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

Application for Consent to Transfer of Control Filed by SBC Communications, Inc. and AT&T Corp.	)	WC Docket 05-65
Application for Consent to Transfer of Control Filed by Verizon Communications, Inc. and MCI, Inc.	)	WC Docket 05-75

PETITION TO DENY
OF THE
AMERICAN PUBLIC COMMUNICATIONS COUNCIL

Pursuant to *Public Notice*, DA-05-656 and *Public Notice*, DA 05-765, the American Public Communications Council ("APCC") hereby petitions to deny the above-captioned applications. APCC is filing simultaneously in both dockets because the proposed mergers of SBC Communications, Inc. ("SBC")/AT&T Corp. ("AT&T") and Verizon Communications, Inc. ("Verizon")/MCI, Inc. ("MCI")[1] raise similar issues for

[1] According to recent press reports, as of April 23, 2005, MCI's board of directors has voted to accept a competing proposal from Qwest Communications. Given that the Commission has opened a proceeding to address a MCI/Verizon merger, but not with respect to a MCI/Qwest merger, this petition to deny addresses the MCI/Verizon merger. If, and when, a proceeding is opened to address a MCI/Qwest merger, we will submit comments at the appropriate time.

APCC's independent payphone service provider ("PSP") members. For the reasons shown below and more fully described in the accompanying analysis, *EFFECT OF PROPOSED BOC/IXC MERGERS ON THE PAYPHONE SERVICE MARKET*, American Public Communications Council, April 25, 2005 ("APCC Analysis"), the Commission should deny the Applications for Consent to Transfer Control filed by SBC/AT&T and by Verizon/MCI .[2]

STATEMENT OF INTEREST

APCC is the non-profit national trade association representing the independent (i.e. non-LEC-owned) payphone industry. Approximately 550,000 of the 1.35 million payphones deployed nationwide are operated by independent PSPs. APCC has 1,144 PSP members, ranging in size from sole proprietorships to publicly-traded companies operating tens of thousands of public payphones.

DISCUSSION

If allowed to go forward, the proposed SBC/AT&T and Verizon/MCI mergers will have dramatic anticompetitive effects on independent PSPs. SBC and Verizon each constitute roughly a third of the payphone industry and are the two dominant players. Because of their size, branding, and sister relationships with their respective regulated local exchange operations—from whom both they and independent PSPs buy local

[2] The Commission's consideration of each merger, though informed by the other, should be independent. While the Commission should deny both mergers, a decision to allow one to go forward should have no effect on its consideration of the other.

service—the SBC and Verizon payphone divisions already enjoy advantages in the marketplace. Permitting the SBC and Verizon payphone divisions to combine with the two largest interexchange carriers, AT&T and MCI, will create two market-dominating entities that will be in a position to throttle payphone competition.

As more fully catalogued in the accompanying APCC Analysis, the merged entities will have every incentive to manipulate the payphone compensation system in anticompetitive ways, including:

- Substantially increased disincentive to devote sufficient resources to ensuring accurate dial-around compensation payments;
- Substantially increased incentive to make judgment calls that reduce payments to their payphone competitors;
- Substantially greater incentive to engage in "takebacks" of alleged overpayments from their payphone competitors without allowing PSPs to dispute the overpayment;
- Substantially greater incentive to withhold payments from high-volume payphones operated by their payphone competitors;
- Substantially greater incentive to delay compensation payments to their payphone competitors;

- Substantially reduced incentive to exercise care in testing the Flex ANI service that is needed to track calls from their competitors' payphones;
- Substantially greater incentive to adjust their business practices regarding payments for non-Flex ANI payphones operated by their payphone competitors;
- Substantially reduced incentive to provide timely, accurate, and complete data identifying calls routed to resellers from their competitors' payphones;
- Substantially reduced incentive to collect and remit compensation payments owed by resellers pursuant to alternative payment agreements;
- Greater disincentive in maintaining accurate ANI lists and more incentive to use minor discrepancies in ANI matchups as an excuse to deny compensation to their payphone competitors;
- Additional incentive to withhold from their payphone competitors calling data needed by the PSPs to check the accuracy of compensation payments made by large IXCs;
- Substantially greater incentive to deny payments to their payphone competitors for dial-around carried by means of IP technology;

- Substantially greater incentive to adopt business rules that result in reduced payments to PSPs; and
- Strong incentive as well as the ability to share information with their PSPs about the volume of completed dial-around calls from competitors' payphones.

CONCLUSION

For the foregoing reasons, the Commission should deny the Applications for Consent to Transfer Control filed by SBC/AT&T and by Verizon/MCI. Allowing either the AT&T/SBC merger or the MCI/Verizon merger would lead to all of the anticompetitive effects described above, and allowing both mergers would multiply those effects. Therefore, the most appropriate remedy is simply to deny the mergers.

In the event that the mergers are allowed, there are a limited number of ways that the mergers could be conditioned in order to limit (but not wholly eliminate) anticompetitive effects on the payphone market, including:

- Imposing behavioral restraints such as enjoining the combined entities from modifying their dial-around compensation payment procedures or using their payments to benefit their own payphone operations;
- Requiring accounting and "regulatory structural" safeguards to restrain the ability of the combined entities to bolster their payphone operations with

revenue from elsewhere in the enterprise and share information about their payphone competitors; and

- Requiring SBC/AT&T and Verizon/MCI to divest themselves of their payphone assets prior to consummation of the merger.

The first two options have inherent limitations that make them inadequate to prevent the combined entities from engaging in anticompetitive conduct with respect to their payphone operations. Both behavioral restraints and accounting safeguards are difficult and costly to police.

The only remedy that is promising – short of denying the mergers outright -- is to require the divestiture of the combined entities' payphone operations. This approach would be the simplest to implement, would require no policing after it was implemented, and removes the incentives that the combined enterprises would otherwise always have to discriminate in favor of their own payphone operations.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on April 25, 2005, the foregoing petition was sent via overnight mail to the following:

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EFFECT OF PROPOSED BOC/IXC MERGERS ON THE PAYPHONE SERVICE MARKET

This analysis discusses the anti-competitive effects that the proposed mergers of SBC Communications with AT&T Corp. and of Verizon Communications with MCI Inc. will have on the payphone industry. The analysis begins by explaining the structure of the payphone industry, in which (1) SBC and Verizon are the dominant providers and compete with independent payphone service providers ("PSPs") and (2) AT&T and MCI are the source of a major revenue stream for independent PSPs. The analysis then explains how the combined entities—SBC/AT&T and Verizon/MCI—will have the ability and the motivation to engage in conduct that will anticompetitively discriminate in favor of their own payphone operations.

The analysis concludes by discussing the options that are available to address the anticompetitive effect of the proposed mergers on the payphone industry. The simplest, cleanest way to prevent the injuries that the proposed mergers would cause to payphone competition is to deny the mergers. In the event that the mergers are allowed, the only remedy that would be effective is to require the divestiture of the combined entities' payphone operations. Short of denying the mergers outright, this approach would be the simplest to implement, would require no policing after it was implemented, and would remove the incentives that the combined enterprises would otherwise always have to discriminate in favor of their own payphone operations.

I. INTRODUCTION

A. The Role Of Payphones

If allowed to go forward, the proposed SBC/AT&T and Verizon/MCI mergers will have dramatic anticompetitive effects on the PSP sector of the telecommunications industry. The PSP sector is a critical one. Payphones *uniquely* afford all Americans guaranteed, low-cost access to the public telephone network, across every strata of society. Payphone service is a dial-tone-on-demand, per-use-priced wireline service available twenty-four hours a day, seven days a week, 365 days a year. Users are not required to make an initial investment in equipment, await activation of the service or pay recurring monthly charges.

Apart from their unique role as a first and last resort for access to the PSTN, payphones also play an important role in enhancing public safety and national security. They provide a critical emergency communications infrastructure that has proven to be more robust that the wireless networks. During blackouts and even in the immediate aftermath of the 9-11 attacks, when the cellular networks failed, payphones worked.

Because of their unique benefits, even with increasing pressure from the wireless industry, payphones remain an important part of the telecommunications infrastructure. At the end of 2004, there were an estimated 1.35 million payphones deployed nationally.

B. The Merged Entities

SBC and Verizon are the two dominant players in the payphone industry, each constituting roughly 20 - 25% of the industry and with well over 50% of the market in their respective local exchange territories. With the other two remaining Bell operating companies ("BOCs"), Qwest and BellSouth, both having exited the market, SBC and Verizon collectively account for almost half of all payphones. Within the SBC and Verizon service areas, independent PSPs—*i.e.*, companies who own and operate their own payphones—compete vigorously among themselves and with the SBC and Verizon payphone operations for the rights to new locations from which to attract end users.

Because of their size, co-branding, and sister relationships with their respective regulated local exchange operations—from whom both they and independent PSPs buy local service—the SBC and Verizon payphone divisions already enjoy advantages in the marketplace. Permitting the SBC and Verizon payphone divisions to combine with the two largest interexchange carriers will create two market-dominating entities that will be in a position to throttle payphone competition.

As explained below, PSPs receive a large percentage of their revenues frolargePSPs1two operations and independent PSPs can have a discriminatory and anti-competitive effect on independent PSPs. Even though such changes may facially apply non-discriminatorily, any adverse effect on the affiliated PSP entity is neutralized at the enterprise level because of the offsetting positive effect on the affiliated IXC. For example, the affiliated PSP operations will not suffer if dial-around compensation payments from its affiliated IXC are reduced or delayed because the affiliated IXC is correspondingly benefited by the reduction or delay in its dial-around payments to the affiliated PSP.[1] For independent PSPs, however, there is no offsetting benefit. The reduced or delayed compensation payments represent an absolute loss to the PSP. Moreover, revenue from dial-around compensation is critical to PSPs' ability to pay location commissions and to otherwise conduct their businesses. Thus a reduction or delay in payment that is facially non-discriminatory in its application to affiliated and unaffiliated PSPs would not cause any net harm to the affiliated PSPs and could be sufficient to drive independent PSPs out of the market.

As for the combined entities' LEC operations, there are several areas that are rife with the potential for abuse. One area of particular concern is the provision of so-called "Flex ANI" service. Flex ANI is a signaling service that the FCC requires all LECs—including SBC and Verizon—to provide to IXCs that allows IXCs to identify calls as originating from payphones. If an IXC does not properly order, or if the LEC does not properly provision, Flex ANI, the IXC may be unable to identify, for purposes of paying compensation, calls originating from "smart" payphones. Smart payphones, in which the intelligence of the payphone is located in the payphone itself instead of in

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[1] It is irrelevant whether the PSP affiliates' "loss" is made up by means of cash flows from the IXC affiliate. Resources are available if needed, and there is no diminution of resources at the enterprise level.

the network—are used almost exclusively by virtually all independent PSPs. By contrast, because they own the network, SBC and Verizon operate predominantly "dumb" payphones. Dumb payphones connect to the network by means of specialized lines and do not require Flex ANI in order to identify or transmit identifying digits to IXCs. Thus, Flex ANI is needed primarily by the independent PSP competitors of SBC and Verizon.

Flex ANI is provisioned on a switch-by-switch and line-by-line basis. Because of this characteristic, it is a relatively high maintenance service, and is prone to outages when other switch functionality is upgraded, changed, or maintained. Independent PSPs are extremely vulnerable to LEC manipulations of Flex ANI because outages may not be discovered until there is lost dial-around revenue.

Today, LECs such as SBC and Verizon are able to manipulate Flex ANI deployment to discriminate against their independent PSP competitors. But in addition to their competitive incentives to do so, the post-merger SBC/AT&T and Verizon/MCI will have a direct financial incentive. Any loss in dial-around compensation by independent PSPs resulting from Flex ANI manipulation is a direct financial benefit to the now-affiliated IXC (which will pay less dial-around compensation to the independent PSP) as well as a competitive gain for the LEC-affiliated PSP.

IXCs—including AT&T and MCI—also depend on lists of payphones provided by LECs—including SBC and Verizon—in order to validate PSP requests for payment. If the mergers go forward, SBC will be providing this information to its IXC side concerning both its own payphone operations and those of its independent PSP competitors.

What makes all of these potential areas of abuse a real concern is that the combined entities will have an incentive to discriminate against their competitors that the IXCs as stand-alone entities do not. At the moment, AT&T and MCI have no particular incentive to make the dial-around compensation system work, but also have no particular incentive to do anything that benefits one class of PSP competitors over another. If the mergers go forward, AT&T and MCI, for the first time, will have the added incentive of discriminating against—or acting in whatever ways it can to disadvantage—the competitors of its LEC-affiliated PSP.

II. BACKGROUND

A. The Payphone Business

1. Payphones provide critical access to the public network

As the FCC has recognized, "payphones unquestionably serve critical public interests in health, safety and welfare."[2] Approximately 1.35 million payphones throughout the country play a unique role in providing Americans with access to the telecommunications network.[3] Even with the boom in wireless communications, roughly half of all Americans still do not own a wireless phone and many, for financial or other reasons, never will.[4]

While payphones are valuable to everyone, they are perhaps most critical to those who cannot afford either a wireless phone or a home phone. As of March 2003, approximately 5 million households did not have a home phone; for the individuals in

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[2] *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, Report and Order, 11 FCC Rcd 20541, ¶ 7 (1996) ("*First Payphone Order*").

[3] FCC, Wireline Competition Bureau, Industry Analysis and Technology Division, *Trends in Telephone Service*, Table 7.6 (August 2003).

[4] *Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993*, Eighth Report, 14 FCC Rcd 14783, ¶ 17 (2003).

these households, payphones are the primary means of placing calls.[5] Most of these households are poor and a disproportionate number of them are minorities. *Id.*, Tables 4 and 7. Ready, affordable access to the network through payphones is vital for this group.[6] For those without a home phone, the removal of a payphone from their neighborhood means that their access to the public telecommunications network has been effectively severed.

Even in the face of growing wireless penetration, payphones remain a critical supplementary method of accessing the public communications network. The limits of wireless service and the value of reliable payphone service were demonstrated in the Summer of 2003 during the power failure that hit much of the northeast. By one account "payphones pulled a Clark Kent trick . . . morphing into the superheroes of urgent, reliable communications for millions of stranded and stressed Northeast2315Tj0n1Tf7.340TD0Tc02315Tj/T.280TD0.000c3(rners."0TD7.080TD7.08166.98390.6essed)Tj/(7

September 11, 2001 attacks. They provided the only reliable means of emergency communications for thousands of New York City residents and emergency services personnel.

2. The competitive landscape

In 1984, the FCC opened the payphone market to competition by authorizing the attachment of independent (i.e. non-telephone company owned) payphones to the public network.[8] Since then, hundreds of independent PSP companies have entered the market to provide public payphone service and equipment. These independent companies range in size from small businesses with a few locations to publicly-traded companies with tens of thousands of payphones.

In providing their payphone services to the public, independent PSPs compete with each other and with SBC's and Verizon's payphone operations for locations at which to install their payphones.[9] Particularly with regard to high volume (and thus potentially high revenue) locations, PSPs pay the location owner a monthly commission for the right to place their payphones. Competition among PSPs for locations turns on their ability to pay commissions to the location owner, which of course depends in turn on the revenue available to PSPs. PSPs also compete for locations by seeking to offer attractive services to the location owner's customers. Independent PSPs have been particularly innovative in this area, introducing novel calling programs that significantly reduce the cost of placing many payphone calls, such as 10 minutes of calling for $1. These calling programs are often focused on immigrant

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8 *Registration of Coin Operated Telephones Under Part 68 of the Commission's Rules and Regulations, Memorandum Opinion and Order*, 57 Rad. Reg. 2d (P&F) 133 (1984).

9 By contrast, Verizon and SBC operate payphones almost entirely within their own regions and engage in little if any competition with each other's payphone operations.

communities and low income users who might otherwise have no access to a phone. For such users, inexpensive payphone calling plans are often much less expensive than prepaid wireless services. The net result for all payphone users of increased payphone competition from independent PSPs has been better, cleaner payphones offering better and more innovative calling options.

Historically, independent PSPs were handicapped in their ability to compete with the payphone operations of SBC, Verizon, and other BOCs. The BOCs treated their payphone operations as an integral part of their rate-regulated local exchange services, and included their payphone equipment in regulated accounts. As a result, the BOCs' payphone operations had access to a vast pool of regulated local exchange and exchange access revenues. These revenue pools effectively guaranteed the BOCs full recovery of their payphone costs, and allowed them to subsidize below-cost payphone service rates and above-market payphone location commissions. SBC, Verizon, and the other BOCs were also able to discriminate against independent PSPs in the provision of the basic local exchange service that is the chief input for independent PSP operations.

In Section 276, which was added to the Act as part of the Telecom Act of 1996 amendments, Congress recognized the public benefit of a robust, competitive payphone market and sought to correct the industry's competitive imbalance. Section 276's stated goals were "promot[ing] competition among [PSPs] and promot[ing] the widespread deployment of payphone services to the befit of the general public." 47 U.S.C. § 276(b)(1). To those ends, Congress prohibited SBC, Verizon, and the other BOCs from subsidizing or discriminating in favor of their payphone services, 47 U.S.C. § 276(a), directed the FCC to eliminate all subsidies, 47 U.S.C. § 276(b)(1)(B), and required "nonstructural" safeguards to prevent future subsidies and discrimination, 47 U.S.C.

§ 276(b)(1)(C). As the FCC said in its order adopting implementing regulations, "we believe that vigorous and unfettered competition is the best way of achieving Congress' dual objectives." *First Payphone Order* ¶ 3.

Section 276 has thus helped to level the playing field for independent PSPs and to prevent SBC and Verizon from using their control of bottleneck local exchange facilities to place their PSP competitors at an unwarranted disadvantage. Nonetheless, SBC and Verizon payphone operations continue to be the dominant providers of payphone service in their respective regions, and are thus poised to exploit any opportunities that may arise to use artificial means to place their PSP competitors at an unwarranted competitive disadvantage. As described below, the control of their competitors' dial-around compensation revenue streams that SBC and Verizon would acquire if allowed to merge with AT&T and MCI constitutes just such an artificial means of imposing unwarranted disadvantages on their competitors.

3. Dial-around compensation is a major revenue stream for PSPs and is critical to the ability of PSPs to compete in the payphone market

A large percentage of the calls that originate from payphones are "dial-around" calls. A dial-around call is initiated when a caller dials a toll-free number (usually an 800, 888, 877, etc. number) from a payphone.[10] Dial-around calls are "coinless"—the PSP receives no payment from the caller for the use of its payphone to make dial-around calls. Instead, the carrier that completes the call is required to pay the PSP a per-call fee to compensate the PSP for the use of its equipment.

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[10] There are two types of dial-around calls: (1) "subscriber toll-free calls," in which the caller dials a toll-free number in order to reach a business or person to whom that toll-free number belongs; and (2) "access code calls," in which the caller dials a toll-free number belonging to a communications service provider in order to "access" the IXC's call processing platform, where the caller provides billing information and dials another number to complete the call to the intended called party.

After coin calls, dial-around calls constitute the largest revenue stream for independent PSPs.

AT&T and MCI are, respectively, the first and second largest payors of dial-around compensation. Together, the two IXCs' compensation payments represent well over 50% of all dial-around compensation paid.

B. Dial-around compensation

1. The FCC's compensation rules

The dial-around compensation obligation is rooted in Section 276. Section 276 requires the Commission to:

> Establish a per call compensation plan to ensure that all payphone service providers are fairly compensated for *each and every completed intrastate and interstate call* using their payphone, except

Since their initial adoption in 1996, the FCC's rules governing dial-around compensation have been subject to almost constant challenges by the carriers. As a result, the FCC itself has issued more than 15 orders revising and refining the process, and the United States Court of Appeals for the District of Columbia Circuit has reviewed the rules no fewer than five times. Aside from the question of what compensation rate should apply, the element of the rules that has generated the most litigation is the issue of which IXC should pay when more than one carrier is involved in a call.

In one common scenario, the caller dials an access code belonging to a switch-based reseller of long distance service ("SBR"). The originating LEC (such as SBC or Verizon) hands off the call to a facilities-based IXC (such as AT&T or MCI), who routes the call to the SBR's call-processing platform. The caller provides billing information to the SBR and dials the number of the intended called party. The SBR then routes the call over its own facilities or another carrier's facilities and sends the call to the terminating LEC. A similar scenario can occur with subscriber toll-free calls, with the difference that there is no need for the call to "pause" at a call processing platform, because the toll-free number belongs to the called party.

The question of who, as between the underlying IXC and the SBR, should bear the payment responsibility was at the center of a recent round of revisions to the FCC's rules. In rules adopted in 2003 and effective on July 1, 2004, the FCC shifted liability from the underlying IXC to the SBR.[12]

Under the current rules, the payment obligation rests with the "Completing Carrier." 47 CFR § 64.1300(b). The Completing Carrier for a long distance call is

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[12] *Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, 18 FCC Rcd 19975 (2003) ("*Tollgate Order*").

defined as "a long distance carrier or switch-based long distance reseller that completes a coinless access code or subscriber toll-free payphone call." 47 C.F.R. § 64.1300(a). In general, the Completing Carrier is the IXC that has the billing arrangement with the party billed for the call.

Under the FCC's rules, Completing Carriers are required to track calls from payphones and compensate the appropriate PSP for every completed call. This obligation is significant because once a call leaves a PSP's payphone, the PSP receives no information from the network regarding (1) the carrier to whom the call was routed, or (2) whether the call was completed for compensation purposes. Only the carrier to whom the call is routed for delivery to an end user is able to track the call through the network to determine if it is completed.

The FCC's rules also impose significant obligations on the IXCs that carry calls to the Completing Carrier. The FCC's rules define such IXCs as "Intermediate Carriers." 47 C.F.R. § 64.1310(b). Intermediate Carriers are required to provide PSPs with quarterly reports listing (1) all the IXCs to whom the Intermediate Carrier delivered dial-around calls; (2) the toll-free and access code numbers to which calls were routed; (3) the volume of calls to each such number from each of the PSPs payphones; and (4) contact information for each IXC to whom calls were delivered. 47 C.F.R. § 64.1310(c). This information is critical to the ability of PSPs to collect and monitor their compensation payments. Without it, PSPs would have no way of knowing how many calls were delivered to any particular SBR and no basis for estimating how much compensation is owed by that SBR.

Thus, even where they are not the Completing Carrier, AT&T and MCI play a critical function in the dial-around process. If the mergers go forward, then the combined entities will be able to discriminate not only through their own payments but also in how they gather and provide the information critical to independent PSPs' ability to recover compensation from other carriers.

2. The dial-around compensation process

As the FCC has recognized, because "PSPs often do not have sufficient information to determine which carrier ultimately completes a given call," they "are often at a disadvantage in the per-call compensation process." *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, Fifth Order on Reconsideration and Order on Remand, 17 FCC Rcd 21274, ¶ 95 2002). Because they do not know to which carrier a call is routed, PSPs generally cannot bill a particular IXC for a particular amount of dial-around compensation each quarter.[13] Instead, PSPs are completely dependent on the IXCs to accurately track and pay for the calls they complete. As described below, it is up to each IXC to pay each PSP for whatever number of calls the particular IXC claims it carried from each of the PSP's payphones. While the FCC has put certain measures in place to verify carrier tracking and payment procedures, *PSPs are dependent on the carriers from whom compensation is owed to determine the amount they owe.*

Dial-around compensation arrives three to six months after the dial-around calls for which the payment is made, without any advance notice to the PSP as to the amount of the payment. Many of the "business rules" of the dial-around compensation system are not expressly specified in the FCC's rules; instead, they evolve as industry practices that are not necessarily even uniformly followed by IXCs. Since there is little or nothing that PSPs can do, short of litigation, to exercise influence over IXCs' call

[13] Dial-around compensation is paid on a quarterly basis pursuant to the FCC's rules.

tracking and payment practices, many of these practices have been unilaterally adopted by the larger IXCs with little or no negotiation with PSPs.

Such a system is obviously far from perfect. In order for PSPs to be able to reasonably rely on it, PSPs must be assured that the [illegible] compensation for the calls.[14] In order for Flex ANI identification digits to be transmitted from a payphone line to an IXC such as AT&T or MCI, the LEC serving the payphone, such as SBC or Verizon, must install Flex ANI capability in the central office switch serving the payphone, and each IXC must order Flex ANI service from that LEC. Flex ANI must be ordered and provisioned at every individual switch and on every individual line in the LEC's network, requiring complex coordination between the LEC and the IXC.

The correct ordering and provisioning of Flex ANI is critical to the ability of SBC's and Verizon's PSP competitors to collect dial-around compensation.[15] If a LEC does not properly provision the service, or if the IXC does not properly order Flex ANI from the LEC, then it is generally not possible for the IXC to recognize a call as having originated from a "smart" payphone. As a result of Flex ANI failures, a significant number of payphone calls go uncompensated. It is therefore significant that, if the mergers are allowed to go forward, SBC and Verizon will be in the position of providing Flex ANI to their own IXC affiliates to enable those IXC affiliates to pay compensation to SBC's and Verizon's PSP competitors. This creates multiple disincentives for AT&T/SBC and Verizon/MCI to use care in ensuring that Flex ANI functions properly to identify calls originating from their PSP competitors' payphones.

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[14] When Flex ANI is not available, some IXCs have been able to use alternative methods of identifying payphone-originated calls, but these methods require IXCs to perform additional procedures and, as utilized by IXCs, may not capture all payphone-originated calls.

[15] Flex ANI is only available because the FCC required it over the objection of SBC, Verizon, and other LECs. *See Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, 13 FCC Rcd 4998 (Com. Car. Bur. 1998) ("*Coding Digit Waiver Order*").

After an IXC such as AT&T or MCI identifies the calls on its network that originated from a payphone, the records of those calls are then sent through a complicated flow of processes and databases in order to (1) verify that the call did in fact originate from a payphone, (2) screen out uncompleted calls, (3) sort out calls for which other carriers are ultimately responsible, and (4) eliminate certain calls based on specific business rules and procedures. Records of payphone calls are then accumulated into quarterly files for dial-around compensation processing.

b. The payment process

The processing of dial-around compensation payments involves not only the IXCs, but also the IXCs' payment clearinghouse, PSP billing clearinghouses, and individual PSPs. The process, involving as much coordination as it does among the various parties, requires the good faith and diligent efforts of all parties involved. The process begins with each PSP sending a list of its originating payphone numbers (known as "ANIs"[16]) to its processing clearinghouse. The largest of these is APCC Services, Inc. ("APCCS"), and its process is typical. During each quarterly compensation cycle, APCCS receives from each of its PSP customers a list of the PSPs' ANIs eligible for payment under the Commission's rules. The individual PSP lists are combined and aggregated into a single list and put into a format that will be processed by and is compatible with the processing capabilities of the IXC clearinghouses and individual carriers. The aggregated list is then sent to AT&T, MCI and hundreds of other carriers, and the IXC clearinghouses.

The IXCs and their payment clearinghouses compare the ANI lists they receive from various PSPs and PSP billing aggregators with separate payphone "LEC

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[16] ANI is an acronym for automatic number identification.

ANI lists" provided by various LECs, including SBC and Verizon. The PSP lists and the LEC ANI lists are compared to validate that the ANIs submitted by the PSPs match with an ANI on a LEC ANI list. If there is an ANI on the PSP list that does not have a counterpart on the LEC ANI list, the IXC payment clearinghouse treats the "disputed" ANI[17] as ineligible for compensation. It is left to the PSP to attempt to get the error corrected in time to try to get payment for the ANI in a later payment cycle. Similarly, if there is an ANI on the LEC list for which no PSP seeks payment, the IXC clearinghouse makes no effort to ascertain which PSP should be paid for that ANI.[18]

Once the IXC's payment clearinghouse has a list of ANIs for which the IXC intends to pay, the list of ANIs must in some manner be matched up against the IXC's stored payphone call records. This process may be done by the payment clearinghouse based on data sent to the clearinghouse by its IXC customers or it may be done by the clearinghouse's sending the list of validated ANIs to the IXCs. In either case, the process is entirely dependent on the data and call tracking records generated by the IXCs, for which the IXC clearinghouse has no responsibility and for which the IXC clearinghouse does no independent validation. In the end, it is up to AT&T, MCI, and

[17] ANI mismatches, or disputed ANIs, are a major source of contention. It is not only the ANI that has to match up; for example, the billing name and address for the ANI must also match. In some cases, small discrepancies in the address are used as the basis for an IXC payment clearinghouse to deny payment on an ANI. Other issues can also create disputed ANIs, such as area code mismatches when area code changes occur. The IXC payment clearinghouse may or may not make an effort to catch these kinds of errors or simply deny payment.

[18] The description of IXC payment clearinghouse functions contained in the text, while mechanical in that it describes the steps, is intended to be conceptual. The steps could occur in different sequence or at a different place in the clearinghouse/payment process. Similarly, the exact process by which a particular step in the payment process is effectuated may differ from the mechanical description contained in the text.

other IXCs to count the number of compensable calls they have carried and thereby to determine the amount of compensation that they will pay to PSPs.

Once the number of calls for each ANI has been ascertained, the IXC payment clearinghouse produces a report for each ANI for each of its carrier customers.[19] Those reports are then translated into payment due each ANI and aggregated up to the payment due each PSP and in turn the various PSP aggregators. At the appropriate point in time in the billing cycle, the money necessary to pay the PSPs and the aggregators will be transferred between the IXC and its payment clearinghouse and transmitted on to the PSPs transferred unilateral adjustments of payments further complicates the payment process and remains a source of controversy between PSPs and IXCs.

Once payment is received by the PSP clearinghouse, the accompanying data is disaggregated and broken out into reports for individual PSPs. Each PSP is sent a report showing the payment received for each of that PSP's ANIs along with the ANI specific detail information required by the Commission's rules, assuming it has been sent by the IXC or the IXC clearinghouse. The report may also contain information identifying ANIs that the carrier disputed and for which the carrier did not pay compensation, ANIs on which the carrier paid the "surrogate" instead of per call compensation, etc. While, throughout this process APCC Services is in communication with the IXC clearinghouses to verify that proper payments are being made,[20] ultimately, PSPs are dependent on the data received from AT&T, MCI, and other IXCs and their clearinghouses.

III. THE MERGED ENTITY WOULD ACQUIRE THE INCENTIVE AND THE ABILITY TO MANIPULATE THE PAYPHONE COMPENSATION SYSTEM IN ANTICOMPETITIVE WAYS

As noted above, if the proposed mergers are allowed to go forward, the nation's largest PSP (Verizon), with more than 25% of the nation's payphone base, would acquire the second largest IXC (MCI), and the second largest PSP (SBC), with about 20% of the nation's payphones, would acquire the largest IXC (AT&T). Each of the post-merger companies would have roughly 20 - 25% of the payphone market while at the same time each would be the payor for 20 - 35% of the reported dial-around calls

[20] For example, if a particular ANI was paid for an excessive number of calls, there may be consultation with the carrier(s) and/or PSP to ascertain whether there was an error or whether there may be some other irregularity involved.

subject to the FCC's payphone compensation requirement. Thus, the two largest payphone competitors, SBC and Verizon, would be merged with the two largest sources—AT&T and MCI—of a crucial revenue source that dramatically determines the extent to which independent PSPs can compete.

As explained below, as a result of the mergers, each of the post-merger companies—AT&T/SBC and MCI/Verizon—would have a substantially reduced incentive to invest resources in maintaining an accurate dial-around call tracking and payment system. Moreover, in making the many unilateral judgments that IXCs have an opportunity to make as to what practice to follow in operating this complex call tracking and payment system, the merged AT&T/SBC and MCI/Verizon would have a substantially increased incentive to make decisions and adopt practices that reduce or delay the flow of dial-around compensation payments to their PSP competitors.

A. A Merged AT&T/SBC Or MCI/Verizon Entity Would Have A Greatly Increased Disincentive To Devote Sufficient Resources To Ensuring Accurate Dial-Around Compensation Payments

The payphone compensation system established by the FCC under Section 276 of the Act is a very unusual system of payments because it places reluctant payers—IXCs—in charge of determining the amount of payments they must make for a service—access to payphones—that PSPs are powerless to withhold from them. As noted above, the compensation system relies on the IXCs to make an honest determination of how many dial-around calls they have completed from each payphone and to pay the owner of each payphone for those completed calls. Although safeguards were recently added to the rules to provide some opportunity for PSPs to verify that IXCs are accurately counting their completed calls, those safeguards are far less protective than those sought by PSPs—including the then non-IXC-affiliated payphone divisions of SBC and Verizon.[21] Moreover, those safeguards are totally untested. As a practical matter, IXCs have a significant amount of latitude in the amount of resources they choose to invest and the design decisions they make in building a dial-around call tracking system, and the degree of care they exercise in maintaining and supervising the operation of the system.

Whatever the incentives that IXCs such as AT&T and MCI currently have to invest the necessary discretionary resources to ensure that they accurately count the dial-around calls originating from payphones, the acquisition of a large PSP such as Verizon or SBC would decrease those incentives substantially. A post-merger AT&T/SBC or MCI/Verizon would be competing in the payphone market with the recipients of AT&T's and MCI's dial-around compensation payments. Therefore, the post-merger AT&T/SBC and MCI/Verizon would have a strong incentive to limit the amount of dial-around compensation paid to their PSP competitors. The less dial-around compensation that these PSPs receive, the more handicapped they would be in competing with the post-merger AT&T/SBC or MCI/Verizon in the payphone market. On the other hand, even though the same practices could—in the absence of discrimination—result in less dial-around compensation for the combined entities' payphone affiliates, that reduction would have no effect at the "enterprise" level because the reduced revenue would be offset by an equal reduction in costs for the IXC operations.

Therefore, the post-merger AT&T/SBC and MCI/Verizon are likely to limit or reduce their investment in their own payphone call tracking systems. As a result, the

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21 *Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, Order on Reconsideration, CC Docket No. 96-128, FCC 04-251 (rel. October 22, 2004) ("*Tollgate Reconsideration Order*").

call tracking systems of the post-merger AT&T/SBC and MCI/Verizon will become less accurate and less likely to “catch” all compensable calls, and the PSPs will go unpaid for will degrees of frequency and zeal, IXCs such as AT&T and MCI have conducted reviews of their past payments in order to identify allegedly erroneous overpayments. As noted above, these IXCs have attempted to correct such payments by deducting the amount allegedly overpaid – in some instances totaling millions of dollars—from their current compensation payments to the affected PSPs. These takebacks, which have caused major disruption and economic harm to the affected PSPs, have generated a significant amount of controversy between PSPs and IXCs, including AT&T and MCI. As a result of one such controversy, AT&T agreed not to engage in takebacks under certain circumstances. However, in a recent rulemaking decision, the Commission declined to prohibit all takebacks, and neither AT&T nor MCI have indicated they will altogether cease engaging in takebacks. *Tollgate Reconsideration Order* ¶ 19 n.66.

There remain a number of unresolved issues, however, concerning the legality of takebacks and the applicable procedural requirements. For example, PSPs contend that IXCs should be required to give advance notice of takebacks, to provide advance information on the payphones and calls in a planned takeback, and to provide an opportunity for the PSP to dispute the basis for the takeback. Major IXCs such as AT&T and MCI have provided some advance notice and information regarding recent takebacks, but do not acknowledge that any particular takeback procedures are legally required.[23]

The incentives for AT&T and MCI to engage in takebacks of questionable merit without according procedural protections to the affected PSPs will substantially increase if the FCC approves SBC's acquisition of AT&T and Verizon's acquisition of MCI. Since the impact of a substantial takeback can be catastrophic for the affected

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[23] Letter to Marlene Dortch from Albert H. Kramer and Robert F. Aldrich, CC Dkt. No. 96-128 (April 15, 2004).

PSPs, the merged SBC/AT&T and Verizon/MCI entities will gain a double advantage from takebacks. The takebacks will not only recoup money that AT&T and MCI claim to have overpaid, but in the process will also inflict significant economic harm on the PSPs competing with their respective SBC and Verizon payphone affiliates, and even if applied in a facially nondiscriminatory manner will have a discriminatory impact, since the takebacks would be "neutral" with respect to the affiliated PSP divisions and at the enterprise level.

Therefore, the post-merger AT&T/SBC and MCI/Verizon will have substantially greater incentive to "err" on the side of identifying past payments as overpayments and "taking back" the amounts allegedly overpaid to their payphone competitors by deducting them from current compensation payments. The post-merger entities will also have substantially less incentive to provide their PSP competitors with advance information that would enable them to dispute the takebacks. Even with sufficient information, contesting takebacks causes a drain on PSPs' resources and is not feasible in every case as a practical matter. Even if PSPs are able to dispute such "takebacks" and the amounts identified as overpayments are later found to be legitimately due, AT&T/SBC and MCI/Verizon will have benefited from the takebacks by depriving their PSP competitors of the use of the amounts in controversy during the pendency of the dispute. Because the dial-around compensation paid by AT&T and MCI constitutes such a large portion of PSP revenue, even a delay in receiving the compensation would cause havoc to independent PSPs. Without that revenue stream, they might be unable to make loan or commission payments or service their payphones. The end result would be payphones removed from service, and in some cases, the PSP being forced to exit the market.

2. The post-merger AT&T/SBC and MCI/Verizon will have a substantially greater incentive to withhold payments from high-volume payphones operated by their payphone competitors

Many IXCs withhold payments for payphones that they consider to be generating suspiciously high numbers of dial-around calls. IXCs believe that some PSPs may be generating spurious dial-around calls by means of automatic dialers in their payphones in order to inflate their compensation payments. IXCs therefore establish parameters to identify payphones that might be producing such calls and withhold payments from those payphones. Establishing the criteria for such holdbacks and providing information to PSPs regarding the amounts held back has been unilaterally determined by the IXC. In the past, AT&T, MCI, and other IXCs have held back payments to high-volume payphones without even informing PSPs that payments were held back. Although some of these IXCs have begun providing more information about holdbacks, they have not acknowledged any legal requirement to do so.

The post-merger AT&T/SBC and MCI/Verizon would have a greater incentive as well as the ability to increase the number of payphones placed on "high-volume" lists of payphones from which compensation payments are withheld, and to withhold payments without fully informing PSPs. As a result, PSPs may not even learn of the holdbacks. Moreover, even if the PSP learns of the holdback, disputing such holdbacks causes a drain on PSP resources. Thus, the PSP may not be able to contest the holdback as a practical matter, and if it does, and ultimately succeeds in convincing the IXC that the payphone is generating legitimate calls, the PSP will still have suffered economic harm as a result of the delay in payment, the consequent interruption of potentially critical cash flow, and the cost incurred in contesting the holdback.

There are also opportunities for the post-merger AT&T or MCI to discriminate in holdback practices by applying stricter criteria to holding back payments from unaffiliated PSPs than from its own SBC or Verizon payphone affiliate. Of course, even if the same holdback criteria are applied to affiliated and unaffiliated PSPs, the overall impact of holdbacks on the IXC's own LEC payphone affiliate will be enterprise neutral—any payments business in jeopardy. To the extent that late payments weaken or destroy the PSP competitors of the SBC and Verizon payphone divisions, AT&T/SBC and MCI/Verizon will have substantially increased incentives to delay their compensation payments.

4. The post-merger AT&T/SBC and MCI/Verizon will have a substantially reduced incentive to exercise care in testing the Flex ANI service that is needed to track calls from their competitors' payphones

The post-merger AT&T/SBC and MCI/Verizon will have a substantially reduced incentive to be diligent in ordering and testing Flex ANI service. As discussed above, there is already a major problem with the reliability of this critical service.

The Flex ANI service has a history of erratic operation. Frequently, unrelated changes made in switching hardware or software can cause interruptions in the operation of Flex ANI at certain switches or certain lines, or even for certain kinds of toll-free calls. Therefore, the FCC requires IXCs to test Flex ANI service and coordinate with LECs under carrier-to-carrier procedures to ensure that they are receiving the Flex ANI identification digits. *See Coding Digit Waiver Order*, 13 FCC Rcd at 5020 ¶ 37. The FCC orders, however, do not specify the frequency of such tests or what kind of tests the IXC should perform.

The post-merger AT&T/SBC and MCI/Verizon would have substantially less incentive to be diligent in testing for proper transmission of Flex ANI digits on dial-around calls. Indeed, Flex ANI presents an unusually high potential for discrimination because of the difference in the payphones and network connections used by SBC and Verizon, on the one hand, and their PSP competitors, on the other. As noted above, the PSPs with whom SBC and Verizon compete use almost exclusively "smart" payphones that depend on the LEC's Flex ANI service to identify payphone calls for IXCs. By contrast, SBC and Verizon employ predominantly "dumb" payphones using specialized legacy payphone lines that are "hard-wired" at the central office to transmit identifying information without the need to rely on Flex ANI service. Therefore, if AT&T or MCI generally become less diligent in testing for proper transmission of Flex ANI digits, and this lapse in diligence results in more Flex ANI problems and increased failures by AT&T and MCI to identify payphone calls, the negative impact on compensation payments fall exclusively on PSPs competing with the merged entities. It will have virtually no impact on the compensation collected by the AT&T/SBC and MCI/Verizon payphone divisions.

In addition, the post-merger entities' LEC affiliates (*i.e.*, SBC and Verizon) would have an additional disincentive to be diligent in satisfying their monitoring, maintenance and coordination obligations *vis-à-vis* Flex ANI service provided to their IXC affiliates. To the extent that Flex ANI fails due to errors or negligence on the part of SBC or Verizon, that failure not only would harm SBC's and Verizon's PSP competitors, but also would benefit the AT&T and MCI affiliates by reducing the amount of compensation they pay to SBC's and Verizon's PSP competitors of compensation to which they are entitled.

5. The post-merger AT&T/SBC and MCI/Verizon will have a substantially greater incentive as well as the ability to adjust their business practices regarding payments for non-Flex ANI payphones operated by their PSP competitors

The post-merger AT&T/SBC and MCI/Verizon will have a substantially greater incentive as well as the ability to adjust their business practices regarding payments for non-Flex ANI payphones operated by their PSP competitors. IXCs have a number of payment options with respect to the roughly 5% of payphones from which Flex ANI digits or other payphone-specific information digits are not currently transmitted. Some IXCs, including MCI, have sometimes used alternative methods to track payphone-originated calls and make per-call payments notwithstanding the unavailability of Flex ANI. Others, including AT&T, have chosen to make their payments for non-Flex-ANI payphones based on a per-phone “surrogate” payment prescribed by the FCC.

In cases where Flex ANI starts or stops working for certain payphones in the middle of a quarter, there are additional variations in carrier practices. Some carriers choose to pay per-phone compensation for the entire quarter, notwithstanding the availability of Flex ANI during part of the quarter. Other carriers choose to pay per-call compensation for the portion of the quarter for which per-call tracking is feasible.[26]

Depending on the number of payphones affected, these variations in carrier practices may have a significant impact on a PSP’s compensation payments. The post-merger AT&T/SBC and MCI/Verizon would have a substantially greater incentive to adjust their practices regarding payment for non-Flex ANI payphones in ways that minimized total compensation payments to independent PSPs. These practices would have little if any impact on the merged entities’ own LEC-affiliated PSPs, because those PSPs use predominantly “dumb” payphones that do not rely on Flex ANI and therefore do not require per-payphone “surrogate” payments when Flex ANI is unavailable.

6. The post-merger AT&T/SBC and MCI/Verizon will have a substantially reduced incentive to provide timely, accurate, and complete data identifying calls routed to resellers from their PSP competitors’ payphones

The post-merger AT&T/SBC and MCI/Verizon would have substantially reduced incentives to provide timely, accurate, and complete data identifying calls

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[26] A significant number have also failed to make any payment where a phone was in service for most of the quarter but might not have been in service on the last day of the period. While this practice is clearly violative of the FCC’s requirements, it has occurred on numerous occasions.

routed to resellers from their PSP competitors' payphones. PSPs already face this problem with respect to certain Intermediate Carriers, but it is likely to become much worse if the two largest IXCs acquire an incentive to limit the information provided to SBC's and Verizon's PSP competitors.

As discussed above, the FCC's compensation rule imposes certain obligations on IXCs such as AT&T and MCI when they act as Intermediate Carriers. Typically, the dial-around calls handled by AT&T and MCI as Intermediate Carriers are routed to call processing platforms operated by their SBR customers.[27] Since the establishment of the per-call compensation system in 1997, PSPs have encountered huge problems in collecting collecting

format of the additional data they are required to provide. In their attempts to verify the accuracy of the payments they receive from SBRs PSPs are totally dependent on the timely availability of reliable, complete data reports and underlying call data from Intermediate Carriers such as AT&T and MCI,

The post-merger AT&T/SBC and MCI/Verizon would have substantially less incentive to provide Intermediate Carrier data reports to their PSP competitors that are timely, accurate, and complete, and substantially less incentive to provide underlying data in a timely fashion that includes the additional information their PSP competitors may need to verify SBR payments. As a result, PSPs competing with the payphone divisions of AT&T/SBC and MCI/Verizon would find it substantially more difficult to collect the full amount of compensation they are due from SBRs.

At the same time, the post-merger AT&T/SBC and MCI/Verizon would have an incentive to provide more complete and accurate Intermediate Carrier data to their LEC-affiliated PSPs.

7. The post-merger AT&T/SBC and MCI/Verizon would have a substantially reduced incentive to collect and remit compensation payments owed by resellers pursuant to alternative payment agreements

The post-merger AT&T/SBR and MCI/Verizon would have substantially less incentive to be diligent in collecting compensation payments from SBRs and remitting them to PSPs pursuant to alternative payment arrangements. Under the FCC's payphone compensation rule, SBRs who do not want to establish their own call tracking systems may arrange an alternative payment mechanism with an Intermediate Carrier such as AT&T and MCI, whereby the Intermediate Carrier pays the PSP on the SBR's behalf. 47 CFR § 64.1310(a). In the most recent payment cycles, AT&T and MCI collectively reported that they had entered alternative payment arrangements on behalf of more than 100 SBRs. The terms of these alternative payment arrangements may vary, as well as the Intermediate Carrier's practices with respect to enforcement. If the IC fails to collect payments from the SBR, the IC may refuse to pay the PSP pursuant to the alternative payment arrangement, and the PSP may be unable to collect payment directly from the SBR.

The post-merger AT&T/SBC and MCI/Verizon would have a substantially lower incentive to be diligent in collecting and remitting SBR's compensation payments to their PSP competitors. By withholding compensation payments for SBRs from their PSP competitors on the ground that they have not been able to collect the payments from the SBRs, AT&T/SBC and MCI/Verizon would inflict economic harm on their PSP competitors. Thus, AT&T/SBC and MCI/Verizon would have an increased incentive to fail to pursue their SBR customers who delay or refuse payment of the compensation amount to be remitted to PSPs.

8. The post-merger entities would have a greater disincentive to be diligent in maintaining accurate ANI lists and more incentive to use minor discrepancies in ANI matchups as an excuse to deny compensation to their PSP competitors

The LEC affiliates of the post-merger entities would have a substantially greater disincentive to be diligent in maintaining accurate lists of the payphone lines, or "ANIs," subscribed to by their PSP competitors. IXCs use these lists to validate that the ANIs submitted by a PSP for payment of compensation are eligible for payment, and the PSP submitting the compensation claim for those ANIs is actually entitled to payment for those ANIs.

Post-merger, SBC and Verizon will have a greater disincentive to be diligent in maintaining accurate lists of the ANIs and in responding to requests for verification of disputed ANIs. If SBC, for example, fails to include certain of its PSP competitors'

ANIs on its ANI lists, and as a result, SBC's affiliate AT&T declines or delays payment for those ANIs, then AT&T/SBC will not only have gained a competitive advantage, but also will have saved the amount of compensation withheld from PSPs.

In addition, the post-merger AT&T and MCI will have a greater incentive to use small discrepancies in the PSP's name or address listings on its compensation claim and on the LEC's verification listings as the basis for denying payment for the affected ANIs. Similarly, the post-merger AT&T or MCI will be more likely to use area code mismatches due to recent area code changes as an excuse to deny payment.

9. The post-merger AT&T/Verizon and MCI/SBC would have an additional incentive to withhold from their PSP competitors calling data needed by the PSPs to check the accuracy of compensation payments made by large IXCs.

The post-merger AT&T/Verizon and MCI/SBC would have an additional incentive to withhold from their PSP competitors calling data that is currently made available to PSPs by some LECs, including SBC, and that is used by the PSPs to check the accuracy of compensation payments made by large IXCs. SBC currently offers PSPs a service that provides data, including the date, time, duration and number dialed for all call attempts made to toll-free numbers from specified payphones. Although the data, known as CCD data, does not necessarily indicate whether dial-around calls were completed, it provides an essential means of checking for patterns indicating, for example, that certain long-duration call attempts have not been recorded and paid as completed calls. CCD data has played an important role in a number of lawsuits brought by PSPs against IXCs for alleged underpayment of dial-around compensation.

Currently, a LEC such as SBC is willing to offer CCD data to independent PSPs, presumably because it is profitable to do so. SBC's acquisition of MCI, however, would create an additional incentive for SBC to cease offering the service to independent PSPs. Similarly, Verizon's acquisition of AT&T would create an additional incentive for Verizon to decline to make CCD available to independent PSPs. Meanwhile, the post-merger entities undoubtedly would continue to use CCD to aid their own PSP f[illegible]

continue aid

11. The post-merger AT&T/SBC and MCI/Verizon would have a substantially greater incentive to adopt business rules that result in reduced payments to PSPs

The post-merger AT&T/SBC and MCI/Verizon would have a substantially greater incentive to adopt business rules in other areas where the FCC rules are not explicit in order to reduce their compensation payments to their PSP competitors. For example, some IXCs appear to be taking the position that calls made from payphones to the IXC's customer service center are "uncompleted calls" for which no compensation need be paid. APCC believes there can be no dispute that such calls are "completed calls" subject to compensation, since the calls are completed to the intended called party, the customer service center. However, the FCC has not issued an explicit ruling on this subject. If AT&T/SBC and MCI/Verizon declined to pay for calls to their customer service centers on the grounds that they were "uncompleted" calls, their compensation payments to their PSP competitors would be substantially lower than if they defined customer service calls as "completed calls." In order to halt such practices, PSPs, once again, would incur litigation costs that drain their resources, and would likely go unpaid for large volumes of customer service calls pending the completion of litigation.

12. The post-merger AT&T/SBC and MCI/Verizon would have a strong incentive as well as the ability to share information with their PSPs about the volume of completed dial-around calls from competitors' payphones

The post-merger AT&T/SBC and MCI/Verizon would have a strong incentive as well as the ability to share information with their PSPs about the volume of completed dial-around calls from competitors' payphones. In so doing, the post-merger entities would provide an unwarranted competitive advantage to their PSP affiliates. Information held by one of the two largest IXCs about the volume of dial-around calls completed from particular payphones operated by PSP competitors is considered highly sensitive. Such information would be of great value to the IXCs' PSP affiliates because it would help the PSP affiliate focus its marketing efforts n locations most likely to provide a profitable return on investment.

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The examples described immediately above involve circumstances where, by making a judgment that has the effect of delaying or reducing the flow of compensation payments to their PSP competitors, the post-merger AT&T or MCI can inflict economic harm on their PSP competitors. There are numerous other similar situations in which, by delaying or reducing the flow of compensation, AT&T or MCI can inflict competitive harm on rival PSPs.

IV. POTENTIAL REMEDIES

The simplest, cleanest way to prevent the injuries that the proposed mergers would cause to payphone competition is to deny the mergers. Allowing either the AT&T/SBC merger or the MCI/Verizon merger would lead to all of the anticompetitive effects described above, and allowing both mergers would multiply those effects. Therefore, the most appropriate remedy is simply to deny the mergers.

In the event that the mergers are allowed, there are a number of ways that the mergers could be conditioned in order to limit (but not wholly eliminate) anticompetitive effects on the payphone market. These include:

- imposing behavioral restraints such as enjoining the combined entities from modifying their dial-around compensation payment procedures or using their payments to benefit their own payphone operations;

- requiring accounting and "regulatory structural" safeguards to restrain the ability of the combined entities to bolster their payphone operations with revenue from elsewhere in the enterprise and share information about PSP competitors; and

- requiring SBC/AT&T and Verizon/MCI to divest themselves of their payphone assets prior to consummation of the merger.

Of these options, the first two have inherent limitations that make them inadequate to prevent the combined entities from engaging in anticompetitive conduct with respect to their payphone operations. Both behavioral restraints and regulatory accounting/structural safeguards are difficult and costly to police. The reality is that it is almost impossible to mandate that an enterprise act counter to its economic interests and not expect the enterprise to find ways to subvert those restrictions. Even if it were possible to design reliable protective measures, they would invariably become outdated as the industry and the combined enterprises change over time.

The only remedy that is promising—short of denying the mergers outright—is to require the divestiture of the combined entities' payphone operations. This approach would be the simplest to implement, would require no policing after it was implemented, and removes the incentives that the combined enterprises would otherwise always have to discriminate in favor of their own payphone operations.

Requiring the divestiture of their payphone operations will not affect the current combined operations of the respective LECs and their payphone divisions. The fact that both Qwest and BellSouth have already exited the payphone market reflects the fact that payphone operations are not an essential part of the BOCs' core service offerings. It also suggests that divestiture is viable and that the market can absorb the divested assets.