

July 12, 2005

BY ECFS

Marlene H. Dortch
Secretary
Federal Communications Commission
445 Twelfth Street, S.W.
Washington, DC 20554

Re: *In the Matter of Applications for Consent to the Transfer of Control of Licenses and Section 214 Authorizations from AT&T Corp., Transferor, to SBC Communications Inc., Transferee, WC Docket No. 05-65*

Dear Ms. Dortch:

We are writing in response to a paper authored by Mark Cooper and filed in this docket by the Consumer Federation of America, Consumers Union, and USPIRG.¹ The paper ignores the rapid technological and marketplace changes affecting the telecommunications industry in order to reach its preordained conclusion that the merger of SBC and AT&T must be harmful to consumers. To the contrary, by enabling SBC and AT&T to respond and adapt to these technological and marketplace changes, the merger will create numerous public interest benefits without any lessening of competition.

Traditional wireline telephone services are indisputably in decline. By removing barriers to competitive entry in the local exchange and long distance businesses, the Telecommunications Act of 1996 helped to usher in an era of technological advances, which are rapidly supplanting traditional wireline services. SBC and AT&T have endured dramatic losses in market capital, revenues, and jobs as traditional wireline services have been displaced, and the pace of these changes is accelerating. SBC and AT&T seek to respond by creating a company that, unlike either SBC or AT&T alone, will have the assets and expertise to offer a broader array of services, enhance efforts to create new and improved services, and thus play a major role in bringing the benefits of this technological transformation to businesses and consumers alike. This combination will create a financially strong, U.S.-based global competitor, capable of delivering the

¹ See Mark Cooper, Consumer Federation of America, et al., *Broken Promises and Strangled Competition: The Record of Baby Bell Merger and Market Opening Behavior* (June 2005) (“CFA Paper”).

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advanced network technologies necessary to offer integrated, innovative, high quality, and competitively priced telecommunications services to meet the needs of all classes of customers.

Dr. Cooper and those who share his perspective are unable or unwilling to acknowledge these unstoppable technological and marketplace changes. They can see only the past and not the realities of the communications marketplace in 2005 and beyond. The Commission should eschew this perspective and allow SBC and AT&T to respond effectively to this new environment and create a combined company capable of meeting the needs of customers.

Technological Advances and Marketplace Developments Are Causing a Decline in Traditional Wireline Services.

Dr. Cooper discounts the unrelenting and accelerating attack on traditional wireline service by such emerging technologies as cable, VoIP and wireless, which are growing geometrically as demand for wireline services steadily declines. He claims that the merging parties “fantasize” about such competition, which he calls “quite limited,” and he bemoans the “dearth of competitive alternatives.”² The facts, however, show otherwise.³ In 2005, it is projected that:

- There will be more wireless “lines” than “wirelines” in the United States.⁴
- Residential broadband connections will surpass dial-up connections.⁵

² CFA Paper at 8, 7, 1.

³ See generally SBC-AT&T Public Interest Statement at 57-63 (“Public Interest Statement”); SBC-AT&T Joint Opposition at 106-16 (“Joint Opposition”); Letter from Gary L. Phillips, SBC Communications Inc., and Lawrence J. Lafaro, AT&T Corp., to Marlene H. Dortch, dated June 1, 2005, at 7-8.

⁴ Frost & Sullivan, U.S. Communication Services Market Overview and Future Outlook, at 89 (2004); Press Release, CTIA, U.S. Consumers Make Wireless Top Choice (July 11, 2005), http://www.ctia.org/news_media/press/body.cfm?record_id=1533.

⁵ Ken Belson, *Dial-Up Internet Starts to Go the Way of Rotary Phones*, N.Y. Times, June 21, 2005, at C1.

- More homes will have access to cable telephony than will not.⁶
- Large enterprises will spend more on wireless and data than on wireline voice.⁷

These developments, all of which reflect reduced demand for traditional wireline services, feed upon one another. For example, the rollout of broadband facilitates the use of related communication technologies, such as VoIP, email, and instant messaging, which reinforce the downward trend in wireline usage. Indeed, relative to 2000 levels, use of wireline products has dropped by more than 20% while wireless, email, and instant messaging use have more than tripled.

The Merger of SBC and AT&T Will Facilitate Their Ability To Embrace These Technological Advances.⁸

Both SBC and AT&T tried on their own to adapt to the transformation of the telecommunications marketplace that has resulted from these rapid technological advances. Each company, however, came to realize that it was missing key components for the future – components that the other possesses.

- SBC is a financially strong provider of voice, data, broadband, and related services to consumers, businesses – especially small and mid-sized business – and wholesale customers, primarily on a local and regional basis in its 13-state region. SBC holds a 60% ownership interest in Cingular Wireless and is a leading provider of residential broadband DSL service where it provides local exchange service in its 13-state region. SBC is making a \$4 billion investment to implement its initial rollout of next-generation video and other IP-based voice and data services to 18 million households within three years. Although AT&T was at one time a participant in the mass market segment, it has ceased all active marketing efforts to mass market customers for

⁶ Bernstein Research, “Cable and Telecom: VoIP Will Reshape Competitive Landscape in 2005,” at 2 (Dec. 17, 2004).

⁷ Bernstein Research, “U.S. Telecom: Enterprise Market to Drive Half the Industry’s Growth,” at 2 (Jan. 21, 2005).

⁸ See generally Public Interest Statement at 13-44; Joint Opposition at 8-22.

numerous reasons unrelated to the merger. As a result, this merger will have no effect on competition in the mass market segment.

- AT&T has an entirely different focus. It provides a broad array of voice, data, and IP-based services to customers on its global and national IP-based networks. It has a presence in more than 50 countries, allowing it to compete for the business of the largest global enterprises. AT&T has been a leader in the development of innovative products through its AT&T Labs.

Combining the two companies' core strengths will result in more investment in, and faster deployment of, innovative new technologies and services. The combined company will have the resources, expertise, and incentive to adapt the sophisticated products that AT&T has developed for its enterprise customers to the needs of small and medium businesses and consumers, and the marketing expertise and infrastructure to reach those customers that are SBC's focus and no longer a part of AT&T's business plan. The integration of the two companies' networks will improve the quality and reduce the cost of service; decrease latency and increase reliability; improve performance for VoIP, video, and other real-time services; and allow the combined company to offer more competitive Service Level Agreements. Together, SBC and AT&T will have the assets and expertise necessary to assemble a true nationwide end-to-end broadband network and play an important role in the ongoing technological advances in the telecommunications industry. Indeed, the merger will produce a flagship U.S. carrier that will offer the most efficient, highest quality capabilities to government, business, and residential customers nationwide.

The Merger Will Not Lessen Competition.

These manifold benefits of the merger will be achieved without any lessening of competition. Because SBC's and AT&T's operations are highly complementary, combining them will not reduce competition for mass market customers, business customers, special access services, or the Internet.

*Mass Market Customers.*⁹ The merger will not reduce the intense competition for mass market customers, notwithstanding Dr. Cooper's overwrought claims that the merger "will have a devastating impact on the nation's residential customers."¹⁰ In

⁹ See generally Public Interest Statement at 44-67; Joint Opposition at 95-121.

¹⁰ CFA Paper at 1.

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July 2004, AT&T irrevocably stopped actively marketing traditional mass market services. AT&T thus no longer promotes its traditional mass market services through advertising, telemarketing, direct mail, or affinity agreements. AT&T also has stopped matching competitive offers. Because AT&T is not actively competing on price or marketing itself as an alternative to SBC for traditional mass market services, the merger will not change SBC's current pricing incentives, which are strongly influenced by cable, wireless, and other traditional and non-traditional competitors. In such a situation, Dr. Cooper's back-of-the-envelope version of an analysis of market definitions and static market shares is inapposite. AT&T's historic market share overstates its future competitive significance¹¹ – with or without the merger, AT&T will not be a competitive constraint on pricing for mass market customers.

The folding into SBC of AT&T's provision of VoIP services to mass market customers also will not harm competition. Dr. Cooper claims that "AT&T has hardly withdrawn itself from competing for residential mass-market customers" but was "turn[ing] to the VoIP market as a more profitable method of reaching mass-market customers" and could have affected competition for mass market customers in that way.¹² In fact, AT&T has ceased direct marketing of its VoIP service to mass market customers,¹³ and those services had struggled in the marketplace with intense competition from numerous competitors offering the same capabilities, including "bring your own broadband" providers like Vonage and cable companies like Cox, Time Warner,

¹¹ See *FTC v. Nat'l Tea Co.*, 603 F.2d 694, 700 (8th Cir. 1979); *Capital Cities/ABC, Inc. v. FCC*, 29 F.3d 309, 315 (7th Cir. 1994) (Posner, C.J.) (it has been "many years since anyone knowledgeable about antitrust policy thought that concentration by itself imported a diminution in competition"); see *In re Applications of AT&T Wireless Servs., Inc. & Cingular Wireless Corp.*, Memorandum Opinion and Order, 19 FCC Rcd. 21522, 21565 ¶ 96, n.309 (2004) (noting that for "a growing and dynamic industry . . . HHIs and changes in HHIs may be less predictive as to whether the merger could result in anticompetitive behavior in a particular geographic market than they would if the market were stable"); *id.* at 21575, ¶ 133 (finding that recent changes in "market share and porting data suggest that Verizon Wireless, T-Mobile, and Nextel may provide more effective competitive constraints on the Applicants than their current subscriber-based market shares might indicate"); *id.* at 21594, ¶ 186 (concluding that "even rival carriers with relatively small market shares currently may have the ability to discipline the market in the future if they do have adequate capacity to add customers").

¹² CFA Paper at 3.

¹³ See Joint Opposition, Declaration of Cathy Martine, ¶¶ 2-9.

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Comcast, and Cablevision.¹⁴ Even more competition is coming, with AOL, Cisco, Covad, and others entering the marketplace.¹⁵

The merger will not affect this burgeoning competition. Cable companies are aggressively targeting mass market customers, VoIP and wireless are growing rapidly, and traditional carriers remain an important alternative. For example:

- Cable executives believe that the industry will sign up more than 20 million VoIP subscribers over the next few years.¹⁶
- Vonage, the largest VoIP provider, already has more than 700,000 subscribers.¹⁷
- Time Warner Cable has announced that 500,000 subscribers have signed up for its digital telephone service, and its chief executive has said that customers are buying into broadband phone service faster than they bought into high-speed Internet service.¹⁸
- Cablevision has announced that it has signed up more than 400,000 subscribers for its telephone service,¹⁹ and is adding about 1,000 subscribers per day.²⁰

¹⁴ See Joint Opposition at 108-110.

¹⁵ See *id.* at 110.

¹⁶ *Cable Executives See More Potential in VoIP, Data, Commercial Services*, Communications Daily, June 16, 2005.

¹⁷ http://www.vonage.com/corporate/aboutus_fastfacts.php.

¹⁸ David Hayes, *Partners Play It Coy*, The Kansas City Star, May 24, 2005, at 11.

¹⁹ Cecile Daurat, *Time Warner Cable Signs Up 500,000 Phone Customers*, Bloomberg News, May 25, 2005.

²⁰ Ted Hearn, *VoIP Firms Get '911' Mandate*, Executive Profile Wire, May 23, 2005, available at 2005 WLNR 8671126.

- Comcast has rolled out VoIP in three markets and expects that the service will be available to 15 million homes by the end of 2005.²¹

*Business Customers.*²² The merger will further heighten the already intense competition to serve business customers. Numerous competitors vie to provide telecommunications services to business customers, SBC and AT&T offer largely complementary services to such customers, and the combined company will be able to respond better to the needs of such customers than either company alone. There is thus no merit to Dr. Cooper's claim that the merger will "exacerbate the already-significant problems" for business customers.²³

The FCC has repeatedly described the marketplace for services provided to larger businesses as "increasingly competitive" in view of the many competitors, which include:

- IXCs such as MCI, Sprint, and Qwest.
- National network providers such as Broadwing, Global Crossing, Level 3, and SAVVIS.
- International networks with an increasing U.S. presence such as France Telecom-Equant, BT-Infonet, and NTT-Verio.
- System integrators such as Accenture, IBM, and EDS.
- Equipment vendors such as Cisco and Nortel.
- VSAT providers such as Hughes and Gilat.
- Cable companies, other ILECs and CLECs.

Technological advances are leading to still more competition as VoIP, cable, and wireless providers enter the marketplace. Dr. Cooper's analysis, which is rooted in data that

²¹ Reinhardt Krause, *Offering Phone Services Helps Cable Companies Gain Users Vs. Satellite TV*, Investor's Business Daily, May 23, 2005.

²² See generally Public Interest Statement at 67-105; Joint Opposition at 121-149.

²³ CFA Paper at 11.

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reflect SBC's historical position in local markets prior to the 1996 Act, fails to reflect these facts.

Not only are numerous competitors vying to serve business customers, but SBC and AT&T's activities in serving business customers are far more complementary than they are similar, minimizing any reduction in competition. SBC's strengths are local services, and simple, traditional voice and data services, while AT&T's strengths are long distance services and complex, managed services. SBC focuses on sales to small and medium-sized businesses within its 13-state region, while AT&T focuses on sales to larger nationwide and worldwide businesses.

By combining their distinct strengths, SBC and AT&T will be able to respond to core customer needs in a way that neither SBC nor AT&T could on its own – end-to-end services; consolidated networks over which a single company will be able to maintain control and provide high-quality, uninterrupted service; a complete package of well-integrated services; and efficient billing and customer service mechanisms. Not surprisingly, dozens of business customers have made filings in this proceeding to voice their support for the merger.²⁴ In short, the merger will enhance, not reduce, competition.

*Special Access.*²⁵ The merger will not affect the market for special access services. As we have stated on numerous occasions,²⁶ AT&T has only limited facilities in the SBC region, and there are many other CLECs with more extensive local networks and greater capacity than AT&T. Indeed, the buildings served by AT&T in SBC's territory that either already are not or readily could not be served by another CLEC comprise but a tiny fraction (0.15%) of the commercial buildings in SBC's territory.²⁷ Dr. Cooper's arguments to the contrary are based on a fatally flawed study by Professor Simon Wilkie who, without record support, assumes wrongly that AT&T's special access

²⁴ See, e.g., Joint Opposition, Customer Statements.

²⁵ See generally Public Interest Statement at 102-05; Joint Opposition at 26-60.

²⁶ See, e.g., Letter from Gary L. Phillips, SBC Communications Inc., and Lawrence J. Lafaro, AT&T Corp., to Marlene H. Dortch, dated June 24, 2005; Letter from Peter J. Schildkraut, Arnold & Porter LLP, to Marlene H. Dortch, dated June 29, 2005.

²⁷ Letter from Peter J. Schildkraut, Arnold & Porter LLP, to Marlene H. Dortch, dated June 29, 2005, Presentation of Dennis Carlton & Hal Sider, Lexecon, June 28, 2005, at 10.

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facilities are many times more extensive than they actually are, and that other CLECs' facilities are less extensive than they actually are.

As we have shown,²⁸ the data used by Professor Wilkie grossly overstates the true competitive significance of AT&T's local facilities while also deflating other CLECs' capabilities and significance. Further, AT&T did not deploy these facilities in order to provide wholesale services, and it receives only a modest amount of revenue from such services. The competitors sponsoring Professor Wilkie have refused to provide access to the data on which he has purportedly based his study or enter the data into the record of this proceeding – a sure indicator of how unreliable it is.

Dr. Cooper also raises the issue of special access pricing. As we have stated before,²⁹ any issues related to special access pricing are not germane to the merger and should be addressed by the Commission in its ongoing Special Access rulemaking proceeding but, in any event, given the facts summarized above, there is no reason for concern that this transaction materially reduces competition in special access services.

*Internet.*³⁰ The merger will not harm competition in the provision of Internet services. Dr. Cooper alleges that “the mergers pose a severe threat to the competitiveness of [the Internet backbone] market and the openness of access to the Internet.”³¹ His arguments, however, are largely premised on a nonexistent combined merger of SBC, AT&T, Verizon, and MCI into a single company and on outdated metrics and views from half a decade ago – an eternity in the current telecommunications revolution.

Lacking a basis to challenge this transaction on its own merits, Dr. Cooper argues that the SBC/AT&T merger must be examined in the context of the acquisition of MCI by Verizon. He postulates, without any support, that the two combined companies will become “mega-peers” that will peer only with each other and will force all other backbone providers to pay for service. However, as we have shown,³² the current

²⁸ See Letter from Gary L. Phillips, SBC Communications Inc., and Lawrence J. Lafaro, AT&T Corp., to Marlene H. Dortch, dated June 24, 2005.

²⁹ See, e.g., Joint Opposition at 28-29.

³⁰ See generally Public Interest Statement at 105-111; Joint Opposition at 60-74.

³¹ CFA Paper at 17.

³² See Letter from Gary L. Phillips, SBC Communications Inc., and Lawrence J. Lafaro, AT&T Corp., to Gary Remondino, dated July 6, 2005.

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competitive nature of the Internet backbone provider (“IBP”) market and fundamental economic principles demonstrate that such a claim must be rejected.

SBC is not a Tier 1 IBP today, and thus its merger with AT&T will have no impact on peering nor create a hypothesized “mega-peer.” MCI’s backbone is no longer so large that merger with Verizon would create a “mega-peer.” Instead, AT&T and MCI are two of at least seven IBPs, each of which has between 5% and 12.5% of total IBP traffic. Thus, there will not be two “mega-peers,” but rather there will continue to be several backbone providers of comparable size.

As a result, SBC/AT&T’s incentives to peer with Verizon/MCI will be the same after the merger as AT&T’s current incentives to peer with several other current IBPs of comparable size to Verizon/MCI. Furthermore, even accepting for the sake of argument the unsupported premise that SBC/AT&T would act in conjunction with Verizon/MCI, the combined SBC/AT&T would not have the leverage to de-peer these other IBPs. Consequently, SBC/AT&T would have the same incentive as AT&T has today to peer with all other backbone providers.

The competitive nature of the IBP market also undercuts Dr. Cooper’s arguments regarding pricing increases and selective quality degradation. Any increase in the merged company’s transit prices (or attempts to impose paid peering) would, in fact, result in the migration of traffic to one of several other IBPs (which the merging parties would have to continue accepting as peers), thereby defeating the price increase and simultaneously reducing the merged company’s own traffic. IBP competition also mandates that, for time-sensitive services, IBPs offer and stand behind Service Level Agreements, which set minimum requirements for packet latencies. Service quality is easily measured by subscribers, and any degradation would again be met by migration to one of many IBP competitors, loss of traffic, and harm to reputation.

Dr. Cooper further posits that SBC’s and Verizon’s separate mergers will, in combination, destroy the existing balance in peering because the broadband ISPs brought into the fold by the mergers give the two backbones access to more “eyeballs” (*i.e.*, users who are in search of content). Even assuming, *arguendo*, that a monopoly over eyeballs would lead to a monopoly over content, SBC’s and AT&T’s shares of eyeballs do not remotely approach monopolization levels. The cable companies and other ISPs have significantly more eyeballs than the two merging parties. When evaluating traffic shares of IBPs, an IBP competes for Internet traffic provided by ISPs. The number of residential and small business broadband lines reported in public statements by the

broadband ISPs indicates that, for residential and small business customers, more than 70% of the total eyeballs are controlled by ISPs not party to either this or the separate Verizon/MCI transaction.³³ Consequently, even when both mergers are completed, neither merging party would be able to alter existing peering arrangements.

The Merger Will Enable SBC To Compete Nationwide.

The merged company will be a nationwide competitor, and Dr. Cooper's claim that it will enter into a "mutual non-aggression pact"³⁴ with Verizon/MCI is absurd. One of the principal benefits of the merger for SBC is an enhanced ability to compete to serve enterprise customers, particularly in out-of-region locations where SBC today finds itself at a competitive disadvantage.³⁵ This goal would be thwarted, and a substantial portion of SBC's \$16 billion investment would be wasted, if SBC were not to compete nationwide. A combined SBC/AT&T will have strong and indisputable economic incentives to continue to make productive use of and expand upon acquired out-of-region facilities and customer relationships. SBC (through Cingular) and Verizon (through Verizon Wireless) compete vigorously against each other today; there is no reason to believe that they would compete against each other in wireline services any less aggressively after both proposed transactions close.

Apart from the fact that the postulated mutual forbearance alliance would be fundamentally incompatible with the goals of the merger, it would also be doomed to fail if tried. Even if Verizon were induced to idle the MCI facilities deployed in SBC's territory, and *vice versa*, both companies would still face stiff competition from the many other active market participants. The weakness of Dr. Cooper's argument is further acknowledged in the Department of Justice's *Horizontal Merger Guidelines*,³⁶ which recognize that it is highly unlikely that companies, such as SBC/AT&T and

³³ Moreover, as Chairman Martin has observed, "broadband platforms are engaged in fierce competition" and "broadband access is increasingly being delivered to consumers via satellite, wireless, and fiber or powerline providers." Kevin J. Martin, *United States of Broadband*, Wall St. J., July 7, 2005, at A12.

³⁴ CFA Paper at 25.

³⁵ As the parties outlined in their Joint Opposition, SBC has been aggressive in competing out of region having invested billions of dollars in out-of-region facilities and marketing efforts. The results unfortunately have fallen below expectations. See Joint Opposition at 150-57.

³⁶ § 2.11.

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Verizon/MCI, could tacitly reach and police an agreement to refrain from competing for certain customers under these conditions.³⁷

* * * * *

The telecommunications industry is in the midst of a trying period of “creative destruction” brought on by rapid technological advances. SBC and AT&T are merging to position themselves to play an important role in the future of the competitive and dynamic telecommunications industry. Their merger will bring numerous public interest benefits and will in no way reduce competition. The Commission should disregard the backward looking vision of Dr. Cooper and promptly approve the merger.

Sincerely,

SBC Communications Inc.

AT&T Corp.

/s/ Christopher M. Heimann

/s/ Lawrence J. Lafaro

Christopher M. Heimann
SBC Communications Inc.
1401 I Street, N.W.
Suite 400
Washington, D.C. 20005
Tel: (202) 326-8909

Lawrence J. Lafaro
AT&T Corp.
Room 3A 214
One AT&T Way
Bedminster, NJ 07921
Tel: (908) 532-1850

cc: Tom Navin
Don Stockdale
Julie Veach
Bill Dever
Marcus Maher

³⁷ Dr. Cooper also attempts to attack SBC’s character by pointing to allegations contained in the Petition to Deny of Cbeyond et al. He neglects to mention, however, that Cbeyond’s allegations generally were discredited by the Commission’s decision in the Cingular/AT&T Wireless merger. *In re Applications of AT&T Wireless Servs., Inc. & Cingular Wireless Corp.*, Memorandum Opinion and Order, 19 FCC Rcd. 21522, 21550 ¶¶ 53-54 (2004).