October 21, 2005

Via ECFS

Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 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:

Various competitors of SBC Communications Inc. and AT&T Corp. (the "Applicants") have flooded the Commission with ex parte submissions in the past few days. While voluminous, these submissions merely repeat the same flawed arguments that have been made previously and merit very little (if any) response. Nonetheless, to set the record straight one more time, the Applicants take this opportunity to respond briefly to some of these competitors' more fanciful claims and requests.

XO's Collusion Claim Is Based on Unsupported Assumptions and Alleged "Data" and Ignores Reality

XO Communications ("XO") has submitted a Supplemental Declaration of Simon Wilkie that purports to establish that the post-merger SBC/AT&T and the post-merger Verizon/MCI would find it profitable to agree tacitly not to compete where the other is the incumbent provider of special access services.[1] The declaration proves nothing of the sort; it establishes only that any conclusion is possible if one makes the right assumptions and ignores or twists facts and logic.

Dr. Wilkie's conclusion is based on the following fundamental hypothetical: "By tacitly colluding, I *assume* that the ILEC can raise special access revenues by (at least) five percent . . . ."[2] Without that assumption, he cannot reach his preordained conclusion.[3] Absolutely no evidence or argument is presented to support that assumption, and it is contradicted by other assumptions he makes.

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1 Supplemental Declaration of Simon Wilkie ("Wilkie Supp."), attached to Letter from Thomas Cohen, Kelley Drye & Warren LLP, to Marlene H. Dortch, FCC, WC Docket No. 05-65 (Oct. 18, 2005).

2 Wilkie Supp. ¶ 8 (emphasis added).

3 For example, if Dr. Wilkie had assumed revenues would increase by 1%, his calculations would lead to the conclusion that collusion would not be profitable.

Dr. Wilkie relies on evidence submitted by SBC showing that "competitors in the wholesale market for special access have won more than [a] 40 percent share within SBC's territory . . . ."[4] He also assumes that MCI's special access revenues are equal to 6%, and AT&T's special access revenues are equal to 4%, of the ILEC's share.[5] If SBC's special access share is 60% (100%-40%), then, according to Dr. Wilkie, MCI's and AT&T's combined shares are 6% ((.06 + .04) x 60%. Simple arithmetic shows that other CLECs have a 34% special access share, almost 6 times the combined share of MCI and AT&T). Dr. Wilkie does not explain why eliminating competitors with such a small share would permit a 5% price increase when other competitors collectively have successfully obtained a much larger share of special access revenues. And, given that MCI's and AT&T's special access facilities are predominantly in major metropolitan areas where other CLECs have excess fiber capacity, it is readily apparent that these other CLECs can and would expand to compete for the business that Dr. Wilkie assumes that AT&T and MCI would abandon. Thus, there is no reason to expect any price rise whatsoever.

The fanciful assumption of a 5% revenue increase has at least two other critical flaws. First, Dr. Wilkie must believe that either (1) MCI has special access facilities throughout SBC's ILEC territory (and AT&T has similar facilities throughout Verizon's ILEC territory) or (2) the revenue increase in areas where MCI and AT&T have facilities would be far larger than 5%. The first belief is contrary to undisputed evidence; the second just makes his revenue assumption all the more illogical. Second, his profit calculation assumes that this revenue increase could be maintained in perpetuity. Given the dynamic nature of telecommunications, including expansions by other CLECs and new, emerging technologies,[6] such an assumption is plainly unreasonable, particularly given that AT&T and MCI have both targeted the same dense metropolitan areas as numerous other CLECs, which would be well-positioned and strongly incented to serve areas experiencing supracompetitive pricing.

Dr. Wilkie repeats the unsupported claim that AT&T's and MCI's special access rates are half of those charged by SBC and Verizon. This claim can be given no credence whatsoever because it is based on selected data that Dr. Wilkie and his sponsors have chosen to keep secret. At least with respect to AT&T, they have repeatedly refused to provide those data for the record of this proceeding, even under a protective order, to protect those data from the critical review of

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4 *Id.* ¶ 7.

5 *Id.* ¶ 10. AT&T does not sell a service it calls special access. It sells a local private line service in certain geographic areas which can be purchased by CLECs to perform the same function as an ILEC's special access service.

6 *See, e.g.*, Carol Wilson, *Recent Moves Give CLECs Air Assault*, Telephony, Oct. 17, 2005, at 6, 7 ("'The technology has been moving fast for the last three to five years,' [XO Communications CEO Carl] Grivner said. 'And it has the ability to give us freedom from the ILEC. It's so cheap and easy to deploy – it's a win-win situation for us and our customers.'").

Commission staff and the Applicants.[7] For example, though we cannot know without inspecting the data, it appears that Dr. Wilkie is comparing apples and oranges by comparing the rates at which AT&T and MCI sell services used for special access and ILECs' rack rates, not the rates the ILECs actually charge, which often include volume or other discounts. Whatever the reason for hiding them from the Commission and the Applicants, data that are not in the record cannot be relied upon, and arguments based on them are entitled to no credence. Dr. Wilkie's claim is inconsistent even with the claims of other CLECs, which have argued that AT&T's rates are 15% to 35% below SBC's rates.[8] Significantly, the Applicants were able to demonstrate that even these claims were spurious because, *inter alia*, they were based on SBC's rack rates, not the rates customers actually pay.[9]

Not only is Dr. Wilkie's "analysis" flawed because it is built on unsupported assumptions, but it also ignores the Commission's precedents, rules and other aspects of business reality. For example, he relies on ARMIS accounting data in claiming that SBC's operating margin in special access services is 64% and Verizon's operating margin in special access services is 36%.[10] As SBC explained in detail in its Comments and Reply Comments in the Special Access NPRM Proceeding, it is not possible to calculate an economically meaningful rate of return for a specific service using ARMIS accounting data. ARMIS accounting is based on outdated cost allocation rules, as the Commission itself has recognized, and the cost allocation process was rendered even more unreliable by the 2001 separations freeze.[11]

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7 To the extent that opponents mean to suggest that the Commission should accept their claims about other CLECs' special access prices as evidence of the relationship between AT&T's and SBC's prices, the unchallenged record evidence demonstrates that AT&T's dedicated access prices are typically *higher* than those charged by other CLECs. Letter from Gary L. Phillips, SBC Communications Inc., & Lawrence J. Lafaro, AT&T Corp., to Marlene H. Dortch, FCC, App. A at 4-5, WC Docket No. 05-65 (Aug. 1, 2005); *see also* Letter from Gary L. Phillips, SBC Communications Inc., & Lawrence J. Lafaro, AT&T Corp., to Marlene H. Dortch, FCC, at 3, WC Docket No. 05-65 (Aug. 24, 2005) ("8/24/05 SBC-AT&T Ex Parte").

8 Letter from Patrick J. Donovan, Swidler Berlin LLP, to Marlene H. Dortch, FCC, Att. at 2, WC Docket No. 05-65 (Aug. 10, 2005).

9 8/24/05 SBC/AT&T Ex Parte.

10 Wilkie Supp. ¶ 7.

11 SBC Commc'ns Inc., Reply Comments at 35-43 *in In re Special Access Rates for Price Cap Local Exchange Carriers; et al.*, WC Docket No. 05-25; et al. (July 29, 2005); SBC Commc'ns Inc., Comments at 24-37 *in id.* (June 13, 2005). Even a merger opponent like Qwest agrees wholeheartedly. *E.g.*, Qwest Commc'ns Int'l, Inc., Reply Comments at 6-9 *in id.* (July 29, 2005) (stating among other points, "Qwest and others have previously explained in detail the numerous pitfalls of drawing any conclusions from special access rates of return. In short, rates of return for individual services based on fully distributed costs are meaningless, because such computations rely on arbitrary allocations of common costs. Moreover, the accounting and jurisdictional separations rules underlying

The hypothetical 5% revenue increase on which the collusion "analysis" is based also ignores the real-world fact that ILEC special access rates are subject to price caps, except where pricing flexibility has been granted. Where rates are capped, they cannot be increased; and where pricing flexibility has been granted, the Commission has found that other competitors are present and constrain the ability of the ILEC to raise prices. Dr. Wilkie does not address these points.

Moreover, the argument that tacit collusion would be profitable inherently assumes that the parties engaged in collusion could get away with it, in other words, that the collusion would not be detected. It may be conceivable that a tacit agreement between two parties not *to enter* into competition with each other may not be detected. Indeed, in introducing the concept of tacit collusion, Dr. Wilkie describes two firms which implicitly agree not to enter into competition against the other.[12] That situation, however, ignores the present reality. AT&T and MCI are currently providing local private line or special access services in Verizon's and SBC's ILEC regions, respectively. In addition, AT&T buys special access services from numerous competitors across the country including in Verizon's region. A sudden discontinuance of these purchases would not go unnoticed. Dr. Wilkie's calculation ignores this fundamental reality. He assumes a world that simply does not exist. More fundamentally, as the Applicants have demonstrated repeatedly in this proceeding, they have neither the incentive nor the ability to refrain from competing in Verizon territory. SBC would not have spent $16 billion to compete more effectively for national and global enterprise customers, only to refrain from competing in some of the most lucrative markets in the world. Nor are market conditions conducive to tacit collusion in any event because of the characteristics of buyers, the heterogeneous nature of the services they purchase and the manner in which they purchase them. All of this has been discussed before. Dr. Wilkie, having no answer, simply ignores that discussion.

Of course, actions speak louder than words. Contrary to Dr. Wilkie's speculation, the Applicants have announced an extension to AT&T's commercial agreement with Time Warner Telecom to purchase out-of-region private line and special access services, including in Verizon territory, through 2010, as well as an agreement with Covad for out-of-region broadband access services.[13]

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the rate-of-return figures have failed to keep up with the introduction of new services over the past decade.") (footnote omitted).

12 Wilkie Supp. ¶ 4 ("For example, suppose firm A could profitable [sic] enter firm B's market, which would compete down the price in that market. However, firm A does not to [sic] enter because of the threat of retaliation – in particular, that firm B would enter and sufficiently compete down price in firm A's market, thus offsetting the firm A's additional profits earned from entry. By a similar logic, firm B does not to [sic] enter firm A's market, and the two firms are engaged in tacit collusion.").

13 SBC Press Release, "Time Warner Telecom, AT&T, SBC Extend Long-Term Service Agreement," June 1, 2005, *available at* http://www.sbc.com/gen/press-room?pid=4800&cdvn=news&newsarticleid=21695; SBC Press Release, "SBC, AT&T

The Conditions Sought by Various CLECs Are Improper Because They Do Not Address Any Merger Specific Concerns and, Even if They Did, They Are Not Appropriately Tailored

Two different groups of CLECs ask that the Commission adopt a host of UNE-related conditions.[14] But, like the conditions proffered by other merger opponents, there is no basis for adopting these conditions, both because there is no merger-specific harm to remedy and because the proposed conditions are not a narrowly tailored response to the extremely limited competitive overlap between SBC and AT&T.[15] Indeed, for the most part, the requested conditions amount to nothing more than procedurally improper petitions for reconsideration of the Commission's *Triennial Review Remand Order* and *Triennial Review Order*, which belong in that docket not this one.

First, these CLECs ask for a cap on SBC's UNE rates,[16] notwithstanding that the Commission has initiated a rulemaking proceeding to consider whether, among other things, UNE rates are too low. The CLECs concede, as they must, that SBC's UNE rates are, in fact, regulated by state commissions and that SBC has no ability to raise these rates unilaterally. Nonetheless, they say that, without AT&T and MCI as advocates for CLECs, state commissions will simply knuckle under to SBC and raise UNE rates.[17] At bottom, these CLECs are claiming that state regulators cannot make sound decisions in the public interest unless AT&T and MCI, and only AT&T and MCI, continue exercising their lobbying and litigation acumen in the service

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Reach Services Agreements with Covad," May 5, 2005, *available at* http://www.sbc.com/gen/press-room?pid=4800&cdvn=news&newsarticleid=21667.

[14] Letter from Brad E. Mutschelknaus & Chip A. Yorkgitis, Kelley Drye & Warren LLP, to Marlene H. Dortch, FCC, WC Docket No. 05-65 (Oct. 18, 2005) ("10/18/05 Kelley Drye Ex Parte"); Letter from Patrick J. Donovan & Philip J. Macres, Swidler Berlin LLP, to Marlene H. Dortch, FCC, WC Docket No. 05-65 (Oct. 19, 2005) ("10/19/05 Swidler Ex Parte"); Letter from Andrew D. Lipman et al., Swidler Berlin LLP, to Marlene H. Dortch, FCC, WC Docket No. 05-65 (Oct. 19, 2005) ("10/19/05 Lipman Ex Parte").

[15] *In re Application of Rainbow DBS Co. LLC & EchoStar Satellite L.L.C.*, IB Docket No. 05-72, Memorandum Opinion and Order, FCC 05-177, at 7-8 ¶ 13 (rel. Oct. 12, 2005) ("Our public interest authority also enables us to impose and enforce narrowly tailored, transaction-specific conditions that ensure that the public interest is served by the transaction."); *In re Applications of Nextel Commc'ns, Inc. & Sprint Corp.*, WT Docket No. 05-63, Memorandum Opinion and Order, FCC 05-148, at 12-13 ¶ 23 (rel. Aug. 8, 2005) (same); *In re Applications of W. Wireless Corp. & AllTel Corp.*, WT Docket No. 05-50, Memorandum Opinion and Order, FCC 05-138, at 13-14 ¶ 21 (rel. July 19, 2005) (same); *In re Applications of AT&T Wireless Servs., Inc. & Cingular Wireless Corp.*, Memorandum Opinion and Order, 19 FCC Rcd. 21522, 21545-46 ¶ 43 (2004) (same).

[16] 10/18/05 Kelley Drye Ex Parte, Att. at 1; 10/19/05 Swidler Ex Parte, Att. at 1.

[17] 10/18/05 Kelley Drye Ex Parte at 3.

of pure CLEC interests. That is nonsense as the flood of lobbying activity in this very docket clearly demonstrates. After this merger, the United States will still have scores of CLECs – including the very CLECs advancing this argument – each of which will remain free to express its position on any regulatory issue, as well as several high-profile trade associations that speak for CLECs in legislative and regulatory forums across the nation.[18]

Next, the CLECs demand that the Commission require that SBC price UNEs provided under § 271's "just and reasonable" standard at a level no more than 115% of UNEs provided pursuant to § 251(c)(3)'s TELRIC standard.[19] This is nothing more than a back-door attempt to flash cut SBC's special access rates and reverse the Commission's *Triennial Review Order* – where the Commission refused to set § 271 UNEs at TELRIC-based rates. As we explain in greater detail in our letter of today responding to rate reduction conditions proposed by Qwest and others, such across-the-board rate reductions cannot remotely be claimed to replicate the effect of AT&T's pre-merger presence in the marketplace. For one thing, *today's* rates already reflect AT&T's pre-merger presence. For another, regionwide discounts are a wholly inappropriate merger condition given that AT&T has an "on-net" presence in only a tiny fraction of the buildings where SBC provides special access services; other CLECs serve many of these buildings, and where they do not, they readily could do so should SBC-AT&T try to raise prices.

Alternatively, the CLECs ask the Commission to freeze all special access rates at January 1, 2005 levels to prevent "price squeezes."[20] The absurdity of this request is demonstrated by the number of buildings involved. As we have shown, there are over 400,000 commercial buildings in SBC's 13-state region with demand of 10 DS1s or above. AT&T has facilities in fewer than 1,700 of these buildings. The opponents urge the Commission to freeze rates, or in some cases even reduce rates, in *ALL* of the buildings across SBC's current in-region operations because of the acquisition of 1,700 buildings. Furthermore, the Applicants have already shown that the merger will not remotely increase either the incentive or the ability of SBC to engage in such conduct because, among other factors, SBC will have no greater opportunity than it has today to recoup in that downstream market the massive opportunity costs such conduct would present in the upstream special access market.[21] In all events, the

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18 *See* Joint Opposition of SBC Commc'ns Inc. & AT&T Corp. to Petitions to Deny and Reply to Comments at 140-144, WC Docket No. 05-65 (May 10, 2005) ("SBC/AT&T Joint Opposition").

19 10/18/05 Kelley Drye Ex Parte, Att. at 1; 10/19/05 Swidler Ex Parte, Att. at 1.

20 10/19/05 Swidler Ex Parte, Att. at 1.

21 SBC-AT&T Joint Opposition at 49-51. The CLECs' argument that a price squeeze could be effected through an increase in prices charged for special access services to wholesale customers, 10/19/05 Lipman Ex Parte at 3, is inconsistent with the Commission's previous findings about competitive conditions in MSAs with Phase II pricing. Such increases only would be possible in the MSAs with Phase II pricing flexibility, but those are the very areas where the Commission has found competition to provide special access services is most intense, and where the result of price increases is most likely to be a loss of wholesale customers and the revenue associated with them to competitors. The merger

Commission is considering whether any interim relief is necessary in its ongoing special access rulemaking proceeding, and this industrywide issue is most appropriately addressed there.[22]

The CLECs further ask the Commission to prohibit state commissions from de-listing any further loop or transport UNEs supposedly to allow the market to adjust to the "loss" of AT&T.[23] This, too, is nonsense. As we also explain in greater detail in our letter of today responding to the Qwest group, AT&T is a competitively insignificant supplier of dedicated access services to CLECs. The "loss" of AT&T will have no measurable impact on the ability of CLECs to obtain competitive access services. Furthermore, and most relevantly, the Commission's rules allow for the "de-listing" of UNEs only where it has found that competitive conditions make it likely that the location is suitable for multiple competitive supply.[24] Thus, what the CLECs request here is that the combined company be forced to provide UNEs even in instances where CLECs are *not* impaired and they or other carriers can readily and economically deploy fiber. As such, this condition would flout § 251 of the Act. To the extent that the CLECs are challenging the Commission's impairment findings, those arguments are properly advanced to the D.C. Circuit, which is currently hearing the appeal of the *Triennial Review Remand Order*.

Relatedly, the CLECs ask the Commission to eliminate the existing caps on the purchase of DS1 and DS3 loops.[25] But they do not even attempt to explain how this condition has any relevance to the merger. Rather, it is a bald attempt to obtain reconsideration of an issue that the CLECs raised before the Commission in the Triennial Review Remand Proceeding. It should be raised and considered there, if anywhere, and certainly not in this merger proceeding.

Finally, the CLECs demand that the Commission order SBC not only to recalculate impaired wire centers by excluding AT&T as an unaffiliated fiber-based collocator, but also to exclude MCI, update its business line information, exclude carriers that are simply cross-connected, monitor constantly the presence of fiber-based collocators, and update all relevant information "every three months."[26] But the impairment standard purports to gauge the feasibility of competitive deployment. The fact that AT&T *pre-merger* was economically and operationally able to serve a particular wire center is directly relevant to whether or not competition is feasible in that wire center. The merger has no bearing on that analysis, nor does it have anything to do with how cross-connects are counted for purposes of the impairment

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will not affect competitive conditions in these MSAs – as we explain in our letter of today responding to the Qwest group's ex parte, AT&T is not a significant provider of special access services to other CLECs.

22 *In re Special Access Rates for Price Cap Local Exchange Carriers*, Order and Notice of Proposed Rulemaking, 20 FCC Rcd. 1994, 2036 ¶ 131 (2005).

23 10/18/05 Kelley Drye Ex Parte, Att. at 1.

24 *In re Unbundled Access to Network Elements; et al.*, Order on Remand, 20 FCC Rcd. 2533, 2629-2633 ¶¶ 174-81 (2005).

25 10/18/05 Kelley Drye Ex Parte, Att. at 1.

26 *Id.*, Att. at 2.

analysis. Thus, these proposals, like the others, are nothing more than unprincipled attempts to gain advantage from the merger.[27]

BT Fails to Rebut the Record Evidence Showing That the Merger Will Not Reduce Competition in the Provision of Internet Backbone Services or Internet Connectivity

Through numerous submissions and declarations of both expert and fact witnesses, the Applicants have demonstrated that the merger will have no adverse competitive effects on the provision of Internet Backbone services, or on Internet connectivity. BT's latest filing, which include a new paper from Economists Incorporated ("EI"),[28] does nothing to alter the landscape. EI has failed to rebut the market share analysis of Dr. Schwartz, which showed that the Internet Backbone market was unconcentrated whether measured by traffic, revenues that reflected Internet Backbone functions, or AS connections. Where, as here, all metrics consistently lead to the identical conclusion, there is no need to debate which of them is the "right" metric. Against the consistent evidence marshaled by Dr. Schwartz, EI's complete reliance on revenue measures considered, and rejected, by Dr. Schwartz as proxies for Internet Backbone market shares, which produce results wildly at odds with all other metrics of record showing the lack of concentration in the Internet Backbone market, is simply not credible. Because there is no harm to competition in the Internet Backbone market, there is no basis for any of the remedies that BT proposes.

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27 It is also worth noting that the CLECs misconstrue the Qwest-US WEST Merger Order. 10/19/05 Lipman Ex Parte at 4. In that order, the Commission addressed the "vertical" impact of the merger both with respect to services that US WEST was already offering (out-of-region long distance) and services that US WEST was not already offering (in-region long distance). *In re Applications of Qwest Commc'ns Int'l, Inc. & US West, Inc.*, Memorandum Opinion and Order, 15 FCC Rcd. 5376, 5397 ¶ 40 (2000). The CLECs selectively quote the portion of the decision holding that the merger would increase US WEST's incentives to discriminate in-region, because, unlike SBC today, Qwest did not then offer in-region long distance services. *Id.* at 5397-98 ¶ 42. However, the Commission went on to observe that the merger would have no impact on US WEST's incentives to discriminate with regard to those downstream services that it was already offering. *Id*. ("An incumbent LEC . . . would have the same incentive to degrade the quality of . . . access it provides to competing interexchange carriers whether the incumbent LEC is providing . . . [interexchange] service over facilities it constructed or that it purchased from another carrier."). The same rationale applies to SBC, both in-region and out-of-region, because SBC currently offers both in-region and out-of-region long distance services.

28 Letter from A. Sheba Chacko, BT, to Marlene H. Dortch, FCC, WC Docket No. 05-65 (Oct. 20, 2005).

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These last minute filings should be seen for what they are, last-gasp attempts to raise unwarranted concerns of collusion and to seek the imposition of unwarranted conditions. They are entirely without merit.

Sincerely,

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