

**REPLY DECLARATION OF  
DENNIS W. CARLTON AND HAL S. SIDER**

May 9, 2005

**In connection with the proposed transaction, SBC intends to file a registration statement, including a proxy statement of AT&T Corp., and other materials with the Securities and Exchange Commission (the "SEC"). Investors are urged to read the registration statement and other materials when they are available because they contain important information.** Investors will be able to obtain free copies of the registration statement and proxy statement, when they become available, as well as other filings containing information about SBC and AT&T Corp., without charge, at the SEC's Internet site ([www.sec.gov](http://www.sec.gov)). These documents may also be obtained for free from SBC's Investor Relations web site ([www.sbc.com/investor\\_relations](http://www.sbc.com/investor_relations)) or by directing a request to SBC Communications Inc., Stockholder Services, 175 E. Houston, San Antonio, Texas 78205. Free copies of AT&T Corp.'s filings may be accessed and downloaded for free at the AT&T Relations Web Site ([www.att.com/ir/sec](http://www.att.com/ir/sec)) or by directing a request to AT&T Corp., Investor Relations, One AT&T Way, Bedminster, New Jersey 07921.

SBC, AT&T Corp. and their respective directors and executive officers and other members of management and employees may be deemed to be participants in the solicitation of proxies from AT&T shareholders in respect of the proposed transaction. Information regarding SBC's directors and executive officers is available in SBC's proxy statement for its 2004 annual meeting of stockholders, dated March 11, 2004, and information regarding AT&T Corp.'s directors and executive officers is available in AT&T Corp.'s proxy statement for its 2004 annual meeting of shareholders, dated March 25, 2004. Additional information regarding the interests of such potential participants will be included in the registration and proxy statement and the other relevant documents filed with the SEC when they become available.

Certain matters discussed in this statement, including the appendices attached, are forward-looking statements that involve risks and uncertainties. Forward-looking statements include, without limitation, the information concerning possible or assumed future revenues and results of operations of SBC and AT&T, projected benefits of the proposed SBC/AT&T merger and possible or assumed developments in the telecommunications industry. Readers are cautioned that the following important factors, in addition to those discussed in this statement and elsewhere in the proxy statement/prospectus to be filed by SBC with the Securities and Exchange Commission, and in the documents incorporated by reference in such proxy statement/prospectus, could affect the future results of SBC and AT&T or the prospects for the merger: (1) the ability to obtain governmental approvals of the merger on the proposed terms and schedule; (2) the failure of AT&T shareholders to approve the merger; (3) the risks that the businesses of SBC and AT&T will not be integrated successfully; (4) the risks that the cost savings and any other synergies from the merger may not be fully realized or may take longer to realize than expected; (5) disruption from the merger making it more difficult to maintain relationships with customers, employees or suppliers; (6) competition and its effect on pricing, costs, spending, third-party relationships and revenues; (7) the risk that Cingular Wireless LLC could fail to achieve, in the amount and within the timeframe expected, the synergies and other benefits expected from its acquisition of AT&T Wireless; (8) final outcomes of various state and federal regulatory proceedings and changes in existing state, federal or foreign laws and regulations and/or enactment of additional regulatory laws and regulations; (9) risks inherent in international operations, including exposure to fluctuations in foreign currency exchange rates and political risk; (10) the impact of new technologies; (11) changes in general economic and market conditions; and (12) changes in the regulatory environment in which SBC and AT&T operate.

The cites to webpages in this document are for information only and are not intended to be active links or to incorporate herein any information on the websites, except the specific information for which the webpages have been cited.

I, Dennis W. Carlton, hereby declare the following:

I, Hal S. Sider, hereby declare the following:

## **I. INTRODUCTION AND OVERVIEW**

1. We previously submitted a declaration in this matter dated February 21, 2005.

Our qualifications and curricula vitae are included in that report.

2. In that declaration we concluded based on our preliminary analysis that the proposed merger of AT&T Corp. (AT&T) and SBC Communications Inc. (SBC) would benefit consumers by creating a more efficient firm which would be better positioned to develop and deploy new products and services for business and residential customers. We also concluded that the proposed transaction would be unlikely to create significant competitive problems.

3. We have now been asked by counsel for SBC and AT&T to evaluate in light of our continuing analysis claims made by various parties submitted in opposition to the proposed transaction. We may supplement our response based on continued analysis of opponents' claims.

4. Given the limited time available to prepare a reply, we have not attempted to address each claim made by opponents. Instead we have attempted to identify and respond to the major arguments that are common to a variety of opponents. This reply focuses on comments made by Prof. Joseph Farrell on behalf of Global Crossing, Prof. Simon Wilkie, on behalf of a coalition of CLECs,<sup>1</sup> and Prof. B. Douglas Bernheim on behalf of Qwest. We

---

1. Prof. Wilkie's testimony was sponsored by Cbeyond, Conservent, Eschelon, Nuvox, TDS Metrocom, XO, and Xspedius (hereafter, CLEC Coalition, or Cbeyond, et al).

also address certain comments made on behalf of the National Association of State Utility Consumer Advocates by Lee Selwyn, Helen Golding and Hillary Thompson (hereafter, Selwyn).

5. Our comments focus on opponents' claims that:
  - The proposed transaction significantly reduces competition in the provision of special (or dedicated) access services in SBC's region by (i) eliminating AT&T as an alternative provider of facilities-based dedicated access services and (ii) eliminating AT&T as an "aggregator" or reseller of SBC special access services.
  - The proposed transaction, by increasing vertical integration, creates incentives for the merged firm to disadvantage or discriminate against rival suppliers of business enterprise services by raising special access rates.
  - The proposed transaction, together with the proposed merger of MCI with Verizon (or Qwest), will reduce competition due to "mutual forbearance" by SBC and Verizon (and perhaps other RBOCs).
  - The proposed transaction will reduce competition in the provision of mass market services by eliminating AT&T as an actual or potential competitor.

6. Available data allow us to address several of the concerns raised by opponents. We conclude that there is no empirical support for these concerns. The opposition comments do not lead us to alter our prior conclusion that the proposed transaction is unlikely to result in harm to consumers. The remainder of this declaration is organized as follows:

- Section II addresses opponents' claims that the transaction will reduce (horizontal) competition in the provision of special (or dedicated) access.
- Section III addresses opponents' claims that increased vertical integration resulting from the transaction will result in harm to consumers;
- Section IV addresses opponents' claims that approval of the merger of SBC and AT&T, along with approval of the pending merger of Verizon and MCI, will harm consumers as the result of "mutual forbearance" between the merged companies.
- Section V addresses opponents' claims that the proposed transaction will reduce competition in the provision of services provided to mass market consumers.
- Section VI replies to miscellaneous comments by opponents and their experts made in response to our prior declaration.

## **II. OPPONENTS EXAGGERATE THE PROPOSED TRANSACTION'S EFFECT ON COMPETITION IN THE PROVISION OF DEDICATED ACCESS SERVICES.**

### **A. BACKGROUND AND OVERVIEW OF OPPONENTS' COMMENTS**

#### **1. Background**

7. Special access services "employ dedicated facilities that run directly between the end user and another carrier's point of presence (POP) or between two discrete end user locations."<sup>2</sup> Special access services do not use local exchange switches.<sup>3</sup>

---

2. FCC, In the Matter of Special Access Rates for Price Cap Local Exchange Carriers, WC Docket No. 05-25, Order and Notice of Proposed Rulemaking, January 31, 2005, (hereafter, Special Access NPRM), ¶7.

3. Ibid.

8. There are several components of special access services provided by LECs. These include (i) “channel termination” facilities, which reflect services provided over facilities between a customer’s premises and the LEC end office; (ii) interoffice facilities between the LEC end office and the LEC serving wire center;<sup>4</sup> and (iii) a second “channel termination” between the LEC serving wire center and the competitive carrier’s point of interconnection with the LEC.

9. In certain geographic areas, CLECs also provide dedicated capacity between a customer’s premises and non-LEC interconnection points using their own fiber and other facilities that bypass the LEC’s network.<sup>5</sup>

**2. Concerns regarding reduced competition for facilities-based dedicated access services**

10. Several opponents claim that the proposed transaction will reduce horizontal competition in the provision of special (or dedicated) access services provided by AT&T and SBC. For example, Prof. Farrell writes:

Of most direct concern is the elimination of the horizontal competition between SBC and AT&T where both offer facilities-based special access to a building or other appropriately granular geographic market that is not so served by several other carriers. (Farrell, ¶3)

- 
4. The serving wire center is the LEC facility at or near the other carrier’s point of interconnection with the LEC network. The serving wire center is typically a facility that is separate from the LEC end office.
5. “Special Access” are ILEC-provided services. AT&T and other CLECs provide “private line” or “dedicated access” services that compete with ILECs’ special access services. We use the more general “dedicated access” terminology in describing services provided by AT&T and CLECs. However, following opponents’ terminology, we do not distinguish between special and dedicated access in responding to the opponents’ competition arguments.

11. In addition, Prof. Farrell contends that AT&T dedicated access services constrain SBC's "region-wide" prices for special access services.<sup>6</sup> Other opponents make similar claims.<sup>7</sup> We respond to these concerns in Section II.B below.

**3. Concerns regarding reduced competition in resale of dedicated access services.**

12. A second horizontal concern raised by certain opponents is that the transaction eliminates competition between SBC and AT&T acting as a reseller of SBC special access services. According to opponents, AT&T is able to purchase SBC special access services at significant volume discounts and then actively resells these services on a wholesale basis to other carriers not eligible for such discounts.<sup>8</sup>

13. For example, Prof. Wilkie states:

... AT&T and MCI compete in local wholesale access markets by providing circuits over their own facilities or by exploiting their special access volume discounts and reselling ILEC circuits to smaller competitors. In the latter role, MCI and AT&T act as efficient aggregators [...] to facilitate CLEC entry to serve business customers through the volume discounts in the special access tariff that MCI and AT&T obtain. (Wilkie, ¶17)

14. Other opponents make similar comments.<sup>9</sup> We respond to concerns that the proposed transaction may harm competition by eliminating a significant "aggregator" or "reseller" of special access services in Section II.C below.

---

6. Farrell, ¶¶ 29-36.

7. See, for example, Wilkie, ¶6, Bernheim, ¶¶40-41, Broadwing/Savvis, p. 4, CBeyond, et. al., p. 3, CompTEL/ALTS, p. 15, and Global Crossing, p. 15.

8. Using AT&T's terminology, "Type I" special access circuits are provided exclusively through CLEC facilities. "Type II" special access circuits are provided at least in part through facilities of another carrier (usually an ILEC).

9. Broadwing/Savvis, p. 23, CBeyond, et. al., p. 24, CompTel/ALTS, p. 14, Global Crossing, p. 15, and Earthlink, pp. 6-7.

**B. THE PROPOSED TRANSACTION DOES NOT SIGNIFICANTLY REDUCE FACILITIES-BASED DEDICATED ACCESS COMPETITION.**

15. Opponents claim that the proposed transaction will harm competition in the provision of dedicated access services but present no data to support this claim. We have obtained data from AT&T and SBC that permit us to analyze this issue. Our analysis of these data indicates that opponents overstate the importance of AT&T as a supplier of facilities-based dedicated access services in SBC's region and the reduction in competition resulting from the proposed merger. The analysis described below indicates:

- AT&T serves a relatively small number of buildings in SBC's territory;
- AT&T is one of many CLECs that provide local fiber optic facilities in SBC's region;
- Most of AT&T's bandwidth sales are in buildings served by other CLECs, even though AT&T is the only CLEC in many buildings it serves;
- Many buildings served by AT&T are in areas in which other CLECs are not "impaired," as reflected in the FCC's criteria for determining when ILECs are obligated to provide special access services as unbundled network elements;
- Even for the relatively small number of AT&T buildings that are in areas where CLECs may be "impaired," other CLECs operate local fiber networks in those areas. This indicates that rivals are often well positioned to compete to provide services to many of these buildings. Also, the availability of unbundled access in these areas may ameliorate opponents' concerns.

16. Our analysis is organized as follows:



- Following Prof. Farrell’s suggestion, we first evaluate the competitive overlap between AT&T and SBC in the provision of local access services on a “granular” level, using buildings as the geographic unit of analysis.
- Next, we analyze the competitive overlap between SBC, AT&T and other CLECs using the area served by SBC central offices as the geographic unit of analysis. The FCC’s “impairment” criteria and our identification of other CLECs located near buildings served by AT&T use this geographic framework.
- Finally, we analyze the extent of competitive overlap using the MSA as the geographic unit of analysis.

17. Our analysis is limited to the 19 MSAs in SBC’s territory in which AT&T operates local facilities.<sup>10</sup> These are the only areas in which there is a potential reduction in horizontal competition in the provision of local fiber access resulting from the proposed merger.

#### **1. Regulatory and Antitrust Standards**

18. In undertaking this analysis, we make use in part of the FCC’s approaches to evaluating competition in the provision of dedicated access services used in current and past proceedings. For example, we utilize the “impairment standard” for high capacity loops defined in the FCC’s recent Triennial Review Remand Order (TRRO), which is used to

---

10. These areas include: Austin, Chicago, Cleveland, Columbus, Dallas, Detroit, Dayton, Hartford, Houston, Indianapolis, Kansas City, Los Angeles, Milwaukee, Reno, Sacramento, St. Louis, San Antonio, San Diego and San Francisco. For the purposes of our analysis, we treat the San Jose, CA MSA as part of the San Francisco MSA, and the Bridgeport, CT MSA as part of the Hartford MSA.

identify areas in which ILECs are obligated to make high capacity loops available to CLECs on an unbundled basis.<sup>11</sup> We also reference the FCC's framework for establishing special access pricing flexibility in its Access Charge Reform Order.<sup>12</sup>

19. In interpreting our analysis and results, it is important to note that the "impairment" standard defined by the FCC in the TRRO, which is defined in more detail below, is not an antitrust standard but a regulatory one. The FCC "impairment" standard focuses on costs faced by non-incumbent firms in an attempt to identify the likelihood of entry.

20. A building served by AT&T (and thus subject to the loss of an independent supplier as a result of the proposed transaction) is not necessarily harmed by the merger, even if it is in an "impairment" area in which the ILEC is required to offer high capacity loops on an unbundled basis. For example, there may be other CLECs within economical reach of such buildings that will constrain price after the merger. The data discussed below show that most CLEC-lit buildings are in areas served by other CLECs.

21. The data also show that, despite the frequent presence of other CLECs in nearby areas, most CLEC-lit buildings are served by only one CLEC. This can indicate that

---

11. FCC, In the Matter of Unbundled Access to Network Elements, Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers, WC Docket No. 04-313; CC Docket No. 01-338, February 4, 2005 (hereafter, Triennial Review Remand Order, or TRRO).

12. FCC, In the Matter of Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers; Petition of U S West Communications, Inc. for Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA, CC Docket No. 96-262; CC Docket No. 94-1; CCB/CPD File No. 98-63; CC Docket No. 98-157, Fifth Report And Order And Further Notice Of Proposed Rulemaking, August 5, 1999 (hereafter, Access Charge Reform Order)

if one CLEC already serves a building, then others often find it more profitable to serve other buildings (instead of becoming the second CLEC at a location). Under these circumstances, it cannot be inferred that a merger harms consumers in buildings where AT&T is now the only CLEC. The fact that one CLEC serves a building does not suggest that other firms would be incapable of doing so economically if prices were to rise.

22. Similarly, if there are already multiple CLECs in a building, then the loss of an independent competitor also may not adversely affect price. CLECs already serving (or capable of serving) a building will have strong incentives to expand service to that building given that they have already sunk the costs associated with establishing an interconnection.

23. In addition, pricing at locations subject to the loss of an independent supplier may be determined by factors other than the number of suppliers at that location. For example, if the customer purchases services as part of a multilocation contract, pricing may be unrelated to any reduction in the number of competitors at the (limited) number of buildings affected by the proposed transaction. Moreover, the availability of high capacity UNE loops may also serve to lessen concerns that the merger will lessen competition. For example, the FCC concluded in the TRRO that “the availability of UNEs is itself a check on special access pricing ...”<sup>13</sup> A merger also may affect prices in areas where ILECs are not obligated to offer high capacity loops on an unbundled basis, although a merger would be unlikely to result in higher prices in such areas if the regulators have properly identified areas where rivals are capable of readily deploying high capacity circuits.

---

13. TRRO, ¶65.

24. If pricing depends on the number of CLECs with local fiber at a given location, this would imply that a building defines a geographic market. We note that the FCC's Access Charge Reform proceedings rejected the use of geographic areas smaller (and larger) than MSAs for evaluating competition in the provision of special access and has granted "pricing flexibility" on an MSA by MSA basis. In that proceeding, the FCC concluded that "... MSAs best reflect the scope of competitive entry, and therefore are a logical basis for measuring the extent of competition."<sup>14</sup> Thus, we present below certain measures of competitive conditions in the provision of dedicated access services on both building-specific and MSA-specific bases.

25. In making MSA-specific determinations regarding pricing flexibility, the FCC in the Access Charge Reform Order evaluated the extent of CLEC collocation based on the geographic area served by ILEC central offices. Similarly, the TRRO set "triggers" based on conditions in geographic areas served by ILEC central offices. Thus, much of our analysis below maintains these approaches.

26. The FCC's analysis in the Access Charge Reform proceeding also was based in part on the number of CLECs that had collocated facilities in a given ILEC central office. The FCC's framework is based on the view that the presence of collocated firms indicates that firms are well positioned to enter and thus can protect competition in the provision of dedicated access. Thus, even if there is a reduction in the number of CLECs operating in a building served by an ILEC central office, competition may not be harmed due to the

---

14. Access Charge Reform Order, ¶72.

presence of collocaters. Thus, we analyze below the impact of the transaction on the number of collocaters serving SBC's central offices.

## **2. Data Description**

27. Our analysis is based on data from AT&T and SBC. We use data from AT&T that identify: (i) the geographic location of each commercial building served by AT&T local fiber facilities;<sup>15</sup> and (ii) the location of buildings served by CLECs that sell dedicated access to AT&T and that meet AT&T's quality standards.<sup>16</sup> We use these data, together with information from GeoResults, to identify the SBC central office service area in which the buildings served by AT&T and other carriers are located.<sup>17</sup>

28. We also use SBC data that identify the number of CLECs that have fiber-based collocations in SBC central offices and the number of business lines served by each SBC central office.<sup>18</sup> These data are used to classify each service area based on the FCC's

---

15. These data report CLLI code (a unique geographic identifier) for each building directly served by AT&T local facilities, as well as the street address of the building. These data also report the total bandwidth AT&T supplies to each building, expressed in DS0 (64 kbs lines) equivalents. SBC's central offices serving each of these building are identified using data from GeoResults, which provides a mapping of building CLLI codes to ILEC central offices. In certain instances, GeoResults data do not allow this mapping. In these instances, we assume the ILEC central office is the closest ILEC local serving office, which these data identify for AT&T-lit buildings.

16. The Declaration of Anthony Fea, Anthony Giovannucci, Bob Handal and Michael Lesher (hereafter, Fea, et. al.) also reports tabulations based on these data. There appear to be minor differences in the criteria used by Fea, et. al. in analyzing the data. For example, our base analysis of buildings served by AT&T-reported CLECs includes both lit and inactive buildings while their tabulations focus on lit buildings alone. Likewise, we understand Fea et al present results that include buildings outside of the MSAs upon which we focus. There are, however, there are no material differences in the conclusions due to differences in the criteria used.

17. See <http://www.georeresults.com/Databases.htm> for an overview of these data.

18. The data do not include information on fiber collocations for central offices with relatively small numbers of business lines.

“impairment” criteria that define areas in which ILECs are obligated to offer high capacity loops on an unbundled basis.

29. As mentioned above, the AT&T data identify buildings served by CLECs that provide dedicated access to AT&T. The data do not include information for a substantial number of CLECs in SBC’s territory including, for example, Sprint. For example, New Paradigm Research Group (NPRG) identifies seven CLECs operating local fiber networks in Chicago.<sup>19</sup> By comparison, the AT&T data include information on only three AT&T-reported CLECs in Chicago. For MSAs in SBC’s region where AT&T operates local fiber networks, there are, on average, [ ] local networks reported in the AT&T data compared to 6.9 networks reported by NPRG. CLECs that do not report to AT&T or do not have networks that meet AT&T’s quality standards still may be economically significant market participants. Therefore, our use of AT&T-reported data is likely to overstate any competitive concerns.

30. The AT&T data, for example, contain very limited information on cable-based providers of dedicated access circuits. Available SBC data, however, indicate that cable companies have become significant providers of such services.<sup>20</sup> For example, a March 2005 SBC survey found that among the DS-1/ T-1 circuits lost by SBC to competitors in 2004, [ ] percent were captured by cable providers. The SBC report concludes that “...

---

19. Our initial declaration reports analyses based on the data from New Paradigm Research Group.

20. Bernheim (¶65) argues that cable-based services are not a viable option for many business customers.

cable companies who provide both Cable Modem and DS-1/T-1, including [ ], captured almost [ ] of SBC's lost circuits."<sup>21</sup>

### **3. Characteristics of buildings served by AT&T and the extent of competitive overlap**

31. In evaluating the potential impact of the proposed merger on facilities-based competition in the provision of dedicated access, it is important to note that AT&T's local access facilities serve a very modest number of buildings in SBC's region. As shown in Table 1, there are roughly [ ] commercial buildings with more than 10 voice line-equivalents in SBC's 13 state region.<sup>22</sup> AT&T serves [ ] buildings on its local facilities in 19 MSAs in SBC's region.<sup>23</sup> This is roughly 0.4 percent of the [ ] commercial buildings with more than 10 voice line-equivalents in SBC's region.

---

21. SBC Customer Analytics and Research, 2004 DS-1/T-1 Disconnect Study (January-December 2004 Disconnects), pp. 16, 23.

22. Special tabulation from SBC, Customer Research and Analytics based on Dun and Bradstreets data.

23. Our analysis excludes about [ ] AT&T-served buildings in SBC's territory that are located outside the 19 overlap MSAs but in SBC's service territories. Thus, as noted, our analysis differs from that of Fea, et al, who include these buildings in the results they present. The figure also excludes roughly [ ] buildings in the 13-state SBC region but located in areas served by other ILECs.

**Table 1**

**Overview of Buildings in SBC Region**

Group	Buildings
Buildings in SBC States with More than 10 Line Equivalents	
Buildings in 19 Overlap MSAs with More than 10 Line Equivalents	
SBC Fiber Served Buildings in 19 Overlap MSAs	
Buildings Served by AT&T-Reported CLECs in 19 Overlap MSAs	
AT&T-Served Buildings in 19 Overlap MSAs	

Source: SBC/D&B; SBC Fiber to Building Data; AT&T Building Census; AT&T CLEC Census.

Note: Line equivalents are measured in 56 kbps equivalents.

32. The [ ] buildings served by AT&T represent roughly [ ] percent of the roughly [ ] buildings served by AT&T-reported CLECs in the 19 MSAs in SBC’s territory served by AT&T. The AT&T data indicate that there are [ ] CLECs that serve more buildings in the overlap MSAs than AT&T. Some of these buildings are served by multiple CLECs and the total number of building connections is roughly [ ]. AT&T accounts for roughly [ ] percent of all connections made by AT&T-reported CLECs to buildings in the SBC territory

33. Table 2 reports the number of CLEC-lit buildings served by AT&T in each of the 19 overlap MSAs, as well as AT&T’s share of buildings served and total connections.<sup>24</sup> (These figures differ because certain buildings are served by multiple CLECs.) This table also reports the number of buildings in which AT&T is the only CLEC providing service. As the table indicates, there are [ ] buildings in SBC’s region in which AT&T is the only

---

24. Throughout this section, unless otherwise noted, data on “CLEC-lit” buildings refers to CLECs that report data to AT&T. Our calculations include buildings at which CLECs have inactive connections based on our understanding that these buildings can be readily served by the reporting CLEC.



CLEC. That is, [ ] percent of all buildings served by AT&T-reported CLECs in the overlap MSAs are served by AT&T alone.

34. Assuming that SBC also provides fiber to each of these buildings, these would be the only buildings for which there would be a decline from 2 to 1 in the number of fiber-based local carriers as a result of the proposed transaction.

**Table 2**  
**Number of Buildings Served by AT&T and Other AT&T-Reported CLECs by MSA**

MSA	Number of Buildings Served by AT&T	Number of Buildings Served by AT&T and No AT&T-Reported CLECs	Number of Buildings Served by AT&T-Reported CLECs
CHICAGO			
INDIANAPOLIS			
KANSAS CITY			
DALLAS			
LOS ANGELES			
SAN DIEGO			
SAN FRANCISCO			
MILWAUKEE			
ST LOUIS			
DETROIT			
HOUSTON			
HARTFORD			
CLEVELAND			
SACRAMENTO			
COLUMBUS			
AUSTIN			
SAN ANTONIO			
DAYTON			
RENO			
TOTAL			

Source: AT&T Building Census and CLEC Census

Note: Based on 19 Overlap MSAs.

35. As shown in Table 3, roughly [ ] percent of AT&T-lit buildings in the overlap MSAs are served by no other AT&T-reported CLEC. However, data based on building counts alone can provide a highly misleading view of the extent to which the proposed merger may reduce competition. One reason is that AT&T bandwidth is sold primarily in buildings that are served by multiple CLECs. The AT&T data indicate that only [ ] percent of AT&T bandwidth is provided in buildings in which AT&T is the only CLEC. That is, following the merger, buildings accounting for more than [ ] percent of AT&T local bandwidth sales will continue to be served by a CLEC other than AT&T following the merger.<sup>25</sup>

**Table 3**

**Number of AT&T-Reported CLECs Serving Buildings in Overlap MSAs**

Number of CLECs (including AT&T)	Buildings Served by AT&T		
	Number of Buildings	Percent of Buildings	Percent of AT&T Bandwidth
1			
2			
3			
4+			
AT&T-Lit Buildings			

Source: AT&T Building Census and CLEC Census

Note: Based on 19 Overlap MSAs.  
Bandwidth based on DS0 Equivalents.

---

25. Bandwidth data are unavailable for CLECs serving these buildings other than AT&T. In addition, available data do not report AT&T revenue for these buildings.

36. The AT&T data also indicate that it is often economical for CLECs with local fiber to serve buildings with modest bandwidth demands. As shown in Table 4, more than [ ] percent of buildings served by AT&T in the overlap MSAs have bandwidth requirements of two DS-3s or less. Buildings in which AT&T provides at least 2 DS-3s of capacity account for more than [ ] percent of capacity provided by AT&T. As discussed further below, the FCC concluded in the TRRO that carriers can economically self-deploy high capacity loops when demand exceeds two DS-3's at a particular location.<sup>26</sup>

**Table 4**  
**Number of DS3 Equivalentents Provided by AT&T in AT&T-Lit Buildings in Overlap MSAs**

Number of DS3 Equivalentents	Number of Buildings	Percent of Buildings	Percent of Bandwidth
1) Less than 2			
2) 2 to <5			
3) 5 to <50			
4) 50+			
AT&T-Lit Buildings			

Source: AT&T Building Census

Note: Based on 19 Overlap MSAs.  
 Excludes 16 AT&T-Served buildings with CLLI codes that match AT&T collocations.

---

26. TRRO, ¶177.

**4. Number of AT&T-served buildings for which ILECs are required to offer high capacity loops on an unbundled basis.**

37. This section classifies AT&T-lit buildings based on the determinants of impairment established in the TRRO in order to assess those that are more and less likely to be at risk of competitive harm as a result of the proposed transaction. As mentioned above, the TRRO establishes criteria for identifying areas where CLECs may be at a cost disadvantage in deploying access facilities. We understand that the FCC's determination was not based on an analysis of the determinants of dedicated access pricing in different geographic areas but on the potential availability of supply. Thus, these analyses provide general guidance for evaluating the likely effect of the proposed merger on price.

38. The TRRO exempts from unbundling obligations facilities with CLEC demand of 2 DS-3 or more. This is based on the FCC's conclusion that "it is generally feasible for a carrier to self-deploy its own high-capacity loops when demand nears two DS-3s of capacity to a particular location."<sup>27</sup> Using this criterion as a guide, we limit our analysis to the [ ] buildings where AT&T provides bandwidth of less than 2 DS-3s. For similar reasons, we exclude buildings served by both AT&T and other CLECs (even if AT&T-provided bandwidth is less than 2 DS-3s). As discussed above, buildings served by multiple AT&T-reported CLECs typically have high bandwidth demand. We assume that buildings supplied by multiple AT&T-reported CLECs have total building bandwidth demand that exceeds 2 DS-3s and, based on the FCC's logic, exclude them from further analysis.<sup>28</sup> This is consistent with the fact, described above, that CLECs already serving (or capable of serving)

---

27. TRRO, ¶177.

28. The AT&T data indicate that more than [ ] percent of the buildings it serves that are also served by other AT&T-reported CLECs have AT&T-provided bandwidth of more than 2 DS-3s.

a building will have strong incentives to expand service to that building given that they have already sunk the costs associated with establishing an interconnection. Below, we also report results if these buildings (served by multiple CLECs with AT&T-provided bandwidth of less than 2 DS3s) are not excluded.

39. A total of [ ] of the [ ] buildings served by AT&T remain after applying these two screens. For each of these buildings, we have determined whether the ILEC is obligated to offer high capacity loops on an unbundled basis under the TRRO's impairment standard. ILECs avoid their unbundling requirement (e.g., there is no impairment) when the ILEC central office meets the following criteria:

- DS-3 Loops: 38,000 or more business lines and at least 4 fiber-based collocators.
- DS-1 Loops: 60,000 or more business lines and at least 4 fiber-based collocators.

40. We implement these criteria as follows:<sup>29</sup>

- For buildings with bandwidth demand of less than 1 DS-3, we determine whether it is located in an area in which the ILEC is obligated to offer DS-1 lines on an unbundled basis. (The more lenient DS-3 impairment standard is inapplicable for such buildings since no customer would be purchasing this level of bandwidth.)

---

29. This approach may be conservative. Some buildings in which AT&T today provides less than 1 DS-3 of service may have total demand in excess of 1 DS-3. To the extent to which these buildings are in central office areas which are not impaired for DS-3, our analysis would overstate the number of buildings not clearly subject to competitive supply under the FCC's impairment standards.

- For buildings with bandwidth demand of between 1 and 2 DS-3, we determine whether it is located in an area in which the ILEC is obligated to offer DS-3 lines on an unbundled basis. (Application of the stricter DS-1 impairment standard is inappropriate given the larger demand at the building.)

41. The results, summarized in Table 5, indicate that [ ] of the buildings in which AT&T currently has less than 2 DS-3s of demand are located in “non-impairment” areas under the FCC’s TRRO. Thus, only [ ] of AT&T’s over [ ] lit buildings (i) have demand of less than 2 DS-3s; (ii) are not served by any other AT&T-reported CLEC in addition to AT&T; and (iii) are located in areas in which the ILEC is obligated to offer unbundled high capacity lines (defined specific to the building’s bandwidth demand).<sup>30</sup>

**Table 5**

**Characteristics of AT&T-Lit Buildings in Overlap MSAs**

Group	AT&T Buildings
All AT&T-Lit Buildings	
<u>Buildings Remaining After Exclusions</u>	
Buildings with less than 2 DS3s provided by AT&T	
Also excluding buildings with multiple CLECs	
Also excluding buildings in areas not subject to unbundling requirements	

Source: AT&T Builling Census; AT&T CLEC Census; GeoResults Data.

30. If we do not exclude from the analysis buildings served by multiple AT&T-reported CLECs with less than 2 DS-3s in AT&T-provided bandwidth, then [ ] buildings survive these screens instead of [ ].

42. These are a small fraction of AT&T's lit buildings and of commercial buildings generally. The [ ] buildings which remain after applying these filters (which exclude buildings identified as being less likely to be at risk of competitive harm as a result of the proposed transaction) are less than [ ] percent of AT&T-served buildings and less than [ ] percent of buildings in SBC's territory with more than 10 voice-grade equivalent lines. These [ ] buildings account for [ ] percent of AT&T-provided bandwidth.

43. In the next section we show that even this figure implicitly overstates potential competitive problems because many are located in areas served by other firms with local fiber facilities.

#### **5. AT&T-lit buildings in areas served by other AT&T-reported CLECs**

44. This section analyzes the extent to which AT&T-lit buildings are in SBC central office service areas that also are served by other AT&T-reported CLECs (and for which AT&T thus maintains data on their locations served). As mentioned above, there are a number of other CLECs not reflected in these data. As a result, the analysis understates, perhaps significantly, the extent to which other CLECs are capable of serving buildings where AT&T now provides service.

45. While the FCC's TRRO criteria are based in part on the geographic areas served by ILEC central offices in defining impairment, the presence or absence of local fiber is not explicitly considered in making this determination. Nonetheless, given the FCC's view that the presence of fiber based collocation equipment in an ILEC central office service area is significant in evaluating competitive conditions, this additional information on the presence of local fiber in the central office service area also is likely to be of value in

assessing the likelihood that the merger results in the risk of harm to competition. If AT&T and other CLECs operate local fiber facilities in an area served by a given ILEC central office, then it is likely that firms also could do so economically if prices rose from current levels.<sup>31</sup>

46. Table 6 reports the number of AT&T-lit buildings classified by the number of AT&T-reported CLECs that provide service to buildings in the same ILEC central office serving area. Results are reported separately (i) for all [ ] AT&T-lit buildings; (ii) for all [ ] AT&T-lit buildings served exclusively by AT&T; and (iii) for the [ ] buildings in areas that meet the “impairment” standard and related criteria described above. These calculations are reported on an MSA-specific basis in Appendix 1.

47. The analysis indicates:

- [ ] of the [ ] AT&T-lit buildings are in SBC central office service areas served by at least one other AT&T-reported CLEC. The [ ] buildings in areas served by no other AT&T-reported CLEC post-merger account for roughly [ ] percent of total bandwidth.
- [ ] of the [ ] AT&T-lit buildings served exclusively by AT&T are in SBC central office service areas served by at least one other AT&T-reported CLEC. Again, the [ ] buildings in areas served by no other AT&T-reported CLEC post-merger account for roughly [ ] percent of total bandwidth.

---

31. The ability of another CLEC to serve a particular building depends on the distance and other geographic factors that affect the cost of a building interconnection. The costs faced by a new CLEC deploying service to a building can depend in part on the physical proximity of its fiber to a building. The new CLEC’s costs may also be lower than those faced by an existing CLEC serving the building if it can utilize building-specific conduit or other facilities established by other CLECs.



- [ ] of the [ ] AT&T-lit buildings in areas that meet the FCC’s impairment triggers and related criteria are in SBC central office service areas served by at least one other AT&T-reported CLEC. The [ ] buildings in areas served by no other AT&T-reported CLEC post-merger account for [ ] percent of total bandwidth.

**Table 6**

**Number of AT&T-Reported CLECs in SBC Central Office Service Areas With AT&T-Lit Buildings**

Number of CLECs (Including AT&T)	All AT&T-Lit Buildings		Buildings Served by AT&T and No AT&T-Reported CLECs		"Impairment Area" Buildings	
	Number	Percentage	Number	Percentage	Number	Percentage
1						
2						
3						
4+						
Total						

Source: AT&T Building Census; AT&T CLEC Census; GeoResults Data.

Note: Excludes CLEC buildings which cannot be mapped to a central office. Based on 19 overlap MSAs.

48. Thus, the vast majority of AT&T-lit buildings, including those that may be considered at greater risk of harm resulting from the proposed merger, are in areas served by SBC central offices which will continue to be served by at least one other AT&T-reported CLEC post-merger. These results indicate that other CLECs are typically well-situated to

supply the large majority of buildings now served by AT&T if prices were to rise from current levels.

**6. MSA area analysis**

49. As noted above, the FCC concluded in its Access Charge Reform Order that MSAs are the appropriate geographic unit for analysis of competition in the provision of special access circuits. As noted above, this reflects the FCC’s conclusion that MSAs “best reflect the scope of competitive entry.”<sup>32</sup> We have used data from alternative sources to identify the number of CLECs that have local fiber facilities in each of the metropolitan areas in which AT&T has local facilities.

50. As shown in Table 7, there are [ ] AT&T-reported CLECs (including AT&T) that operate local fiber networks in [ ] of the [ ] overlap MSAs. There is no metropolitan area in which AT&T is currently the sole CLEC provider of local fiber facilities.

**Table 7**

**CLECs with Local Fiber Serving Overlap MSAs**

Number of CLECs (Including AT&T)	Number of MSAs	
	With AT&T-Reported CLECs	With CLECs Identified by NPRG
1		1
2		0
3		0
4+		18
Average Number of CLECs		6.9

Source: NPRG; AT&T Building Census; AT&T CLEC Census.

32. Access Charge Reform Order, ¶72.

51. As noted earlier, the AT&T data do not include information on a variety of CLECs. Data on fiber deployment from NPRG are also reported in Table 7 and indicate that there are currently four or more CLECs that offer local fiber in all but one of the 19 overlap MSAs. As the table notes, the average number of CLECs in the overlap MSAs reported by NPRG (6.9) greatly exceeds the comparable figure based on AT&T-reported CLECs.

## **6. Implications**

52. The data and analyses lead to a number of important conclusions regarding the competitive effect of the proposed transaction on dedicated access.

- The data indicate that only a small number (less than [ ]) buildings in SBC's territory are served by AT&T and thus are subject to any potential reduction in competition. This reflects less than [ ] percent of commercial buildings with more than 10 voice-grade line equivalents in SBC's service territory.
- More than [ ] percent of bandwidth sold by AT&T through its local facilities in the overlap areas is in buildings that will continue to be served by independent CLECs post-merger.
- The vast majority of AT&T-lit buildings (more than [ ] percent) are in SBC central office service areas where other CLECs operate. This facilitates the ability of other firms to replace AT&T as a competitor in serving these buildings and implies that a reduction in the number of CLECs providing local fiber to a building does not necessarily imply a material reduction in competition.

- Despite the frequent presence of other CLECs in the central office serving area, most CLEC-lit buildings are served by only one CLEC. This indicates that if one CLEC already serves a building, then others often find it most profitable to provide facilities to other buildings. The fact that only one CLEC typically serves a building does not imply that other firms are incapable of economically serving the building if prices were to rise.
- Instead, the fact that buildings are typically served by only one CLEC often reflects limited bandwidth demand at the location. The AT&T data, however, indicate that CLECs with local fiber often find it economical to serve buildings with even modest bandwidth demand. The fact that AT&T successfully served the building suggests that other CLECs also would find it profitable to pursue opportunities at such locations if prices were to rise.

53. In sum, there is no basis to conclude that the relatively small number of buildings and traffic at issue means that this merger will materially reduce competition or harm consumers of special access. This conclusion holds using both granular and regional analyses, as suggested by Prof. Farrell.

**C. THE PROPOSED TRANSACTION DOES NOT SIGNIFICANTLY REDUCE THE NUMBER OF CLECS COLLOCATING FACILITIES IN SBC CENTRAL OFFICES.**

54. As discussed above, the FCC relies on information on the extent to which CLECs have collocated fiber-based equipment in ILEC wire centers and related information in evaluating whether to grant ILECs pricing flexibility for special access services. While collocation in central offices does not necessarily imply the presence of local fiber to

customer premises, the FCC considers these criteria to be a “proxy for irreversible, sunk investment in channel terminations between the end office and the customer premises.”<sup>33</sup> We have used data on all physical and virtual collocations in SBC central office including non-fiber collocations in an attempt to analyze this issue. These data provide information on CLECs’ ability to provide services other than dedicated access in narrowly defined geographic areas.

55. We have used these data to evaluate the extent to which the proposed transaction will result in a significant reduction in the number of independent CLECs that operate in SBC central offices in which AT&T operates. A significant reduction in the number of independent CLECs resulting from the merger could have implications for the competitiveness of both dedicated access services and other telecommunications services in areas served by SBC’s central offices.

56. Available data, however, indicate that a number of other CLECs operate in virtually all SBC central offices in which AT&T has collocated equipment.<sup>34</sup> As Table 8 indicates, AT&T is the sole CLEC with collocated equipment in only [ ] SBC central offices. These central offices account for less than [ ] percent of business lines served by SBC

---

33. FCC, Access Charge Reform Order, ¶104. The FCC concluded that collocation “is probative of the degree of sunk investment by competitors in channel terminations between the end office and the customer premises throughout the MSA. In addition, as we discuss above, collocation is a conservative measure of competition in that it does not measure competition from competitors that bypass LEC facilities altogether. Given the lack of other data in the record, therefore, we conclude that it is reasonable to rely on collocation as a proxy for irreversible, sunk investment in channel terminations between the end office and the customer premises and to set the applicable thresholds high enough to account for the limitations inherent in this trigger.”

34. We have conservatively included all AT&T collocations in our analysis, even non-facilities based collocations that are not associated with its local metro fiber and instead used primarily in connection with AT&T’s purchase of special access services.

central offices with collocated equipment. More than [ ] percent of SBC central offices with collocated AT&T equipment also have equipment collocated by three or more CLECs other than AT&T.

**Table 8**

**Number of CLEC Collocations in SBC Central Offices**

AT&T Collocation in CO	Number of Non-AT&T CLECs	Number of COs with Any Collocation	Percentage of COs	Weighted Percentage of COs*
YES				
NO				

Source: SBC Physical and Virtual Collocation Data.

Note: Excludes SBC (including AADS) collocations.  
\* Weighted by Number of Business Lines in CO.

57. In sum, these data indicate that following the proposed transaction a variety of CLECs will remain in virtually all central offices in which AT&T has collocated equipment. Following the FCC’s logic, this implies that the transaction will not substantially reduce prospects for competition in the provision of dedicated access services in these areas.

**D. AVAILABLE DATA INDICATE THAT THE PROPOSED TRANSACTION DOES NOT ELIMINATE A SIGNIFICANT RESELLER/AGGREGATOR OF SBC SPECIAL ACCESS SERVICES.**

58. Opponents' claims that the transaction will harm competition by eliminating AT&T's role as a significant reseller/aggregator of SBC special access services are not supported by available evidence.

59. First, we understand that AT&T does not act as a simple "reseller" of SBC special access services. Instead, we understand that AT&T sells wholesale dedicated access services to other carriers only when two of the three components of dedicated access services are provided by AT&T using its own facilities.<sup>35</sup> As described above, special access services typically include three components – two "channel terminations" at either end of the circuit and the "interoffice transport" leg in between. That is, AT&T does not as a general matter purchase for resale to wholesale customers complete special access circuits from SBC or other ILECs. Rather, it only utilizes an ILEC circuit as one of the three components.

60. Even then, AT&T's sales of wholesale local private line services that include SBC special access service are competitively insignificant. AT&T's wholesale local private line services in SBC's territory attributable to Type II special access circuits (in which some component of the dedicated access circuit is provided by SBC) generate only [ ] million in revenue annually.<sup>36</sup> In contrast, we understand that SBC had several billion dollars in special access revenue in 2004.

61. Contrary to opponents' claim, AT&T does not have a cost advantage relative to other significant purchasers of special access services from SBC. For example, although

---

35. Fea, et. al.

36. Fea, et. al.

AT&T is SBC's largest purchaser of special access services, SBC's tariff structure does not contain volume-related discounts. SBC, through its MVP program, offers discounts to special access customers that commit to certain purchase levels for five years based on the customer's past purchases.<sup>37</sup> We understand that there are [ ] carriers that participate in this program and that each purchases under the same discount schedule. We also understand that at least one special access customer, which has agreed to a higher volume commitment relative to its historical purchases, earns a higher discount than AT&T.

62. In sum, available data indicate that AT&T is a relatively insignificant provider of dedicated access as an aggregator or reseller of SBC special access services. In addition, the proposed transaction does not eliminate a firm that has any unique ability or incentive to resell SBC special access services.

### **III. COMMENTERS' CLAIMS THAT VERTICAL INTEGRATION BY SBC HARMS COMPETITION ARE MISPLACED AND BASED ON INCOMPLETE ANALYSIS.**

#### **A. OVERVIEW OF OPPONENTS' COMMENTS**

63. In addition to concerns about the reduction in horizontal competition for the provision of dedicated access services, opponents also express concern that vertical integration between SBC's special access facilities and AT&T's provision of business enterprise services (which may rely in part on SBC special access facilities) will have an independent adverse effect on competition.

---

37. SBC's MVP tariff is available to customers with annual special access purchases of more than \$10 million in a given SBC region (West, Southwest, or Midwest). It offers discounts for customers that maintain the annual volume of purchases from the pre-contract benchmark period over a five year period. These customers receive discounts that increase from nine percent in year one of the contract to 14 percent in year five.



64. Prof. Farrell, for example, states that following the transaction:

SBC will [...] have increased incentives to raise special access prices to downstream enterprise network service providers (or generally special access customers)... The effect of such a price increase [...] would in part be to shift business from independent downstream providers to SBC's downstream affiliate; this is more likely to happen [...] if SBC's downstream affiliate is larger and more attractive to customers and would be the case post-merger. (Farrell, ¶¶40-41)

65. Other opponents make similar claims.<sup>38</sup>

**B. OPPONENTS IDENTIFY CONCERNS THAT ARE INDEPENDENT OF THE PROPOSED MERGER.**

66. The vertical concerns raised by merger opponents are the consequence of SBC's alleged market power in the provision of special access services. If special access services are competitively supplied (or if the downstream services that utilize special access are competitive) then there can be no concern that the proposed merger creates any incentive for SBC to raise special access prices.

67. On the other hand, the opponents' allegation that SBC exercises market power in the pricing of special access is an issue that exists independently of the proposed merger. If this problem does exist and creates social harm then a regulatory solution may be required. Opponents' complaints about SBC's market power in the provision of special access presumably would apply to all ILECs, not just SBC. A regulatory review enables all interested parties to comment on the issue and enables a general remedy to be fashioned if a competitive problem is identified. Such a review by the FCC is already underway.<sup>39</sup>

---

38. See, for example, Bernheim, ¶12, Wilkie, ¶25, Broadwing/Savvis, pp. 29-30, CompTel/ALTS, p. 27, Global Crossing, p. 18.

39. See, generally, Special Access NPRM.

68. It is also important to note that if, as opponents claim, SBC has market power in the provision of special access, then vertical integration may also have efficiency benefits.<sup>40</sup>

**C. ANALYSIS OF THE COMPETITIVE EFFECT OF THE PROPOSED TRANSACTION REQUIRES ANALYSIS OF ALL MERGER-RELATED EFFICIENCIES.**

69. Evaluation of the competitive effects of the proposed transaction also requires considerations of merger-related efficiencies. Various efficiencies were discussed in declarations submitted by Christopher Rice of SBC and Hussein Eslambolchi of AT&T as part of the parties Application. These declarations, which were discussed in our prior declaration, established that the proposed transaction would be expected to: (i) generate substantial cost savings; (ii) increase the parties' incentives to innovate; and (iii) increase service quality and reliability due in part to increasing the number of customer locations that can be directly served by the merged firm's network.

70. Although consumers may benefit from merger-related efficiencies, the parties opposing the proposed transaction would not. To the contrary, many parties opposing the proposed merger are CLECs that both purchase inputs from SBC and compete with AT&T and SBC in the provision of business services. The creation of a more efficient competitor through the merger would be expected to harm certain opponents' prospects in competing to provide business services.

71. The value of potential efficiencies that the proposed transaction is likely to create is reflected by a variety of statements submitted by customers in support of the

---

40. Carlton and Perloff, *Modern Industrial Organization*, 4<sup>th</sup> ed. (2005), pp. 415-418 and Farrell, ¶42.

proposed transaction. Customers would not be expected to support the proposed transaction if the risk of harm to competition outweighed the potential efficiencies.

72. In response to requests from SBC and AT&T, a number of companies have made statements in support of the proposed transaction. These statements typically discount concerns that the proposed transaction will result in a reduction in competition, highlight the importance of non-traditional sources of supply such as cable companies, and explain that the customers expect the transaction to enable the merged firm to offer better products and service.<sup>41</sup> For example:

- The facilities manager for a large Midwest-based insurance company stresses the competitive importance of VoIP services and other new technologies and cable modem services as well as the ability of the merged company to offer better coordinated services.

... we have recently incorporated VoIP gateways in many of our offices.... We also offer our agents and employees Virtual Private Network services for remote access; and we have ISP services through cable companies...

As it stands, SBC and other LECs control a portion of the network, and AT&T and other IXCs control another portion. Consequently communication breakdowns and construction delays are commonplace, and I have little to no control over how or when they are resolved. [...] I am hopeful that in dealing with a combined SBC and AT&T company, I will have more control over how my services are implemented....

---

41. We understand that, with the exception of statements made by customers who expressed a desire that their statements not be made part of the public record, these statements are being filed separately with the Commission. The customers not identified by name in the discussion that follows have authorized SBC and AT&T to quote from their statements and identify them in a generic manner.

... I generally think that an adequate number of players and technologies will be available to provide us with competitively priced services after the anticipated industry consolidation.

I anticipate that the merger will bring significant improvements to the provisioning of network services going out to our agents.

- The head of infrastructure engineering for ServiceMaster, a large supplier of outsourced residential services (such as lawn care, pest control, HVAC, plumbing, home warranty and housekeeping) writes:

Currently in the marketplace there are more than a sufficient number of alternative telecommunication providers for all types of services. This competitive environment will not be endangered by the proposed merger of SBC and AT&T.

We view these two companies as complementary in the provisioning of IXC and local services.

- The Executive VP of an Oklahoma bank stresses that they have obtained bids from a wide variety of providers using alternative carriers such as Chickasaw, OpticTel, and Catalog.com. They also use cable-based services from Cox:

The primary purpose of our selection of Cox to provide this circuit was to create redundancy for the data connection running between the two buildings. The Cox cable physically enters the building at a different point and through a different method from SBC's DS-3 frame connection.

I have no competitive concerns about the merger of SBC and AT&T; in fact, it is a non-event from my perspective.

- The network service analyst for an Iowa-based insurance company stressed that the merger would likely enable his company to consolidate purchases with a reduced number of suppliers.

I do not have any competitive concerns about the merger between SBC and AT&T. Rather, I hope that the merger will allow the combined company to move closer to being able to provide a single point of contact, which would be a good thing. With the pooled resources of the combined companies, they should be able to offer more and better product offerings.

- The Director of Information Technology at an international engineering and construction company with headquarters in Kansas stresses the ability of the merged firm to offer a broader range of products:

I have no competitive concerns about the merger of SBC and AT&T. [...] The merger will make the combined company more competitive and better able to provide a broader range of services in the marketplace. I see the current consolidation in the marketplace as healthy as it will result in stronger teams.

73. Statements such as these indicate that many customers recognize that the proposed transaction can offer benefits to customers and is unlikely to result in a significant reduction in competition they face. These statements are consistent with the analysis presented in our initial declaration (p. 4) in which we concluded that it is unlikely that the transaction will harm competition either through coordinated or unilateral action.

**IV. THERE IS NO BASIS FOR CONCERN THAT THE PROPOSED TRANSACTION WOULD HARM COMPETITION DUE TO “MUTUAL FORBEARANCE” BETWEEN SBC AND OTHER ILECS.**

**A. OVERVIEW OF OPPONENTS’ COMMENTS**

74. Several opponents suggest that the proposed merger, together with the proposed merger of Verizon and MCI, will harm competition in the provision of a variety of services due to the history of “mutual forbearance” and “tacit collusion” between SBC and Verizon.<sup>42</sup>

75. According to Prof. Bernheim, “SBC and Verizon have a history of mutual forbearance, and the mergers would reinforce their incentives to divide the telecommunications market geographically.”<sup>43</sup> He also claims that “AT&T and MCI currently compete vigorously with each other. But as arms of SBC and Verizon, they likely would not.”<sup>44</sup>

76. Similarly, Prof. Wilkie argues that such forbearance exists between Verizon and MCI. He explains:

This type of tacit collusion is orchestrated by a simple strategy: ‘I will not undercut your special access rates to competing carriers in your territory if you do not undercut my special access rates to competing carriers in my territory.’ The strategy is consistent with both behavior of SBC and Verizon in other markets.<sup>45</sup>

Prof. Wilkie further claims that mutual forbearance would extend to the provision of services to business customers.<sup>46</sup>

---

42. See: Broadwing, p. 21, CBeyond, et. al., p. 44. Opponents use the terms “mutual forbearance” and “tacit collusion” in discussing these concerns. For simplicity, we adopt the “mutual forbearance” terminology in responding to these comments.

43. Bernheim, ¶10

44. Bernheim, ¶35

45. Wilkie, ¶30.

46. Wilkie, ¶¶34-35.

77. Opponents also argue for similar reasons that the proposed merger will reduce innovation competition and that the merged company would have a reduced incentive to innovate.<sup>47</sup>

**B. ANY POLICY OF “MUTUAL FORBEARANCE” WOULD BE EXTRAORDINARILY COSTLY TO THE MERGED FIRM.**

78. Opponents’ mutual forbearance claims are based on what they claim to be an absence of historical competition and an “aversion to out-of-region competition” by SBC and Verizon.<sup>48</sup> As discussed further below, opponents ignore important historical examples of competition between SBC and other ILECs and ignore explanations for ILECs’ limited out-of-region activity unrelated to mutual forbearance.

79. However, even if we accept opponents’ characterization, they ignore the fact that the proposed transaction fundamentally alters the mix of assets owned by SBC as well as Verizon. Changes in the structure of SBC (and Verizon) lead to changes in their incentives.

80. The merged SBC/AT&T will have extensive physical and human assets throughout the United States and abroad. AT&T today operates local and long distance network facilities throughout the Verizon, BellSouth and Qwest service areas and is a leading provider of business services throughout these areas. Any strategy by the merged firm not to continue to compete aggressively for customers outside of SBC’s region would be extraordinarily costly because SBC is the ILEC to only 32 percent of the United States.<sup>49</sup> Due to the fixed nature of many network costs, revenue lost by the merged firm’s failure to bid aggressively in Verizon’s territory would have a large effect on profitability.

---

47. Wilkie, ¶¶58-59; Cbeyond, et. al, pp. 68-72.

48. Bernheim, ¶32.

49. FCC, Trends in Telephone Service, May 2004, Table 7.3

81. Put simply, there is no reason to expect that the merged firm would find it in its interest not to compete aggressively outside of SBC's region. This holds with respect to the merged company's incentive to utilize and extend its local fiber facilities (and compete with ILECs for access traffic) as well as its sales of business services. Opponents stress that, due to ILECs' market power, local fiber facilities operated by AT&T and other CLECs provide them a significant cost advantage. There is no reason to expect that the merged firm would choose not to continue to fully utilize these out-of-region cost advantages following the merger.

82. If, as opponents claim, the proposed transaction were to lead to mutual forbearance with respect to the provision of business services then, all else equal, the beneficiaries of this behavior would be the merger opponents that provide such services. In contrast, if the merger enabled SBC and AT&T to offer improved service quality and reliability, merger opponents that provide business services would be harmed by the more efficient firm even though consumers would be better off.

**C. OPPONENTS IGNORE EXISTING COMPETITION BETWEEN SBC AND OTHER ILECS AND NON-COLLUSIVE EXPLANATIONS FOR HISTORIC PATTERNS OF COMPETITION.**

83. As noted above, opponents' "mutual forbearance" claim is based in part on their view that SBC and ILECs do not, and will not, actively compete. However, there are significant examples of such competition.

84. For example, SBC and Verizon compete directly for wireless customers through Cingular (owned jointly by Cingular and BellSouth) and Verizon Wireless (which is 50 percent owned by Verizon). Cingular and Verizon Wireless are the first and second



largest wireless suppliers in the United States. These firms compete aggressively and provide service nationally.

85. While SBC's efforts have centered on bidding to serve customers with most of their locations inside SBC's regional footprint, it has bid on a variety of projects in competition with Verizon and other ILECs. SBC's focus on serving customers with most locations inside its territory is readily explained by the fact that SBC's physical assets and customer relationships are concentrated inside its regional footprint.

86. Opponents cite the failure of SBC's out-of-region strategy, which was undertaken in conjunction with its Ameritech acquisition, as further evidence of its "aversion to out-of-region competition."<sup>50</sup> Opponents, however, present no evidence that SBC's failure was due to mutual forbearance instead of other economic factors. As discussed in the Declaration of James Kahan, previously filed in this matter, SBC's out-of-region strategy was hindered by the fact that SBC did not obtain authorization to provide long distance services until considerably later than it expected at the time of the Ameritech acquisition.

**D. A VARIETY OF INDUSTRY FACTORS MAKES MUTUAL FORBEARANCE IN THE PROVISION OF BUSINESS SERVICES UNLIKELY**

87. While opponents argue that the proposed merger will result in mutual forbearance among providers of telecommunications among business customers, they ignore a variety of industry characteristics that complicate such behavior. For example:

- Customers of business services are highly heterogeneous with respect to size, geography, and services demanded as well as service quality required.

---

50. Bernheim, ¶32.

Customers also differ with respect to their desired supplier mix, with some choosing a single provider for all services, others using different providers for different services, and others using multiple suppliers for the same service for redundancy purposes. These circumstances make it more difficult for firms to monitor each others' behavior and thus provide incentives to cheat on a collusive agreement.

- Customers differ with respect to purchasing practices, with some customers using formal RFPs and biddings while others negotiate informally. Problems in observing prices resulting from negotiated deals make it more difficult to monitor rivals' prices and more difficult to sustain a collusive agreement.
- Sales to business customers often involve lumpy, multi-year contracts which can provide strong incentives to "cheat" on a collusive agreement.
- Customers are often highly sophisticated and often purchase with the assistance of professional third parties, including consultants, value-added resellers and systems integrators. Such circumstances enhance customers' ability to detect collusion.
- Services often involve services provided over owned and leased facilities. Thus, the actual firms involved in providing services may not be transparent to rivals. This in turn indicates that attempts to deviate from a collusive agreement can be difficult to detect.

88. These circumstances, along with differences in supplier characteristics, complicate the ability of firms to engage in mutual forbearance. For example, suppliers may differ with respect to the technological solutions that they offer and cost structure (e.g., the extent to which they utilized their own facilities, etc.). Opponents fail to explain how suppliers could successfully engage in mutual forbearance in the face of these obstacles and present no evidence that the transaction would facilitate any such outcome.

**E. THERE IS NO BASIS FOR OPPONENTS' CLAIM THAT THE PROPOSED TRANSACTION WOULD HARM INCENTIVES TO INNOVATE**

89. There can be no dispute that the telecommunications industry has been marked by rapid technological changes in recent years. Dramatic growth in the Internet, wireless services, private voice and data networks, the convergence of voice and data transmission technologies, the deployment of long distance and local fiber optic networks, and improvements in network electronics are a few examples.

90. In our prior declaration, we discussed how the merged company's larger customer base and more extensive network enable it to deploy innovations rapidly to a broader base of customers. The firm's larger network also increases its incentive to invest in productivity enhancing network features. The parties also submitted declarations explaining SBC's intention to increase spending on certain new AT&T technologies above the level budgeted by AT&T.<sup>51</sup> Moreover, it may be difficult for firms to achieve these gains in the

---

51. See, for example, Rice declaration, ¶19, ¶¶20-25 and Eslambolchi declaration, ¶7-8, ¶¶16-18.

absence of merger given the recognized difficulties in establishing contracts for new technologies.<sup>52</sup>

91. In dismissing these arguments, opponents present no evidence to support their view that the merger would harm innovation competition. For example, they do not claim that large telecommunications mergers in the recent past slowed the development or deployment of the new technologies noted above.

92. Many parties compete to develop new telecommunications innovations. New telecommunications services and technologies result from efforts of not only ILECs and IXCs but also equipment manufacturers, CLECs, new long distance network providers, wireless service providers, and systems integrators as well as others outside the industry. Given these circumstances, it is unlikely that the proposed transaction will reduce innovation competition.

**V. THE PROPOSED TRANSACTION IS UNLIKELY TO ADVERSELY AFFECT COMPETITION IN THE PROVISION OF SERVICES FOR MASS MARKET CONSUMERS**

**A. OVERVIEW OF OPPONENTS' COMMENTS**

93. Opponents also claim that the proposed transaction will harm mass market consumers. For example:

- The Selwyn report characterizes “the current industry condition” as a “debacle.”<sup>53</sup> The report concludes that “[t]he vertical and horizontal integration and market concentration that will result from these two

---

52. Carlton and Perloff, *Modern Industrial Organization*, 4th ed. (2005), pp. 548-558.

53. Selwyn, p. iii.

combinations will afford the two post-merger RBOCs near-monopoly control of the local market within each RBOC's core local service footprint."<sup>54</sup>

- Prof. Wilkie concludes, based in part on a merger simulation analysis, that “the merger will induce significant consumer harms in the market for mass wireline service.”<sup>55</sup> He also adds that “it is highly problematical” to conclude that the transaction will not harm mass market consumers due to AT&T's decision to cease marketing these services. This is because “there is no assurance that, absent the transaction, AT&T would not re-enter the market.”<sup>56</sup>

**B. OPPONENTS FAIL ADEQUATELY TO ACCOUNT FOR AT&T'S PRE-MERGER DECISION TO CEASE MARKETING MASS MARKET SERVICES.**

94. Many of the competitive concerns relating to mass market services expressed by merger opponents are not merger related. Mr. Selwyn believes that implementation of the regulatory framework of the 1996 Telecom Act has been a “debacle” due to court decisions “to withdraw regulatory protections that had been put in place to preserve the intended procompetitive opportunities ...” However, these events occurred prior to the merger.

95. AT&T's pre-merger decision to stop marketing mass market services implies that it would rapidly cease to be a significant competitive factor in serving these customers in the absence of the transaction. AT&T's decision, and the factors leading to it -- such as a history of declining prices for mass market services and changes in regulatory requirements

---

54. Selwyn, p. 42.

55. Wilkie, ¶47.

56. Wilkie, ¶49.

facing ILECs -- are discussed in our initial declaration. In light of AT&T's rapidly declining importance as a supplier of mass market services, the merger is likely to benefit remaining AT&T long distance consumers because SBC has stronger incentives than AT&T to retain these customers. Thus, it has less incentive to pursue the "harvesting" strategy now being undertaken by AT&T.

96. Opponents present no evidence suggesting that AT&T's decision to stop marketing its mass market services and to dismantle its marketing organization was economically baseless and likely to be reversed. Given recent changes in the legal and regulatory environment and prior trends in AT&T business that predate its recent legal and regulatory events, it is highly speculative for Prof. Wilkie to conclude that the merger eliminates a firm that has any substantial probability of re-entering into the provision of mass market services. Indeed, Prof. Wilkie presents no evidence to support his suggestion that there is any realistic possibility that AT&T would profitably reenter in the absence of the proposed merger.

97. Prof. Wilkie also attempts to support his claim that the proposed transaction will harm competition by presenting the result of a "Bertrand" merger simulation analysis.<sup>57</sup> Merger simulation calculations attempt to identify the effect of price on merger-related incentives to raise the price of differentiated products. These incentives arise because the merged firm can "recapture" customers that otherwise would be lost to rivals as the result of a price increase.

---

57. Wilkie ¶46.

98. While the details of the analysis must be inferred from his brief description, it appears that Prof. Wilkie's calculations do not account for a variety of factors that differentiate the proposed transaction from the "typical" situation evaluated with Bertrand merger-simulation models. For example:

- If AT&T has determined that its profit-maximizing strategy in the absence of the merger is to cease marketing these services (which must be the starting point of the merger analysis), then it is unlikely that a significant number of SBC customers would be recaptured by AT&T in response to an increase in SBC prices. Under such circumstances, there would be little if any merger-related incentive to raise prices to current SBC customers. Prof. Wilkie appears not to have accounted for this in his calculation.
- SBC has stronger incentives than AT&T to retain AT&T's current customers. This is due in part to SBC's interest in selling to current AT&T customers ancillary services such as wireless or other services that AT&T does not offer. Prof. Wilkie appears not to have considered this in his analysis.
- In addition, SBC, to the extent that it has a lower cost structure than AT&T for serving mass market consumers, would have a greater incentive to retain these customers. Prof. Wilkie appears not to account for merger-related cost savings in his analysis.
- Furthermore, the incentive and ability of the merged firm to raise price may be affected by its regulatory obligations to integrate AT&T and SBC pricing

plans as well as regulatory obligations relating to geographic price uniformity. Prof. Wilkie appears to not account for these factors.

**VI. RESPONSE TO ADDITIONAL COMMENTS MADE BY OPPONENTS**

99. This section briefly responds to additional comments made by opponents and their experts in reference to our declaration that are not addressed above. Our failure to address any additional comments made by opponents or their experts should not be interpreted to imply that we agree with their particular claim.

**CompTel/ALTS, p. 24**

100. CompTel/ALTS claim that “for a certain, and likely significant, number of in-region large business customers this merger will significantly reduce competition.” To support this point, they quote a portion of our declaration which cites the Department of Justice’s view, which we share, that market shares may be poor indicators of a firm’s potential market power in bidding situations.

101. Simply put, the statement of ours quoted by CompTel/ALTS does not support their inference. Despite CompTel/ALTS’ assertion, the DOJ’s comment (which is from its Merger Guidelines) cannot be meant to imply that any merger in a bid situation will “significantly reduce competition.”

**CompTel/ALTS, p. 25**

102. CompTel/ALTS claim that there is a tension between (i) SBC’s claim that increased “end-to-end” control of network facilities is a benefit of the merger and (ii) that systems integrators are a significant participants in the market for the provision of business services. They cite our declaration for the latter proposition.



103. There is no tension between these statements. Systems integrators typically assemble and manage a firm's telecommunications networks. This provides customers assurance that a single party is responsible for the performance of a service or network. Increased end-to-end control of network facilities resulting from the merger better enables SBC also to make such assurances to customers.

**Bernheim, ¶45**

104. Prof. Bernheim states that “[a]nother problem with the Carlton and Sider analysis of horizontal effects is that they fail to recognize the importance to many CLECs of originating and terminating traffic with AT&T. With SBC's announced plans to migrate the traffic to SBC's network in-region, the transaction will further decrease the market share and financial strength of other carriers.”

105. There are several problems with Prof. Bernheim's statement. First, he presents no support for the proposition that the loss of AT&T traffic will harm carriers that serve AT&T. Second, he fails to distinguish harm to competition from harm to a competitor. For example, if the merger enables SBC and AT&T to realize efficiencies by moving traffic to each others' networks, then it is not surprising, or troubling, that other firms may be disadvantaged in the competitive process. The appropriate focus of antitrust policy is consumer welfare, not the welfare of rival firms. Creation of a more efficient firm benefits society by improving resource allocation and also may benefit consumers.

**Bernheim, ¶51**

106. Professor Bernheim states that “[o]n some secondary and tertiary routes to smaller cities, SBC and AT&T may be the only firms with transport facilities. The aggregated nationwide analysis of Carlton and Sider fails to address these overlaps.”

107. Prof. Bernheim presents no evidence to support his claims and identifies no specific routes that raise competitive concerns. Given the explosion of long distance fiber capacity in recent years by firms such as Qwest, Broadwing, Global Cross, Level 3 and many others, it would seem to be difficult for Prof. Bernheim to argue that there are significant barriers to the deployment of new long distance fiber capacity.

**CONCLUSION**

108. Opponents make a wide variety of arguments regarding the effect of the proposed transaction on competition but present no data to support these claims. In the limited time available to prepare a response, we have used available data to analyze many of these claims. Based on this analysis, we find no empirical support for opponents’ concerns. The opposition comments do not lead us to alter our prior conclusion that the proposed transaction is unlikely to result in harm to consumers.

I declare under penalty of perjury that the foregoing is true and correct to the best of my information and belief.

Signature: Dennis W. Carlton  
Dennis W. Carlton

Date: 5/9/05

I declare under penalty of perjury that the foregoing is true and correct to the best of my information and belief.

Signature: Hal S. Sider  
Hal S. Sider

Date: May 9, 2005

**Appendix 1**

**Number of AT&T-Lit Buildings of Different Characteristics by MSA**

MSA	AT&T-Lit Buildings	Buildings Served by AT&T and Not Served by AT&T-Reported CLECs	Buildings with Less than 2 DS3s	Buildings in "Impairment Areas"	
				All	No Other AT&T-Reported CLECs in CO Area
CHICAGO					
INDIANAPOLIS					
KANSAS CITY					
DALLAS					
LOS ANGELES					
SAN DIEGO					
SAN FRANCISCO					
MILWAUKEE					
ST LOUIS					
DETROIT					
HOUSTON					
HARTFORD					
CLEVELAND					
SACRAMENTO					
COLUMBUS					
AUSTIN					
SAN ANTONIO					
DAYTON					
RENO					
Total					

Source: AT&T Building Census; AT&T CLEC Census; GeoResults Data.