May 17, 2005

<u>By Hand and via ECFS</u>

Marlene H. Dortch
Secretary, Federal Communications Commission
445 12th Street, NW
Washington, DC 20554

Re: DA 05-656, WC Docket No. 05-65
DA 05-762, WC Docket No. 05-75

Dear Ms. Dortch:

On May 10, 2005, a group of CLECs[1] – accompanied by Dr. Simon J. Wilkie, who also filed a Declaration[2] on behalf on these same CLECs on April 25, 2005 – met with Scott Bergman, Legal Advisor to Commissioner Adelstein. The CLECs presented an analysis claiming significant effects from the transaction in reducing horizontal competition between SBC and AT&T in the provision of network-based access services, with the result – or so they claimed – of adverse effects in retail and wholesale markets.

This analysis is fatally flawed for a number of reasons, the most obvious of which is that it is based on highly erroneous data. As AT&T and SBC showed in their Joint Opposition, filed May 10, these CLECs (1) woefully understate the number of CLEC buildings in SBC territory and in the MSAs on which these CLECs selectively focus; and (2) grossly overstate the number of AT&T buildings in those areas. They also ignore that AT&T's fiber network – in contrast to that of many other CLECs -- was designed and deployed primarily to serve AT&T's own *retail* customers, not to support wholesale special access service. And finally, they ignore that, under the Commission's own impairment test, CLECs would be able to replace AT&T's facilities in almost all of the extremely limited number of buildings – and it is a small fraction of the buildings these CLECs maintain – where AT&T is currently the only facilities-based competitive provider in SBC territory. In short, contrary to the claims of these CLECs, the merger would not materially increase concentration in the provision of special access services and would benefit, not harm, consumers of special access services.

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[1] The CLECs involved in the ex parte presentation were, according to their letter filed on May 10, 2005, Eschelon Telecom, NuVox Communications, TDS Metrocom, XO Communications, and Xspedius Communications ("the CLECs"). *See, Notice of Ex Parte Presentation, DA 05-656, WC Docket No. 05-65/DA 05-762, WC Docket No. 05-75*, filed May 10, 2005, by Kelley, Drye &Warren ("Eschelon Ex Parte May 10"), including presentation entitled "SBC/AT&T: Preliminary Analysis of Competitive Effects" ("Wilkie Presentation").

[2] Petition to Deny of CBeyond Communications, Conversent Communications, Eschelon Telecom, NuVox Communications, TDS Metrocom, XO Communications, and Xspedius Communications, April 25, 2005 ("CBeyond Petition"), including Declaration of Simon J. Wilkie ("Wilkie Decl.").

More specifically, contrary to the CLECs' assertions, AT&T accounts for only a small fraction of the CLEC-owned building connections in the SBC region. Other CLECs collectively and even individually have many more building connections than AT&T. Further, AT&T accounts for an even smaller fraction of building connections where it is the only facilities-based CLEC serving the building. AT&T *knows* this to be true because AT&T purchases wholesale private line services from more than 25 CLECs in SBC states.[3] To facilitate the provision of service to AT&T, many of these CLECs provide AT&T (on a monthly or quarterly basis) with lists of the specific buildings they can serve with their own facilities. These data show that the 25 CLECs from whom AT&T purchases wholesale special access services collectively have constructed their own dedicated fiber connections to **[REDACTED– SUBJECT TO PROTECTIVE ORDER]** buildings in areas where SBC is the incumbent LEC.[4] Of course, other CLECs, such as Sprint, from which AT&T does not purchase wholesale special access in SBC's incumbent service areas, serve additional buildings not reflected in these data.[5] Even so, the number of buildings to which AT&T has direct connections is dwarfed by the number of direct connections of these 25 CLECs. Specifically, AT&T has direct connections to only **[REDACTED– SUBJECT TO PROTECTIVE ORDER]** commercial buildings in the SBC region, and **[REDACTED– SUBJECT TO PROTECTIVE ORDER]** of these are already served by other CLECs as well.[6]

These data thoroughly refute the basis for the CLECs' claims. Whereas the CLECs assert that AT&T has thousands of exclusive connections to buildings in SBC territory, that is simply not the case. Indeed, their data is so far off the mark that they claim AT&T has fiber connections to more buildings in Milwaukee alone than AT&T, in fact, has in the entire SBC region. One reason for this discrepancy is that the CLECs count as "lit" large numbers of buildings in which AT&T *has no connection at all*, and in which AT&T provides service by leasing SBC special access channel terminations. Another reason is that the CLECs rely on incomplete data on lit buildings from GeoResults. The bottom line is that the CLECs grossly overstate the number of buildings in which AT&T is the only provider of competitive fiber and thus misrepresent the competitive impact of the merger.

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[3] In 2004, AT&T purchased special access services from the following competitive carriers in the 13 SBC states: **[REDACTED– SUBJECT TO PROTECTIVE ORDER]**. Fea Decl. ¶ 15. (All references to "Decl" and "Reply Decl" refer to Declarations and Reply Declarations filed by the Joint Opponents.

[4] Fea Reply Decl. ¶20

[5] Fea Reply Decl. ¶ 18; see also Carlton & Sider Reply Decl. ¶¶ 32-35 (providing data on MSA-specific basis). AT&T's data also largely excludes buildings served by cable-based providers of special access, notwithstanding that a March 2005 SBC survey found that **[REDACTED– SUBJECT TO PROTECTIVE ORDER]** of the DS-1 circuits that SBC had lost to competitors in 2004 were lost to cable providers.[5] All told, whereas the CLECs that provide data to AT&T have an average of 3.3 local networks in the SBC areas in which AT&T operates local fiber networks, the New Paradigm Research Group reports an average of 7 "other" CLEC networks in the same areas.

[6] Fea Reply Decl. ¶ 19; *see also* Carlton & Sider Reply Decl. ¶¶ 32-35 (providing data on MSA-specific basis).

While this is reason in itself to reject the CLECs' claims, that is not the only hole in their analysis. The CLECs also ignore Commission precedent that establishes that other CLECs readily could replace the AT&T connections in all or virtually all of the approximately **[REDACTED– SUBJECT TO PROTECTIVE ORDER]** buildings where AT&T is the only CLEC with direct connections. In the majority of these buildings,[7] *which account for* **[REDACTED– SUBJECT TO PROTECTIVE ORDER]** *of the bandwidth that AT&T provides through direct connections to buildings in SBC territory*,[8] AT&T is providing the OCn-level (or near OCn-level) facilities which the Commission has found can be deployed to any building anywhere by a reasonably efficient CLEC.[9] Many of the remaining few buildings are located in the most dense urban wire centers where the Commission has found that there is no impairment to the competitive deployment of DS3, or even DS1, facilities.[10] Still others are served by wireless connections that competitors could readily duplicate.[11] And virtually all of the rest present other conditions that would allow alternative facilities to be deployed.[12] The fact that customers in these buildings already have demonstrated their willingness to take service from a CLEC only makes these buildings all the more attractive targets for CLEC entry.

To the extent the CLECs raise concerns about the "loss of competition" from AT&T in buildings that AT&T serves only by leasing special access facilities from SBC or other carriers, these concerns are unfounded. In fact, the CLECs' own presentation demonstrates the point, albeit unwittingly. On page 18 of the presentation, the CLECs cite an example of an ostensible bid received by a CLEC for a single DS1 circuit from SBC, AT&T, MCI, and Sprint. The example, which is offered without any information whatsoever regarding the context, location or other circumstances in which these ostensible bids were made, purports to show that SBC's bid was the highest by far. But, it also shows that *none* of the other three companies was offering

[7] *Id.* ¶ 36 & Table 4; *see also* Fea Reply Decl. ¶¶ 30-31.

[8] Carlton & Sider Reply Decl. ¶ 36.

[9] *In re Unbundled Access to Network Elements.* Order on Demand, 18 FCC Rcd. 16978, ¶¶¶12, 20, 30, WC Dkt. No. 04-313, CC DKT No. 01-338, 2005 WL 289015 (Feb 4, 2005) (*"TR Remand Order"*).

[10] *Id.* ¶¶ 174-81; *see* Carlton & Sider Reply Decl. ¶¶ 15, 37-43; Fea Reply Decl. ¶ 16.

[11] *Triennial Review Remand Order*, 2005 WL 289013, ¶¶ 174-81; Fea Reply Decl. ¶ 34; Carlton & Sider Reply Decl. ¶¶ 37-43.

[12] Fea Reply Decl. ¶ 34. For example, some of AT&T's largest multi-location customers will demand that all of their locations be placed "on net." *Id.* ¶ 34. In such instances, most such locations will have OCn-level demand but some smaller offices may only have DSn-level demand. Because of the overall value of the contract, AT&T was able economically to deploy fiber for lower demand locations that would not be economic on a stand-alone basis. But this also means that other competitive carriers could self-deploy in these circumstances too. AT&T is also sometimes able to "hub" multiple buildings on a "campus" to a central point of aggregation. *Id*. ¶ 34. In those circumstances, some of the individual buildings might have less than OCn-level demand, but because of their proximity and ease of access, it is feasible to install short laterals to those individual buildings and backhaul the traffic to a common point of aggregation. Again, because of the aggregate revenue opportunity presented in such circumstances, other competitive carriers have the same economic ability to self-deploy facilities.

the service over its own facilities. Therefore, even accepting this purely anecdotal evidence as probative of something – which it is not -- the CLECs' own example shows that multiple CLECs – not just AT&T-- are able to offer highly competitive bid prices for channel termination facilities even where they lack their own network facilities. Nothing about the merger will change that; CLECs should be just as successful in competing with SBC (and each other) on bid prices after the transaction as before.[13]

To the extent that the presentation focused on AT&T's metropolitan fiber substituting for SBC's dedicated interoffice transport,[14] it is equally flawed. As the Commission has determined, the central business districts and other dense areas of the metropolitan areas where AT&T's metro fiber is concentrated are served by many other CLECs' fiber rings and are also the areas that offer the greatest "potential for further competitive build-out."[15] Indeed, multiple other CLECs are already collocated in all but six of the COs where AT&T has facilities-based collocations associated with its metropolitan fiber networks.[16] Thus, the transaction does not raise competitive concerns with respect to dedicated interoffice transport.

The final assertion made by the CLECs in their *ex parte* presentation is that, if both the SBC/AT&T transaction and the Verizon/MCI transaction were approved, neither company would compete in the other's region. This argument defies common sense. AT&T's principal assets are its national and international customer base and the facilities it uses to serve them. It is these assets that were the driving force behind the merger in the first instance. Thus, SBC is investing $16 billion to acquire AT&T precisely *because* it seeks to compete more effectively for businesses with national and international operations, including those with operations in the 30% of the country served by Verizon. Large and small customers alike located outside SBC's region constitute profitable customer segments, and SBC has every intention of making the most of its considerable investment by aggressively pursuing them.

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[13] If the CLECs argued in their presentation, as some did in Comments, that AT&T is able to offer such competitive bid prices because it purchases SBC special access services at deeper discounts than are available to other carriers, and then arbitrages those discounted rates against SBC's bid rates, there is no basis for such a claim. As demonstrated in detail in the Joint Opposition, AT&T has not received any unique prices based on its volume, and in fact at least one CLEC who opposed the Merger pays lower prices to SBC than does AT&T. More broadly, the suggestion that AT&T is a "frequent bidder" for the provision of wholesale special access circuits to other CLECs is belied by the facts. As shown in Reply affidavit of Anthony Fea *et al.*, AT&T's local access facilities – unlike those of many other CLECs -- were designed and deployed primarily to service its own retail customers, not to support wholesale special access alternatives for other carriers. Moreover, AT&T only rarely resells other carriers' local access facilities, as evidenced by its minimal Type II private line revenues. Thus, contrary to CLEC claims, and notwithstanding the one or two isolated and unidentified examples they offer, AT&T is *not* a key supplier of private line service to competitive carriers. *See* Fea Reply Dec. ¶¶ 35-43.

[14] Wilkie Presentation, at. 3, 13-16.

[15] *Triennial Review Remand Order* ¶ 94; *id.* ¶¶ 70 & 95.

[16] *See*, Joint Opposition, at 43-44.

To be sure, SBC's national/local business plans have thus far fallen short of expectations. Although SBC has spent well over $1 billion to date for facilities, sales and marketing, and product introduction, and although it is collocated in at least ten central offices in each of 30 MSAs, SBC's successes have been limited. But claims that any lack of success to date in competing out-of-region demonstrates a lack of commitment to out-of-region competition are simply wrong. The reality is that seventeen months passed after the announcement of the national-local strategy before implementation could begin, and another four years passed before the last Section 271 proceedings were completed and SBC was finally free to offer interLATA services everywhere. Moreover, a significant economic downturn, which particularly affected the telecommunications industry, began just as SBC was beginning to implement the national-local strategy, ushering in an era of massive overcapacity, falling demand, and collapsing prices.[17]

With the acquisition of AT&T, all of this will change. The combined company will be in a position to compete for the large and far-flung multi-location businesses AT&T serves today and therefore will have every incentive to compete vigorously nationwide, regardless of ILEC region. If the combined company were to redirect its focus to SBC's region alone, and serve only a portion of these customers' locations – which it can already do today – it could expect to lose customers to a multitude of competitors, including traditional IXCs, new long distance network operators, CLECs, and system integrators, among others.[18] The implicit suggestion that SBC will spend $16 billion simply to continue to operate as it does today is fanciful, inconsistent with simple economics,[19] and makes no business sense.

In addition, numerous characteristics of today's business marketplace make coordination or collusion highly unlikely.[20] First, the needs of customers are heterogeneous.[21] For example, Deloitte notes that it is common for business customers to combine the procurement of multiple types of telecommunications services with network installation and maintenance services.[22] Second, the stakes are high on each bid, with customers making the most of competition by combining or dividing requirements and using long contract terms (with "reopeners,"

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[17] Kahan Decl. ¶¶ 15-16.

[18] *Id.* ¶ 79.

[19] *See* Carlton & Sider Reply Decl. ¶¶ 78-80.

[20] Carlton & Sider Reply Decl. ¶¶ 83-84.

[21] *See generally*, Horizontal Merger Guidelines, Section 2.11 ("[R]eaching terms of coordination may be limited or impeded by product heterogeneity or by firms having substantially incomplete information about the conditions and prospects of their rivals' businesses, perhaps because of important differences among their current business operations. In addition, reaching terms of coordination may be limited or impeded by firm heterogeneity, for example, differences in vertical integration or the production of another product that tends to be used together with the relevant product.").

[22] Bazzi Reply Decl. ¶ 8.

benchmarking, or other clauses).[23] As Deloitte explains, business customers typically enter into long-term contracts with telecommunications suppliers.[24] Third, different customers use and prefer different sets of competitors. The customer statements filed with the Joint Opposition alone illustrate this point; Deloitte's analysis of the procurements in which it has been involved confirms it.[25] Virtually every customer is different with respect to its preference for providers and technologies to meet its unique needs.

As the foregoing discussion indicates, there is no basis for opponents' fear that the combined SBC/AT&T will engage in "tacit collusion" or "mutual forbearance" with respect to any customers, whether retail or wholesale, business or residential. SBC does not have a history of mutual forbearance, contrary to the merger opponents' charge, and both the fact and the price of the AT&T acquisition are inconsistent with the notion that the combined company will engage in tacit collusion. Finally, with respect to the business marketplace which forms the core of AT&T's business, significant marketplace factors render multi-firm coordination highly unlikely and extraordinarily difficult.

For more detailed discussion of these issues, we invite the Commission's attention to the Joint Opposition we filed on May 10, 2005.

Sincerely,

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[23] *See* Horizontal Merger Guidelines, Section 2.12 ("If orders for the relevant product are frequent, regular and small relative to the total output of firm in a market, it may be difficult for the firm to deviate in a substantial way without the knowledge of rivals and without the opportunity for rivals to react. If demand or cost fluctuations are relatively infrequent and small, deviations may be relatively easy to deter. . . . Where large buyers likely would engage in long-term contracting, so that the sales covered by such contracts can be large relative to the total output of a firm in the market, firms may have the incentive to deviate.").

[24] Bazzi Reply Decl. ¶ 8.

[25] *Id.* ¶ 7, 8.