

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

In the Matter of)
)
Transfer of Control Filed by SBC) WC Docket No. 05-65
Communications Inc. and AT&T Corp.)

**COMMENTS ON BEHALF OF
THE NEW JERSEY DIVISION OF THE RATEPAYER ADVOCATE**

SEEMA M. SINGH, ESQ.
RATEPAYER ADVOCATE
31 Clinton Street, 11th Floor
Newark, NJ 07102
(973) 648-2690 - Phone
(973) 648-2193 - Fax
www.rpa.state.nj.us

On the Comments:

Christopher J. White, Esq.
Deputy Ratepayer Advocate
Ava-Marie Madeam, Esq.
Assistant Deputy Ratepayer Advocate

Economic Consultants:

Susan M. Baldwin
Sarah M. Bosley

Date: April 25, 2005

Table of Contents

I.	INTRODUCTION.	1
A.	Interest of the Ratepayer Advocate in the Instant Proceeding.	2
B.	Overview/Background	4
C.	Relationship of the Proposed Transaction to the Development of Competition	5
II.	SUMMARY OF THE RATEPAYER ADVOCATE’S RECOMMENDATIONS.	7
A.	Introduction	7
B.	Impact of the Proposed Merger on Competition	7
1.	SBC’s enormously successful entry into new markets underscores its ability to re-monopolize local and long distance markets.	11
2.	In assessing the plausibility of the Applicants’ intention to compete out of region, the FCC should examine SBC’s actual out-of-region entry.	12
3.	SBC’s apparent compliance with the bare bones out-of-region entry conditions the FCC imposed on its merger with Ameritech does not provide compelling evidence of likely concerted future out-of-region efforts.	14
4.	If the past is a guide, the likelihood of benefits flowing to mass market consumers is negligible.	16
5.	Absent enforceable regulatory conditions, it is unlikely that SBC will pursue residential and small business consumers.	20
C.	LOSS OF AT&T AS A REGULATORY “ACTIVIST”	23
1.	The proposed merger would create a regulatory vacuum, and diminish the comprehensiveness of state and federal investigations of telecommunications policy.	23
D.	SYNERGIES	24
1.	If the FCC approves the proposed transaction, it should increase the X factor in its price cap regulation accordingly.	24

2.	In assessing the potential benefits and harms from the proposed transaction, the FCC should examine SBC’s home-region behavior.	27
E.	CONDITIONS	28
1.	The FCC should impose conditions to mitigate and/or prevent harms to consumers.	28
2.	The FCC should impose conditions to enhance and/or increase the likelihood of benefits for consumers.	30
III.	CONCLUSION.	30

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

In the Matter of)	
)	
Transfer of Control Filed by SBC)	WC Docket No. 05-65
Communications Inc. and AT&T Corp.)	DA 05-656

COMMENTS OF THE NEW JERSEY DIVISION OF THE RATEPAYER ADVOCATE

I. INTRODUCTION.

On February 22, 2005, SBC Communications Inc. (“SBC”) and AT&T Corp. (“AT&T”) (collectively, the “Applicants”) submitted an application with the Federal Communications Commission (“FCC” or “Commission”) for approval to transfer control of AT&T’s licenses and authorizations to SBC. Under the proposed merger, AT&T would become a wholly owned subsidiary of SBC. The Applicants submitted a public interest statement and seven declarations in support of their proposed transaction.¹ The New Jersey Division of the Ratepayer Advocate (“Ratepayer Advocate”) submits these initial comments in response to the pleading cycle established by the FCC on March 11, 2005, regarding the proposed transaction.²

^{1/} Merger of SBC Communications Inc. and AT&T Corp., *Description of the Transaction, Public Interest Showing, and Related Demonstrations*, filed with the Federal Communications Commission, dated February 21, 2005 (“Public Interest Statement”), including Declarations of James S. Kahan, Christopher Rice, Thomas Horton, John Polumbo, Hossein Eslambolchi, Dennis W. Carlton and Hal S. Sider, and Marius Schwartz.

^{2/} Federal Communications Commission, “Commission Seeks Comment on Application for Consent to Transfer of Control filed by SBC Communications Inc. and AT&T Corp.,” Public Notice released March 11, 2005.

A. Interest of the Ratepayer Advocate in the Instant Proceeding.

The Ratepayer Advocate is an independent New Jersey State agency that represents and protects the interests of all utility consumers, including residential, business, commercial, and industrial entities. The Ratepayer Advocate participates actively in relevant federal and state administrative and judicial proceedings. The above-captioned proceeding is germane to the Ratepayer Advocate's continued participation and interest in implementation of the Telecommunications Act of 1996.³ The New Jersey Legislature has declared that it is the policy of the State to provide diversity in the supply of telecommunications services, and it has found that competition will promote efficiency, reduce regulatory delay, and foster productivity and innovation and produce a wider selection of services at competitive market-based prices.⁴ The proposed merger of SBC and AT&T – two telecommunications carriers that presently serve New Jersey's consumers as competitive local exchange carriers ("CLECs"), competing with other RBOCs – directly affects the structure of telecommunications markets, and the prices that consumers pay for telecommunications services.

The Ratepayer Advocate brings a unique perspective to this proceeding as a result of its participation in, among others, the following related regulatory proceedings in which the Ratepayer Advocate conducted detailed analyses of granular competitive data and assessed the status of local mass market competition in New Jersey: the investigation by the FCC and the New Jersey Board of Public Utilities ("Board") of Verizon's Section 271 application, the FCC's Triennial Review Order remand

^{3/} Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996 Act). The 1996 Act amended the Communications Act of 1934. Hereinafter, the Communications Act of 1934, as amended by the 1996 Act, will be referred to as the 1996 Act, or "the Act," and all citations to the 1996 Act will be to the 1996 Act as it is codified in the United States Code.

^{4/} N.J.S.A. 48:2-21.16(a)(4) and 48:2-21.16(b)(1) and (3).

proceeding,⁵ and the Board's "impairment" and hot cut proceeding.⁶

In assessing the impact of the proposed merger between SBC and AT&T on consumers and on competition, it is essential to recognize that the merger is not an "isolated" merger but rather is the beginning of another wave of market concentration. The proposed merger of Verizon Communications Inc. and MCI Inc. raises similar concerns. Although, in this investigation, the FCC must consider the merits of the specific transaction that the Applicants propose, determining whether the SBC/AT&T merger is in the public interest depends partly on an assessment of the market structure as it is potentially evolving.

The merger of SBC and AT&T – two telecommunications giants, each with more than a century of experience – would affect significantly the prices that consumers pay for telecommunications services and the prospects for competition in various markets. The Ratepayer Advocate has a critical interest in this proceeding because the issues to be decided herein will affect all ratepayers, regardless of the carrier from which they take service. The Ratepayer Advocate urges the Commission to impose conditions upon the Applicants to (1) protect consumers sufficiently from anti-competitive behavior, excessive rates for non-competitive services, and service quality deterioration and (2) ensure that mass market consumers gain more from the merger than the "trickle-down" benefits that the Applicants describe. Absent such conditions, there is insufficient information to deem the transaction to be in the public interest.

^{5/} Unbundled Access to Network Elements, Review of the Section 251 Unbundling Obligations of Local Exchange Carriers, Federal Communications Commission WC Docket No. 04-313, CC Docket No. 01-338, Initial Comments of the Division of the Ratepayer Advocate and Affidavit of Susan M. Baldwin on behalf of the New Jersey Division of the Ratepayer Advocate, filed October 4, 2004; Reply Comments of the Division of the Ratepayer Advocate, filed October 19, 2004.

^{6/} In the Matter of the Implementation of the Federal Communications Commission's Triennial Review Order, New Jersey Board of Public Utilities Docket No. TO03090705, Testimony of Susan M. Baldwin on behalf of the New Jersey Division of the Ratepayer Advocate, February 2, 2004.

B. Overview/Background

The Applicants anticipate that their merger, if approved, would be completed in late 2005 or early 2006.⁷ SBC would acquire AT&T and, at merger closing, a wholly-owned subsidiary of SBC would be merged with and into AT&T. Each share of common stock of AT&T would be converted into 0.77942 shares of SBC common stock and AT&T would pay a \$1.30 per share special dividend to its shareholders. AT&T would continue to hold the stock of its subsidiaries after the merger and would continue to hold its own FCC authorizations it held prior to the merger.⁸

SBC is a voice, data, and Internet services provider for residential, business, and government customers, predominantly in its 13-state incumbent operating territory. SBC serves 52.4 million access lines and has 5.1 million DSL lines in service. SBC also holds a 60 percent economic and 50 percent voting interest in Cingular Wireless, which serves 49.1 million wireless customers. SBC reported \$40.8 billion in operating revenues⁹ and AT&T reported \$30.5 billion in operating revenues in 2004.¹⁰ Financial data reported to the Securities and Exchange Commission (“SEC”) in the SBC Prospectus/AT&T Proxy Statement indicates operating revenues of \$69.5 billion for 2004 and over 210,000 employees for the combined telecommunications giant.¹¹

It has been many years since the FCC has investigated a proposed transaction of this magnitude

^{7/} Prospectus of SBC Communications Inc., Proxy Statement of AT&T Corp., S-4, filed with the Securities and Exchange Commission, March 11, 2005 (“SBC Prospectus/AT&T Proxy Statement”), at 5.

^{8/} Public Interest Statement, at 11.

^{9/} SBC Prospectus/AT&T Proxy Statement, at 10.

^{10/} *Id.*, at 11.

^{11/} *Id.*, at 12.

and significance, and it is the first time that the FCC has considered a merger between a Bell operating company and AT&T. The last wave of mergers, during the 1990s, (between NYNEX Corporation and Bell Atlantic Corporation; Bell Atlantic Corporation and GTE Corporation; SBC Communications Inc. and Southern New England Telecommunications Corporation; SBC Communications Inc. and Pacific Telesis Group; and SBC Communications Inc. and Ameritech Corporation) resulted in substantial market concentration. The Ratepayer Advocate recognizes that this investigation encompasses an assessment of a single proposed merger, but nonetheless urges the FCC to consider the merits of the transaction within the context of the status of the telecommunications industry. The loss of AT&T (a carrier with unique “brand” recognition”) as an independent CLEC, as a regulatory “activist,” and as an SBC rival would be monumental, irrevocable and potentially a major setback to competition. The wave of mergers that occurred during the 1990s differed fundamentally from the two mega-mergers now before the FCC.¹² SBC and Verizon Communications Inc. (“Verizon”) have each obtained interLATA authority throughout their “home” regions. Their positions of dominance are greater than they have ever been since divestiture as a result of the Bells’ leveraging their incumbent local positions into the bundled services market and simultaneously fortifying walls around their local markets. The SBC/AT&T merger would further entrench SBC’s dominance and diminish the prospects for competition.

C. Relationship of the Proposed Transaction to the Development of Competition

Extending the sobering image depicted in Commissioner Adelstein’s statement dissenting from the FCC’s *TRO Remand Order*, the FCC’s approval of the proposed merger between SBC and AT&T

^{12/} Commission Seeks Comment on Applications for Consent to Transfer of Control filed by Verizon Communications Inc. and MCI, Inc., WC Docket No. 05-75, Public Notice, DA 05-762, released March 24, 2005.

would “pound in” yet another nail in the coffin for local competition.¹³ AT&T is indisputably a potential competitor in the local market. Although AT&T announced its plan to exit the mass market almost one year ago,¹⁴ AT&T has far greater resources than most CLECs with which to enter local markets dominated by incumbent local exchange carriers (“ILECs”). The proposed transaction would eliminate AT&T irrevocably as a potential competitor to incumbent carriers throughout the nation including SBC. Although one can only speculate about AT&T’s chances of success in local mass markets, if it had not merged nor exited the market, it is clear that the proposed multi-billion dollar transaction does not bode well for consumers. Furthermore, even if one believes AT&T’s claim that, if it did not merge, it either could not or would not compete in the local market,¹⁵ AT&T’s monumental decision to merge with its rival does not hold out promise for the prospect of local competition. That AT&T, a nation-wide carrier with seemingly the greatest potential to compete head-on with the Bells, would throw in the towel casts doubt on the potential for effective local competition.

^{13/} Statement of Commissioner Jonathan S. Adelstein, Dissenting Re: *Unbundled Access to Network Elements* (WC Docket No. 04-313); *Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers* (CC Docket No. 01-338), December 15, 2004, at 1.

^{14/} “AT&T Posts 80% Drop in Net, Confirms Consumer Retreat,” *The Wall Street Journal*, July 23, 2004, page A11; AT&T announced its plan to pull out of seven states. “AT&T: No New Home Customers in 7 States,” Reuters, June 23, 2004, http://news.yahoo.com/news?tmpl=story&u=/nm/20040623/bs_nm/telecoms_att_local_dc.

^{15/} See, e.g., Declaration of John Polumbo (SBC/ATT), at paras. 22-23.

II. SUMMARY OF THE RATEPAYER ADVOCATE'S RECOMMENDATIONS.

A. Introduction

The Ratepayer Advocate urges the FCC to consider carefully and thoroughly the implications of the proposed transaction on consumers. Based on the precarious status of competition in New Jersey, the Ratepayer Advocate's experience with previous mergers between telecommunications carriers, and the Applicants' filing, the Ratepayer Advocate has assessed the likelihood of harm and benefits the proposed merger between SBC and AT&T would likely yield. Where feasible, this section discusses proposed conditions to mitigate and/or reduce the possibility of harm and to enhance and/or increase the possibility of benefits occurring.

B. Impact of the Proposed Merger on Competition

In order to assess the impact of the proposed merger on the *future* of competition, it is important to determine the *present* status of competition in relevant markets. Despite the efforts of state and federal regulators to eliminate market barriers, successful entry to ILEC-dominated markets is not easy and requires CLECs to overcome (1) customer inertia, (2) economic and operational impediments, and (3) more than a century of dominance by incumbents in their "home" operating territories (Verizon NJ in New Jersey's local markets). Based on the FCC's statistics, Verizon NJ dominates the vast majority of the local market either directly through its own retail services or indirectly by leasing its wholesale facilities to its competitors (*i.e.*, the non-facilities-based competition that occurs through resale, UNE-P, and UNE loop).¹⁶ Even if viewed solely on a retail basis (which would be misleading because it would mask CLECs'

^{16/} CLECs owned fewer than 106,000 (or less than 2%) of the total 6.5-million end-user switched access lines in service in New Jersey as of June 30, 2004. Federal Communications Commission, Wireline Competition Bureau, Industry Analysis and Technology Division, *Local Telephone Competition: Status as of June*

reliance on the incumbent carrier's facilities), Verizon NJ dominates 80 percent of New Jersey's local markets.¹⁷

Of course, in the wake of the FCC's Triennial Review Remand Order ("TRRO"),¹⁸ end-user lines provided by CLECs through unbundled network elements ("UNEs") are already declining. Verizon reported providing 93,000 fewer UNE-P lines in the fourth quarter of 2004 compared to the third quarter 2004.¹⁹ SBC's UNE-P lines declined by 283,000 in the fourth quarter of 2004, following a decline of 192,000 in the third quarter of 2003 and the BellSouth and Qwest report similar results.²⁰ It is unlikely that all of the UNE-P lines will migrate to UNE-L or that CLECs currently serving customers via UNEs can continue economically to serve those customers. In both the FCC's and New Jersey's impairment proceedings, the Ratepayer Advocate demonstrated indisputably that UNE-L-based entry is scarce in rural

30, 2004, (December 2004), at Table 10: "CLEC-Reported End-User Switched Access Lines by State (as of June 30, 2004)" and Table 6: "End-User Switched Access Line Served by Reporting Local Exchange Carriers (As of June 30, 2004)."

^{17/} *Id.*, at Table 6. CLECs provided 1,319,513 end-user access lines, the vast majority (987,393) provided through the use of UNEs. CLECs also relied on resold lines (226,662) and provided just 105,458 facilities-based lines. *Id.*, at Table 10.

^{18/} *Unbundled Access to Network Elements; Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, FCC WC Docket No. 04-313; CC Docket No. 01-338, Order on Remand, rel. February 4, 2005 ("Triennial Review Remand Order" or "TRRO").

^{19/} "Verizon Reports Strong 4Q and 2004 Results, Driven by Wireless Revenue Growth, Solid Cash Flows and Margins," Verizon Press Release, January 27, 2005, available at <http://investor.vzmultimedia.com/news>; Verizon Investor Quarterly, 2004, released January 27, 2005.

^{20/} SBC Investor Briefing, No. 245, January 26, 2005. BellSouth provided 1,972,000 UNE-P lines in the fourth quarter 2004 down from 2,082,000 in third quarter 2004 (a 5.3% decline). Qwest noted in its fourth quarter earnings report that it benefitted in the fourth quarter because of a "reduction in UNE competition." "The company continues to make significant inroads in stemming competitive loss from facilities-based competitors. Resold lines declined 28,000 sequentially as changes in the regulatory environment have reduced competition from UNE resellers." BellSouth Corporation Consolidated Statements of Income; "Qwest Improves in Key Growth Areas and Sees Margin Expansion in Fourth Quarter 2004," Qwest News, February 15, 2005; Qwest Communications International Inc. Selected Consolidated Data available at www.qwest.com/about/index.html.

areas, and is also scarce in many suburban and urban areas.²¹ Furthermore, the FCC adopted an overly optimistic view of the likelihood that CLECs will deploy their own facilities to serve the mass market in the wake of the dismantling of unbundling requirements.²² The recent spate of merger announcements underscores the fallacy in the FCC's wishful thinking about the industry's investment decisions post-*TRRO*. AT&T, a giant among CLECs in the mass market, has chosen to merge with an incumbent rather than continue to compete in the face of recent regulatory decisions. As AT&T explained in a New Jersey proceeding, "AT&T announced in the summer of 2004 that it would no longer actively market traditional wireline services to consumer and small-business customers as a result of FCC decisions that hinder AT&T's ability to compete for the customers using unbundled network elements."²³

The Applicants contend that the merger does not result in the loss of a potential competitor because, if the merger did not occur, AT&T would not actively compete in the mass market, and therefore its presence would not constrain SBC.²⁴ Furthermore, according to the Applicants, if the merger did not

^{21/} Unbundled Access to Network Elements, Review of the Section 251 Unbundling Obligations of Local Exchange Carriers, Federal Communications Commission WC Docket No. 04-313, CC Docket No. 01-338, Initial Comments of the Division of the Ratepayer Advocate and Affidavit of Susan M. Baldwin on behalf of the New Jersey Division of the Ratepayer Advocate, filed October 4, 2004, at paras. 87-97; Confidential Attachments (see, e.g., Confidential Attachment Exhibit SMB-12 (showing UNE-P as a percentage of total lines on a wire center basis in the Newark and Camden MSAs); Confidential Attachment SMB-13 (showing mass market local competition in the Newark and Camden MSAs that is entirely UNE-P based); Confidential Attachments SMB-14 and SMB-15 (showing competition based on UNE-Loop on a wire center basis).

^{22/} *TRRO*, at para. 2. "In this Order, the Commission takes additional steps to encourage the innovation and investment that come from facilities-based competition. ... This approach satisfies the guidance of courts to weigh the costs of unbundling, and ensures that our rules provide the right incentives for both incumbent and competitive LECs to invest rationally in the telecommunications market in the way that best allows for innovation and sustainable competition." *Id.*

^{23/} In the Matter of Verizon New Jersey, Inc., Revision of Tariff BPU NJ No. 2, Providing for a Revenue Neutral Rate Restructure Including a Restructure of Residence and Business Basic Exchange Service and Elimination of \$.65 Monthly Credit BPU Docket No. TT04060442, AT&T Response RPA-ATT-2.

^{24/} Declaration of Dennis W. Carlton and Hal S. Sider, at paras. 51-52.

occur, AT&T would raise prices to its consumers, whereas, the Applicants contend that SBC would not be likely to raise rates to its newly acquired customers.²⁵ The Applicants contend that AT&T has irrevocably exited from the mass market (lacking the employees as a result of an intentional reduction in infrastructure, employees, and marketing resources).²⁶

The Ratepayer Advocate urges the FCC to seek detailed information from the Applicants about their respective competitive successes in local and bundled services markets:

- AT&T's actual entry into markets in SBC's home states, both before and after AT&T announced its exit plans.
- AT&T's actual entry into markets in states where SBC is an actual or potential out-of-region competitor (*e.g.*, New Jersey), both before and after AT&T announced its exit plans.
- SBC's market shares (local and bundled) in its home states.
- SBC's market shares (local and bundled) in out-of-region states.

In SBC's out-of-region states the proposed alliance holds out the promise of more vigorous competition with RBOCs. If the proposed merger provides an opportunity for SBC to compete successfully with other RBOCs in out-of-region mass markets, such head-to-head rivalry between two large Bells could mitigate the loss of AT&T as a competitor. However, for mass market customers nationwide to realize benefits from such competition, firm, enforceable commitments are essential to ensure that SBC competes vigorously in all out-of-region markets.

^{25/} *Id.*, at paras. 54, 105-106.

^{26/} Polumbo (SBC/ATT), at paras. 22-23.

1. SBC's enormously successful entry into new markets underscores its ability to re-monopolize local and long distance markets.

In assessing whether the proposed multi-billion-dollar transaction serves the public interest, the FCC should assess the degree to which SBC has already become a formidable competitor in the bundled services market and the trend toward re-monopolization of the telecommunications industry. Some indicators of SBC's impressive success in new markets are evidenced by statistics contained in SBC's Investor Briefing report for the quarter ending December 31st, 2004:

- SBC's Investor Briefing states its wireline revenue growth in 2004 was “driven by 10.5% growth in data revenues and increased penetration of bundled services such as DSL and long distance.”²⁷
- Revenues for SBC's long distance voice services were up 23.5% in 2004 compared to the fourth quarter of 2003.
- SBC provided 20.9 million lines with long distance at the end of 2004, an increase of 1.1 million lines in the fourth quarter of 2004, and *more than triple* the number served by SBC just two years earlier.²⁸
- SBC reported that 61% of SBC's consumer retail lines bundle their local wireline with at least one other service (e.g., long distance, DSL, Cingular wireless, video), a substantial increase from the fourth quarter of 2003, when 44% of SBC's retail consumers purchased

²⁷/ SBC Investor Briefing, No. 245, January 26, 2005, at 1.

²⁸/ *Id.*, at 2.

bundled services.²⁹

2. In assessing the plausibility of the Applicants' intention to compete out of region, the FCC should examine SBC's actual out-of-region entry.

There is negligible evidence of Bells seeking to compete head-on as rivals with other Bells, particularly for mass market consumers. The Ratepayer Advocate recommends that the FCC seek information from SBC to determine how vigorously SBC has attempted to compete to date. The FCC should consider whether SBC's lack of penetration in "out-of-region" markets is evidence of SBC's lack of resources or lack of interest in competing with other Bell companies. Despite statements that SBC is seeking to "bulk up" so that it can compete with other telecommunications providers, including RBOCs, the interest appears to be primarily focused on the enterprise customer, large business and government contracts.³⁰ The Applicants have not provided persuasive evidence (either through SBC's historic actions or the Application) that they will compete for mass market consumers.

Almost seven years ago, SBC and Ameritech filed an application with the FCC for approval of their merger, and promised, if the merger were approved, that SBC would enter 30 out-of-region markets throughout the country.³¹ When SBC sought regulatory approval to merge with Ameritech, it touted the benefit of its "National Local Strategy" which would purportedly bring competition to markets throughout the country as the merged entity entered rival BOC local markets. Among other things, SBC predicted

^{29/} *Id.*

^{30/} "Because of the merger, residential and small business customers will start to enjoy capabilities that once were available only to the largest business and government customers." Public Interest Statement, at 5, citing Kahan (SBC/AT&T), at para. 32; Declaration of Thomas Horton, at paras. 11, 13.

^{31/} In re: Applications of Ameritech Corp., Transferor, and SBC Communications, Inc., Transferee, for Consent to Transfer Control, FCC CC Docket No. 98-141, *Application*, filed July 27, 1998, § II.A.1.

that:

SBC will begin offering service to residential customers within one year of the closing with Ameritech, and plans to offer service to a majority of the households in the 30 out-of-region markets within four years of closing. We anticipate that we will achieve an overall penetration rate of 4 percent of the residential customers in all of these 30 markets. ... We anticipate achieving similar results in the small business segment.³²

Skepticism about SBC's planned entry into out-of-region market was expressed at the time of its proposed merger with Ameritech: "SBC's fiduciary responsibilities lie with its stockholders, not its customers, and if top management subsequently determines that out-of-region markets are not likely to become profitable within a reasonable period of time, SBC may well abort or scale back its National/Local strategy."³³ Furthermore, one of SBC's own managers recognized that local entry might not be profitable. As was observed at the time the application was pending regulatory approval, "Mr. Kahan specifically states that the business plan for the National/Local Strategy contemplates a 'negative cash flow for nearly ten years'"³⁴ and the "Applicants' claims with respect to the benefits for residential and small business market are particularly unpersuasive. In fact, the Applications are openly disparaging of the residential and small business market."³⁵

^{32/} SBC/Ameritech Merger, Description of the Transaction, Affidavit of James S. Kahan, CC Docket No. 98-141, July 20, 1998, at para. 63.

^{33/} In re Applications of Ameritech Corp., Transferor, and SBC Communications, Inc., Transferee, For Consent to Transfer Control, Federal Communications Commission CC Docket No. 98-141, Affidavit of Susan M. Baldwin and Helen E. Golding, on behalf of Indiana Utility Consumer Counselor, Michigan Attorney General, Missouri Public Counsel, Ohio Consumers' Counsel, Texas Public Utility Counsel and Utility Reform Network, filed on October 13, 1998, at para. 41.

^{34/} *Id.*, at footnote 65, citing James S. Kahan (SBC), at para. 80.

^{35/} *Id.*, at para. 87.

The FCC transformed the carrier's *promises* into *regulatory conditions*.³⁶ The fact that SBC's entry into out-of-region local markets was among the *conditions* of the FCC's approval of the merger simply underscores the regulatory concern that, absent such an explicit requirement, SBC, despite its substantial size, resources, and expertise serving the local market, might have decided not to enter markets in New Jersey (and other out-of-region markets), once it had obtained the requisite regulatory approval to merge.

The size of a company may affect that firm's ability to raise capital and to allocate resources to local entry, but in no way alters whether management perceives entry into a new market to be profitable, and thus worthy of active pursuit. Carriers' ability *and* willingness to enter and serve a market are both critical factors in assessing the probability of consumer benefits.

3. SBC's apparent compliance with the bare bones out-of-region entry conditions the FCC imposed on its merger with Ameritech does not provide compelling evidence of likely concerted future out-of-region efforts.

The FCC established minimum market entry conditions when it approved the SBC/Ameritech merger in 1999. The "verifiable entry requirements" set by the merger order were:

- installing or obtaining switching capability;
- providing facilities-based service to each of three business or residential customers;
- collocating in each of ten wire centers;
- offering facilities-based service to all business and all residential customers served by each

^{36/} In re: Applications of Ameritech Corp., Transferor, and SBC Communications Inc., Transferee, for Consent to Transfer Control, FCC CC Docket No. 98-141, *Memorandum Opinion and Order*, released October 8, 1999 ("SBC/Ameritech Merger Order"), at paras. 398-399, Appendix E. The FCC's conditions required SBC to enter 30 of 50 potential out-of-region markets.

of those ten wire centers; and

- offering service, whether by resale, unbundled elements of facilities to all business and all residential customers with the entire service area of the incumbent RBOC of Tier 1 incumbent LEC in the market.³⁷

Two years ago, SBC reported to the FCC that Condition 21 (*i.e.*, the Out-of-territory competitive entry condition) had been met.³⁸ On March 5, 2002 (a month shy of the April 8, 2002 deadline) SBC provided notice to the FCC that it had satisfied all remaining entry requirements. SBC had installed switching capacity and was providing facilities-based local exchange service to at least three unaffiliated customers in Charlotte, Jacksonville, Las Vegas, Louisville, Memphis, Nashville, Norfolk, Portland, Raleigh and Tucson.³⁹ Also on March 5, 2002, SBC claims to have collocated facilities in at least 10 wire centers in the market “that could be used to provide facilities-based service to customers served by those wire centers”; was offering facilities-based local exchange service all residential and business customers served by the 10 wire centers; was offering local exchange service to all business and residential customers throughout the areas within RBOC service territories in the following markets: New York, Atlanta, Ft. Lauderdale, Phoenix, Denver, Salt Lake City, Washington DC, Minneapolis, Orlando, Baltimore, Philadelphia, Tampa, and West Palm Beach. In August of 2002, SBC reported to the FCC that it had met

^{37/} *SBC/Ameritech Merger Order*, at para. 399.

^{38/} SBC Communications, Inc., *SBC/Ameritech Merger Conditions 2002 Compliance Report to the FCC*, March 15, 2003.

^{39/} *Id.*, at 26.

all of the entry requirements for each of the 30 out-of-territory markets.⁴⁰ However, although SBC may have fulfilled the “letter” of the FCC’s requirements, there is no evidence that SBC has fulfilled the “spirit” of the FCC’s condition approving its merger with Ameritech.⁴¹

The FCC must once again exercise its regulatory authority and require the merged entity to compete in all out-of region residential markets consistent with the FCC’s finding in its TRRO Order that an efficient competitor can compete nationwide.⁴² Failure to meet this requirement should result in the divestiture of all AT&T’s residential customers and the transfer of those customers to another local exchange carrier.

4. If the past is a guide, the likelihood of benefits flowing to mass market consumers is negligible.

Although the proposed combined SBC/AT&T entity may have greater resources with which to compete with other RBOCs, based on SBC’s track record, it is not evident that, as the merger is presently structured, mass market consumers would actually benefit from more vigorous local competition. In 1998, Affiant James S. Kahan, on behalf of SBC and Ameritech stated that the merged company planned to “offer service to a majority of households in the 30 out-of-region markets within four years of closing.”⁴³

^{40/} *Id.*, at 27. The FCC required SBC to enter Boston, Miami, and Seattle within twelve months after the merger closing; an additional twelve markets within 18 months of the merger closing, and all 30 markets by the later of 30 months after the merger closing date or 60 days following SBC’s authorization to provide in-region interLATA services in states representing at least 60 percent of all access lines that the merged entity served. *SBC/Ameritech Merger Order*, at para. 399.

^{41/} See, e.g., “Bells Are Failing to Compete As They Promised,” David Rohde, *Network World*, March 5, 2001.

^{42/} See TRRO Order at paras. 24, 28.

^{43/} SBC/Ameritech Merger, Description of the Transaction, Affidavit of James S. Kahan, CC Docket No. 998-141, July 20, 1998, at para. 63.

As part of the FCC's approval of the SBC/Ameritech merger in 1999, the following conditions regarding competition in out-of-region markets (termed SBC's National-Local Strategy):

SBC and Ameritech will select the 30 out-of-territory markets from the list of 50 major markets that they included in their proposal. As part of the combined firm's entry into each of these new markets, SBC and Ameritech will either meet certain verifiable entry requirements in each market (i.e., installing or obtaining switching capability; providing facilities-based service to each of three business or residential customers; collocating in each of ten wire centers; offering facilities-based service to all business and all residential customers served by each of those ten wire centers; and offering service, whether by resale, unbundled elements or facilities, to all business and all residential customers within the entire service area of the incumbent RBOC or Tier 1 incumbent LEC in the market), or make voluntary incentive payments to a state-designated fund (or as governed by state law) in the amount of \$110,000 per day for each missed entry requirement, for a total of \$1.1 million per entry requirement per market . . . The Applicants' implementation schedule requires the combined firm to enter Boston, Miami and Seattle within 12 months after the merger closing, an additional 12 markets within 18 months of closing, and all 30 markets by the later of 30 months after the merger closing date or 60 days following the company's authorization to provide in-region, interLATA services in states representing at least 60 percent of all access lines served by the combined firm's incumbent LECs.⁴⁴

Even at the time of the merger approval, the FCC found that there was no evidence that SBC/Ameritech's National-Local Strategy would benefit residential and small business consumers. In fact, the FCC found that the companies' plan was to target the top quartile of the residential market in terms of telecommunications expenditures.⁴⁵ SBC's Senior Executive Vice President of Corporate Development, James S. Kahan admits as much in his February 18th, 2005 declaration, stating:

SBC has sought since the late 1990s to become a significant provider to enterprise customers at the national level . . . Despite the commitment of significant resources and investment to execute the "National-Local" strategy we envisioned at the time of the Ameritech acquisition, the results so far have fallen short of our expectations. We have

⁴⁴/ *SBC/Ameritech Merger Order*, at para. 399.

⁴⁵/ *Id.*, at paras. 313-314.

come to realize that acquisition of a firm that has the strengths and resources we lack is far more prudent than incurring the massive investment and time that, without a substantial likelihood of return in a reasonable period of time, would be required to develop them independently.⁴⁶

Mr. Kahan also suggests that the National-Local strategy was always geared towards acquiring the large business customers, describing the strategy as “our organic attempt to achieve in a reasonable time frame the critical mass of customers needed to achieve the scale and scope economies required to compete successfully in the large business segment. It involved the expansion to 30 out-of-region cities with an interconnecting backbone network. We have so far spent in excess of \$1 billion over five years . . . Still, we find it very difficult to win a prime supplier role for large enterprise customers . . .”⁴⁷

Consumer advocates have examined granular data regarding SBC’s actual out-of-region entry in at least two states.⁴⁸ The Ratepayer Advocate urges the FCC to request SBC to submit the following information so that the FCC can assess critically the plausibility of SBC’s promises to compete out of region *throughout the nation*. The Ratepayer Advocate recommends that the FCC seek information on the following:

⁴⁶/ Kahan (SBC/AT&T), at para. 23.

⁴⁷/ *Id.*, at para. 24.

⁴⁸/ Qwest Petition for Competitive Classification of Business Services, Washington Utilities and Transportation Commission Docket No. 030614, Direct and Rebuttal Testimony of Susan M. Baldwin, on behalf of Public Counsel, August 13, 2003 and August 29, 2003; In the Matter of the Implementation of the Federal Communications Commission's Triennial Review Order, New Jersey Board of Public Utilities Docket No. TO03090705, Testimony of Susan M. Baldwin on behalf of the New Jersey Division of the Ratepayer Advocate, February 2, 2004; Unbundled Access to Network Elements, Review of the Section 251 Unbundling Obligations of Local Exchange Carriers, Federal Communications Commission WC Docket No. 04-414, CC Docket No. 01-338, Affidavit of Susan M. Baldwin on behalf of the New Jersey Division of the Ratepayer Advocate, filed October 4, 2004, *see*, para. 84 of the confidential version of Baldwin Affidavit.

- A list of each out-of-region market in which SBC has entered, and the date SBC served its first out-of-region customer in each market.⁴⁹

For each out-of-region market that SBC has entered:

- The boundaries of the geographic market entered (defined by (1) territory encompassed by advertising and (2) territory encompassed by customers actually served) .
- The density zone(s) of the geographic market (based on the UNE loop density zones established by the state public utility commission).
- The customer classes served (e.g., residence, small business, etc.).
- The quantities of customers served separately by type of customer, separately for each of the quarters since the SBC/Ameritech merger was consummated.
- The quantities of customers that have discontinued service with SBC, separately for each of the quarters since the SBC/Ameritech merger was consummated.
- Marketing and advertising materials that SBC presently uses in association with its out-of-region entry.
- The mode of entry (UNE-L, UNE-P, etc.) employed by SBC to enter out-of-region markets.
- Quantities of all SBC out-of-region customers served by (1) UNE-L; (2) UNE-L; and (3) other modes (SBC should specify, and quantify by mode of entry).
- Copies of any and all business case, cash flow, or other analyses prepared for or on behalf of SBC that assess the success of SBC's out-of-region entry.
- SBC's most recent business plan in which it discusses out-of-region entry.

Separately for each of SBC's "home" states:

- Quarterly data (since it obtained Section 271 authority) on residential customers that

^{49/} The Ratepayer Advocate recognizes that the FCC has sought some of this information in a recently issued information and document request. See Letter to Applicants from Michelle M. Carey, Deputy Chief, Wireline Competition Bureau, April 18, 2005, Initial Information and Document Request, *see e.g., Part E*.

subscribe to SBC's local service and its (1) long distance service; (2) DSL service; (3) both long distance and DSL service.

- Quarterly data (since it obtained Section 271 authority) on business customers that subscribe to SBC's local service and its (1) long distance service; (2) DSL service; (3) both long distance and DSL service.
- Total complaints from SBC's retail consumers received for past three years categorized by type of complaint.
- Total complaints from SBC's wholesale consumers received for past three years categorized by type of complaint.

Separately for each state that AT&T serves, information about its presence in the local market:

- Quantities of residential customers separately by mode of entry (UNE-P, UNE-L; other).
- Quantities of business customers separately by mode of entry (UNE-P, UNE-L; other).

5. Absent enforceable regulatory conditions, it is unlikely that SBC will pursue residential and small business consumers.

The documents filed with regulators and the investor community demonstrate that the motivation for the merger is to gain access to the enterprise customer. The purported advantage to residential customers is that in its aggressive push to acquire enterprise customers, SBC will "trickle down" some of AT&T's innovations to residential and small business customers.⁵⁰ The Applicants contend that "[b]ecause of SBC's strong focus on residential and smaller business consumers, the merged firm will have the incentive to bring those customers innovative services and features originally developed for higher-end

^{50/} See, e.g., Kahan (SBC/AT&T), at para. 32; Declaration of Hossein Eslambochi (AT&T) (discussing the prediction that the combination of the companies will allow AT&T Lab innovations to eventually reach residential and small business customers. Among the potential innovations, according to Declarant Eslambochi, are IP-based video, speech/text technologies, fraud reduction, service provisioning, and repair.) Eslambochi (AT&T), at paras. 7, 10-14.

customers, and it will have the expertise, financial strength and incentives to do so.”⁵¹ According to the Applicants, “[t]he proposed transaction will promote competition by creating a more efficient firm which will achieve significant cost savings and will be better positioned to develop and deploy new products and services for business and residential customers.”⁵²

Although the Applicants tout benefits for residential customers, absent regulatory requirements, their competition in the mass market is unlikely in the foreseeable future. The following excerpt from SBC’s sales team material, which emphasizes potential profits from business customers but is silent about residential customers, underscores SBC’s clear corporate priorities:

Q: Is there anything that I can or should be doing differently as it relates to the acquisition?

A: No. We must continue to treat AT&T as a powerful competitor, and we must continue to win business and succeed in the marketplace with our strong existing strategy and portfolio. We should continue to focus on our sweet spot and efforts to grow share of wallet with business customers.⁵³

The Applicants’ assertion that the merger would not harm competition is unpersuasive. They assert that “[i]n addition, our analysis to date indicates that the transaction is unlikely to create significant competitive problems due to a variety of characteristics of the industry and Parties, including: (i) the largely complementary nature of AT&T’s and SBC’s networks, services and target customers; (ii) the rapid on-going pace of developments in telecommunications technology; (iii) AT&T’s prior decision to cease

⁵¹/ Kahan (SBC/AT&T), at para. 36.

⁵²/ Carlton/Sider (SBC/AT&T), at para. 5.

⁵³/ AT&T Acquisition Background for Sales Teams, Updated March 22, 2005, Filed by SBC Communications Inc., Commission File No.: 1-01105, submitted to the SEC April 6th, 2005.

marketing its services to residential and small business customers; (iv) the growth of facilities-based competition for both businesses and residential consumers; and (v) the sophistication and purchasing practices of business customers as well as the importance of non-price dimensions of telecommunications services.”⁵⁴ These generalities provide insufficient evidence to demonstrate that the proposed merger would not harm competition. The lack of economic substitutes for ILECs’ voice grade service offered to mass market consumers in sufficient supply and strength to discipline ILECs’ prices and behavior raise the stakes for the FCC’s analysis of the purported merger benefits.⁵⁵

The Applicants further assert that “AT&T’s decision to cease marketing traditional services to residential consumers and small businesses means that it will rapidly cease to be a significant competitive factor in serving these customers in the absence of the transaction. Moreover, residential customers that would have remained with AT&T in the absence of the transaction are likely to benefit from the merger because SBC, which has no plans to exit, does not face the same incentives as AT&T to raise prices to this group.”⁵⁶ However, the Applicants provide no support for this statement. The Applicants fail to explain why SBC would seek to retain a small number of AT&T customers in out-of-region states when SBC is not actively competing for other residential customers in the state. The Ratepayer Advocate urges the FCC to impose regulatory conditions to translate these generalities into specific commitments to serve residential and small business consumers in SBC’s out-of-region markets.

^{54/} Carlton/Sider (SBC/AT&T), at para. 5.

^{55/} Residential consumers’ increasing reliance on DSL and intermodal substitutes for *additional* lines does not provide evidence of facilities-based competition for their primary lines.

^{56/} *Id.*, at para. 6.

C. LOSS OF AT&T AS A REGULATORY “ACTIVIST”

1. The proposed merger would create a regulatory vacuum, and diminish the comprehensiveness of state and federal investigations of telecommunications policy.

AT&T’s change in identity from CLEC to ILEC would create a significant regulatory vacuum and diminish the breadth and depth of state and federal proceedings.⁵⁷ Since divestiture in 1984, and since the enactment of the Telecommunications Act of 1996, AT&T has been an active, vocal participant, shaping state and federal telecommunications policy. The transformation of this well-heeled regulatory activist into an incumbent’s partner will irrevocably alter state and federal investigations of telecommunications policy, ultimately harming consumers. The “if-you-can’t-beat-them-join-them” mentality that has overtaken the telecommunications industry reduces consumers’ prospects for meaningful competition and underscores the necessity of federal and state regulators to exercise oversight of the local mass market. With each successive phase of market concentration, the need for regulatory oversight of the re-monopolized telecommunications market becomes more critical.

The Applicants’ insistence that regulatory issues are irrelevant to their merger because the FCC

⁵⁷/ See, e.g., *AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM-10593, Petition for Rulemaking, filed October 15, 2002; “The disappearance of AT&T and MCI as independent corporations will also have significant second-order effects in the regulatory arena . . . AT&T has long supported enterprise customer groups working to keep a lid on RBOC special access pricing. It did that for its own reasons—it had to buy most of its dedicated access from the RBOCs, and didn’t want to pay exorbitant prices or take the blame for installation delays. Whatever its motives, in recent years AT&T was often aligned with enterprise users before the FCC, and their joint efforts have recently started to pay off—in response to pressure from enterprise customers and AT&T, the FCC started a new proceeding less than a month ago to examine the rules and pricing for dedicated access services such as T1s, DS3s, OCns, etc. Unfortunately for its allies, AT&T’s contribution to this effort will now come to a screeching halt, leaving large users to fend for themselves.” (Hank Levine and David Rhode, “Protecting Enterprise Customers after the Telecom Mega-Mergers,” *Business Communications Review*, March 2005).

is addressing “industry-wide issues” in various ongoing proceedings,⁵⁸ oversimplifies the way in which the telecommunications industry and Federal policy interact. Post-merger, AT&T’s incentives and obligations to shareholders would change dramatically. AT&T’s metamorphosis from a consumer of Bell services to a supplier of Bell services would strengthen considerably SBC’s regulatory position, to the harm of consumers. Furthermore, until the FCC resolves critical industry issues such as unifying the intercarrier compensation regime, addressing BOCs’ exorbitant special access profits, and ensuring appropriate interaffiliate transactions, it would be unwise to allow the market to undergo further concentration, absent commitments aimed at curtailing abusive behavior by the merged entity. The Ratepayer Advocate urges the FCC to impose conditions to detect and to prevent (1) anti-competitive behavior and (2) extracting supra-competitive profits from consumers.

D. SYNERGIES

1. If the FCC approves the proposed transaction, it should increase the X factor in its price cap regulation accordingly.

The Applicants predict that the merger will reduce substantially fixed and variable costs, which will, in turn, make the combined company a “more effective competitor” and will lead to greater research and innovation.⁵⁹ The Applicants estimate *annual* synergies of \$2 billion by 2008, or a net present value of approximately \$15 billion.⁶⁰ Cost reductions are expected in the following areas:

- network operations and IT (consolidations of facilities and operations);

^{58/} Public Interest Statement, at 65, footnote 213.

^{59/} *Id.*, at 43.

^{60/} *Id.*, at 44; Kahan (SBC/AT&T), at para. 37.

- combination of sales and support functions of the business services organizations;
- elimination of duplicate corporate functions; and
- “revenues would be enhanced, as SBC would migrate existing service offerings to new customer segments.”⁶¹

Competitive pressures are not sufficient to cause SBC to flow through these substantial synergies to consumers of basic services and other monopoly services (such as special access) through rate reductions, service innovation, or enhanced service quality. The FCC should recognize this market failure in its decisions in the Special Access and the Intercarrier Compensation proceedings in order to prevent SBC from earning supracompetitive profits from its non-competitive services.

The FCC released its “Special Access NPRM” (Order and Notice of Proposed Rulemaking) in WC Docket No. 05-25 on January 31, 2005,⁶² which addresses issues directly related to the proposed merger between SBC and AT&T. The Special Access NPRM commences a “broad examination of the regulatory framework to apply to price cap local exchange carriers’ (LECs) interstate special access services”⁶³ given the expiration of the CALLS plan on June 30, 2005. The FCC seeks comments regarding both traditional price cap issues and its current pricing flexibility rules for special access

^{61/} SBC Prospectus/AT&T Proxy Statement, at 26.

^{62/} In the Matter of Special Access Rates for Price Cap Local Exchange Carriers; AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services, FCC WC Docket No. 05-25; RM-10593, Order and Notice of Proposed Rulemaking, Released January 31, 2005 (“Special Access NPRM”).

^{63/} *Id.*, at para. 1.

services.⁶⁴ The FCC has recognized that special access is a key input for competitive LECs, CMRS providers, business customers, and interexchange carriers (IXCs). Special access revenues have grown from 12.8 percent of BOC interstate operating revenues in 1991 to 45.4 percent of interstate operating revenues in 2003.⁶⁵ Among the issues that the FCC is considering is the need for and appropriate magnitude of a productivity factor⁶⁶ and the merits of earnings sharing.⁶⁷

The Special Access NPRM also addresses an AT&T petition for rulemaking asking the FCC to revoke pricing flexibility and reexamine the CALLS Plan claiming that predicted competitive entry in the special access market has not materialized and that BOC special access rates have increased or remained flat in every market where pricing flexibility has been granted.⁶⁸ Indeed, the FCC notes in the Special Access NPRM that the BOCs have “earned special access accounting rates of return substantially in excess of the prescribed 11.25 rate of return that applies to rate of return LECs.”⁶⁹ If the FCC approves the proposed merger between SBC and AT&T, the FCC should indicate its intentions:

- To require SBC to share the substantial synergies that the Applicants anticipate in the Special Access rulemaking with special access customers through measures such as the productivity factor and an earnings sharing mechanism.
- In assessing Bell operating companies’ pricing flexibility, to consider the impact of the

⁶⁴/ *Id.*, at paras. 1 and 4.

⁶⁵/ *Id.*, at para. 3.

⁶⁶/ *Id.*, at paras. 35-36.

⁶⁷/ *Id.*, at para. 44.

⁶⁸/ *Id.*, at para. 19.

⁶⁹/ *Id.*, at para. 35.

merger on the competitiveness of relevant markets.

2. In assessing the potential benefits and harms from the proposed transaction, the FCC should examine SBC's home-region behavior.

The proposed merger exposes consumers to two possible ill effects related to the Applicants' achievement of the predicted merger synergies:

- First, as is discussed below, the Applicants' efforts to reduce operating expenses could jeopardize service quality.
- Second, the Applicants' efforts to enhance revenues could lead to aggressive sales practices.

In their zeal to achieve anticipated merger synergies, the Applicants would likely seek ways to reduce operating expenses. Federal and state regulators should monitor carefully the quality of basic local service to ensure that those consumers most vulnerable to cost-cutting measures (*i.e.*, those in rural areas and those that do not purchase bundled services) do not receive inferior service quality as a result of the Applicants' simultaneous pursuit of revenues from competitive services and implementation of operating efficiency measures. Similarly, regulators should monitor the Applicants' sales practices for its discretionary and bundled services to ensure that consumers are sufficiently well-informed to be able to make efficient purchasing decisions. Finally, regulators should heed comments from the remaining CLECs so that they can prevent SBC from squeezing out those competitors that are still attempting to compete in the many markets that the merged entity would dominate.

E. CONDITIONS

If the FCC approves the merger, it should only do so contingent upon explicit conditions that would (1) mitigate and/or prevent harms that the merger would likely cause and (2) enhance and/or increase the likelihood of merger benefits. Furthermore, these conditions should be designed so that:

- The FCC, state public utility commissions, competitors, and consumers can readily monitor the Applicants' compliance.
- The FCC can enforce them (*i.e.*, the financial incentives for compliance are sufficient, and the Applicants' compliance can be assessed).
- The conditions do not sunset, but rather only terminate based upon an affirmative finding by the FCC that they are longer necessary. The Applicants should bear the burden of proving that the conditions are not longer necessary.

1. The FCC should impose conditions to mitigate and/or prevent harms to consumers.

In this section of its comments, the Ratepayer Advocate identifies potential harms of the merger and describes possible conditions to mitigate and/or prevent consumer harm.

Implications of Merger Synergies – Pursuit of New Revenues

Potential harm: The Applicants anticipate that one component of the merger synergies would flow from sales to new customers. According to the Proxy Statement, “revenues would be enhanced, as SBC would migrate existing service offerings to new customer segments.”⁷⁰ The pursuit of enhanced revenues

⁷⁰/ SBC Prospectus/AT&T Proxy Statement, at 26.

from SBC's existing services (which likely include bundled services) would create incentives for (1) for overly aggressive sales practices; (2) cross-subsidization of competitive services with revenues from monopoly services.

Conditions: The FCC should require an independent audit of SBC's sales practices, an independent audit of SBC's interaffiliate transactions, and comprehensive customer education.

Implications of Merger Synergies – Cost-cutting Measures

Potential harm: The Applicants' efforts to lower operating expenses could jeopardize the quality of basic services offered to mass market consumers, for which there is no effective competition.

Conditions: The FCC should coordinate with state public utility commissions to impose sanctions if service quality for non-competitive SBC-supplied telecommunications services declines below benchmark levels.

Market concentration

Potential harm: The proposed merger would eliminate a significant, nationwide supplier of telecommunications services, thereby diminishing competitive options.

Conditions:

- The Applicants should commit to deploying “naked DSL” to increase the likelihood of consumers having competitive choices.⁷¹

^{71/} The FCC recently found that states could not require incumbent LECs to provide DSL service to customers over the same UNE loop used by a competitive LEC to provide voice service to an end user. *Bell South Telecommunications, Inc. Request for Declaratory Ruling that State Commissions May Not Regulate Broadband Internet Access Services by Requiring BellSouth to Provide Wholesale or Retail Broadband Services to Competitive LEC UNE Voice Customers*, FCC WC Docket No. 03-251, Rel. March 25, 2005. The order specifically addressed states' authority to establish unbundling requirements inconsistent with FCC unbundling rules. However, the FCC did not issue any findings with respect to concerns raised by competitors that such tying policies by incumbents are anticompetitive and, in fact, issued a Notice of Inquiry regarding the tying issue. *Id.*, at para. 31.

- The Applicants should commit to out-of-region entry to serve residential and small business consumers in more than a “barebones” fashion.

2. The FCC should impose conditions to enhance and/or increase the likelihood of benefits for consumers.

In this section, the Ratepayer Advocate describes conditions that would increase the potential for consumers to benefit from the proposed merger.

Implications of merger synergies

Potential benefit: In a competitive market place, suppliers would lower prices, increase service quality and/or offer new, innovative products as a result of generating merger synergies. However, in many of the telecommunications markets that the Applicants serve, there is inadequate competitive pressure to ensure that consumers of non-competitive services share fairly in the merger synergies.

Condition: The Applicants should flow through merger synergies by reducing rates for its non-competitive interstate services. The FCC should establish an adequate X factor and restore earnings sharing in its Special Access proceeding. In its overhaul of the intercarrier compensation regime, the FCC should be aware of the substantial merger synergies that SBC will enjoy.

III. CONCLUSION.

WHEREFORE the reasons set forth above, the Ratepayer Advocate submits the following recommendations to the Commission:

- The FCC should impose enforceable conditions to protect consumers from harm and that

“We seek comment on whether such bundling behavior is harmful to competition, particularly unaffiliated providers of new services, such as voice over Internet protocol (VoIP), and if so, how this is related to several previous decisions or ongoing proceedings relating to dominance and classification issues.” *Id.*, at para. 37.

increase the likelihood of benefits flowing to mass market consumers.

- Absent such conditions, the Applicants have failed to demonstrate that, on balance, the proposed merger is in the public interest.
- The FCC should seek detailed data and information from the Applicants, as described generally in these comments.

Respectfully submitted,
SEEMA M. SINGH, Esq.
RATEPAYER ADVOCATE

By: Christopher J. White
Christopher J. White, Esq.
Deputy Ratepayer Advocate

Economic Consultants:

Susan M. Baldwin
Sarah M. Bosley