Ann Arbor, Michigan; Cleveland/Lorain/Elyria, Dayton, and Columbus, Ohio.

(D) Contract Offer No. 20 provides a discount of 50% off the monthly recurring tariff rates listed in Section 22.20.2 (A) for existing and new Subject Services.

Example:

Subject Services Monthly Recurring Charge	= $2000
50% Discount	= $1000

(E) Customer agrees to maintain a Current Annual Revenue Commitment (as described in Section 22.20.5) for the calendar years of 2004 and 2005.

(F) Customer agrees to a quarterly true-up as described in Section 22.20.6 for the calendar years of 2004 and 2005.

(N)

22. Pricing Flexibility Contract Offerings (Cont'd)

22.20 Contract Offer No. 20 – MVP DS1, DS3 and OCN Service Offer (Cont'd)

22.20.5 Current Annual Revenue Commitment (N)

Under Contract Offer No.20, Customer will commit to maintain a Current Annual Revenue Commitment (CARC). The CARC will be established using either the Customer's current MVP MARC or an Annual Revenue Commitment calculated as outlined below in Section 22.20.5(A), whichever is greater. The CARC will be established as soon as the Telephone Company receives the Letter Of Authorization from the customer.

(A) Determining the Annual Revenue Commitment

The Customer's Annual Revenue Commitment is calculated based on the total of the previous three (3) months recurring billing for all MVP qualified access services prior to any MVP discounts (as listed in F.C.C. 2, Section 19.2), multiplied by four (4). The Annual Revenue Commitment is calculated as follows:

Previous Three (3) Months Recurring Billing X 4 = Annual Revenue Commitment

(B) The CARC will not change during the contract Term Period.

(C) If the Customer fails to achieve the CARC on either of the contract anniversary dates (December 31, 2004 or December 31, 2005), and fails to remit the annual projected gap payment, the Customer will be deemed to have terminated its participation in Contract Offer No. 20 and termination liability charges will apply as set forth in Section 22.20.7. (N)

22. Pricing Flexibility Contract Offerings (Cont'd) (N)

22.20 Contract Offer No. 20 – MVP DS1, DS3 and OCN Service Offer (Cont'd)

22.20.6 Quarterly True-Up

To ensure that the customer will meet the CARC by the end of year 2004 and 2005, the Telephone Company will review revenues quarterly. In the event that the Customer has an estimated shortfall, the Customer is required to remit Quarterly Gap Payments as described below. Quarterly is defined as consecutive three (3) month periods commencing January 1, 2004. The process of remitting payments to eliminate the Annual Projected Gap is referred to as the True-Up process.

The Telephone Company will calculate the Customer's Annual Projected Gap (if any) on a quarterly basis. The Annual Projected Gap is the CARC, less any annual projected MVP discounts, less actual annualized revenues. Actual annualized revenue is the Customer's actual billed amount to date, annualized to determine end of year estimated revenues. Actual annualized revenues will include any previous quarterly gap payment that the Customer has made. For this calculation, the actual annualized revenues are calculated after discounts from this Contract Offer No. 20, and any other applicable credits or discounts (i.e., MVP) have been applied.

Example A: Annual Projected Gap calculation at end of 1st quarter

CARC	= $12,000,000
Less projected MVP discounts	= $ 2,000,000
Sub total	= $10,000,000
Less actual quarterly revenue ($1.5M) X 4 (annualized)	= $ 6,000,000
Annual Projected Gap	= $ 4,000,000

(A) If there is a positive Annual Projected Gap as measured above for the quarter, the Customer agrees to make Quarterly True-Up payments. Quarterly True-Up payments will be calculated using the percentages in section 22.20.6 (B) and will be applied to the Annual Projected Gap to determine the gap payment. See example B in Section 22.20.6.

(B) Quarterly True-up payments will be calculated utilizing the following percentiles:

Quarter	Percent
1st	0%
2nd	25%
3rd	66%
4th	100%

(N)

22. Pricing Flexibility Contract Offerings (Cont'd) (N)

22.20 Contract Offer No. 20 – MVP DS1, DS3 and OCN Service Offer (Cont'd)

22.20.6 Quarterly True Up (Cont'd)

(B) (Cont'd)

Example B: Quarterly True-up

1st Quarter
Actual revenue 1st Quarter:

January	= $ 400,000
February	= $ 500,000
March	= $ 600,000
Total	= $1,500,000

CARC	= $12,000,000
Less projected MVP discount	= $ 2,000,000
Sub total	= $10,000,000
Less actual 3 months revenue ($1.5M) x 4 (annualized):	= $ 6,000,000
Annual Projected Gap	= $ 4,000,000

$4,000,000 x 0% = $0.00 Quarterly True-up payment

2nd Quarter
Actual revenue 1st and 2nd Quarter:

January	= $ 400,000
February	= $ 500,000
March	= $ 600,000
April	= $ 600,000
May	= $ 700,000
June	= $ 700,000
Total	= $3,500,000

CARC	= $12,000,000
Less projected MVP discount	= $ 2,000,000
Sub total	= $10,000,000
Less actual 6 months revenue ($3.5M) x 2 (annualized):	= $ 7,000,000
Annual Projected Gap	= $ 3,000,000

$3,000,000 x 25% = $750,000 Quarterly True-up payment

(N)

22. Pricing Flexibility Contract Offerings (Cont'd) (N)

22.20 Contract Offer No. 20 – MVP DS1, DS3 and OCN Service Offer (Cont'd)

22.20.6 Quarterly True Up (Cont'd)

(B) (Cont'd)

Example B: Quarterly True-up (Cont'd)

3rd Quarter

Actual revenue 1st, 2nd and 3rd Quarter

January	= $ 400,000
February	= $ 500,000
March	= $ 600,000
April	= $ 600,000
May	= $ 700,000
June	= $ 700,000
July	= $ 500,000
August	= $ 600,000
September	= $ 665,038
Total	= $5,265,038

CARC	= $12,000,000
Less projected MVP discounts	= $ 2,000,000
Sub total	= $10,000,000
Less (9 months actual revenue + 2nd Quarter Gap payment) x 1.33:	
($5,265,038 + $750,000) x 1.33	= $ 8,000,000
Annual projected Gap	= $ 2,000,000

$2,000,000 x 66% = $1,320,000 Quarterly True-up payment (N)

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22. Pricing Flexibility Contract Offerings (Cont'd) (N)

22.20 Contract Offer No. 20 – MVP DS1, DS3 and OCN Service Offer (Cont'd)

22.20.6 Quarterly True Up (Cont'd)

(B) (Cont'd)

Example B: Quarterly True-up (Cont'd)

Quarter 4

Actual revenue 1st, 2nd, 3rd and 4th Quarter

January	= $ 400,000
February	= $ 500,000
March	= $ 600,000
April	= $ 600,000
May	= $ 700,000
June	= $ 700,000
July	= $ 500,000
August	= $ 600,000
September	= $ 665,038
October	= $ 500,000
November	= $ 550,000
December	= $ 614,962
Total	= $6,930,000

CARC	= $12,000,000
Less projected MVP discounts	= $ 2,000,000
Sub total	= $10,000,000
Less (12 months actual revenue + 2nd & 3rd Quarter Gap payment):	
$6,930,000 + $750,000 + $1,320,000	= $ 9,000,000
Annual Projected Gap	= $ 1,000,000

$1,000,000 x 100% = $1,000,000 Quarterly True-up payment

In the example above at the end of the 4th Quarter the Customer's actual revenue plus the Customer's Quarterly Gap payments, plus projected MVP discounts will equal the CARC.

$6,930,000 + $750,000 + $1,320,000 + $1,000,000 + $2,000,000 = $12,000,000

(C) SBC will provide customer a quarterly gap payment bill (if applicable) within 30 days after the end of the quarter.

(D) If at the end of either contract anniversary date (December 31, 2004 or December 31, 2005) the customer has exceeded their CARC (actual revenue + gap payments) and have made Quarterly Gap Payments, SBC will credit the customers account the amount exceeding the CARC, but not greater than the total gap payments the customer has made. (N)

(N)

22. Pricing Flexibility Contract Offerings (Cont'd)

22.20 Contract Offer No. 20 – MVP DS1, DS3 and OCN Service Offer (Cont'd)

22.20.7 Termination Liability Charges

If the Customer terminates service before the completion of the term for any reason whatsoever the customer agrees to pay the Telephone Company termination liability charges described below. These charges shall become due as of the effective date of the cancellation or termination. The Customer must provide written notification 60 days prior to the desired date of termination to the Telephone Company.

If the Customer fails to meet any of the eligibility criteria in section 22.20.3 or fails to maintain any of the Terms and Conditions in section 22.20.4, the Customer will be deemed to have terminated its participation in Contract Offer No. 20 and termination liability charges will apply as stated below and will be payable pursuant to F.C.C. No. 2 , Section 2.4.

Customers termination liability shall be equal to:

(A) 100% of all Discounts received under this Contract Offer No. 20 during the six (6) months immediately prior to the date of termination, plus;

(B) 25% of the CARC for each year in the remaining portion of the Term Period.

Any previous gap payments paid by the customer will be forfeited.

Example C:

The Customer signs up for Contract Offer No. 20 on November 1, 2003. The Customer terminates its participation in Contract Offer No. 20 effective September 15, 2004. The termination liability charge that would apply is calculated as follows:

Annual CARC = $12M
Monthly CARC = $12M / 12 months = $1M
Number of months remaining in contract = 15.5
Remaining value of CARC = 15.5 x $1M = $15.5M
25 % of remaining value of CARC = .25 x $15.5M = $3.875M
March 2004 - August 2004 discounts = $500K

Total Termination Liability Charge = $3.875M + $500K = $4.375M

(N)